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The Hewitt logo consists of the word "Hewitt" in a white, serif font, centered within a dark blue square.

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RIN 1210-AB13  
Office of Regulations and Interpretations  
Employee Benefits Security Administration  
Room N-5665  
U.S. Department of Labor  
200 Constitution Avenue, NW  
Washington, DC 20210

Attention: Investment Advice Final Rule

Dear Sir or Madam:

Subject: Comment Letter Relating to Investment Advice—Participant and Beneficiaries: Final Rule  
(RIN 1210-AB13)

Hewitt Associates LLC (Hewitt) welcomes the opportunity to submit comments on the Department of Labor's (Department's) final regulations governing the provision of investment advice by a fiduciary adviser to participants<sup>1</sup> in participant-directed individual account plans (e.g., 401(k) plans). These comments are submitted pursuant to the notice of proposed extension of effective date and applicability date published by the Department in the *Federal Register* on February 4, 2009.

### **Who We Are**

Hewitt Associates (NYSE: HEW) provides leading organizations around the world with expert human resources consulting and outsourcing solutions to help them anticipate and solve their most complex benefits, talent, and related financial challenges. Hewitt consults with companies to design and implement a wide range of human resources (HR), retirement, investment management, health management, compensation, and talent management strategies. As a leading outsourcing provider, Hewitt administers health care, retirement, payroll, and other HR programs to millions of employees, their families, and retirees. With a history of exceptional client service since 1940, Hewitt has offices in more than 30 countries and employs approximately 23,000 associates who are helping make the world a better place to work.

Hewitt welcomes the opportunity to submit our comments for the Department's consideration.

### **Comments Relating to Investment Advice Exemptions**

- 1. Participants need unbiased investment advice.** We firmly believe that almost all 401(k) participants need investment advice to assist in the selection and appropriate allocation of investment options. That advice must be either free from conflicts of interest or subject to sufficient safeguards to ensure that it will be unbiased.

The trend of cutting back or eliminating defined benefit plans continues among employers. For many Americans, 401(k) plans have become the primary source of retirement income in addition to Social

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<sup>1</sup> For purposes of this letter, the term "participant" means participants and beneficiaries.

Security. This shift means the effective management of their 401(k) assets may be the single most important factor in determining whether retirees leave the workforce with adequate retirement income.<sup>2</sup> In addition, the current economic crisis has triggered new levels of public and media scrutiny of financial services firms. The timing seems very poor to establish a set of regulations that will give investment advisers the opportunity for self-dealing.

The preamble to the proposed investment advice regulations states that “[b]iased advice may be less beneficial to investors than unbiased advice, or possibly even harmful in some cases.”<sup>3</sup> We agree that participants must be protected from such bias. However, even when conflicts of interest clearly exist, actual bias may be difficult to prove. If a recommendation is intentionally biased, there are still numerous “generally accepted investment theories” an investment adviser might use to support its advice. This could leave participants at a disadvantage and with little recourse. Therefore, where adequate safeguards do not exist, conflicts of interest, which can lead to biased investment advice, must not be allowed.

Although intentional bias might be difficult to prove, the incentive to provide biased advice and steer participants to more lucrative investment products is obvious. Advisers whose compensation is tied to the overall profitability of their organization might be inclined to support the promotion of stock funds over other investment funds. It is no secret that fees charged against stock-based funds are substantially higher than those charged for bond and fixed-income funds.<sup>4</sup> We are not questioning the long-term advantages of stock investments, but rather whether a conflicted investment adviser might recommend a more risky portfolio mix than is ideal for participants.

The financial industry appears to support moving qualified plans toward retail practices. It is important to understand that the 401(k) market is very different from the retail market. Not only do plan sponsors have a fiduciary duty to act in the best interests of participants,<sup>5</sup> but also, 401(k) participants are a more captive audience. They have little power to select a new fund manager if they are not satisfied with those offered by the plan. And although participants can hire independent personal financial advisers to assist them with their plan investments, it is unclear how many actually do. For this reason, participants need protections from advice that may be influenced by the profit goals of the individual and corporate adviser.

