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on behalf of
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Comments Presented to the
Committee on Education and Labor
Subcommittee on Health, Employment,
Labor, and Pensions
United States House of Representatives

401(k) Fair Disclosure for Retirement Security Act of 2009

April 22, 2009

Thank you, Mr. Chairman and members of the subcommittee. My name is Julian Onorato and I am the CEO of ExpertPlan, Inc. based in East Windsor, New Jersey. ExpertPlan was founded as a technology innovator in the administration of retirement programs. With continued investment in operating efficiencies and client service, ExpertPlan is a leader in the defined contribution market, providing retirement services for thousands of companies and organizations with billions of dollars in retirement assets.

I am here today on behalf of the Council of Independent 401(k) Recordkeepers (CIKR), the American Society of Pension Professionals & Actuaries (ASPPA), and the National Association of Independent Retirement Plan Advisors (NAIRPA) to testify on important issues relating to 401(k) plan fee disclosure addressed in Chairmen Miller and Andrews' legislation, the 401(k) Fair Disclosure for Retirement Security Act of 2009.

CIKR, ASPPA and NAIRPA strongly support the premise that plans and plan participants should be provided with all the information they need about fees and expenses in their 401(k) plans—in a form that is clear, uniform and useful—to make informed decisions about how to invest their retirement savings plan contributions. This information is critical to millions of Americans' ability to invest in a way that will maximize their retirement savings so that they can achieve adequate retirement income. Accordingly, CIKR, ASPPA and NAIRPA strongly support the 401(k) Fair Disclosure for Retirement Security Act of 2009.

CIKR, ASPPA and NAIRPA also believe that working Americans should not have their retirement assets exposed to conflicted investment advice where the adviser has a financial interest in what investment choices to recommend to the plan and participants. Instead, American workers should have access to independent investment advice provided by qualified advisers. This issue was addressed by this Committee at a hearing on March 24. CIKR, ASPPA and NAIRPA strongly support legislation recently introduced by Chairman Andrews that would promote the provision of independent advice to plans and participants.

CIKR is a national organization of 401(k) plan service providers. CIKR members are unique in that they are primarily in the business of providing retirement plan services as compared to larger financial services companies that primarily are in the business of selling investments and investment products. As a consequence, the independent members of CIKR, many of whom are small businesses, make available to plan sponsors and participants a wide variety of investment alternatives from various financial services companies without bias or inherent conflicts of interest. By focusing their businesses on efficient retirement plan operations and innovative plan sponsor and participant services, CIKR members are a significant and important segment of the retirement plan service provider marketplace. Collectively, the members of CIKR provide services to approximately 70,000 plans covering three million participants holding in excess of $130 billion in assets.

ASPPA is a national organization of more than 6,500 members who provide consulting and administrative services for qualified retirement plans covering millions of American workers. ASPPA members are retirement professionals of all disciplines, including consultants, investment professionals, administrators, actuaries, accountants and attorneys. Our large and broad-based membership gives ASPPA a unique insight into current practical applications of ERISA and qualified retirement plans, with a particular focus on the issues faced by small- to medium-sized employers. ASPPA's membership is diverse but united by a common dedication to the employer-sponsored retirement plan system.

NAIRPA is a national organization of firms, not affiliated with financial services companies, which provide independent investment advice to retirement plans and participants. NAIRPA's members are registered investment advisors whose fees for investment advisory services do not vary with the investment options selected by the plan or participants. In addition, NAIRPA members commit to disclosing expected fees in advance of an engagement, reporting fees annually thereafter and agreeing to serve as a plan fiduciary with respect to all plans for which it serves as a retirement plan advisor.

Background on 401(k) Plan Fee Disclosure

Legislation

CIKR, ASPPA and NAIRPA strongly support the House Education and Labor Committee's interest in examining issues relating to 401(k) fee disclosure and the impact of fees on a plan participant's ability to save adequately for retirement. We are particularly pleased with the reintroduction of the 401(k) Fair Disclosure for Retirement Security Act of 2009. This bill will shine much needed light on 401(k) fees.

We also are encouraged by the introduction of two other pieces of legislation by Congress on the fee disclosure issue. On February 9, 2009, Senators Tom Harkin (D-IA) and Herb Kohl (D-WI) reintroduced their 401(k) plan fees legislation, S. 401, the "Defined Contribution Fee Disclosure Act of 2009." In addition, H.R. 3765, the "Defined Contribution of Plan Fee Transparency Act," was introduced on October 4, 2007 and sponsored by House Ways and Means Committee Subcommittee on Select Revenue Measures Chairman Richard Neal (D-MA) and co-sponsored by Rep. John Larson (D-CT).

