

LOWENSTEIN SANDLER PC CLIENT ALERT

EMPLOYEE BENEFITS AND INVESTMENT MANAGEMENT

ATTORNEY ADVERTISING

NEW FORM 5500 REQUIREMENTS: WHAT INVESTMENT MANAGERS OF ERISA COVERED BENEFIT PLAN ASSETS NEED TO KNOW

By: Andrew E. Graw, Esq., and Karen W. Scheffler, Esq.

June 2010

Introduction

As sponsors and administrators of employee benefit plans ("plans") begin preparing their annual Form 5500 filings, it is important for investment managers to understand that the new 2009 Form 5500 requires the disclosure of information about investment management fees and may necessitate action in the form of a notice to benefit plan investors. This alert provides an overview of the rules and other requirements imposed upon investment managers by the new Form 5500.

General

A Form 5500 is the annual report filed by employee benefit plans subject to the Employee Retirement Income Security Act of 1974, as amended ("ERISA"). The annual filing reports the financial and operational conditions of the plan to the U.S. Department of Labor ("DOL") and the Internal Revenue Service ("IRS"). Plans with more than 100 participants (a "large plan") must include in the filing certain schedules, which provide detailed listings of investments, including a description of each asset and its value, as well as detailed information about fees paid to service providers. The Form 5500 is due seven months after the close of the

plan year, unless an extension is requested. A two and one-half month extension is available. The contents of these reports are public, and plan participants have a right to request copies of the report.

A plan must rely on information provided by its investment managers and other service providers in order to complete the Form 5500 properly. The DOL has released new amendments to the 2009 Form 5500 regulations that significantly increase the types and amount of information a plan must report about its service providers on Schedule C: "Service Provider Information." **Note that reporting of investment manager fees on Schedule C is required of each benefit plan whether or not the investment vehicles in which it invests exceed the 25% "plan assets" threshold.**

Schedule C

Direct and Indirect Compensation

Schedule C requires a plan to identify each service provider that received \$5,000 or more in direct or indirect compensation from a plan.

Direct compensation is compensation received by a plan service provider directly from plan assets, or reimbursed to the sponsor from the plan. For example,

charges paid directly out of a pension plan account for legal services are direct compensation.

Indirect compensation is any payment (monetary or nonmonetary) for services provided to the plan, or in connection with a service provider's position with the plan, received from sources other than directly from the plan or plan sponsor. For example, management fees paid by a fund to its investment manager are indirectly compensation from the plan that invests in the fund.

The plan must report direct and indirect compensation received as separate line items. In addition, the plan must report the name and employer identification number of the service provider; the type of services provided; the amount of compensation received; and whether a formula to calculate the compensation was provided by the service provider to the plan in lieu of a dollar amount.

If the plan reports indirect compensation received by a service provider of \$1,000 or more, the plan must also report the name and employer identification number of the payor of the indirect

LOWENSTEIN SANDLER PC CLIENT ALERT
EMPLOYEE BENEFITS AND
INVESTMENT MANAGEMENT

payment to the service provider and a description of the indirect compensation. For example, if an investment manager receives "soft dollars," the plan would have to report who paid the soft dollars to the investment manager and include a description of the payment.

Eligible Indirect Compensation

The DOL recognized that some service providers, such as investment managers, receive only indirect compensation from plans. In response, the DOL created a simplified reporting option for indirect compensation that qualifies as "eligible indirect compensation." The simplified reporting can only be used if certain information is disclosed to the plan administrator. Under the simplified reporting, only the name and employer identification number of the person who provided disclosure information to the plan will be required on Schedule C.

Eligible indirect compensation is generally indirect compensation that is charged against an investment fund and reflected in the value of the plan's investment, including the investment manager management fee from the fund, fees related to the sale and purchase of interests in the fund (including 12b-1 fees), soft dollars, and brokerage commissions, among other items.

The disclosure to the plan administrator must be in writing and include information regarding: (1) the existence of the eligible indirect compensation; (2)

the services provided for the eligible indirect compensation or the purpose for payment of the eligible indirect compensation; (3) the amount or an estimate of the compensation or a description of the formula used to calculate or determine the compensation; and (4) the identity of the parties paying and receiving the compensation. While this information is similar to that which is required on Schedule C, if it is disclosed to the plan administrator, then the plan does not have to disclose it on Schedule C.

Schedule C requires plans to list the names of service providers who fail or refuse to provide the information required for a plan to complete Schedule C. While it is not clear what action the DOL will take against such service providers, it is likely that most investment managers and other service providers would not want such exposure.

Action Item

It is important for investment managers to provide the disclosure described above to their plan investors within a reasonable time before the plan's Form 5500 is due in order to benefit from the simplified reporting. Plans will not ask investment managers for this disclosure. Rather, if plans do not receive the disclosure from investment managers they will request the information required to complete Schedule C for indirect compensation.

This is the first year of the new Schedule

C and "good faith efforts" will be acceptable such that a plan may still be able to report the fees as eligible indirect compensation if the investment manager sends the disclosure in response to an information request rather than before. However, the rules generally require the investment manager to send the disclosure to the plan within a reasonable period of time prior to the reporting date in order for the fees to be considered eligible indirect compensation.

Conclusion

The Form 5500, Schedule C requires service providers, such as investment managers, to a plan to provide information to plan investors that may ultimately be disclosed to the DOL and the IRS. Investment managers should understand their responsibilities in this area so that they are prepared to meet the requests of their plan investors and to take advantage of simplified reporting opportunities by providing disclosures to their benefit plan investors.

If you have any questions related to the Form 5500 and Schedule C, please contact:

Andrew E. Graw, Esq.

973 597 2588

agraw@lowenstein.com

Karen W. Scheffler, Esq.

973 587 2578

kscheffler@lowenstein.com

Lowenstein Sandler makes no representation or warranty, express or implied, as to the completeness or accuracy of the Alert and assumes no responsibility to update this Alert based upon events subsequent to the date of its publication, such as new legislation, regulations and judicial decisions. Readers should consult legal counsel of their own choosing to discuss how these matters may relate to their individual circumstances.

www.lowenstein.com

New York

1251 Avenue of the Americas
New York, NY 10020
212 262 6700

Palo Alto

590 Forest Avenue
Palo Alto, CA 94301
650 433 5800

Roseland

65 Livingston Avenue
Roseland, NJ 07068
973 597 2500