

Update

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Defined contribution plan fee disclosure

Making sense of the new regulatory landscape

New regulations proposed by the Department of Labor (DOL) would require comprehensive disclosures to 401(k) and other defined contribution (DC) plan participants regarding administrative and investment-related fees. The new guidance, issued July 23, 2008, is the last of three DOL initiatives on DC plan fee disclosures. As a result of the increased reliance on DC plans as the primary retirement savings vehicle and a growing awareness of how fees can affect the ultimate benefit available to plan participants, DOL is taking steps to promote rigorous fiduciary monitoring and disclosure of plan fees and expenses:

- **Disclosures to participants.** In a recent Mercer survey, one-fourth of defined contribution plan sponsors stated that they were not fully confident that the fees and expenses associated with their 401(k) plans have been properly disclosed. The recently released proposed regulations would give fiduciaries of participant-directed plans a new roadmap for communicating fees to participants. Upon joining a participant-directed DC plan, and annually thereafter, participants would receive descriptions of plan-wide administrative fees and any fees charged for individual transactions. They also would be provided with a comparison table detailing actual fund performance, expenses and appropriate benchmark returns. Fiduciaries could opt to use DOL's model chart to provide this information. Quarterly benefit statements would show the total dollar amount charged to a participant's account for plan-wide administrative services (if not reflected in investment-related fees), along with loan fees and other individual charges. Failure to comply with the new rules, when finalized, could be a breach of fiduciary duty. The regulations are on a fast track – comments to DOL are due Sept. 8, 2008, and DOL aims to have final regulations in place for the 2009 plan year.

- **Disclosures to fiduciaries.** Proposed DOL regulations published in December 2007 would require investment managers, recordkeepers, consultants and other service providers to disclose their direct and indirect compensation so that plan fiduciaries can better gauge the reasonableness of service providers' contracts. The rules are proposed to take effect 90 days after being finalized, but their application to existing arrangements is unclear.
- **Disclosures to the government.** Final revisions to Form 5500, released in November 2007, call for plan administrators to provide more details about direct and indirect fees and expenses in Schedule C. The form revisions will generally take effect for the 2009 reporting year (with the Form 5500 due in July 2010, absent any extension, for calendar-year plans). The changes to the Schedule C coincide with the new mandatory e-filing requirement, also effective for 2009 plan year reporting.

What does it mean for plan sponsors?

While many questions remain, it's not too early to start planning for the required changes:

Work with service providers. Plan fiduciaries will have to work closely with recordkeepers and other service providers to expand participant communications, meet government reporting obligations, and potentially revise contracts for plan services. A first step would be to identify plan service providers and the compensation they receive (directly or indirectly) for their services. Plan fiduciaries will bear ultimate responsibility for participant-level disclosures, but may reasonably rely on investment-related information furnished by service providers; therefore, we recommend starting a dialogue to determine how the required information can be efficiently assembled and disseminated. If the January 1, 2009, effective date holds, plan sponsors may need to work with their providers to develop interim solutions until more automated approaches to information delivery can be developed.

Review communication strategy. Considering the proposed fee disclosure rules on top of the many new DC notices required by the Pension Protection Act (for example, auto-enrollment, default investments and stock diversification right notices), it's clear that the communication landscape has been radically altered. For example, plan sponsors that have implemented auto-enrollment may find their communication themes changing from a participation emphasis to a greater focus on account management and retirement planning. To avoid distributing a patchwork of notices, the first step is to understand all the requirements and potential overlap, and how they affect the array of communications participants already receive. Then a coherent and effective communication program can be built within the required framework.



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Monitor fees and expenses. Bear in mind that the purpose of DOL's regulatory efforts is to encourage both participants and plan sponsors to focus on fees. It's important that your process for regularly reviewing plan fees and expenses is thorough and up-to-date. This includes:

- Ongoing monitoring to determine whether investment expenses are reasonable and appropriate, taking advantage of lower-cost vehicles, if appropriate, in light of other factors
- Effective governance policies for payment of expenses from plan assets, and the allocation of expenses among participants
- Periodic marketplace comparisons, either through a vendor search or fee benchmarking

Some plan sponsors may assume that because they've recently gained fee concessions from their providers, they don't need to perform a marketplace comparison. However, marketplace comparisons are recommended to give plan sponsors the information they need to re-evaluate the fee structure in light of changing conditions, including participant demographics, savings rates and electronic service enhancements.

Fee disclosure movement likely to continue in 2009

Congress also may revisit legislation to make DC plan fees more transparent to participants and plan sponsors. House Education and Labor Committee Chairman George Miller, (D-Calif.), and other lawmakers have criticized DOL's proposed regulations for not going far enough. That dissatisfaction could fuel legislative activity next year. Miller and other members of the House and Senate may reintroduce fee disclosure legislation in 2009, but whether such legislation will advance, and how it might be coordinated with DOL's regulations, remains to be seen.

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