

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

Testimony of Mercer E. Bullard

President and Founder
Fund Democracy, Inc.

and

Associate Professor of Law
University of Mississippi School of Law

before the

Subcommittee on Health, Employment, Labor, and Pensions

Committee on Education and Labor

U.S. House of Representatives

April 22, 2009

Chairman Andrews, Ranking Member Kline, members of the Subcommittee, thank you for the opportunity to appear before you to discuss the 401(k) Fair Disclosure for Retirement Security Act of 2009. It is an honor and a privilege to appear before the Subcommittee today.

I am the Founder and President of Fund Democracy, a nonprofit advocacy group for mutual fund shareholders, and an Associate Professor of Law at the University of Mississippi School of Law. I founded Fund Democracy in January 2000 to provide a voice and information source for mutual fund shareholders on operational and regulatory issues that affect their fund investments. Fund Democracy has attempted to achieve this objective in a number of ways, including filing petitions for hearings, submitting comment letters on rulemaking proposals, testifying on legislation, publishing articles, lobbying the financial press, and creating and maintaining an Internet web site for the posting of information. I also have served as an expert witness for plaintiffs and defendants in a variety of securities cases and am a senior adviser with financial planning firm Plancorp, Inc.

EXECUTIVE SUMMARY

The 401(k) Fair Disclosure for Retirement Security Act of 2009 (“401(k) Fee Disclosure Act” or “Act”) takes significant steps toward enhancing competition in the 401(k) marketplace and ensuring that plan beneficiaries will have the fee information they need to make informed investment decisions. The Act adheres to the fundamental principle that fee disclosure should be designed not for the self-directed, fee-sensitive investor, but rather to increase awareness of fees and their impact on investment returns among those retirement plan beneficiaries who are not fee-sensitive. The Act will ensure that services providers and plan sponsors must provide participants with the information they need, in a form they can understand, and at a time when it is useful to them in making and assessing their investment decisions. ***The Act is not just a giant leap forward in the 401(k) marketplace; it introduces reforms that are long overdue across the spectrum of financial services in America.***¹

The 401(k) Fee Disclosure Act’s principal means of accomplishing these goals are as follows:

- **Delivery Vehicles**: Rather than continuing to require participants to decipher a combination of mutual fund prospectuses, Form 5500s and account statements in order to understand the fees they are paying, the 401(k) Fee Disclosure Act requires disclosure of *all* fee information in both: (1) a plan summary that also includes essential non-fee information that beneficiaries need to evaluate the plan, and (2) the account statement in a way that directs fee-insensitive beneficiaries’ attention to the importance of fees.
- **Comprehensive Fee Disclosure**: Under current law, fees are disclosed piecemeal and are not comprehensive. In contrast, the 401(k) Fee Disclosure Act requires disclosure of all 401(k) fees, including: (1) asset-based investment option fees, (2) asset-based plan fees, (3) administrative and transaction-based fees, and (4) any other fees that may be deducted from participants’ accounts.

¹ My testimony is based, in part, on analysis that I developed with Barbara Roper, Director of Investor Protection, Consumer of Federation of America, in comments on prior legislation and rule proposals.

- Dollar Disclosure of Fees: The disclosure of fees in dollars rather than as a percentage of assets provides the most effective means of causing investors to consider the impact of fees on their 401(k) accounts. The 401(k) Fee Disclosure Act requires disclosure of the dollar amount of fees deducted from the account during each quarter, which will proactively direct participants' attention to the true cost of their 401(k) plans and further promote competition in the 401(k) industry.
- Comparative Fees: Comparative information provides the context that gives fees their meaning. The 401(k) Fee Disclosure Act requires the express disclosure of comparative fees for the first time anywhere in the retail financial services marketplace.
- Freedom from Active Management Risk: Many plan sponsors limit participants to actively managed investment options, thereby requiring them to pay higher fees and assume the risk of significant market underperformance. In view of widely understood and uncontroverted economic research, it is unclear how plan sponsors can force participants to assume active management risk consistent with their fiduciary duty to the plan. The 401(k) Fee Disclosure Act frees participants from the straightjacket of active management risk by requiring sponsors to offer at least one passively-managed debt or equity fund.
- Small Business Concerns: Operating a 401(k) plan can be a costly enterprise for small businesses. Any 401(k) reforms therefore must include measures to ensure that the benefits of the reforms are not lost because of the increased administrative costs that they may impose. The 401(k) Fee Disclosure Act includes specific provisions that address these concerns and ensure that investor protection measures will not have unintended consequences for small employers.

The 401(k) Fee Disclosure Act will effect dramatic, positive changes in the competitive environment in the 401(k) marketplace, but there are certain changes that could provide further benefits to 401(k) participants:

- Differential Compensation: Like other retail investors, 401(k) participants are victimized by sales abuses when service providers have financial incentives to recommend investment options that generate the highest fees for the providers, rather than the options that are in the best interests of the plan and its participants. The 401(k) Fee Disclosure Act should require full disclosure of such conflict of interest payments, if not prohibit them altogether.

- Comparative Fees: The Act requires comparisons of fee options within the plan, which will result in apples to oranges comparisons and distorted asset allocation decisions. The purpose of comparative fee information is to inform participants about what they could pay elsewhere for services and products that are comparable to those offered by the plan. The Act should be amended to require comparisons are between: investment options within common assets classes, passively and actively managed funds, and 401(k) and non-401(k) investment vehicles.
- Unlimited Exposure to Employer Stock: While the Act takes a major step forward in freeing participants from the active management risk that many sponsors force on them, it leaves unaddressed the risk of overinvestment in employer stock. There is no rational basis for granting tax deferral to 401(k) investments only to permit the gambling of 100 percent of a participant’s account on the stock of a single employer. The Act should limit investments in employer securities to 20 percent of the participant’s 401(k) balance.

TABLE OF CONTENTS

I.	INTRODUCTION	7
II.	BACKGROUND	8
	A. Importance of 401(k) Fees	8
	B. Judicial Repeal of ERISA’s Fiduciary Standard	9
III.	FEE-INSENSITIVE INVESTORS	10
IV.	DELIVERY VEHICLES	13
V.	FORM OF FEE DISCLOSURE	18
	A. Account Statement Fee Disclosure	18
	B. Plan Summary Fee Disclosure	20
	C. Fee Table	22
	D. Additional (Non-Expense-Ratio) Expenses	23
VI.	CONFLICTS OF INTEREST AND DIFFERENTIAL COMPENSATION	24
VII.	COMPARATIVE FEE INFORMATION	28
	A. Investment Option Fees	29
	B. Plan Fees	31
	C. Potential Conflicts of Interest	32
	D. Form of Comparative Fee Information	32

VIII.	ACTIVE MANAGEMENT RISK AND PASSIVELY MANAGED INVESTMENT OPTIONS	33
IX.	COST ISSUES	39
X.	CONCLUSION	41

I. INTRODUCTION

Fee disclosure for 401(k) plans has long been in need of improvement, and I applaud the Subcommittee for taking up this issue. Fee disclosure reform for 401(k) plans has the potential to bring about substantial reductions in overall plan expenses for beneficiaries and strengthen the foundation of Americans' financial security in retirement.² A primary goal of 401(k) regulation should be to ensure that beneficiaries keep as much of the performance of the markets as possible. Excessive investment expenses present one of the most significant impediments to the achievement of this goal. Fees paid by 401(k) beneficiaries directly reduce their investment returns and, as a result, their financial security in retirement. Of course, excessive regulatory compliance costs can also reduce investment returns. For that reason, fee disclosure reforms should be designed so that they generate a net benefit to 401(k) participants. Transparent, standardized fee disclosure can create substantial net benefits for 401(k) beneficiaries by raising fee awareness among beneficiaries and increasing competition among industry participants. ***The 401(k) Fair Disclosure for Retirement Security Act of 2009 ("401(k) Fee Disclosure Act" or "Act") takes significant steps toward enhancing competition in the 401(k) marketplace and ensuring that plan beneficiaries will have the fee information they need to make informed investment decisions.***³

² Although the focus of this hearing is 401(k) plans, my testimony generally applies to all types of participant-directed plans. In addition, my testimony often uses mutual funds as examples of 401(k) investment options because they are the most common type of 401(k) plan investment option, comprising more than 50 percent of 401(k) assets.

³ A similar bill has been proposed in the Senate. See *Defined Contribution Fee Disclosure Act of 2009*, S. 401 (Feb. 9, 2009) available at http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_bills&docid=f:s401is.txt.pdf.

II. BACKGROUND

A. Importance of 401(k) Fees. The importance of 401(k) plan fees needs no detailed elaboration here. As noted by the GAO, 401(k) plan fees “can significantly decrease retirement savings over time.”⁴ For example, the GAO estimates that paying an additional 1 percentage point in fees will reducing an account’s ending balance after 20 years by 17 percent.⁵ Mutual fund fees have a substantial impact on total 401(k) plan fees because the bulk of 401(k) plan assets are invested in mutual funds. As noted by the SEC, “[t]he focus on fund fees is important because they can have a dramatic impact on an investor's return.”⁶ The GAO’s and SEC’s observations regarding fees apply equally to other 401(k) investment vehicles.

The amount of fees charged by a 401(k) investment option within any particular investment category is arguably the strongest predictor of its investment performance.⁷ For example, researchers have found that mutual funds generally are no more likely, from one quarter to the next, to repeat top-quartile performance as they are to fall into the second, third or fourth tier. To the extent that a small minority of fund managers outperform the markets over the long-term, there is no evidence that investment professionals, much less amateurs, can consistently identify these managers *ex ante*.⁸ Unlike past investment performance, fees are

⁴ *Private Pensions: Increased Reliance on 401(k) Plans Calls for Better Information on Fees*, Government Accountability Office at 10 (Mar. 6, 2007).

