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February 14, 2008

The Honorable Brad Campbell  
Assistant Secretary  
Employee Benefits Security Administration  
US Department of Labor  
Washington, DC 20515

**Re: Proposed rules on "Reasonable Contract or Arrangement," Section 408(b)(2) and "Fee Disclosure and Proposed Class Exemption for Plan Fiduciaries When Plan Service Arrangements Fail to Comply with ERISA," Section 408(b)(2), issued by the Department on December 13, 2007**

Dear Assistant Secretary Campbell:

We appreciate the Department finally taking preliminary steps to ensure that employers and employees are fully knowledgeable about the costs and benefits of their retirement plans. But, we believe Department must go much further than these proposed regulations in order to achieve clear and understandable disclosure of fees and conflicts.

It is critical that retirement plans provide the best possible deals for all participants. Unfortunately, many 401(k)-style plans charge hidden fees that can cut deeply into workers' retirement savings.

At a hearing last year, the Government Accountability Office (GAO) told us that weak fee disclosure requirements under current law are putting American workers' retirement savings at risk. According to GAO, 80 percent of workers were not aware of the fees that were being taken out of their accounts. The negative consequences of these hidden fees can be significant. According to GAO, a 1 percentage point increase in fees could cut retirement income by almost 20 percent over 20 years.

Some fees may be reasonable and necessary. Yet without clear and complete information about what fees are being charged and why, employers and employees simply cannot make informed choices about the best investment options.

### **Summary of Comments:**

This issue is of the utmost importance to the estimated 50 million participants and beneficiaries who depend on employer sponsored plans for their retirement security. In light of more employers shifting into “do-it-yourself” retirement vehicles such as 401(k) plans, Department vigilance is essential to ensure that participants are offered investment options in their best interests and that they are fully knowledgeable of all of the costs of these investments.

We urge the Department to act promptly to more seriously monitor 401(k) plan operations. The Department should not only stop practices that endanger workers’ retirement security, but also fulfill its role as the leading agency protecting private sector retirement security by encouraging best practices.

### **Discussion:**

- 1. The Department needs to more fully consider the unique nature of participant-directed plans and focus its regulations on protecting participants who are neither informed nor protected by employer decision-making.**

The Department’s regulation seeks to provide a unified reporting rule for defined benefit pension plans, defined contribution plans, and welfare plans. The Department ignores the very real and significant difference between these types of plans. Because workers and retirees are particularly vulnerable and at risk under 401(k)-type plans, we urge the Department to separately consider and protect participants in these plans.

Defined benefit plans primarily rely on employer contributions and employers are directly liable to pay out promised benefits should the plan’s fees and expenses prove excessive. Therefore, employers have incentives to actively monitor and negotiate plan fees and expenses. In contrast, 401(k) plans primarily consist of employee contributions and employers may pass 100% of all plan costs onto employees. For this reason, even the most well-meaning of employers have less incentive to zealously monitor and negotiate the best fees and expenses on workers’ behalf.

Administrative and recordkeeping expenses are a key example. Such expenses should decline over time, but if included in a percent of assets fee, non-vigilant employers would “imprudently” increase participant costs and reduce their retirement security. The

Department needs to put its emphasis on the 401(k) contracting process to ensure that it has fully and fairly protected the individuals who actually pay all of the fees and whose retirement money is at risk.

**2. The Department must more fully exercise its authority to monitor pension plan operations and make that information widely available so that policymakers can monitor the adequacy of existing policies and practices.**

The Department needs better information on how employers, plan administrators and plan fiduciaries make decisions to invest workers' retirement monies either directly or through the investment options offered to them.

At least since the Enron scandal in 2001, the Department and the employer community have been on notice that there were significant failures by some employers to seriously carry out their statutory fiduciary obligation under the Employee Retirement Income Security Act (ERISA) to oversee workers' retirement monies "prudently" and "solely in the interest of participants and beneficiaries." The Department should annually survey employers and existing reporting requirements to analyze who is making investment decisions and their knowledge about such investments.

