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Comments on Participant Investment Fee Disclosure

## Comments on Participant Investment Fee Disclosure

Department of Labor  
Employee Benefits Security Administration

November 30, 2005

The American Society of Pension Professionals & Actuaries (ASPPA) appreciates this opportunity to comment on the Department of Labor's (DOL) consideration of participant investment fee disclosure and Section 404(c) of the Employee Retirement Income Security Act of 1974, as amended (ERISA).

ASPPA is a national society of retirement plan professionals. ASPPA's mission is to educate pension professionals and to preserve and enhance the private pension system. Its membership consists of almost 6,000 actuaries, plan administrators, attorneys, CPAs and other retirement plan experts who design, implement and maintain qualified retirement plans covering tens of millions of American workers.

ASPPA appreciates DOL considering the issue of participant disclosure of investment fees and expenses. As noted to the ERISA Advisory Council, ASPPA supports the principle of full, open and transparent disclosure to plan sponsors, and urges that full and fair disclosure be provided to plan participants to enable them to make informed investment decisions and more effectively manage their retirement assets.<sup>(1)</sup>

ASPPA is limiting its comments to the disclosure of investment fee information to participants, particularly for plans that are utilizing ERISA §404(c). However, ASPPA asks that DOL consider any disclosures plan sponsors should make to participants in tandem with the disclosures DOL requires of plan service providers, so that sponsors will be able to more easily obtain complete information to disclose to participants.

### Background and Issues

Over the past 20 years, employee participation in participant-directed defined contribution plans has exploded. As of year-end 2004, approximately 43 million United States workers participated in defined contribution plans. <sup>(2)</sup> By one measure, participants in these plans had average account balances of \$56,878. <sup>(3)</sup> While this increase in participant-directed defined contribution plan participation permits an ever-greater number of participants to reap the benefits of sound investment decisions, it also places increasing pressure on those participants to ensure that their investments will be sufficient to allow them a comfortable retirement. As Congress and the Administration review potential tools to assist participants in meeting their investment obligations, such as measures encouraging automatic enrollment and investment advice, ASPPA believes it is also important to focus on issues that impact the retirement security of plan participants, such as the effect of fees associated with defined contribution plan investment options.

Each dollar paid by a plan participant for retirement plan expenses reduces that participant's investment returns proportionately. Even fee differences that seem insignificant at first glance can have a substantial effect over the long term. For example, as noted in ASPPA's testimony to the ERISA Advisory Council, over a 25-year period, a participant paying only 0.5% per year in plan expenses will net an additional 28% in retirement plan income rather than a similar plan bearing 1.5% in participant plan expenses per year.

Although ERISA §404(c) and provisions of securities and state insurance laws require fees to be disclosed to participants, many participants still do not

understand the retirement plan investment fees that they pay. This may be due in part to the many different sources of disclosure—currently, depending on the types of investments a plan offers, participants may have to review ERISA §404 (c) plan disclosures, the plan's summary plan description, mutual fund prospectuses, collective fund disclosures and insurance contracts to develop a clear picture of the fees charged for each plan investment. Additional confusion may result from the many different types of fees that can be charged to a participant for plan services, including wrap fees, administrative fees, investment management fees, 12b-1 fees, and fees charged for specific plan transactions, such as distributions and loans. Service providers may offer, and plan sponsors may choose, products that bundle these services and fees, with some offsets for revenue obtained by the service provider from third parties, or plan sponsors may elect to obtain services from multiple vendors charging individual fees for each service provided.

The ERISA Advisory Council on Employee Welfare and Pension Benefit Plans established a Working Group on Fee and Related Disclosures to Participants (Working Group) to review the state of fee disclosure to participants. In November 2004, the Working Group released its report, providing certain consensus recommendations to DOL. As DOL evaluates whether changes should be made in participant investment fee disclosure requirements, ASPPA encourages DOL to adopt the Working Group's consensus recommendations.

As the Working Group noted, additional disclosure obligations, if imposed, should be limited to plans seeking the fiduciary protection offered under ERISA §404(c), and should balance the completeness of disclosure with evaluation of whether there is utility in additional disclosure of specific information to participants. DOL also should carefully consider the burden on small plan sponsors to provide additional disclosure information, and balance participant interests in full disclosure with the need to avoid discouraging plan sponsors from offering retirement plans. Lastly, ASPPA urges DOL to work toward ensuring that disclosure be presented in a format that is easy for participants to review and comprehend, and efficient for the plan sponsor to compile.

### Recommendations

Given the complexity in the way retirement plan participants' services are billed and how those fees are disclosed, participants could benefit from a single form showing the most relevant fees—those that directly reduce the participant's investment return—grouped by investment choice. ASPPA has drafted a model fee disclosure form, attached to these comments, intended to achieve this result. The form is meant to provide the appropriate information in clearly identifiable sections for the participants, with the footnotes on the form providing explanatory information regarding how the plan sponsor should use the forms.

ASPPA has a number of specific recommendations related to the model fee disclosure form. These recommendations address the scope and timing, content and format of participant investment fee disclosure.

