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**Via Electronic Transmission**  
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Office of Regulations and Interpretations  
Employee Benefits Security Administration  
Room N-5655  
U.S. Department of Labor  
200 Constitution Avenue, NW  
Washington, DC 20210

**Re: Proposed Regulations Under Section 408(b)(2) of ERISA**

Dear Sir or Madam:

The Segal Company is a major provider of actuarial, employee benefits and human capital consulting services to employers and employee benefit plans throughout the United States, and the largest such company serving multiemployer plans. The Segal Company's subsidiary, Segal Advisors, Inc., advises plans and plan sponsors on the development of investment policies and assists in selection and monitoring of investment managers; it is a Registered Investment Advisor under the Investment Company Act of 1940. That is the only entity within Segal that provides investment-related advice or services. Segal is also a broker for selected clients' fiduciary liability insurance and, for those health and welfare funds that choose to be insured, their health, disability and life insurance. Except with respect to these insurance services, which represent a very small percentage of our business, all of Segal's businesses are compensated directly by our clients, and we do not participate in any third-party, revenue-sharing or similar arrangements.

We are writing to recommend that the December 13, 2007 proposed regulations regarding required fee disclosures in connection with a reasonable contract or arrangement under Section 408(b)(2) of ERISA be more directly targeted to achieving their goals. Specifically, we believe the Department should reconsider application of the rules to the relatively narrow class of service providers with uncomplicated fee-for-service and/or flat rate compensation arrangements, as long as the services to be performed and the flat fees and the bases for any other charges are always fully disclosed. These are arrangements that do not present the challenges that have in part motivated the Department to regulate in this area, because they have traditionally been completely transparent to plan sponsors. We believe that as long as they stay as straightforward and transparent as they are now, plan sponsors and participants will be fully protected even if the service providers are not subject to new rules.

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## Introduction

The Department proposes to apply the new rules to three categories of contracts with service providers. A contract or arrangement will be covered if it provides for services from any of the following providers:

1. Providers that provide (or may provide) services as a fiduciary under ERISA or the Investment Advisers Act of 1940.
2. Providers that provide (or may provide) banking, consulting, custodial, insurance, investment advisory (plan or participants), investment management, recordkeeping, securities or other investment brokerage, or third party administration services, regardless of type of compensation.
3. Providers receiving (or that may receive) indirect compensation in connection with accounting, actuarial, appraisal, auditing, legal, or valuation services.

(“Category 1, 2, and 3 Providers”) 29 C.F.R. §2550.408b-2(c) (proposed).

We understand that the proposed rules are designed to address recent changes in the way services are provided to plans and compensation is paid to the providers. In particular, the explosive growth of defined contribution plans, especially 401(k) plans, has led to a significant rise in participant-directed investing and greater involvement of investment companies, mutual funds, and other investment-related entities in employee benefit plans. The complexity of investment industry services has made it difficult for plan fiduciaries and participants to identify and understand all of the costs associated with the services, and to identify potential conflicts of interest.

On the other hand, some service providers have been providing the same services for many years, under straightforward compensation arrangements that have not changed. For example, persons providing legal, actuarial, and audit services (“Category 3 Providers”) have typically billed plans using a combination of flat fees for some services, and hourly billing rates for others. The Department states in the Preamble to the proposed regulation that it does not think that additional disclosures regarding these arrangements are needed as a general matter, so it proposes to subject these providers to the new rules only when they receive indirect compensation (*i.e.*, compensation from a party other than the plan) in connection with their services to the plan.

We are glad to see that the Department recognizes the validity and transparency of the compensation arrangements that Category 3 providers have long had in place. We are concerned, however, that under the proposed rules, a Category 3 Provider could too easily fall under Category 2. For example, the Category 2 term “consulting” could be construed broadly and thereby capture Category 3 Providers and others with historically uncomplicated, straightforward compensation structures. We respectfully submit that the term “consulting” is

simply too broad and vague, and should not be included as a separate category of the services covered by the proposed rules. Rather, consulting of all types should be included in Category 3 (if not otherwise covered in the earlier categories), so that any arrangement that involves direct or indirect 3rd-party payments would be brought within the new disclosure regime.

The fee-for-service and flat rate arrangements that benefits consultants and certain other types of providers use are nothing like the sophisticated layered arrangements that appear in the investment industry. Where a plan's relationship with a provider requires it to pay nothing but a pre-established flat fee or hourly charges for a service, application of the same rules that are warranted for providers of investment products could result in confusion, not greater transparency. We therefore suggest that the proposed rules not apply to providers of services listed in Category 3 (and related consulting services), as long as the services are provided under arrangements using only hourly charges or flat rates, or a combination of both, and no other compensation of any type is paid for a service to which the hourly charges or flat rate applies. We believe that this can be accomplished by eliminating the term "consulting" from Category 2.

