

**Statement of Matthew H. Scanlan, CFA**  
**Head of Americas Institutional Business, Barclays Global Investors, N.A.**  
**Before the Committee on Education and Labor,**  
**U.S. House of Representatives**  
**October 4, 2007**

On behalf of Barclays Global Investors (BGI), I appreciate the opportunity to testify today regarding H.R. 3185, the *401(k) Fair Disclosure for Retirement Security Act of 2007*. An increasing number of Americans rely on employer-sponsored defined contribution plans to help them accumulate the savings they will need for a secure retirement. But far too many 401(k) and other defined contribution (DC) plans fail to achieve their purpose, if they are meant to provide security in retirement for the workers who contribute to them. There are three main reasons for this: inadequate or no contributions into the plan; low investment returns with high fees; and lack of a distribution strategy to fund consumption in retirement. The technology for saving and investing today to receive a benefit far in the future is already in place, and is in use by well-managed defined benefit (DB) pension plans. We need to bring some of these practices into the DC marketplace, and the bill under discussion today would, if enacted, take an important step in this direction.

Executive Summary

Fees and expenses can over time significantly erode the amount of income available for a participant's retirement. Participants need clear information on fees and expenses in order to make informed selections from among the investment options provided in their plan. Participants, who are typically not experts in financial planning, would benefit most from summary categories rather than a long list of items which may confuse or discourage decision-making. Plan sponsors, however, require more and better information than is currently available. To fully evaluate potential investment options and service providers, and their appropriateness for the plan, sponsors must be given information which permits them to understand how each service provider is compensated, directly or indirectly. It is not enough for plan sponsors only to understand what fees and expenses are explicitly deducted from a participant's account, or paid from plan assets or by the sponsor itself.

Further, recordkeeping and other administrative expenses on one hand and asset management fees on the other must also be disclosed separately by service providers to plan sponsors: only then can sponsors determine that fees and expenses are reasonable, as required under the Employee Retirement Income Security Act (ERISA).

#### Background on BGI

BGI<sup>1</sup> was founded in 1971 as part of Wells Fargo Bank in San Francisco, California. Today, we are owned by Barclays PLC, one of the world's leading diversified financial services companies. We remain headquartered in San Francisco with approximately 1900 employees in California and elsewhere in the U.S. and 1800 worldwide serving the needs of our global clients. With approximately \$2 trillion in assets under management, BGI, together with its affiliates, is one of the world's largest institutional asset managers, and is the largest provider of structured investment strategies, such as index, tactical asset allocation and quantitative active strategies. BGI pioneered the first institutional index fund strategy in 1971, and has continued a tradition of financial innovation ever since—including the creation of the concept of a target date retirement (lifecycle) fund and the launch of the first lifecycle fund in the early 1990's.

Since its founding, BGI has remained true to a single global investment philosophy, which we call *Total Performance Management*. BGI manages *performance* through the core disciplines of *risk*, *return*, and *cost* management. The success of our investing methodology results from our focus on delivering superior investment returns over time while minimizing trading and other implementation costs and rigorously controlling investment and operational risks. It has been the foundation for the way we've managed money for over 30 years and we believed it has served our clients very well.

BGI's clients are "institutional", by which we mean defined benefit and defined contribution pension plans sponsored by corporations or public agencies, and endowments, foundations and other similar pools of capital. BGI's services to its clients are completely focused on investment management; we do not provide other

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<sup>1</sup> BGI includes Barclays Global Investors, N.A., and its worldwide asset management affiliates.

services, such as recordkeeping. Among those institutions we have been honored to serve is the Federal Thrift Savings Plan (TSP). BGI was appointed as the first external manager for the TSP in 1988, and we have successfully retained and grown this relationship in regular, highly competitive bidding processes since that time.

#### Elements of Disclosure Regime for Plan Sponsors

Plan sponsors need adequate information about investment options (and the fees and expenses associated with them) so that the plan sponsor can exercise its fiduciary responsibility to choose which investment options should be available under the plan. Plan sponsors also have the fiduciary obligation to choose other plan service providers and to understand the cost of those services. Today, the information the plan sponsor needs is sometimes difficult to obtain or difficult to compare. There are two reasons for this. First, there are different investment vehicles (mutual funds, insurance products, bank collective trusts, separate accounts) which have different structures, different compensation mechanisms and different terminology for what may be the same service. Second, it can be more difficult to evaluate fees and expenses when fees for investment management are bundled with fees for administrative and related services.

It is not enough for plan sponsors to understand what fees and expenses are explicitly deducted from a participant's account or paid directly from plan assets or by the plan sponsor from its own funds. To fully evaluate potential investment options and service providers, and their appropriateness for its plan, plan sponsors must understand how each service provider is compensated, both directly and indirectly. BGI supports legislative efforts to require service providers to provide specific disclosures, by fee category, so as to make plan sponsor's decision making less burdensome.

