

Submitted electronically [e-ORI@DOL.gov]

December 2, 2016

Office of Regulations and Interpretations
Employee Benefits Security Administration
Attn: RIN 1210-AB63; Annual Reporting and Disclosure, Room N-5655
U.S. Department of Labor
200 Constitution Avenue NW
Washington, DC 20210

RE: RIN 1210-AB63; Proposed Revision of Annual Information Return/Reports

Ladies and Gentlemen:

Morningstar, Inc. appreciates the opportunity to comment on the proposed changes to the Form 5500 Annual Return and Report forms. Morningstar's interest in the Form 5500 stems from our offering a variety of services to employer-sponsored plans, and from our Retirement Plan Intelligence business unit (formerly RightPond), which aggregates retirement plans' annual reports and auditors' reports from the Form 5500.

Morningstar applauds the Agencies for proposing important steps to increase retirement-plan transparency. We believe that the proposed revisions to the Form 5500 will make it much easier to understand the investments that retirement plans hold and the compensation they pay to their providers. We also believe the proposed changes will improve defined-contribution (DC) plans for participants and beneficiaries by making it easier to understand the investments available to them, and the costs of investing through the plan. These disclosures are even more important today because plan participants need to consider whether to roll money from one DC plan to another, or whether to roll some (or all) of their money into an IRA. Without clear information, it is difficult for plan participants to ascertain whether (and in what areas) their plan provides a good value compared with other options. Further, it is difficult for financial advisors to ascertain the strengths or weaknesses of an advisee's plan when they give advice.

We also believe that the private sector has an important role to play in gathering, analyzing, and disseminating plan information so that participants can understand and measure their plans in context. In that spirit, we have suggestions for three areas that might further strengthen the Form 5500: 1) adding additional structured data, which the agencies currently propose to collect as non-standardized attachments; 2) collecting additional identifiers that match the identifiers required by the Securities and Exchange Commission (SEC); and 3) making

additional improvements to the Schedule C that could reduce the burden on plan sponsors while generating a rich dataset on indirect compensation. We also wish to note the areas where the proposed changes could greatly aid researchers studying the U.S. retirement system as a whole.

Adding Additional Structured Data on Investment Choices and Fees

We believe that requiring plans to submit key elements of the Investment Options Comparative Chart (as required under 29 CFR 2550.404(a)(5)) in a standardized format, instead of included as a non-standard attachment as proposed, would greatly increase the utility of the Form 5500, and help achieve the Agencies' goals. First, this would partially correct a gap in information for small plans that do not need to file a Schedule I (or Schedule H pursuant to the revisions.) In addition, such a standardized disclosure would fill gaps in information about collective investment vehicles, which remain despite the positive changes in the new proposal. This disclosure would also help Form 5500 users understand annuity products offered inside plans. The key elements from the 404(a)(5) disclosure that should be included in a standardized format are the expense ratios and additional shareholder-type fees for investment options, as well as the annuity objectives and goals, pricing factors, restrictions, and fees.

To be clear, the proposal as written would already correct an important issue with the Form 5500's investment disclosures for plans: At present, there is no way to ascertain from the Form 5500 which mutual funds and share classes a plan offers—just the investment strategy. Further, the data we have is reported inconsistently within plans from one year to the next. Instead, plans disclose investment strategies, but it is not possible to determine the fee associated with the investment. Additionally, the current attachment on which plans disclose their investments (line 4i on the Schedule H), does not have a standard reporting requirement, so data is inconsistent between plans. For these reasons, data aggregators, and consequently the public, have a limited view of the quality and cost of the investments a plan offers. It is true that plan participants have access to investment disclosures pursuant to 404(a)(5), but these disclosures are not available to the public at large, making it difficult to compare plans to each other. The proposed changes to the Form 5500 largely correct this issue for mutual funds by requiring a host of identification information and standardizing the disclosures in a revised line 4i. Further, the Agencies are requiring these 404(a)(5) disclosures as an attachment in line 4o (or as part of the short form for eligible plans).

