

Retirement Plan Transparency

Opaque Data Hinders Best-Interest Advice

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The Investor Success Project

Investors, Not Investments
The Morningstar Investor Success Project is a series of new research on investors—who they are, what their goals are, and how the advisors and asset managers that serve them can make the most impact in helping them reach those goals.

Executive Summary

Although often overlooked in policy debates, the annual disclosures for defined contribution plans, such as 401(k)s, need major improvements to provide useful information to regulators, retirement investors, advisors, and plan sponsors themselves. For example, the investment lineup information on the retirement plan disclosure (called the *Form 5500*) is often incompatible with Securities and Exchange Commission filings, making it impossible to match information on the investments available inside of 401(k) plans to other data the SEC already collects. Without such linkages, retirement plan filings only give glimmers of information, rather than connecting to the robust data on investments the government already collects in other forms. The Form 5500 also fails to require key data on popular investment types, such as collective investment trusts. These investments already include more than \$2.1 trillion in assets, so it is important to know more about them than the minimal data the federal government collects today. Finally, information on the administrative and investment fees participants pay is inaccurate and limited. These constraints undermine the entire purpose of public financial reporting, as the data is not actionable.

Given the limitations of retirement plan disclosures, it is impossible for financial professionals and regulators, let alone investors, to compare retirement plans' investment lineups to each other or to fully understand the state of defined contribution lineups. Improving the disclosures would make it much easier to see how much of a saver's hard-earned money pays for investment management (picking which individual stocks and bonds to buy and sell) and how much goes to third parties for services or for administering the retirement plan itself. Such transparency could also put pressure on high-cost providers to reduce fees. Even federal regulators—such as the Department of Labor—who collect the data, cannot easily identify retirement plan sponsors with questionable investments who might not be living up to their fiduciary duties. Further, inadequate public disclosures hamstring investors (and investment advisors trying to serve them) as they try to decide whether rolling over money from one 401(k) to another or from a 401(k) to an individual retirement account is a good or bad idea, as there is no central repository of information from which to gather key data. Modest adjustments to the Form 5500 could unlock retirement investment information to empower financial professionals and the individuals they serve.

Key Takeaways

- ▶ Current public defined contribution disclosures (found on the Form 5500) are inaccurate and incomplete
 - ▶ Retirement plan investment data usually cannot be linked to SEC filings, limiting its usefulness.
 - ▶ The DOL fails to collect key data on popular investment types, such as CITs.
 - ▶ Public information on the administrative and investment fees participants pay is inaccurate and limited.
 - ▶ Poor data impedes investors saving for retirement.
 - ▶ Employers and regulators cannot access critical information to help them improve the defined contribution system.
 - ▶ Third parties and advisors do not have the data to assess the quality of most defined contribution plans when evaluating rollovers from 401(k)s to IRAs or other 401(k)s.
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Introduction

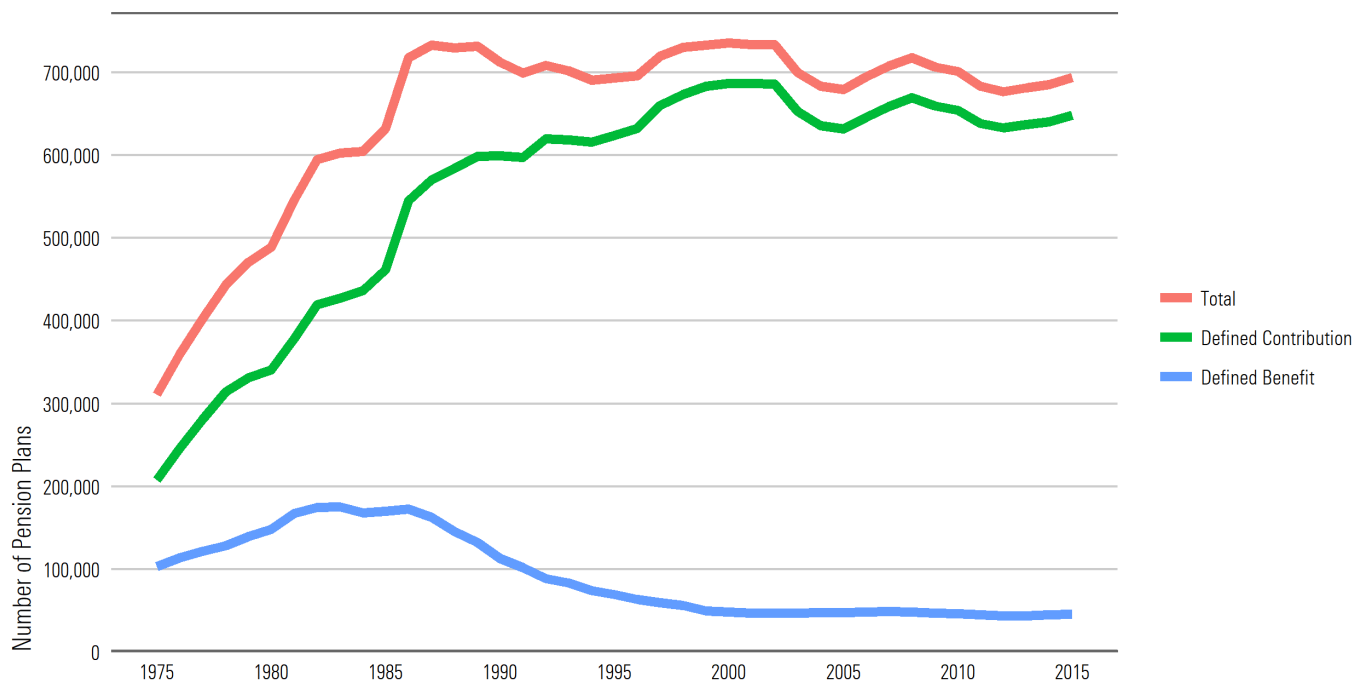
When most Americans invest, they do so through retirement plans: More than 648,000 private-sector defined contribution retirement plans cover almost 100 million participants and contain more than \$5 trillion in assets (Employee Benefits Security Administration, 2018b). Further, 75% of Americans invest solely through tax-privileged retirement plans, according to our analysis of the Federal Reserve's Survey of the Consumer Finance (Board of Governors of the Federal Reserve System, 2016). Most of these retirement plans are 401(k) types, which allow workers to contribute their own money and usually to choose investments from a preselected set of strategies, called *the plan lineup*.

