Date: May 13, 2008

TCRS 2008-05: Department of Labor Makes Technical Corrections to Qualified Default Investment Alternative (QDIA) Final Regulations and Issues Additional QDIA Guidance in Field Assistance Bulletin 2008-03

On April 30, 2008, the Department of Labor (DOL) published technical corrections to the final QDIA regulations. A day earlier, on April 29, 2008, the DOL issued additional QDIA guidance in the form of Field Assistance Bulletin 2008-03. This summary includes highlights of both pieces of guidance.

Background

On October 24, 2007, the Department of Labor published final QDIA regulations as required by the Pension Protection Act of 2006. Under these regulations a plan fiduciary of a participant-directed defined contribution plan that complies with these final regulations is afforded relief from fiduciary liability for decisions to invest participant contributions in a QDIA absent participant direction. Thus, the plan fiduciary will not be liable for any loss, or by reason of any breach, that occurs as a result of the decisions to invest such contributions in the QDIA.

Highlights of Technical Corrections to Final QDIA Regulations

The DOL made 3 technical corrections to the final QDIA regulations:

- The Supplementary Information to the final QDIA regulations provided that any participant-initiated transfer or withdrawal from a QDIA during the 90-day period beginning on the date of a participant's first elective contribution (or other first investment) in the QDIA shall not be subject to any restrictions, fees or expenses other than ongoing administrative and investment fees. The DOL included a few examples of restrictions, one of which is referred to as a "round-trip" restriction on the ability of the participant to reinvest amounts in the QDIA within a defined period of time. The DOL concluded that this example should not have been included as an example of an impermissible restriction under the final QDIA regulations. Thus, typical "round-trip" restrictions will be permissible in a QDIA.
- The DOL amended the language in the final QDIA regulations that describe persons who are permitted to manage a QDIA. As amended, the reference to a "plan sponsor who is a named fiduciary of the plan" also includes a committee that is a named fiduciary of the plan and is comprised primarily of employees of the plan sponsor. Thus, as amended, the final regulations now make clear that such a committee may manage a QDIA.
- The final QDIA regulations included a "grandfather stable value" provision to provide relief to employers who had selected stable value products or funds as their default investment prior to the effective date of the final QDIA regulations. This provision was added to accommodate employers who may not be able to transfer assets out of such investments without incurring significant expenses and penalties. To ensure broad application of this relief, the final QDIA regulations, as amended, now provide that a grandfathered stable value product or fund must be designed to "preserve" principal rather than designed to "guarantee" principal. In addition, the amendment also provides that such stable value products or funds must invest primarily in investment products that are backed by State or federally regulated financial institutions. Thus, these investment products may be issued directly by such institutions. Alternatively, the principal and accrued interest on the investment products may be backed by contracts issued by such institutions.

These technical corrections are effective April 30, 2008.

Highlights of Field Assistance Bulletin (FAB) 2008-03

This FAB is intended to provide additional guidance on the final QDIA regulations. The FAB covers the following areas:

- Scope of Final QDIA Regulations
- Notice Requirements
- 90-Day Limitation on Fees and Restrictions
- Management and Asset Allocation
- 120-day Capital Preservation QDIA
- Grandfather-Type Relief for Stable Value Products and Funds

Scope of Final QDIA Regulations

- A plan sponsor that chooses to create and manage a QDIA itself may be relieved of liability for investing in the QDIA only if the requirements of the final QDIA regulations are met and the plan sponsor is a named plan fiduciary.
- The FAB makes clear that the relief available under the QDIA regulations is not limited to assets invested in the QDIA on and after the effective date of the final QDIA regulations. If the notice and other requirements for fiduciary relief under the QDIA regulations are satisfied, the fiduciary will be relieved of liability with respect to all assets invested in the QDIA, except to the extent limited in the QDIA regulations. However, the relief only applies to the fiduciary's decisions made on and after the date all requirements of the final QDIA regulations are satisfied. No relief is available under the QDIA regulations for fiduciary decisions made before the effective date of the final QDIA regulations.

  Furthermore, the fiduciary relief extends to assets invested in the QDIA on behalf of participants who, on and after the effective date of the final QDIA regulations, fail to provide investment direction whether or not the participant made an earlier affirmative election to invest in the default investment.
- A fiduciary that invests amounts consisting of Qualified Nonelective Contributions (QNECs) or proceeds from litigation or other settlements in a plan's QDIA without first giving participants the opportunity to direct such amounts will not get relief from the final QDIA regulations. However, if participants are given the opportunity to direct such amounts or, after the amounts are invested in the QDIA, participants are provided with the opportunity to direct the investment, relief under the final QDIA regulations may be available.
- Fiduciary relief under the QDIA regulations is available to 403(b) plans subject to Title I of ERISA.

Notice Requirements

- Using separate, but simultaneously furnished documents would satisfy the notice requirements regarding disclosure of fee and expense information attendant to a plan's QDIA. According to the FAB, in the absence of additional guidance, the furnishing of a prospectus or profile prospectus of an investment allocation subject to the Securities Act of 1933 along with the other information required by the final QDIA regulations could be used to satisfy the required QDIA disclosures.

