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Final DOL 408(b)(2) Disclosure Regulation

Final regulation provides a number of helpful clarifications and changes, but continues to impose what will be a highly burdensome disclosure framework.

February 8, 2012

As described in our LawFlash dated February 2, 2012,[1] the Department of Labor (DOL) has issued a final regulation adopting disclosure requirements for retirement plan service providers under Section 408(b)(2) of the Employee Retirement Income Security Act of 1974 (ERISA). That LawFlash focused mainly on the extension of the effective date to July 1, 2012 for providing the required disclosures. This LawFlash examines the changes from the interim final regulation that was published in July 2010. For a comprehensive review of the disclosure rules based on the interim final regulation, see our LawFlash dated July 21, 2010.[2]

The final regulation makes several changes and clarifications to the disclosure requirements, including a statement about the permissibility to use estimates and ranges of fees and confirmation of the ability to provide the disclosures electronically. Importantly, it coordinates the provisions on information regarding participant-directed plan investment options with the new participant-level disclosure requirements for such plans. Discussions in the preamble also emphasize the responsibilities of plan fiduciaries to review the disclosed information, and a change to the exemptive relief for such fiduciaries highlights the need for them to terminate noncompliant service providers.

Disclosure Requirements

Many of the comments on the interim final regulation asked for clarifications of, or changes to, the requirements for disclosing the services to be provided under a covered service arrangement and for disclosing "indirect" compensation received by the covered service provider in connection with the arrangement. In response, DOL made a few changes and offered a number of clarifications.

1. See "DOL Releases Final 408(b)(2) Disclosure Regulation" (Feb. 2, 2012), available online at http://www.morganlewis.com/pubs/EB-LF_Final408b2DisclosureRegulation_02feb12.pdf.

2. See "DOL Publishes Interim Final ERISA Regulation on Service Provider Disclosure Obligations" (July 21, 2010), available online at http://www.morganlewis.com/pubs/EB-LF_DOL-InterimFinalReg-ServiceProviderDisclosureObligations_21july10.pdf.

Services Disclosure

In the final regulation, DOL clarified two points with regard to the requirement to disclose a description of the services to be provided.

DOL had said in the preamble to the interim final regulation that a detailed description of the services may not be necessary when the parties already understand the nature of the services. DOL declined to further define the level of detail necessary. It said only that responsible plan fiduciaries have a duty to carefully review the information they receive when entering into a service arrangement and that the regulation requires that they receive the basic information needed to make informed decisions about service costs and potential conflicts of interest. If plan fiduciaries need assistance in understanding any of the furnished information, their duty to act prudently obligates them to request assistance, either from the service provider or third parties.

DOL clarified that a covered service provider must describe all the services that will be provided pursuant to the contract or arrangement, not just those that make it a “covered” service provider. This includes services that will be performed by its affiliates and subcontractors pursuant to the arrangement.

<u>Observations</u>

It is likely that many disclosures will consist of a general overview of the services to be provided, with a reference to the contract terms for more detailed information. Such an approach would presumably meet the described standard.

Compensation Disclosure, Including Estimates and Ranges

Two key concepts under the final regulation are those of “direct” compensation and “indirect” compensation, both of which must be disclosed by the covered service provider.

DOL noted that “direct” compensation includes compensation that is initially paid by the plan sponsor, but is then reimbursed from the plan. DOL said that parties cannot avoid disclosure by creating intermediary payments and arguing that, as a technical matter, such payments do not constitute “compensation.”

With regard to “indirect” compensation, DOL added a new requirement that the covered service provider identify not only the payer of the compensation, but also describe the arrangement between the payer and the covered service provider, affiliate, or subcontractor, as applicable, pursuant to which the indirect compensation is paid. This is intended to illustrate potential conflicts of interest resulting from the receipt of indirect compensation, permitting the responsible plan fiduciary to analyze why the payer, which is generally an unrelated third party, is making the payment in connection with the service contract or arrangement. DOL said it intends that the concept of compensation to be received “in connection with” a particular service contract or arrangement be construed broadly, to include compensation that a covered service provider reasonably expects to receive that is based in whole or in part on the service arrangement with the covered plan. As an example of what would be included, DOL cited an arrangement described in a 2010 DOL Office of Inspector General report on plan conflicts of interest, under which a service provider had not disclosed that certain financial institutions with respect to which it may be making recommendations had subsidized conference costs for the service provider's clients.

