

House Introduces 401(k) Fee Disclosure Bill

House Education and Labor Committee Chairman George Miller (D-CA), introduced the 401(k) Fair Disclosure for Retirement Security Act (H.R. 3185) on July 26, 2007. The bill is aimed at “hidden” fees that purportedly decrease 401(k) savings and disclosing potential conflicts of interest of service providers.

Hewitt is actively involved in the ongoing discussions surrounding this legislation. It is important to note that this bill has been only introduced and is not close to becoming law at this point. The bill will be vigorously opposed in this Congress and is fairly unlikely to be enacted this year or in 2008. However, Democrats are anticipating that 2009 will bring a Democratic-controlled administration as well as a Democratic-controlled Congress. If this happens, proponents of legislation such as this bill will believe they have a good chance of pushing the bill through to enactment. Hewitt will provide more insight and research on the topic of fee disclosure in the coming months.

Fee Disclosure for Employers

H.R. 3185 would impose new reporting and disclosure rules under ERISA. Employers would not be able to enter into a contract with a service provider unless the service provider provides a written statement containing specific information. The written statement would be required to:

- Identify who will be performing services for the plan and describe each service;
- Detail the expected itemized total annual cost of such services, including any amounts to be paid to affiliated or other third-party service providers.
 - Itemized fees would include commissions, start-up fees, expenses for investment management, fees for investment advice, trading expenses, administration and recordkeeping expenses, legal fees, trustee fees, termination or surrender charges, total asset-based fees, remuneration paid under Rule 12b-1 of the Investment Company Act of 1940, and other costs specified by the Secretary of Labor. Estimates could be used if actual amounts are not known. Materially incorrect estimates would have to be corrected and reported as soon as is practical.
- Include any conflicts of interest (of the service provider) due to a financial or personal relationship with the plan sponsor, the plan, or other persons providing services to the plan for which the service provider receives payment.
- Disclose that different share classes may result in different share prices within and outside of the plan.

- Include details on any “free” or discounted services or rebates from service providers and whether any consideration is obtained by the employer, plan, or service provider through direct or indirect charges to participants.

The Department of Labor (DOL) would be required to provide a model disclosure statement. The disclosure statement would have to be provided before a contract is entered into and annually thereafter. Employers would be required to provide a copy of the disclosure statement to participants within 30 days after receipt of a written request and also post a copy of the statement on any intranet site.

Fee Disclosure to Participants

Employers or plan administrators would be required to provide participants with investment election information as well as an annual benefit statement.

Investment Election Information

Plan administrators would be required to provide participants with the following information for each investment option:

1. Fund name;
2. Investment objectives;
3. Level of risk;
4. Amount of diversity (i.e., is the option a comprehensive investment, or should it be combined with other options to achieve retirement security);
5. Historical returns and percentage fee assessed against amounts invested;
6. Fees, including an explanation of asset-based versus other types of fees (additionally, see below for information on required “fee menu” requirement);
7. A comparison of the option to a “nationally recognized market-based index” or other investment option recommended as a “benchmark” retirement investment option;
8. Where and how additional information can be obtained; and
9. A statement explaining that funds should be selected not only based on fees, but on many factors such as risk and historical return.

Within this notice, a fee “menu” relating to all available investment options would have to be included, written in a manner easily understood by the average participant. The fee menu would be required to include any potential fees that could be assessed against a participant’s account in a plan year, including:

- A general description of each fee, including whether such fee is for investment management, commissions, administration, and recordkeeping.

- Details on the following investment options:
 - Fees that vary depending on the investment options chosen, such as the expense ratio, possible redemption fees, or any other asset-based fees;
 - Ongoing fees that are assessed as a percentage of total assets across all funds (not fund specific);
 - Administration and transaction-based fees that are automatically deducted or result from certain transactions, such as any ongoing administrative-type fees or transactional fees like loan origination costs.
- Disclosure of any conflicts of interest with respect to any service providers.
- Estimates could be used if actual amounts are not known. Materially incorrect estimates would have to be corrected and reported as soon as is practical.
- The DOL would be required to provide a model investment election notice. The notice would be required to be provided to participants and beneficiaries at least 15 days before the beginning of the plan year, the effective date of any material change in investment options, or upon enrollment.

Annual Benefit Statement

Plan administrators would be required to provide participants with an annual benefit statement. The annual benefit statement would have to include the following information regarding participant accounts:

- Starting balance;
- Vesting status;
- Annual contributions with separate totals for employer and employee contributions;
- Annual earnings;
- Annual fees assessed;
- Ending balance;
- Current asset allocation categorized by investment option, including current asset value, changes in value during the year, and the return for the year expressed as an amount and a percentage;
- Annual service fees charged for each investment option, including expense ratios, trading costs, total asset-based fees, mortality and expense charges, guaranteed investment contracts, employer stock fees, directed brokerage charges, plan administration fees, total fees, and total fees as a percent of current assets; and

- Annual performance by fund compared to a “nationally recognized market-based index.”

The benefit statement may also include information regarding historical risk and return information as well as an estimated amount of how much employees need to save each month to retire at age 65.

The DOL would be required to provide a model annual benefit statement. This statement would be required to be sent within 90 days after the close of each plan year.

Minimum Investment Option

The bill would require a 401(k) plan that allows participant control over the assets to include at least one investment option that is a “nationally recognized market-based index fund” that offers a combination of historical returns, risk and fees likely to meet “retirement income needs at adequate levels of contribution.”

Advisory Council

The bill would create a 12-person advisory council in which six of the members would be appointed by the President, three members would be appointed by the chairman of the Education and Labor Committee, and three members would be appointed by the chairman of the Senate Health, Education, Labor, and Pensions Committee. The council would consider issues affecting employee pension benefit plans, hold hearings, issue advisories, present best practices, and issue information and an annual report on Retirement Trends and Issues.

Enforcement

The Department of Labor would be required to provide model notices for the service disclosure statement, investment election notice, and annual benefit notice. The DOL would also conduct an annual audit of a representative sampling of plans to determine compliance with these new disclosure requirements. The DOL would refer violations to the Securities Exchange Commission and other regulatory agencies.

Effective Date

H.R. 3185 would generally apply to plan years beginning after the date of enactment.

Next Steps

The House Education and Labor and Ways and Means Committees are expected to hold hearings on the bill this fall.