Testimony
on Behalf of Hewitt Associates LLC

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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, 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 over 30 countries and employs approximately 23,000 associates who are helping make the world a better place to work. For more information, please visit www.hewitt.com.

Introduction

Mr. Chairman and Members of the Subcommittee: Thank you for the opportunity to testify at this important hearing on 401(k) Fair Disclosure for Retirement Security Act of 2009. My name is Alison Borland, and I am the Retirement Strategy Leader for Hewitt Associates. As requested, I will focus my remarks today on the experience of mid- to large-sized employers in their role as 401(k) plan fiduciaries.

Hewitt Associates is a global human resources outsourcing and consulting company providing services to major employers in more than 30 countries. We employ 23,000 associates worldwide. Headquartered in Lincolnshire, Illinois, we serve more than 2,000 U.S. employers from offices in 30 states, including many of the states represented by the members of this distinguished Subcommittee.

As one of the world's premier human resources services companies, Hewitt Associates has extensive experience in both designing and administering 401(k) plans for mid- to large-sized employers, including helping employers to communicate with their participants about this increasingly important benefit. We are the largest independent provider of administration services for retirement plans, serving more than 11 million plan participants. We do not manage funds and have no affiliations with any investment management firms.

The focus of our testimony today is to make a case for much greater transparency in the disclosure of fees by service providers to plan fiduciaries, a position that we believe Chairman Miller's bill addresses well. Now more than ever, employees need to accumulate the greatest retirement savings possible for every dollar saved. Our experience shows that increased fee transparency increases fiduciaries' understanding and their negotiating power, ultimately leading to lower fees and higher retirement benefits for participants. We will provide several real-world examples that illustrate how full transparency can benefit both fiduciaries and participants. We will also discuss the need for full disclosure of potential conflicts of interest by service providers, the advantages of providing mandatory fee disclosure to plan participants and the need for unbiased investment advice and financial education to help participants adequately prepare for retirement.

Plan Fiduciaries Must Understand All Fees

As the Subcommittee is well aware, 401(k) plans play a vital role in retirement income security for the majority of Americans. In a recent Hewitt survey, 65 percent of the 302 employers surveyed indicated that 401(k) plans were the primary retirement vehicle for their workforce.[1] This dependence, coupled with the negative impact of the economic downturn on 401(k) account balances, gives even greater urgency to taking the necessary steps to prepare employees to be financially secure when it comes time to retire. Since most plan fees are paid by participants out of their accounts, these fees can significantly affect the overall income that plan participants earn and, consequently, affect their overall retirement security. To protect the interests of their participants and beneficiaries, plan fiduciaries must increasingly act as experts in plan fee arrangements.

Plan fiduciaries need a complete understanding of all fees under a contract to ensure that the charges constitute reasonable compensation. This is necessary before any contract can be covered by the prohibited transaction exemption under section 408(b)(2) of ERISA. Equally as important, understanding plan costs is necessary for fiduciaries to act prudently and solely in the interest of plan participants and beneficiaries when selecting a service provider, as required by section 404(a) of ERISA.

[1] Hewitt Associates, Trends and Experience in 401(k) Plans (2007)

Plan fiduciaries cannot fulfill their obligations without clear and concise fee disclosures from service providers. Further, these fees must be disclosed in a manner that allows for ready and consistent comparisons. Without a uniform basis of disclosure, plan fiduciaries cannot make the best decisions. The disclosures required under current law are both unclear and insufficient, and the 2008 Department of Labor's proposed regulations on 408(b)(2) also fall short.

Service Providers Must Fully Disclose Fee Details

To fully meet their obligations, fiduciaries must understand the most significant fee components of their plans and the services covered by these costs. A recent study highlighted that there is significant variation in how fees are charged for defined contribution plan services.[2] Uniform disclosure rules that permit meaningful fee comparisons will help fiduciaries better evaluate the costs of services among competing service providers, even when different packaging and pricing methods are used. It is especially important that plan sponsors understand the embedded cost of services that a service provider may wrap into a single price and represent as "free." In addition to evaluating fees at the time of contract signing, fiduciaries need to consider the impact of fees on an ongoing basis to understand how they may change over time. Full disclosure by service providers is essential if plan fiduciaries are to act in the best interest of plan participants.