Commenters had expressed concern about the ability of a broker-dealer to properly identify the payer of indirect compensation in advance of brokerage window and similar arrangements. DOL responded that indirect compensation for this purpose may be described in general terms, "provided that the description contains information that is sufficient to permit a responsible plan fiduciary to evaluate the reasonableness of such compensation in advance of the service arrangement." Under this standard, the description need not identify the specific payer if such information were unknown at the time the disclosure is made, but should provide information that would allow the responsible plan fiduciary to compare the expected compensation with the compensation that would be received by competing broker-dealers for similar services.

In the definition of "compensation," DOL clarified that the use of estimates in providing compensation disclosure is not limited to recordkeeping costs, as appeared to be the case under the interim final regulation. Therefore, a description of compensation or cost may include a "reasonable and good faith estimate" if the covered service provider cannot otherwise readily describe it, provided that the methodology and assumptions used to prepare the estimate are explained.

Some commenters asked whether compensation or cost may be disclosed in ranges. DOL said that disclosure of expected compensation in the form of known ranges can be a "reasonable" method if it is reasonable under the surrounding circumstances. To ensure that the compensation information is meaningful and understandable, DOL said that "more specific, rather than less specific, compensation information is preferred whenever it can be furnished without undue burden."

Observations

This guidance is helpful in several respects. The issue of being unable to identify the payers of indirect compensation in advance may arise in instances other than brokerage windows, so the approach described by DOL presumably can be applied in those other situations. It is important to have confirmation of the ability to use estimates and ranges, as that is the only feasible approach in many instances. But the need to disclose indirect compensation may still pose many issues and challenges for covered service providers.

Recordkeeping Services

One of the potentially more challenging aspects of the disclosure rules is the provision on recordkeeping services. It requires that if the services were provided without an explicit recordkeeping charge, or with a recordkeeping charge that is offset or rebated based on other compensation received, the covered service provider must furnish a "reasonable and good faith estimate of the cost to the covered plan of such recordkeeping services," including an explanation of the methodology and assumptions used to prepare the estimate and an explanation of the services to be provided.

Commenters were concerned that the breadth of the definition of "recordkeeping services," and the fact that the cost figures provided may be "mere estimates," would make it difficult for responsible plan fiduciaries to make meaningful comparisons. DOL said that it had constructed the provision to manage these concerns. The definition of "recordkeeping services," while broad, is designed to ensure that providers of these services will be covered service providers and will not avoid their disclosure responsibilities by narrowly defining the services they provide. The requirement that the provider include a "detailed explanation of the recordkeeping services that will be provided to the plan" should better enable a responsible plan fiduciary to understand precisely what is being included so as to facilitate comparisons. The estimates issue is addressed by the requirement that the disclosure include an explanation of the underlying methodology and assumptions, to enhance the ability of responsible plan fiduciaries to analyze and compare estimates.

Observations

While the required explanations will be helpful in facilitating comparisons, they highlight the challenge that recordkeepers will face in fully explaining their "reasonable and good faith estimates" in a manner that aids comparability, and the burden for plan fiduciaries in being able to sort through varying levels of explanations to determine what arrangement would provide the best value for their plans. It had been predicted that services would develop for benchmarking recordkeeping service costs. That is already occurring, but they pose the same challenge of presenting recordkeeping service data in a manner that illustrates both the commonalities and differences for comparative purposes.