⁵ *Id.* See also *Changes Needed to Provide 401(k) Plan Participants and the Department of Labor Better Information on Fees*, Government Accountability Office (Nov. 2006).

⁶ *Report of Mutual Fund Fees and Expenses*, SEC Division of Investment Management at Part IA (Dec. 2000).

⁷ Mark Carhart, *On Persistence in Mutual Fund Performance*, 52 J. Fin. 57 (1997) (persistence in mutual fund returns is almost entirely explained by expenses and portfolio transaction costs).

⁸ See Remarks of Andrew Donohue before the PLI’s Investment Management Institute (Apr. 2, 2009) (“At a time when some 70 percent of actively managed funds underperform their benchmarks, if an investor or an investment adviser can not accurately identify who might outperform, what is the value proposition in taking on the risk for this variance in performance?”) available at <http://www.sec.gov/news/speech/2009/spch040209ajd.htm>.

highly predictable and represent a certain reduction in fund's performance. Thus, within any given asset class, fees arguably constitute the most important factor in the evaluation of different 401(k) investment options.

B. Judicial Repeal of ERISA's Fiduciary Standard. Fee disclosure has taken on heightened urgency in the wake of court decisions that have effectively repealed ERISA's fiduciary standards as applied to the evaluation of plan investment options. Under ERISA, plan sponsors have a fiduciary duty to exercise "care, skill, prudence, and diligence" in selecting plan investment options. Although there is a safe harbor for plan sponsors to the extent that participants direct how their particular accounts are invested, it is well-established that this safe harbor does not extend to the selection of individual investment options. As recently stated by a U.S. Court of Appeals, "the prudence of investments or classes of investments available to plan participants must be judged individually by a fiduciary, who must initially determine, and continue to monitor, the prudence of each investment option available to plan participants."⁹ "[A]lthough section 404(c) does limit a fiduciary's liability for losses that occur when participants make poor choices from a satisfactory menu of options, it does not insulate a fiduciary from liability for assembling an imprudent menu in the first instance."¹⁰

In a stunning departure from law and precedent, a U.S. Court of Appeals panel of judges recently substituted a market-based inquiry for ERISA's fiduciary standard of "care, skill, prudence, and diligence."¹¹ The panel found that the plan

⁹ *DiFelice v. U.S. Airways, Inc.*, 497 F.3d 410, 423 (4th Cir. 2007); see *Kanawi v. Bechtel Corp.*, 590 F.Supp.2d 1213, 1232 (N.D. Cal. 2008).

¹⁰ *DiFelice*, 497 F.3d at 418 n.3.

¹¹ *Hecker v. Deere & Co.*, 2009 WL 331285 (7th Cir. Feb. 12, 2009); see also *Braden v. Wal-Mart Stores Inc.*, 590 F.Supp.2d 1159 (W.D. Mo. 2008) (complaint alleging fees that were six times larger than fees charged by comparable funds was insufficient to survive a motion to dismiss ERISA claim for excessive fees); see generally *Hecker*, *supra* (briefs in support of rehearing and rehearing *en banc* filed by *amici curiae* (1) AARP, National Senior Citizens Law Center, Pension Rights Center, Fund Democracy, and Consumer Federation of America (Mar. 16, 2009), and (2) Law Professors (Mar. 17, 2009)).

sponsor that selected the investment options that were alleged to be excessively expensive was insulated from liability primarily because “all of these funds were also offered to investors in the general public, and so the expense ratios *necessarily* were set against the backdrop of market competition.” The panels’ decision effectively repeals ERISA’s fiduciary standard with respect to important characteristics of plan investment options and directly contradicts extensive empirical evidence of market inefficiencies in the mutual fund marketplace. In a similar case involving allegations that a mutual fund manager charged excessive fees, another 7th Circuit panel applied a similarly misguided economic analysis in finding that mutual fund fees were set in a competitive market which thereby precluded fiduciary claims of excessive fees.¹² Judge Posner, the world’s leading law and economics theorist, disagreed with the panel, noting that mutual funds operate under a “governance structure that enables mutual fund advisers to charge exorbitant fees” and where “abuses have been rampant.”¹³

The inclination of some courts to reject claims regarding excessive fees on the ground that fiduciary obligations are supplanted when there is evidence of a competitive marketplace increases the urgency of ensuring the full and fair disclosure of 401(k) fees. If participants can no longer rely on courts to protect their rights under ERISA, then it is incumbent upon Congress to require service providers and plan sponsors to disclose all fees, including especially fees that reflect a conflict of interest on the part of a plan fiduciary.

III. FEE-INSENSITIVE INVESTORS

The purpose of fee disclosure is not to provide the minimum information necessary to enable diligent, fee-sensitive investors to evaluate the cost of investing

¹² *Jones v. Harris Associates L.P.*, 527 F.3d 627 (7th Cir. 2008), *cert. granted*, 77 U.S.L.W. 3281 (Mar. 9, 2009).

¹³ *Jones v. Harris*, 537 F.3d 728, 730-732 (dissenting from denial of rehearing *en banc*).

in their 401(k) plans, but rather to draw the attention of all investors, especially fee-insensitive investors, to the importance of fees. The purpose of 401(k) fee disclosure reform therefore should be to furnish beneficiaries who are not sufficiently sensitive to the effect of fees on the performance of their 401(k) accounts with the information they need to raise their awareness of fees.¹⁴ To emphasize, it is *not* sufficient merely to ensure that fee information is available because making fee information available will not by itself change the behavior of fee-insensitive beneficiaries.

Research conducted by the Consumer Federation of America and assisted by Fund Democracy indicates that a large percentage of those who invest through workplace retirement plans are not sensitive to fees.¹⁵ In a 2006 survey on mutual fund purchase practices, only 51 percent of those respondents who purchased most of their funds through a workplace retirement plan said they considered fees even somewhat important.¹⁶ Furthermore, workplace purchasers were the least fee-sensitive of the three purchase groups identified by the survey.¹⁷ This likely reflects, in part, the fact that workplace purchasers typically make their fund selections from a fairly narrow menu of options. However, the relative lack of investing experience and financial sophistication among workplace purchasers almost certainly also plays a role.¹⁸ A 2007 survey of 401(k) participants' awareness and understanding

¹⁴ Jonathan Clements, *Investors Flock to Low-Cost Funds*, Wall St. J. at D1 (July 18, 2007) (citing Morningstar finding that 13% of stock fund assets are invested in funds charging more than 1.5% annually and 24% of bond fund assets are invested in funds charging more than 1% annually) available at <http://online.wsj.com/article/SB118471831946369665.html>.

¹⁵ *Mutual Fund Purchase Practices*, an analysis of survey results by Barbara Roper and Stephen Brobeck, Consumer Federation of America, June 2006.

¹⁶ *Id.* Thirty percent said fees were a very important factor in their fund selection, while 21 percent indicated fees were somewhat important. In contrast, 70 percent indicated fund company reputation was at least somewhat important, while 68 percent rated past performance as at least somewhat important.

¹⁷ *Id.* The other groups were direct purchasers and those who purchased most of their funds through a financial professional outside a retirement plan.

¹⁸ *Id.* Just 12 percent rate themselves as very knowledgeable about mutual funds, while nearly a third (32 percent) rate themselves as knowing only a little. They also tend to be somewhat younger and

of fees conducted by the AARP reinforces the findings of the CFA survey.¹⁹ The AARP found that two-thirds of respondents thought that *they did not pay any 401(k) fees* and another 18 percent did not know whether they paid fees. Eighty-three percent did not know how much they pay in fees in their 401(k) plans.

This general lack of investing sophistication is compounded by the fact that the financial media, financial advertisements and the structure of disclosure requirements consistently overemphasize the importance of past investment performance and underemphasize the significance of fees. The financial media's focus on "The Best Funds for 2007" as determined by their short-term investment performance sends exactly the wrong message regarding the factors that investors should consider when evaluating investment options. Financial advertisements focus almost solely on past investment performance, which has little predictive power, to the exclusion of fees, the impact of which is significant, relatively certain and quantifiable.

Furthermore, fee disclosure presents fees almost exclusively as a percentage of assets, which structurally minimizes the true significance of fees in the overall picture of an investor's portfolio. The effects can be seen in the fact that 68 percent of workplace purchasers in the CFA survey indicated that a fund's past performance was at least somewhat important to their selection, with 38 percent indicating it was very important – a far higher percentage than considered fees to be even somewhat important. Similarly, the AARP survey found that 92 percent of respondents rated past performance as very or somewhat important, compared with only 79 percent who rated fees as very or somewhat important.

less educated than other mutual fund purchasers, and to have held mutual fund investments for a shorter period of time, particularly when compared with those who purchased most of their funds directly from a fund company or through a discount broker or fund supermarket.

¹⁹ See *401(k) Participants' Awareness and Understanding of Fees*, AARP (July 2007) available at http://assets.aarp.org/rgcenter/econ/401k_fees.pdf.