Nonetheless, these revisions do not help data aggregators and researchers fully fill in the details of the investments offered to sponsors and plan participants; more could be done to improve plan transparency. First, although the required 4(i) attachment will collect the cost of the acquisition, it does not require the expense ratio of assets such as mutual funds, nor other types of shareholder fees. This data will only be available in an unstructured format as an attachment. In the case of mutual funds, it will be possible to get this information from a database of funds using the Committee on Uniform Security Identification Procedures (CUSIP) or other identifying information, but this adds an additional potentially cumbersome step.

Moreover, for collective trusts, for which expenses can vary by client, the unstructured 404(a)(f) disclosure is likely to be the only public source of information about what a participant in that specific plan pays.

For small plans that do not need to file the Schedule H, data aggregators and researchers would be forced to “scrape” the data from their 404(a)(5) attachments. While this is not impossible, such an approach will not be as reliable as structured data in a standard 4i format. Although small plans only cover about 10 percent of participants, there are about a half-million of them, so gathering data without the aid of a structured format could be very challenging, particularly since the 404(a)(5) formats may change over time with no notice. Small-plan participants deserve to know how their plan compares to others, but it will be difficult for data aggregators to provide this information unless the fee elements and fund names at a minimum are included in a structured format.

In the case of fees on collective or common investments held in Direct Filing Entities (DFEs), the proposal will still make it difficult to ascertain the expense ratio or fees a participant might pay by actually electing to invest in investments held in DFEs. This issue could be corrected by including the fee elements from the 404(a)(5) in Schedule H for these types of investments. To be clear, Morningstar applauds the Agencies for the new fee disclosure breakouts for DFEs, and believes the changes to the way DFE administrative fees are reported will also enhance transparency. But we believe this data should be supplemented by the information in the 404(a)(5) disclosure.

The proposal also partially addresses another key problem with the current disclosure: Users of the form can only learn about undifferentiated direct investments and cannot make a reasonable assessment of the plan’s investments in DFEs. However, we think that the proposed snapshot of these investments may not provide sufficient insight into the plans because many of these direct investments are target-date funds, and managers intend to adjust their asset allocations significantly over time. Indeed, in our database of collective investments, we identify more than half of them as pursuing a target-date strategy. While the Department of Labor has not yet released final guidance on how plans should disclose the attributes of target date funds on their 404(a)(5) disclosures, giving the Form 5500 room to accommodate these attributes when they are finalized would help Form 5500 users aggregate and compare collective investments in target date strategies across plans.

Regarding annuity products, the information disclosed under 404(a)(5) would supplement the information in Schedule A and on Schedule 4i under the proposal. Using annuity product identifications from 4i, data aggregators could capture some additional information about the annuities offered in some cases, and we support including this data on the schedule. The 404(a)(5) disclosures would further allow data aggregators to see what types of in-plan annuities are being offered, the pricing factors, and the fees. However, unlike other data elements on the 404(a)(5) disclosures such as expense ratios, the narrative structure can make it harder to compare plans with each other. A further enhancement would be to require plans to indicate whether each product is a variable, deferred, or immediate annuity in a structured

format. The proposed additions to Schedule A add additional information on the extent to which plans hold variable annuities, but still provide an incomplete picture of a participant's options for selecting these products.

Morningstar tracks and aggregates financial data across the world on a variety of products. We have a long history of advocating for investor transparency in opaque parts of the capital markets. In our experience, most disclosures are moving to structured data formats, and this move is important for transparency. At the core of any research is high-quality, timely, and affordable data. If the agencies do not require structured elements of the 404(a)(5) disclosures for small plans, it may simply be too costly to aggregate and share this data with our clients, many of whom work with individual investors and plan participants. In terms of the burden to the plan sponsors, we believe that since they must collect and disclose this information anyway, adding it to the Form 5500 in a structured data format should not impose a large additional burden. Indeed, we have observed that the 404(a)(5) disclosures are not bespoke, but rather typically come in a handful of formats. To that end, requiring plans to convert this data into a standardized format on Schedule H, line 4i should not impose a large additional burden.

