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October 18, 2006

VIA ELECTRONIC MAIL

John J. Canary, Division Chief
Office of Regulations and Interpretations
Employee Benefits Security Administration (EBSA)
Room N-5669, U.S. Department of Labor
200 Constitution Avenue, NW
Washington, DC 20210

RECEIVED
OFFICE OF REGULATIONS
AND INTERPRETATIONS
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Re: **Form 5500 Regulation Revisions (RIN 1210-AB06)**

Dear Joe:

We appreciate the opportunity to comment on U.S. Department of Labor's (DOL) Proposed Form 5500 Regulation Revisions (the "Proposed Revisions"). The provision of marked-up versions of the Form 5500 and corresponding instructions by the DOL on its website has been very helpful. Additionally, the DOL's provision of a streamlined reporting form for certain small employers on the Form 5500-SF (Short Form) will be invaluable for these plan sponsors.

We also commend the DOL for its effort to bring better disclosure to plans, participants and fiduciaries. We believe that increased disclosure will result in a better understanding of fees and expenses as well as beneficially impact participants' benefits. Additionally, this disclosure will facilitate the efficient operation of a competitive marketplace. However, we have suggested that the DOL make some minor changes to the Proposed Revisions to facilitate more accurate and uniform disclosure. Our comments focus on the reporting of compensation received by service providers to retirement plans, that is, the information reported on Schedules A, C, H, I and the Short Form. Please let us know if you would like us to provide examples where there is a need for clarification.

GENERAL BACKGROUND INFORMATION

We believe that all plans, large and small, should have certain basic information about the expenses being paid by the plan, regardless of whether they are direct or indirect. Those expenses should be divided out into three categories:

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- Investment-related expenses (“investment expenses”).
- Recordkeeping and administration expenses, which could also include communications, compliance, and other services related to the operation of a plan (“administrative expenses”).
- Investment consulting, brokerage or advisory services (“advisory expenses”).

The first category, investment expenses, would consist of the expenses associated with each of the investments in a plan. For example, for a mutual fund, it would be the expense ratio of the mutual fund, including the management fee of the advisory firm. For a group annuity contract, it would also include any separate charges in the group annuity contract that were attributable to the investments (but not to the administration). There would then be subtracted, from that total number, the amount of any revenue sharing, or other fees or expenses, that were to be applied to either of the other two categories. That would include, for example, fees or commissions that would be paid to the intermediary, such as the broker, consultant or adviser. It would also include any subsidy for the recordkeeping or administration. The resulting net number would be the true cost of the investments.

The second category, administrative expenses, would include any charges specifically for recordkeeping, administration, compliance, communications, and other operational services, as well as any revenue sharing or other payments from the first category, the investments.

The third category, advisory services, would include any amounts paid by the plan to consultants, advisers, or brokers, as well as any indirect payments (that is, any payments or benefits from any source, but most likely from the investments or companies related to the investments). That would include, for example, finder’s fees, 12b-1 fees, production bonuses, and so on.

Equipped with this information, plan sponsors and fiduciaries would be in a position to evaluate the services that they are receiving in each of those three categories, with the costs properly allocated for purposes of that comparison. While no system is perfect, and this one is not either, the information would be a higher quality than is currently generally available, and would be much more useful to fiduciaries in performing their duties.

In our estimation, it is very difficult, if not almost impossible, for fiduciaries to properly assess the value of the investments and services without this kind of allocation and reporting of expenses. For example, if a plan were to use index funds or institutional class shares of mutual funds, which paid little if any revenue sharing, the plan or the employer would necessarily be required to pay additional amounts for advice, recordkeeping, administration and compliance. However, if they use retail class shares, which would be considerably more expensive, many, if not all, of those services would be paid for by the revenue sharing from the higher cost

investments. Without some allocation, it is very difficult to determine whether a plan is overpaying or paying a reasonable amount for the services. In other words, it would be difficult for fiduciaries to compare the costs and services of different alternatives and of different providers.

As a result, we believe that all providers, regardless of industry and regardless of whether or not bundled, should be required to segregate revenues, expenses, and revenue sharing type payments into those categories.

