

# The new era of fee transparency: Making sense of the details

The 401(k) landscape has changed dramatically over the past 30 years. What began as a mention in a code section has become the most valuable savings plan for workers' retirements. Simple plans have become more complex, small balances have grown into larger portfolios, and regulators have struggled to keep pace with the speed of change. New laws, new regulations and additional requirements have been appended to the 401(k). But one constant has been the role of the fiduciary, and the obligation to put the best interests of participants first.

One of the most important fiduciary responsibilities is to understand the services being provided and ensure that the fees being charged to the plan are reasonable. This paper will help you build best practices for evaluating plan fees and determine whether you are striking a balance between the fees you pay and the services you receive.

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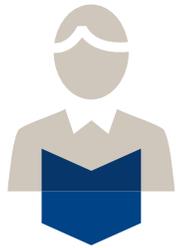
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For years, Bank of America Merrill Lynch has been a strong proponent of more consistent and complete fee disclosures. We believe our clients are best served when they can see the details of the fees and the corresponding services provided in support of each plan.

The ERISA Section 408(b)(2) regulations published in February 2012 specify service provider fee disclosure requirements and outline how service providers deliver specific fee information in a format that makes it easier and clearer for plan fiduciaries to understand the services they receive and the fees they pay for those services.

In the *Plan Sponsor Guide to Fee Disclosure*, we shared the initial actions fiduciaries should take to understand the fee disclosure regulations and make a fee reasonableness determination (see below).

### Actions to take



**Familiarize yourself** with the fee disclosure regulations (if you haven't already).

**Identify** any additional covered service providers that are required to provide you with a 408(b)(2) notice.

**Evaluate** the reasonableness of fees charged to the plan under the service agreement.

**Consider** all of the factors to determine whether the fees are reasonable.

**Include** the review within the governance process and maintain adequate documentation of the review process.

Now that fee disclosures have been delivered, plan fiduciaries are asking how to leverage the new fee disclosures to help assess whether plan fees are reasonable.

### Beginning with a well-defined process

Best-practice governance routines and fee disclosure regulations place equal emphasis on documenting the process for determining reasonableness and making the determination itself. If you establish and document processes and procedures for understanding and assessing the fees paid by your plan, and you are diligent in following them, generally you are assured that you've fulfilled the fee disclosure requirements.

Consider these best practices for establishing and documenting a formal fee review process:

- Identify all of your “covered service providers” — the list may include attorneys, benefits consultants, actuaries, CPAs, investment advisors, TPAs and record-keepers.
- Document the steps you will take to ensure you’ve received all required fee disclosures and that they are adequate and in good order for your evaluation.
- Document the steps you will take if information is missing from any of your covered service providers.
  - If you determine that information is missing, you must request the disclosures in writing.
  - If you do not receive the requested information within 90 days, you must terminate services with the service provider while allowing time to find a suitable replacement.
  - If you terminate services, you must report the offending service provider to the Department of Labor.
- Name key people who will be accountable for each step of the process and consider establishing a formal plan fee review committee.
- Document the plan committee’s annual reviews and decisions in formal meeting minutes.
- Identify the benchmark you will use to compare fees and determine how often you will benchmark fees.
- Set up a calendar for fiduciary tasks, indicating how long the tasks may take and if they need to coordinate with any of your company’s other processes.

#### **Convert fee information to dollars for fair comparisons**

*Even with new fee disclosure statements, it can be challenging for plan fiduciaries to know how much they actually pay for a particular service and how that fee compares with those of other providers. One tip is to convert all fees listed in basis points (bps) or percentages into dollars. Comparing dollar amounts is important in your review.*

*For example, let’s say one service provider reports a charge of 45 bps for providing “advice” to plan participants, and another provider in the same plan charges \$25,000. How can the fiduciary compare pricing? The fiduciary will need to find the basis for the payment and complete the computation. If the provider that charges 45 bps bases it on the participant’s account balance, take the total balance of all participants receiving advice and multiply it by 45 bps.*

*Converting all fees into dollars will be important for benchmarking to determine whether the amount you are paying is reasonable and valuable to the plan.*

Even with new fee disclosure statements, it can be challenging for plan fiduciaries to know how much they actually pay for a particular service and how that fee compares with those of other providers.

As a part of ongoing fiduciary duties, employers also must communicate plan fees to employees. The regulations are under Section 404(a)(5).