To ensure that these plans serve their participants, the federal government requires public disclosures called *the Form 5500* from employers that sponsor plans. These filings are the main source of data on defined contribution plans and are vital for government regulators as well as private-sector financial professionals who wish to gain insights into this large pool of assets. Only plans that are covered by the Employee Retirement Income Security Act of 1974 must file, exempting most government retirement plans. These wide-ranging disclosures include information on a plan's investments, fees, and actuarial funding ratios for defined benefit plans, which in turn allows third parties to assess plan benefits, fees, and fiscal health. However, the government has not significantly updated the Form 5500 for decades.

During the last 40 years, defined contribution plans—which Congress originally envisioned as supplemental savings plans—replaced traditional defined benefit pensions as the principal retirement offering among U.S. private-sector employers. Exhibit 1 demonstrates how the number of defined contribution plans grew rapidly from their inception to the 1990s, while defined benefit plans saw a decrease from their peak in the mid-1980s through the late 1990s. The numbers have stabilized with almost 13 times as many defined contributions plans. Data elements that government auditors or third parties need to assess defined contribution plans are quite different from the elements they need to assess defined benefit pensions. Specifically, to assess the strengths and weaknesses of a defined

contribution plan, analysts need to know the investment lineup in which a retirement plan participant can invest, the fees for different investment options, and the overall administrative costs of the plan.

Exhibit 1 DOL Historical Graph of Plans by Type



Source: Employee Benefits Security Administration, 2018c.

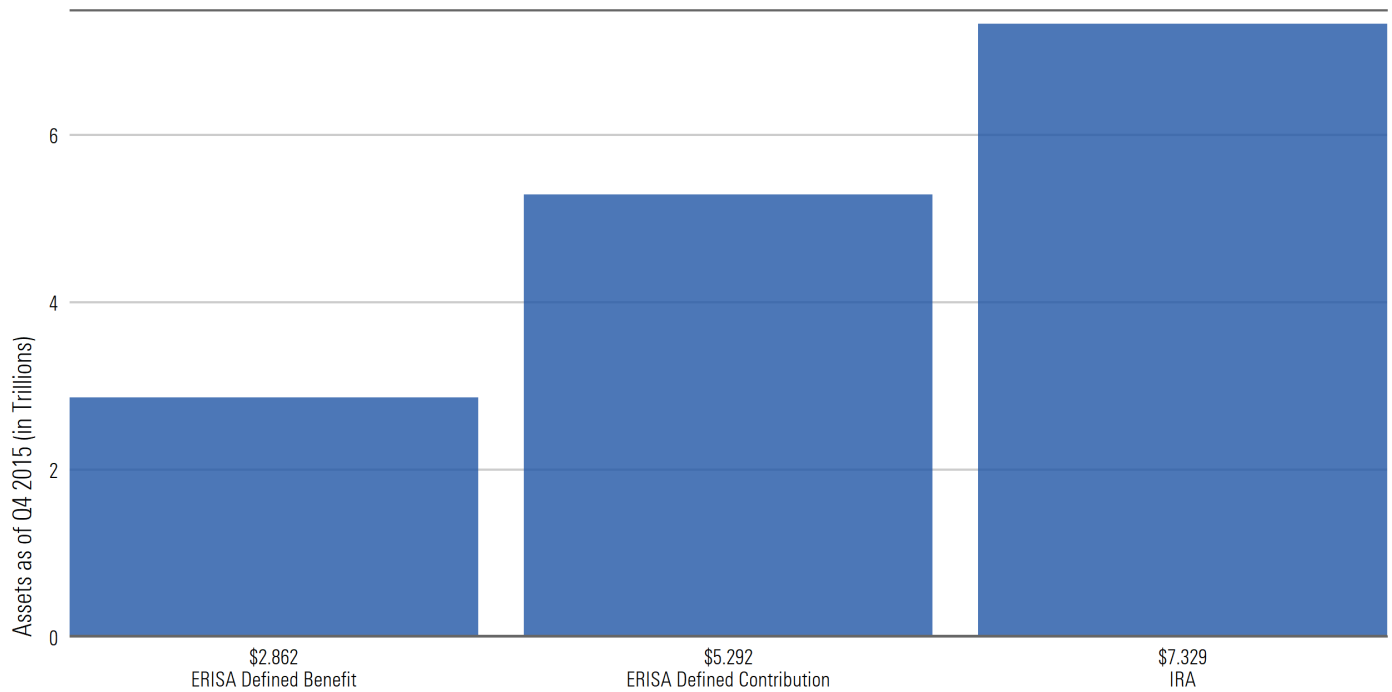
Concurrent with the rise of the defined contribution system, technological innovation unleashed new ways to help people save for retirement. Technology has democratized access to sophisticated retirement planning and investing techniques. However, regulators designed the Form 5500 disclosures for a different era, when technology did not permit modern techniques of consuming, repackaging, analyzing, and using the retirement plan data these disclosures contain.

