

ERISA Plan Expenses Overview and Checklist

PAYMENT OF PLAN EXPENSES IS A FIDUCIARY DECISION

The assets of an ERISA plan may be used for two purposes: (1) to pay benefits, and (2) to pay the reasonable expenses of administering the plan. ERISA §§403(c)(1) and 404(a)(1)(A). The decision to pay expenses from the assets of a plan is a fiduciary decision subject to the fiduciary rules of ERISA. *See* DOL Adv. Op. 2001-01A (Jan. 18, 2001); DOL Adv. Op. 97-03A (Jan. 23, 1997).

CRITICAL QUESTIONS

The plan fiduciary should be able to answer the following questions before making the decision to pay an expense from plan assets:

1. Does the plan document permit (or at least not prohibit) the payment of this expense?
2. Is the expense (and therefore the goods or services purchased) related to the fiduciary's administration of the plan and not related to the plan sponsor's "settlor" function?
3. Is the expenditure prudent and is the amount reasonable?
4. Is the service being provided by a party in interest or by the plan fiduciary (*e.g.*, the plan sponsor or an affiliate)?

CHECKLIST APPROACH

The attached checklist will help answer these questions. If the answer to the first three questions is "YES," then the expense is likely one that can be paid from the assets of the plan. If the answer to the fourth question is "YES," then additional analysis is required to determine whether the expense is payable by the plan and, in some instances, how much may be paid from the plan.

The checklist contains 9 broad categories of services for which expenses are incurred (Column 1) and provides specific examples within each category (Column 2). Column 3 of the checklist identifies whether a type of expense is considered fiduciary or settlor in nature and column 4 provides the legal authority for this determination.

Each expenditure requires a separate and independent determination regarding whether or not the expense is permitted by the plan (or at least not prohibited by it). Column 5 of the checklist provides a place to document this determination. Similarly, each expenditure must be determined to be prudent and reasonable, which requires that the plan fiduciary gather the sufficient information to judge the value of the services in relation to their cost. Column 6 of the checklist provides a place for the plan fiduciary to indicate whether the expense has been judged prudent and reasonable and how the determination was made. Column 7 of the checklist reminds the fiduciary of the importance of knowing whether and how the service provider is related to the plan. Below, we discuss how this information affects the analysis regarding a plan's payment of expenses.

SERVICES PROVIDED BY PARTIES IN INTEREST

If the service provider is a party in interest to the plan (*e.g.*, a service provider, fiduciary, or employer of employees covered by the plan) then the service must meet three requirements: (1) it must be necessary for the operation of the plan; (2) it must be furnished under a contract or arrangement which is reasonable; and (3) no more than reasonable compensation is paid for the service. *See* ERISA § 406(a)(1)(c) (prohibits the provision of services to a plan by a party in interest); and ERISA § 408(b)(1) (exempts services by a party in interest if the exemption's conditions are met). A service is considered "necessary" for the plan's operation if it is "appropriate and helpful . . . in carrying out the purposes for which the plan is established or maintained." *See* 29 C.F.R. § 2550.408b-2(b). In order for a plan services contract to be a "reasonable contract or arrangement," the plan must have the right to terminate the contract on "without penalty." *See* 29 C.F.R. § 2550.408b-2(c). The "reasonableness" of a compensation for services rendered to a plan depends on the fact and circumstances surrounding the payment. *See* 29 C.F.R. § 2550.408c-2(b)(1). This analysis should be applied, for instance, where a current plan service provider is to be subsequently re-hired to perform the same or additional services for the plan.

