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Full Disclosure

Sponsors have all this information under 408(b)(2). Now what?

The year 2012 may long be remembered as the year of disclosure. Now that all this information has changed hands, 2013 is shaping up to be the year the employee benefits community faces the task of actually doing something with the information.

The final 408(b)(2) regulation answered many questions the community had raised about the proposed regulation. However, it raised just as many as it resolved, including the big question of what exactly plan sponsors were supposed to do with all of this information. The Department of Labor (DOL) promised that frequently asked questions (FAQs) would be forthcoming, but, as of now, we are still waiting for this important guidance. In the end, service providers were left to interpret the regulation in good faith and to comply as best they could. Providers seem to have done a good job of supplying plan sponsors with appropriate and timely disclosures. However, in the absence of guidance about what to do with these disclosures, many plan sponsors have simply put them in a folder and moved on to the task of sending out the participant disclosures.

This is a significant problem, and many plan sponsors are coming to the realization that they still have a fairly thick stack of fee disclosure documents waiting to be reviewed and no clear guidance on how to fulfill this responsibility. However, the sad truth is that, even in the absence of guidance, sponsors will have to establish a process to review the information they receive or face the very real prospect that they will commit a fiduciary breach.

So what should this review process entail?

First, a fiduciary must determine whether it has received the required information from all of the appropriate service providers. Generally, every "covered service provider" must furnish certain specified information to a "responsible plan fiduciary." While other measures may be necessary, a good starting point for determining who is providing services to a plan would be to look at Schedule C of the plan's Form 5500 and determine whether any service providers have regularly been paid from the plan's trust.

Second, a fiduciary will also need to confirm that the disclosures contain all the required information. Generally, each disclosure should state whether the service provider is acting as a fiduciary or a registered investment adviser, identify the services that it expects to provide and describe the compensation it expects to receive for providing those services.

If all the required information has been supplied, the fiduciary should review it and confirm that the compensation received by the service provider is reasonable in light of the services being provided. Hopefully, this review will not be overly burdensome. That said, the fact that a provider's compensation was deemed reasonable in previous years when the value of the assets was a small percentage of current assets may not mean that today's compensation is reasonable. Current compensation must be compared to what other providers would charge for similar services.

Presumably, at the time the service provider was hired, its compensation was reviewed and deemed reasonable. The new disclosure document should, generally, reaffirm the information used to make that earlier determination. However, fiduciaries should pay particular attention to any indirect compensation included in the disclosure documents. These disclosures may be the first time a fiduciary learns that a service provider has other, indirect, sources of income. Nothing in the Employee Retirement Income Security Act (ERISA) or the new regulations prevents a service provider from receiving indirect compensation; however, a fiduciary must take account of all forms of compensation when determining the reasonableness of a service provider's compensation.

Hopefully, most fiduciaries will find this review process to be straightforward and unsurprising. Every covered service provider should be furnishing the necessary information in a timely manner. However, it is up to the plan fiduciary to have a process in place to confirm that it has received the required information and that it is using it to make the proper determinations about the service provider. Without an established review process, a fiduciary risks engaging in a prohibited transaction and committing a fiduciary breach.

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