We further submit that providers and plans be given enough flexibility to revise or supplement their arrangements during the term of a contract, including the ability to agree to different charges for work already performed. This could mean the addition of new projects subject to time charges or a flat rate, or an agreed-upon increase to applicable to time charges, applicable to services performed prior to such agreement.

**I. A single focus on the types of services that are provided overlooks the key factor for determining whether new rules are necessary – the simplicity and transparency of the compensation arrangement currently in place.**

We believe that dividing the world of service providers into the three categories listed here may not be the best way to determine which compensation arrangements should be subject to new, detailed disclosure rules and procedures. First, some of the terms used are too broad and threaten to undercut distinctions that the Department appears to have intended. For example, strictly speaking, the term "consulting. . .services" of Category 2 could be broad enough to cover all of the services described in Category 3, including accounting, actuarial, appraisal, auditing, legal, or valuation services. Every time that a lawyer speaks to a client, he or she is consulting with the client. Similarly, when actuaries serve clients, they are in some sense "consulting," even when doing no more than explaining the results of a valuation. Indeed, an actuary who simply submits a valuation report is not providing what a plan sponsor needs, which is an explanation of the implications and possible actions to be taken in light of them.

In the Preamble to the proposed regulations, however, the Department explained that it did not believe that requiring every contract or arrangement with Category 3 Providers to satisfy the proposed rules would be "appropriate or yield helpful information to plan fiduciaries." We agree, and we submit that the reason for this is not necessarily the type of services provided, but is instead the type of compensation arrangement that is in place between some of these providers and their client plans. Accordingly, we respectfully submit that the undifferentiated term "consulting" be deleted from the Category 2, which would make all types of consulting automatically covered by the proposed rules, and added to Category 3.

**A. A compensation arrangement based only on time and/or flat rate charges does not present the types of problems the proposed rules are designed to address.**

We understand that the genesis of this proposed regulation is in the expanded prominence of defined contribution retirement plans, increased use of multiple layers of charges in investment products and in the investment management/record-keeping/plan administration industries. Plan fiduciaries are aware of some of the charges, unaware of others, and do not understand how certain charges are calculated or what the total cost is to their plans and, accordingly, their participants. By contrast, a compensation arrangement under which a provider receives hourly fees or a flat-dollar amount for its services is easy to understand and has never been a source of confusion for fiduciaries.

We submit that as long as plan fiduciaries are apprised of the specific services that are to be provided, and are aware of the hourly rates or flat fees that are to be paid, these compensation arrangements should not be subject to additional regulation. If the term “consulting” is eliminated from the proposed rules, service providers operating under these arrangements would not be treated as covered, unless they are otherwise described.

To assure full protection of plan sponsors and plan participants, the Department should be very specific as to the requirements that would have to be met:

1. The plan and the service provider would have to agree on the flat fee amount that would apply to particular services; both sides would be required to consent to any changes.
2. The parties would have to agree on the services that are covered by the flat fee; both sides would be required to consent to any changes.
3. The provider would have to state the basis for its charges, and describe the types of services that would be billed on that basis. The provider would be required to advise the plan as early as possible about rate increases, but no increase would go into effect unless both parties agree to it.

We are not seeking to limit disclosures to plan fiduciaries; we are instead hoping to limit the new rules to those situations presenting the concerns the rules are designed to address. To the extent that an element of compensation other than an hourly charge or a flat fee complicates the arrangement, the provider would have to comply with the regulations.\* Accordingly, the number of arrangements subject to the suggested exclusion should be in line with the Department’s expectations in developing the Category 3 list of providers.

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\* We assume, and ask that the Department confirm, that a provider can have more than one arrangement with a client employee benefit plan. If an arrangement for certain services includes only hourly charges and flat fees, then as discussed above, that arrangement should not be subject to the new rules. If that same provider offers another service under a separate arrangement with the client plan, and if that arrangement involves insurance commissions, then only the commission-based arrangement should be subject to the regulations.

If the Department wishes to retain the term “consulting” as part of Category 2, then we submit that the rules should expressly exclude from its meaning providers described in Category 3, who operate under the hourly charge and/or flat fee arrangements described above. Otherwise, Category 2 would completely swallow, and thus negate, the exclusions the Department intended in proposing Category 3. Narrowing the meaning of the term preserves the exclusions the Department intended.

**B. The proposed rules present practical problems for parties to hourly charge and flat fee arrangements, without adding corresponding benefits for plan sponsors.**

The proposed rules raise some concerns about a number of practices that are standard today and protective of plans. The proposal anticipates advance notice of all services and related fees, and disclosure of any material changes within a 30-day period. Under many long-time arrangements between providers and plans, new services and rates may not be formally memorialized within the Department’s preferred timeframe, but plans are fully protected because they do not have to pay unanticipated fees until plan fiduciaries have agreed that the fees are appropriate. We request clarification that the Department is not seeking to prevent retroactive adjustments in fees as long as the plan is not obligated to pay compensation to which it has not agreed.

