From: arnoldandkadjan@aol.com [mailto:arnoldandkadjan@aol.com]
Sent: Monday, February 11, 2008 1:20 PM
To: EBSA, E-ORI - EBSA
Subject: Comments Regarding Proposed Regulation Concerning Reasonable Contract or Arrangement

February 11, 2008

Via-E-mail

e-ORI@dol.gov
and www.regulations.gov

Re: Comments Regarding Proposed Regulation Concerning Reasonable Contract or Arrangement under Section 408(b)(2) by Chicago Painters and Decorators Pension Fund, Chicago Painters and Decorators Welfare Fund, NECA-IBEW Local No. 176 Defined Contribution Pension Fund, NECA-IBEW Local No. 176 Welfare Fund, Automobile Mechanics Local No. 701 Union and Industry Pension Fund and Automobile Mechanics Local No. 701 Union and Industry Welfare Fund

Dear Sir or Madam:

The following represents the comments of six Taft Hartley multi-employer plans, the Chicago Painters and Decorators Pension Fund, the Chicago Painters and Decorators Welfare Fund, the NECA-IBEW Local No. 176 Defined Contribution Pension Fund, the NECA-IBEW Local No. 176 Welfare Fund, the Automobile Mechanics Local No. 701 Union and Industry Pension Fund, and the Automobile Mechanics Local No. 701 Union and Industry Welfare Fund regarding the Proposed Regulation Concerning Reasonable Contract or Arrangement found at 72 Fed. Reg. 70998 (Dec. 13, 2007). As discussed more fully below, it is the position of these plans that the Regulations should contain additional language which would establish a per se rule that a service provider's contractual arrangement with a plan is not reasonable if it calls for either a plan or a plan fiduciary to indemnify a service provider.

The fiduciaries of these plans face a consistent struggle whenever they negotiate contracts with service providers regarding the issue of indemnification of these providers. In at least 80% of contracts regarding matters as diverse as investments, banking, pharmacy provider arrangements, preferred medical provider contracts and other necessary plan services, these plans, face demands from service providers for indemnification provisions. Frequently this demand will result in costly, protracted negotiations for the Funds which could be avoided if a clear rule was established precluding service providers from requiring that they receive indemnification from either the plan or plan fiduciaries. In addition, the fiduciaries are left with uncertainty concerning whether their successful or unsuccessful efforts to limit indemnification are sufficient to satisfy their fiduciary duties to their respective plans under ERISA.

Current statutes and regulations fail to provide plan fiduciaries guidance sufficient to assure them that their conduct will satisfy the terms of these regulations or to convince service providers that it is necessary for them to modify their contracts in order to satisfy laws and policies under ERISA. It is very clear under relevant statutes, that there is a bar against any indemnity provisions which would indemnify a fiduciary against a fiduciary breach. See ERISA Section 410(a), 29 U.S.C. § 1110(a). Obviously, any indemnification provision would be invalid if it relieved the service provider from any liability for violation of fiduciary duties. However, there have been cases in which a service provider has attempted to include in contracts provisions which would indemnify a service provider against a fiduciary breach. Further, in one recent instance one of these plans has found itself faced with a different approach which would require the plan fiduciaries themselves to indemnify the service provider for the breach of other fiduciaries. This is particularly difficult for Taft Hartley plans, where the plan fiduciaries are the individual members of the Board of Trustees, rather than a plan sponsor corporation. In these instances, because insurance is unavailable to compensate them for this indemnification, the individual Trustees are placed in the untenable position where their personal assets are at risk if they were to agree to the service provider's indemnification demand.

The problem, however, extends beyond the area of prohibited indemnification for a fiduciary breach. Even when ERISA Section 410(a) not directly implicated, an ERISA plan lacks broad freedom to agree to an indemnification provision in cases other than those involving a service provider's fiduciary breach. Although there may not be an automatic fiduciary violation in agreeing to these terms, the relevant legal authorities leave open the clear possibility that Trustees could be guilty of fiduciary violations in agreeing to particular indemnification provisions.

