STATEMENT FOR THE RECORD

SUBMITTED BY

AMERICAN BENEFITS COUNCIL
AND
AMERICAN COUNCIL OF LIFE INSURERS
AND
INVESTMENT COMPANY INSTITUTE

TO THE

U.S. HOUSE OF REPRESENTATIVES
EDUCATION AND LABOR COMMITTEE

FOR THE HEARING

on

H.R. 3185, THE 401(k) FAIR DISCLOSURE FOR RETIREMENT SECURITY ACT OF 2007

THURSDAY, OCTOBER 4, 2007

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Introduction

The role of section 401(k) plans in providing retirement security has grown tremendously over the last 25 years and is continuing to grow. In that light, legislative and regulatory actions with respect to such plans similarly take on an increased importance. Applicable legislation and regulations should ensure that these plans function in such a way as to help participants achieve retirement security. At the same time, we all must bear in mind that unnecessary burdens and cost imposed on these plans will slow their growth and reduce participants' benefits, thus undermining the very purpose of the plans.

It is in this spirit that the American Benefits Council (the "Council"), the American Council of Life Insurers ("ACLI"), and the Investment Company Institute ("ICI") submit this statement with respect to H.R. 3185, the 401(k) Fair Disclosure for Retirement Security Act of 2007.

The Council is a public policy organization representing principally Fortune 500 companies and other organizations that assist employers of all sizes in providing benefits to employees. Collectively, the Council's members either sponsor directly or provide services to retirement and health plans that cover more than 100 million Americans.

The ACLI represents 373 member companies accounting for 93 percent of the life insurance industry's total assets in the United States. Life insurers are among the country's leaders in providing retirement security to American workers, providing a wide variety of group annuities and other products, both to achieve competitive returns while retirement savings are accumulating and to provide guaranteed income past retirement.

ICI is the national association of U.S. investment companies, which manage about half of 401(k) and IRA assets. ICI advocates policies to make retirement savings more effective and secure.

Legislative and Regulatory Processes

At the outset, we want to address the legislative and regulatory processes with respect to plan fees. Chairman Miller has introduced H.R. 3185, which addresses the disclosure of plan fees by a service provider to a plan administrator, as well as the disclosure of plan fees by a plan administrator to participants. Other Committees and Members have also indicated interest in exploring the issues related to disclosure of plan fees. In addition, the Department of Labor has been working on regulatory initiatives with respect to plan fees. The Department's initiatives address three issues: the same two issues addressed by Chairman Miller's bill plus plans' obligations to report plan fees to the Department and the Internal Revenue Service on the annual Form 5500.

We have been very active participants in the legislative and regulatory processes. For example, we have participated with other trade groups in providing extensive input to the Department on their initiatives.

The Department is nearing completion of the Form 5500 project. The Department will likely, in the next month or two, issue proposed regulations relating to disclosure of plan fees by service providers to plan fiduciaries. We understand that the Department intends to issue proposed regulations on disclosures to plan participants in late 2007 or early 2008.

We support improvement to the rules regarding plan fee disclosure. Effective plan fee disclosure to participants can enable them to understand their options and choose the investments best suited to their circumstances. Disclosure to plan fiduciaries equips fiduciaries to negotiate and shop for the best services at reasonable prices. In addition, clarity with respect to both sets of rules can provide plan fiduciaries with a means of helping their participants without incurring potential liability.

In the effort to improve the fee disclosure rules, we believe that it is very important that the legislative and regulatory processes be coordinated. For example, it would be very harmful for the system for one set of rules to apply for a year or two, only to be supplanted by a different set of rules. The additional programming and data collection costs caused by such a scenario would be enormous, not to mention the resulting confusion among participants and plan fiduciaries. Such cost would, of necessity, be absorbed by plan participants or

possibly to some extent by plan sponsors. Plan sponsors could react by reducing benefits and possibly even eliminating or failing to adopt plans; plan participants would simply receive smaller benefits, which would be very unfortunate.

Accordingly, we urge both Congress and the Department to consider how best to coordinate their efforts to avoid very adverse consequences.

Plan Fee Issues

We welcome this opportunity to share our views on H.R. 3185. We very much appreciate the open manner in which Chairman Miller has invited input on his bill.

We present our views in the context of a list of principles that we believe should guide the development of plan fee disclosure rules. This is not by any means a comprehensive list; we would, of course, be very pleased to work with the Committee on additional important issues related to plan fee disclosure.

Disclosure to Plan Participants

At the outset, it is critical to emphasize that the disclosure rules should take into account the sharply different circumstances of participants and plan fiduciaries. Participants need clear, simple, short disclosures that effectively communicate the key points that they need to know to decide whether to participate and, if so, how to invest. Excessive detail can prevent employees from reading or understanding the disclosure and can also serve to obscure key points. Plan fiduciaries need more detailed information since it is their duty to understand fully the options available and to make prudent choices on behalf of all of their participants.