Finally, during the past 40 years, participants have increasingly needed to make complex decisions when they switch jobs or retire. When defined contribution plans were merely supplemental, and retirees relied on a traditional monthly payment, the stakes were not as high. Today, most Americans' largest asset beside their home is their retirement savings, and an estimated 12 million annually need to determine whether to roll money from one plan to another or roll it into an IRA. The DOL has not adjusted the main source of data on retirement plans to account for these changing obligations for individual retirement investors.

Rolling money into IRAs has become so prevalent in recent years that total IRA assets (\$8.58 trillion as of October 2017) have eclipsed 401(k) assets—but there is widespread concern that many of these

rollovers are not in participants' best interests because IRAs often have higher administrative and investment fees (Employee Benefits Security Administration, 2016; Board of Governors of the Federal Reserve, 2017). In fact, the DOL's years-long effort to extend a best-interest standard of advice to financial advisors working with rollovers out of 401(k)-style defined contribution plans reflects this concern.

Exhibit 2 U.S. Retirement Landscape (Data as of the End of 2015 for Even Comparisons)



Source: Board of Governors of the Federal Reserve System, 2017; Employee Benefits Security Administration, 2018b.

In addition to the Form 5500—which is a publicly available record of retirement plans investments and administrative costs among other things—the DOL issued regulation 404a-5, which requires plans to provide retirement savers with a participant fee disclosure. These disclosures provide different information from the Form 5500 disclosures, but they are not widely or easily available to participants, let alone third parties, nor are they filed with any federal regulator.

In this white paper, we explore the data elements on the Form 5500 to examine 1) the extent to which the data is accurate and complete and 2) whether omissions or inaccuracies on the form impede ordinary retirement savers and their advisors as they try to make decisions to ensure a secure retirement.

Background on the Form 5500

Three agencies—the DOL, the Pension Benefits Guaranty Corporation, and the Internal Revenue Service—produce the form that covers defined contribution retirement plans, defined benefit retirement plans, and welfare benefit plans, but the DOL collects it and determines most of the information that is

relevant to defined contribution plans, such as 401(k)s. Most of the information the Pension Benefits Guaranty Corporation and the Internal Revenue Service require relate to traditional defined benefit plans and are out of the scope of this paper.

Employers fill out the Form 5500 for each retirement plan they offer, and due to an automatic extension, the deadline is usually October 15 of the year following the fiscal year of the plan. In addition to employers (known as *plan sponsors*), some investment providers fill out the form as well, typically for products that do not already have existing public filings with the SEC. (The SEC is the primary regulator of most investment products, such as mutual funds.) Collectively referred to as *direct filing entities*, these investment providers include master trusts that hold assets from related plans; pooled investment vehicles not limited to related plans maintained by a bank or trust company, known as *CITs*; and pooled separate accounts maintained by an insurance company. Whether the filing is required or optional for the provider of a given pooled product depends on the type of DFE.¹

The Form 5500 consists of three general cover pages and up to 12 specific schedules. The cover pages collect high-level data that is applicable across the various types of filers—small plans, large plans, welfare plans, DFEs—while the schedules each focus on one aspect and are each only required for a subset of filers. (A description of each schedule and what types of filers must include them can be found in the Appendix.) For example, the Schedule D gathers information on DFEs and plans participating in DFEs. All DFEs that file must complete this, as well as Form 5500 filers that invest in any type of DFE.

There is also an abbreviated version of the Form 5500, called *the Form 5500-Short Form*, that is available to most small plans that have fewer than 100 participants. Unlike the filing requirements for large plans, 5500-SF only requires plans to complete three pages with key information focusing on plan identification, number of participants, amount of assets, summary expenses, and compliance oversight. The simplified 5500-SF is meant to make the filing process less cumbersome and, therefore, less of a barrier to plan creation for small companies.

Current Defined Contribution Disclosures Are Inaccurate and Incomplete

Retirement Plan Investment Data Usually Cannot Be Linked to SEC Filings, Limiting Its Usefulness

Large retirement plans report all the investments in which the plan had assets at the end of the year; however, the Form 5500 does not require information that is compatible with databases on investments maintained by the SEC. Instead, the only identifying information plans provide on their 401(k) investment lineup is a strategy name, and there are few guidelines on other details the plans must provide. Further, retirement plans report their investments as an attachment to the main filing without using a standardized format and sometimes as a scanned image. This unstructured data makes it hard for the DOL or third parties to aggregate, analyze, and understand 401(k) plan investments. Text recognition technology enables a few companies (including Morningstar) to parse these unstructured filings, but the nonstandard data creates additional obstacles, reducing plan transparency.

¹ For DFEs that have optional filing, the alternative is for the plan itself to file additional disclosures, but we don't see this frequently in practice.

Current guidance for plan sponsors on how to identify the investments they offer plan participants is vague. As a result, most of the information plan sponsors provide on investments is not useful, although some plan sponsors provide better information identifying their investments than others. Specifically, the Form 5500 asks for the “identity of issue, borrower, lessor or similar party” and a “description of investment, including maturity date, rate of interest, collateral, par or maturity value,” allowing filers to interpret how these relate to their various investments (Employee Benefits Security Administration, Internal Revenue Service, and Pension Benefits Guaranty Corporation, 2016). The resulting level of detail provided in the name can vary from simply stating the strategy of the investment, such as *Small Core Fund*, all the way to specifying the investment provider, share class, and ticker, such as *Vanguard Short Term Treasury Admiral (VFIRX)*, which can be linked to an investment’s other public filings with the SEC via the contract or class ID. There is even variation in what is reported in each of the two fields. Some plans will put the entire investment name as the identity and provide the investment vehicle, such as a mutual fund, in the description, yet others consider an investment provider like PIMCO to be the identity of issue and the investment name to be the description. The latter approach leaves no place to specify the type of vehicle and, since many providers offer the same strategy through multiple vehicles to accommodate different plans, this can further complicate matters.