For this reason, it is essential that fee disclosure be designed to counter the misleading message that investors generally receive regarding the relative importance of fees. To benefit fee-insensitive investors, fee disclosure must be based on a “push” principle that measures the efficacy of disclosure by its success in promoting competition and efficiency. To accomplish this, fee disclosure for 401(k) plans should be crafted not only to make fee information available, but also to affirmatively direct beneficiaries’ attention to fees and to do so in a way that helps them understand those fees and the effect they have on investment returns. In short, fee disclosure should be designed to overcome many investors’ predilection for overemphasizing past investment performance and discounting fees when making investment decisions. Investors’ fee-insensitivity represents a market failure for which fee disclosure (rather than price regulation) offers the most cost-effective solution. ***In many respects, the 401(k) Fee Disclosure Act adopts measures that are designed to ensure not only that 401(k) information is available to participants, but also that fee-insensitive participants’ attention is proactively directed to the importance of fees.***

IV. DELIVERY VEHICLES

The delivery vehicles used for fee disclosure play a crucial role in determining whether the disclosure is effective in directing fee-insensitive investors to consider fees when making investment decisions. Yet one of the most significant shortcomings of fee disclosure has been the reliance on investor-unfriendly delivery vehicles. Fees for 401(k) plan administration (*i.e.*, plan-level fees, as apart from fees charged by investment options) are required to be disclosed only in Form 5500, where the fees are disclosed as a dollar amount, in contrast with the presentation of fees as a percentage of assets for most investment options.²⁰ The Form 5500 is not

²⁰ See *Private Pensions: Increased Reliance*, *supra* note 4 (“the Form 5500 does not include the largest type of fee, even though plan sponsors receive this information from the mutual fund companies in the form of a prospectus. In 2004, the ERISA Advisory Council concluded that Form 5500s are of little use to policy makers, government enforcement personnel, and participants in terms of understanding the cost of a plan and recommended that Labor modify the form and its accompanying

required to be provided to beneficiaries, but is delivered only upon request, and is of no value when plan fees are paid through the investment options and the Form reports zero plan-level expenses.²¹

In the mutual fund context, fund expenses are described in the prospectus and the dollar amount of expenses for a hypothetical fund account are provided in the annual report for the period covered. Employers generally provide plan participants with the prospectus or a document that contains the fee information in the prospectus,²² but they do not provide the annual report or the hypothetical fee information, and neither fund documents or any documents provided by employers provide fee information about comparable investment options. Thus, basic fee information for each investment option is not provided in the same place as plan-level fees, no hypothetical or comparative fee information is provided at all, and no fee information is provided that is specific to a beneficiary's account.²³ Investor-specific information is contained only in the quarterly statement. The latter document is generally the document that investors read, whereas fund prospectuses and plan summaries are more likely to be summarily discarded with little or no review.

schedules so that all fees incurred directly or indirectly can be reported or estimated. Without information on all fees, Labor's oversight is limited because it is unable to identify fees that may be questionable.”).

²¹ See *H.R. 3185: The 401(k) Fair Disclosure for Retirement Security Act of 2007*, hearing before the Committee on Education and Labor, U.S. House of Representatives (Oct.4, 2007) (statement of Tommy Thomasson) (“There are literally tens of thousands of 401(k) plans that report zero costs for recordkeeping and administration on their annual report (Form 5500) filed with the Department of Labor. In actuality, participant accounts are being charged for these ‘free’ plan services in the form of investment fees assessed against their accounts.”).

²² As discussed further below, although fund expense ratios are standardized, they sometimes are not comparable because expenses that appear in the fund expense ratio for some funds may be excluded from the fund expense ratio for others (*e.g.*, transfer agency expenses may appear either in the fund expense ratio or in plan-level expenses). Expense ratios for non-mutual-fund investment options generally are not even standardized.

²³ See *Private Pensions: Increased Reliance*, *supra* note 4 (“Inadequate disclosure and reporting requirements may leave participants without a simple way to compare fees among plan investment options”); *Changes Needed*, *supra* note 5 (401(k) fee disclosure “is limited and does not provide for an easy comparison among investment options”).

Reliance on delivery vehicles currently used to convey 401(k) fee information assumes that investors are proactive and fee sensitive. The prospectus and Form 5500 require 401(k) beneficiaries to request information, calculate their total fees, and seek out comparative data on their own to put their total fees in context. One witness before the ERISA Advisory Council suggested that, by combining Form 5500 and prospectus fee disclosure, a 401(k) beneficiary “should be able to readily calculate the aggregate fees that reduce the value of his or her account.”²⁴ The witness concluded that 401(k) fees are “currently disclosed to participants in sufficient detail to allow participants to evaluate the costs they pay against the services they receive.”²⁵

I disagree. Few investors, and certainly not fee-insensitive investors, will make the effort to “calculate” fees in the manner described above. As noted above, they simply do not place sufficient emphasis on fees in the first place. In addition, according to the CFA survey, most workplace mutual fund purchasers are unlikely to make use of the written information sources available to them. Just over four in ten (43 percent), for example, rated the prospectus as even somewhat influential on their investment purchases, with only 19 percent rating it as very influential. The AARP found that only 34% of respondents who were involved in investment decisions cited the prospectus among the materials they turn to for guidance when making decisions.

To change the behavior of fee-insensitive beneficiaries, fees must be presented in a document beneficiaries are likely to read, they must be presented in a

²⁴ *Report of the Working Group on Fee and Related Disclosures to Participants*, Advisory Council on Employee Welfare and Pension Benefit Plans at n.4 (2004) (*Advisory Report*) (quoting testimony of John Kimpel, Sr. Vice President and Deputy General Counsel, Fidelity Investments). Actually, the fee dollar amounts in the Form 5500 would have to be converted to a percentage of assets and then added to the investment option’s asset-based fees.

²⁵ *Id.*

standardized format, and they must be presented in a manner that makes it easy for beneficiaries to understand how their 401(k) fees compare to fees charged by comparable plans and investment options.²⁶ Fee disclosure accordingly should focus on two primary delivery vehicles. First, beneficiaries should receive a summary plan document that contains essential information about the plan, including fee information. Second, information about fees should be included in account statements. Although the primary purpose of an account statement is to apprise beneficiaries of recent activity in and changes in the value of their accounts, it would be consistent with this purpose to provide limited fee information as well. Beneficiaries are very likely to review their statements, and for the most fee-insensitive among them, fee disclosure in account statements may provide the best and possibly the only realistic opportunity to impress upon them the importance of fees. That being said, adding too much fee information to the account statement runs a significant risk of reducing its effect. Fee information in account statements should be designed to draw the beneficiary's attention to the fees they pay, while minimizing the risk of information overload.

Account statements, however, provide information only after the investment selection has been made. To provide beneficiaries with pre-investment fee disclosures, Congress should require that such disclosures be provided in a short document that summarizes the plans' essential features. Such plan summaries should be required to be presented to all employees who are eligible to participate in the plan. Like the account statement disclosure described above, this disclosure should also provide information that enables beneficiaries to easily determine how those fees compare to fees for comparable plans and investment options.

Finally, Congress should encourage the use of the Internet and electronic communications as one appropriate delivery vehicle for fee information. The

²⁶ See *Private Pensions: Increased Reliance*, *supra* note 4 (“The information on fees that plan sponsors are required to disclose to participants does not allow participants to easily compare the fees for the investment options in their 401(k) plan.”).

Internet and electronic communications offer the opportunity both to enhance fee disclosure for beneficiaries and to reduce plan expenses. For increasing numbers of investors, the Internet and email constitute their primary information source and communication tool. According to the CFA survey, for example, nearly all workplace investors (91 percent) have access to the Internet, and the vast majority (87 percent) expressed a willingness to use the Internet for at least some mutual fund purchase-related activities. The AARP found that 34 percent of surveyed investors who make financial decisions use the Internets as an information source, with the employer Intranet being the most popular site.

At a minimum, all fee disclosure should be required to be made on or be easily accessible from employer web pages. Where delivery is required, email, including especially employer Intranets, should be mandated as a delivery option investors can choose to use. In appropriate circumstances, such as when an employee has affirmatively decided to use either medium to obtain and receive information, Internet posting and delivery by email should be deemed sufficient to satisfy legal delivery requirements.

The 401(k) Fee Disclosure Act meets all of these standards regarding the optimal delivery vehicles for fee disclosure. The Act requires that participants be provided with a notice at least 10 days prior to the earliest date on which they can invest in the plan. The notice must include basic information about each investment option and, importantly, a plan fee comparison chart that shows: (1) asset-based investment option fees, (2) asset-based plan fees, (3) administrative and transaction-based fees,²⁷ and (4) any other fees that may be deducted from

²⁷ These include: “fees charged to participants to cover plan administration, compliance, and recordkeeping costs, plan loan origination fees, possible redemption fees, and possible surrender charges, that are not assessed as a percentage of the total assets in the account and are either automatically deducted each year or result from certain transactions engaged in by the participant or beneficiary.”

participants' accounts.²⁸ The purpose of the fees also must be provided. The Act permits the required disclosure to be provided via the Internet. In addition, the Act requires that participants receive a quarterly benefit statement that includes, among other things, the dollar amount of the fees deducted from the participant's account during the period covered.

V. FORM OF FEE DISCLOSURE

Disclosure of 401(k) fees should be provided in two forms. As noted above, 401(k) fees should be disclosed on beneficiaries' account statements, in order to proactively direct beneficiaries' attention to the amount of fees that they pay, and in a plan summary document, to ensure that beneficiaries are made aware of fees when they make their initial investment selections.

A. Account Statement Fee Disclosure. The 401(k) plan document that investors are most likely to review is their account statement, and Congress therefore should require that account statements include 401(k) fee disclosure. In 2003, the GAO recommended, for example, that the SEC require mutual funds to disclose in shareholders' account statements the dollar amount of fees paid during the period covered.²⁹ Partly in response to industry claims that dollar disclosure of fees would be ruinously expensive,³⁰ the SEC decided instead to require the disclosure of the dollar amount of fees charged on a hypothetical account in the annual report.³¹ Industry cost claims have proven to be a red herring, as firms such

²⁸ Cf. *Private Pensions: Information That Sponsors and Participants Need to Understand 401(k) Plan Fees*, GAO-08-222T (Oct. 30, 2007) (arguing for disclosure of all types of fees).

