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DEPARTMENT OF LABOR ISSUES INTERIM FINAL RULES ON ERISA PLAN FEE DISCLOSURES

Where are the advocates for ERISA plan fiduciaries?

Background

Today, the United States Department of Labor ("DOL") is expected to publish interim final rules with respect to contracts and arrangements with retirement plan service providers. This rule focuses on the disclosure of fees charged by providers to maintain retirement plans. These long awaited rules were issued after DOL determined that formal legislation that would require greater fee disclosure was unlikely to pass in the near term. In particular, Rep. George Miller (D- Calif.) has been working hard to move fee disclosure legislation through Congress, but his effort has been met with significant resistance. Although DOL would prefer to defer to legislative initiatives, it has determined that this regulation had to be issued now, due to roadblocks on broader sweeping proposed legislation.

The Problem Being Addressed

DOL and other industry experts, have for some time been extremely concerned about the lack of transparency and complexity of service fees being charged by various providers, principally to 401(k) retirement plans. The clear focus is conflicts of interest and determination of the reasonableness of fees paid to providers. This started with a DOL study issued in 1999. Since then, the industry has been under scrutiny for the reasonableness of fees received by various industry players. Fiduciaries who are responsible for managing these fees have been under similar pressure.

Target on Fiduciaries

Fiduciaries have long been targeted by DOL on fees, because DOL cannot regulate the securities or recordkeeping industries. Compensation paid to service providers must be reasonable in order for it not to be prohibited under ERISA. This rule applies even though fiduciaries who do inquire, often lack the knowledge and understanding to ask the right questions.

The Rules – In General

The basic construct of this interim rule places significant requirements and burdens on fiduciaries to maintain "reasonable" contracts or arrangements with providers. Plans that are subject to the rules include all retirement plans, such as 401(k), profit sharing and defined benefit pension plans. Welfare plans and IRAs are excluded from the scope of these rules.

The rules identify "covered service providers" whose compensation will have to be fully disclosed and evaluated by fiduciaries for reasonableness. These covered service providers include those who are paid more than $1,000 in direct, or indirect compensation. Covered service providers that receive compensation "directly" include: ERISA fiduciaries; investment advice fiduciaries subject to the Investment Advisors Act of 1940; investment advisors subject to state law; and certain recordkeepers or brokerage houses. Covered service providers who receive fees "indirectly" include many other providers, such as accounting, audit, actuarial, appraisal, banking, consulting, custodial, insurance, and more.

Compensation for services rendered by any covered service provider is subject to an initial disclosure rule and a general reporting and disclosure rule. Suffice it to say that all direct and indirect compensation must be disclosed prior to the date contractual services are rendered, except as a result of subsequent events which have a 30-day disclosure requirement. The scope of the disclosure requirement is complex, because it includes compensation to related and affiliate parties. For bundled providers, they must "unbundle" certain aspects of their fee, but the precise method of doing so is not stated. Ongoing disclosures, and the disclosure of any prior errors in disclosure, must be made upon request, by the provider, within thirty (30) days.

Not surprisingly, the rules are extremely detailed and more involved than disclosed here. They become fully effective in one year.

Now What?

"Fiduciaries should act now to put into place a prudent process for evaluating service provider relationships, contracts and fee disclosures," recommends our Benefits Department Chair, Jeffrey Zimon. "These rules place significant new burdens on ERISA plan fiduciaries to update their provider relationships, know what questions to ask, and recognize whether provider disclosures will satisfy these rules. Plan fiduciaries need their own advocates to ensure that they comply with the rigors of these new rules."

Additional Information

If there are any questions on these new rules, our clients and friends may contact any member of our Employee Benefits and Compensation Department, or **Jeffrey D. Zimon**, Chair, directly at 216-363-4657 or jzimon@beneschlaw.com. Biographical information is available at www.beneschlaw.com.