#### A. Scope and Timing of Model Disclosure

*No Mandatory Disclosure.* ERISA §404(c) currently requires a laundry list of affirmative and on-demand disclosure to participants; many plan sponsors attempting to comply with ERISA §404(c) are not confident that they are meeting the safe harbor's requirements in every case. One recent study found that, while 71% of the plan sponsors surveyed intended that their plans be ERISA §404(c) compliant, only 48% of them were sure that they were actually meeting all ERISA §404(c) requirements. (4)

**ASPPA recommends** that DOL not impose any additional participant fee disclosure as a condition for ERISA §404(c) relief. Rather, ASPPA recommends that DOL use the model participant investment fee disclosure as an opportunity to assist plan sponsors in providing information that is already required to be disclosed under ERISA §404(c).

Additionally, while plan sponsors are aware of their fiduciary obligations to obtain full and fair disclosure of fees and services from any plan service provider, some plan sponsors have had difficulty obtaining that disclosure. ASPPA strongly urges DOL to avoid imposing additional fee disclosure obligations on plan

sponsors if the information to be disclosed may not be available to them in the required form, if at all, from service providers. Instead, ASPPA asks that DOL provide model disclosure formats and additional guidance for plan sponsors to consider using with service providers when asking for fee information. (5)

If DOL determines that additional participant fee disclosure will be required, then ASPPA recommends that the following items be considered:

1. *Limit to 404(c) Plans.* Participant investment fee disclosure will be most useful for those in participant-directed defined contribution plans; however, only those plans that attempt to comply with ERISA §404(c) are protected from fiduciary liability from the consequences of participants' exercising investment control. Accordingly, ASPPA recommends that DOL limit any changes in participant investment fee disclosure requirements to ERISA §404(c) plans.

2. *Delayed Implementation for Small and Medium Plans.* ASPPA recommends that DOL adopt the Working Group's recommendation to delay implementation for small and medium plans (*i.e.*, plans with fewer than 500 participants) to enable service providers to develop systems that will assist those plans in providing the required information to participants.

3. *Annual Disclosure.* ASPPA recommends that DOL make clear that disclosure should only be required annually, similar to the summary annual report. This recommendation would enable plan sponsors to gather and compile fee information at a given point during the plan year, thereby providing information to participants as a "snapshot" of investment fees. Without an annual limitation on a plan sponsor's affirmative disclosure obligations, participants could be overwhelmed with fee disclosures and plan sponsors could be set up to fail in their attempts to provide disclosure that satisfies DOL requirements.

#### **B. Content and Format of Model Participant Investment Fee Disclosure**

ASPPA's model participant investment fee disclosure recommendations attempt to strike a balance between comprehensive disclosure and useful information for participants and a format straightforward for both small and large plan sponsors to compile.

##### *1. Tabular Fee Disclosure for both Mutual Funds and Insurance Products.*

ASPPA's model disclosure provides fee information for each plan investment option in a tabular format, with descriptions of each investment, its objectives and fees. Because investment fee structures are different for mutual funds and insurance products, ASPPA recommends separate tables for each. (6)

For mutual fund investments, fees are listed in separate columns for the investment's expense ratio, net asset charge or wrap fee and the total participant investment expense. The expense ratio should reflect the fees charged at the mutual fund level for each relevant investment, while the net asset charge or wrap fee should incorporate any fee offsets that are credited back to the plan by its service provider. Together, these numbers should add up to a total participant investment expense reflecting all plan and investment-level fees that directly reduce participant investment return. For insurance product investments, fees are listed in separate columns for account investment ratio and, as for mutual funds, net plan asset charge and total participant investment expense.

ASPPA's disclosure form attempts to equalize disclosure for mutual fund products and insurance-based products, to encourage price transparency and full and fair comparisons across product lines. To the extent that any other investment-related fees reduce participant investment return, ASPPA encourages disclosure of such fees through additional items on the form, if that information is provided or available to plan sponsors. If DOL mandates additional disclosures and such information is not available or disclosed to plan sponsors (such as any portfolio transaction costs not already reflected in the expense ratio), ASPPA recommends that DOL confirm that sponsors will not lose ERISA §404(c) protection due to failure to provide such information, even when the information is arguably relevant to participants in evaluating plan investment options.

2. *Redemption Fees.* ASPPA suggests that fees charged only in the event of specific participant behavior, such as redemption fees or surrender charges, not be required. For example when an investment disclosure is annually updated,

the redemption fees information provided may be outdated too quickly. As an alternative to requiring a list of actual redemption fees charged for each investment alternative, ASPPA's model highlights the possibility that redemption fees or surrender charges may apply to the participant's investment, and suggests that the participant review the fund prospectus or contact the plan administrator for specific information. In this regard, many web-based products alert participants who are submitting an investment change if the change will result in a redemption fee. ASPPA recommends that DOL confirm that this approach to disclosure of redemption fees satisfies ERISA §404(c) requirements.

