U.S. TREASURY DEPARTMENT OFFICE OF PUBLIC AFFAIRS

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TESTIMONY OF TREASURY BENEFITS TAX COUNSEL W. THOMAS REEDER BEFORE THE HOUSE WAYS AND MEANS COMMITTEE ON RETIREMENT PLAN FEES AND EXPENSES

Washington, DC— Chairman Rangel, Ranking Member McCrery and Members of the Committee, I appreciate the opportunity to appear today to discuss retirement plan fees and expenses, and the transparency of those costs to plan participants and sponsors.

Background

The Administration is committed to facilitating the establishment of retirement savings plans by as many employers as possible and encouraging participation in those plans by as many workers as possible. Transparency of the cost of investing the assets of those plans is an important factor in making employer-sponsored savings plans more attractive to employers and their employees.

The Labor Department has primary jurisdiction over most issues relating to retirement plan fees and expenses, and the disclosure of plan fee and expense information to plan sponsors and plan participants. The Employee Retirement Income Security Act of 1974 ("ERISA"), as originally enacted, established minimum standards for retirement plans and provided extensive rules on the federal income tax effects of retirement plan transactions. ERISA was enacted, in part, to protect the interests of retirement plan participants and their beneficiaries by requiring the disclosure of financial and other information concerning the plan, establishing standards of conduct for plan fiduciaries, and providing for appropriate remedies. Responsibility for the interpretation and enforcement of ERISA was divided among the Labor Department, the Treasury Department, and the Pension Benefit Guaranty Corporation. Originally, ERISA granted dual jurisdiction to both the Labor and Treasury Departments over certain issues, but, shortly after its enactment, the ERISA Reorganization Plan No. 4 of 1978 allocated and transferred responsibility for particular issues between the Labor and Treasury Departments. Pursuant to ERISA and the Reorganization Plan, the Labor Department has primary jurisdiction over the reporting, disclosure, and fiduciary responsibility rules of ERISA. The division of jurisdiction between the Labor and Treasury Departments has evolved into a balance that works well.

Treasury Department Activities Regarding Plan Costs and Fees

Although the Labor Department has primary jurisdiction over disclosure issues, the Treasury Department certainly shares the goals of minimizing plan expenses, through accurate and meaningful disclosure of information to plan participants, plan sponsors, and the federal government. The Internal Revenue Code ("Code") contains substantial favorable tax treatment for retirement savings, and we all are working to maximize the efficiency of that treatment. Dollars spent on plan fees and expenses are dollars not available for retired Americans and, over time, excessive fees will significantly erode a worker's retirement savings.

At the Treasury Department, we strive to work with plan sponsors and plan service providers to reduce the costs of sponsoring and maintaining tax-qualified retirement plans, including plans that include cash or deferred arrangements under Code section 401(k). For example:

- We continue to expand plan sponsors' ability to use pre-approved plans (which are less expensive to sponsor and maintain than individually designed plans).

- We developed, and continue to refine, a voluntary correction program under which plan sponsors can voluntarily correct qualification failures in a structured, predictable, cost effective manner rather than having the plan completely disqualified.

- We have issued guidance on safe harbor 401(k) plan designs that permit plan sponsors to avoid complicated and costly nondiscrimination testing. Under these safe harbors, minimum employer matching contributions or employer non-elective contributions are made to non-highly compensated employees. We are also working to provide guidance on a new safe harbor 401(k) plan design that was approved by Congress last year – so-called automatic enrollment arangements. Under these arrangements, workers automatically participate in their employer-sponsored 401(k) plan unless they take affirmative action to opt out of elective contributions. Sponsors that make minimum required employer matching contributions or employer non-elective contributions can avoid costly nondiscrimination testing. We are working to help sponsors implement this kind of arrangement by, for example, preparing a participant-friendly sample notice that explains how this kind of plan design works.

We have also specifically addressed – or are considering options for addressing – plan fees and expenses in a limited number of contexts within the Treasury Department's jurisdiction. For example:

- We issued guidance in Revenue Ruling 2004-10 clarifying that a plan may not allocate the expenses of active employees among all plan participants, while allocating the expenses of former employees only among plan participants who are former employees. Allocating expenses in this manner would violate the rule that a plan sponsor may not impose a "significant detriment" on an individual's decision to leave his or her plan benefits in the plan (rather than taking a distribution).