  In the absence of further guidance, the DOL believes that the following information should be provided to participants with respect to the fees and expenses attendant to the QDIA:
    - a description and the amount of any shareholder-type fees, such as sales loads, sales charges, deferred sales charges, redemption fees, surrender charges, exchange fees, account fees, purchase fees and mortality and expense fees; and
    - for investments with respect to which performance may vary over the term of the investment, the total annual operating expenses (expense ratio).
- The DOL is developing a proposed regulation that would establish disclosure requirements for participant-directed defined contribution plans. The DOL expects that furnishing the information required under this proposed regulation will satisfy the QDIA required investment-related fee and expense information.
- The QDIA notice may be distributed by use of electronic media.
- As we previously reported in TCRS 2007-07, the final QDIA regulations provide that the QDIA notice and the automatic enrollment notice may be combined. The FAB makes clear that the employee notice required for traditional 401(k) safe harbor plans may also be combined with the QDIA notice.

90-Day Limitation on Fees and Restrictions

- The FAB makes clear that the payment of a fee or expense (e.g. a redemption fee) by a plan sponsor or service provider would satisfy the requirement of the QDIA regulations that no restrictions, fees or expenses (including surrender charges, liquidation or exchange fees and redemption fees) be charged to a participant's account for transfers and withdrawals by the participant within the first 90 days of the participant's first investment in a QDIA. The FAB further clarifies that the 90-day period does not apply to participants who have existing assets invested in the QDIA.
- Consistent with the technical corrections to the final QDIA regulations, for the first 90 days of a participant's first elective contribution (or other investment) in a QDIA, "round-trip" restrictions will be permissible, unless the "round-trip" restriction affects the participant's ability to liquidate or transfer from a QDIA or to invest in any other investment alternative under the plan.

QDIAs – Management and Asset Allocation

The FAB clarifies that an investment fund with zero fixed income or zero equity will not qualify as one of the QDIAs described in the final QDIA regulations. According to the DOL, a QDIA should have some fixed income and equity exposure. The final QDIA regulations do not, however, establish minimum fixed income or equity exposures necessary to satisfy the requirement for a “mix” within a QDIA. It is up to the entity with responsibility for managing a plan’s QDIA to determine any minimums.

- Participants defaulted in a QDIA should be furnished the same materials relating to their investment in a QDIA as are provided to participants who direct their own investments in an ERISA 404(c) plan. Thus, for purposes of the final QDIA regulations, defaulted participants are required to be automatically provided the most recent prospectus or profile prospectus (in the case of registered investment companies) and any material relating to the voting, tender or similar rights under the plan. In addition, information regarding the plan’s investment alternatives, such as annual operating expenses and the value of shares or units in the investment alternatives must also be furnished either automatically or upon request.
- A plan sponsor may use more than one QDIA under its plan, for example, one QDIA for automatic enrollment contributions and a second QDIA for other contributions.
- Consistent with the technical corrections to the final QDIA regulations, the FAB states that a committee that is the named fiduciary of a plan and is comprised primarily of employees of the plan sponsor may manage a QDIA.

120-Day Capital Preservation QDIA

- The FAB clarifies that the 120-day Capital Preservation QDIA may only be used with an Eligible Automatic Contribution Arrangement (EACA). Thus, a plan fiduciary that uses a 120-day Capital Preservation QDIA with assets other than those contributed pursuant to an EACA will not obtain fiduciary relief under the final QDIA regulations.
- A plan sponsor is not required to use a 120-day Capital Preservation QDIA.
- A plan sponsor, generally, may not manage a 120-day Capital Preservation QDIA. The investment fund or product must be offered by a State or federally regulated financial institution as required by the final QDIA regulations.

Grandfather-Type Relief for Stable Value Funds

- The FAB reiterates that the fiduciary relief provided by the final QDIA regulations for prior contributions to a stable value product or fund generally will not take effect until thirty (30) days after the initial notice is furnished to participants. Furthermore, regardless of the date on which fiduciary relief is available, the relief will extend only to assets invested in the stable value product or fund on or before the effective date of the final QDIA regulations.
- Consistent with the technical corrections to the final QDIA regulations, the FAB provides that to ensure broad application of the grandfather-type relief for assets invested in certain stable value products or funds, the relief is available to stable value products or funds designed to preserve principal; provide a rate of return generally consistent with that earned on intermediate investment grade bonds; and provide liquidity for withdrawals by participants, including transfers to other investment alternatives. No fees or surrender charges may be imposed on withdrawals by participants and the products or funds must invest primarily in investment products backed by State or federally regulated financial institutions.

Questions about FAB 2008-03 and the QDIA regulations may be directed to the Division of Fiduciary Interpretations, Office of Regulations and Interpretations, at (202) 693-8510 (not a toll free number).

*This Summary is designed to provide an overview of the DOL’s Technical Corrections to the final QDIA regulations and Field Assistance Bulletin 2008-03 and is not intended to be comprehensive. The Transamerica Center for Retirement Studies® (“The Center”) is a non-profit corporation and private operating foundation. The Center may be funded by contributions from Transamerica Life Insurance Company and its affiliates or other unaffiliated third-parties. For more information about The Center, please refer to **www.transamericacenter.org**. The Center and its representatives cannot give ERISA, tax or legal advice. This material is provided for informational purposes only and should not be construed as ERISA, tax or legal advice. Interested parties must consult and rely solely upon their own independent advisors regarding their particular situation and the concepts presented here. Although care has been taken in preparing this material and presenting it accurately, The Center disclaims any express or implied warranty as to the accuracy of any material contained herein and any liability with respect to it.*