²⁹ See *Mutual Funds: Information On Trends In Fees And Their Related Disclosure*, Government Accounting Office (March 12, 2003).

³⁰ *H.R. 2420: The Mutual Funds Integrity and Fee Transparency Act of 2003*, hearing before the Subcommittee on Capital Markets, Insurance and Government-Sponsored Enterprises, Committee on Financial Services, U.S. House of Representatives (June 18, 2003) (statement of Melody Hobson).

³¹ See *Shareholder Reports and Quarterly Portfolio Disclosure of Registered Management Investment Companies*, Investment Company Act Rel. No. 26372 (Feb. 27, 2004).

as MFS Investment Management have found it cost-effective to provide investors with precisely the dollar disclosure of fees on quarterly statements³² that the industry had argued would be “breathtakingly high.”³³ Individualized fee disclosure is obviously affordable, and just as obvious is the need to move it from the annual report, which investors virtually never cite as an information source they use, to the account statement, which they review on a regular basis.

Congress should require 401(k) plans to disclose the following information in account statements: the dollar amount of total fees paid by the investor for the period covered³⁴ and the dollar amount that would have been paid in the average comparable plan and investment options. The disclosure of the dollar amount of fees is of particular value because beneficiaries are more accustomed to thinking about expenses in dollars rather than percentages. Fee-insensitive beneficiaries are more likely to take notice of disclosure that looks more like a common bill for services than a mathematical calculation. Dollar disclosure will translate somewhat esoteric expense ratios into more understandable dollar amounts and cause any beneficiary who is paying higher than average fees to rethink whether the services provided are worth the price.

One drawback of both dollar amount and percentage fee disclosures is that they may mean little to beneficiaries without a comparative context in which to place them. The AARP survey referenced above showed the effect that comparative fee information can have. When presented with two funds that differed only as to the size of their expense ratios, seventy-nine preferred the fund with the lower

³² See *Bundled Provider of the Year*, Defined Contribution News, 2005 WLNR 7781126 (Apr. 18, 2005).

³³ See *H.R. 2420*, *supra* note 30 (statement of Melody Hobson) (claiming that account statement fee disclosure would impose “breathtakingly high costs.”)

³⁴ It is my understanding that the fee disclosure provided by MFS uses the simplifying assumption that there have been no purchases or redemptions during the period other than reinvestment of fund distributions, which still would provide an effective reminder of the amount of fees paid.

expense ratio. If investors are presented with clear comparative data, they will know what to do with it. I believe that this disclosure would do more to promote competition among 401(k) services providers and drive down fees than any other form of fee disclosure.

B. Plan Summary Fee Disclosure. Fee disclosure for 401(k) plans should be provided in the plan summary document and standardized to facilitate comparisons across different investment options within 401(k) plans and to expenses in other comparable plans. To some extent, standardization of investment option fees already exists. For example, mutual funds are required to use a standardized format for their expenses ratios and other expenses. Other types of 401(k) investment options use non-standardized fee disclosure, however, which prevents investors from comparing the true cost of different investment options. The goal of standardization is further frustrated by the fact that payments for services sometimes occur at the investment option level and sometimes at the plan level. For example, 401(k) plans that invest in a retail class of mutual fund shares often pay lower plan expenses, because the mutual fund rebates part of its fees to the plan administrator to cover those expenses. If the mutual fund's fees are compared to investment options that do not use such a rebate structure, the mutual fund's fees will appear higher. An accurate fee comparison generally can be made only when the plan's total fees are disclosed in a standardized format.

There are a number of potential solutions to the standardization challenge. One solution would be for Congress to impose fee disclosure requirements on non-mutual-fund investment options that are similar to those for mutual funds. Such standardization is clearly in the best interests of beneficiaries. Congressional action has the advantage of avoiding interagency conflicts that will arise if rulemaking is left to the Department of Labor. A number of different agencies have primary responsibility for fee disclosure rules for various 401(k) investment options, and it is unlikely that the Department would be able to bring these agencies' rules into alignment. I therefore recommend that Congress enact legislation that preempts

potential interagency conflicts and paves the way for standardized fee disclosure at least across all 401(k) investment options. ***Toward this end, the 401(k) Fee Disclosure Act should be amended to direct the Department of Labor to require standardized fee disclosure for all types of investments, including imputed fees for investments that internalize fees (e.g., guaranteed investment contracts).***

Another potential solution would be to require the disclosure of 401(k) fees on a functional basis. For example, fees for transfer agency functions could be identified separately, which would permit comparisons of these fees across different plans regardless of whether the fees were collected by the plan administrator, or by a mutual fund and then rebated to the plan administrator. The downside of functional fee disclosure is that it may be administratively burdensome and excessively costly without providing a material benefit to plans fiduciaries and beneficiaries. Fees generally are not disclosed on a functional basis under existing legal rules for collective investment vehicles or for 401(k) plans, and the cost of designing and implementing new systems to provide functional disclosure might not be justified. In any case, it is not clear that functional fee disclosure as a general matter is a cost-effective disclosure approach, and it can be misleading.³⁵

These concerns are reflected in the problem of treating bundled and unbundled fee arrangements consistently.³⁶ Requiring disclosure of fees received by each service provider on a functional basis may distort competition if bundled providers are not subject to the same requirement. If bundled providers (*i.e.*, providers who provide all or a wide range of fees under one fee) are required to

³⁵ For example, one of the problems with mutual fund 12b-1 fees, which purport to reflect the use of mutual fund assets for distribution services, is that investors in funds that do not charge 12b-1 may actually pay as much for distribution services as investors in 12b-1 fee funds. It can be extremely difficult to define precisely the different types of services for purposes of functional disclosure of fees.

³⁶ See generally *H.R. 3185: The 401(k) Fair Disclosure for Retirement Security Act of 2007*, hearing before the Committee on Education and Labor, U.S. House of Representatives (Oct. 4, 2007) (statement of Tommy Thomasson) (discussing problem of functional fee disclosure).

break out their fees functionally, fees might rise, especially if individual service provider's willingness to charge such fees is contingent on their fee not being separately disclosed. Similarly, unbundled providers may negotiate special deals that are conditioned on their remaining confidential. This principle is illustrated by Internet travel agent Travelocity's policy that it will not break out separately the part of a package deal that is separately attributable to the flight, hotel and rental car.³⁷

I believe that the best immediate solution to the problem of standardizing 401(k) fees is to present each fee component in the context the plan's total fees. Toward this end, the standardization of 401(k) fees should be accomplished through the use of a fee table (including a fee example) and a list of additional expenses as described below.³⁸

C. Fee Table. As illustrated in Exhibit A, the fee table would include three categories of data for each investment option. These are: the investment option expense ratio,³⁹ total plan fees (including both the investment option fees and plan-level fees) as a percentage of assets, and the dollar amount of annual fees on a hypothetical \$1,000 account. For each category, a comparative expense figure

³⁷ Travelocity confirmations contain the following disclosure: "The TotalTrip combines special rates that we receive from our air, hotel, and car suppliers for package inclusions. Our agreements with such suppliers prohibit us from breaking down the prices for the individual components. Our packages offer customers the convenience and savings of booking their entire trip in one transaction."

³⁸ The overall structure of this approach is similar to the mutual fund fee table, which includes an expense ratio, a list of other expenses, and a dollar-amount fee illustration.

³⁹ I note that a significant failing of the mutual fund expense ratio is its omission of portfolio transaction costs, which can equal many multiples of a fund's other expenses. See Jason Karceski, Miles Livingston and Edward O'Neal, *Portfolio Transaction Costs at U.S. Equity Mutual Funds* (2004), available at http://www.zeroalphagroup.com/news/Execution_CostsPaper_Nov_15_2004.pdf. Although the SEC has requested comments on ways to address this omission, it has yet to take final action. See *Request for Comments on Measures to Improve Disclosure of Mutual Fund Transaction Costs*, Investment Company Act Rel. No. 26313 (Dec. 18, 2003). I strongly encourage Congress to mandate that the mutual fund expense ratio and the expense ratio of other investment options include all of the relative costs of investing.

would also be included. This approach has the advantage of permitting easy comparison of different investment options investing in the same asset class when the investment options' expense ratios are comparable, such as for mutual funds. The total expense ratio figure not only would provide a total cost figure, it also would help address the problem of non-comparable investment fee information. Where easily comparable fee information of the type provided by mutual funds is not available,⁴⁰ it would indirectly indicate the relative cost of different investment options in the same asset class, because the plan-level expenses for each option generally could be assumed to be relatively constant. Assuming that plan-level expenses are comparable across different investment options, to the extent that the total expense ratio for different investment options differed, the difference generally would be attributable to the cost of the investment options. ***I strongly recommend that the 401(k) Fee Disclosure Act be amended to require fee table as discussed above and illustrated at Exhibit A (this would necessitate requiring disclosure as a percentage of assets and incorporating comparative fees as a dollar-amount and percentage of assets for non-plan investment options).***

D. Additional (Non-Expense-Ratio) Expenses. By making expenses charged through asset-based fees more visible, this approach may create an incentive to shift costs to other forms. To minimize any such cost-shifting designed to avoid disclosure, additional disclosures should be provided along with the fee table listing expenses that are not included in the expense ratio table but that may be incurred directly or indirectly by beneficiaries. These expenses would include, for example, purchase and redemption fees, minimum account charges, and non-asset-based sales charges. These expenses should be presented as a percentage of assets or a dollar amount, depending on the basis on which they are deducted, with explanations as appropriate.

