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Final Regulation Relating to Service Provider Disclosures Under Section 408b-2

This information includes portions of the U.S. Department of Labor Employee Benefits Security Administration Fact Sheet dated February 2012

The Employee Retirement Income Security Act (ERISA) requires plan fiduciaries, when selecting and monitoring service providers and plan investments, to act prudently and solely in the interest of the plan's participants and beneficiaries. Responsible plan fiduciaries also must ensure that arrangements with their service providers are "reasonable" and that only "reasonable" compensation is paid for services. Fundamental to the ability of fiduciaries to discharge these obligations is obtaining information sufficient to enable them to make informed decisions about an employee benefit plan's services, the costs of such services, and the service providers.

Background

- In recent years, arrangements for how services are provided to employee benefit plans and how service providers are compensated (e.g., through revenue-sharing and other arrangements) have become increasingly complex.
- Many of these changes have improved efficiency and reduced the costs of administrative services and benefits for plans and their participants. However, the complexity resulting from these changes has made it more difficult for many plan sponsors and fiduciaries to understand how, and how much, service providers are compensated.
- This rule establishes, for the first time, specific disclosure obligations for plan service providers to ensure that responsible plan fiduciaries are provided the information they need to make informed decisions when selecting and monitoring service providers for their plans.

Overview of Final Regulation

- The rule requires covered service providers (CSPs) to provide responsible fiduciaries with information they need to:
 - Assess reasonableness of total compensation, both direct and indirect, received by the CSP, its affiliates, and/or subcontractors;
 - Identify potential conflicts of interest; and
 - Satisfy reporting and disclosure requirements under Title I of ERISA.
- The rule applies to ERISA-covered defined benefit and defined contribution pension plans. It does not apply to simplified employee pension plans (SEPs), SIMPLE retirement accounts, IRAs, and certain annuity contracts and custodial accounts described in Internal Revenue Code section 403(b). The rule does not apply to employee welfare benefit plans. EBSA intends to separately publish proposed disclosure requirements for welfare benefit plans in the future.
- The rule applies to covered service providers who expect at least \$1,000 in compensation to be received for services to a covered plan. The rule applies to the following covered service providers:
 - ERISA fiduciary service providers to a covered plan or to a "plan asset" vehicle in which such plan invests;
 - Investment advisers registered under Federal or State law;
 - Record-keepers or brokers who make designated investment alternatives available to the covered plan (e.g., a "platform provider");
 - Providers of one or more of the following services to the covered plan who also receive "indirect compensation" in connection with such services:
 - Accounting, auditing, actuarial, banking, consulting, custodial, insurance, investment advisory, legal, recordkeeping, securities brokerage, third party administration, or valuation services.

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- The rule includes a class exemption from the prohibited transaction provisions of ERISA for responsible plan fiduciaries that enter into service contracts without knowing that the CSP has failed to comply with its disclosure obligations. **The class exemption requires that fiduciaries notify the Department of the disclosure failure. Fiduciaries can file the notice online at www.dol.gov/ebsa/regs/feedisclosurefailurenotice.html.**

Disclosure Requirements

Disclosure of Services and Compensation

- Information required to be disclosed by a CSP must be furnished in writing to a responsible plan fiduciary for the covered plan. The rule does not require a formal written contract delineating the disclosure obligations.
- CSPs must describe the manner in which compensation will be received (ie: billed to the covered plan, or deducted from plan accounts or investments).
- CSPs must describe the services to be provided and all direct and indirect compensation to be received by a CSP, its affiliates, or subcontractors.
- **“Direct compensation”** is compensation received directly from the covered plan. **“Indirect compensation”** generally is compensation received from any source other than the plan sponsor, the CSP, an affiliate, or subcontractor.
- In order to enable a responsible plan fiduciary to assess potential conflicts of interest, CSPs who disclose “indirect compensation” also must describe the arrangement between the payer and CSP pursuant to which indirect compensation is paid. CSPs must identify the sources for indirect compensation, plus services to which such compensation relates.
- Compensation disclosures by CSPs will include allocations of compensation made among related parties (i.e., among a CSP’s affiliates or subcontractors) when such allocations occur as a result of charges made against a plan’s investment or are set on a transaction basis.
- CSPs must include a description of any compensation they (or an affiliate or subcontractor) expect to receive upon termination of the contract, and how any prepaid amounts will be calculated, and if applicable refunded.
- If applicable, the disclosure must include a statement that the service provider (or an affiliate or subcontractor) will provide services as an ERISA fiduciary or as a registered investment advisor.
- CSPs must disclose whether they are providing recordkeeping services and the compensation attributable to such services, even when no explicit charge for recordkeeping is identified as part of the service “package” or contract.
- Some CSPs must disclose an investment’s annual operating expenses (e.g., expense ratio) and any ongoing operating expenses in addition to annual operating expenses (ie: commissions, sales loads, deferred sales charges, redemption fees, etc.). For participant-directed individual account plans, such disclosures must include “total annual operating expenses” expressed as a percentage, any other information that is required by the plan administrator to comply with the Department’s new participant-level fee disclosure regulation at 29 CFR §2550.404a-5.
- The rule contains a “pass-through” for investment-related disclosures furnished by recordkeepers or brokers. A CSP may provide current disclosure materials of an unaffiliated issuer of a designated investment alternative, or information replicated from such materials, provided that the issuer is a registered investment company (i.e., mutual fund), an insurance company qualified to do business in a State, an issuer of a publicly-traded security, or a financial institution supervised by a State or Federal agency.
- Service providers may use electronic means to disclose information under the 408b-2 regulation to plan fiduciaries provided that the covered service provider’s disclosures on a website or other electronic medium are readily accessible to the responsible plan fiduciary, and the fiduciary has clear notification on how to access the information.

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Ongoing Disclosure Obligations

- **Changes:** Generally, CSPs must disclose changes to initial information as soon as practicable, but no later than 60 days from when the CSP is informed of such change. Disclosures of changes to investment-related information are to be made at least annually.
- **Reporting and Disclosure Requirements:** Service providers must disclose compensation or other information related to their service arrangements upon the request of the responsible plan fiduciary or plan administrator, reasonably in advance of the date upon which such person states that they must comply with ERISA's reporting and disclosure requirements.

Disclosure Errors

- The rule allows for timely corrections of an error or omission in required disclosures when a CSP is acting in good faith and with reasonable diligence. Such corrections must be made not later than 30 days from the date that the CSP knows of the error or omission.

Benefits of the Final Regulation

- EBSA estimates that significant benefits will result from the reduced time and cost for fiduciaries to obtain compensation information needed to fulfill their fiduciary duties, the discouragement of harmful conflicts of interest, reduced information gaps, improved decision-making by fiduciaries about plan services, enhanced value for plan participants, and increased ability to redress abuses committed by service providers. They believe these benefits will outweigh the costs associated with the rule.