Unfortunately, most plan filings provide little information and the public generally can only glean the investment provider and strategy name, as shown in Exhibit 3. *Plan A* does not report sufficient information to assess which investments are available, which is typical. *Plan B* includes ticker symbols, making it easier to link these investments to public filings; however, these tickers only exist for certain investments. *Plan C* includes share-class-level data, which, in turn, makes it easiest to identify the investments and fees charged to retirement savers.

Exhibit 3 Investment Lineup Reporting Examples as Reported on Actual Form 5500s**Plan A**

<u>IDENTITY OF ISSUE</u>	<u>DESCRIPTION OF INVESTMENT</u>	<u>CURRENT VALUE</u>
500 INDEX FUND	7,297.960 SHARES (1)	143,565
ABERDEEN INTERNATIONAL EQUITY	6,178.366 SHARES (1)	78,596
ACTIVE BOND FUND	32.954 SHARES (1)	480
BLACKROCK BASIC VALUE	1,449.352 SHARES (1)	57,994

Plan B

(a) * identifies party-in-interest	(b) Identity of issue, borrower, lessor or similar party	(c) Description of Investment	(e) Current Value
	Vanguard	Vanguard 500 Index Adm (VFIAX)	\$ 1,811,418
	Vanguard	Vanguard Wellesley Income Investor (VWINX)	1,659,693
	Dimensional Fund Advisors	DFA International Core Equity (DFIEX)	1,100,819
	Parnassus	DFA US Core Equity II (DFQTX)	851,353

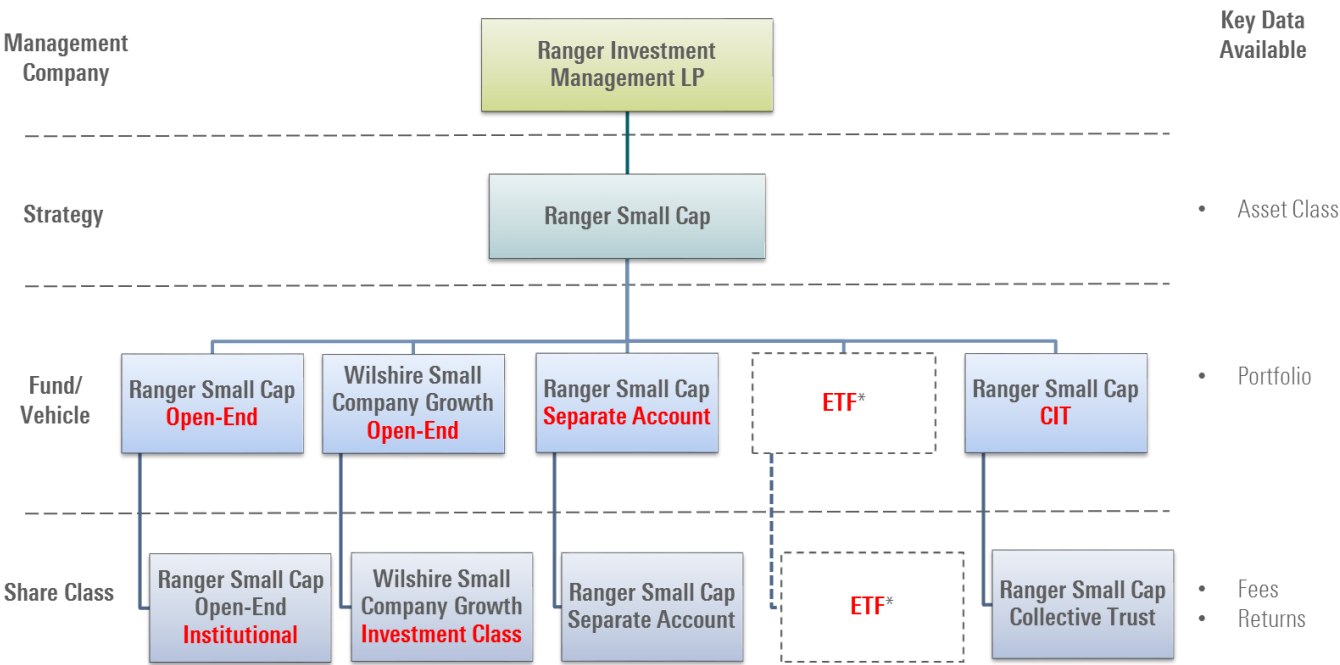
Plan C

(a)	(b) Identity of Issue, Borrower, Lessor or Similar Party	(c) Description of Investment	(d) Cost Value **	(e) Current Value
		<u>Collective Fund</u>		
*	Wells Fargo Bank, N.A.	Stable Return Fund N		\$ 4,969,407
		<u>Mutual Funds</u>		
	TCW Funds	Galileo Core Fixed Income I		1,899,217
	American Beacon Funds	Large Cap Value Fund Inst		2,895,062
	Vanguard Funds	Small Cap Index Fund Adm		1,572,961

Source: Morningstar database of Form 5500 filings.

