

Defined Benefit Retirement

Don't become a cautionary tale

Sponsors must beware paying plan expenses from the plan

BY PAT BYRNES

An employer might ask: Can plan expenses be paid from my pension plan or 401(k) plan? Yes, they certainly can and, in fact, probably already are.

However, the decision to do so must be made by the responsible plan fiduciaries who make sure that proper documentation and disclosures are provided.

This is important because, in light of recent financial turbulence,



many plan sponsors are looking for ways to reduce corporate costs.

Since the Department of Labor in 2003 issued guidance allowing expenses to be allocated differently among active and terminated participants, much more focus has been placed on expenses being paid from a retirement plan.

Fiduciaries have the responsibility to ensure that only reasonable expenses are being incurred in the operation of the plan.

If expenses are to be passed on to participants — i.e., paid by the plan — they must be what is known as “plan expenses.”

If expenses paid by the plan are either not plan expenses or are not reasonable, a fiduciary breach may be incurred.

DOL generally takes the position that if a fiduciary breach does occur, it must be unwound — the expenses are paid back to the plan by the plan sponsor.

Since the collapse of Enron, there has been much more focus on the duties and responsibilities of the fiduciaries.

In 2007, a large number of class-action lawsuits were filed against large plan sponsors over the issues of expenses being paid by the plan.

Eligible expenses

Eligible expenses are generally operational expenses, as opposed to costs associated with the design and implementation of a plan.

For example, the creation of plan documents associated with the initial adoption of the plan, as well as all le-

gal fees associated with such adoption, would generally be settlor expenses, which may not be paid by the retirement plan.

In many Department of Labor matters, bright-line interpretations generally do not exist.

However, over the years, DOL has issued several pieces of guidance around the section of ERISA governing this matter.

Based on these bits of guidance, plan expenses in both defined contribution and defined benefit plans may include:

- Costs incurred to secure an IRS Favorable Determination Letter on the plan.
- Annual accounting of trust assets.
- Cost of valuing assets in the plan.
- Service provider fees, which could include third-party recordkeeping, accounting fees, preparation of employee communication materials and summary plan description.
- Fees related to trustee and custodial services, investment adviser fees, investment management fees, asset management fees, broker commissions and banking fees.
- Legal fees in making the determination of a domestic relations order of status as a qualified domestic relations order.
- Expenses due to selecting, appointing and monitoring fiduciaries.
- Premiums for fiduciary liability policies and fiduciary bonds.
- Fees for implementing the decision to terminate a plan.

However, fees with respect to making the decision to terminate a plan are not plan expenses.

Disclosure

In 2003, the DOL gave broad discretion to responsible plan fiduciaries in deciding how plan expenses could be allocated to participants and beneficiaries.

This discretion includes whether to allocate an expense on a per capita or pro rata basis and/or to allocate an ex-

It is likely that there will be legislation that will require disclosure of expenses being allocated to participants' accounts.

pense directly to the account of a participant on whose behalf the expense was incurred.

For example, a plan could treat active and terminated participants differently.

It is becoming increasingly more popular for employers to make this distinction and to allocate certain ongoing administrative and distribution expenses directly to terminated participants if they do not remove their monies from the plan shortly after termination.

Regardless of whether plan expenses are incurred for active or terminated participants, expenses should be spelled out either in an addendum or an amendment to the summary plan description.

This is often referred to as an expense policy.

Expenses should not be paid by the plan unless the participants are informed in advance of what those expenses are and how they are to be allocated.

Since we are in an era of disclosure, it is recommended that specific dollar amounts for various expenses that are being passed on to the plan participants be stated in the communication materials.

Reasonableness

There is no specific standard of reasonableness of expenses, although DOL's Web site does include a 401(k) fee disclosure form tool. In the next couple of years, it is likely that there will be federal legislation that will require line-item disclosure of specific expenses being allocated to the participants' accounts on

benefit statements for defined contribution plans. With that extra disclosure, new standards of reasonableness will evolve quickly. Once total participant costs for general administrative services and investment management exceed 300 basis points or, in small plans, something in the area of \$150 to \$200 per year, the question of reasonableness may begin to surface.

There is an increased likelihood that the House may call for a floor vote on a pending 401(k) participant level fee disclosure bill before the August recess. In addition, the Department of Labor has issued proposed guidelines on plan level fee disclosures, which are likely to be finalized for a January 2009 effective date. Retirement plan fee disclosures are big on our government's mind. Certain plan expenses can be borne by the participants in defined contribution and defined benefit plans. The decision to allocate fees among participants is a fiduciary matter that should be the result of following prudent fiduciary processes to make sure fees are legitimate, reasonable and properly disclosed. —**E.B.N.**

Pat Byrnes is president of Actuarial Consultants, a Torrance, Calif.-based firm that provides retirement plan administration and consulting services.

In recent years, “much more focus has been placed on expenses being paid from a retirement plan.”