Breaking Out Fees Increases Knowledge and Negotiating Power

Typical plans have investment management, administrative, trustee, and other miscellaneous fees. Investment management and administrative fees generally account for more than 90 percent of individual account plan costs. Investment management fees are based on the value of the assets. Administrative fees include costs for recordkeeping, communication, compliance, and education, which are generally based on the number of participants served by the plan. Rather than charge a separate fee based on the number of participants in the plan, many providers who manage funds in addition to providing administration services will embed the administrative fees within the asset based fees that also cover investment management. By obtaining a breakout of these administrative fees from the asset-based fees, fiduciaries gain improved negotiating power by having the information needed to more effectively model how these fees may fluctuate over time with changing asset values and participant size. More details about the two primary sources of fees in 401(k) plans and the importance of separating them are described below.

Investment Management Costs

Investment management expenses are the largest plan cost, making up approximately three-quarters of total plan fees. These fees are reflected in the expense ratios of the funds represented in the plan. Research has proven that fees are a critical—if not the most important—factor when selecting funds. In fact, studies have shown that lower-cost funds consistently and substantially outpace higher-cost funds over time.[3]

Understanding a fund's investment costs helps plan fiduciaries select investment alternatives with strong relative historical returns and the lowest possible fees. For instance, 401(k) plans for mid- to large-sized employers with substantial assets might secure a tiered fee schedule that guarantees a decrease in expense ratios as the assets grow. This is accomplished by using fund vehicles available only to institutional investors, such as separate accounts and collective trusts. These fund vehicles have been

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[2] Deloitte, Defined Contribution 401(k) Fee Study (Spring 2009), conducted for the Investment Company Institute

[3] For example, Christine Benz, director of personal finance at Morningstar Inc., stated that "In almost every study we've run, expenses show up as a very significant predictor of future performance." In other words, lower costs are an indicator of high performance. http://online.wsj.com/article/SB122099798601116727.html?mod=googlenews_wsj; See also, Haslam, John, Baker, H. Kent, and Smith, David M., Performance and Characteristics of Actively Managed Retail Mutual Funds with Diverse Expense Ratios, Financial Services Review, Vol. 17, No. 1, 2008 http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1155776

common in defined benefit plans and are gaining popularity in 401(k) plans because of the clear cost advantages.

Administrative Costs

Administrative costs are the second largest source of fees in 401(k) plans. On average, administrative fees represent an additional 20 percent of total plan fees. These fees are often embedded within the expense ratio of the mutual funds within the plan. If a plan sponsor does not understand that it is paying administrative fees through the investment management fees, it may believe administration services are "free." This might lead the plan sponsor to inadvertently choose investment options or administrative services that do not maximize participant savings.

According to Hewitt survey data, 75 percent of plans require plan participants to pay some or all fees associated with administrative services.[4] Unlike investment management costs, which logically vary based on the amount of assets in the plan, the actual cost of administrative services is more dependent on the number of participants served. Because many service providers charge administrative fees as a percentage of assets embedded within the investment management fee, administrative fees fluctuate as plan asset values change over time. Under normal market conditions, this means that the administrative fees will often increase over time, even if participant counts remain the same. This practice is most common with bundled providers that combine investment management services *and* administrative services in one bundled price.

There is no reasonable explanation why administrative costs should fluctuate based on asset size. If administrative fees are broken out separately from investment management fees and understood in dollars per participant (even if charged in basis points), responsible fiduciaries will have the ability to accurately compare all plan fees and make the optimal investment and administrative choices. Scrutiny of the initial contract is a necessity, but periodic review over the life of the contract is also very important to ensure fees remain reasonable.

