AMERICAN BENEFITS
COUNCIL

TESTIMONY OF
ROBERT G. CHAMBERS

ON BEHALF OF

AMERICAN BENEFITS COUNCIL

BEFORE THE

EMPLOYEE BENEFITS SECURITY ADMINISTRATION,
U.S. DEPARTMENT OF LABOR

IN THE HEARING ON

REASONABLE CONTRACTS OR ARRANGEMENTS UNDER
SECTION 408(b)(2) – FEE DISCLOSURE

MONDAY, MARCH 31, 2008

Good morning. My name is Robert Chambers and today I am a partner in the Charlotte, North Carolina office of the law firm of Helms Mulliss & Wicker. Tomorrow, I will be a partner of McGuireWoods, with whom Helms Mulliss is merging later today. I have advised clients with respect to 401(k) plan issues since section 401(k) was added to the Internal Revenue Code in 1978. I am also the past chair of the board of the American Benefits Council on whose behalf I am testifying today.

The Council appreciates the opportunity to present testimony with respect to the disclosure of 401(k) plan fees. Our goal is the creation and maintenance of an effective and fair employee benefits system that functions in a transparent manner and provides meaningful benefits at a fair price – in terms of both fees and other expenses. In this regard, we commend the Department of Labor for its efforts to enhance transparency, including the issuance of the proposed Section 408(b)(2) regulation. We understand that this was a difficult task.

However, as you will hear over the next two days, considerably more work is still required. We have many, many suggestions for improving the regulation, but I limited the list to those dealing with the scope of the regulation, fiduciary safe harbors, the treatment of employer-paid services, conflicts of interest, gifts and the regulatory effective date.

Scope of the Regulation

As drafted, the proposed regulation would apply broadly to defined contribution plans, defined benefit plans, and health and welfare plans. We urge you to finalize the proposed regulations in three separate tranches or components - - first, disclosure for defined contribution plans; second, for defined benefit plans; and finally for health and welfare plans.

Our reasons for this request are as follows.

- Each component will require a massive and time-consuming enormous negotiated undertaking.
- Each type of plan is sold and serviced very differently and their fee structures are quite dissimilar.
- Each type of plan has distinctive legal structures.
- Any attempt to bring all three types of plans into compliance at the same time, especially in the breakneck fashion contemplated in the proposed regulations, will fail.
- The publicity and public policy discussions regarding the fee issues over the last couple of years have focused on the defined contribution plan arena so that it would be most appropriate to start there.

Interaction with Section 4975 of the Internal Revenue Code

The proposed regulation is silent on whether it applies to arrangements that are covered by the prohibited transaction rules of section 4975 of the Internal Revenue Code, but not by ERISA. This broad sector includes tax-qualified retirement plans that are exempt from ERISA because they cover only non-employee business owners, IRAs, HSAs, and Coverdell education savings accounts.

The Council strongly recommends that the Department clarify in the final regulations that these plans are not subject to the disclosure requirements. There is no plan fiduciary involved in these arrangements; to the contrary, individuals understand that they are acting in their own stead in determining which service providers to engage and what investment decisions to make. In this sense, IRA owners and other individual arrangement owners are far more like plan participants than plan fiduciaries. It would be neither appropriate nor sensible to impose the "service provider-to-plan" disclosure requirements on these non-ERISA arrangements.

Fiduciary Safe Harbor and Correction Mechanism

The Council greatly appreciates the "innocent" plan fiduciary class exemption that has been proposed in connection with the proposed regulation. The proposed class exemption, however, only provides protection from prohibited transaction consequences. The final regulation should also provide that these disclosures serve as an adequate factual predicate for a plan fiduciary in fulfilling its duty to understand any covered service arrangement. Of course, the fiduciary would still have to evaluate the quality of the services and the reasonableness of the cost.

The proposed regulation also implies that any violation of the requirements, no matter how minor, will result in a prohibited transaction and excise tax. This structure would benefit greatly from a correction mechanism that provides a means of dealing with reasonable errors without draconian penalties.

