

MEMO# 16105

May 22, 2003

DOL FIELD ASSISTANCE BULLETIN ON ALLOCATION OF PLAN EXPENSES IN DEFINED CONTRIBUTION PLANS

[16105] May 22, 2003 TO: PENSION MEMBERS No. 25-03 PENSION OPERATIONS ADVISORY COMMITTEE No. 30-03 RE: DOL FIELD ASSISTANCE BULLETIN ON ALLOCATION OF PLAN EXPENSES IN DEFINED CONTRIBUTION PLANS The Department of Labor recently issued Field Assistance Bulletin (FAB) 2003-3 providing guidance on the allocation of expenses in defined contribution plans. In particular, the FAB addresses two issues: (1) the extent to which plan expenses are required to be allocated on a pro rata, rather than a per capita, basis among all plan participants, and (2) the extent to which plan expenses may be charged to an individual participant, rather than the plan as a whole. Generally Applicable Standards The FAB generally provides that plan sponsors and fiduciaries have considerable discretion in determining, as a matter of plan design or plan administration, the manner in which plan expenses may be allocated among participants and beneficiaries. With the exception of certain ERISA provisions and regulations,¹ the FAB notes that ERISA does not specifically address how plan expenses should be allocated among participants and beneficiaries. Rather, the fiduciary standards of ERISA section 404(a)(1) apply, under which fiduciaries must act prudently, solely in the interests of participants and beneficiaries, and in accordance with plan documents to the extent consistent with Title I of ERISA. Accordingly, the FAB provides that where a method of allocating expenses is set forth in plan documents, fiduciaries generally must follow the prescribed method. Where plan documents are silent or ambiguous on how expenses are to be allocated, fiduciaries must prudently select the method of allocation. This standard requires fiduciaries, at a minimum, to weigh the competing interests of various classes of participants and the effect of various allocation methods on them. 1 Examples of situations in which a plan may impose charges on a specific participant include (1) costs under ERISA section 104(b)(4) for furnishing copies of plan documents upon a participant's request, (2) reasonable expenses associated with a participant's exercise of investment direction under ERISA section 404(c), and (3) reasonable expenses for participant loans under ERISA section 408(b)(1). 2 Under the FAB, a fiduciary also must satisfy the "solely in the interest of participants" standard set forth in ERISA section 404(a)(1). Here, the FAB provides that where a rational basis exists for the selected method, a fiduciary's obligation would not change merely because the method disfavors a class of participants. If, however, the allocation method has no reasonable relationship to the services furnished or available to an individual account, the fiduciary may have violated this requirement.² Pro Rata vs. Per Capita Allocation of Expenses Among All Plan Participants The FAB observes that while a pro rata method of allocating expenses among individual accounts (i.e., allocations based on assets in the accounts) would appear to be equitable in most cases, it is not the only permissible method. A per capita method

(i.e., allocating expenses equally to each account, without regard to assets in the account) may also provide a reasonable method of allocating “certain fixed administrative expenses of the plan, such as recordkeeping, legal, auditing, annual reporting, claims processing and similar administrative expenses.” However, “where fees or charges to the plan are determined on the basis of account balances, such as investment management fees, a per capita method of allocating such expenses among all participants would appear arbitrary.” With regard to expenses relating to investment advice provided to participants, the FAB permits the allocation of expenses on either a pro rata or per capita basis and without regard to actual utilization of services by a particular participant. Charging such investment advisory expenses based solely on actual utilization of the service also is permissible.

Allocating Expenses to a Particular Individual Account vs. the Plan The FAB supersedes the prior guidance on allocation of expenses set forth in Advisory Opinion No. 94-32A. Under that advisory opinion, imposing the costs of a Qualified Domestic Relations Order (QDRO) determination on the participant (or alternate payee) seeking the QDRO, rather than the plan as a whole, violated ERISA. In the FAB, the Department observed that this conclusion was not compelled by ERISA and that, with the exception of the few ERISA provisions that specifically address the imposition of expenses on individual participants, the statute places few constraints on how expenses may be allocated. Accordingly, the FAB concludes that the same principles applicable to determining the allocation methods among all participants (discussed above) apply to determining whether specific expenses may be allocated to the account of an individual participant, rather than among all participants. Notably, the FAB provides examples of plan expenses for which ERISA does not preclude the allocation of reasonable expenses to the account of a specific participant seeking a distribution or other service from the plan: (1) expenses associated with hardship withdrawals; (2) calculation costs of benefits payable under different plan distribution options (e.g., joint and survivor annuity, lump sum, single life annuity); (3) distribution costs (e.g., a check writing fee); and (4) costs relating to QDROs and Qualified Medical Child Support Orders (QMCSOs). In addition, because nothing in Title I of ERISA limits the ability of a plan sponsor to pay only certain plan expenses or expenses on behalf of only certain plan participants, a plan may 2

The FAB also notes that a potential prohibited transaction could arise where a fiduciary who is also a participant selects an allocation method that confers a greater than incidental benefit to him or herself. 3 charge a vested separated participant account its share (on either a pro rata or per capita basis) of reasonable plan expenses, notwithstanding (1) whether active participants are charged such expenses or (2) whether the vested separated participant was provided the option of withdrawing the funds from his or her account or the option to roll the funds to another plan or IRA. Disclosures through Summary Plan Descriptions Finally, the FAB cautions that the Department’s current regulations in 29 C.F.R. 2520.102-3(1) require plans to include in the Summary Plan Description (SPD) a summary of any provision that may result in the imposition of a fee or charge on a participant or beneficiary, the payment of which would be a condition of the receipt of plan benefits. Under this regulation, SPDs also must include a statement identifying circumstances that may result in an offset or reduction of any benefits that a participant or beneficiary might otherwise reasonably expect the plan to provide “on the basis of the description of benefits.” The FAB explains that these requirements are intended to ensure that participants and beneficiaries are apprised of fees and charges that may affect their benefit entitlements.

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