We support all three bills' even-handed application of new disclosure rules to all 401(k) plan service providers. Further, we also encourage you to strike the right balance between disclosure information appropriate for plan sponsors versus plan participants. To demonstrate how both of these goals can be accomplished, we have attached to these comments two sample fee disclosure forms for your consideration – one for plan fiduciaries and another for plan participants. Each is tailored to provide plan fiduciaries and plan participants with the different sets of information on fees that are needed to make informed decisions.

Department of Labor Regulations

The Department of Labor (DOL) has finalized one 401(k) fee disclosure project, a revised Form 5500, including a revised Schedule C, which was effective beginning on January 1, 2009.

In December 2007, DOL issued proposed regulations under ERISA §408(b)(2) which would have provided sweeping changes on what constitutes a reasonable contract or arrangement between service providers and plan fiduciaries. The proposed rules would have required enhanced disclosures for service providers to 401(k) plan fiduciaries. However, the proposed regulations would have required only an aggregate disclosure of compensation and fees from bundled service providers, with narrow exceptions, and would not have required a separate, uniform disclosure of the fees attributable to each part of the bundled service arrangement.

In July 2008, DOL also issued proposed regulations under ERISA §404(a) setting forth a set of new participant fee disclosure requirements. The proposed rules would have required the disclosure to plan participants and beneficiaries of identifying information, performance data, benchmarks and fee and expense information of plan investment options in a comparative chart format, plus additional information upon request. However, no information on investment fees actually incurred with respect to a participant's account would have to be disclosed. Further, administration charges embedded in investment-related fees would not have to be separately disclosed.

On January 20, Rahm Emanuel, assistant to President Obama and White House Chief of Staff, signed an order requiring the withdraw from the Office of the Federal Register (OFR) of all proposed or final regulations that had not been published in the Federal Register so that they could be reviewed and approved by a department or agency head. The proposed ERISA § 408(b)(2) and participant fee disclosure regulations were sent to the Office of Management and Budget (OMB) in final rule form for review and approval. However, the regulations had not yet been released by OMB or sent to the OFR as of January 20. Therefore, the regulations have been

stopped by the Emanuel order.

ASPPA and CIKR submitted comprehensive comment letters to the DOL on both the 408(b)(2) and participant fee disclosure proposed regulations.[1] In both of these comment letters, we made a number of significant recommendations to improve each of the disclosure regimes in order to ensure that understandable and meaningful disclosure is provided, and stressed the need for uniform disclosure requirements – among all types of service providers.

Plan Sponsor 401(k) Fee Disclosure – Need for Uniform Requirements

The 401(k) plan industry delivers investments and services to plan sponsors and their participants using two primary business models–commonly known as "bundled" and "unbundled." Generally, bundled providers are large financial services companies whose primary business is selling investments. They "bundle" their proprietary investment products with affiliate-provided plan services into a package that is sold to plan sponsors. By contrast, "unbundled," or independent, providers are primarily in the business of offering retirement plan services. They will couple such services with a "universe" of unaffiliated, non-proprietary, investment alternatives. Generally, the costs of the bundled and unbundled arrangements are comparable or even slightly less in the unbundled arrangement. Under current business practices, bundled providers disclose the cost of the investments to the plan sponsor but do not break out the cost of the administrative services. Unbundled providers, however, disclose both, since the costs are paid to different providers (*i.e.,* administrative costs paid to the independent provider and investment management costs paid to the managers of the unaffiliated investment alternatives).

Bundled and unbundled providers have different business models, but for any plan sponsor choosing a plan, the selection process is exactly the same. The plan sponsor deals with just one vendor, and one model is just as simple as the other.

Plan sponsors must follow prudent practices and procedures when they are evaluating service providers and investment options. This prudent evaluation should include an "apples to apples" comparison of services provided and the costs associated with those services. The only way to determine whether a fee for a service is reasonable is to compare it to a competitor's fee for that service.

The retirement security of employees is completely dependent upon the business owner's choice of retirement plan service providers. If the fees are unnecessarily high, the workers' retirement income will be severely impacted. It is imperative that the business owner have the best information to make the best choice.

