



## BURNING BENEFITS NEWS

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### IN THIS ISSUE: NEW REQUIREMENTS FOR PARTICIPANT-DIRECTED PLANS

“Participant-directed” retirement plans, in which employees and beneficiaries are allowed to select how to invest their plan accounts, have become immensely popular and now account for the vast majority of 401(k) and similar plans. Along with their increased popularity, however, these plans have attracted increased attention by the Department of Labor and others. This scrutiny has now culminated in new participant disclosure regulations issued by the Department that will, starting later in 2011, apply to all participant-directed plans that are subject to the Employee Retirement Security Act of 1974 (“ERISA”).

There are already in place (and have been for many years) *optional* regulations that apply to participant-directed plan, under ERISA Section 404(c). Choosing to comply with Section 404(c) allows a sponsor (and other fiduciaries, like the plan committee and company officers) to avoid fiduciary liability for losses caused by participants’ own investment elections. To qualify for this special rule a sponsor must provide a sufficiently diverse “menu” of investment options under the plan, and meet specific disclosure and other requirements.

Stevenson Keppelman Associates has always strongly encouraged our clients who sponsor participant-directed plans to comply with Section 404(c). A plan sponsor that does not do so is potentially liable as a fiduciary for patently imprudent investment allocation decisions that participants make in their own accounts. That said, Section 404(c) compliance has been and continues to be legally optional. **The new disclosure requirements, by contrast, are not voluntary; they are mandatory.** These new rules have been issued by D.O.L. under ERISA § 404(a), the statute’s general prudence provision, and therefore apply to *every participant-directed plan subject to ERISA*. Any sponsor of a participant-directed ERISA plan that does not satisfy the new rules will be in violation of the statute and hence subject to an array of potential civil and even criminal penalties. (At the same time, Section 404(c) relief will continue to be optionally available to plan sponsors so long as they both comply with the new Section 404(a) disclosure rules and meet the remaining 404(c) requirements, including the diverse investment menu requirement mentioned above.)

The new regulations make compulsory many of the same participant disclosure requirements that have heretofore applied on an elective basis under Section 404(c). A sponsor must provide to participants:

- a description of each investment alternative available under the plan, including a general description of the investment objectives and risk and return characteristics, and information regarding the type and diversification of assets in the portfolio, and identity of any investment manager;

- an explanation of the circumstances under which participants may give investment instructions, transaction fees and expenses chargeable against a participant's account;
- a list of additional information which may be obtained by a participant upon request; and
- the name, address and phone number of the plan fiduciary responsible for giving additional information on request.

There are some differences, however, between the new rules and the existing 404(c) regulations. The most significant is that under the new regulations participants must be given a very specific type of comparison of the available investment options, in the form of a table that meets detailed DOL requirements. The table must include specific columns comparing, for each option, investment returns and expenses across different time periods and against relevant benchmarks. A copy of a “safe harbor” form of the new table provided by D.O.L., which will be deemed to comply with the regulatory requirement, is shown below.

One positive note: The new regulations do not require that a plan sponsor provide participants with paper prospectuses for investment options unless participants ask for them. The Section 404(c) regulations’ requirement that a paper prospectus be provided to any participant electing to invest in a mutual fund or similar investment option has been a long-standing source of administrative frustration (and, seemingly, wasted paper). The new rules eliminate this requirement for both Section 404(a) and 404(c) purposes. (Note, though, that the existing 404(c) rules – with the paper prospectus requirement intact – continue to be effective until the new rules’ effective date, for employers that seek to obtain 404(c) protection. **Thus, through the end of 2010 [for calendar year plans] the current 404(c) rules must be followed in order to retain such protection currently. SKA strongly recommends compliance with the current and future rules.**)

The new regulations become effective as of the start of the first plan year beginning after October 31, 2011 (that is, January 1, 2012, for a calendar year plan). Sponsors of participant-directed plans must be ready to provide the required disclosures as of that date. (Historically, large recordkeepers such as Fidelity, T.Rowe Price, Mass Mutual, etc. have disclaimed responsibility for complying with ERISA Section 404(c), and it remains to be seen if they will assist with compliance under the new 404(a) regulations. In any case, compliance requires legal analysis, and recordkeepers, etc. disclaim giving legal advice [as they must, as they are not attorneys.]) We will be contacting each of our clients as the new regulations’ effective date approaches in order to form a plan of compliance; in the meantime, however, if you have any questions, please contact one of us. We will also host a dial-in teleconference on these regulations in March (date to be announced).

Note that the new regulations are part of a broader initiative by the Department of Labor focused on fiduciary issues relating to participant-directed and other defined contribution retirement plans. The D.O.L. has been particularly concerned with the level of fees paid by plans, an issue that has also triggered a significant amount of recent litigation. In July of 2011, new regulations will take effect requiring full disclosure, by service providers to plans, of the fees they are charging. In this climate it is very important that plan sponsors be prepared to demonstrate “best practice” fiduciary steps. These include, among other things:

- establishing a properly chartered fiduciary committee;
- well-documented formal delegations of investment and administrative authority; and
- review of the adequacy of insurance, indemnification and bonding arrangements.

All of these actions should be undertaken by plan sponsors who have not already done so.

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**Table 1—Variable Return Investments**

Name/ Type of Option	Average Annual Total Return as of 12/31/XX				Benchmark			
	1yr.	5yr.	10yr.	Since Inception	1yr.	5yr.	10yr.	Since Inception
<b>Equity Funds</b>								
A Index Fund/ S&P 500 www. website address	26.5%	.34%	-1.03%	9.25%	26.46%	.42%	-.95%	9.30%
					S&P 500			
B Fund/ Large Cap www. website address	27.6%	.99%	N/A	2.26%	27.80%	1.02%	N/A	2.77%
					US Prime Market 750 Index			
C Fund/ Int'l Stock www. website address	36.73%	5.26%	2.29%	9.37%	40.40%	5.40%	2.40%	12.09%
					MSCI EAFE			
D Fund/ Mid Cap www. website address	40.22%	2.28%	6.13%	3.29%	46.29%	2.40%	-.52%	4.16%
					Russell Midcap			
<b>Bond Funds</b>								
E Fund/ Bond Index www. website address	6.45%	4.43%	6.08%	7.08%	5.93%	4.97%	6.33%	7.01%
					Barclays Cap. Aggr. Bd.			
<b>Other</b>								
F Fund/ GICs www. website address	.72%	3.36%	3.11%	5.56%	1.8%	3.1%	3.3%	5.75%
					3-month US T-Bill Index			
G Fund/ Stable Value www. website address	4.36%	4.64%	5.07%	3.75%	1.8%	3.1%	3.3%	4.99%
					3-month US T-Bill Index			
Generations 2020/ Lifecycle Fund www. website address	27.94%	N/A	N/A	2.45%	26.46%	N/A	N/A	3.09%
					S&P 500			
					23.95%	N/A	N/A	3.74%
					Generations 2020 Composite Index*			

\*Generations 2020 composite index is a combination of a total market index and a US aggregate bond index proportional to the equity/bond allocation in the Generations 2020 Fund.