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# DOL Releases Final Disclosure Regulations for Participant-Directed Individual Account Plans

**October 26, 2010**

On October 14, the Department of Labor (DOL) released final regulations that will impose new requirements for the disclosure of fee and investment information to participants and beneficiaries in participant-directed individual account plans (such as typical 401(k) plans). The final regulations modify and clarify the proposed regulations that were released on July 23, 2008.[1] In the same release, the DOL included a final amendment to the regulations under section 404(c) of the Employee Retirement Income Security Act of 1974, as amended (ERISA), which provides the safe harbor from fiduciary liability for participant-directed plans. This amendment integrates and coordinates the disclosure requirements of the section 404(c) regulation with the final regulations, substantially modifying section 404(c)'s disclosure requirements. The new rules will require plan sponsors and service providers to develop compliant disclosure materials in time for distribution to plan participants by their plan's first year beginning on or after November 1, 2011 (e.g., for calendar-year plans, the plan year beginning January 1, 2012).

## Background

ERISA provides that the investment of plan assets is a fiduciary act governed by fiduciary standards, which require plan fiduciaries to act prudently and solely in the interest of the plan's participants and beneficiaries. If a plan assigns investment responsibilities to participants, the DOL takes the position that plan fiduciaries must take steps to ensure that participants and beneficiaries are provided with sufficient information regarding the plan, including plan fees, expenses, and investment alternatives, so that participants and beneficiaries can make informed investment decisions. Under the final regulations, if the described disclosure requirements are met, the plan administrator will be treated as having satisfied this obligation to provide sufficient information.

Plans that adhere to the requirements of the ERISA section 404(c) safe harbor are currently required to disclose many similar aspects of investment options that are required by the final regulations. However, compliance with section 404(c) is voluntary. Under the final regulations, *all* participant-directed individual account plans, even those not claiming section 404(c) status, are required to provide participants and beneficiaries with this information, which is a significant change from current law.

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[1] For more information, see the July 28, 2008 Morgan Lewis LawFlash, "Department of Labor Proposes New Fee Disclosure Requirements for Participant-Directed Individual Account Plans," available at http://www.morganlewis.com/pubs/EB_NewFeeDisclosureRequirements_LF_28jul08.pdf.

**Final Regulations**

The final regulations require the plan administrator to provide participants and beneficiaries with two types of information: (1) plan-related information and (2) investment-related information. They make clear that plan administrators will not be liable for the completeness and accuracy of information used to satisfy the disclosure requirements when the plan administrator reasonably and in good faith relies on information received from or provided by a plan service provider or the issuer of a designated investment alternative.

The rules apply to participant-directed individual account plans only (e.g., 401(k) plans). They do not apply to individual retirement accounts or individual retirement annuities, simplified employee pension plans, or "SIMPLE" retirement account plans.

**Plan-Related Information**

Plan-related information includes general operational and identification information, as well as information about administrative expenses charged to the plan and the individual participant accounts. Such information generally should be provided to the employee on or before the first date the employee can direct the investments to his or her account, and annually thereafter. Further, the final regulations require that participants be furnished with a description of any changes to the required information at least 30 days, but not more than 90 days, in advance of the effective date of the changes. In the event there are circumstances when changes must be made within a time frame that does not allow for sufficient time to meet the 30-day advance-notice requirement, the final regulations require that the information be furnished as soon as is reasonably practicable. This is a significant change from the proposed regulations, which only required notice of material changes within 30 days after the adoption of such change. The final regulations require disclosure of the following:

***General Operational and Identification Information.*** Under the final regulations, plan administrators are required to include in the general operational and identification information descriptions and explanations relating to (i) how participants and beneficiaries may give investment instructions; (ii) limitations on the investment instructions; (iii) the exercise of voting, tender, and similar rights appurtenant to an investment in a designated investment alternative, (iv) designated investment alternatives under the plan; and (v) brokerage windows, self-directed brokerage accounts, or similar arrangements that allow participants to choose investments outside of those designated by the plan, as well as any fees or expenses associated with such arrangements.

***Information on Administrative Expenses.*** This information includes an explanation of any fees and expenses for general plan administrative services (such as legal, accounting, or recordkeeping services) that may be charged against or deducted from all individual accounts. In addition to the timing requirements described above, the plan administrator must, on a quarterly basis, disclose the fees and expenses that were charged to the individual's account for administrative services during the preceding quarter. This notification must also include a description of the services to which the charges relate and an explanation, if applicable, as to whether any of the plan's administrative expenses for the preceding quarter were paid from the annual operating expenses of one or more of the plan's designated investment alternatives.