The problems fiduciaries face in these circumstances were discussed by the Department of Labor in Department of Labor Opinion Letter 2002-08A (August 20, 2002). In that case a service provider attempted to obtain limitation of liability and indemnification provisions in a contract with an ERISA plan. The DOL emphasized that plan trustees "must engage in an objective process designed to elicit information necessary to assess the qualifications of the provider, the quality of services offered, and the reasonableness of the fees charged in light of the services provided." DOL Opinion Letter 2002-08A. As part of this inquiry it is necessary to examine "contractual provisions . . . relating to limitations of liability and indemnification." Id. Although indemnification provisions were considered not to be per se unreasonable or imprudent except in cases where they require indemnification for fraud or willful conduct, Trustees will violate their fiduciary duties under ERISA if they simply agree to indemnification provisions without considering "the reasonableness of the arrangement as a whole and the potential risk to participants and beneficiaries." Id. The minimum duty required in all cases involving indemnification provisions is for the Trustees to "assess the plan's ability to obtain comparable services at comparable costs either from service providers without having to agree to such provisions, or from service providers who have provisions that provide greater protection to the plan." Id. In addition, the Trustees must also:

assess the potential risk of loss and costs to the plan that might result from a service provider's act or omission subject to a proposed limitation of liability or indemnification provision. In making such an assessment, a fiduciary should consider the potential for, and outside limits of, such a loss as well as any additional actions that may be available to the plan to minimize such a loss.

Id. Obviously, the Trustees task is much more comprehensive than just agreeing to the service provider's self-serving "comfort" with an indemnification provision that can result in a fiduciary breach. This is especially true in light of the Plan's fiduciary insurance provisions which exclude indemnification of service providers from the scope of covered losses.

The problem fiduciaries face in these circumstances is that they generally must negotiate with a service provider who will attempt to convince them that the duties set forth by the Department of Labor in Opinion Letter 2002-08A either do not exist or can be satisfied by agreeing to service provider demands which may not, in fact, satisfy the Trustees' fiduciary duties. In implementing the requirements the Department places upon fiduciaries confronted with service provider requests for indemnification provisions, the Department has provided general direction that Trustees must determine whether they can obtain "comparable services at comparable costs . . . from service providers who have provisions that provide greater protection to the plan." DOL Opinion Letter, 2002-08A. This is a very difficult process for fiduciaries who must analyze each individual marketplace for services and determine whether they could obtain services elsewhere without indemnification terms which present a risk of fiduciary duty for the Trustees. Trustees, including the Trustees of each of these plans, have often faced the need to solicit additional bids for services after they had thought they had chosen a provider who would be satisfactory, but then were presented with unacceptable service provider indemnification provisions.

Establishment of a per se regulation forbidding indemnification of service providers from either plan assets or plan fiduciaries will avoid the costly and lengthy negotiations which plan fiduciaries now must experience in order to achieve a satisfactory resolution of this issue and will also relieve these Trustees from the uncertainty faced in every case regarding whether they have done enough to avoid fiduciary breach. In making the absence of indemnification a requirement for all service provider contracts, it will be possible for Trustees to enter contracts based on important considerations of price and quality of service without being required to engage in heated negotiations to remove indemnity provisions or to create indemnity provisions which may be sufficient to satisfy an amorphous standard of fiduciary duty. Further, it is unlikely that creation of this requirement will result in a significant loss of choice among service providers as the market for various services to ERISA plans is sufficiently lucrative to ensure that service providers will continue to participate in that market even if they cannot have indemnity provisions in their agreement.

Based upon the foregoing, the above-referenced plans strongly urge that the Department of Labor amend the proposed regulation to include a provision establishing that a contract is not reasonable if it includes a provision requiring a plan or plan fiduciaries to indemnify a service provider.

Sincerely,

ARNOLD AND KADJAN

By:
Hugh B. Arnold