

MEMO# 11770

March 28, 2000

DOL ISSUES PROPOSED INDIVIDUAL EXEMPTION FOR INVESTMENT ADVISORY SERVICE; APRIL 13TH CONFERENCE CALL SCHEDULED

1 As you know, the Institute has developed a legislative proposal concerning the provision of investment advice to participants. See Institute Memorandum to Pension Committee No. 17-00 and Ad Hoc Committee on Investment Advice, dated February 23, 2000. The proposal was described in the Institute's testimony recently submitted to the House Education and the Workforce Subcommittee on Employer-Employee Relations. See Institute Memorandum to Pension Committee No. 19-00 and Pension Operations Advisory Committee No. 18-00, dated March 17, 2000. 1 [11770] March 28, 2000 TO: PENSION COMMITTEE No. 22-00 AD HOC COMMITTEE ON INVESTMENT ADVICE RE: DOL ISSUES PROPOSED INDIVIDUAL EXEMPTION FOR INVESTMENT ADVISORY SERVICE; APRIL 13TH CONFERENCE CALL SCHEDULED

The Department of Labor has published a proposed individual exemption regarding the provision of certain asset allocation advisory services by Standard & Poor's Investment Advisory Services ("S&P"), an independent advice provider. A conference call has been scheduled for Thursday, April 13, 2000 at 2:00 p.m. EST to discuss whether the Institute should submit a comment letter.¹ Comments to the proposed exemption must be submitted by May 6, 2000. Under the proposed exemption, S&P, a registered investment adviser, would provide "personalized asset allocation advice" to plan participants through an agreement with a plan sponsor or with a service provider. Fees for the service would be based on a flat dollar amount per participant paid by the plan, plan sponsor, participant or the service provider. Participants would access the service through the Internet, by written materials or by telephone, and would be required to complete a risk tolerance questionnaire prior to using the service. Any recommendations provided would be implemented only at the express direction of the participant. Additionally, participants would be informed that S&P's recommendations, "based on an objective methodology developed in accordance with generally accepted investment theories," would be valid for one year and that the questionnaire process must be repeated in order to receive updated recommendations. Accordingly, S&P would remind participants annually about the possible need to update their investment allocations. S&P also would inform participants that they may need to respond to the questionnaire more than on a yearly basis where they experience "major life changes." In connection with the advisory service provided to participants, S&P would evaluate the investment options offered under a plan. For example, at the plan level, a plan with more than 5 investment options would be eligible to receive S&P's service. Where a plan offers 3 to 5 investment options, S&P would advise the plan

sponsor to add more options. In order to participate in the advisory program, a plan would also be required to meet certain standards relating to the diversity of funds 2 The Department, in the proposed exemption, notes that the fiduciary provisions of ERISA section 404 apply to an independent fiduciary's decision to authorize a plan's participation in the advisory service. An independent fiduciary, therefore, must act prudently in its decision to participate in the service. 2 offered and limits placed on transfers among investment options. Additionally, S&P would limit its service to investment options meeting certain criteria. For instance, each investment option's total net assets must be greater than \$25 million for all share classes of the fund combined. Furthermore, the investment option must have a minimum of three years of monthly total return data or reasonably sufficient alternative data. The proposed exemption conditions relief from sections 406(a) and (b) of ERISA on a number of requirements. Conditions that must be met include: ! An independent plan fiduciary must expressly authorize in writing the retention of S&P to provide its service2; ! S&P must provide to the independent fiduciary a number of disclosures in writing, including a description of the service and all fees and expenses associated with the service, and a 45-day advance notice of any material changes to the service or increase in related fees or expenses; ! A service provider that offers the investment vehicles for which the advisory services are provided must not at any time own any interest in S&P, and neither S&P nor an affiliate must own any interest in the service provider; ! The annual revenues received by S&P from any one service provider must not constitute more than 5 percent of the annual revenues of S&P; ! Fees payable to S&P may consist only of an annual flat fee based on a fixed dollar amount per participant and certain administrative fees, and no portion of the fees or consideration paid by plans or plan sponsors to S&P may be shared with a service provider; and ! S&P must comply with certain recordkeeping requirements that would enable individuals to determine whether the conditions of the exemption have been met. The proposed exemption also imposes eligibility requirements to qualify as a "service provider" under the exemption. The entity must have been in the financial services business for at least three years and must be: (i) a bank, savings and loan association, insurance company or registered investment adviser which meets the definition of a "qualified professional asset manager" set forth in Prohibited Transaction Exemption 84-14, with total client assets under management of at least \$250 million; or (ii) a broker dealer registered under the Securities Exchange Act of 1934 with \$1 million in shareholders' or partners' equity and total client assets under management of at least \$250 million. The service provider also may not have been a party to a settlement with the Department or the IRS, or found guilty in a court of law with respect to an employee benefit plan. If you would like to participate on the conference call scheduled for Thursday, April 13, 2000 at 2:00 p.m. EST to discuss the proposed exemption, please fill out the response form below and fax it to Daniel Ayers by Tuesday, April 11, 2000. If you have any questions or comments, please contact Russ Galer at (202) 326-5835, Kathryn Ricard at (202) 218-3563 or myself at (202) 326-5837. Thomas T. Kim Assistant Counsel Attachment 3

RESPONSE FORM FOR INSTITUTE CONFERENCE CALL REGARDING PROPOSED INDIVIDUAL EXEMPTION FOR INVESTMENT ADVISORY SERVICE THURSDAY, APRIL 13, 2000 AT 2:00 PM EST Please fax this form by Tuesday, April 11, 2000 to Daniel Ayers at (202) 326-5839. Yes, I will participate on the Conference Call on Thursday, April 13, 2000 at 2:00 p.m. EST. To participate in the call, dial (888) 727-2950 and ask for the Investment Company Institute call, confirmation number 3686662.

 _____ Committee Member
 _____ Company _____ Phone
 Number

Copyright © by the Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice.