

Investment Related Regulation Update - Part II

July 25, 2011

Murray McBride, President
Sunlin Consulting Investment Advisory Services, LLC

AGENDA

- ❖ Fee Disclosure to Plan Sponsors - 408(b)(2)
- ❖ Disclosures to Plan Participants - 404(a)(5)
- ❖ Changes to the Fiduciary Definition



Fee Disclosure to Plan Sponsors

DOL 408(b)(2)

Fee Disclosure to Plan Sponsors

- ❖ DOL Section 408(b)(2)
- ❖ Effective April 1, 2012
- ❖ Requires fiduciaries to understand all fees and expenses associated with retirement plans
- ❖ All direct and indirect compensation
- ❖ All sub-TA fees, credits between vendors, funds in plan, and investment advisors/brokers

Fee Disclosure to Plan Sponsors

Written Disclosures

- ❖ Services being provided
- ❖ Fiduciary Status
- ❖ Direct & indirect compensation
- ❖ Manner of receipt

Fee Disclosure to Plan Sponsors

Timing

- ❖ Initial — in advance of contract date
- ❖ Changes — within 60 days

Format

- ❖ Format for disclosure not prescribed

Fee Disclosure to Plan Sponsors

Plan Sponsor Responsibilities

- ❖ Identify all service providers to plan that should provide disclosure
- ❖ Determine whether information provided is reasonably correct
- ❖ Request required information if gaps discovered
- ❖ Notify DOL if service provider does not respond to request within 90 days

Fee Disclosure to Plan Sponsors

Record Keeper (and TPA) Responsibilities/Actions

- ❖ Identify all relationships and information that require disclosure
- ❖ Develop procedures for obtaining and distributing information to clients in timely fashion to meet deadlines
- ❖ Disclose potential conflicts of interest

Fee Disclosure to Plan Sponsors

Impact on Investment Advisors

- ❖ Fee only advisors not likely impacted unless there are sources of indirect compensation to disclose
- ❖ Brokers will be required to disclose actual compensation, both direct and indirect, derived from plan assets and/or other sources



Disclosures to Plan Participants

DOL 404(a)(5)

Disclosures to Plan Participants

- ❖ ERISA Section 404 (a)(5)
- ❖ Replaces voluntary provisions of 404(c) with mandatory disclosure
- ❖ Covers investment related information including fees and expenses
- ❖ Failure to comply is breach of fiduciary responsibility
- ❖ Failure to comply with 404(a)(5) and residual components of 404(c) eliminates fiduciary protection against responsibility for result of participants' asset allocation decisions
- ❖ 60 days after effective date of 408(b)2 regulation

Disclosures to Plan Participants

Required Notices

❖ Initial Notice

- Extensive detail to be provided on each investment alternative
- Plan related information and procedures (e.g. voting rights)
- Detail on plan wide fees that may be charged to participant accounts

❖ Quarterly Notice

- Fees and expenses actually charged to participant accounts
- Description of services provided for these fees
- Disclosure of revenue sharing, if applicable

Disclosures to Plan Participants

Required Notices (continued)

- ❖ Annual Notice
 - Same information as initial notice

- ❖ Change Notice
 - Any change to information provided in other notices
 - Must be provided at least 30 but not more than 90 days prior to date of change

Other Information upon Request

- ❖ Examples: prospectuses, financial statements, list of assets

Disclosures to Plan Participants

Plan Sponsor Responsibility

- ❖ Provide all 404 (a)(5) required information to plan participants by required deadlines
 - May reasonably rely on information provided by service providers

Disclosures to Plan Participants

Plan Sponsor - practical steps to ensure compliance

- ❖ Establish procedures to monitor disclosure fulfillment by record keeper
- ❖ Ask provider for anticipated timing for initial 2012 disclosures
- ❖ Ask provider for pro-forma of disclosure well in advance of deadline
- ❖ Review pro-forma for completeness & accuracy
- ❖ Ask provider how notices will be distributed to participants and beneficiaries and procedures to ensure deadlines are being met

Disclosures to Plan Participants

Plan Sponsor - steps to take in 2011

- ❖ Plan for compliance with 404(c) for 2011 plan year
- ❖ Review current fees for reasonableness and consider payment methodology
- ❖ Develop HR procedures for handling distribution and responding to participant inquiries
- ❖ Educate participants about disclosure information that will be coming

Disclosures to Plan Participants

Plan Sponsor - steps to take in 2012

- ❖ Review drafts of disclosure material provided by record keeper for completeness
- ❖ Prepare supplemental participant materials to fill gaps