Without clear identification to connect reported investments to SEC filings, important information on fees and other investment attributes is often unattainable. The SEC collects filings at the company, fund, and class or series level, spanning everything from company registrations to general descriptions of investments and annual statements detailing class-level expenses. While some of the company, strategy, and fund information is useful, the fees participants pay and the performance of their investments depend on the share class. Exhibit 4 illustrates how one strategy can manifest itself through multiple vehicles and share classes, with different information available at varying places in the hierarchy. Significantly, many of these have very similar names and, since most retirement plans do not report the share class name, the related filings cannot be identified. Data from 2015 filings indicates that almost \$2 trillion dollars, representing 43% of total net assets from plans that reported, are invested in vehicles that are registered with the SEC. Although specific information for these investments is available through the SEC, when retirement plans provide only the strategy name, it is impossible to access this rich information on the underlying investments.

Exhibit 4 Typical Hierarchy of Investment Strategies and Their Availability to Investors in Different Forms



*This strategy does not have an ETF version. Included for demonstrative purposes as strategies will leverage a variety of combinations of these vehicles.

There is a similar disconnect in how the SEC and the DOL collect company data, which inhibits both the agencies and third parties from easily and completely assessing arrangements between plans and service providers. In addition to collecting public filings for registered investments, the SEC also collects registration and business information from investments advisors through the Form ADVs. The Form 5500 requires large plans to identify service providers, such as companies that provide administrative or investment advisory work, to whom they paid more than \$5,000 in the previous year. In this case, the information is reported in a standardized format that can be easily aggregated, but the sole identifier the DOL requires is a company's employer identification number. Meanwhile, the SEC uses central index key numbers. If the DOL collected CIK information on the Form 5500, it would allow them and third parties to better understand these arrangements and provide a more holistic understanding of the retirement landscape.

DOL Fails to Collect Key Data on Popular Investment Types Such as CITs

The DOL recognizes that plan sponsors include investments that are not registered with the SEC, or any other federal agency, in their retirement plans and require additional reporting on these types of unregistered investments. However, the Form 5500 reporting requirements leave out critical information for evaluating these investments. Three prevalent types of unregistered investments in retirement plans are master trusts, CITs, and separately managed accounts (SMAs). Plan sponsors with multiple plans, perhaps for different types of employees or as a result of mergers and acquisitions, can use master trusts to pool all their plans' assets. For reporting purposes, each plan with assets in the master trust must hold a representative portion of the master trust's investments. Whereas master trusts generally hold underlying investments covering multiple strategies, CITs are pooled vehicles with a specific investment strategy. CITs can hold assets from unrelated plans, are administered by banks and trust companies, and are designed exclusively for qualified retirement plans, which is why they are not registered with the SEC. Collectively, master trusts and CITs represented more than \$4 trillion in plan assets in 2015, covering more than 50 million participants. Unlike these pooled investments, every SMA is unique to one plan, allowing larger plan sponsors to customize their investment options. With current reporting standards, it is impossible to even estimate total SMA assets. Each of these investment types is subject to different reporting requirements on the Form 5500 but there is not a complete picture for any of them, as summarized in Exhibit 5.

Exhibit 5 Overview of Popular Non-SEC Investments

	Master Trust	CIT	SMA
Issuer	Bank, trust, or insurance	Bank or trust	Asset manager
Additional Regulatory Oversight	Office of the Comptroller of Currency (OCC) or state regulators	OCC or state regulators	The SEC oversees asset managers but does not collect information on separate account investments
Number of Investors	Pooled	Pooled	Single
Connection Between Pooled Investors	Related plans	Plans, related or not	N/A
Strategy	Multiple strategies	Single strategy	Single strategy
Form 5500 Filer	Required	Optional (very common)	No
Assets as of December 2015 (master trust and CIT are not mutually exclusive)	\$2.1 trillion	\$2.117 trillion	Unknown

Source: Morningstar; Employee Benefits Security Administration, 2018a.

Each plan having a fractional interest in a master trust should simplify the process for understanding multiple plans' investment options; however, in most cases, it instead creates more uncertainty. Master trusts report their investments in the same manner as large plans. In theory, this means that all plans participating in the master trust offer those investments to their participants. The confusion arises because many master trusts report hundreds of individual common stocks, bonds, and derivatives on their Form 5500. These do not make sense as unique investing options for 401(k) plans and are likely used for accounting purposes when transitioning assets between plans or investments. As participating plans are only required to report their overall investment in the master trust, this, unfortunately, muddles the picture of what investments participants have access to for thousands of plans.

The Form 5500 is the main public disclosure of CITs and it specifically exempts them from providing information on the fees participants pay or the portfolio in which they invest. This basic information is critical for understanding or evaluating these investments. While plans investing in a CIT must report the CIT's name and the managing bank or trust company's name and EIN on their Form 5500, CITs themselves often file a Form 5500 to simplify the process for plans investing in them. The only information they must report, however, is the plans investing in them, any CITs or other pooled investments in which they invest, and summary numbers on the vehicles their assets are invested in. Although there are flaws in the data currently collected, the Form 5500 is equipped to collect information on compensation to service providers and the specific investments of a filer, but CITs are exempted from completing these sections. Further, understanding the performance of an investment is central to the evaluation of it and this information is not publicly available for CITs, nor is the current Form 5500 set up to collect this information. CITs represent a large part of the retirement landscape, and without improvements to their Form 5500 reporting, there will be a persistent gap in data availability based on investment structure.

