Got Mail?
Participant Notices in Retirement Plans

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Got Mail?
Participant Notices in Retirement Plans

- The Range of Participant Disclosures
  - IRS
  - DOL
- Participant Fee Disclosure Notices:
  - 404(a)
  - 404(c)(5):
  - Target Retirement Funds & QDIA Regulations
- Workflow Processing & Electronic Distribution
The Changing Retirement Plan Paradigm

- 401(k) Plans are overtaking DB Plans as the Primary Retirement Plan in the US
- Participants must increasingly take responsibility for their own retirement planning and saving
- The Government Agencies want Participants to have fundamental information regarding their Retirement Plans and Benefits
- Participants do what is easy, not always what is “rational”—Behavioral Finance/Paradox of Choice
Is that all?

- There can be up to 45+ disclosure documents required by both DOL and IRS depending on Plan design & Investment alternatives
- Generally, DOL and IRS do not allow “cross-reference” or reliance on other agencies’ disclosure for participants:
  - Each Agency creates its notices relative to its own jurisdiction:
    - DOL will allow combining notices under its purview: quarterly benefit statements with quarterly participant disclosure
    - IRS will not allow Safe Harbor Notice to reference Plan Design already given to Participants via the SPD

DOL vs. IRS Disclosure

**DOL**

- Disclosure in order to satisfy Fiduciary Obligations
- May or May not be Plan-Design Driven
  - 404(a) Disclosures for Plan Fees & Investments
  - 404(c) & QDIA Disclosures
  - Quarterly Benefit Statements
  - SPD

**IRS**

- Disclosure for Tax-Qualified Status
  - Includes Notices/Forms
- Qualification Requirement:
  - Plan Design Driven:
    - Safe Harbor Notice
  - Event Driven:
    - 402(f) Special Tax Notice for Distributions
    - 204(h) Future Benefit Accruals Notice
## IRS: Safe Harbor Notices

- Safe Harbor formula (Match or Non-Elective)
  - Allocation Provisions
  - Administrative: how/when can make changes, or take withdrawals and
  - Vesting provisions that apply to contributions
- Timing:
  - 30-60 days prior to plan year start
- Operational failure to not give notice
  - Can’t default to plan ADP/ACP testing

## DOL: Auto-Enrollment Notice

Eligible participants must receive an automatic enrollment notice prior to being enrolled in the Plan:

<table>
<thead>
<tr>
<th>WHEN</th>
<th>CONTENT</th>
<th>OPT-OUT</th>
</tr>
</thead>
</table>
| The Plan Sponsor must give the notice a reasonable period before each plan year | **Notice must explain:**
  - Employee’s right to opt out or defer at a different percentage
  - Default investment to which deferrals will be directed | Following receipt of notice, employee must have reasonable period of time to opt out of arrangement and direct investment of his deferrals. |
| A 60-30 day decision period is a “safe-harbor” timeframe | | |
Fee Notices: 404(a) Participant Disclosures

When Do You Comply?

• For Calendar Year Plans, the initial participant disclosure needed to be provided by August 30, 2012.
  • The 2013 Notice is due a year from when it previously was sent.
• For a calendar year plan the first quarterly fee disclosure must be provided by November 14, 2012.
  • Typically the participant’s quarterly statement was changed to comply with the disclosure rules.
Timing for Annual Disclosures:
Plan Related Information

“On or before the date of first investment direction and at least annually thereafter”

- At least once in any 12-month period, without regard to whether the plan operates on a calendar or fiscal year basis
- So, you can pick the timing, so long as you provide the information no more than 12 months after you provided it last

- DOL 18 Month Exception for 2013 or 2014
  - The DOL provided a single year exception for plans (and service providers) to “catch up” to align the participant 404a-5 disclosure with year-end disclosures that may need to go to participants
  - DOL also working on potential guidance to address notice “creep”

If a change is made to the investments in a Plan, an updated disclosure must be provided 30-90 days before effective date of the change, but there is flexibility to provide notice closer to effective date if investment change must occur more quickly.

- If there will be a black out period associated with the investment change, the disclosure notice can be distributed along with the SOX black out notice.
Who Receives Disclosure

• All Eligible Participants:
  • “Each participant or beneficiary that, pursuant to the terms of the plan, has the right to direct the investment of assets held in, or contributed to, his or her individual account”
    ▪ Do you need to provide disclosure to someone with $0 account?
      ✓ Yes
    ▪ Do you need to provide disclosure to someone with account > $0 but no vesting?
      ✓ Yes