We support improved disclosure of plan fees to participants (and improved disclosure to plan fiduciaries, as discussed below). As noted, participants need disclosures that are simple and concise. At the same time, however, participants need to understand the fees they are paying within the context of the investment and other services they are receiving. This means that participants must recognize that fees are only one factor to consider in choosing an investment option. Fee disclosure must not be elevated in a manner that discourages plan participants from considering potential or expected investment returns, their projected retirement date, their risk tolerance, and other factors when making investment decisions, as well as decisions regarding participation in, contributions to, and distributions from the plan.

In this context, we offer the following principles that we believe should guide plan fee disclosure rules with respect to participants. In connection with each principle, we discuss briefly our concerns with H.R. 3185.

- **The disclosure needs to be short, simple, and easy to understand.** As noted, H.R. 3185 requires extensive fee disclosure. We believe that participants will be far more likely to read and use information that is shorter and simpler. One possible solution could be to require affirmative delivery of basic fee information and make more comprehensive fee information available on request.

- **Disclosure should include key information important to participants, generally including, for example, the investment objectives, risk level, fees, and historical returns of investment options. Undue emphasis on fees will only mislead participants by elevating fees above other equally or more important factors.** We are concerned that the volume of fee information required by H.R. 3185 outstrips the volume of other information, such as information regarding investment objectives, historical return, and risk level. This over-emphasis on fees could cause participants to make imprudent choices or possibly could cause them not to participate in the plan. Again, one possible solution could be to require affirmative delivery of basic fee information and make more comprehensive fee information available on request.

- **Reform of existing rules regarding electronic communication is needed to facilitate less expensive, more efficient forms of communication, including the use of internet and intranet postings. Consideration should be given to adopting rules at least as workable as the Internal Revenue Service's rules regarding electronic communication. Such rules ensure that electronic communications are only used with respect to participants who can access such communications; at the same time, the Service's rules are also generally workable for plans.** H.R. 3185 does not address electronic communication. Without the effective ability to use electronic communication, compliance with extensive new disclosure rules would be unreasonably costly and burdensome.

- **Participant-level disclosure rules should apply to all participant-directed plans not just 404(c) plans.** H.R. 3185 applies the disclosure rules to all participant-directed plans.

- **Fee information should be provided upon enrollment and updated annually.** H.R. 3185 is generally consistent with this principle. However, on a related note, it is critical that the annual benefit statement required by

H.R. 3185 be coordinated with the existing benefit statement requirements.

- **Fee information should be disclosed in the manner in which fees are charged. Artificial division of a single fee into components that are not available separately is costly and serves no purpose.** This issue applies to disclosure both to participants and to plan fiduciaries. Because it applies more acutely in the latter context, it is discussed below.

Where disclosure of exact dollar amounts would be costly, the use of estimates or examples based on prior year data should be permitted. H.R. 3185 can be read to require the exact dollar amount of fees to be determined for plans and for participants. This could be enormously costly. For example, for participants moving in and out of investment options all year, determining the precise dollar amount of fees charged for the year would require tremendous work as well as new recordkeeping systems. Very helpful fee information can be conveyed efficiently through the disclosure of expense ratios and reasonable estimates; the cost of turning those estimates into precise numbers would be very high and clearly not justified by the marginal difference between a reasonable estimate and the exact number.

- **Plan fiduciaries should retain flexibility to determine the format for disclosure based on the nature, expectations, and other attributes of their workforce.** H.R. 3185 generally does not require a specific format for disclosure.

- **The rules must be flexible enough to accommodate the full range of possible investment options.** H.R. 3185 establishes a very detailed disclosure regime that will not be able to cover all the products that are or may be used in the 401(k) plan market. While it seeks to set out specific disclosure elements for many investment products used in 401(k) plans today, the bill's framework does not easily accommodate certain other products, such as those providing a guaranteed rate of return based on the general assets of the provider. The framework also may be inadequate or inappropriate to address new types of products that may develop. We would be pleased to continue working with this Committee on how to address these issues.

Disclosure by Service Provider to Plan Fiduciary

We support improved disclosure of plan fees by service providers to plan fiduciaries. Plan fiduciaries need fee information in order to negotiate and shop effectively for services. In this regard, we offer the following guiding principles and related comments on H.R. 3185.