Real-World Examples of the Benefits of Uniform and Detailed Fee Comparisons

In our work with large employers, Hewitt finds that detailed and uniform fee comparisons across different types of service providers often results in lower negotiated fees. Armed with disclosure of fee components, the plan fiduciary can consider alternate providers, evaluate lower-cost fund options, and/or negotiate lower fees with the current provider. Lower fees directly benefit plan participants by increasing their account balances and compounding this savings throughout their working years. Several real-life examples illustrate the point.

Company X

Company X wanted to evaluate the benefits of combining the two separate 401(k) plans it sponsored through two different service providers. The combined plans had nearly $5 billion in assets and served 45,000 participants. Total fees for the plans were 0.30 percent, with embedded administrative fees of just over $50 per participant for one plan to more than $100 per participant for the second plan, with an average of $85 per participant. Administrative fees had not been broken out for the more expensive plan in the past, explaining the wide differential in per participant fees.

Consolidating the two plans, including investment options and administration services, created significant savings on investment management and administrative costs. Further, unbundling the administrative fees from the investment management fees provided the company with the ability to look more closely at the investment choices and evaluate the administration services in greater depth. This resulted in the selection of institutional funds (non-mutual fund vehicles) and a significant reduction in administrative costs through the negotiation of per participant fees. The combined fee structure across both plans dropped by nearly one-half to only 0.16 percent, including administrative fees of just over $40 per participant.

[4] Hewitt Associates, Trends and Experience in 401(k) Plans (2007)

The approximately $2 million of annual savings in administrative fees accrued directly and entirely to participants. Total fees decreased nearly $7 million per year.

Company Y

Company Y sponsored a plan using a bundled fee structure with total fees of 0.63 percent of plan assets, which included an estimated $242 per participant in embedded administrative charges. The firm had 3,000 participants and $250 million in assets. Although satisfied with the services, as a responsible fiduciary, Company Y hired a consultant to help them better understand their fees and fee structure. Following the analysis, Company Y was able to negotiate with their same service provider for a drop in total fees from 0.63 percent to 0.46 percent, with a reduction of administrative fees from $242 per participant to $155 per participant. Further, Company Y negotiated additional services for participants as part of the same administrative fee structure. All $290,000 of annual savings accrued entirely to participants.

Company Z

Company Z used a bundled provider for a plan that was predominantly invested in mutual funds. The firm had over 50,000 participants and in excess of $4 billion in assets. Total fees were just over 0.50 percent, with embedded administrative fees estimated at nearly $100 per participant. After disclosing and evaluating the fee structure, the current service provider offered to substantially reduce fees and offered alternative institutional (non-mutual fund) products. With this new opportunity, fees could decline to approximately 0.30 percent, with estimated administrative fees reduced to just under $50 per participant. Plan participants would realize the annual savings on administrative fees of nearly $4 million per year. In addition, under the new fee structure, as assets grow over time, participants' savings will grow.

Before and After Pricing Summary for Real-World Examples

Example	Assets	Participant Count	Total Fees Before	Total Fees After	Admin/Trustee Fees Before	Admin/Trustee Fees After
Company X	$5B	45,000	0.30%	0.16%	$85/ppt	■ Just over $50 per participant ■ 15% to 60% reduction ■ **Over $2 million in annual savings**
Company Y	$250M	3,000	0.63%	0.46%	$242/ppt	■ $155 per participant ■ 36% reduction ■ **$290,000 in annual savings**
Company Z	>$4B	>50,000	0.50%	0.30%	$100/ppt	■ Less than $50 per participant ■ More than a 50% reduction ■ **Nearly $4 million in annual savings**

The resulting savings in these examples were possible once plan sponsors understood that a significant portion of plan costs was not dependent on asset size but rather on number of participants. This allowed them to quantify the fees on that basis. When all costs are bundled into an aggregate asset-based fee, fiduciaries must be able to model how fees will change over time and how reasonable they are when considering changes in asset size and participant counts.