**1. Supplemental Services**

A typical retainer agreement between a provider and a plan would include a flat fee for basic services, and hourly rates for additional or supplemental services. For example, an actuarial and consulting firm might perform an actuarial valuation for a pension plan for a flat fee. That fee might also cover general consulting on questions that arise during the year. Supplemental services for that plan might include compliance and operational reviews; preparation of participant communications; special analyses and reports in connection with mergers, spinoffs, a mass withdrawal, or a plan termination; and financial modeling related to legislative and regulatory activities.

At the time a retainer agreement is negotiated and signed, the parties do not know what supplemental services may be necessary, so they cannot describe them in advance. The proposed rule contemplates this scenario and anticipates that there will be material changes to the arrangement. What concerns us, however, is whether the Department’s required timing will be workable. In the case of many new services that a provider is asked to perform, it might be difficult to meet a 30-day deadline for describing them in writing, indicating the appropriate flat fee or hourly rate and documenting the exchange formally. Trying to do so would add an unnecessary level of complexity and bureaucratic-type process to the existing, well-functioning provider/plan relationship.

**2. Unanticipated Time and Effort**

A more complicated scenario arises where the type of services may have been adequately described in a written agreement between a plan and provider, but the parties have not accurately anticipated the level of work that will be required to perform the services. For example, a typical flat fee provision for basic services may say that the fee covers the reasonable and customary time involved in providing those services. The provision might go on to say that if unanticipated

factors require the provider to invest significantly more time than either party expected, the provider will bill the plan for that time at the hourly rates in effect.

One example is a plan (either single employer or multiemployer) that had been well-funded historically and was expected to stay well-funded. Then, because of a sudden severe market decline like that experienced in recent months, the plan's outlook reverses and the plan sponsor (either the employer or the multiemployer board of trustees) has to quickly prepare for the implementation of benefit restrictions. For either type of plan, this would include a thorough review of all funding, actuarial and implementation options, participant communications, employer communications, government filings and the development of a correction program. The benefit restriction issue would involve a great deal of unanticipated work for the retirement consultant, but it would not make sense to delay the project to renegotiate an optimal compensation arrangement in time to meet the regulation's 30-day deadline.

Another example would be the mid-contract decision of a health plan to add a new benefit or a new type of vendor, such as a pharmacy benefit manager ("PBM"). This could require substantial effort by the consultant to vet the candidates, assemble the data they need to bid on the business, digest and array their responses so the client can make an informed choice and then negotiate the best terms and conditions with the successful vendor on behalf of the client, all within a time frame that accommodates the deadlines on the price quote, the client's deliberative processes, and the need for a conclusion in time to adapt the administrative arrangements and communicate with participants by the scheduled start date for the new offering. Again, it would not make sense to put the substantive work on hold to make time for an immediate negotiation between service provider and plan over the cost of the additional work.

A final example would involve an actuary that expected data collection for a valuation to involve a certain range of hours, but then found, for reasons related to the plan's administrative arrangements, that the effort required time significantly exceeding the range. If the collection effort exceeded the parties' expectations because of bad data or some other factor not created by the actuary, a supplemental billing could be appropriate. It would not make sense for the actuary to have to stop midway through the project to renegotiate the arrangement in time to meet a 30-day deadline – and possibly endanger the timeliness of the valuation.

Instead, the provider should be permitted at any time to issue a retroactive bill for services performed or time invested that was not described in detail in the original retainer agreement. To protect the plan, retroactive billing would be permitted only if the plan fiduciaries are free to evaluate the facts and decide whether to consent to the additional charges. In other words, the provider would not receive compensation that was not specifically set out in the original agreement unless the appropriate fiduciaries have determined that the additional compensation is reasonable.

## **II. The Department should consider addressing the complications that insurance commissions can create for compensation arrangements.**

As noted above, we are not seeking to exclude from the proposed rules an arrangement to the extent that it includes any compensation component other than hourly time charges and flat fees, such as a commission or other indirect compensation. We wish to point out, however, that

providers, including insurance brokers and agents, are often not permitted by state insurance law to structure a compensation arrangement in whatever manner they and their client would prefer. Indeed, in many cases, a broker is required to receive a commission to place insurance for a client plan. While the broker who is also a provider of other services (under the same compensation arrangement with the client) may want to use that commission as an offset against other fees that it charges the client, some states may consider that to be an impermissible rebate. Providers would welcome guidance from the Department regarding its view of appropriate methods for handling commissions. We suspect that in at least some cases, there may be ways to report and otherwise handle insurance commissions that would satisfy the Department that plan sponsors and plan participants are adequately informed and protected.

### **Conclusion**

We appreciate the opportunity to comment on the proposed regulations under section 408(b)(2) of ERISA. We would be pleased to provide the Department with any additional information it might need, and to answer any questions.

Sincerely,

Judith F. Mazo  
Senior Vice-President and Director of Research



Margery Sinder Friedman  
Senior Vice President and Assistant Director of Research