

# New Regulation Shines the Light on Retirement Plan Fees

BY BILL HASTIE, HAYASHI & WAYLAND

In an investment environment focused on consumer protection, many have applauded the recent passage of an “interim final” regulation under ERISA Section 408(b)(2). While this regulation has broad implications to both plan sponsors and advisors alike, it is primarily a disclosure regulation designed to provide plan fiduciaries (trustees, etc.) with the information they need to help satisfy their fiduciary responsibilities under ERISA regarding the reasonableness of fees and expenses paid by the plan. ERISA requires plan fiduciaries to review and understand their plan’s fee structure and determine if “reasonable fees are being paid for reasonable services.” What constitutes “reasonable” is for plan fiduciaries to determine based on the value proposition delivered by their service providers, which include record keepers, third party administrators (TPAs), custodians and investment advisors.

Industry studies have long illustrated the adverse effects of excessive fees on the accumulation of retirement assets in a retirement plan—even a 0.25 percent difference in annual fees can make a substantial difference over 20 or 30 years. Since the inception of 401(k) plans, for example, fees have been largely wrapped in the overall pricing of the investment platform, making it almost impossible to clearly understand how much is being paid to whom and for what service. In some cases, plan fiduciaries assumed their plans were free because no specific fee was ever disclosed.

The new disclosure requirement applies to all defined contribution (profit sharing and 401(k) plans) and defined benefit plans subject to ERISA. Simplified Employee

Pensions (SEP’s), SIMPLE plans, IRA’s and non-ERISA plans are not covered plans for purposes of the new regulation. Welfare

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The new regulation presents a great opportunity for companies to better understand fees being charged to their retirement plan, and for “covered service

providers” (any plan service provider who reasonably expects to receive at least \$1,000 or more in direct or indirect compensation) to better articulate their value in light of the fees they charge.

Section 408(b)(2) will become effective July 16, 2011, one year from its publication by the Department of Labor. At that time, covered service providers must provide written disclosure to plan fiduciaries covering three issues:

1. Services - A description of the services to be provided to the plan.
2. Status - An indication of whether the covered service provider is a plan fiduciary or an advisor (Registered Investment Advisor) under the Investment Advisors Act of 1940.
3. Compensation - A description of all reasonably expected direct or indirect compensation (“soft dollar,” finder’s fees, etc.) in aggregate or by service. This includes compensation being paid between related parties. Every dollar leaving the plan and being paid to someone must be accounted for. It must be disclosed to whom compensation was paid, for what service and who benefited from that service.

If nothing else, regulation 408(b)(2) is a call to action. Between now and mid-July 2011, all plan fiduciaries should meet with their advisors or brokers and determine how the new regulation may affect them. Here are a few ideas of what to cover:

1. Disclosure of all plan fees, including all direct fees, sub-transfer agent fees and 12b-1 fees. This transparency will improve clarity for both the plan fiduciary and participants. With a better understanding of what fees are being paid out of the plan and what services are being provided and paid for, better decisions can be made with regard to the best plan for each particular company.
2. Redefine the relationship with the plan advisor/broker. If the advisor is going to be retained as a co-fiduciary, establish the framework of that relationship (i.e., quarterly investment reviews, annual trustee meetings, etc.) Also, discuss any potential conflicts of interest the advisor/broker may have. Acting as a co-fiduciary of the plan, the advisor, by statute, must hold the plan and its participants at the highest level of fiduciary care—the only focus of the advisor should be that which provides greatest benefit to the plan/participants.
3. Discuss alternative plans. There is certainly no shortage of available investment platforms, offering many different types of investments with a wide range of fees. In addition to actively managed mutual funds, platforms are available which offer a complete line-up of inexpensive index mutual funds and exchange traded funds (ETF's). Many plan fiduciaries are finding a great performance/cost benefit with platforms that offer a combination of actively managed mutual funds, index funds and ETF's.

By July 16, 2011, every "covered" retirement plan must address regulation 408(b)(2), how it may potentially affect that plan and make any changes as deemed appropriate. This regulation has increased the level of fiduciary care for which plan fiduciaries/trustees are responsible. Communication with the plan advisor/broker is vital, and now is a great time to start. **cc**

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