404(a) Participant Disclosure Framework

<table>
<thead>
<tr>
<th>Initially/Initial</th>
<th>Initially/Annual</th>
<th>Quarterly</th>
<th>Upon Request</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Descriptive</strong></td>
<td><strong>Comparative</strong></td>
<td><strong>Actual Expense</strong></td>
<td><strong>Legal Detail</strong></td>
</tr>
<tr>
<td>Participants’ Rights</td>
<td>Investment Specific data:</td>
<td>Specific <strong>dollar amount</strong> taken from Participant’s account for plan expenses</td>
<td>• Prospectus or Summary Prospectus</td>
</tr>
<tr>
<td>Type of Investment Alternative</td>
<td>Expenses &amp; performance vs. Benchmark</td>
<td>Must have label/description: “Loan set up fee”</td>
<td>• Annual Reports</td>
</tr>
<tr>
<td>Fund Management</td>
<td>Website for more info</td>
<td></td>
<td>• Summary of underlying holdings</td>
</tr>
<tr>
<td>Voting rights</td>
<td>Annuity specific information</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Plan-based Fees</td>
<td>Fixed Account rate/date/restrictions</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Participant/transaction fees</td>
<td>Annuity info</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ER stock, etc.</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Any change warrants new disclosure to participants—No longer “material” standard
Annual plan information can be provided:

- In summary plan description or
- In participant benefit statement
- But watch frequency--
  - If you “package” expense information in an SPD and the information changes, then you will potentially need to provide an updated SPD

Quarterly information can be provided in/as part of the participant benefit statement

So…Where is the uproar?

- Most fee disclosure was met quietly by participants
  - Lack of understanding
  - Too Busy
  - Just not vocal?
- Quarterly Statement may be more specific, but employees may not be paying attention and/or revenue sharing may or may not show as a line item.
Fee Notices: 404(c) Participant Disclosures

404(c) Compliance Greatly Simplified

- Although organized differently, essentially all information 404(c) regulations previously required is now required under 404(a)
  - Plus
    - Information on plan expenses
    - Benchmarks
    - Requirement of chart
    - Required “statements”
- Prospectus not provided automatically
- Plan no longer needs to describe investment objectives and risk/return characteristics of each alternative
Important Side Note

• 404(c) regulations will get a new statement:
  • Compliance does not serve to “relieve a fiduciary from its duty to prudently select and monitor any designated investment manager or designated investment alternative offered under the plan”

• 404(a) regulations will get a new statement:
  • compliance will not “relieve a fiduciary from its duty to prudently select and monitor providers of services to the plan or designated investment alternatives offered under the plan”

No Comment on Prior Periods

• If plan satisfied 404(c) before final regulations, fine
  • “The Department expresses no view with respect to plans that did not comply with section 404(c) and the regulations thereunder as to the specific information that should have been furnished to participants and beneficiaries in any time period before this regulation is finalized.”
404(c)(5): Target Retirement Funds & QDIA Notices

Under 404(c)(5)…

“fiduciary is not liable for any loss or by any reason of any breach that occurs as a result of an investment in a qualified default investment alternative…as long as participants & beneficiaries receive information concerning the investments made on their behalf…”
QDIA: 404(c)(5) Protection & Notice

In order for Fiduciary protection for default investments in QDIAs

### Required Notice Content

- Identification of default investment
- Investment objectives
- Risk/return characteristics
- Fees

### Disclosure Upon Request

If participant’s account invested in QDIA, participant entitled to 404(c)(1) investment information:

- Prospectus/profile
- Proxy, etc. information
- Information available on request

Proposed Target Retirement Date Fund Regulations

Updates the Qualified Default Investment Alternative Regulations

Fiduciary Relief for Default Investment Alternatives granted if the disclosure complies with the new Participant Disclosure Regulations under 404(a)
Proposed Target Retirement Fund Regulations

Target Retirement Fund Disclosure to provide great specificity for the participant as to how the fund is designed.

- **Structure of the Target Retirement Fund portfolio**
  - Description & illustration:
  - "Glide Path"--How does the fund’s allocation change pre & post the “target date”
  - “Landing point”--when does the fund get to its most conservative allocation, the “landing point”

- **Risks associated with these Funds**

- **What Age or type of individual, is the fund designed**

- **“Caution” disclosure language:**
  - “Not All Funds Created Equally
  - You may loose money, etc.

Workflow Processing:

➤ Using Technology to Facilitate Disclosure
Electronic Distribution to Manage Participant Disclosure

- There is much interest and lobbying to allow electronic disclosure to become the “norm” and participants can elect out of electronic disclosure.
- Technology can facilitate prioritization of information, allowing participants to “click through” to more detail.
- Workforces are becoming more technically savvy:
  - An increasing number of workplaces allow telecommuting by their employees;
  - Traditionally non-desk driven jobs are connected via smartphones to their workplaces and can access email or their company’s intranet systems remotely via these devices.
  - Large Plan participants take for granted that information will be available to them on their service provider’s website.

Electronic Disclosure Methods

**DOL**

- Active Consent
- Alternative:
  - If computer is “reasonably accessible” as an integral part of duties, disclosure may be furnished electronically to Plan participants.
  - “Ever-green” secure websites may be used for disclosure in certain circumstances:
    - Glossary for investment terms if referenced on 404(a) chart
    - Plan Administrator must take steps to ensure receipt

**IRS**

- Active Consent
- Alternative:
  - If participant is “effectively able” to access electronic medium, then okay to furnish disclosure electronically to participants.
  - Recipient must be advised they can get a paper copy of the notice at no charge.
  - Plan Administrator does not need to ensure receipt.
DOL Technical Release 2011-03

  - Multiple parts/types of disclosure under 404(a)(5)
  - Clarifies that if electronic disclosure was permitted via a website in prior guidance (FAB 2006-03), then 404(a)(5) can be provided on website.
  - Can use electronic media to distribute 404(a)(5) material (initial, annual and quarterly notice) if affirmative consent satisfied, or if alternative arrangement is satisfied
    - Depending on timing of participant eligibility for the initial 404(a)(5) notice, paper disclosure may be more practical

Workflow Processing:

➢ Plan Sponsor Expectations
Most Recordkeepers/Investment Custodians will be doing the heavy lifting as far as preparing the required participant disclosures—if they are being engaged as a retirement plan recordkeeper.

