

MEMO# 2614

March 13, 1991

DEPARTMENT OF LABOR REPROPOSES ERISA 404(C) REGULATION

March 13, 1991 TO: PENSION COMMITTEE NO. 8-91 RE: DEPARTMENT OF LABOR
REPROPOSES ERISA 404(c) REGULATION

Attached is a copy of the Department of Labor's repropose regulation under ERISA Section 404(c). ERISA Section 404(c) provides that, when a participant of an employee pension benefit plan exercises control (as defined by regulation) over the investment of assets in an individual account, the fiduciaries of the plan are not liable for plan losses which result from the participant's exercise of control. The Department of Labor first proposed a regulation under ERISA Section 404(c) on September 3, 1987. (See Institute Memorandum to Pension Members No. 44-87, dated September 8, 1987.) The repropose regulation provides, in general, that in order for a participant to exercise control over the assets in his individual account, the participant or beneficiary must have the opportunity to (1) choose from a broad range of investment alternatives, which consist of at least three diversified investment categories, each of which has materially different risk and return characteristics, (2) give investment instruction with a frequency which is appropriate in light of the market volatility of the investment alternatives, but not less frequently than once within any three month period, and (3) diversify investments generally and within investment categories. Unlike the 1987 regulation, the new proposal does not require defined investment alternatives to be made available to participants. Rather, the regulation is designed so that plan sponsors are not limited in their ability to accommodate changes in employee needs and changes in investment products and markets. The regulation does not require any "safe" or "default" investment option which plan administrators could use to invest accounts of participants who make no affirmative investment decision. As a result, ERISA Section 404(c) could not apply to the accounts of such individuals. The regulation requires quarterly transferability among at least three investment vehicles. The plan may offer additional investment vehicles with greater or less frequency of transfer. However, the least volatile of the three basic investment alternatives must permit transfers as often as that permitted by the most volatile investment alternative under the plan. In determining whether a plan provides a broad range of investment alternatives, only those investment alternatives are to be taken into account as to which sufficient information is available to the participant to permit informed investment decisions. This requirement is satisfied if an identified plan fiduciary is available to provide participants and beneficiaries with directions as to how such information may be obtained. The proposed regulation allows an ERISA 404(c) plan to offer employer stock as an investment alternative as long as the stock is "qualifying employer securities" as defined in ERISA Section 407(d)(5), publicly traded on a national exchange or other recognized market in sufficient volume to assure prompt purchase and sale, informational materials and proxy voting and similar rights are passed through to

participant shareholders and all activities relating to the purchase, sale and exercise of voting and similar rights are the responsibility of an independent fiduciary (one who is not affiliated with the plan sponsor) who carries out such activities on a confidential basis. The Department of Labor stated that it continues to believe that plan fiduciaries have an ongoing duty to consider the suitability of designated 404(c) plan investment vehicles in order to protect the interest of participants. This includes the continuing determination that each investment vehicle remains a prudent investment option. Section VII of the preamble to the proposal contains a request by the Department of Labor for specific information. The Department is interested in the number and type of investment options offered by participant-directed individual account plans, the frequency of investment direction, the type and value of investments selected by participants and the administrative costs involved in having at least three options in a participant- directed investment plan. Written comments on the re-proposed regulation must be received by the Department of Labor by May 13, 1991. A meeting has been scheduled tentatively for Wednesday, April 17, 1991 at 1:00 pm at the Institute to discuss the regulation. Please call Wynetta Singhateh at 202/955-3525 by April 1, 1991 if you will be able to attend. We will keep you informed of further developments. W. Richard Mason Assistant Counsel - Pension Attachment

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