The Form 5500 instructions and previous DOL guidance do not address the unique challenges of reporting investments in SMAs, resulting in plans adopting a variety of reporting methods, none of which capture all the necessary data. SMAs are another growing investment vehicle for retirement plans, mostly among large plans, as they allow for customization in both the strategy and the fee structure. Although asset managers may have models or composites on which SMAs are based, each plan investing in an SMA will have their own account where they can customize the strategy and holdings as desired. Through these accounts, the plans directly own the underlying holdings (stocks, bonds, etc.) rather than just owning shares of a pooled vehicle such as a mutual fund or CIT. Since these accounts are specific to a given plan, the fees that plans pay for investment management, custodial, and administrative work can vary by plan. As with CITs, SMAs are unregistered and, therefore, lack publicly available disclosures of fee, performance, and portfolio information. Currently, we have found examples of plans reporting SMAs as a subset of a CIT, as a unique CIT, and as the underlying investments. While there are advantages and disadvantages to each of these methods, the lack of consistency prevents a complete understanding of the use of SMAs within retirement plans, and none of these resolve the lack of fee and performance information for these vehicles.

Public Information on the Administrative and Investment Fees Participants Pay Is Inaccurate and Limited

The Form 5500 fails to capture the full cost to an individual of participating in a plan, a key factor in analyzing plan quality. The costs associated with investing in a retirement plan are generally bucketed into plan fees associated with the administrative expense of operating a plan and investment fees incurred through the investments that are offered. As small plans are not required to disclose their investments, there is no way to determine the investment fees participants pay from the Form 5500. Large plans disclose their investment options but generally do not provide enough information to identify the investment fees. As previously detailed, there is often insufficient information to connect reported investments to SEC class filings, and there are no public disclosures that would include fees charged for unregistered investments such as CITs and SMAs.

Knowing the investment fees of a specific plan lineup is significant, given that we estimate the most common non-index investments in plan lineups can range from 0.24% to 1.73% of the assets, annually. To arrive at this estimate, we used Morningstar's Retirement Plan Intelligence data for the 2015 plan year. We started by considering plans with more than five and fewer than 50 investment options to eliminate outliers. We identified investments in the 17 most common Morningstar categories offered by plans. We then reviewed the top 20% most common non-index investments in each category and averaged the cheapest and most expensive to account for variation in expense related to the complexity of different investment strategies. Assuming a starting balance of \$10,000 we can estimate the impact to an investor's savings of paying up to 149 more basis points in fees over 20 years can be almost \$7,908 or a 25% loss, assuming an annual real return of 6%.

Understanding the investment fee structure of a plan is even more important when we consider that many investments include distribution, sub-transfer agency, or revenue-sharing fees that are meant to offset plan fees. Included within the expenses of some share classes, these fees are funneled from the asset manager who collects them to the recordkeeper of the plan where the share class is being used. Since retirement plans require individual accounts be kept for each participant, the theory is that these fees take advantage of the economies of scale by allowing the asset manager to treat many accounts as one account in their books and having the recordkeeper keep track of the details for each participant. Although these are paid through the investment fees, because they end up being paid to the traditional recipients of plan administrative fees, they can reduce the direct plan fees paid by participants. Therefore, plans that offer investments with these arrangements should generally have lower direct plan fees and plans without them may have higher direct plan fees, but that cost is weighed against the nominal investment expenses. Without knowing the investment fees of a plan and what transfer payments they include, it is difficult to fairly evaluate the plan fees. Further, plans are specifically exempted from reporting these types of indirect expenses on the Form 5500 as they are treated as *eligible indirect compensation*. This concept was introduced in the 2009 revisions of the Form 5500 and created significant confusion as the term does not exist in other regulation and has no clear parallel. Unfortunately, the misunderstanding of eligible indirect compensation persists, resulting in inconsistent and, therefore, unreliable reporting.

While it is not ideal to assess plan fees in isolation, it would still be preferable to not having information on plan fees, but the plan fee data collected by the Form 5500 is internally inconsistent, creating doubt about its overall accuracy. All plans are required to report the total dollar amount of plan fees paid by participants in the previous year.² As previously mentioned, only large plans are required to report the distinct service providers that these fees were paid to and only if it was more than \$5,000. For the large plans that report both total plan fees and the distinct payments to service providers, it is, therefore, possible to compare and validate their numbers. Since the specific payments are not reported for values less than \$5,000, it is reasonable to expect that, in some cases, the sum of the distinct payments will be less than the reported total plan fees. However, we found that 19% of plans had discrepancies in the opposite direction. In order for the sum of the distinct payments to be greater than the total plan fees, the plan must either be overreporting distinct payments by including some that were covered by the company or underreporting the overall plan fees paid by participant accounts.

An additional 18% of plans reported total expenses that were more than \$5,000 greater than the sum of the distinct payments reported. While this could be explained by plans paying multiple service providers below this threshold, the differences in fees represented more than a third of the total fees for 60% of these plans. This suggests that the \$5,000 threshold is not capturing key information on service provider relationships for a large proportion of plan fees across all retirement plans. With the prevalence of inconsistency within Form 5500 plan fee data, there are inevitably questions surrounding the overall accuracy and usability of this information.

² Although more than 120,000 left it blank in 2015.

Finally, small plans serving more than 30 million individuals are permitted to file extremely simplified information, yet these are the plans that we estimate cost participants the most. It has been well documented that small plans generally serving fewer than 100 people are under-researched due to the lack of publicly available data (Rekenthaler, Spiegel, and Szapiro, 2017). While we estimate they are the most expensive to participants, this is based on a limited dataset and the true cost is unknown. The intent to reduce costs for small plans by exempting them from the time-consuming and costly effort of filing a full Form 5500 is reasonable; nonetheless, this has led to a gap in understanding and is inconsistent with how these plans are treated by other regulations. In particular, these plans are not exempt from the 404a-5 regulation that requires them to furnish information on investment options and service provider arrangements annually to participants — information that is lacking from the Form 5500 filings.