⁴⁰ As noted *supra* note 35, although fund expense ratios are standardized, they sometimes are not comparable because expenses that appear in the fund expense ratio for some funds may be excluded from the fund expense ratio for others (*e.g.*, transfer agency expenses may appear either in the fund expense ratio or in plan-level expenses). This distinction is partly responsible for the recent flurry of excessive fee cases brought against employers in connection with their 401(k) plans.

One disadvantage of the foregoing approach is that it may not fully remove the incentive to shift expenses, in this case from the expense ratio to the additional expenses category. For example, a 401(k) provider could reduce the plan's expense ratio by replacing an asset-based transfer agency fee with a flat fee for each account. This strategy would have the effect of artificially reducing the expense ratio, on the assumption that investors would pay less attention to the concomitant increase in the expenses listed as additional expenses. The problem of expenses being shifted out of the expense ratio would also be mitigated by the disclosure in account statements of the total dollar amount of fees charged during the period, which would include fees not included in the expense ratio. ***The 401(k) Fee Disclosure Act addresses this problem by requiring the disclosure of all types of fees as a dollar amount, thereby removing the fee-shifting incentives identified above. The Act would be more effective, however, if disclosure were required both as a dollar amount and a percentage, as illustrated in the Table at Exhibit A.***

VI. CONFLICTS OF INTEREST AND DIFFERENTIAL COMPENSATION

One of the most difficult challenges presented by fee disclosure is the need to apprise plan fiduciaries and beneficiaries of the conflicts of interests that differential compensation can create. Differential compensation refers to arrangements whereby salespersons are paid more for selling products offered by one financial services provider than for selling those offered by another provider. Remarkably, courts have held that it is consistent with a fiduciary's duties under ERISA not to disclose to participants the receipt distribution compensation such as revenue sharing payments,⁴¹ notwithstanding that "investment providers or record keepers

⁴¹ See, e.g., *Braden v. Wal-Mart Stores Inc.*, 590 F.Supp.2d 1159, 1168 (W.D. Mo. 2008).

may try to steer sponsors to funds which result in higher hidden fees for themselves or other providers.”⁴²

In its recent survey of pension consultants who advise fiduciaries regarding investment options and other matters, the SEC found: (1) that most pension consultants receive compensation from *both plans and money managers*, with compensation from money managers in some cases comprising a significant part of their revenue, (2) that most pension consultants have affiliates (*e.g.*, broker-dealers) through which they receive compensation from plans that they advise, (3) evidence that consultants were more likely to recommend money managers from whom they received compensation, and (4) that consultants frequently provided inadequate disclosure of the conflict of interest created by these arrangements.⁴³ The SEC has brought enforcement actions against certain consultants for failing to disclose fully their conflicts of interest in connection with their pension consulting business.⁴⁴ In 2007, the GAO found that pension consultants with significant undisclosed conflicts of interest with their defined pension fund clients had annual

⁴² *Private Pensions: Fulfilling Fiduciary Obligations Can Present Challenges for 401(k) Plan Sponsors*, GAO-08-774 at n.32 (2008); *see also id.* at 24 (“Hidden’ fees may also mask the existence of a conflict of interest. Hidden fees are usually related to business arrangements where one service provider to a 401(k) plan pays a third-party provider for services, such as record keeping, but does not disclose this compensation to the plan sponsor. Without disclosing these arrangements, service providers may be steering plan sponsors toward investment products or services that may not be in the best interest of participants.”).

⁴³ *See Staff Report Concerning Examinations of Select Pension Consultants*, Office of Compliance Inspections and Examinations, SEC (May 16, 2005).

⁴⁴ *See, e.g., In the Matter of Callan Associates*, Admin. Proc. File No. 3-123808 (Sep. 19, 2008) (pension consultant failed to disclose payments from broker-dealer in connection with trades by consultant’s pension clients) *available at* <http://www.sec.gov/litigation/admin/2007/ia-2650.pdf>; *In the Matter of Yanni Partners, Inc.*, Admin. Proc. File No. 3-12746 (Sep. 5, 2007)(pension consultant misled pension clients regarding undisclosed payments from money managers that it recommended) *available at* <http://www.sec.gov/investor/pubs/sponsortips.htm>; *see also SEC Charges Merrill Lynch With Misleading Pension Consulting Clients*, SEC Press Release (Jan. 30, 2009)(“Merrill Lynch failed to disclose its conflicts of interest when recommending that clients use directed brokerage to pay hard dollar fees, whereby the clients directed their money managers to execute trades through Merrill Lynch”) *available at* <http://www.sec.gov/news/press/2009/2009-13.htm>.

returns that were 1.3 percentage points lower than for other consultants.⁴⁵ These abuses are particularly troubling because they have been foisted on presumably sophisticated plan fiduciaries. Unsophisticated participants are even less likely to be able to discern and defend against abusive sales practices that hidden distribution payments encourage.

The 401(k) Fee Disclosure Act should be amended to require that 401(k) service providers provide full and separate disclosure to plan fiduciaries and participants of all conflict of interest payments received by persons (and their affiliates) who provide distribution services to service providers, especially in connection with investment advice to participants.⁴⁶ The disclosure should expressly identify the conflict of interest created by such arrangements and be designed so as to specifically and separately draw the fiduciary's or participant's attention to the conflict. The disclosure also should identify the amount of compensation received under such arrangements and its significance in the service provider's total revenues in that line of business.⁴⁷ For too long, fiduciaries and participants have been kept in the dark about their advisers' incentives to recommend service providers based on compensation paid to the adviser, rather than on the best interests of the plan. This problem will greatly exacerbated if the

⁴⁵ See *Private Pensions: Conflicts of Interest Can Affect Defined Benefit and Defined Contribution Plans*, GAO-09-503T (Mar. 24, 2009) available at <http://www.gao.gov/new.items/d09503t.pdf>; *Defined Benefit Plans: Conflicts of Interest Involving High Risk or Terminated Plans Pose Enforcement Challenges*, GAO-07-703 (June 28, 2007) available at <http://www.gao.gov/new.items/d07703.pdf>.

⁴⁶ The current version of the Act does not clearly include this requirement. It nowhere mentions disclosure directed specifically at the issue of conflict of interest payments, and its fee disclosure requirements generally could be interpreted to permit the disclosure of asset-based fees that included a conflict of interest payment (e.g., a payment by the manager of an investment option to a person who provides investment advice to participants about investment options) without breaking out separately the that payment, much less explaining that the fee created an incentive to recommend certain investment options over others. This practice is accepted in the securities industry (and authorized by the SEC). If not prohibited by Congress or the Department of Labor, it will become commonplace in the 401(k) marketplace.

⁴⁷ In its recent amendments to Form 5500, EBSA opted not to require disclosure of eligible indirect compensation, but to permit disclosure of the identity of the person receiving the compensation instead. See *Annual Reporting and Disclosure*, 72 Fed. Reg. 4709 (Nov. 16, 2007).

Department of Labor adopts its pending rules regarding the providing of conflicted investment advice to plan participants.⁴⁸

Advisers should be required to prominently disclose the extent to which their compensation may vary based on the investment options selected by the beneficiary. In order to qualify as “prominent,” the disclosure should be in separate document, email message or web page. The disclosure must be provided separately because otherwise it is likely to be confused with fee disclosure that is designed to highlight the costs of investing, rather than the economic incentives of the adviser.⁴⁹ The disclosure should focus on the amount of the adviser’s differential compensation in order to permit the beneficiary to evaluate the objectivity of the adviser’s recommendations.

Moreover, differential compensation disclosure should be provided before the beneficiary makes the decision to retain the adviser so that the beneficiary can evaluate the adviser’s services before soliciting recommendations. After the beneficiary has retained the adviser and received the adviser’s recommendations, the opportunity to evaluate the wisdom of retaining that adviser will have passed. In this respect, Congress should require that, in addition to disclosure made prior to the retention of the adviser, the adviser specifically disclose any differential compensation received in connection with the recommended investments at the time that the recommendation is made. Finally, periodic reminders should be provided to beneficiaries as long as differential compensation payments continue.

⁴⁸ See *Retirement Security: The Importance of an Independent Investment Adviser*, Subcommittee on Health, Employment, Labor, and Pensions, Committee on Education and Labor, U.S. House of Representatives (Mar. 24, 2009) (testimony of Mercer Bullard). For example, the Department’s rules would allow a person to advise participants regarding investment options even if that person’s immediate supervisor were paid higher compensation when certain investment options were selected.

⁴⁹ See Investment Advisers Act Rule 206(4)-3 (requiring disclosure of solicitor’s capacity and compensation in a separate document).

Some may argue that disclosure of differential compensation is too costly and complex. Advisers who choose to create the conflict of interest that differential compensation disclosure would address, however, should not be allowed to avoid disclosure of differential compensation because of the complexity and disclosure costs they are responsible for creating. If, for example, a mutual fund charged dozens of different fees that depended on an investor's particular situation, the fund's sponsor should not be heard to complain that the cost of fee disclosure far exceeded its benefits. In short, the cost of fee disclosure should be viewed not as a reason to permit conflicts of interest to be concealed, but as a natural market constraint on inefficient pricing practices. To the extent that investors reject complex fee structures, such as differential compensation arrangements, when they are fully disclosed, fee disclosure should be viewed as having operated successfully by promoting informed investor choice, competition and efficiency.⁵⁰

VII. COMPARATIVE FEE INFORMATION

The 401(k) Fee Disclosure Act takes the important step of requiring that fee comparisons be incorporated into 401(k) disclosure documents. The disclosure of fees accomplishes little when it is presented in a vacuum because few investors can readily assess whether the fees charged are high or low relative to the services provided or the fees charged by comparable investments. Mutual fund investment performance information is required to be compared to the performance of a comparable market index, because regulations recognize the importance of putting performance in context (although this has the effect of overemphasizing the significance of past performance), but funds are not required to do the same for fees. Providing comparative fee information makes even more sense than providing comparative investment performance information, because

⁵⁰ Although the speciousness of arguments that fee disclosure is too costly due to its complexity is most applicable to differential compensation arrangements, it is not limited to such arrangements. The same analysis applies to all types of complex fee arrangements, such as the use of different types of account and activity charges that are in addition to a fund's expense ratio and plan expenses as disclosed in the Form 5500.

past fees (unlike past performance) are strongly predictive of future fees. Furthermore, fee comparisons are more valid than performance comparisons, because fees of different 401(k) plans generally will be more comparable than investment performance across different investment options.