- **Fee information should be disclosed in the manner in which fees are charged. Artificial division of a single "bundled" fee into components that are not available separately serves no purpose. Service providers should be required to disclose what services are included in the "bundle" and what services can be purchased separately by the plan fiduciary.** H.R. 3185 can be read to require "unbundling the bundle", i.e., to require that a service provider ascribe separate fees to services that are not sold separately by the service provider. This is not meaningful information. It is burdensome and costly to produce; it has no significance since the services cannot be purchased separately from the service provider; and accordingly, it would not further fiduciaries' understanding of their options.

  Plan fiduciaries can reasonably make the decision whether to purchase services on a bundled or unbundled basis. Some fiduciaries believe, for example, that bundling provides economies of scale and facilitates efficient shopping for service providers, especially with respect to plans maintained by small employers. In some circumstances, it may be easier and more efficient to compare service providers that provide bundled services than to construct a full array of plan services from multiple vendors and to try to compare services from such vendors that are significantly different in scope.

  A plan fiduciary purchasing services on a bundled basis retains the duty to determine if (1) the bundled package of services is appropriate for the plan, and (2) the bundled price is reasonable, both initially and over time. This will require the plan fiduciary to monitor, for example, whether any asset-based fees continue to be reasonable, especially with respect to services that do not vary based on the size of the plan assets. Again, for some fiduciaries, those monitoring tasks may be simpler in the bundled context than where there are multiple providers with respect to a single plan.

- **Where disclosure of exact dollar amounts would be costly, the disclosure of fee formulas should be permitted.** As in the case of participant disclosure, disclosure of exact fee dollar amounts to plan fiduciaries could be extremely expensive in circumstances where fees are based on a percentage of assets. Plan fiduciaries only need the fee formula (such as the basis points charged); that gives them all the tools they need to evaluate the cost of the service. The high cost of calculating exact dollar amounts clearly outstrips the value of such exactitude.

- **Disclosure of revenue sharing received by plan service providers from third parties should be required. Disclosure of the affiliation between two or more service providers should also be disclosed. However, payments from one service provider to another affiliated service provider are not revenue sharing and should not be required to be disclosed.** H.R. 3185 can be read to require payments among affiliates to be disclosed. Affiliates are part of one economic unit, so that any explicit payments between them may not reflect an arm's length transaction and thus may have little or no significance. Moreover, financial relationships between affiliates can be complex, including numerous non-market transactions, such as the exchange of services without any charges; in this context, calculating the value of "revenue sharing" would require identifying and valuing all of these non-market transactions and would thus be enormously difficult and uncertain.

  In short, determining the value of intra-affiliated group payments would be costly and filled with speculation and uncertainty. Also, in light of the relationship between the entities, such payments are not revenue sharing in a true sense. We look forward to working further with the Committee on this issue.

- **Fees paid by plan sponsors should not be subject to any of the disclosure rules. Where plan assets are not involved, ERISA's rules are not implicated.** H.R. 3185 should be clarified in this regard.

- **Fees charged by service providers to plans should be disclosed. Fees charged to service providers by their suppliers have no relevance to plans and should not be required to be disclosed.** H.R. 3185 can be read to require disclosure of a service provider's transactions with almost all of its suppliers, which could be a huge number. These suppliers have no contractual relationship to the plan, thus making the massive disclosure requirement meaningless for the plan.

<u>Investment Option Requirement</u>

H.R. 3185 requires one specific type of index fund to be offered under all participant-directed plans. This would set a dangerous precedent, as it would (1) substitute Congress' current judgment regarding investments for the judgment of plan fiduciaries who are familiar with their workforce and (2) establish an investment rule based on today's thinking that does not take into account future investment trends and principles. This provision could also send a signal to participants that this particular investment option is the best one, despite the fact that another option might better fit their circumstances.

We urge that this provision be deleted.

"Conflicts of Interest"

H.R. 3185 requires disclosure of conflicts of interest to both participants and plan fiduciaries. Conflicts of interest are prohibited by ERISA's prohibited transaction rules, so it is not clear which if any permitted practices must be disclosed under these rules. The disclosure rules in H.R. 3185 may simply be aimed at requiring disclosure that a service provider is selling its own products or the products of an affiliate or business partner. If so, it is very important that a different term - - other than "conflict of interest" - - be used. As long as a service provider is not acting as a fiduciary, selling its own products or those of an affiliate or business partner is simply selling, not a conflict of interest. Labeling such actions as a conflict of interest is technically incorrect and will create confusion for all parties, including participants who could be unnecessarily discouraged from participating in the plan.

Effective Date

Any revisions to the fee disclosure rules will require (1) interpretation and implementation by the Department of Labor, (2) extensive systems changes, and (3) development of effective communication methods. Accordingly, it is critical that legislation not be effective prior to plan years beginning at least 12 months after the publication of final regulations interpreting the legislation.