Participant-Directed Plan Investment Alternatives

Where a plan makes a direct equity investment in an investment fund, the rules require disclosures about the fees and expenses associated with an investment in the fund. The only change made here is to coordinate this provision with the rules on disclosures of "investment-related information" under DOL's new participant-level disclosure rules for participant-directed individual account plans. For a designated investment alternative under such a plan, the fee and expense disclosure requirements of the final regulation are cross-referenced to the participant-level disclosure regulation, so that the plan administrator will receive the information from the covered service provider in a form it can then use to comply with the participant-level disclosure rules. Some of the wording has been modified to make the two rules consistent.

An additional subsection has been added to require that, for a designated investment alternative, the covered service provider must provide any other information or data that is required for the plan administrator to comply with the participant-level disclosure requirements, to the extent such information is within the service provider's control or is reasonably available to the service provider. DOL does not intend this requirement to create a new or increased burden, or to require the preparation of information not otherwise reasonably available to the service provider. For example, in the case of mutual funds, this requirement should be satisfied through providing the fund prospectuses and should not require the service provider to seek any additional information from the fund issuer. DOL described this provision as covering information such as identifying information about designated investment alternatives, performance data, benchmarks, principal strategies and risks, fees and expenses, and portfolio turnover rate, even for annuity options and employer securities (to the extent applicable). However, the covered service provider would not be responsible for preparing the required glossary of terms, which is not specific to particular investments, or for the overall obligations of the plan administrator, which continues to bear legal responsibility for providing the participant-level disclosures.

Similar disclosures are required from covered service providers that provide recordkeeping and brokerage services to participant-directed individual account plans, so that parallel changes were made to that provision. However, several commenters did not think that brokers/recordkeepers should be responsible for furnishing investment information for designated investment alternatives that are not on their platform. DOL disagreed, saying that the broker/recordkeeper is in the best position to furnish the required information about plan investment options. DOL pointed out that the concerns would be addressed by the rule permitting the broker/recordkeeper to meet this requirement through providing current disclosure materials of the fund issuer or information replicated from such materials. (The "replicated from such materials" clause, which is new in the final regulation, was added to avoid discouraging brokers/recordkeepers from consolidating or summarizing the required information in a more user-friendly format.)

The rule permitting reliance on issuer disclosure materials applies only if the issuer is not an affiliate of the broker/recordkeeper. DOL confirmed that the broker/recordkeeper can also pass through disclosure materials from affiliated issuers and need not prepare separate materials to meet the disclosure requirements. However, unlike with materials for nonaffiliated issuers, the broker/recordkeeper would be responsible for the accuracy of the content.

The interim final regulation also had required that the disclosure materials be regulated by a state or federal agency. In response to comments that this limitation would dissuade plan fiduciaries from offering products such as collective trusts and insurance general accounts, DOL revised it to focus instead on regulation of the issuer. The final regulation requires that the issuer be a registered investment company, an insurance company qualified to do business in a state, an issuer of a publicly traded security, or a financial institution supervised by a state or federal agency.

A further requirement of this provision in the interim final regulation was that the covered service provider not know that the disclosure materials being provided are incomplete or inaccurate. This has been supplemented in the final regulation by requirements that the service provider act in good faith and that the service provider furnish the responsible plan fiduciary "with a statement that the covered service provider is making no representations as to the completeness or accuracy of such materials." The latter provision does not require that the covered provider furnish a separate statement for each disclosure item. According to DOL, it could be met by a single statement in the service contract, along with a description of the investment disclosure materials to which the statement applies.

In connection with the provision on disclosure errors, commenters asked about the ability of recordkeepers to use data obtained from a central digital database of investment fund information maintained by a third party, which the commenters said would be more efficient. DOL said that using a reputable and reliable third-party commercial database would ordinarily be consistent with the rule's "good faith" and "reasonable diligence" requirements, which are prerequisites for being able to treat a corrected error as not violating the rules. According to DOL, an important element in demonstrating the reliability of the information would be a contractual provision that makes the third-party provider responsible for ensuring that the information in the database is passed on accurately. If the covered service provider were to become aware of an error or omission in the data, it would need to disclose the error within 30 days after learning about it to meet the error correction rule.