- We are coordinating with the Labor Department on guidance regarding the option under the Pension Protection Act of 2006 that allows plan sponsors to permit individuals who are automatically enrolled in a 401(k) plan to withdraw those contributions within a 90-day window period. The guidance will likely limit the imposition of any fees or expenses on amounts withdrawn under these rules.

- We are working to issue guidance regarding new rules under Code section 401(a)(35) to permit participants to diversify plan investments in employer securities. We have received comments relating to the assessment of employer stock-fund fees that differ from fees assessed on other kinds of plan investment funds. We are considering these comments in light of the new requirement that plan participants not be unreasonably encouraged or discouraged from investing in employer securities.

- Section 1102(b) of the Pension Protection Act of 2006 requires that the description of a participant's right, if any, to defer receipt of a distribution under Code section 411 must also describe the consequences of failing to defer such receipt. In Notice 2007-7, the Treasury Department and the Internal Revenue Service (IRS) provided a safe harbor for satisfying this new notice requirement under which a defined contribution plan would include a description indicating the investment options available under the plan, including employer subsidized fees, that will be available if distributions are deferred.

- The Treasury Department and the IRS are currently working on a guidance project addressing whether a "wrap" or asset-based fee (as opposed to a brokerage-based fee) will be deemed to be a contribution to an IRA if the fee is paid outside of the IRA and, if not, whether it will be deductible. We hope to have this guidance finalized within the coming nine months.

We appreciate the Committee's concern for enhancing participant disclosure and providing transparency of fee and expense information. At the same time, we share the Labor Department's concern that legislation in this area could disrupt the Labor Department's significant ongoing efforts to require enhanced disclosures of plan fees and costs.

Specifically, we believe that overly detailed, lengthy disclosures on plan fees and costs may impair, rather than enhance, participants' ability to make informed decisions regarding their participant-directed plan investments. We are also concerned that additional disclosure costs, and the costs of anticipated related litigation, will ultimately be borne by plan participants. These expected participant costs should be weighed carefully against expected benefits to participants of additional disclosure.

While fees and other costs are very important factors in a plan sponsor's choice of third-party investment and administrative service providers and a participant's choice of particular investment options, those costs are not the only factors. Customer service, reliability, accuracy, communications, returns, management continuity and quality, and many other factors may appropriately inform sponsor and participant decisions. Care should be taken in structuring disclosure requirements so that fees and costs are not over-emphasized.

At the broadest level, the creation of a new bureaucracy that duplicates responsibilities of Labor Department, the Treasury Department, and other government agencies carries the risk of inconsistency, delay, and error.

There have been recent reports of undisclosed fees, penalties, and restrictions in defined contribution plans sponsored by State and local governmental entities, which are not subject to Title 1 of ERISA and thus not subject to the disclosure rules administered by the Labor Department. The exception from ERISA of governmental plans (as well as most plans sponsored by churches) was a conscious decision by Congress in enacting ERISA. State and local legislative bodies have been left to regulate these plans, and we do not propose to apply federal fiduciary rules to those plans. We note, however, that most types of tax preferred defined contribution plans, including those sponsored by governments and churches, must be operated for the exclusive benefit of employees or their beneficiaries. It is conceivable that certain excessive or hidden fee arrangements under which the fees are paid with plan assets and are not used for the exclusive benefit of employees or their beneficiaries could violate that standard. However, plan disqualification would adversely affect innocent participants. State enforcement mechanisms are more effective than the Internal Revenue Code at appropriately addressing these issues with respect to State and local government plans.

We look forward to working within the Administration and with Congress to address issues regarding plan investment fee transparency in a manner that facilitates the establishment and maintenance of retirement savings plans by American employers for their employees and facilitates participation in these programs by American workers.

Conclusion

Mr. Chairman and Members of the Committee, I appreciate the opportunity to appear today, and I will be happy to respond to any questions.

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