**3. The Department needs to more actively work with other federal and state agencies to monitor investment products that are marketed and sold to pension plans.**

The Department, the Securities and Exchange Commission, and other regulatory agencies have not fully exercised their obligation to act in the best interests of investors. The subprime mortgage crisis is the latest example of this failure.

Regulators knew that subprime mortgages were being consolidated into risky securities but took little or no action to warn investors. In 2005, the SEC surveyed pension consultants and found that over half had undisclosed conflicts of interest. The SEC privately reprimanded the firms, but took no action to alert employers or the public. The SEC referred many of these cases to the Department, but we know of no action by the Department to prosecute offending firms. Similarly, the Department and SEC jointly issued "Selecting and Monitoring Pension Consultants – Tips for Plan Fiduciaries," but have not surveyed the industry for compliance.

**4. The Department should regularly review the documents that are being provided to pension plans and participants to ensure that financial service firms are providing needed information in understandable terms.**

It is clear from research and surveys that employers and workers have widely different levels of knowledge about financial terms and products. As both the GAO and AARP found, 80 percent of workers do not know that they are paying any fees from their 401(k) account balances. In addition, the GAO also found that nearly 40 percent of workers born in 1990 will have no 401(k)-style savings at all and worker nearing retirement today will only be able to replace 22 percent of the income.

We urge the Department to act promptly to more seriously monitor 401(k) plan operations. The Department should not only stop practices that endanger workers' retirement security, but also fulfill its role as the leading agency protecting private sector retirement security by encouraging best practices.

With respect to the proposed regulations:

**Class Exemption for Fiduciaries Who Fail to Receive Required Disclosures.**

**Rather than excusing failures, the Department should update its guidance on fiduciary responsibility and provide model documents and explanations of key terms to pension plan officials.**

The Department is understandably concerned that pension plan fiduciaries may not always be able to insist that service providers disclose their fees and conflicts of interest. While the Department's Proposed Rule is focused on what is and is not a prohibited transaction under ERISA, the Department ignores the more important fiduciary responsibility requirements of ERISA.

If a pension plan fiduciary does not receive critical information on the terms of a contract or arrangement, then it is imprudent under the rules for that fiduciary to sign such a contract. Similarly, if the fiduciary does not fully understand the terms of a contract, then it also is imprudent for the fiduciary to sign the contract. Pension plan administrators have agreed to act in the best interests of workers and retirees and rather than creating exemptions to that responsibility, the Department should provide further rules to make that responsibility clear.

**Bundled Services.**

**The Department should consider a more comprehensive rule that fully assures that pension plan fiduciaries understand all of the components they seek to purchase from a bundled provider.**

The Department appears concerned that a significant portion of the retirement market is provided through service providers that offer a combination of services and often do not

break down the components of their charges, even when requested. The Department's focus on what is or is not reasonable compensation does not appear to be resolvable without the Department also providing updated guidance on the fiduciary responsibility rules. It is the plan fiduciary's responsibility to know what he or she is buying, to ask questions, to shop around for the best price, and ultimately to be certain that he/she is purchasing services that are in the interests of the participants and beneficiaries. Consequently, plan fiduciaries should be expected to be aware of the values of each

service they purchase as well as potential hidden incentives such as revenue sharing charges.

The proposed regulation states that: *“an investment of plan assets or the purchase of insurance is not, in and of itself, compensation to a service provider for purposes of this regulation. However, persons or entities that provide investment management, recordkeeping, participant communication, AND other services to the plan as a result of an investment of plan assets will be treated as providing services to the plan.”*

This needs to be clarified by the Department. If a plan fiduciary SOLELY contracts for investment services and all fees are assessed out of plan assets, then all the fees should be disclosed to the plan fiduciary. There is no reason that fees assessed for investment services not be disclosed, but fees for recordkeeping or participant communication are required to be disclosed.