## Understanding what you're paying and the services provided

Evaluating plan fees requires plan sponsors to understand the services they are receiving and the costs associated with each of them. Here are guidelines for understanding your fees:

1. **Ensure each covered service provider has clearly defined the services being provided and the amount you are paying for those services.**
2. **Evaluate whether you have received all of the services listed in the disclosures provided to you.**
  - Review the details of “direct compensation.”
  - Familiarize yourself with all “indirect compensation” fees and arrangements between the service provider and any subcontractors.
    - Understand revenue-sharing arrangements.
    - Fully understand indirect costs, including float arrangements, conferences and training sessions, subcontractor payments, etc.
    - Recognize advisory costs from financial advisors and brokers who help manage the plan or investments and whether the costs are commission-based or fee-for-service.
  - Review record-keeping services for direct and indirect costs.
  - Understand the investment-related fees that are passed along to plan participants.
3. **Review all disclosures to identify any conflicts or discrepancies in the fees versus services provided and know how to remedy or report the situation.**
  - Compare cost increases from year to year. Are they warranted? Check whether the increases are related to increases in services, transactions or the number of participants in the plan.
  - Document any necessary action items with specific covered service providers, as well as a plan and specific time frame for addressing them.
  - Ask questions if you don't understand the information you have received.

## Managing participant fee disclosures



As a part of ongoing fiduciary duties, employers also must communicate plan fees to employees. The regulations are under Section 404(a)(5).

### Employers may want to:

Document the procedures and requirements for implementing participant fee disclosures.

Determine whether they will draft and deliver participant fee disclosures or hire someone to do it for them.

Document how eligible nonparticipating employees will be notified and who is responsible for tracking eligibility.

## Comparing costs to the value of services provided

Plan fiduciaries are required to ensure that the costs of operating the plan are reasonable compared to the value of the service being received. When comparing fees for reasonableness, it may be helpful to think of a balance or scale. Services you receive are on one side; fees paid are on the other. Are they relatively equivalent? Any side-by-side comparison must be careful not to be weighted in favor of fees.

### Guidelines for comparing fees and value



**Test the balance** for each covered service provider that is involved in your plan. When you find a balance between value and cost, you'll be in position to deem the fees reasonable.

**Compare all plan services** received with the costs, and decide the real value gained from each provider based on the qualitative aspects of your plan, like plan health and participant financial wellness.

**Assess how much support** the provider delivers to your employees. Is the service provider helping employees reach retirement goals and overall financial wellness?

## Determining reasonableness of fees and investment options in your plan

Determining reasonableness of fees does not mean you seek the lowest-cost provider. Focus instead on overall value, experience, service, and confidence that the provider is servicing both the plan and the participants well. If you determine reasonableness solely on the lowest cost, you probably are not meeting the fee reasonableness requirement.

For investment assessment and evaluation, leverage your Investment Committee processes already in place under the Investment Policy Statement, and adjust as needed to:

- Understand the intersection of investment fee competitiveness, fee-sharing arrangements and the impact on individual fund performances.
- Include your policy on considering investment options that provide fee sharing.
- Determine whether investment objectives of each fund continue to meet plan participants' needs.

Determining reasonableness of fees does not mean you seek the lowest-cost provider. Focus instead on overall value, experience, service, and confidence that the provider is servicing both the plan and the participants well.

It is critical that your comparative data be from unrelated outside sources. If any covered service providers recommend their own benchmarks — even with the best of intentions — it could be considered flawed or a conflict of interest.

## Developing a benchmarking strategy

While benchmarking can be an effective way of fulfilling your fiduciary responsibility for validating fee reasonableness, one size does not fit all. There are a number of approaches and methods to consider when establishing a benchmarking strategy. It can be challenging for plan fiduciaries to know which approach is most appropriate for their plan. Yet the fiduciary must still determine reasonableness, and understanding these quantitative and qualitative measures is important in developing a benchmarking strategy.

- **Quantitative industry standards and peer averages.** These include the rates you pay for services, and the total dollars relative to the services provided for the plan.
- **Qualitative aspects that help you define overall plan success.** You might assess and track employee activities and corresponding results over time. These behaviors may help employees reach a better level of financial wellness.

When creating your benchmarking strategy, also consider the size of your plan, the depth of resources available and the budget available for obtaining benchmark information. This Benchmarking guide (opposite) may assist you in developing a strategy that meets the needs of your company.