Putting fee information in context by providing comparative information is important for a number of reasons. First, comparative information would promote competition among investment option providers and place downward pressure on fees. Second, comparative information would enable beneficiaries to evaluate the costs and benefits of investing in the 401(k) plan relative to other taxable and tax-deferred investment options.⁵¹ Third, fiduciaries' interests may conflict with beneficiaries' with respect to the negotiation of 401(k) fees, as fiduciaries may be able to lower the administrative costs paid by the employer by shifting them onto plan beneficiaries in the form of asset-based fees.

A. Investment Option Fees. Without the context of comparative fee disclosure, the disclosure of an investment option's expense ratio is of limited utility because it only conveys the fact that an investment option and the plan are not free.⁵² Standing alone, the fees provide little basis for evaluating whether they are reasonable in light of the services provided. The disclosure of comparative fee information would provide beneficiaries with a general sense of whether an investment option is more or less expensive than its peers and increase the likelihood that beneficiaries will think about whether above-average-cost options are worth the price. Also, providing average cost information for comparable investments should increase the likelihood that beneficiaries will make appropriate

⁵¹ In theory, comparative disclosure would enable employees to compare employers based on the relative qualities of their 401(k) plans. This potential benefit is secondary, however, to the benefits of promoting competition among investment option providers and facilitating an informed comparison of 401(k) and non-401(k) investment options.

⁵² The AARP survey suggests, however, that many beneficiaries may actually be unaware that they pay any fees in connection with their 401(k) plans. *See supra* text accompanying note 19.

cost comparisons – for example, comparing a bond fund’s fees to average bond fund fees rather than to fees for an actively managed stock fund – rather than simply comparing costs among various investment options with very different investment characteristics and choosing the cheapest option.

Providing comparative fee information to beneficiaries would promote competition among investment option providers for several reasons. First, providing this information should help incentivize employers, who are primarily responsible for the selection of investment options, to choose a plan with lower investment costs. Second, many 401(k) plans offer multiple investment options with overlapping asset or style categories. In this context, beneficiaries’ investment decisions constitute a secondary marketplace (the plan itself) within which investment option providers compete for assets. This marketplace is recreated in every plan with multiple investment options, which has the effect of combining the market power of investment decisions by beneficiaries across many plans. Even if fiduciaries fail to populate plans with low-cost investment options, beneficiaries will tend to move assets to lower cost providers, if the comparative cost of different options is prominently disclosed. Such intra-plan dynamics will promote competition and place downward pressure on fees.

When a plan does not offer overlapping investment options, however, fee disclosure is less effective and can even be misleading. A requirement that the comparative fees charged in connection with an investment in international stock fund and a domestic stock fund, for example, may mislead beneficiaries by confusing the primary basis on which comparisons across different options should be made. While it would be important for participants to understand that international funds generally are more expensive than domestic funds, the comparison between these options should not be driven primarily by fees. The comparison among different investment categories should be based on beneficiaries’ overall investment objectives, not their relative expenses. A participant who chose the domestic stock fund because it was less expensive would lose the significant benefits of

diversification that investing in both domestic and international markets provides. ***Accordingly, Congress should consider amending the 401(k) Fee Disclosure Act to require disclosure of comparative fees between comparable investment options within a plan, and between plan fees and the average fees charged by comparable investments in the marketplace.***

B. Plan Fees. ***The 401(k) Fee Disclosure Act will promote competition and provide better information to participants by facilitating comparisons with comparable non-401(k) investment vehicles.*** Such comparative fee information would enable beneficiaries to make informed comparisons between 401(k) and non-401(k) investment vehicles. The axiom that employees should “max out their 401(k)” before investing elsewhere is no longer always valid advice⁵³ because employees will sometimes be able to achieve superior long-term, after-tax investment returns in other contexts. The proliferation of tax-deferred investment vehicles, many of which are designed, like 401(k) plans, for retirement planning, has provided numerous investment alternatives that offer tax advantages that are comparable to those offered by 401(k) plans. The historically low level of capital gains taxes relative to income taxes means that capital gains in 401(k) plans are taxed at higher income rates when distributed than are capital gains in taxable accounts when they are distributed.⁵⁴ Tax-managed funds, index funds and exchange-traded funds employ strategies that minimize taxes, thereby substantially minimizing their tax disadvantage relative to 401(k) plans. Thus, non-401(k) tax-advantaged investment vehicles, lower capital gains rates, and tax-minimizing investment vehicles mean that an employee will often be better off investing in a taxable account rather than a high-cost 401(k) plan (assuming no employer match).

⁵³ In contrast, the related axiom that employees should always “max out their 401(k) match” (*i.e.*, fully exploit matching employer contributions) still holds.

⁵⁴ To some extent, this taxable account advantage is reduced because capital gains taxes are paid on an ongoing basis, whereas income taxes on 401(k) capital gains are not paid until distributions from the account are made. Legislation has been proposed (and is slowly gaining support), however, that would permit the deferral of taxation of capital gain distributions by mutual funds that are reinvested in the funds.

Fee disclosure for 401(k) plans should facilitate fee comparisons with non-401(k) investment vehicles. ***Toward this end, the 401(k) Fee Disclosure Act should be amended to require that the information provided to participants include a comparison to fees charged by comparable 401(k) plans and non-401(k) investment vehicles.***⁵⁵

C. Potential Conflicts of Interest. It is particularly important that comparative fee information be placed in the hands of beneficiaries who may have a stronger economic incentive than fiduciaries to reduce fees because it is primarily beneficiaries who pay them. In some cases, beneficiaries' and fiduciaries' interests can conflict. Fiduciaries may have an incentive to choose high-cost investment options as a means of shifting expenses from the employer to the beneficiaries. Plan fiduciaries therefore may be conflicted, because they have an incentive to reduce plan expenses (*i.e.*, expenses incurred by their employer) in return for accepting higher investment option expenses. Plan fiduciaries also may wish to be perceived as having successfully negotiated a low-cost administrative contract, or may simply be unaware of the trade-off between higher cost investment options and lower cost administrative services. Although fiduciaries generally will be more financially sophisticated than the average beneficiary, this is not always the case. Ultimately, beneficiaries have stronger economic incentives to uncover such tradeoffs. It takes only a single, activist beneficiary, armed with the appropriate information, to bring these issues to the attention of plan fiduciaries.

D. Form of Comparative Fee Information. ***The 401(k) Fee Disclosure Act requires the disclosure of comparative fees as a dollar amount, which will provide an easy to understand illustration of the bottom-line impact of differences among different investments and plans.*** Congress also should consider requiring that comparative fee information be provided as a percentage of

⁵⁵ The Act recognizes the availability of comparable fees in its requirement that new plans estimate their fees based on "a comparable plan with participants and beneficiaries of similar demographics."

assets (the Act makes this voluntary) and that the information be provided in the fee table for each investment option. The comparative expense ratio row should show average expense ratios for the investment option, and for total expenses, including investment and plan-level expenses charged as a percentage of assets (see Exhibit A). These data should be presented in a manner that ensures that they are easily distinguishable from, and readily comparable to, the plan's actual expense ratios. Congress should consider whether additional comparative information should be provided, such as the amount of the difference between each average expense ratio and the actual expense ratio or a graphic illustration of each investment option's expenses relative to the average.⁵⁶ In making such decisions, both about content and format, the Congress should consult with disclosure experts to help design disclosures that maximize beneficiaries' ability to understand key fee information.

Congress should permit employers to use a variety of sources for comparative data, provided that the information is provided by an independent third party. It may be necessary, however, to establish some guidelines regarding what constitutes appropriate comparative data for different types of investment. Employers also should be permitted to use average plan-level expense ratios that reflect the size of the plan, subject to regulatory guidelines.