In addition, there will be times when a bundled service provider is unable, despite diligent efforts, to obtain accurate information needed for disclosure from the other parties to its bundle. We recommend that the Department create a class prohibited transaction exemption for such situations similar to the prohibited transaction exemption provided for plan fiduciaries that are unable to obtain necessary information from their service providers.

Employer Payments

The proposed regulation appears to provide that its disclosure requirements apply not only where a plan pays for services, but also where the employer that sponsors the plan pays for services out of its general assets. ERISA regulates only the amount that a plan pays for services. It does not regulate the amount that the plan sponsor directly pays for services. For these reasons, the Council strongly recommends clarifying that the proposed regulation does not apply where a plan service is paid for entirely out of the plan sponsor's general assets.

The Council appreciates that there are situations where the plan has the legal obligation to pay for plan expenses, except to the extent paid by the employer. The Council believes that the proposed regulation should not apply to the extent an employer commits contractually to be responsible for specified plan fees.

Conflicts of Interest

We are puzzled by two aspects of the proposed requirements to disclose conflicts of interest.

The first relates to a service provider's ability to affect its own fees. We understand that, where a service provider uses its powers in a discretionary manner to affect its own compensation, the service provider is functioning as a fiduciary and has committed a prohibited transaction. If this is correct, what must be disclosed under this rule? Only prohibited transactions? Or is the proposed regulation intended to implicitly overrule the Department's prior position that a service provider's ability to affect its own compensation is a prohibited transaction? We very strongly doubt this was intended, but we are left puzzled as to the actual intent. Seeing no purpose for this disclosure requirement, we recommend that it be deleted.

The requirement to disclose conflicts of interest is also puzzling. A conflict of interest can only arise where a service provider is acting as a fiduciary in providing a service, such as advice, with respect to which the service provider could be seen to have divided loyalties or interests that are contrary to the plan's interests. In such cases, the existence of a conflict of interest generally gives rise to a prohibited transaction. Where the service provider is not acting as a fiduciary, the service provider is simply selling a service in an arm's length transaction; no fiduciary duty of loyalty to the plan exists and, accordingly, no conflict of interest can exist. In this context, what must be disclosed under the proposed regulation? Only prohibited transactions for which there is no exemption?

We strongly support full disclosure of fees. And we strongly support enforcement of the prohibited transaction laws generally banning conflicts of interest. But the

regulatory disclosure rules I have just described serve neither purpose and should be deleted.

Gifts

While the Council agrees with the Department that plan fiduciaries should be made aware of excessive gift giving, we request two clarifications to the rules in the proposed regulations:

- First, the disclosure rules should be appropriately targeted so that disclosure is only required when there is a clear and direct relationship between the "gifts" and the plan.
- Second, the final regulations should include a de minimis concept, such as the $50 threshold in the Form 5500 instructions, to avoid a problem with logo-ed coffee cups and occasional sandwiches.

Effective Date

One of the most important issues for Council members is the proposed effective date of 90 days after publication of final regulations. Implementation of the final regulations will require immense effort by plan fiduciaries and service providers and very little of this work can be done in advance of the issuance of the final regulations. The 90-day time period is simply not sufficient for service providers because the rule, as proposed, would require significant modifications to computer systems, the training of operational and administrative staff, the preparation of new communication and administrative materials for plan fiduciaries, as well as the development of actual disclosure documents. This work is in addition to the modification and renegotiation of agreements with plan fiduciaries and other service providers.

The Council recommends that the final regulation be generally effective for new service contracts and material modifications of existing service contracts entered into on or after the first day of the year beginning at least 12 months following publication of final regulations.

Notwithstanding our recommendation, if the Department requires an earlier effective date, we strongly recommend a delay in the effective date for outstanding contracts that have not been materially modified. Any revisions to outstanding contracts will be an enormous undertaking, and it would be in everyone's best interest if there is time to facilitate an orderly transition.

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We very much appreciate this opportunity to present our views, and I would be happy to answer any questions.