While some providers may argue that it is difficult or expensive to provide the information in that format, we have difficulty understanding that argument. For example, providers should know, based on their internal accounting practices, at least reasonable estimates of the costs of each of their operations, as well as the profits from one activity that are used to subsidize another, less profitable, activity. (While the knowledge of the costs, subsidies and profits need not be reported, they do enable the provider to properly allocate, at least in an estimated basis, appropriate amounts of costs and revenue sharings--in other words, the economic expense to the plan of the three categories of activities.) Keep in mind that these are sophisticated financial institutions with in-depth financial capabilities and analysis, as well as reporting and accountability functions that are used to evaluate the profitability of their various lines of business. Of course, exact numbers may not be available, but reasonable estimates should be satisfactory.

SUMMARY OF COMMENTS

The following is a summary of our recommendations.

- ***Clarification of Definitions.*** The Proposed Revisions do not provide definitions for all of the terms used. We suggest that definitions and examples be provided for all terms that are not defined in ERISA. In fact, the DOL may even want to consider including a definitions sections. By defining terms, there would be less confusion regarding whether a portion of the Short Form and/or Form 5500 applies with respect to a particular entity.
- ***Details Regarding Amounts Reported.*** The Proposed Revisions do not provide sufficient information regarding the amounts to be reported. We recommend that additional details be included in the Proposed Revisions that clarify the fees to be reported.
- ***Neutral Reporting for All Types of Providers.*** The information reported by plans is not neutral as to different types of providers. We recommend that the fee disclosure requirements be the same regardless of the type of investment provider used by the plan.
- ***Total Cost Approach.*** The Proposed Revisions provide that different amounts are disclosed for small plans rather than large plans. We recommend that the amounts

disclosed reflect the total costs paid by the plan, regardless of the plan's size. While we agree that the amounts of detail reported should be less for small plans, we believe they should still report the total amounts paid for all service providers.

- ***Separation of Payment and Conflict of Interest Issues.*** The proposed Schedule C requires both information regarding amounts paid by the plan as well as amounts paid that could result in potential conflicts of interest. We suggest that the Form 5500 be divided into two sections. The first section would address payments out of plan assets, while the second section would address potential conflicts of interest.
- ***Coordination with ERISA Section 408(b)(2).*** We understand that the DOL is in the process of revising the regulation under ERISA section 408(b)(2) with respect to the reasonable contract or arrangement prohibited transaction exemption. We suggest that the DOL coordinate the disclosure and reporting requirements of the proposed Form 5500 revisions and the anticipated ERISA section 408(b)(2) regulations.

DETAILED COMMENTS

I. Clarification of Reporting Requirements

The instructions do not clearly detail the types of information service providers need to give to plans for reporting purposes. Although the language is written broadly, it does not provide sufficient details to determine under which circumstances it applies as well as whether the amounts include certain related items.

A. Clarification of Definitions

The Proposed Revisions do not provide definitions for all of the terms used. As a result, it is unclear whether particular portions of the Short Form and Form 5500 apply to certain entities. For example, the Proposed Revisions state that the total amounts of salaries, fees and commissions paid to administrative service providers must be reported on the Short Form and Schedule I. The Proposed Revisions provide examples, but do not define the term "administrative service provider." To further complicate matters, Schedule H uses different terminology. Instead of reporting amounts paid to administrative service providers, it reports fees paid for "outside accounting, actuarial, legal and valuation/appraisal services."

The most obvious interpretation of the term "administrative service provider" is anyone who provides services to the plan. However, this is not specified in the Proposed Revisions. As a result, it suggests that the term is more limited than all service providers to the plan, yet, the limitation cannot be determined.

Similarly, heightened disclosure requirements apply for certain specified service providers, including “securities brokerage (stock, bonds, commodities), insurance brokerage or agent, custodial, consulting, investment advisory (plan or participants), investment or money management, recordkeeping, trustee, appraisal, or investment evaluation.” However, these terms are not defined.

If you would like more information and/or examples regarding potential areas for confusion, please let us know.

We suggest that definitions and examples be provided for all terms that are not defined in ERISA. In fact, the DOL may even want to consider including a definitions sections. By defining terms, there would be less confusion regarding whether a portion of the Short Form and/or Form 5500 applies to a particular entity.