Collecting Additional Identifiers That Match With the SEC's Systems

We also applaud the Agencies for adding additional identifiers for investments, including requiring plans to list for each investment (if available) CUSIP identifiers, a Central Index Key (CIK), a Legal Entity Identifier (LEI), and the Federal Instrument Global Identifier (FIGI). However, these identifiers do not necessarily align with the SEC's identification schema, in the Electronic Data Gathering, Analysis, and Retrieval (EDGAR) system.

We would note that the CIK provides insufficient information for matching investments to the SEC's data, as it only indicates the issuer, and we believe that the department should require an SEC Contract ID. This would allow users of the Form 5500 to easily link the investment in their plan to the EDGAR system. In the absence of this data, there is no standard identifier of investments other than the CUSIP, which is a proprietary system owned by a private company. In addition, such an SEC Contract ID would be particularly helpful for variable-annuity contracts. Connecting to the SEC's dataset using the SEC Contract ID would grant both the SEC and the DOL access to a broader set of data. Accessing the SEC data also may reduce the overall reporting requirements for investment companies registered under the Investment Company Act of 1940.

Investment options such as collective investment trusts would not have SEC Contract IDs. We suggest instead that the agencies require reporting of information on these non-1940 Act products in a standard format. We would also suggest that if the Form 5500 is to require CUSIPs, the electronic collection system should use the built-in check digit to validate whether the data has been submitted correctly. This check digit indicates whether the CUSIP is valid or not, and allows for immediate validation of CUSIP data.

Despite these suggestions, we think many of the proposed changes in collecting data on plan investments and fees will greatly improve the Form 5500's usability. For example, adjusting the "Other" category of investments to add more granularity will improve plan transparency. Additionally, this change will position the Form 5500 for the future, as DC plans have been exploring alternative investments and may offer more investments in the future that fall into the "Other" category today.

Comments on Changes to Schedule C

Morningstar also applauds changes in Schedule C as we think aligning the Form 5500 with 408(b)(2) will greatly improve the Schedule C. In particular, Morningstar believes that the revisions will present a clear picture of revenue-sharing arrangements. At present, we are concerned that many share class fees are not "clean"—that is to say, it is difficult to ascertain what percentage of the management fee is actually used for management. We believe the proposed changes will add further transparency, and we would encourage the Agency to require investment providers to disclose revenue-sharing payments as such, rather than under names that make it difficult for data aggregators, much less plan participants, to understand what they are paying to whom, and for what services.

In terms of whether indirect compensation received by covered service providers should be disclosed on a dollar basis as is proposed for Schedule C, or on a formula basis as is required in 408(b)(2), we think both data points are useful but suggest an alternative approach that might lessen burden on plan sponsors and provide clear data. The total dollar compensation is a useful retrospective measure of compensation, whereas a formula for compensation is much more useful for predicting likely costs in the future. This is because formulas for compensation based on assets under management are generally paid on a daily basis. The total compensation is dependent on the percentage charged but it is also dependent on the sequence of returns.

We suggest an alternative approach: Align the Schedule C with the 408(b)(2) disclosures, and collect the formulas in a structured format while adding an additional data field—the average (dollar-weighted) daily balance on the fund or funds (from the completed plan year) on which the formula is applied. With this approach, the Form 5500 will provide enough data to look prospectively at likely future compensation using the compensation formula. Further, Form 5500 users can calculate a very close estimate of the amount paid in compensation for the plan year in dollars, by simply multiplying the average daily balance by the compensation formula.

Concluding Observations

The Agencies' proposed revisions will align the Form 5500 with today's retirement plan and regulatory environment. In addition, the proposed changes should greatly help researchers interested in the state of American retirement plans and retiree choices, as well as private-sector users of the data. Our suggestions for improvements would make it easier to aggregate

Form 5500 data, and we believe this would be a benefit to individual participants, who could place their plan's strengths or weaknesses in context with other plans and other retirement options.

We also wish to applaud the Agencies for some long overdue additions that could greatly aid researchers. In particular, we applaud the proposed inclusion of the default elective deferral percentage for automatically enrolled participants, the number of participants invested in default investment options, the matching formula for elective deferrals, and the number of participants contributing enough to reach the maximum.

Sincerely yours,

Aron Szapiro
Director of Policy Research
Morningstar, Inc.