VIII. ACTIVE MANAGEMENT RISK AND PASSIVELY MANAGED INVESTMENT OPTIONS.

The 401(k) Fee Disclosure Act takes the long overdue step of prohibiting pension plans from limiting investment options to actively managed portfolios and thereby forcing their participants to pay higher fees and assume active management risk. It is widely accepted that actively managed funds cannot, as a

⁵⁶ Cf. *Are Hidden 401(k) Fees Undermining Retirement Security?* hearing before the Committee on Education and Labor, U.S. House of Representatives (Mar. 6, 2007) (statement of Stephen Butler) (proposing requirement to disclose opportunity cost of fees as measured by the amount by which an account would be reduced by fees during a 10- or 20-year period).

group, outperform the marketplace after taking fees into account.⁵⁷ There is no reason why the actively managed funds offered by pension plans that do not offer a passively managed investment option would be any different from all actively managed funds as a group.⁵⁸ This means that these plans as a group will – with virtual certainty – force their participants to accept lower returns than the market. This is only one component of active management risk.⁵⁹

A second component of active management risk is the variance in the returns of actively managed funds. The performance of passively managed funds generally will cluster around the performance of the index or asset class on which they are based. In contrast, actively managed funds' performance varies greatly. An investment in an actively managed fund assumes the risk of performance that substantially outperforms or *substantially underperforms* the market. For example, investors who bet on the widely touted, past performance of Bill Miller's funds were rudely awakened to this aspect of active management risk when they experienced losses that were more than 50 percent greater than losses in the relevant equity

⁵⁷ See, e.g., Nicolas Bollen and Jeffrey Busse, *Short-Term Persistence in Mutual Fund Performance*, 18 *Review of Financial Studies* 569 (2005); Erik Sirri and Peter Tufano, *Costly Search and Mutual Fund Flows*, 53 *Journal of Finance* 1589 (1998); Mark Carhart, *On Persistence of Mutual Fund Performance*, 52 *Journal of Finance* 57 (1997); Martin Gruber, *Another Puzzle: The Growth of Actively Managed Mutual Funds*, 51 *Journal of Finance* 3 (1996); Burton Malkiel, *Returns from Investing in Mutual Funds 1971 – 1991*, 50 *Journal of Finance* 549 (1995); Stephen Brown and William Goetzmann, *Performance Persistence*, 50 *Journal of Finance* 679 (1995); William Sharpe, *The Arithmetic of Active Management*, 47 *Financial Analysts' Journal* 7 (1991) available at <http://www.stanford.edu/~wfsarpe/art/active/active.htm>; Michael Jensen, *The Performance of Mutual Funds in the Period 1945 – 1964*, 23 *Journal of Finance* 389 (1968); William Sharpe, *Mutual Fund Performance*, 39 *Journal of Business* 138 (1966). It should be noted that the ineluctable underperformance of actively managed funds as a group does *not* answer the question of whether: (1) some actively managed funds outperform the market, or (2) it is possible (or reasonable to attempt) to identify *ex ante* such actively managed funds.

⁵⁸ The industry concedes that 30 percent of plans do not offer a passively managed equity option. Sara Hansard, *Require 401(k) Plans to Offer Fixed-Income Products, Key Congressman Says*, *Workforce Management* (Apr. 17, 2009) (comments of Paul Schott Stevens, President, Investment Company Institute).

⁵⁹ See generally Kenneth French, *The Cost of Active Investing* (Apr. 12, 2008) (estimating annual cost of active management to be 0.67%); Ross Miller, *Measuring the True Cost of Active Management by Mutual Funds* (Aug. 2005) (finding that actively managed funds' "active expense ratios" are more than six times higher than their published expense ratios of 1.15%).

market in 2008.⁶⁰ They assumed the risk of sharp declines by investing in equities; they assumed an additional risk of *even sharper* declines resulting from active management risk.⁶¹ Entire classes of actively managed funds have recently exhibited an extraordinary degree of variance that undermines the utility of investing in a specific asset class in the first place.⁶²

It should go without saying that employers should not be allowed to force participants to assume active management risk by offering only actively managed investment options. Indeed, it is unclear how an employer could fulfill its fiduciary duty in selecting plan investments without offering passively managed options.⁶³ Under any reasonable understanding of a fiduciary standard, requiring that plan participants assume active management risk, not to mention the burden of higher

⁶⁰ Sam Mamudi, *Dubious '60% Club' For 3 Mutual Funds*, Wall St. J. (Jan. 2, 2009) (Bill Miller's Legg Mason Opportunity Trust and Legg Mason Growth Trust lost 65 percent and 60 percent, respectively, in 2008, compared with an average 38 percent decline in domestic stock funds).

⁶¹ In addition, conflict of interest payments to pension plan consultants and advisers to plan participants create an incentive to refer plans and participants to more profitable actively managed investment options in order to generate higher conflict of interest payments. *Staff Report on Examinations of Select Pension Consultants*, Office and Compliance Inspections and Examinations, U.S. Securities and Exchange Commission (May 16, 2005) (finding that consultants' affiliations and other relationships with broker-dealers through which they received undisclosed compensation created concerns that "these arrangements may provide an incentive for a pension consultant to recommend an active trading strategy, because the pension consultant or its affiliated broker may receive more money in commission payments.") *available at* <http://www.sec.gov/news/studies/pensionexamstudy.pdf>.

⁶² See generally Eric Jacobson, *Where Leverage Lurks*, Morningstar.com (Apr. 1, 2009) (some "conventional" bond funds lost more than 35 percent in 2008) *available at* <http://advisor.morningstar.com/articles/article.asp?docId=16293>. In many instances, fund disclosure is inadequate to inform investors regarding the active management risk that they are taking. *Id.* ("Futures, interest-rate swaps, total-return swaps, credit default swaps, forward contracts, options, swaptions, and any number of other derivatives are typically buried in portfolio footnotes and endnotes, some of which are ambiguous or useless.").

⁶³ See Remarks of Andrew Donohue before the PLI's Investment Management Institute (Apr. 2, 2009) ("At a time when some 70 percent of actively managed funds underperform their benchmarks, if an investor or an investment adviser can not accurately identify who might outperform, what is the value proposition in taking on the risk for this variance in performance?") *available at* <http://www.sec.gov/news/speech/2009/spch040209ajd.htm>.

fees, violates an employer's fiduciary duty to the plan and its participants.⁶⁴ It is no less fundamental to minimum fiduciary standards to mandate that passively managed investment options be provided than it is to require at least three materially different types of investment options (as is currently required under ERISA). Defenders of the status quo argue that plan sponsors should have the freedom to refuse to offer a passively managed option, but this issue is a red herring.⁶⁵ It is the employee's choice, just as it is the employee's financial security, that is the issue. And employees should have the choice not to assume active management risk when investing for their retirement.

The Act takes two significant steps to address this fiduciary gap. First, the Act requires that, at a minimum, a plan offer either a passively managed U.S. equity or debt mutual fund.⁶⁶ This requirement takes the first step in ensuring that America's 401(k) beneficiaries are not forced to assume active management risk when investing for their retirement.⁶⁷ The Act in no way limits a plan sponsor's

⁶⁴ See *DiFelice v. U.S. Airways, Inc.*, 497 F.3d 410, 418 (4th Cir. 2007)(404(c) safe harbor "does not apply to a fiduciary's decisions to select and maintain certain investment options within a participant-driven 401(k) plan;" citing Department sources).

⁶⁵ To illustrate such Orwellian analysis, the industry recently testified *in opposition to* mandating passively managed investment options: "Eighty-seven percent of respondents in our survey agreed that the government should allow individuals to make their own investment decisions in DC retirement accounts and IRAs, and we agree." *Strengthening Worker Retirement Security*, hearing before the Education and Labor Committee, U.S. House of Representatives (Feb. 24, 2009) (testimony of Paul Schott Stevens, President, Investment Company Institute). Yet it is precisely *the mandating of passively managed investment options* that would "allow individuals to make their own investment decisions" to invest passively, whereas the industry position would deny individuals any guarantee of this freedom to choose.

⁶⁶ The Act uses the term "mutual fund," although participants would be benefited if non-mutual fund alternatives could also be used to serve this role. Additionally, the technical term "registered open-end investment company" would be clearer than the term "mutual fund."

⁶⁷ The Act also requires that each of these options "offer[] a combination of historical returns, risk, and charges . . . that is likely to meet retirement income needs at adequate levels of contribution." I recommend that this provision be revised and moved to another section of the Act. The requirement that plans not force participants to assume active management risk is a separate concept from the requirement that a plan offer an option that is designed to meet a participant's retirement income needs. In addition, a single passively managed equity or debt fund generally could not satisfy all participants' retirement income needs. A younger participant would not obtain sufficient inflation risk protection from most debt funds and an older participant would not obtain sufficient market risk

ability to offer actively managed investment options or require it to offer more than one passively managed option. The Act merely imposes the least intrusive standard necessary to ensure that participants are not forced to assume active management risk when investing in their 401(k) plans.

Second, the Act requires that the investment option disclosure document state whether each option is actively or passively managed and “set forth . . . the difference between active management and passive management.” This disclosure necessarily will draw participants’ attention to the nature of active management risk and the higher costs that active management entails, thereby enabling them to make a more informed choice between active and passive management. In this respect, the text of the bill could be improved by requiring that the document “explain,” rather than “set forth” this difference in order to ensure that all of this information is provided. In addition, it would be beneficial to insert “or a recognized asset class” after “index” in order to clarify that the passively managed option should not necessarily be required to match an established index, which can impose additional unnecessary expenses (this clarification probably could be left to the conference report).⁶⁸ Finally, Congress should consider directing the Department or SEC to develop guidelines regarding the meaning of “passive management.” Certain managers have developed products that, while claiming to reflect a passive management approach, actually operate like actively managed funds.⁶⁹

protection from an equity fund. A passively managed, properly designed age-based, target date fund could serve this provision’s intended purpose, but not without reforms designed to ensure that target date funds are prohibited from misleading investors about their portfolios. *See generally* Letter from Mercer Bullard, President and Founder, Fund Democracy, and Barbara Roper, Director of Investor Protection, Consumer Federation of America, to Senator Herb Kohl and Senator Mel Martinez (Apr. 2, 2009) *available at* <http://www.funddemocracy.com/targetdateltraging.pdf>.

⁶⁸ *See, e.g., Index Changes and Losses to Index Fund Investors*, 62 *Financial Analysts J.* 31 (2006) (investors in S&P 500 and Russell 2000 funds lose \$1 billion and \$2.1 billion, respectively, due to arbitrage around the time of index reconstitution) *available at* <http://ssrn.com/abstract=922296>.