B. Details Regarding Amounts Reported

The Proposed Revisions do not provide sufficient information regarding the amounts to be reported. They would require the “total fees paid” to be reported on the Short Form and Schedules H and I. The instructions for the Short form and Schedule I state “administrative service providers (salaries, fees, and commissions) include the total fees paid...by the plan...” The instructions for Schedule H state “include the total fees paid...by the plan for outside accounting, actuarial, legal, and valuation/appraisal services.”

Although the term “total fees paid” is very broad, it is not clear what amounts it includes. For the Short Form and Schedule I, the term “administrative service providers” is not defined. Consequently, it is not entirely clear which service providers this item covers.

Additionally, the Proposed Revisions do not specify whether “total fees paid” includes indirect compensation. Although the Preamble for the Short Form refers to direct compensation, the instructions for the Short Form and for Schedule I do not include this clarification. Because these schedules and this portion of the Short Form are structured like balance sheets, it appears as though it would not include indirect compensation. However, it is not clear.

In the event only direct compensation is to be reported, it is not entirely clear whether certain types of compensation would be direct or indirect. For example, we assume that compensation would be considered direct if a third party holds plan assets and pays it to a service provider at the direction of a fiduciary. Do you agree? Additionally, does “indirect” refer to compensation that doesn’t have a direct and immediate impact on the balance sheet for the plan?

The Proposed Revisions also do not specify what information bundled service providers should provide plans for this item. For example, suppose an insurance company receives 75 basis points (bps) from a plan. It pays 50 bps of the amounts received to a broker. The amounts paid to the broker is reported on Schedule A. The insurance company would not know whether to report the 75 bps or 25 bps (75 bps less the 50 bps paid to the broker) to the plan for reporting purposes.

Finally, the lack of clarity in the Proposed Revisions could result in the double-counting of fees paid. For example, if a provider or adviser charges the plan a flat percentage or a flat dollar amount, but then offsets that by revenue sharing receipts, they should not be required to report both, since that would be duplicative. They should only be required to report the charges with an explanation that all revenue sharing will be offset against the charges thereby reducing the net direct cost to the plan.

We recommend that additional details be included in the Proposed Revisions that clarify the fees to be reported.

II. Uniform Disclosure Requirements for Investment Providers

The information reported by plans is based on the type of entity that provides the plan's investments. Different information is reported for an insurance company on Schedule A than is reported for other types of investment providers on Schedule C.

A. Neutral Reporting for All Types of Providers

It is important that the information be reported in a manner that is neutral as to different types of providers. For example, much of the information given to plan sponsors today is in a format dictated by the industry of the provider, for example, securities laws disclosure requirements, insurance industry disclosure formats, and so on. The reporting and disclosure related to participant-directed plans should not be dictated by the laws regulating the industry of the provider, but instead by the needs of fiduciaries of participant-directed plans.

We recommend that the fee disclosure requirements be the same regardless of the type of investment provider used by the plan.

B. Total Cost Approach

The Proposed Revisions provide that different amounts are disclosed for small plans rather than large plans. Pursuant to the Proposed Revisions, small plans would file either

the Short Form or the Form 5500, including Schedules A and I.¹ Small plans also need to know the compensation paid. As a result, there should be similar reporting for all types of investments. For example, there should be reporting similar to the Schedule A for brokers' compensation for the sale of mutual funds and other investments in plans. As a practical matter, fiduciaries of small plans are typically not aware of expenses such as finder's fees paid to brokers. Large plans would file the Form 5500, including Schedules A, C and H.²

The amounts of information service providers will need to disclose for plan reporting purposes varies based on the plan's size. Small plans, including Short Form filers will need to receive a total of the fees paid to administrative service providers and Schedule A.³ Schedule A reports "all insurance fees and commissions directly or indirectly attributable to the contract or policy" of the plan. These amounts include "sales and base commissions and all other monetary, and non-monetary forms of compensation..." Large plans report detailed information on Schedule C regarding amounts paid to all service providers who receive at least \$5,000 in total direct and indirect compensation (including non-monetary amounts) from the plan or any other entity other than the plan sponsor in connection with services provided to the plan or their position with the plan. Additionally, large plans report the total fees paid by the plan for outside accounting, actuarial, legal and valuation/appraisal services. They also receive the Schedule A from insurance companies.