Plan Sponsors Need Unbiased Information About Revenue Sources

Service providers often generate revenue streams by providing services to 401(k) plan participants that are unrelated to the 401(k) plan. It is critical that all potential sources of revenue generated from servicing the plan are disclosed so that the plan sponsor can identify and control conflicts of interest that may affect plan participants.

A useful example is when a 401(k) service provider offers participants the ability to roll over their 401(k) account balances into the provider's own retail individual retirement accounts (IRAs) upon termination of employment. Many administrative providers actively market their IRA solution, because encouraging these rollovers can lead to very lucrative add-on revenue. So in essence, some providers may do the administration work on a 401(k) plan with the ultimate goal of obtaining a high percentage of participant rollovers at termination or retirement, given that high dollar balances, along with the often higher investment fees in an IRA environment, are generally more profitable than providing the 401(k) services.

These cross-selling practices may be detrimental to participant retirement security. Hewitt's research shows that it is usually better from a cost perspective to either leave the accounts in the existing mid- to large-sized 401(k) plan, or to move those funds into another mid- to large-sized employer sponsored 401(k) plan if available through a new employer. The marketing of rollover products often does not adequately explain the trade-offs and potential benefits between alternatives. In addition, the provider servicing the 401(k) plan may not have the best IRA solution or pricing. Participants may be encouraged to use a sub-optimal product when it is promoted in conjunction with plan services, believing the employer has selected the provider through the fiduciary process.

Consider an example of a participant with access to a 401(k) plan with institutionally priced investment options. Using conservative assumptions and typical account balances, our modeling shows that a 35-year-old who is an *average* saver and moves her $33,000 balance from her company plan to a retail IRA could lose $37,681, or 9 percent (or more), compared to what she would have if she remains invested in the 401(k) plan until she receives required distributions at age 70½. If she is an *active* saver who contributes 8 percent per year over the course of her career and then moves her $101,808 balance to an IRA at age 35, she could lose $116,250 or more. If we consider the greater fee savings she typically would experience in a large 401(k) plan, the IRA loss increases to $244,078, representing a loss of 18 percent of the total accumulated balance.[5]

Plan sponsors must understand the incentives that may exist for service providers to encourage participant behaviors that may not be in their best interest because they do not contribute to greater retirement security. Service providers may directly market products like retail IRAs, other retail investment products, or life insurance products to this captive audience. Plan fiduciaries need to understand how these potential revenue streams may affect services received and administrative fees paid. They also need to carefully consider the potential consequences for participants. Identifying these potential conflicts of interest requires more detailed disclosure than is available today.

Participants Need Better Fee Disclosure

Plan participants will also benefit from improved disclosure of fees. While Hewitt believes that comprehensive fee information should be readily accessible when requested, mandatory disclosures should be concise and provide information that is truly meaningful for the vast majority of participants. Fee disclosures to participants must be understandable without overloading the average participant with so much technical detail that the information is likely to be ignored or discarded. The worst-case scenario is that the disclosure actually discourages savings.

[5] Hewitt's Statement for the Record to the U.S. Senate Special Committee on Aging Hearing on "Saving Smartly for Retirement: Are Americans Being Encouraged to Break Open the Piggy Bank," July 16, 2008

Plan participants' needs for expense disclosure are very different from their employers' (or other plan fiduciaries) requirements. Before participants choose to contribute to the plan, the plan fiduciary has already selected service providers and investment funds for the plan. This means that most plan costs are determined before the participant is ever involved; thus the importance of full fee transparency for plan fiduciaries. It is also the plan fiduciary, and not the participant, that must regularly monitor and evaluate service providers, including investment managers and administrators. Service provider fee disclosure is of primary importance to enable plan fiduciaries to keep plan costs low and maximize retirement income for participants.

Hewitt believes that participants should be informed if and how administrative fees are paid by the plan, regardless of how fees are charged, whether bundled or unbundled. As with disclosures to plan fiduciaries, fee disclosures from all service providers to plan participants should be available on a uniform basis to allow for meaningful comparisons.