- 2. Hewitt believes that the class exemption should be revoked.** Because it is uncertain how many participants actually seek out individualized investment advice, Hewitt believes investment advice should be readily available through employers. We agree that without assistance, participants may make a number of mistakes that negatively impact the investment performance of their accounts.<sup>6</sup>

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<sup>2</sup> In a 2008 report addressing retirement adequacy for employees of large employers, Hewitt Associates determined that only employees who actively contribute to their employer savings plans have a chance at achieving adequate retirement income by age 65. Hewitt’s research found that only about 19% of employees were expected to satisfy 100% of their income needs at retirement without an employer retiree medical subsidy. Further, 67% of employees are expected to meet less than 80% of their income needs, with the average income gap of 41% of preretirement income. This research was conducted before the drastic market decline. Hewitt Associates Research Report, *Total Retirement Income at Large Companies: The Real Deal 2008* (June 2008).

<sup>3</sup> 73 Fed. Reg. 49896, 49910, footnote 61 (August 22, 2008).

<sup>4</sup> In 2007, the asset-weighted average expense ratio was 74 basis points for stock mutual funds offered by 401(k) plans, 56 for bond mutual funds, and 40 for money market mutual funds. Investment Company Institute, *Research Fundamentals*, “The Economics of Providing 401(K) Plans: Services, Fees, and Expenses 2007,” (December 2008, Vol. 17, No. 5) 12.

<sup>5</sup> Section 404(a)(1) of the Employee Retirement Income Security Act (ERISA), 29 U.S.C. 1104(a)(1).

<sup>6</sup> 73 Fed. Reg. 49896, 49903-49905 (August 22, 2008). The DOL reviews several common participant investment mistakes in the preamble to the proposed regulations.

However, because it is nearly impossible to determine the damage that may be caused by conflicted advice, every effort must be taken to protect participants from the possibility of self-dealing. Hewitt is not confident that the regulations currently create effective controls to guard against abusive behavior by conflicted investment advisers.

The proposed class exemption adds additional requirements to those under the statutory exemption and allows person-to-person investment advice by a conflicted fiduciary adviser that may contradict advice provided by a computer model. Under the fee leveling class exemption, a conflicted fiduciary adviser may recommend a more expensive fund of the same class if the compensation received by the individual adviser does not increase based upon the advice provided. However, as written the exemption does not offer the same protections against increased compensation by the corporate adviser. The class exemptions do not counter the opportunity for self-dealing with effective controls and should be withdrawn.

- a. **Limited audits based upon self-imposed policies and procedures cannot provide adequate protection against self-dealing investment advisers.** The class exemption relies on a number of deterrents. Proprietary computer models require an annual audit. In addition, person-to-person investment advice (whether face-to-face or by phone) must be audited for both the computer model and advisers who qualify for the fee leveling class exemption.

Notably, there are no specified audit standards in the final regulations. Rather, person-to-person advice will be audited for compliance with policies and procedures established by the fiduciary advisers themselves, effectively allowing them to self-police. In addition, the scope of the audit will also, of necessity, be limited to a reasonable sampling of the advice provided by a corporate fiduciary investment adviser (not individual investment advisers). Under these parameters, a financial adviser intent on increasing its own profit margin may not perceive the audit requirement as a significant deterrent. Given the turmoil in the financial markets due, in large part, to the financial services industry's inability to effectively self-regulate, this is the wrong time to propose solutions that rely on self-policing and leave participants with little protection. Without adequate protection, the class exemption cannot be in the best interests of plans or their participants as required by ERISA.<sup>7</sup>

- b. **The disclosure requirements do not protect participants from conflicts of interest.** When person-to-person investment advice is given by a fiduciary adviser, the adviser must conclude that the advice is prudent and in the best interest of the participant at the time it is given. The adviser must also explain the basis for the conclusion and the reasons for any advice that may appear to be conflicted. Then the fiduciary adviser must document this explanation within 30 days and retain the documentation for six years.

Additionally, before the advice is provided, the fiduciary adviser must disclose all potential conflicts of interest, explain the limitations of any computer model used, provide historical information on fund performance, and explain where to find additional information. The regulations are premised on the assumption that the fiduciary adviser's disclosure obligations will serve as a deterrent against self-dealing. We must respectfully disagree.

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<sup>7</sup> Section 408(a) of the Employee Retirement Income Security Act (ERISA), 29 U.S.C. 1108(a).