Observations

Because the information that will be used by plan administrators to meet the participant-level disclosure requirements is expected to be provided mostly by plan recordkeepers, the changes made by DOL are important to ensure consistency between the two disclosure rules. In accordance with the final regulation, plan recordkeepers should include in their disclosure materials the required statement about not making any representation about the completeness and accuracy of third-party disclosures. In addition, to be able to rely in good faith on third-party commercial databases, they should incorporate the type of contractual provision described by DOL in their arrangements with database providers.

Self-Directed Brokerage Arrangements

Commenters asked for clarification on what information would have to be disclosed concerning brokerage windows and similar arrangements.

These arrangements are not included in the definition of "designated investment alternatives," so the provisions dealing with such alternatives would not apply. However, DOL said that the covered service provider must disclose all the information required by the other provisions of the final regulation. These include a description of the services that would be provided to electing participants, any fees or charges that may be paid directly from the plan or participant accounts, and any compensation that may be received indirectly or from related parties in connection with the brokerage window. DOL understood that some of the required information may depend on the investments ultimately selected by participants, but said that there is sufficient flexibility under the rule to enable the covered service provider to communicate meaningful information about the compensation it expects to receive.

Observations

As described above under "Compensation Disclosure, Including Estimates and Ranges," self-directed brokerage arrangements pose challenges with regard to disclosure of indirect compensation. Because the investments are not known in advance, the potential sources of indirect compensation will not be known in advance. This is an area where the use of estimates and ranges may be particularly appropriate.

Disclosure Summary/Guide

As we indicated in our prior LawFlash, DOL has undertaken a separate rulemaking on the issue of whether to specify a format for the required disclosures, which had been left open in the interim final regulation. At that time, DOL had requested comment on the issue, noting that covered service providers could use different documents from separate sources as long as they all, collectively, contain the necessary information, and asking if it would be helpful to require a summary or guide.

Commenters on the interim final regulation had disagreed about the utility and feasibility of requiring a summary or guide. Some favored flexibility, expressing concern about the costs and utility of a mandated format; others supported requiring a summary disclosure or guide to organize the information for less sophisticated plan fiduciaries, and thought that the costs would be minimal and greatly outweighed by the benefits of increased clarity. Given the lack of specific suggestions or data on how best to structure such a requirement and what the real costs would be, DOL determined that it was not prepared to include such a requirement in the final regulation, but that it would publish a notice of proposed rulemaking on the matter in the near future for public review and comment (its recently released regulatory agenda calls for publication in June 2012).

In the meantime, DOL noted, it understands that many service providers are already moving in the direction of furnishing a guide or index to their disclosures and/or a summary of certain key disclosures. DOL indicated its strong support for doing so, as a means of assisting fiduciaries (particularly those of small- and medium-sized plans) in managing and analyzing potentially complex disclosure documents, including where multiple documents are involved. To further encourage this practice, DOL has included a "sample guide" in an appendix to the final regulation to help covered service providers that may wish to use such a format on a voluntary basis. DOL also encouraged plan fiduciaries that have difficulty finding and reviewing the required disclosures to request assistance from the covered service provider and possibly discuss the use of such a guide. The guide would also provide a basic framework to responsible plan fiduciaries for reviewing the disclosures they receive.

DOL encouraged interested persons to submit their views on the relative benefits and costs of a guide requirement versus a summary requirement and other formatting alternatives.

Observations

Given that DOL appears to be moving in the direction of requiring some type of guide or summary, covered service providers would be well advised to consider the sample provided by DOL. It is essentially a table of contents—a chart that lists the information required by the final regulation with a cross-reference to the document or agreement provision where that information can be found. It can be used on a stand-alone basis or in conjunction with a more detailed summary disclosure document.