## Getting started is easy

Your team at Bank of America Merrill Lynch is available to help navigate the process of determining reasonableness for plan fees. As part of our continuing support for plan sponsors, we have resources and information you may find helpful as you design and document your policies and procedures. We encourage you to:

- Use materials and information from Bank of America Merrill Lynch to analyze total plan fees, assess reasonableness and list any questions you may want to discuss with your Merrill Lynch financial advisor.
- Work with your Bank of America Merrill Lynch representatives to outline your specific fiduciary duties.
- Set up well-organized written internal processes you can readily repeat and measure.
- Establish a calendar of fiduciary tasks related to assessing fees and determining reasonableness.

Benchmarking guide

|  <b>BENCHMARK</b>                                   | <b>Surveys and benchmarking studies from unbiased sources</b>   | <b>Third-party assessments</b>            | <b>Request for information (RFI)</b>   | <b>Consultant</b>  | <b>Request for proposal (RFP)</b>  |
|--|---|---|--|--|--|
| <b>SERVICES PROVIDED</b><br><br><b>401(k)</b>  | Broad industry view of various plan fees and practices  | General pricing comparisons for your plan | Plan-specific pricing information from service providers                                     | In-depth pricing comparisons and competitive data                  | Comprehensive plan-specific comparison and pricing review                                    |
| <b>EXAMPLES OF BENCHMARKING RESOURCES*</b><br><br> | 401(k) Averages Book<br><br>Plan Sponsor Council of America Annual Survey<br><br>Deloitte Defined Contributions/ 401(k) Fee Study | Fiduciary benchmarks<br><br>Brightscope   | Internal resources<br><br>Benefits consultant<br><br>Investment advisor<br><br>DC consultant | Benefits consultant<br><br>Investment advisor<br><br>DC consultant | Internal resources<br><br>Benefits consultant<br><br>Investment advisor<br><br>DC consultant |
| <b>COST</b><br><br>                               | \$  | \$\$                                      | \$\$   | \$\$\$   | \$\$\$\$   |
| <b>FREQUENCY</b><br><br>                          | Annual  | 1–2 years                                 | 2–3 years  | Periodic, as resources allow                                       | 3–5 years  |

\*Not a complete list. Please contact your Bank of America Merrill Lynch representative for more information.

## The role of your services team

You may find it most helpful to develop your policies and procedures with a team. Reach out to benefits consultants, tax advisors, legal counsel, investment advisors, actuaries and other financial professionals who support your plan. They can help a plan sponsor align fees with services in a meaningful way in order to meet the plan's objectives and needs. There is strength in having a support team in place, and you already have many such resources at Bank of America Merrill Lynch.

Bank of America Merrill Lynch representatives are positioned to help with both structural plan design and investment options. They look at your goals and needs, and recommend improvements for the financial wellness of each and every plan participant.

Anyone involved in supporting your plan is required to specifically report the fees associated with provided services. Our representatives who support your plan may be compensated for their services, and you will see their fees listed separately in these categories: direct compensation, indirect compensation, or compensation paid among related parties.

### The following fee disclosure resources are available from Bank of America Merrill Lynch:

- *Fiduciary Fundamentals: Basics and Best Practices Guide*
- *Fiduciary Compliance Checklist*
- *Plan Sponsor Guide to Fee Disclosure*

**Note:** Fee disclosures are updated and posted monthly on Benefits OnLine®, so you will always have access to the most current fee information.

*If you have any questions about our compensation or fees, please contact your Bank of America Merrill Lynch representative.*

Bank of America Merrill Lynch  
representatives are positioned  
to help with both structural plan  
design and investment options.

Important: This publication provides general information about fiduciary ideas and strategies for retirement plans. Always consult with your legal, tax, insurance and investment advisors before implementing any changes. The strategies presented are intended to illustrate the products and services available through Bank of America Merrill Lynch; it should not be considered an offer, solicitation or endorsement. These illustrations may not be used with the general public under any circumstances. This material does not take into account your plan's objectives, financial situations or needs and is not intended as a recommendation, offer or solicitation for the purchase or sale of any security, financial instrument or strategy. Before acting on any information in this material, you should consider whether it is suitable, if necessary, to seek professional advice. Unless otherwise noted, all trademarks and registered trademarks are the property of Bank of America Corporation.