Defined contribution plan service arrangements generally fall into two principal categories. The arrangements may be "bundled", that is, record keeping combined with asset management services or "unbundled", where the plan sponsor selects its investment options separately from its record keeper and other service providers. In some cases, bundled providers limit investment choices solely to their proprietary

investment offerings, and in other cases there is the ability for the plan sponsor to choose investment options outside of the record keepers proprietary funds.

Bundled service arrangements may be appropriate for some plans, particularly smaller ones. This is only appropriate if the fee components of both recordkeeping and asset management are separately and clearly disclosed. Clear, comparable and fully disclosed information about these charges will allow the plan sponsor to more easily and adequately meet its fiduciary responsibility under ERISA to determine that the fees and expenses are reasonable.

We have observed practices by some bundled service providers to provide “free” (or extremely low cost) services, provided the plan sponsor elects to place specified proprietary investment options in its plan. Participants who invest in the options stipulated by the recordkeeper may in this instance be subsidizing recordkeeping for participants who choose other plan investment choices. We believe that recordkeeping and similar administrative charges should be disclosed separately from investment management fees so the plan sponsor may evaluate each of the services independently. It is worth noting that in our experience in the defined benefit market, asset management services and administrative services, such as trustee services, are generally disclosed separately.

We support the bill’s conflict of interest disclosure requirements, and urge that this provision be clarified to assure that plan sponsors receive information that is specific to the plan sponsor and the particular service provider. Many of the benefits of disclosure will be lost if generic boilerplate language is sufficient to be compliant. Further, conflicts disclosure should also involve disclosure of potential revenue that the service provider may receive from its ‘cross-sell’ activities (IRA rollovers, brokerage or insurance) with plan participants. Record keepers and potentially other service providers have unique access to information about individual plan participants—especially their termination or retirement date--and sometimes use this access to market other financial services to these individuals. For example, record keepers may suggest that retiring employees use their affiliates to roll their 401(k) balances into IRAs managed by another affiliate.

### Elements of a Disclosure Regime for Plan Participants

The goal of any disclosure framework should be to provide relevant information in a cost effective manner to enable the best possible decisions. The information which plan participants need when choosing an appropriate investment from amongst those investment options selected by their employer differs from that which plan sponsors need to use to determine which investment options to offer (and which service providers to retain).

The most fundamental decisions that plan participants need to make are whether, and at what level, to participate in the plan; which investment options to choose; whether and when to change their investment allocations; and when to take distributions from the plan. These decisions are critical to the future value of the account. Participants' decision making is influenced by many considerations including basic behavioral finance factors.

The bill requires plan sponsors/administrators to individually list every service fee assessed against the participant's account. We agree that participants should be informed about these fees and expenses, and provided information about the impact of these charges on their choice of investment. We believe, however, that the average participant might be better served with a summary of these charges, grouped into categories, with the additional detail available upon request or on the plan's website. These categories would be recordkeeping and similar administrative expenses and asset management fees, and if necessary a third category for any other fees or expenses assessed against their account.<sup>2</sup> Behavioral finance research shows that when confronted with too much information, or information that is not organized to be customer friendly, participants fail to participate or engage in decisions about their investment allocation.

Participant disclosures should provide a consistent, comparable measure of fee and expense information, and should allow plan participants to easily understand

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<sup>2</sup> Participant activity generated charges, such as loan fees, would be disclosed in annual statements or the summary plan description and if incurred, reflected in the participant's periodic statement.

investment performance after all fees and expenses paid by the participant, regardless of whether the fees and expenses are asset-based or per participant. In addition, again in a comparable format, these disclosures should include the investment objective and strategy, key investment risks and historical performance for each investment option.

While mutual fund prospectuses, whether standard or in simplified form, may be appropriate for retail investors who are choosing among a vast array of investment alternatives, the amount of information presented in such documents is likely to overwhelm and confuse plan participants. Further, the typical mutual fund prospectus does not contain all the fees and expenses which are charged to a participant's account and for this reason should not be the standard used for disclosure. We support the adoption by the Department of Labor of standardized "fund fact sheets" as the form of disclosure for plan participants. Standardization provides benefits for all: service providers will have clarity on what information, and in what form, they must provide to all of their clients; plan sponsors will have confidence that the disclosures are adequate and not subject to challenge; and employees, who are increasingly mobile, will be able to make more effective comparisons and gain from increasing familiarity with the information when they change employers.

