

MEMO# 4178

October 14, 1992

DEPARTMENT OF LABOR ISSUES FINAL REGULATION UNDER ERISA SECTION 404(C)

October 14, 1992 TO: BOARD OF GOVERNORS NO. 74-92 RE: DEPARTMENT OF LABOR
ISSUES FINAL REGULATION UNDER ERISA SECTION 404(c)

Attached is a copy of the final regulation issued yesterday by the Department of Labor under section 404(c) of the Employee Retirement Income Security Act of 1974 (ERISA). Section 404(c) provides that, where a participant in a retirement plan exercises control over the assets in his individual account, the fiduciaries of the plan (i.e., the employer) are relieved of liability for the results of the participant's exercise of control. The Institute first submitted proposals for a regulation under section 404(c) 16 years ago, in June of 1976. The final regulation includes a number of provisions recommended by the Institute and we are hopeful that the regulation will lead many plan sponsors to select mutual funds as their plans' funding vehicles. In order to constitute an "ERISA section 404(c) plan" under the regulation, an individual account plan must provide an opportunity for a participant to exercise control over the assets in his account and must provide the participant an opportunity to choose, from a broad range of investment alternatives, the manner in which some or all of the assets in his account are invested. In order for a participant to have the opportunity to exercise control over his account, he must have a reasonable opportunity to give investment instructions to an identified plan fiduciary who is generally obligated to comply with such instructions. The instructions may be in writing or otherwise, but the participant must have the opportunity to obtain written confirmation of such instructions. A plan may impose reasonable restrictions upon the frequency with which participants may give investment instructions; however, the frequency must be appropriate in light of the market volatility of the investment. In addition, the participant must have sufficient information to make informed decisions concerning the available investments. The participant must be provided certain items of information concerning the available investments, including a general description of the investment objectives and risk and return characteristics of the investment, and any transaction fees and expenses in connection with purchases or sales, including sales loads and deferred sales charges. Participants must also be informed of the information that may be obtained upon request, which includes the annual operating expenses of the investment, copies of any prospectuses provided to the plan, and performance information. The requirement that the plan offer a broad range of investment alternatives will be satisfied if participants can choose among at least three diversified alternatives, each of which has materially different risk and return characteristics and which in the aggregate enable the participant to achieve a portfolio with risk and return characteristics at any point within the range normally appropriate for the participant. The

range of investments must also tend to minimize through diversification the overall risk of the participant's portfolio. With respect to these "core" investment options, participants must be permitted to give investment instructions at least once within any three-month period. The participant must also be able to diversify his account so as to minimize the risk of large losses. Where the participant's account is limited in size, a plan can satisfy this requirement only by offering "look-through investment vehicles," including investment companies. The final regulation is generally effective for transactions occurring on or after January 1, 1994. Transactions occurring before that date are governed by section 404(c) without regard to the regulation. Matthew P. Fink Attachment

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