There is no reason for this distinction if both services are assessed as a percent of plan assets. In the case of a 401(k) plan, this is especially egregious. Where every penny is an offset against workers' retirement accounts, (and the employer or plan may not be paying any portion of any expenses) such a regime exonerates employers, plan fiduciaries, and service providers and leaves workers and the Department unable to ensure that decisions are made *solely in the interest of participants*.

The Department's proposed rule does not address how pension plan fiduciaries should evaluate the cost of “in-house” services. Many large employers structure their employee benefit services within the company and the Department should address how such services shall be evaluated and monitored for “reasonableness” and fiduciary compliance.

### **Disclosure of Information.**

**The proposed rule must ensure that service providers provide all fee and expense information in understandable and prominently disclosed language.**

The Department's proposed rule would permit service providers to submit disclosure information in any manner and in multiple documents. The Department also says that these documents may be provided electronically and by reference and gives examples of

a mutual fund prospectus and SEC Form ADV. The Department states that it “expects that the service provider will clearly describe these additional materials and explain to the responsible plan fiduciary the information they contain.” This latter requirement must be included in the actual final regulatory language.

It is imperative that the plan fiduciary know where all of the relevant disclosures are and be provided them a reasonable period in advance of signing any contract. As the

Department well knows, even a mutual fund prospectus can be hundreds of pages long and the pertinent information not easily identifiable. Further, prospectuses can be for one or more “funds” and not for the specific plan and not all relevant fee information is included in mutual fund prospectuses. Additional critical information is in the “Schedule of Additional Information” that must be separately requested.

The SEC Form ADV has similar issues. The ADV form is not necessarily provided in advance and compensation information is not always specific and clear. The Department needs to make it clear that such documents may only be used if specific to the plan and if they include plan-specific compensation information. While it is reasonable to expect that not all fee or conflict of interest related information will be in one document, the service provider must clearly and prominently identify the location of all specific compensation and conflict of interest information. In all cases, disclosure must be in advance, prominent, clear and understandable. It seems hard to imagine a scenario in which a plan fiduciary could sign a contract if he/she has not received or understands the above required information.

The proposal also permits service providers to disclose compensation or fees in terms of a specific monetary amount, formula, percentage of plan assets, or per capita charge. The Department must make it clear that such disclosure must be clear and specific to the actual plan involved. As the Department knows, many service provider documents may apply to a general or specific fund, but not necessarily be specific to the plan. Also, many documents only refer to fees that “may” apply, but do not specify if the fees “do” apply.

The Department’s proposal would require that service providers that are providing a “bundle” of services disclose the aggregate direct compensation or fees, but not within services. Similarly, a bundled service provider must disclose total revenue sharing but not the allocation among affiliates or subcontractors. Presumably, the Department believes that a prudent fiduciary would seek this more detailed information. If the Department cannot state it in this proposed rule, then the Department should provide other guidance making clear that a prudent fiduciary, if presented with a total charge for a bundle of services, has the responsibility to determine the charges for individual services.

Finally, the proposed rule is silent on whether the information disclosed under this rule will be available to participants. In all employee benefit plans, and particularly in 401(k) plans, employees are the parties to whom this information is of the most need and importance. The Department should be clear in the final rule that all disclosure information should be available to participants and beneficiaries. The Department should specify how and under what conditions participants will be able to access fee disclosure information so that they can understand and monitor their expected benefits.

**Termination Penalties.**

**The Department needs to examine a variety of existing contracts for termination penalties and impose penalties on violations of its longstanding regulations.**

It is widely reported that some service providers -- primarily in the insurance industry -- include what are typically called "surrender charges" for either contract terminations or changes in investment options. These charges may be imposed against a plan or participant based on either party's actions. It is unclear that these charges currently are clearly disclosed and limited to the cost of any early contract termination. If so, this would be in violation of Department's existing regulations. The Department needs to examine existing practices as part of this regulatory agenda.

We appreciate the Department's consideration of these comments.

Sincerely,



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