We recommend that the amounts disclosed reflect the total costs paid by the plan, regardless of the plan's size. While we agree that the amounts of detail reported should be less for small plans, we believe they should still report the total amounts paid for all service providers.

III. Separation of Payment and Conflict of Interest Issues

The proposed Schedule C requires both information regarding amounts paid by the plan as well as amounts paid that could result in potential conflicts of interest. The manner in which the

¹ Small plans are defined as plans that cover fewer than 100 participants as of the beginning of the plan year. A small plan may file the Short Form if: (1) the plan does not hold any employer securities; (2) the plan is eligible for the small plan audit waiver, but not due to enhanced bonding; (3) the plan gives certain disclosures and supporting documents to participants regarding the plan's investments and the fact that the plan is exempt from the annual audit requirements; and (4) the plan has 100% of its assets in investments that have a readily ascertainable fair market value.

² Large plans are plans that cover 100 or more participants. For plans that have between 80 and 120 participants as of the beginning of the plan year, the Plan Administrator can elect to use the same category (that is, large or small plan) as the plan used for the prior year. This rule applies for purposes of the Short Form as well.

³ Although Short Form filers do not have to file Schedule A, ERISA § 103(e) requires insurance companies to provide this information to them.

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Schedule is currently designed obfuscates the difference between these two issues. As a result, plan sponsors could mistakenly think that all of the amounts identified are paid from plan assets. For example, a mutual fund complex may provide gifts to broker-dealers who cumulatively sell a certain amounts of their mutual funds. This may be misinterpreted as a payment by the plan, rather than reflecting a potential conflict of interest.

As a result, we suggest that the Form 5500 be divided into two sections. The first section would address payments made out of plan assets, while the second section would address potential conflicts of interest.

IV. Coordination with ERISA Section 408(b)(2)

We understand that the DOL is in the process of revising the regulation under ERISA section 408(b)(2) with respect to the reasonable contract or arrangement prohibited transaction exemption. The DOL has stated that it is considering requiring the following categories of information to be disclosed in order to satisfy the exemption: (i) information the fiduciary needs in order to determine if the contract or arrangement is reasonable; (ii) information regarding conflicts of interest; and (iii) information the plan administrator needs for the annual report.

We suggest that the DOL coordinate the disclosure and reporting requirements of the proposed Form 5500 revisions and the anticipated 408(b)(2) regulations. That is, the regulation should require the upfront disclosure of fees and expenses, while the Form 5500 should require the after-the-fact reporting of those fees and expenses.

V. Conclusion

Increased reporting and disclosure will ultimately provide significant benefits to participants. That is because, with the sunshine effect of complete disclosure, fiduciaries will be able to make better educated decisions on behalf of their plans and participants. For example, if fees and expenses are fully understood by the fiduciaries, they will be in a better position to evaluate whether the services are worth the fees. Obviously, that can only happen if providers from all industries are required to report the same information in a relatively standard format.

This is critically important for the small companies that sponsor approximately 80% of the participant-directed plans in America. The issues in this area are very complex. For example, there is a need for fiduciaries to understand concepts like contingent deferred sales charges, redemption fees, the different classes of shares of mutual funds, revenue sharing, sub-transfer agency fees, 12b-1 fees, etc. Small employers often lack the resources to be able to delve into all of the contracts, prospectuses, and other materials needed to evaluate company and providers. Additionally, they may not be able to afford the cost of hiring sophisticated advisers to do that for them. As a result, we encourage the DOL to pay particular attention to the interests of small companies as it finalizes the Proposed Revisions.

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We hope that these comments have been helpful. Please let us know if you would like us to provide additional examples or clarification. We would be pleased to discuss these issues with you or provide supplemental comments. Please contact me at 310-478-5656 if you would like to discuss this further.

Very truly yours,

C. FREDERICK REISH

DEBRA A. DAVIS