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[1] We note that House Education and Labor Committee Chairman Miller, House Education and Labor Subcommittee Chairman Andrews, Senate HELP Committee Chairman Kennedy (D-MA), Special Aging Committee Chairman Herb Kohl (D-WI) and Senate HELP Committee Member Tom Harkin (D-IA) also submitted joint comment letters to the DOL on both the 408(b)(2) regulation and participant fee disclosure regulation. These comments expressed concerns about the DOL's approach to these disclosure initiatives and requested additional actions be taken to protect plan participant and beneficiaries.

While the DOL's proposed ERISA §408(b)(2) rules (relating to whether a contract or arrangement is reasonable between a service provider and plan fiduciary) *would* have required enhanced disclosures for service providers to 401(k) plan fiduciaries, the proposed regulation would have required only an aggregate disclosure of compensation and fees from bundled service providers, with narrow exceptions, and would not have required a separate, uniform disclosure of the fees attributable to each part of the bundled service arrangement. Although we appreciated the DOL's interest in addressing fee disclosure, we do not believe that any requirement that benefits a specific business model is in the best interests of plan sponsors and participants.

Without uniform disclosure, plan sponsors will have to choose between a single price business model and a fully disclosed business model that will not permit them to appropriately evaluate competing provider's services and fees. Knowing only the total cost will not allow plan sponsors to evaluate whether certain plan services are sensible and reasonably priced and whether certain service providers are being overpaid for the services they are rendering.

In addition, if the breakdown of fees is not disclosed, plan sponsors will not be able to evaluate the reasonableness of fees as participant account balances grow. Take a $1 million plan serviced by a bundled provider that is only required to disclose a total fee of 125 basis points, or $12,500. If that plan grows to $2 million, the fee doubles to $25,000, although the level of plan services and the costs of providing such services have generally remained the same.

The bundled providers want to be exempt from adhering to uniform disclosure rules and regulations. Simply put, they want to be able to tell plan sponsors that they can offer retirement plan services for free while independents are required to disclose the fees for the same services. Of course there is no "free lunch," and there is no such thing as a free 401(k) plan. In reality, the costs of these "free" plan services are being shifted to participants through the investment management fees charged on the proprietary investment alternatives, in many cases without their knowledge.

The uniform disclosure of fees is the only way that plan sponsors can effectively evaluate the retirement plan they will offer to their workers. To show it can be done, attached is a sample of how a uniform, plan sponsor disclosure would look. By breaking down plan fees into only three simple categories – investment management, recordkeeping and administration, and selling costs and advisory fees – we believe plan sponsors will have the information they need to satisfy their ERISA duties.

We commend Chairmen Miller and Andrews for the even-handed application of new disclosure rules to all 401(k) plan service providers in the 401(k) Fair Disclosure for Retirement Security Act of 2009.

Uniform disclosure of fees, as provided by the Miller-Andrews legislation, will allow plan sponsors to make informed decisions and satisfy their ERISA duties. The breakdown of fees required in the legislation also will allow plan sponsors to assess the reasonableness of fees by making "apples to apples" comparison of other providers and will allow fiduciaries to determine whether certain services are needed, leading to potentially even lower fees.

Plan Participant 401(k) Fee Disclosure – Need for Uniform and Understandable Requirements

The level of detail in the information needed by 401(k) plan participants differs considerably from that needed by plan fiduciaries. Plan participants need clear and complete information on the investment choices available to them through their 401(k) plan, and other factors that will affect their account balance. In particular, participants who self-direct their 401(k) investments must be able to view and understand the investment performance and fee information charged directly to their 401(k) accounts in order to evaluate the investments offered by the plan and decide whether they want to engage in certain plan transactions.

The disclosure of investment fee information is particularly important because of the significant impact these fees have on the adequacy of the participant's retirement savings. In this regard, studies have shown that costs related to the investments account for between roughly 87 percent and 99 percent of the total costs borne by participant accounts, depending on the number of participants and amount of assets in a plan.[2]

CIKR, ASPPA and NAIRPA urge that any new disclosure requirements to plan participants also be uniform, regardless of whether the service provider is bundled or unbundled. In July 2008, the DOL issued proposed regulations on participant fee disclosure that required the annual disclosure to plan participants and beneficiaries of identifying information, performance data, benchmarks and fee and expense information in a comparative chart format, plus additional information upon request. The proposed regulation further required an initial and annual explanation of fees and expenses for plan administrative services to plan participants and beneficiaries (disclosed on a percentage basis) *except* to the extent included in investment-related expenses. The effect of this exception would have been to highlight administrative costs for one business model (unbundled) over another (bundled), which would result in a disparity of treatment and confusion.