Poor Data Impedes Investors Saving for Retirement

Employers and Regulators Cannot Access Critical Information to Help Them Improve the Defined Contribution System

Employers cannot easily assess if the fees they pay in their retirement plans are appropriate, if their investment lineups are best-in-class, or how they can improve their retirement offerings, given the opacity of data in the U.S. defined contribution retirement system. For example, despite the popularity of CITs among many retirement plan sponsors, employers cannot easily find out if the fees they pay are too high because they cannot see what other similar plans pay. Similarly, plan sponsors cannot easily assess if the administrative fees they pay are reasonable because the publicly available data is incomplete and of questionable quality.

Regulators do not have a full picture of the retirement system. First, the regulators cannot easily leverage each other's work because the filings the DOL requires cannot be easily matched with the ones the SEC collects. Therefore, the DOL cannot automate processes for finding unusual plan lineups that might merit more investigation. If the SEC finds problems with an asset manager, the DOL cannot look for retirement plans that asset manager works with to extend an investigation. The DOL also collects such limited information on popular investments, such as CITs, that they cannot determine whether retirement plans using these vehicles are acting in their participants' best interests. As with employers, the DOL is blind to whether certain plans pay fees that are well out of the normal range unless they investigate and request more information.

In contrast to the public-facing Form 5500 disclosure, the disclosures the DOL requires plans to provide directly to participants provide much of the information necessary to help retirement investors evaluate their plans. As discussed in the introduction, the DOL requires plans to provide retirement savers with a participant fee disclosure, often called a *404a-5 disclosure*, after the regulation for which it is named. These disclosures provide different information from the Form 5500 disclosures, but they are not widely available to anyone or even required to be filed with the DOL. As illustrated in Exhibit 6, making information on the 404a-5 public would greatly improve the overall quality of the data available to regulators, employers, plan participants, and their agents and advisors.

Exhibit 6 Data Available From Public and Private Disclosures

Investment Information and Fee Information	Large Plan Public Disclosure (Form 5500)	Small Plan Public Disclosure (Form 5500-SF)	All Plans Private Disclosure to Participants (404a-5)
Strategy Name	Yes	No	Yes
Fee for Each Investment Option	No	No	Yes
Benchmarks for Investment Options	None	None	Yes
Link to SEC Filings	No	No	Indirect
Administrative Fees	Partial	Partial	Yes
Payments to Service Providers	Partial	No	Partial
Frequency	Annual	Annual	Annual + when changes
Time Period Covered	Previous plan year	Previous plan year	Current as of filing

Source: Morningstar analysis of 2016 Instructions for Form 5500 (Employee Benefits Security Administration, Internal Revenue Service, and Pension Benefit Guaranty Corporation, 2016) and 404a-5 Regulation (Fiduciary Requirements for Disclosure in Participant-Directed Individual Account Plans, 2010).

To summarize, the combination of the information in the private 404a-5 disclosure and the public Form 5500 does fill in many of the gaps in the current regulatory regime, empowering regulators and plan sponsors to understand and improve the system. The Form 5500 does not include most investment fee information, but the 404a-5 does so. The 404a-5 does not always include information on how much service providers are paid, but the Form 5500 does so, even if the information is not as high quality as it should be. The Form 5500 has unreliable administrative fee data, but the 404a-5 has better information, at least detailing the maximum administrative fee a participant might pay. Finally, although the 404a-5 cannot be directly linked to identifiers the SEC uses, it provides enough information for sophisticated third parties to identify which SEC-registered investment the plan provides its participants.

Third Parties and Advisors Do Not Have the Data to Assess the Quality of Most Defined Contribution Plans When Evaluating Rollovers

Inadequate public disclosure harms investors and investment advisors trying to serve them as they try to decide about rolling over money from their current retirement plan. Most retirement investors do not have the background to properly assess one of the most important decisions they need to make — whether to roll their retirement savings from a 401(k) or other defined contribution plan into an IRA, leave it where it is, or roll it over to another employer's 401(k). Retirement savers often make these decisions when they are switching jobs or retiring — moments that are quite stressful already.

To evaluate a rollover, participants or their advisors must perform sophisticated analyses including 1) modeling their ideal asset allocation based on their age, retirement income needs, desired retirement date, and other sources of income, among other variables; 2) determining how to allocate the funds or investment alternatives in their plan to this ideal allocation; 3) assessing whether another defined contribution plan or an IRA could deliver the same asset allocation with higher-quality or lower-fee funds; and 4) evaluating the value of advice and financial planning offered through the 401(k) plans' services or as part of the IRA program. For people approaching retirement, the Form 5500 has limited

information on lifetime income options in the plan, which could be helpful for assessing cases where participants should stay in their plans through retirement.

Public and accurate disclosure of plans' investment alternatives would make evaluating rollovers simple and easy, as is already true for other products. Financial products with clear public disclosures empower third parties to organize and contextualize this information. For example, ordinary investors using Morningstar's (and our competitors') services can easily compare the cost and quality of mutual funds to each other. But if someone is trying to assess what their 401(k)'s strengths and weaknesses are, no one can easily run the analysis described previously based on public filings. (Of course, a few companies, including Morningstar, try to use the data that does exist to give their best assessment of a rollover, but there are limits to the analysis that can be performed with existing information about defined contribution plans.)

From our experience working with advisors, this lack of transparency hampers advisors trying to act in their clients' best interests, particularly when they try to serve less-well-off clients. If a plan participant meets with an outside financial advisor, the advisor cannot easily compare the plan to a rollover option or make recommendations about rebalancing in a plan without detailed plan lineup data. Even in cases in which a participant brings a hard copy of the plan's 404a-5 disclosure, the advisor would need to manually enter the information and then set up a follow-up meeting to analyze the client's options. This additional effort greatly increases the cost of offering financial advice. Allowing financial technology firms access to high-quality plan filings, in contrast, would help democratize access to advice on rolling over from or between defined contribution plans.