Disclosures to Plan Participants

Record Keeper Responsibilities

- ❖ While the final responsibility for disclosure falls on the plan sponsor, plan sponsors will be looking to their record keepers to provide required information
- ❖ DOL has provided “Model Chart” to cover bulk of information. Record keepers need to prepare to gather information from fund companies / investment managers and consolidate into single package

Disclosures to Plan Participants

Practical issues facing Record Keeper

- ❖ Procedure to ensure each fund company will provide all required fund related information
- ❖ If using third party fund info provider, procedure to ensure that all info is provided for every fund
- ❖ Procedure to ensure that direct internet address is provided for each fund and that site provides all mandated information
- ❖ Procedure to identify changes to information and preparation and distribution of change notices by deadline
- ❖ Procedures for distribution of hard copy notices

Disclosures to Plan Participants

Consultant / Advisor Opportunities

- ❖ Educate clients on new responsibilities
- ❖ Review prototype disclosure statements released by service providers
- ❖ Test actual data for reasonableness and completeness
- ❖ Help to fill gaps identified, if any



Changes to the Fiduciary Definition

Fiduciary Rules Under ERISA

- ❖ ERISA 404(a) imposes a “prudent man standard of care” for qualified plan fiduciaries.
- ❖ For the exclusive purpose of:
 - providing benefits to participants and their beneficiaries; and
 - defraying reasonable expenses of administering the plan;

Fiduciary Rules Under ERISA

- ❖ With the care, skill, prudence and diligence
 - that a prudent man acting in a like capacity and familiar with such matters
 - would use in the conduct of an enterprise of a like character and with like aims;

- ❖ By diversifying the investments of the plan
 - so as to minimize the risk of large losses,
 - unless under the circumstances it is clearly prudent not to do so; and...

Fiduciary Rules Under ERISA

Fiduciary is a person who

- ❖ Exercises control or authority over the management of the plan or the plan's assets;
- ❖ Provides investment advice for a fee; or
- ❖ Has discretionary authority over the plan's administration

Fiduciary Rules Under ERISA

Common fiduciaries

- ❖ Plan sponsor
- ❖ Administrative and investment committees and their individual members
- ❖ Compensation committees and board members on the committees, individually
- ❖ Members of the Board who appoint committee members

Fiduciary Rules Under ERISA

Current Test: person is deemed an investment advice fiduciary if they meet five conditions. Provides advice:

- ❖ As to value of securities or other property, or makes recommendations as to advisability of purchasing or selling securities
- ❖ On a regular basis
- ❖ Pursuant to a mutual agreement with plan or plan fiduciary
- ❖ That will serve as primary basis for investment decisions with respect to plan assets, and
- ❖ That is individualized based on particular needs of the plan

Fiduciary Rules Under ERISA

Proposed Test: A person who

- ❖ Provides advice, appraisals or fairness opinions as to the value of investments, recommendations as to buying, selling or holding assets, or recommendations as to the management of securities or other property

and

Fiduciary Rules Under ERISA

Proposed Test: (continued)

- ❖ Does one of the following:
 - Acknowledges acting as a fiduciary within the meaning of ERISA, providing investment advice, or
 - Is a fiduciary under section 3(21) (A) (i) or (iii) of ERISA, or
 - Is an investment advisor under section 202(a)(11) of the Investment Advisors Act of 1940, or
 - Provides advice pursuant to an agreement, arrangement or understanding, written or otherwise, with the plan, plan fiduciary, plan participant or beneficiary, where the advice may be considered in making investment decision with respect to plan assets, and the advice will be individualized to the needs of the plan, plan fiduciary, plan participant, or beneficiary

Fiduciary Rules Under ERISA

Plan Sponsor Considerations

- ❖ Determine if proposed rule changes relationship with current providers
- ❖ Determine if proposed rule introduces any conflict-of-interest situations
- ❖ Consider utilization of 3(38) investment manager

Fiduciary Rules Under ERISA

Investment Advisor Considerations

- ❖ If fee only advisor, most likely already a co-fiduciary and no change in responsibilities. May want to consider offering expanded role as a 3(38) investment manager
- ❖ Currently brokers for the most part deny having fiduciary responsibility at plan level. Under proposed rule if broker provides services such as IRA roll-overs or annuity sales to plan participants, for compensation, they may trigger a prohibited transaction and have a conflict.
 - Need to determine what services they will or will not provide
 - Need to clarify for clients services where they are acting as fiduciary and services where they are not

Fiduciary Rules Under ERISA

Dilemma facing smaller plans

- ❖ May have relied on financial advisor to fulfill fund selection role
- ❖ May now need to engage RIA for this role. Costly!
- ❖ Are there other solutions available?

Q & A