SERVICES PROVIDED BY THE EMPLOYER

Where an employer provides services to its own plan, the plan may pay only the "direct expenses" for those services. These "direct expenses" do not include: (1) any expense that would have been incurred by the employer even if the employer had not provided the service to the plan, or (2) any overhead expenses. Thus, where the employer acts as a service provider to its own plan, the plan may pay only for those expenses that would not have been incurred "but for" the employer's provision of services to the plan and may not pay for any of the employer's overhead costs. For example, in order for a plan to pay for services provided to the plan by an employee of the employer, the amount of the employee's compensation attributable to work for the plan must be determined, and the employer must conclude that "but for" the services the employee provides to the employer's plan, the position would be eliminated and the employer would therefore not incur the salary expense. For purposes of this analysis it should be permissible for the employer to aggregate the work any single employee does providing services to multiple plans, and to aggregate the work multiple employees perform for plans. Thus, where one employee spends all of her time providing services to 5 plans, it would be reasonable to conclude that but for the services to plans as a group, the position would be eliminated. Based on this conclusion, each of the 5 plans could pay their allocable share of the employee's compensation. Similarly, where 5 employees each spend 20% of their time providing services to the employer's plan or plans, the employer might reasonably conclude that if it didn't provide services to the plan or plans, it could eliminate 1 of the 5 positions, and that therefore the plan or plans could pay their allocable share of the 20% of each employee's compensation.

ALLOCATION

Where a single service provider provides services to more than one plan, it is important that each plan pay only those expenses properly payable by it, and not the expenses of another plan. In addition, U.S. Department of Labor ("DOL") guidance indicates that certain expenses which are generally payable by plans, may be properly chargeable to the account of an individual participant for whom the expense was incurred. Specifically, these expenses include: hardship withdrawals, the calculation of benefits payable under different plan options, benefit distribution charges (*e.g.* check writing fees), and expenses associated with QDRO and QMSCO determinations and loan processing. *See* Field Assistance Bulletin 2003-3 (May 19, 2003). Charges to locate missing plan participants are also be allocable to the individual missing participant. *See* Field Assistance Bulletin 2004-2 (September 30, 2004).

ERISA PLAN EXPENSE CHECKLIST

| Type Of Service For Which Expense Was Incurred | Example | Legally Permitted (Fiduciary, Not Settlor In Nature)? | Authority For Legal Conclusion | Chargeable to the Plan Under Plans Terms? | Arrangement And Amount Prudent And Reasonable? | Does Employer, Plan Fiduciary or Service Provider (Unrelated) Provide Service? |
|--|---|---|--|---|--|--|
| 1. Basic Administrative Services (plan wide) | Plan record keeping | Yes | Field Assistance Bulletin 2003-3 (May 19, 2003) ("FAB 2003-3"); DOL Booklet entitled "A Look At 401(k) Plan Fees for Employees" ("DOL Guidance for Employees") | | | |
| | Plan accounting | Yes | DOL Guidance for Employees | | | |
| | Legal services relating to plan fiduciary issues (not settler issues) | Yes | FAB 2003-3; DOL Guidance for Employees | | | |
| | Trustee | Yes | DOL Guidance for Employees | | | |
| | Safekeeping of plan assets (<i>i.e.</i> custodial services) | Yes | <i>401(k) Plan Fee Disclosure Form</i> from the EBSA's web site, prepared by the American Bankers Association/American Council of Life Insurance/Investment Advisory Institute ("Fee Disclosure Form") | | | |
| | Periodic/annual compliance auditing | Yes | FAB 2003-3; DOL Info. Ltr. To Henderson (July 28, 1998) ("Henderson Letter") | | | |
| | Legally Required Reporting (<i>e.g.</i> , Form 5500) | Yes | FAB 2003-3 | | | |
| | Claims Processing | Yes | FAB 2003-3 | | | |
| | Participant Communications (<i>e.g.</i> , distribution of SPDs, SARs, benefit statements) | Yes | 2001 Hypos, Ex.2, 5 | | | |