Mandatory disclosure to plan participants should aid them in understanding fees on their account balances, but not confuse their decision making or overwhelm them with information they cannot control. For example, if participants simply move their portfolios toward the lowest-cost funds solely based on the fee information provided, this may decrease their retirement readiness. Many participants do not have the basic financial acumen to understand the importance of diversifying their portfolio and changing that asset allocation over time based on their changing personal circumstances. Greater disclosure will not solve these critical awareness issues. This is when investment advice, education, and certain plan design features can make a real difference.[6]

Objective advice can aid participants in maximizing their investment returns and achieving a level of risk that is acceptable to the individual participants, given their unique circumstances. However, the regulatory oversight provided in the DOL investment advice regulations currently under review is not sufficient. Unlike fee disclosure to plan fiduciaries, greater disclosure under the investment advice rules without greater regulatory scrutiny may not do enough to protect plan participants. Hewitt believes that all but the most sophisticated plan participants could benefit from more investment advice and that unbiased investment advice should be readily available.

The 401(k) Fair Disclosure for Retirement Security Act of 2009 Can Help

Hewitt supports Chairman Miller's bill because its provisions enhance the retirement security of Americans. The bill addresses the key disclosure gaps from both a plan sponsor and a plan participant perspective and does not allow service provider exemptions that get in the way of full transparency.

Full Fee Disclosure

The 401(k) Disclosure for Retirement Security Act of 2009 would require service providers to break out total costs into the main fee categories: investment management, administrative/recordkeeping, transactional, and other. The bill would also require disclosure of all fees paid to affiliates and subcontractors in a bundled fee arrangement. This will allow plan sponsors to readily compare the services of different types of providers in a uniform manner leading to better control and management of fees. By comparison, the Department of Labor's 2008 proposed service provider fee regulations permit bundled providers to report all fee types in the aggregate. Under the proposed regulations, fiduciaries would not be able to uniformly evaluate services offered by different providers, severely impairing their ability to negotiate lower fees for plan participants.

[6] Hewitt Associates, Building the Ideal 401(k) Plan: Providing Optimal Accumulation and Effective Distribution (October 2008)

Potential Conflicts of Interest
The 401(k) Disclosure for Retirement Security Act of 2009 would also requires disclosure of any material personal, business, or financial relationship with the plan sponsor, plan, or other service provider (or affiliate) that benefits the service provider. The service provider must also disclose the extent to which it uses its own proprietary investment products. These provisions would go far to arm plan sponsors with the information they need to identify any potential conflicts of interest that could disadvantage their plan participants over time.

Meaningful Participant Disclosures
The 401(k) Disclosure for Retirement Security Act of 2009 would provide for uniform and transparent disclosure of fees to participants, regardless of how plan services are provided (e.g., bundled or unbundled). This is a good starting point, although we believe that the mechanics of participant fee disclosure merit further review and discussion. On the other hand, the proposed DOL regulations on participant fee disclosure appear to treat disclosure very differently, depending on how plan services are packaged. Under these rules, it is quite likely that plan participants in a plan with bundled services may never realize that they are paying for plan administration or how much. In contrast, plans with independent plan recordkeepers would be required to provide a special quarterly disclosure of administrative fees. Such different disclosure standards are inconsistent, misleading, and lack the transparency that participants deserve and increasingly demand.

Conclusion
In closing, Mr. Chairman and Members of the Subcommittee, Hewitt believes that complete fee transparency is a key factor in maintaining a strong defined contribution retirement plan system. Knowledge is power, and by arming plan sponsors with complete and comparable information, they will be better equipped to negotiate and provide high-quality plans for their participants at reasonable costs. The current economic and financial environment makes it even more important to provide uniform fee transparency in 2009. Hewitt would be pleased to offer our data analysis, our experience, and our consulting and administration expertise in helping the Committee complete its work on this issue.
Thank you.