3. *Actual, Affirmative Dollar Disclosure Should Not Be Mandatory.* ASPPA concurs with the Working Group's conclusion that disclosing the actual dollars charged to participants' accounts could be overly costly and complex. Accordingly, ASPPA requests that any additional participant investment fee disclosure information be disclosed as a percentage of plan assets in the investment, which will be significantly simpler for plan sponsors to report. Alternatively, if dollar disclosure is required, ASPPA asks that it be limited to a hypothetical illustration of costs ( e.g., per \$1,000 of investment).

4. *Open Brokerage Windows Should Not Be Included in Model Disclosure.* Some plan sponsors make open brokerage windows available to participants. Through such products, participants are permitted to invest in options beyond the "core" investments selected by the plan sponsor. Many of these products place few restrictions on participants, allowing them to choose among thousands of mutual funds, insurance products, publicly or non-publicly traded securities. Accordingly, as ASPPA has previously noted and the Working Group concluded, it would be extremely burdensome for plan sponsors to be required to compile and disclose fee information for each potential investment a participant could choose. ASPPA asks DOL to confirm that, as noted on the attached model disclosure, plan sponsors may direct participants to carefully review investments outside the plan's core set of options and indicate that participants are responsible for gathering fee information for those investments on their own.

5. *Disclosure of Compensation Paid to Consultants.* The structure, source and disclosure of compensation paid to service providers has been under increasing scrutiny by various governmental agencies and interest groups during the past few years. Most recently, the Securities and Exchange Commission released its report regarding compensation of retirement plan consultants, and whether certain revenue sharing or other arrangements with investment providers were adequately disclosed to plan sponsors. ASPPA encourages full and fair disclosure on this topic, but suggests that the most complete disclosure be limited to the plan sponsor, who is responsible for choosing and overseeing the performance of plan service providers.

In the model disclosure, ASPPA provides a footnote in which plan sponsors may disclose to participants the identity and compensation structure of the plan's main investment consultant(s). In that footnote, ASPPA suggests that plan sponsors explain whether a consultant is paid based on commissions, 12b-1 fees or wrap fees, and whether the fees are charged against participant assets or are instead absorbed by the plan sponsor directly. As noted above, plan service providers and plan sponsors negotiate methods of charging fees that vary by product and by plan. A blanket sample disclosure will not adequately address all of the ways that plan sponsors may choose to pay plan expenses. However, plan participants should have basic information regarding the factors that are relevant in determining a plan consultant's fee and should have access to more complete information upon request. The model disclosure is intended to balance that goal with the competing goal of providing a simple form for disclosure of key information.

## Conclusion

In conclusion, ASPPA again applauds DOL for continuing to examine and refine the nature of fee disclosure to both participants and plan sponsors. Should DOL conclude that a public hearing is necessary as it considers the issues involved, ASPPA would be happy to participate and to further discuss the recommendations in these comments.

These comments were prepared by ASPPA's DOL subcommittee of the Government Affairs Committee, Todd J. Berghuis, Esq., APM, Chair, and were

primarily authored by Stephanie L. Napier, Esq., APM. Please contact us if you have any comments or questions regarding the matters discussed above. Thank you for your consideration of these comments.

Sincerely,

Brian H. Graff, Esq. APM Executive Director	Teresa T. Bloom, Esq., APM, Co-chair Gov't Affairs Committee
Ilene H. Ferenczy, Esq., CPC, Co-chair Gov't Affairs Committee	David Lipkin, MSPA, Co-chair Gov't Affairs Committee
Sal L. Tripodi, Esq., APM, Co-chair Gov't Affairs Committee	Robert M. Richter, Esq., APM, Chair Administrative Relations Committee
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Testimony Before the ERISA Advisory Council on Behalf of the American Society of Pension Actuaries Working Group on Fee and Related Disclosures to Participants (September 21, 2004). ASPPA continues to support full disclosure to plan fiduciaries of all costs payable out of plan assets as referenced in our February 14, 2005 comment letter to the DOL.

Sarah Holden and Jack VanDerhei, *401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2004*, EBRI Issue Brief, No. 285 (September 2005).

*Id.* This figure is obtained from the EBRI/ICI Participant-Directed Retirement Plan Data Collection Database, which includes data covering approximately 38% of the 401(k) plan participants, holding 44% of 401(k) plan assets.

Fred Schneyer, *Survey Finds More Sponsors Minding Governance Ps and Qs*, Plan Sponsor (November 17, 2005), at [www.plansponsor.com/pi\\_type10/?RECORD\\_ID=31529](http://www.plansponsor.com/pi_type10/?RECORD_ID=31529) (survey performed by Plan Sponsor Advisors, LLC and Grant Thornton, LLP).

ASPPA is aware that DOL is also considering changes to the conditions for the ERISA §408(b)(2) statutory prohibited transaction exemption for provision of services by a party in interest to a plan, perhaps to require additional disclosure of fees collected by the service provider in connection with its services. ASPPA requests that DOL consider these changes in tandem with any new participant investment fee disclosure requirements for plan sponsors.

For other investment options, such as collective trusts, fees may be disclosed in a way that is analogous to mutual funds or insurance products.

[Sample form](#) [Excel: 48K]