



BEST PRACTICE

Monitoring and Disclosure of Fees for Defined Contribution (DC) Plans (2008) (CORBA)

Background. State and local government defined contribution (DC) plans currently include 457(b), 401(k), 401(a) and 403(b) plans. These plans generally supplement state and local government defined benefit plans and offer an additional means for public employees to increase their savings for retirement.

In carrying out their responsibilities as fiduciaries, in both the public and private sector, plan sponsors make decisions in the best interests of plan participants and beneficiaries. In making these decisions, it is assumed that plan sponsors have knowledge about all fees and expenses charged to the plan and participants while ensuring that these costs are reasonable. It is also assumed that plan sponsors are disclosing to plan participants adequate and accurate information about the fees and expenses that affect their account balances.

There is growing interest in the disclosure and reasonableness of fees charged to DC plans and participants. DC plans offered in both the public and private sectors have been the focus of congressional, regulatory and public scrutiny. Therefore, public sector plan sponsors must ensure that their policies and practices allow both the plan sponsor and the participants to be well-informed about fees and expenses and their potential impacts.

Recommendation. GFOA recommends that plan sponsors establish and implement policies and practices to assure that DC plan costs are reasonable and appropriate, compared to DC plans of similar size, structure and service levels. These policies and practices should ensure that plan sponsors:

1. Thoroughly review and document the process used to select DC plan service providers and the types of fees that are charged.
2. Require potential service providers to disclose all compensation arrangements they have with other providers for endorsements, reimbursements, marketing fees and the like in their DC plans (e.g. revenue sharing, 12b-1 fees), and then evaluate all relevant information regarding these fee arrangements and fully disclose such arrangements on plan websites and in plan documents and investment materials sent to employees.
3. Monitor plan service providers for potential conflicts of interest (e.g. changing fee arrangements).
4. Periodically audit actual charges to assure compliance with agreed-upon fees.
5. Regularly monitor the reasonableness of fees, which may include independent periodic benchmark studies, as well as the services provided.
6. Consider whether an independent consultant should be engaged to assist with the initial or ongoing evaluation of fees.

GFOA further recommends that plan sponsors establish and implement policies and practices to provide participants with meaningful, ongoing, accessible information regarding fees and expenses along with other information needed by participants to make sound investment decisions. These policies and practices should ensure that plan sponsors:

1. Provide participants with educational materials to assist in understanding fees and the role fees play in related investment returns.
2. Disclose and communicate fee information in a way that is concise, straightforward and transparent and allows for comparison among investment options. This may include issuing annual statements to individual participants with personalized fee disclosures. Where practical, participant fee information should consistently be disclosed as a dollar amount and as a percentage of assets.
3. Ensure that fee information is not disclosed in isolation. Disclosures should include fee information, past investment performance, risk and investment objectives. Comparative information, including appropriate benchmarks on fees, investment risk and investment returns should be provided to all participants. Such information should be sufficient to allow participants to evaluate the various investment products offered.¹
4. Communicate fee information at enrollment and at regular intervals and notify participants annually regarding where they can find or how they can request updated information. Fees associated with special transactions (e.g., loans) should be disclosed in advance of the transaction.
5. Provide disclosures for: (1) investment fees, which include fees associated with management of the plan's investments, (2) plan administration fees, which may include recordkeeping, communications, education, and fees for the plan's professional advisors, and (3) special transaction based fees or service charges such as loans, brokerage accounts, and qualified domestic relations orders.
6. Re-evaluate fee disclosure practices on an ongoing basis to assure compliance with applicable regulatory requirements and best practices.

References

- *Changes Needed to Provide 401(k) Plan Participants and the Department of Labor Better Information on Fees*, Government Accountability Office, November 2006.
- *Scrutinizing DC Plan Fees and Expenses for Transparency, Awareness and Disclosure*, The Segal Company, May 2007.
- *Defined Contribution Fee Disclosure Best Practices*, The Committee on Investment of Employee Benefit Assets, Association for Financial Professionals, June 2007.
- "Retirement Vendor Kickbacks," *Governing.com*, September 2007.
- *A Primer on Plan Fees*, American Bankers Association, et al, October 18, 2007.
- Mindy L. Harris, President, National Association of Government Defined Contribution Administrators, Testimony before the House Ways and Means Committee, Hearing on the Appropriateness of Retirement Plan Fees, October 30, 2007.
- "Fees in Your Face," *Governing.com*, November 2007.

Approved by the GFOA's Executive Board, February 22, 2008.

¹ Under the Pension Protection Act of 2006, the quarterly benefit statements must include a notice directing participants to a Department of Labor (DOL) website on individual investing and diversification (<http://www.dol.gov/ebsa/investing.html>).