

ERISA § 408(B)(2) OVERVIEW

March 2012

THE REGULATION

New regulations that go into effect on July 1, 2012, require 401(k) plan service providers to report fees and certain other information to their plan sponsor clients. Regulations further require that plan sponsors evaluate their plans and terminate any service arrangements that are found not to be in the best interest of participants.

Regulations specify that plan sponsor evaluation must be based on three broad criteria:

- ✓ Each service arrangement must be:
 - Necessary
 - Reasonable
 - Cost Effective

Regulations provide no guidance on how evaluations are to be performed, only that the evaluation must be a prudent process, and that the plan sponsor must be able to demonstrate the process that is used. The expectation is that industry experts will develop methodologies that meet these goals.

COMPLYING WITH REGULATION

CSP Duties

Service providers covered by the regulation (CSP) must make the required disclosures to plan sponsors in the prescribed format and update this information annually.

Plan Sponsor Duties

Plan sponsors must develop a method of performing evaluations and maintain records to be able to demonstrate that decisions were in the best interest of plan participants.

CONFLICTS OF INTEREST

Plan sponsors who have previously relied on service providers and advisors to meet their compliance requirements are unable to turn to these experts because of the conflict of interest. Plan sponsors would breach fiduciary responsibility if they permitted service providers or advisors to evaluate themselves to determine if they were necessary, reasonable and cost effective.

Plan sponsors will not be able to comply with this regulation without some assistance.

DALBAR'S ROLE

DALBAR has developed a solution for plan sponsors who are faced with this dilemma. The DALBAR solution performs a business evaluation of the plan and issues an opinion certifying whether the plan services are necessary, reasonable and cost effective.

By using the DALBAR solution, the conflicts of interest are eliminated. This is because DALBAR is independent of any service providers and advisors and has the well established expertise and experience to conduct the evaluation.

NEW ROLE FOR ADVISORS

The DALBAR solution creates a new role and compensation source for the advisor.

The advisor earns a fee for performing two critical services required by the DALBAR solution.

1. Assisting the plan sponsor to complete the DALBAR profile that describes the success of the plan, the needs and preferences of the plan sponsor and participants and the exposure to risk. This profile is submitted to DALBAR for analysis.
2. Presenting the DALBAR opinion and findings to the plan sponsor and making any changes that may be required.

For these services, the advisor earns a fee that can be a flat amount of money, a basis point fee or an hourly fee as the advisor chooses.

THE DALBAR SOLUTION AND THE BROKER/DEALER

Advisors will treat the support of the fee evaluation process as an outside business activity (OBA), subject to oversight under FINRA Rule 3270. The broker/dealer will be responsible for complying with 3270 and is expected to obtain the required information from the advisor.

Advisors will receive compensation for these activities from any of three sources, depending on the specific arrangement:

- From the plan itself
- From the plan sponsor
- From DALBAR

The advisor will receive separate form 1099 statements and is responsible for preparing the appropriate tax reporting.

The DALBAR solution does not require the advisor to engage in any fiduciary activity but does not preclude fiduciary activities if the advisor is authorized to engage in such activities.

Details of the DALBAR solution and the expected role of advisors is available at the Web site www.ERISAFeeDisclosure.com.