In most plans, the administrative costs of recordkeeping, reporting, disclosure and compliance are borne, at least to some extent, by the investments. For bundled providers, the entire administrative cost is generally covered by investment-related fees charged on proprietary investments. For an unbundled provider, however, those costs are often paid through revenue sharing received from unrelated investments, which, in many instances, is not sufficient to offset the entire cost. Accordingly, for unbundled providers, there would be a direct administrative charge assessed against participants' accounts.

In effect, the DOL's proposed requirement to disclose administrative expenses *except* to the extent included in investment-related expenses would have imposed an additional and burdensome disclosure requirement on unbundled service providers, whereas there would be no such disclosure in the case of a bundled service provider. This would be misleading to most plan participants. In only the unbundled case would participants see separate administrative costs charged against his or her account, while with bundled providers, participants would be given the impression there were no administrative costs at all as the administrative costs would be imbedded in the investment costs.

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[2] 2007 edition of the *401(k) Averages Book*, published by HR Investment Consultants.

Accordingly, CIKR, ASPPA and NAIRPA recommend that the disclosure of administrative and investment information be provided on a uniform basis in any legislation considered by Congress. We believe that administrative fee information provided on the same annualized basis as investment costs would provide participants a more complete picture of the total costs of the plan at a single time, regardless of the business model of a service provider.

It also is important to recognize that there is a cost to any disclosure, and that cost is most often borne by the plan participants themselves. To incur costs of disclosure of information that will not be relevant to most participants will unnecessarily depress the participants' ability to accumulate retirement savings within their 401(k) plans. Thus, appropriate disclosure must be cost-effective, too. The result of mandatory disclosure should be the provision of all the information the plan participant needs, and no more. To require otherwise would unjustifiably, through increased costs, reduce participants' retirement savings. Those participants who want to delve further into the mechanics and mathematics of the fees associated with their investment choices and other potential account fees should have the absolute right to request additional information—it should be readily available on a Web site, or upon participant request. This will take care of those participants who feel they need more detailed information. For the Committee's consideration, ASPPA, CIKR and NAIRPA have attached a sample fee menu to the testimony that we believe would contain, in a clear and simple format, all the information a plan participant would need to make informed decisions about his or her plan.

The 401(k) Fair Disclosure for Retirement Security Act of 2009 requires two participant disclosure requirements: a "before-the-fact" notice of investment options and a revised quarterly statement requirement. The notice of investment options requires specific information be provided with respect to each available investment option, such as the investment option's risk level. The notice also must include a plan fee comparison chart that includes a comparison of actual service and investment charges that will or could be assessed against the participant's account. The chart must set fees into four categories: (1) fees depending on a specific investment option selected by the participant (including expense ratio and investment-specific asset based fees); (2) fees assessed as a percentage of total assets; (3) administrative and transaction based fees; and (4) any other charges deducted not described in the first three categories. The legislation also would amend the existing quarterly benefit statement requirement to mandate inclusion of specific information attributable to each participant's account, including starting balances and investment earnings or losses.

We are very pleased that the disclosure requirements for plan participants in the 401(k) Fair Disclosure for Retirement Security Act of 2009 are uniform, regardless of whether the service provider is bundled or unbundled. This will provide participants with a complete picture of total costs and avoid confusion. We also commend Chairmen Miller and Andrews for the legislation's plan fee comparison chart requirement. This chart is similar to the sample participant fee menu that is attached to this testimony. It will provide participants with an easy to understand summary of fees which will allow them to make informed decisions about how to invest their retirement saving plan contributions. However, we ask the Committee to reconsider the level of detail required for participants. It is important that participant disclosures be concise, meaningful and readily understandable – especially, since any new disclosure requirements will carry costs for participant disclosures. We also ask that the Committee consider defining "small plan", for purposes of permitting annual statements, as "fewer than 100" participants and

beneficiaries, as in H.R. 3185 passed by the Committee in the last Congress. Many small employers with more than 25 participants are struggling in the current economy, and the additional cost of more frequent reporting may discourage them from maintaining the company's 401(k) program.