Electronic Delivery

In response to questions regarding the ability to furnish the required disclosures electronically, DOL confirmed that there is nothing in the regulation that limits the ability of covered service providers to do so. Notably, DOL assumed in its economic analysis that 50% of the disclosures would be delivered electronically. However, with regard to making the information available on a secure website, DOL said that such an approach may not be regarded as "furnishing" the information, unless the information on the website is readily accessible to responsible plan fiduciaries and the fiduciaries have clear notification on how to gain access.

Observations

The confirmation of the ability to provide disclosures electronically is welcome, as it supports the general approach that many covered service providers are looking to use. It will be important that the format used for electronic disclosure is accessible and easy to use, consistent with DOL's observations regarding use of a secure website.

Changes to Previously Provided Disclosures – Investment-Related Information

The rules require that changes in the required information be disclosed as soon as practicable, but not later than 60 days from the date the covered service provider is informed of the change, unless the disclosure is precluded due to "extraordinary circumstances" beyond the covered service provider's control. The final regulation modified this requirement as it applies to changes in information regarding investment funds.

Commenters argued that a requirement to disclose changes to investment funds on an ongoing basis within 60 days would be highly burdensome to both covered service providers and responsible plan fiduciaries, because there may be myriad minor changes. Instead, they suggested a periodic update requirement, which they said would be more consistent with current industry practice and more likely to get the attention of the responsible plan fiduciaries. Agreeing with these concerns, DOL modified the rules to instead require that a covered service provider must at least annually disclose any changes to the investment fund information required to be provided either by covered service providers that are fiduciaries of investment funds, or by brokers/recordkeepers for participant-directed individual account plans.

Observations

This is a helpful change, also making the timing of disclosure of investment fund changes consistent with the general rule under the participant-level disclosure regulation.

REPORTING AND DISCLOSURE INFORMATION REQUESTS – TIMING

The interim final regulation required a covered service provider to provide, upon request, information relating to its compensation that is necessary for the plan to comply with the ERISA reporting and disclosure requirements. This was important to coordinate with the service provider compensation disclosures mandated on Schedule C to the Form 5500 annual report filed by plans with DOL. The final regulation requires that the plan's request be in writing and also modifies the timing requirement.

Under the interim final regulation, the information generally had to be provided no later than 30 days following receipt of a written request. Commenters suggested that this timing be better aligned with the timing of the ERISA reporting and disclosure standards. Agreeing, DOL deleted the 30-day rule, replacing it with a requirement that the information be furnished "reasonably in advance of the date" on which the requesting fiduciary "states that it must comply with the applicable reporting or disclosure requirement," subject to an exception in the event of extraordinary circumstances beyond the covered service provider's control.

Observations

This change should be helpful because it avoids the problem of a 30-day limit applying where plan administrators request information significantly in advance of the Form 5500 due date, long before the service provider may have had a chance to compile its year-end compensation information.

"COVERED PLANS" DEFINITION – EXCLUSION OF CERTAIN 403(B) PLANS AND OTHER CLARIFICATIONS

In response to comments, DOL added to and clarified the exclusions from the definition of "covered plans" subject to the new disclosure rules.

The interim final regulation had defined a "covered plan" as an employee pension benefit plan or pension plan within the meaning of ERISA that is not excepted from ERISA coverage. DOL had excluded (1) simplified employee pension plans, (2) simple retirement accounts, (3) individual retirement accounts, and (4) individual retirement annuities. The final regulation adds 403(b) plans that consist exclusively of "frozen" custodial or annuity contracts or accounts for which DOL had provided relief from ERISA's Form 5500 reporting requirements, since the sponsors and fiduciaries of those plans generally would have no dealings with the relevant service providers. The sponsor must have ceased making contributions to the contract or account for periods before January 1, 2009; all rights and benefits under the contract or account must be legally enforceable by the individual owner without any involvement by the employer; and the individual owner must be fully vested.

