

U.S. Department of Labor Issues Proposed Regulations on Required Disclosures to Plan Participants

The Department of Labor (the "DOL") has recently issued proposed regulations under Section 404(a) of the Employee Retirement Income Security Act of 1974 ("ERISA"), as amended, along with conforming proposed regulations under Section 404(c), that require disclosure of certain investment-related information to participants and beneficiaries in plans that permit them to direct the investments of their plan accounts ("Participant Directed Plans"). The proposed regulations are designed to ensure that participants and beneficiaries in Participant Directed Plans have the information they need to make informed decisions about the management and investment of their accounts. If the proposed regulations become final, the DOL has indicated that the final regulations will apply to plan years beginning on and after January 1, 2009. This update examines the proposed regulations, as well as the impact they will have on plan sponsors, fiduciaries, participants, beneficiaries, and service providers.

Overview of the Proposed Regulations

The proposed regulations establish uniform, basic disclosure for all participants and beneficiaries in all Participant Directed Plans, whether or not the plan fiduciaries have elected to voluntarily comply with Section 404(c) of ERISA. Specifically, the proposed regulations require all fiduciaries of Participant Directed Plans to take steps to ensure that participants

and beneficiaries are provided, on a regular and periodic basis, information that is sufficient to make them aware of their rights and responsibilities with respect to assets held in their accounts. This information may be divided into plan-related information and investment-related information that must be provided in a comparative chart or similar format.

Plan-Related Information

Plan-related information consists of general plan information and information regarding administrative and individual expenses. Generally, plan-related information must be disclosed to each participant on or before his or her date of eligibility to participate in the plan and on an annual basis thereafter and must be based on the latest information available to the plan. Plan fiduciaries should note that material changes to the plan must be disclosed to participants and beneficiaries within 30 days after the adoption of such changes, not after the effective date of such changes. Disclosure of all plan-related information may be provided by a plan fiduciary or his or her designee.

The proposed regulations require disclosure of the following general plan-related information:

- an explanation of the circumstances under which participants and beneficiaries may give investment instructions and any limitations on such instructions under the terms of the plan, including restrictions on transfer between investment alternatives;
- a description of, or reference to, plan provisions relating to the exercise of rights incumbent with an investment in an investment alternative, as well as any restrictions on such rights;
- an identification of all designated investment alternatives available under the plan;
- an identification of all designated investment managers; and
- an explanation of the plan's day-to-day operational expenses that will be charged generally against their individual accounts, as well as the expenses that are assessed on an individual basis.

Under the proposed regulations, participants and beneficiaries must be provided with an explanation of any fees and expenses for plan administrative services (such as legal, accounting, and recordkeeping) that may be charged to the plan and the basis for allocating these expenses to their accounts (such as pro rata or per capita), as well as an explanation of any fees and expenses that may be specifically charged against their accounts for services specifically provided to their accounts. In addition to this general disclosure, information regarding the amount charged during the preceding quarter to the participants' or beneficiaries'

accounts for administrative and individual services, along with a brief description of such services, must be provided on a quarterly basis. This individual information may be provided to participants and beneficiaries on their quarterly benefit statements.

Investment-Related Information

Under the proposed regulations, certain investment-related information must automatically be provided to participants by a plan fiduciary before the date of plan eligibility *and* on an annual basis thereafter. In addition, certain other investment-related information must be disclosed upon a participant's or beneficiary's allocation of funds to an investment alternative under the plan.

Automatic Disclosure of Information

The proposed regulations require automatic disclosure, in a comparative format, to participants and beneficiaries of general information regarding each designated investment alternative as well as specific performance data and fee information with respect to each such alternative. This general information includes the type or category of each alternative (such as a money market fund or a balanced fund), whether each alternative is actively or passively managed, and a web site address that will direct participants and beneficiaries to certain performance and other information regarding each designated investment alternative.

The specific performance data that must be disclosed depends on whether the investment alternative has a fixed rate of return. If the investment alternative has a fixed rate of return, only the rate of return and the term of the investment must be disclosed. If the investment alternative does not have a fixed rate of return, the required disclosure includes the average annual total return (expressed as a percentage) for the preceding one-year, five-year, and ten-year periods and a statement to the effect that past performance is not necessarily an indication of how the investment will perform in the future. These average annual returns must be benchmarked against an appropriate broad-based securities index.

Similar to the required performance data, the fee information that must be disclosed depends on whether the investment alternative has a fixed rate of return. If the investment alternative has a fixed rate of return, the amount and a description of each fee charged directly

against a participant's or beneficiary's account in the event of a purchase, transfer, or withdrawal involving the investment alternative must be disclosed. If the investment alternative does not have a fixed rate of return, the required disclosure includes the amount and description of each fee charged directly against a participant's or beneficiary's investment (such as sales loads, sales charges and redemption fees), the total annual operating expense of the investment alternative (e.g., the expense ratio), and a statement that fees and expenses are only one of several factors that should be considered when making investment decisions.

The investment-related information described above must be disclosed to participants and beneficiaries in a comparative format, such as a chart or a table, that is designed to facilitate a comparison of each designated investment alternative. The DOL has issued a model chart that may be used to satisfy this requirement.¹ Participants and beneficiaries must also be provided with the contact information of the person responsible for providing them with information upon request and must be informed that more up-to-date information regarding investment alternatives can be found at the previously disclosed web site.

Subsequent to an investment in a designated investment alternative, plan participants and beneficiaries are to receive any materials provided to the plan relating to the exercise of voting, tender, and similar rights to the extent that the plan passes such rights through to plan participants and beneficiaries.

Information Available Upon Request

Participants and beneficiaries may request copies of a prospectus or summary prospectus (or similar

¹ www.dol.gov/ebsa/modelcomparativechart.doc

documents for non SEC-registered investment alternatives), copies of financial statements, reports and related documents (but only to the extent provided to the plan), a statement of the value of shares or units (including the date of valuation), and a list of assets comprising the portfolio of each investment alternative that constitutes "plan assets" within the meaning of ERISA, including the value of each asset (or portion of the investment that it comprises).

Effect of the Proposed Regulations

Much of the information required to be disclosed under the proposed regulations is already required to be disclosed by fiduciaries who have elected to comply with Section 404(c) of ERISA in order to take advantage of the fiduciary liability relief provided by such Section to plan fiduciaries of participant-directed plans. However, the proposed regulations add additional disclosure requirements with respect to such fiduciaries and impose new disclosure requirements on plan fiduciaries who have not elected to comply with Section 404(c) of ERISA. Plan sponsors and fiduciaries need to determine how their current practices may be impacted by the proposed regulations.

In these regulations, the DOL explicitly states that the limitation on fiduciary liability provided under ERISA Section 404(c) does not extend to the selection and monitoring of investment options made available to plan participants.

Comments on the proposed regulations may be submitted to DOL by email to e-ORI@dol.gov (Participant Fee Disclosure Project).

Practice group contacts

If you have questions regarding the information in this legal update, please contact the Dechert attorney with whom you regularly work, or any of the attorneys listed. Visit us at www.dechert.com/employeebenefits.

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