There are a broad variety of investment types that can be offered to plan participants in 401(k) plans. These can be mutual funds, separately managed accounts, bank collective trusts, employer stock, stable value funds, annuities or other insurance products. For a variety of reasons, this broad range of investment types are subject to a variety of regulatory regimes. We know of no regulatory impediment, however, to providing comparable disclosure to participants across all such investment types, regardless of legal structure. In this regard it would be extremely helpful for the Securities and Exchange Commission to confirm that for registered investment options, such as mutual funds, that fund fact sheets are not prospectuses as that term is defined under the federal securities laws.<sup>3</sup> This will assist the industry to reach consensus on a standard, simplified disclosure format across all investment types.

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<sup>3</sup> See Section 2 (a) (10) of the Securities Act of 1933, 15 U.S.C. 77b (a) (10).

While transparency as to fees and expenses is important for plan participants, any disclosure document also needs to present this information in context, as too much focus on fees and expenses could promote a tendency among participants to opt for the lowest cost option, (most likely to be a money market fund or company stock) to the detriment of their retirement income. Failure to adequately diversify investments is one of the more common errors made by plan participants.

A number of plans provide multiple investment options within the same general strategy (for example, several large cap domestic equity funds). When a plan does so, behavioral finance research suggests that plan participants would also benefit if the alternatives within the same strategy were either ranked by cost or the least cost alternative were highlighted in some way.

The bill also proposes that all DC plans provide an investment option that is a market-based index fund meeting certain criteria and as prescribed by the Department of Labor. While we believe one of the advantages of ERISA is that it permits plan fiduciaries to make their own prudent decisions about what investments are appropriate for their beneficiaries, the Committee may wish to consider the approach taken by the Federal Employee Retirement Security Act of 1986 (FERSA) which established the Federal Thrift Savings Plan. As amended, FERSA includes six categories of investment options, with a focus on index strategies across the investment spectrum (equity and fixed income) as well as lifecycle funds. While many plan sponsors do provide passive investment options in their plans, this Committee should consider how to further encourage this trend.

### Conclusion

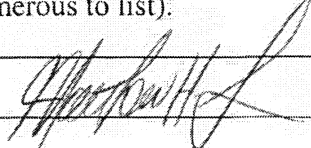
Achieving financial security in retirement is a significant challenge for most Americans. Currently, many DC plans have challenges with all three of the major components: the contribution, or savings, component; the investment performance component; and the retirement distribution component. By promoting such features as auto-enrollment and automatic contribution escalation, the Pension Protection Act of 2006 has already focused on the first challenge. By promoting more effective disclosure of fees and expenses to plan sponsors and plan participants, the *401(k) Fair Disclosure for Retirement Security Act of 2007* would improve the second component.

Transparency can be an important catalyst for making DC plans perform more like DB plans in the balance of costs and investment performance and thereby improving the future income of all retirees.



**Committee on Education and Labor**  
**Witness Disclosure Requirement - "Truth in Testimony"**  
**Required by House Rule XI, Clause 2(g)**

1. Your Name (Please Print): Matthew H. Scanlan		
2. Will you be representing a federal, State, or Local Government entity? (If the answer is yes please contact the Committee).	Yes	No <b>X</b>
3. Please list any federal grants or contracts (including subgrants or subcontracts) which <u>you</u> have received since October 1, 2004?  None		
4. Will you be representing an entity other than a government entity?	Yes <b>X</b>	No
5. Other than yourself, please list what entity or entities you are representing:  Barclays Global Investors, N.A., and its U.S. subsidiaries, Barclays Global Fund Advisors, Barclays Global Investors Services and Barclays Global Investors USA Inc.		
6. Please list any offices or elected positions held and/or briefly describe your representational capacity with each of the entities you listed in response to question 5:  Managing Director, Head of Americas Institutional Business, Barclays Global Investors, N.A.		
7. Please list any federal grants or contracts (including subgrants or subcontracts) received by the entities you listed in response to question 5 since October 1, 2004, including the source and amount of each grants or contract:  BGI provides asset management services to:  US Air Force NAF Employee Retirement Plan Trust Army Air Force Exchange Service Bureau of Naval Personnel Federal Employees Retirement System Federal Reserve Employee Benefits System National Railroad Retirement Investment Trust Navy Exchange Service Command Retirement Trust Pension Benefit Guaranty Corporation U.S. Army NAF Retirement Plan Trust  Fees are confidential as required by the federal entity.		
8. Are there parent organizations, subsidiaries, or partnerships to the entities you disclosed in response to question number 4 that you will not be representing? If so, please list:  Barclays Group PLC and its foreign and non BGI U.S. subsidiaries (too numerous to list).	Yes <b>X</b>	No

Signature: 

Date: 10/2/07

Please attach this sheet to your written testimony.