DOL also clarified that the following are not "covered plans":

- Health savings accounts—because they are not "pension" plans and may not even be ERISA-covered plans

- Plans that provide benefits only to a business owner and his or her spouse and plans covering only self-employed individuals, such as a Keogh or "HR-10" plan—because they are not ERISA-covered plans

"COVERED SERVICE PROVIDERS" DEFINITION; NONMONETARY COMPENSATION

Under the final regulation, as under the interim final regulation, one of the conditions that must be met for a plan service provider to be considered "covered" by the disclosure rules is that the service provider reasonably expects to receive $1,000 or more in compensation, direct or indirect, in connection with providing certain types of services.

Some commenters asked about the time period over which the $1,000 must be measured. DOL said that the focus is on whether $1,000 is expected to be received "in connection with" providing the services specified in the contract, regardless of whether it is to be received in a particular year or during the stated term of the contract. Trailing commissions received after the services are furnished, for example, are still "in connection with" the services. DOL cautioned parties against attempting to structure contracts to avoid the $1,000 threshold.

The final regulation, like the interim final regulation, excludes from the $1,000 any nonmonetary compensation valued at $250 or less, in the aggregate, during the term of the contract or arrangement. Commenters argued that the $250 should be measured on an annual basis rather than over the life of the contract, but DOL disagreed. DOL also was asked for guidance on accounting for and allocating nonmonetary compensation to different clients of the covered service provider. In response, DOL said that for purposes of the final regulation, covered service providers may look to the guidance and methodologies DOL has approved for purposes of the Form 5500 Schedule C disclosure rules.

<u>Observations</u>

DOL's response to the comments confirms the view that the $1,000 threshold will not be hard to meet; thus, it will be difficult for service arrangements of any substance to avoid coverage.

FIDUCIARY OBLIGATIONS UNDER ERISA SECTION 404

Some commenters asked DOL to clarify the responsibilities of the responsible plan fiduciaries that receive the disclosed information under ERISA Section 404, which imposes fiduciary duties of prudence and loyalty. DOL said that, in its view, if a plan fiduciary needs particular information to make an informed decision when selecting or monitoring a plan service provider, Section 404's duty of prudence requires the fiduciary to request the information. If the service provider does not provide such information, Section 404 may preclude the fiduciary from entering into or continuing the arrangement. DOL added that the Section 408(b)(2) disclosure requirements are independent of a fiduciary's obligations under Section 404.

DOL further added that the disclosure requirements of the final regulation should be construed broadly to ensure that responsible plan fiduciaries base their review of a service contract or arrangement on comprehensive information.

Observations

DOL's comments further highlight the burden that the new rules will impose on the responsible plan fiduciaries to review the disclosed information.

EXEMPTION FOR RESPONSIBLE PLAN FIDUCIARIES

The final regulation, like the interim final regulation, provides exemptive relief for responsible plan fiduciaries that take certain steps when a covered service provider fails to disclose required information. DOL modified one of the conditions of the exemption.

The interim final regulation had required the responsible plan fiduciary to determine whether to terminate or continue the contract or arrangement once the covered service provider has failed to comply with the fiduciary's request for the undisclosed information. The final regulation removes language about evaluating the nature of the failure and the ability to find a replacement service provider, and instead requires that (1) the determination be made consistent with the fiduciary's duty of prudence under ERISA Section 404 (which DOL said assumes the fiduciary will take into account the factors no longer specified in the operative language, such as the nature of the failure and the availability and cost of a replacement service provider); and (2) if the requested information that has not been disclosed relates to future services, the fiduciary terminate the contract or arrangement as expeditiously as possible consistent with its duty of prudence. DOL said that although this subsection is intended to give the responsible plan fiduciary some flexibility in securing a replacement, it is not intended to permit a fiduciary to continue arrangements indefinitely where there has been an unresolved disclosure failure.

DOL declined a request to make the exemption available if the fiduciary does not "know or have reason to know" of the disclosure failure, retaining the requirement that the fiduciary must have "reasonably believed" that the requisite disclosures were made. DOL said this requires the fiduciaries to appropriately review the disclosures and form a reasonable belief about them. DOL also declined to expand the relief to covered service providers that, through no fault of their own, are unable to obtain information from other parties, as the rules already address this issue in part through mechanisms for correcting inadvertent errors and omissions and updating changes. DOL also believes that the covered service provider should bear ultimate responsibility for providing the required disclosures. DOL observed, in response to comments, that in the event a termination of the service arrangement is required, the class exemption does not void negotiated provisions designed to compensate the service provider for its termination losses at the plan's expense.

