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Comments by Bruce Ashton, Esq. APM, partner
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about Proposed Regulations at the

Hearing on Reasonable Contracts or Arrangements under Section 408(b)(2)

March 31, 2008

U.S. Department of Labor
Employee Benefits Security Administration

My name is Bruce Ashton. I am a partner of Reish Luftman Reicher & Cohen, Los Angeles, California. I'm here to testify on behalf of the American Society of Pension Professionals & Actuaries and the Counsel of Independent 401(k) Recordkeepers.

The department's proposed 408(b)(2) regulation will cause a sweeping change in how plan service arrangements are made and documented in the future. That said, we must disagree with some of our colleagues who have previously testified. In our view, the change is not substantive – fiduciaries are already required to know and understand all the information that must be disclosed under the proposed regulation.

Rather, the regulation will result in a shift of focus, a shift of responsibility. That is, the regulation will take the responsibility to find out information off the fiduciaries -- whose day-to-day real job is often to run a business – and place the responsibility to disclose the information on the experts whose day-to-day real job is to service plans.

Some may argue that the changes are too sweeping, that the department has gone overboard in the proposed regulation. We disagree. In our view, the proposed regulation only requires service providers to tell the truth -- and how can that be bad?

We believe there are a number of areas in which the proposed regulation, as well conceived as it is, can be improved. We have submitted a lengthy comment letter with our extremely cogent and well thought-out views on what should be done. Let me highlight some of our proposals:

I. It is crucial that responsible plan fiduciaries understand the aggregate costs being borne by their plans. It is equally important that they understand the compensation being received by service providers and by those who have an interest in transactions involving plan assets. As the Department has pointed out in prior guidance – the SunAmerica Advisory Opinion comes to mind – the amount of compensation being received by a party may have a material impact on its recommendations, actions or judgment.

Thus, in our view, the responsible fiduciaries must understand the transaction fees, such as commissions, finder's fees and the like, being paid to third parties in connection with the plan's investments.

One of the principal requirements of the proposed regulation is the disclosure of conflicts of interest. An important element of that disclosure is the transaction fees, first, because of the issue of self-interest vs. participant interests and, second, because transaction fees often affect the value of the plan's investments and ultimately the funds available for participants at retirement.

We urge, therefore, that distinct disclosure of transaction fees be retained in the final regulation.

II. ERISA makes it clear that only the shares of mutual funds held by a plan are assets of the plan and that the assets of the mutual funds themselves are not plan assets. ERISA also makes it clear that investment managers of mutual funds in which a plan invests are neither fiduciaries nor even parties in interest to the plan. Nevertheless, in today's 401(k) environment, mutual fund investment managers are clearly providing an indirect service to plans because their actions directly affect the value of plan assets – i.e., the mutual fund shares. Accordingly, we submit that direct and indirect compensation of the fund manager should have to be disclosed.

As a practical matter, however, except where the fund manager is affiliated with the plan record keeper, trustee, or other covered service provider, there does not seem to be a mechanism for making that disclosure except through another service provider, such as an independent record keeper. Thus, to the extent information regarding the direct and indirect compensation of the fund manager is required to be disclosed, the final regulation should make it clear that the party making the disclosure – in our example, the independent record keeper – may rely on information provided by the mutual funds without any duty to verify the information beyond commercially reasonable efforts.

In this connection, we also suggest that the department issue a prohibited transaction class exemption, similar to that proposed for responsible plan fiduciaries, exempting the record keeper from excise taxes under section 4975 if the fund manager fails to provide accurate or complete information to the covered service provider. It also would seem appropriate for such an exemption to include the requirement that the covered service provider notify the department if the fund manager fails or refuses to provide the information.

III. We encourage the department to require compensation disclosure in three general categories: investment-related fees and expenses; transaction-related fees and expenses (e.g., commissions, 12b-1 fees, finder's fees, etc.); and record keeping and administrative fees and expenses. We also submit that this type of disclosure should be required of all providers, whether or not they are considered a bundled provider under the proposed regulation. We have attached to our written comments a suggested form of disclosure.

An element of the proposed regulation that has received limited attention is the fact that the responsible plan fiduciary will be required to do something with the information – that is, make a prudent, informed decision. Uniform disclosure will, we believe, help facilitate this outcome in that it would make the disclosures uniform, which would facilitate consistent comparisons among providers, and it would provide the responsible plan fiduciary with information in categories that are most relevant to its decision to engage or replace a service provider. Such uniform disclosure would not replace other written materials, disclosures or formal contracts but would provide a single, comparable source for the extensive disclosures through which a responsible plan fiduciary will need to sift to make a decision.

IV. We encourage the department to require a consolidated form of disclosure for all service providers, even where other forms of disclosure are provided and additional documents are incorporated by reference. In our view, a consolidated summary of the information required by the proposed regulation would be more readily usable by a fiduciary than (for example) a stack of 25 or 50 prospectuses, even summary prospectuses, and would make the process of comparison of service providers both clearer and simpler.

In the small-plan market, we believe this type of disclosure would be essential to provide the most meaningful disclosure to the decision makers. Uniformity also could help service providers by ensuring that they do not inadvertently omit a disclosure item, and by making compliance less burdensome for the service provider.

I'll touch on just a few of our other comments, and then I would be pleased to answer your questions.

V. We request an effective date no sooner than January 1, 2008, or 120 days after release of the final regulation, whichever is later, for new, extended or renewed arrangements, and no sooner than January 1, 2009, for existing arrangements. With respect to the latter, it will take time for service providers to go back to existing clients to document the information required by the final regulation.

VI. Failure to satisfy any element of the final regulation would appear to cause a prohibited transaction. This could be a harsh result in cases of inadvertent or immaterial breaches, and we urge the Department to consider including a materiality standard for all disclosures or, alternatively, a substantial compliance exception. Further, we urge the Department to provide for a “cure” period for inadvertent failures and clarification that correction of a failure would only apply to compensation related to missing information and not to all compensation received by a service provider. Finally, it may be appropriate to add correction of a failure to disclose to the highly successful VFC program.

VII. We encourage the Department to restrict the application of the Proposed Regulation to situations in which costs are borne by a plan, and not by the plan sponsor, since this would have little if any impact on participants.

VIII. Finally, with respect to the conflict of interest disclosures, we recommend that the department provide greater clarity regarding the types of relationships that it believes should be disclosed in order to assist covered service providers in meeting this requirement.

Thank you for the opportunity to present these remarks. I would be happy to answer any questions about these or other points in our written comments.