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Legal Risk Management Tip
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NEW DISCLOSURE OBLIGATIONS FOR SERVICE PROVIDERS TO ERISA PLANS

In July 2010, the Department of Labor (the "DOL") issued its interim final regulation ("the "Regulation") requiring service providers to plans subject to the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), to provide disclosures and descriptions of the services to be provided and the compensation to be received by a "covered service provider". This Legal Risk Management Tip will provide an overview of the new required disclosures, who will be required to make the disclosures, and what types of information must be included in the disclosures. Due to an extension of the compliance deadline, covered service providers will have until April 1, 2012 to comply with the following new disclosure obligations.

1. Background

Under ERISA, the furnishing of goods, services, or facilities between a plan and a party in interest to the plan generally is prohibited. As a result, a service relationship between a plan and a service provider would constitute a prohibited transaction, because any person providing services to the plan is defined by ERISA to be a ''party in interest'' to the plan. However, section 408(b)(2) of ERISA exempts certain arrangements between plans and service providers that otherwise would be prohibited transactions. Specifically, section 408(b)(2) provides relief from ERISA's prohibited transaction rules for service contracts or arrangements between a plan and a party in interest if the contract or arrangement is: (i) *reasonable*; (ii) the services are *necessary* for the establishment or operation of the plan; (iii) and *no more than reasonable compensation* is paid for the services (emphasis added). The Regulation, which clarifies each of these conditions to the exemption, also provides that non-compliance with the disclosure obligations established by the DOL will render the provision of services to the ERISA plan a prohibited transaction.

2. Scope of the Regulation

In order for a contract or arrangement to be considered *reasonable*, a "covered service provider" providing services to a "covered plan" must disclose specified information to the responsible plan fiduciary.

a. Definition of "Covered Plan"

The Regulation defines a ''covered plan'' as an employee pension benefit plan or a pension plan within the meaning of ERISA, but excludes SIMPLE IRAs,[1] Simplified Employee Pension Individual Retirement Accounts ("SEP IRAs"),[2] Individual Retirement Accounts ("IRAs").

[1] A SIMPLE IRA plan (**S**avings **I**ncentive **M**atch **P**lan for **E**mployees) allows employees and employers to contribute to traditional IRAs set up for employees.
[2] A SEP is a simplified employee pension plan. A SEP plan provides employers with a simplified method to make contributions toward their employees' retirement and, if self-employed, their own retirement. Contributions are made directly to an Individual Retirement Account or Annuity (IRA) set up for each employee (a SEP-IRA).

Generally, the Regulation applies to defined contribution and defined benefit pension, including certain 403(b) plans.

b. Definition of "Covered Service Provider"

The Regulation defines a ''covered service provider'' as a service provider that enters into a contract or arrangement with a covered plan and reasonably expects $1,000 or more in compensation, direct or indirect, to be received in connection with providing one or more of the following:

- Fiduciary or investment advisory services;
- Certain recordkeeping or brokerage services; and
- Other services for indirect compensation, including custodial, insurance, legal, accounting, auditing, actuarial, appraisal and/or banking services.

Notably, the definition of covered service provider is broad in scope, and includes entities providing the above services regardless of whether such services will be performed by the covered service provider, an affiliate or a subcontractor.

3. Disclosures Required by Covered Service Providers

Under the Regulation, covered service providers will be required to deliver disclosures to responsible plan fiduciaries of ERISA plans initially, upon request and whenever there are changes to the information contained in the disclosures. The Regulation requires that a covered service provider provide the initial disclosures to the responsible plan fiduciary *reasonably in advance* of the date the contract or arrangement is entered into, extended or renewed. Among other things, the initial disclosure must provide the responsible plan fiduciary with information regarding:

- The services to be provided to the covered plan. Notably, there is no specific level of specificity required under the Regulation and the level of detail required to adequately describe the services to be provided will therefore vary depending on the needs of the responsible plan fiduciary.
- The status of the covered service provider. In this section of the disclosure, the service provider must inform the responsible plan fiduciary whether the service provider will be acting in a fiduciary capacity under ERISA or under the Investment Advisers Act of 1940.
- The compensation to be paid by the plan to the service provider under the contract or arrangement. For purposes of this disclosure, the DOL has segmented "compensation" into four categories:
    - Direct compensation
    - Indirect compensation
    - Compensation paid among related parties
    - Compensation for termination of arrangement or contract

In addition to covered service providers' initial obligations to disclose the above information to responsible plan fiduciaries, they are also under an obligation to make ongoing periodic disclosures upon request and when there are changes to the information contained in the disclosures previously provided. For changes in the disclosures information, the service provider must disclose the change as soon as practicable, but not later than 60 days from the date on which the service provider is informed of the changes. However, if the updated disclosure was not possible due to extraordinary circumstances beyond the service provider's control, the updated information must be disclosed as soon as practicable.

The Regulation does not require the service provider to make the disclosures in any particular manner or format. As a result, the disclosures could be made through multiple documents and means, which for registered investment advisers, may include enhanced disclosures in Form ADV Part 2, investment advisory agreements and a separate disclosure document. Given the fact that the services provided to a covered plan vary from service provider to service provider, the disclosures will need to be customized to meet the requirements of the Regulation.

For more information about this topic, including suggestions on how to draft your 408(b)(2) disclosure document(s), please contact us at (619) 298-2880, info@jackolg.com or visit www.jackolg.com. Thank you.

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