***Information on Individual Expenses.*** Plan administrators are also required to disclose to participants and beneficiaries the expenses that are actually charged to the participant's or beneficiary's account (i.e.,

the specific dollar amounts) on an individual, rather than on a planwide, basis. This includes fees related to qualified domestic relation orders (QDROs), loans, and investment advice services. The participant must be provided with a quarterly statement of such amounts charged during the preceding quarter.

**Investment-Related Information**

The final regulations require the plan administrator to disclose several subcategories of core information about each designated investment alternative under the plan. It is important to note that brokerage windows, self-directed brokerage accounts, or similar arrangements are not considered to be designated investment alternatives and therefore are not subject to the disclosure requirements described herein. The following information should be provided automatically to each employee who is eligible to participate in the plan:

- ***Identifying Information:*** The name and type or category of the investment alternative, along with an Internet address that will lead participants to supplemental information about the investment option.
- ***Performance Data:***
    - For designated investment alternatives where the rate of return is not fixed (such as typical mutual funds), the plan administrator should disclose the average annual total percentage return of the investment for one-year, five-year, and ten-year periods, or, if shorter, for the life of the designated investment alternative. The final regulations clarify that stable value funds and money market mutual funds fall under this category of performance data.
    - For designated investment alternatives where the rate of return is fixed (such as guaranteed investment contracts), the plan administrator should disclose the current rate of return and the minimum rate guaranteed under the contract, and include a statement advising participants and beneficiaries that the issuer may adjust the rate of return prospectively.
- ***Benchmark Information:*** Where the rate of return is not fixed, the plan administrator should disclose the name and returns of an appropriate broad-based securities market index over the one-year, five-year, and ten-year periods comparable to the performance data periods described above.
- ***Fee and Expense Information:*** Plan administrators should disclose the fees and expenses related to the purchase, holding, and sale of the investment alternative, including (a) shareholder-type fees charged directly against the investment, such as sales loads, sales charges, and redemption fees; and (b) total annual operating expenses expressed both as a percentage of assets (e.g., expense ratio) and, as added by the final regulations, as a dollar amount for each $1,000 invested for a one-year period.

The information should be provided to participants in a chart or similar format that facilitates comparison of the information for each investment alternative. Further, the chart must include the date it was compiled, the name and address of the plan administrator, and information on how to obtain additional information from the website provided. The DOL has included a model chart for presenting this information, which can be accessed at http://www.dol.gov/ebsa/participantfeerulemodelchart.doc.

Special rules will apply to disclosures regarding designated investment options that consist primarily of qualifying employer securities or that are used to purchase annuity benefits, in recognition of the different nature of such options. The DOL reserved a subsection to provide special disclosure rules for target-date or similar funds, which are expected to be the subject of a separate proposed regulation in the near future.

**Final Amendment to Section 404(c) Regulation**

The DOL also included a final amendment to the regulation under section 404(c) of ERISA. The amendment integrates the disclosure requirements described above into the section 404(c) regulation to ensure that plans that are intended to comply with section 404(c) must meet the same requirements as all plans with participant-directed investment accounts. Many of the requirements in the final regulations are duplicative of the disclosure requirements currently required of a section 404(c) plan. However, some disclosure requirements of section 404(c) plans, such as the requirement to send participants prospectuses relating to investment options, have been supplanted by the final regulations and are no longer applicable. (Prospectuses still must be provided on request.)

Further, consistent with the proposed regulations, the amendment provides that section 404(c) does not relieve a plan fiduciary of its duty to prudently select and monitor the plan's service providers and designated investment alternatives. This is in response to court decisions finding no such limitation under the current section 404(c) regulation.

**Compliance**

Compliance with the final regulations is expected to be onerous, as it will involve communication between plan administrators, third-party administrators, recordkeepers, issuers of designated investment alternatives, and other service providers to ensure that the required information is available to be distributed to participants and beneficiaries. Additionally, the compiling and presentation of this information in the format prescribed by the DOL will take considerable time. Therefore, it is recommended that parties affected by these new disclosure rules begin to take steps to comply with the final regulations well in advance of the effective date.

**Effective Date**

The disclosure requirements must be met for plan years beginning on or after November 1, 2011. For calendar-year plans, this means the final regulations are applicable for plan years beginning on January 1, 2012.

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