⁶⁹ *See* Paul Lim, *The Indexing Wars*, U.S. News & World Report (May 7, 2007) (discussing debate regarding meaning of passively managed).

If the 401(k) Fee Disclosure Act is to provide full protection against in appropriate investment options, it should be amended to limit the amount of a participant's 401(k) account that can be invested in employer stock to 20 percent of their account value. Under current law, participants are permitted to invest 100 percent of their accounts in employer stock, notwithstanding that this allocation violates fundamental investment principles.⁷⁰ Permitting participants to invest 100 percent of their retirement assets in the stock of a single issuer when that issuer is also the participant's sole source of earned income is irresponsible.⁷¹ Yet many employers permit and effectively encourage their employees to invest in this manner.⁷² The effect can be devastating, as many Enron employees learned when that company declared bankruptcy. More than 60 percent of Enron's 401(k) assets, worth more than \$1.3 billion in early 2001, were invested in Enron stock.⁷³ It is irrational to prohibit defined benefit plans, which are placing the employer's assets at risk, from investing more than plan assets in employer securities, while permitting individual participants to bet 100 percent of their retirement on the securities of a single company. And there is no rational basis for granting tax deferral to 401(k) investments only to permit the gambling of 100 percent of a

⁷⁰ In 2007, 9.9% of 401(k) assets held by participants *in their sixties* were allocated to employer stock. See 2008 ICI Fact Book, at 93 (2008) available at http://www.ici.org/stats/mf/2008_factbook.pdf.

⁷¹ See *Private Pensions: Participants Need Information on the Risks of Investing in Employer Securities and the Benefits of Diversification*, GAO-020943 (Sep. 2002) available at <http://www.gao.gov/new.items/d02943.pdf>; Testimony of Paul Schott Stevens, *supra* note 65, at 11.

⁷² Twelve percent of employees whose plans offer employer stock have at least 60 percent of their plan assets invested in that option. See Jason Zweig, *Wall Street Lays Egg With Its Nest Eggs*, Wall St. J. (Sep. 28, 2008). The current financial crisis has exacerbated the problem because some employers are restricting or eliminating the employer stock option in response to the decline in the stock's value and presumably will restore the plan when the stock rises again. See Mark Bruno, *Corporates Rethinking Company Stock in 401(k)s*, Financial Week (Dec. 9, 2009) available at <http://www.financialweek.com/apps/pbcs.dll/article?AID=/20081209/REG/812089989>. This approach effectively formalizes a buy-high, sell-low strategy that is guaranteed to increase participants' losses.

⁷³ See *Enron Employee Ride Stock to Bottom*, CNN.com (Jan. 14, 2002) at <http://archives.cnn.com/2002/LAW/01/14/enron.employees/>.

participant's account on the stock of a single employer. The public policy purpose of granting tax deferral to 401(k) accounts is in no way served by allowing participants to invest 100 percent of their accounts. The beneficiaries of current policy are employers who seek a more friendly, pliable, stable market for their shares. If investments in employer securities were limited to 20 percent of participants' account balances, they would continue to be able to participate in the performance of their employers' stock inside their 401(k) plans *and* remain free to make additional investments in employer securities outside of their 401(k) on a non-tax-deferred basis.

IX. COST ISSUES

Regarding the issue of which parties should bear the cost of providing fee information, Congress generally should leave the allocation of disclosure costs to the marketplace. Each of the three principal providers of information to 401(k) beneficiaries – employers, plan administrators and investment option sponsors – has sufficient negotiating power to ensure that markets work efficiently to find the optimal allocation of costs among the different parties. For example, I recommend that beneficiaries' quarterly statements include uniform dollar fee disclosure, which would require the calculation of the dollar amount of fees that would have been paid by a hypothetical \$1,000 account. If the annual cost of producing that information were \$1.00 for the investment option sponsor, \$1.05 for the administrator, and \$1.10 for the employer, then one would expect the cost ultimately to be allocated to the investment option sponsor as the lowest-cost provider. Formally "allocating" the cost to the administrator, for example, would simply result in the administrator's paying the investment option sponsor to provide the information at lower cost, with the only economic difference being the added cost of negotiating the transfer of this responsibility from the administrator to the investment option sponsor.

Thus, allocating costs by rule will not change the ultimate allocation of costs, but it can be expected to increase total costs to the extent that the rule does not choose the most efficient information provider. In a competitive 401(k) market, all costs ultimately will be borne by the lowest-cost provider, because structures that allocate costs to higher-cost providers will lose market share to more efficient, lower-cost competitors.

Another aspect of cost allocation is the allocation of costs across different employers. The greatest risk of implementing new fee disclosure requirements is that they will increase the cost of 401(k) plans for small employers to the point that they will choose not to offer the plan at all. Congress should be sensitive to these relative cost burdens for small plans and to seek ways to minimize them, including by identifying disclosure and other requirements that could be modified or eliminated in order to reduce 401(k) expenses.⁷⁴ ***The 401(k) Fee Disclosure Act includes specific provisions that address these concerns and ensure that investor protection measures will not have unintended consequences for small employers.***

Finally, Congress should pay particular attention to the relative costs and benefits of fee disclosure reform, while keeping in mind that, to a great extent, a cost-benefit analysis of fee disclosure requirements must be based on economic principles rather than hard dollar analysis. The exact dollar amount of the benefit of fee disclosure simply cannot be measured, because there is no way to determine the

⁷⁴ See *85% of Small Business Owners Have High Regard for 401(k)s*, Money Management Executive (Apr. 17, 2009) ("Small business owners view having a solid retirement plan as critical, both personally and for employees, according to a survey of 1,000 people by SunTrust Bank. Nonetheless, nearly 40% do not offer one," with 90 percent citing cost as the overriding reason) available at <http://www.mmexecutive.com/news/-192318-1.html?ET=mmexecutive:e2298:43795a:&st=email>. Anecdotal evidence collected by the industry reveals that expenses of some of the 15 self-reporting plans studied with less than \$1 million in assets (out of approximately 288,000 plans of that size) paid 2.30 percent or more in total fees, or almost 6 times the average paid (0.42 percent) by a similarly small sample of plans with more than \$500 million in assets. See *Inside the Structure of Defined Contribution/401(k) Plan Fees: A Study Assessing the Mechanics of What Drives the "All-In" Fee*, Deloitte and Investment Company Institute (2009) available at http://www.ici.org/pdf/rpt_09_dc_401k_fee_study.pdf.

total reduction in expenses that will result from greater fee transparency and standardization. Based on its review of the empirical literature, however, the Department of Labor expected that its fee disclosure proposal would “result in the payment of lower fees for many participants. . . . as more fee transparency fosters more price competition in the market.”⁷⁵ The Department found a wide dispersion in 401(k) fees that it attributes “to market inefficiencies”⁷⁶ and estimated – “conservatively” – that “plan participants on average pay fees that are higher than necessary by 11.3 basis points per year.”⁷⁷ The Department’s findings are consistent with substantial evidence that investors are not sufficiently price sensitive, and enhanced price transparency, price standardization and comparative information should provide a powerful stimulus toward lowering the overall cost of investing by increasing price sensitivity. The steady migration of mutual fund investors to lower-cost mutual funds is partly, if not substantially, attributable to the high level of fee transparency mandated by the securities laws. ***The kind of fee disclosure reform embodied in the 401(k) Fee Disclosure Act will generate substantial net economic benefits to 401(k) participants.***

X. CONCLUSION

The 401(k) Fee Disclosure Act takes significant steps toward enhancing competition in the 401(k) marketplace and ensuring that plan beneficiaries have the fee information they need to make informed investment decisions. The Act adheres to the fundamental principle that fee disclosure should be designed not for the self-directed, fee-sensitive investor, but rather to increase

⁷⁵ *Fiduciary Requirements for Disclosure in Participant-Directed Individual Account Plans*, 73 Fed. Reg. 43013, text accompanying notes 14 – 15 (July 23, 2008) (citing James J. Choi, David I. Laibson, and Brigitte C. Madrian, *Why Does the Law of One Price Fail? An Experiment on Index Mutual Funds*, NBER Working Paper W12261 (May 2006) (finding “that presenting the participants with a comparison fee chart, and not just a prospectus, reduced the fees paid by 12% to 49% depending on the group studied”)).

⁷⁶ *Id.* at text accompanying note 11 (citing *The Economics of Providing 401(k) Plans: Services, Fees, and Expenses*, Investment Company Institute (2006)).

⁷⁷ *Id.* at text accompanying note 13.

awareness of fees and their impact on investment returns among those retirement plan beneficiaries who are not fee-sensitive. The Act will ensure that services providers and plan sponsors must provide participants with the information they need, in a form they can understand, and at a time when it is useful to them in making and assessing their investment decisions. ***The Act is not just a giant leap forward in the 401(k) marketplace; it introduces reforms that are long overdue across the spectrum of financial services in America.***

EXHIBIT A

Fee table:

Investment Option	Fund Expenses	Total Plan Expenses	Illustrative Annual Fee Paid on \$1,000 Balance
Stock Fund	0.80%	1.00%	\$10.00
<i>Industry Average</i>	<i>0.70%</i>	<i>0.88%</i>	<i>\$8.80</i>
Bond Fund	0.50%	0.70%	\$7.00
<i>Industry Average</i>	<i>0.45%</i>	<i>0.63%</i>	<i>\$6.30</i>
Balanced Fund	0.65%	0.85%	\$8.50
<i>Industry Average</i>	<i>0.60%</i>	<i>0.78%</i>	<i>\$7.80</i>

Additional Expenses:

Small Account Fee: \$2.50/quarter

Redemption Fee: 1.00%