Fee disclosures could make it harder on small, midsize plan sponsors

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The U.S. Department of Labor's final rule regarding fee disclosure to plan sponsors could have some unintended consequences.
Because of its lack of specificity regarding how plan service providers must provide fee information, some in the industry worry that small plan providers will not be able to figure out what they are paying based on what they receive. As the regulation stands, it is on the shoulders of the plan sponsors to let the Department of Labor know if they haven't received the information they are supposed to receive from their service providers.

Plan administrators could get a box of information dumped on them during the last couple of weeks before the July 1 compliance deadline and not have a clue how to read it or figure out what fees they are actually paying.

The 408(b)(2) regulation, which is part of the Employee Retirement Income Security Act , requires 401(k) service providers to furnish information that will enable plan fiduciaries to determine if compensation they are paying to service providers is reasonable and whether there are any conflicts of interest that may affect a service provider's performance under the service contract or arrangement.

The rule applies to those service providers that expect to receive $1,000 or more in compensation and provide certain fiduciary or registered investment advisory services, make available plan investment options in connection with brokerage or recordkeeping services or otherwise receive indirect compensation for providing certain services to a plan.

The department also said it will publish for public comment a separate proposal that would require service providers to furnish a guide or similar tool to assist plan fiduciaries in identifying and locating the potentially complex information that must be disclosed and that may be located in multiple documents.

The Employee Benefits Security Administration included a sample guide in its final rule as a model for how this information should be distributed.

“The voluntary roadmap is a step in the right direction, but it falls far short of [Plan Sponsor Council of America's] recommendation that disclosure be provided in a single comprehensive document,” said David Wray, president of PSCA in a recent blog.

The biggest problem, according to Wray, is that plan sponsors will “receive a quantity of information from the plan providers, probably compiled by the plan's recordkeeper. Embedded in this information will be detailed fee information that the plan sponsor will be required to identify and evaluate. For

large employers, this is no problem. They have internal expertise and are advised by the country's top retirement plan experts. In fact, they are already getting this information. For small and medium-sized employers the situation is different. Most do not have internal expertise and their advisor, to the extent they have one, is an expert on investments but not the technicalities of ERISA," he said.

"The one group where this will be a wakeup call is for small plan sponsors who haven't adjusted their fee arrangements since they initiated the plan many years ago," Wray said in an interview with BenefitsPro. "Fee bracket creep is an issue."

Wray explained that the original fee arrangement when a plan is first formed is typically high because there are virtually no assets in the plan. The fee is supposed to go down as assets grow and account balances grow, but it is the plan sponsor's job to have the discussion with their provider.

"As account balances grow, the plan is eligible for reduced fee arrangements. However, if the plan sponsor doesn't go to the provider and ask for them, these lower fee arrangements don't occur," Wray said.

He added that he doesn't believe plan sponsors have given fees much thought because they have mostly focused their attention on plan performance.

"Net performance is something you can evaluate very easily. There are benchmarks to deal with that. It is difficult to take net performance and adjust thinking for an internal fee structure that's involved as well," he said.

Companies like The Standard, Vanguard and The Principal already have prepared for the fee disclosure regulations.

Vanguard said in a statement that it has provided clear information about fees to both plan sponsors and participants.

For more than 15 years, the plan service provider has provided plan sponsors with a detailed "all-in" fee report, reflecting a plan's total investment and recordkeeping costs.

"[Vanguard's] all-in fee report traditionally included expense ratios for Vanguard and non-Vanguard investments, detail showing compensation from outside fund companies to defray the cost of recordkeeping, any explicit sponsor or participant-paid recordkeeping fees and costs for additional service items. Beyond that, Vanguard has enhanced the report's effectiveness with an easy-to-read summary and additional information that was both required and not required," the company said in a statement.

For plan participants, Vanguard has shown "clear participant fee information on participant statements and plan materials, including fund expense ratios and plan-level participant-paid fees. In addition to existing disclosures, it will now also be including additional detail about participant-level fees on the participant statement."

Joel Mee, director of retirement plan sales operations for The Standard, said that his company also has been very transparent about its fees so it hasn't taken much to comply with the new DOL regulations.

The regulation is so specific about the wording and format for how fees need to be disclosed that even though The Standard has been fairly transparent with its fees, it has "impacted us in needing to invest in infrastructure to make sure we are complying with the exact regulation and format prescribed. But it will not have the same impact to us as we expect with other providers," he said.

“I think it is going to be very challenging for smaller and mid-size providers. Even a company as large as ours, we have had to invest hundreds of hours of manpower in making sure our benefits statements and disclosures meet the regulations…The investment of time to comply is not insignificant. I’ve got to imagine for smaller providers this could be quite a challenge,” Mee said.

The Standard’s retirement packages are sold primarily through brokers and registered investment advisors. If anything, the impact to them will be greater than for large plan providers, Mee said. Most of the advisors and brokers who sell retirement plan options or services provided by The Standard are “small companies, small mom and pop organizations, five to 10-person companies. It is tough for them to comply. The extension will help them a lot,” he said.
The Standard has “done quite a lot to help our advisors comply. When advisors work for us, we take on most of the heavy lifting in helping them to comply. We provided sample service agreements for 408(b)(2),” he said.

When asked about a backlash in the market because of fee disclosure, Mee said that The Standard has had ongoing conversations with its plan sponsors about fee disclosure, so he doesn’t expect complaints from that sector. “The outcry from the broker and advisor community has been loud,” he said. “We’ve definitely heard from them.”

Mee said he believes the regulations will “create more competition and more benchmarking, but they will push us even further to a fee for service model.” The rules will have a detrimental effect on individuals who charge for their services to a plan, but don’t really do much for the plan, he added.

With the new disclosures, all of those people will have to write out a description of what they have done for the plan to earn their fees. “When they are forced to spell out what they do and how much they are charging to do that, this will force the hand in a lot of cases. …That ultimately will make the private retirement system more efficient,” he said.

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