As the model demonstrates, the notice will be lengthy. After the disclosure of all conflicts of interest, the participant must be instructed to consider the impact of the adviser's fees when evaluating the investment advice. The participant must also be informed that he or she can also consult individually with an independent adviser. Then, the participant must be advised to also consider investment returns. Other information must also be disclosed.

Required disclosure will set out a variety of competing considerations for the participant, with no suggestions for analysis. This may leave many participants confused as to the meaning and intent of the notice. For others disclosure may raise awareness, but it will not necessarily enable participants to distinguish good advice from biased advice.

- c. **There is no single regulatory structure to monitor compliance and protect participants from self-dealing investment advisers.** These regulations are issued by the Department because they relate to retirement plans governed by ERISA. However, other federal and state agencies, such as the Securities and Exchange Commission, regulate the investment industry and investment advisers. Accordingly, regulatory protection of participants receiving biased investment advice is likely to become mired in jurisdictional confusion and inconsistencies.

A potential result is that participants who believe biased advice caused them harm will be forced into litigation. The time, cost, and uncertainty of litigation could result in very limited enforcement of participant protections under this class exemption. This further lessens the risk for fiduciary investment advisers that engage in self-dealing.

Under the existing structure, the only way to provide participants with the protection they need and deserve is to limit the opportunities for conflicted investment advice. The class exemption only serves to expand such opportunities.

- d. **Participant investment advice is available from independent providers, or through the statutory exemption.** The class exemption is not necessary to the expansion of unbiased participant investment advice. In the preamble to the proposed regulations, the Department anticipates that with the availability of the statutory exemption for fiduciary investment advice, some type of investment advice will be available to approximately 50% of plan participants. The Department also estimates that the addition of the class exemption will further increase the availability of investment advice to 60% of participants, and further increase the availability of person-to-person advice, which seems to be most favored by participants.<sup>8</sup> Although it may be true that advice will increase with the class exemption, Hewitt does not believe that an increase in biased investment advice will be beneficial, especially when there are more desirable alternatives.

Many plan sponsors currently make investment advice available to plan participants through independent providers. Independent investment advice companies utilize computer models, person-to person advice (both in-person and by phone), or a mix of both. As brokers and investment management companies take advantage of the statutory exemption to offer investment advice, we would also expect that the availability of investment advice to participants will further increase. While we applaud efforts to make unbiased advice more widely available, we believe

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<sup>8</sup> 73 Fed. Reg. 49896, 49907-49909 (August 22, 2008).

that the statutory exemption (with our suggested revisions) offers the best and only prudent means of providing investment advice where the advice provider has conflicts of interest. For these reasons, we recommend that the class exemption be revoked.

- 3. The regulations for the statutory exemption do not provide enough guidance to protect against self-dealing.** One option is to amend the regulations to provide more guidance around the basis of advice provided and the standards for required audits. Alternatively, it may be time to seek Congressional clarification of the statutory language.

The preamble to the regulations explains why the fee leveling requirement of the statutory exemption of section 2550.408g-1(b) applies only to the fiduciary adviser or its employees, and not to affiliates of the fiduciary adviser that do not provide investment advice.<sup>9</sup> The need for this explanation demonstrates the confusion of the statutory language.

While we understand the statutory interpretation, for the reasons cited in Section 2, above, we are concerned that the regulations do not provide sufficient regulatory structure and definition to protect participants from self-dealing in a fee leveling situation. As noted above, we believe that where conflicted advice is allowed there must be effective controls to protect participants against self-dealing. To accomplish this, the regulations must provide more structure around the definition of "generally accepted investment theories," as well as specify the audit standards that must be applied.

Finally, we understand that the Department cannot alter the statute through regulations. However, as noted above, there has been some confusion around the intent of the fee leveling provision. Therefore, one alternative would be to seek Congressional clarification of the fee leveling statutory exemption. Then if Congress determined it was necessary, it could pass technical corrections to address the confusion.

## Conclusion

Hewitt commends the Department for its extension of this comment period. Please feel free to contact us with any comments or questions relating to the matters discussed in this letter.

Sincerely,  
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<sup>9</sup> 74 Fed. Reg. 3822, 3825 (January 21, 2009). The DOL also addressed the confusion over the application of the fee leveling provision to affiliates of the fiduciary investment adviser in the preamble to the proposed regulations, 73 Fed. Reg. at 49898 and in Field Assistance Bulletin 2001-01 (February 2, 2007).