<u>Observations</u>

The change to the conditions of the exemption is a significant one, taking the position that if a responsible plan fiduciary continues a service arrangement after a disclosure failure, it must have a clear and well-documented reason for doing so consistent with its fiduciary duty of prudence. This will add to the leverage that responsible plan fiduciaries will have in obtaining the required disclosures, which is what DOL intends. If the relationship is continued, cost is likely to be the reason, which is in line with DOL's confirmation that the disclosure rules do not preempt contract provisions that may impose costs on the plan for early termination.

PROHIBITED TRANSACTION EXCISE TAXES

Several commenters asked DOL how to determine the "amount involved" in a prohibited transaction for excise tax purposes, and what would be required to "correct" the prohibited transaction, in the event the requirements of the final regulation are not met. DOL declined to state a view, saying that these matters are under the authority of the Department of the Treasury and beyond the scope of the final regulation.

<u>Observations</u>

Given DOL's response, it continues to be unclear exactly what the excise tax liability would be for a covered service provider that fails to meet the conditions of the final regulation.

EFFECT ON OTHER PROHIBITED TRANSACTION EXEMPTIONS

Some commenters asked DOL to clarify the effect of the new disclosure rules on the availability of previously issued exemptions. DOL said that it is reviewing a number of pertinent class exemptions involving service provider arrangements and anticipates providing guidance in the near future.

<u>Observations</u>

This issue was raised because Section 408(b)(2) is a statutory exemption from ERISA's prohibited transaction rules, so that the new disclosure requirements conceivably could be avoided through compliance with a different exemption. However, many exemptions that could be available for service arrangements impose their own disclosure rules, or only provide limited relief so that compliance with Section 408(b)(2) is still necessary. At least at this point in time, DOL has not foreclosed the use of alternative exemptions.

DISCUSSION

While DOL provided a number of helpful clarifications and changes, the final regulation continues to impose what will clearly be a highly burdensome disclosure framework. The DOL cost estimate for the first year alone is more than $164 million, with $64 million of that devoted to legal review. Although costs are expected to decline substantially after the first year, they are expected to continue to exceed

$20 million annually through 2021. According to some sources, the DOL cost figures significantly underestimate the actual costs.

A possible area of contention will be disputes over whether the disclosures provided are "adequate." Responsible plan fiduciaries may decide to be aggressive on such issues to ensure that they will qualify for the exemption embedded in the final regulation. It will be important for both responsible plan fiduciaries and covered service providers to carefully manage the process of requesting information and responding to such requests, to avoid delays or problems that will place responsible plan fiduciaries in the position of having to report service providers to DOL to secure coverage under the exemption, and possibly becoming obligated to terminate the service providers to meet the exemption's requirements.

The next step is for covered service providers to get their disclosures and disclosure processes in place by the effective date—now only four and a half months away. Despite the clarifications provided by DOL on the use of estimates and ranges, there are still many categories of indirect compensation that do not lend themselves easily to disclosure. Those issues must still be addressed. In addition, there may remain questions on how best to provide the disclosures through the use of electronic media, given the issues raised by DOL on accessibility and possible limitations on the resources available to fully implement an electronic disclosure regime by the effective date.

Plan sponsors, meanwhile, should be anticipating the need to monitor the receipt of the disclosure materials by developing a review process. To the extent they will need assistance from outside consultants and others, those discussions should start now if they are not already well underway.

Morgan Lewis's Employee Benefits and Investment Management attorneys have been actively assisting both service provider and plan sponsor clients with issues under these rules. We anticipate providing further updates to our clients as needed, including through LawFlashes and webinars, as appropriate.

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