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|---|---|---|--|---|--|--|
| | Third party administration expenses including "start up," ongoing expenses, and termination charges | Yes | 2001 Hypos, Ex.6 | | | |
| 2. Additional Administrative Services (plan wide) | Telephone Voice Response Systems | Yes | DOL Guidance for Employees | | | |
| | Educational Seminars | Yes | DOL Guidance for Employees | | | |
| | Retirement Planning Software | Yes | DOL Guidance for Employees | | | |
| | Investment Advice | Yes | FAB 2003-3; DOL Guidance for Employees | | | |
| | Electronic Access to Plan Info | Yes | DOL Guidance for Employees | | | |
| 3. Investment-Related Services | Sales Charges (also known as loads or commissions) | Yes | DOL Guidance for Employees | | | |
| | Management Fees (also known as investment advisory fees or account maintenance fees) | Yes | DOL Guidance for Employees; FAB 2003-3 | | | |
| | Contract termination charges | Yes | 29 C.F.R. § 2550.408b-2; Fee Disclosure Form | | | |
| | Product termination fees | Yes | 29 C.F.R. § 2550.408b-2; Fee Disclosure Form | | | |
| 4. Expenses Incurred In Connection With Settlor Decisions | Legal or consulting services in connection with plan formation | No | DOL Adv.Op. 2001-01A ("2001-01A"); 2001 Hypos, Ex.1; DOL/PWBA Letter to Maldonado (March 2, 1987) ("Maldonado Letter") | | | |

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| May NOT Be Paid With Plan Assets | Plan Design Activities (e.g., legal or consulting expenses incurred in advance of the adoption of the plan or plan amendment; plan design studies; cost projections to determine the financial impact of the plan change) | No | 2001-01A; 2001 Hypos, Ex.1, 2, 3, 4; Maldonado Letter | | | |
| | Drafting of discretionary Amendments (e.g., plan spin-off; establish a participant loan program; early retirement window) | No | 2001 Hypos, Ex.1; Maldonado Letter | | | |
| | Other Employer Responsibilities (e.g., preparation of FASB Statement No. 87, 88) | No | 2001-01A; 2001 Hypos, Ex.2 | | | |
| | Legal and consulting expenses in connection with plan termination (decision to terminate and drafting of plan amendment) | No | 2001-01A; 2001 Hypos, Ex.1; DOL Adv.Op. 97—03A (Jan. 23, 1997) ("97-03A"); Maldonado Letter | | | |
| 5. Fiduciary Implementation of Settlor's Decisions | Drafting required plan amendments (e.g., to maintain the plan's tax-qualified status) | Yes | 2001-01A; 2001 Hypos, Ex.3, 4; 97-03A | | | |
| | Routine non-discrimination testing (including actuary fees) | Yes | 2001-01A; 2001 Hypos, Ex.3, 4 | | | |

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| | Seeking IRS determination letters | Yes | 2001-01A; 2001 Hypos, Ex.3, 4; 97-03A | | | |
| | Implementing Discretionary Amendment | Yes | 2001 Hypos, Ex.1, 3 | | | |
| | Implementing a plan termination (including auditing the plan, preparing/filing annual reports, preparing benefit statements and calculating accrued benefits, and notifying participants of their benefits under the plan) | Yes | 97-03A | | | |
| 6. Insurance and Bonding | Insurance costs for the plan fiduciaries or for the plan to cover liability or losses occurring by reason of the act or omission of a fiduciary provided such insurance permits recourse by the insurer against the fiduciary in the case of a breach of a fiduciary obligation by the fiduciary | Yes | ERISA § 410(b); Henderson Letter | | | |
| | Bonding | Yes | ERISA § 412; Maldonado Letter | | | |
| 7. Sanctions /Penalties | Imposed on the plan | Yes | Henderson Letter | | | |

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|--|---|---|--|---|--|--|
| | Imposed on someone other than the plan (e.g., on a plan administrator as personal liability) | No | Henderson Letter | | | |
| | Audit-CAP sanction | No | IRS Rev. Proc. 2003-44, § 13.01 | | | |
| 8. Qualification Error Correction | EPCRS – VCP Compliance Fee. | No | IRS Rev. Proc. 2003-44, § 10.01 | | | |
| 9. Fiduciary Error Correction | Cost of correction under the Voluntary Fiduciary Correction Program ("VFC Program") (e.g., closing costs, prepayment penalties) | No | VFC Program, 67 F.R. 15062, 15075 (March 28, 2002) | | | |