Conclusions


The DOL has long been concerned with ensuring that participants understand their investment options and fees. In the preamble to the fee disclosure regulation, the department noted the regulation was "intended to ensure that all participants and beneficiaries in participant-directed individual account plans have the information they need to make informed decisions about the management of their individual accounts and the investment of their retirement savings." The preamble goes on to say that the DOL "believes that all participants and beneficiaries with the right to direct the investment of assets held in their individual plan accounts should have access to basic plan and investment information" (Employee Benefits Security Administration, 2010). In a 2016 Form 5500 reform proposal, the DOL acknowledged the Form 5500 needed to be refreshed in order "to assist plan participants, and beneficiaries and the public in better monitoring the activities and investments of employee benefit plans." (Proposed Revision, 2016).

Simply put, shrouding fee and investment information in secrecy due to widespread exemptions, inconsistencies, and gaps undermines the goals of making fee information accessible to participants. Even sophisticated retirement savers who find their disclosures and understand them cannot put the fee information into context. Further, they cannot easily link their retirement plan disclosures to the robust investment disclosures the SEC collects. Similarly, regulators and employers cannot determine whether

the defined contribution system is working without the data to answer key questions about the investments retirement savers can access.

Recommendations

The DOL could greatly improve outcomes for many retirement investors with a few relatively small changes to the Form 5500, some of which the DOL already proposed in 2016. The DOL should:

- ▶ Require plan sponsors to include the most recent plan 404a-5 disclosure with the Form 5500 to give a more complete picture of the U.S. defined contribution retirement system and shed light on retirement investment fees. As discussed in the background, the data could potentially be out of date, given the filing deadlines for the Form 5500. However, Congress should amend the plan filing requirements to ensure that if a plan changes its investment lineup or fees, it reports these changes to the DOL in a timely way. Plans already need to tell their participants when they make such adjustments, so such a requirement should not be onerous.
- ▶ Collect the SEC contract/class ID for the investment information plans report on the Schedule H of the Form 5500, which would facilitate connecting retirement plan investment options to SEC data and empowering employers, regulators, and third parties as they evaluate retirement plan investments options.
- ▶ Improve the quality, depth, and breadth of data collected on CITs, SMAs, and other unregistered investments on the Form 5500 to provide a more complete picture of the U.S. retirement system. This can be accomplished by:
 - ▶ Defining a uniform manner for reporting nonpooled investments (e.g., SMAs) to facilitate their identification. This definition should require end-of-year holdings, annual fees, and recent returns.
 - ▶ Requiring unregistered pooled investments (e.g., CITs) to report their end-of-year holdings on the Schedule H, Part IV, Line 4i attachment and requiring plans that make these pooled investments available to their employees to report annual fees and recent returns on the Schedule D.
- ▶ Update the service provider reporting on the Form 5500 to require plans to report the formula used to determine compensation for plan service providers and the daily average assets or accounts upon which that formula was applied for the previous plan year. This reform would provide a more complete understanding of plan operations and their associated costs. The requirement would not be onerous because service providers already share this information with plan sponsors under regulation § 2550.408b-2. 

Appendix

Exhibit 7 Summary of Form 5500 Schedules

Schedule	Who Files	What It Contains
A (Insurance Information)	Small plans, large plans and certain DFEs (e.g., master trusts) that had benefits provided by an insurance company	Identification and fee information for insurance and annuity contracts
C (Service Provider Information)	Large plans and certain DFEs (e.g., master trusts) that paid \$5,000 or more to at least one service provider	Service provider arrangements (e.g., investment management, recordkeeping fees) that result in at least \$5,000 of compensation from plan assets, i.e., not paid for by the plan sponsor
D (DFE/Participating Plan Information)	Small and large plans that invested in a DFE	For both: Name, DOL reference (EIN and plan number) and plan assets of each DFE held by the filer
	DFEs that are required to file (e.g., master trusts) or that opt to file to reduce the reporting burden on participating plans (e.g., CITs, PSAs)	For DFEs only: Name and DOL reference of plans that held the DFE
G (Financial Transaction Schedules)	Large plans and certain DFEs (e.g., master trusts) that had loans or leases in default or that had nonexempt transactions with a party-in-interest (e.g., plan service provider)	Identification of other party and general description, and price and expense information for each defaulted loan, defaulted lease, or nonexempt transaction
H (Financial Information)	Large plans and DFEs	For all: Summary of plan assets, liabilities, income and expenses
		For large plans and certain DFEs (e.g., master trusts): Compliance checks, plan termination information, and (as an attachment) schedule of investments
I (Financial Information – Small Plan)	Small plans	Total plan assets, liabilities, income, expenses, and transfers; specific amounts for hard-to-value assets (e.g., employer securities)
MB (Multiemployer Defined Benefit Plan and Certain Money Purchase Plan Actuarial Information)	Multiemployer defined benefit plans and money purchase plans subject to minimum funding standard	Actuarial valuation of plan funding submitted by plan-enrolled actuary
R (Retirement Plan Information)	Small and large defined benefit plans	Summary of plan distributions, minimum funding obligation, contributors for multiemployer plans, and compliance checks
SB (Single-Employer Defined Benefit Plan Actuarial Information)	Single-employer and multiple-employer defined benefit plans subject to minimum funding standards	Actuarial valuation of plan funding submitted by plan-enrolled actuary

Note: Most small plans are eligible to file the Form 5500-SF and are exempt from filing all of the listed schedules.

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