“Can we outsource it?…”

Managing Participant Disclosures is a Consulting Opportunity

- The Plan Fiduciary/Plan Sponsor is generally always legally responsible for providing required Plan disclosure notices to participants
  - They will look to outsource to their Service Providers
- Plan Design will inform required notices
- Use Vendor software if possible.
- Template your own notices as much as possible.
  - EX: Safe Harbor Notice, Special Tax Notice—3 party software
  - Fund Change Notice: Draft a template form & re-use it
  - Use internal Technology to create a “Library of forms”
Assumed Outsourcing

- Most employers have relied on their Recordkeepers/investment custodians to prepare the required participant disclosures—as well as distribute the notice if they are willing.
- If the client’s 401(k) service arrangement is with a TPA using a individual brokerage account to provide a 401(k) solution—the participant disclosure will need to be addressed by the TPA.
  - TPA may need to create or partner with brokerage company for investment related information.
- If a broker is involved he/she may or may not provide the disclosure per the guidelines/policy of their broker-dealer.

A Single Year-End Statement

- A Year-End/Beginning of the Plan Year Statement that consolidates all participant disclosures for investments and plan design will hopefully become the norm:
  - Annual Investment disclosures
  - QDIA notice
  - Safe Harbor Notice
  - Chart with Investment Performance Data
  - For TPAs who must prepare this in-house- returns data is available on the internet or via third party subscription services like Morningstar Principia, or Newkirk.
Less Flexibility with Large Recordkeepers

- Annual Disclosure Statement Drafted by Recordkeeper
  - Recordkeeper will distribute (nominal fee)
  - Won’t bundle all notices to year-end
- Fund Changes require Plan Sponsor/Broker to draft Fund Change Notice (may or may not require SOX black-out notice language)
- ALT: Notice may be automatically updated monthly & posted for participants

More Robust Quarterly Benefit Statements will Drive Change If Participants Decide to Act

- Quarterly Benefit Statements include the actual fees against participant’s accounts.
  - Many statements already show fees; labeling will become more precise
  - Explicit nature of fees will require Plan Sponsors to “own” their cost-sharing arrangements, but participants may likely blame their service providers
  - Education opportunity!
Can You Keep it To 1 Page?

- When Drafting Notices, determine:
  - Disclosure to Inform?
  - Disclosure to drive participant action
- When possible keep to one page: create a table or illustration or chart to make information more concise
- EX:
  - Show Target Date funds in a QDIA notice as a chart
  - Show current vs. new funds in a Fund Change Notice—don’t write out the changes in paragraph form.

In Conclusion

- The Future with Increased Disclosure
Plan Sponsors Will Push For

- Fee Compression
- Service Based Pricing
- Participant Fee Equity

Continuing Pressure for Fee Compression

- Consultants and Plan Sponsors will continue to press service providers to price more aggressively or provide increased levels of service for the same price
- Service providers will need to look for additional sources of revenue
- Service providers will need to increase efficiencies and refine service levels
Continuing Interest in Outsourcing

- Unless extremely budget conscious, plan sponsors want to outsource draft & distribution to service providers.
  - May do internal email, but terminated participant mailings are the hang up
  - Increased awareness & interest (and budget) for fiduciary administration services

Plan Design & Investment Offerings Will Shift

- Plans with limited fund windows may curtail this offering unless disclosure can be provided electronically or the service provider (investment provider) absorbs some of the cost of the fund disclosure materials.
  - There are third-party disclosure/documentation sources that can partner with the major independent recordkeeping software systems to provide independent TPAs & recordkeepers most of the annual and comparative information.
In my opinion...

• DOL is keen on providing participants meaningful disclosure so they have better opportunity to control their retirement destiny
• DOL also holds Plan Sponsors—as the fiduciary—responsible to provide this disclosure.
  • DOL Not satisfied with the “Voluntary Status” of “traditional” 404(c) to accomplish this goal
  • DOL Not satisfied with current QDIA disclosure regarding Target Retirement Funds

In my opinion...

• DOL is open to electronic communication & graphic representation to satisfy disclosure requirements:
  • Chart
  • Target Date Illustration
• DOL is reaching out to the SEC & FINRA—Securities Regulatory entities for support of their regulations
  • It is unclear but likely that the IRS will still mandate their own participant disclosures where they have authority
• Service providers have a great value proposition to provide education & guidance to both Plan Sponsors and Participants.
  • As much as possible - Batch Process:
    ✓ Existing disclosure for participants
    ✓ Combine with other notices
  • Promote electronic disclosure methods and training

Questions?