Independent Investment Advice

DOL Investment Advice Regulations

ERISA and the Internal Revenue Code generally prohibit plan fiduciaries from rendering any investment advice to plan participants and beneficiaries that would result in the payment of additional fees to the fiduciaries or their affiliates. The Pension Protection Act of 2006 (PPA) §601 provided a statutory prohibited transaction exemption to the rule [codified at ERISA §§ 408(b)(14) and 408(g) and IRC §§ 4975(d)(17) and 4975(f)(8)] for certain transactions that may occur in connection with the provision of "eligible investment advice" by a "fiduciary adviser," subject to specific requirements. In particular, the final PPA investment advice provision allowed two specific permissible investment advice exceptions: (1) certain "fee-leveling" arrangements; or (2) certified computer model arrangements.

On August 22, 2008, the Department of Labor (DOL) issued proposed investment advice regulations interpreting PPA §601. On the same date, the DOL issued a separate prohibited transaction class exemption (Class Exemption) that provided relief for certain transactions that went beyond the scope of relief contemplated in the statutory language. DOL issued final investment advice regulations (Final Regulation) on January 21, 2009, that incorporated the separate Class Exemption into the Final Regulation. However, the status of these regulations is unclear at this point. In response to Rahm Emanuel's memorandum directing Agency Heads to consider extending for 60 days the effective date of regulations that had been published in the Federal Register but not yet taken effect, on February 4, 2009 the DOL proposed extending the effective date for the investment advice rules from March 23 until May 22, 2009 to allow the public to comment on whether the rules raise significant policy and legal issues. ASPPA and CIKR submitted comments in support of the extended effective date due to the uncertainty surrounding the final disposition of the regulations. On March 19, the DOL issued a final rule delaying the effective date to May 22.

The Final Regulation's interpretation of the statutory exemption in PPA will make it more likely that participants and beneficiaries may obtain assistance in diversifying investments and appropriately reflecting their own risk tolerances and investment horizons in asset allocations. However, the portion of the Final Regulation which implements the non-statutory Class Exemption (*i.e.,* the portion that does not relate to the statutory exemption from the prohibited transaction rule enacted in PPA) may expose participants and beneficiaries to conflicted investment advice without sufficient protection from the effects of an adviser's conflicts of interest. Furthermore, this exemption is contrary to Congressional intent.

Accordingly, ASPPA, CIKR and NAIRPA recommend that the DOL withdraw the Class Exemption portion of the Final Regulation. The enactment of ERISA §§ 408(b)(14) and 408(g) reflect Congressional desire to provide very limited relief for providing conflicted investment

advice. The Final Regulation expands this relief in a manner that does not provide adequate protection to participants and beneficiaries.

Independent Investment Advice Legislation

With the growth of participant-directed individual account plans, the importance of investment advice to participants and beneficiaries of retirement plans has become increasingly clear. The majority of Americans are not experts on how to appropriately invest their retirement savings. However, due to the shift from defined benefit to defined contribution plans, many Americans are required to do just that.

CIKR, ASPPA and NAIRPA believe that working Americans are best served by independent investment advice provided by qualified advisers, not conflicted investment advice where the adviser has a financial interest in what investment choices to recommend. We believe that participants' rates of return are better when served by an independent adviser. We commend Chairmen Andrews for his recent legislation promoting independent advice for retirement plans and participants.

Summary

The retirement system in our country is the best in the world, and competition has fostered innovations in investments and service delivery. However, important changes are still needed to ensure that the retirement system in America remains robust and effective into the future. By supporting plan sponsors through uniform disclosure of fees and services and by encouraging plan sponsors to provide independent investment advice to participants, American workers will have a better chance at building retirement assets and living the American dream.

CIKR, ASPPA and NAIRPA applaud the House Education and Labor Committee's leadership in exploring issues related to 401(k) plan fee disclosure and independent investment advice and in introducing the 401(k) Fair Disclosure for Retirement Security Act of 2009. The Committee's consistent focus on retirement issues over the years has advanced improvements in the employer-sponsored pension system and led to an increased concern about the retirement security of our nation's workers. CIKR, ASPPA and NAIRPA look forward to working with Congress and the Administration on these important issues.

Attachments: Sample fee disclosure form (plan sponsors)
Sample fee menu (plan participants)