NAGDCA NOTES

The Department of Labor Provides More Guidance on QDIAs

Although the Department of Labor's Employee Benefits Security Administration (EBSA) does not oversee the administration of governmental defined contribution plans, much of its guidance is used as a benchmark for public plans where applicable laws may not dictate a best practice. Recently the Department of Labor (DOL) finalized a rule on qualified default investment alternatives (QDIAs) for 401(k) plans. This final regulation was released on October 24, 2007 and is anticipated to go into full effect on December 24, 2007. The following information includes highlights from the final regulations, but a full version of the DOL's ruling can be viewed at www.dol.gov/ebsa/regs/fedreg/final/07-5147.htm.

Qualified Default Investment Alternatives (QDIA)

"The final regulation does not identify specific investment products – rather, it describes mechanisms for investing participant contributions. The intent is to ensure that an investment qualifying as a QDIA is appropriate as a single investment capable of meeting a worker's long-term retirement savings needs. The final regulation identifies two individually-based mechanisms and one group-based mechanism – it also provides for a short-term investment for administrative convenience.

The final regulation provides for four types of QDIAs:

- A product with a mix of investments that takes into account the individual's age or retirement date (an example of such a product could be a life-cycle or targeted-retirement-date fund);
- An investment service that allocates contributions among existing plan options to provide an asset mix that takes into account the individual's age or retirement date (an example of such a service could be a professionally-managed account);
- A product with a mix of investments that takes into account the characteristics of the group of employees as a whole, rather than each individual (an example of such a product could be a balanced fund); and
- A capital preservation product for only the first 120 days of participation (an option for plan sponsors wishing to simplify administration if workers opt-out of participation before incurring an additional tax).

A QDIA must either be managed by an investment manager, plan trustee, or plan sponsor who is a named fiduciary, or be an investment company registered under the Investment Company Act of 1940.

A QDIA generally may not invest participant contributions in employer securities."

Fiduciary Relief

"The final regulation provides the following conditions that must be satisfied in order to obtain safe harbor relief from fiduciary liability for investment outcomes:

- Assets must be invested in a "qualified default investment alternative" (QDIA) as defined in the regulation.
- Participants and beneficiaries must have been given an opportunity to provide investment direction, but have not done so.
- A notice generally must be furnished to participants and beneficiaries in advance of the first investment in the QDIA and annually thereafter. The rule describes the information that must be included in the notice.

- Material, such as investment prospectuses, provided to the plan for the QDIA must be furnished to participants and beneficiaries.
- Participants and beneficiaries must have the opportunity to direct investments out of a QDIA as frequently as from other plan investments, but at least quarterly.
- The rule limits the fees that can be imposed on a participant who opts out of participation in the plan or who decides to direct their investments.
- The plan must offer a "broad range of investment alternatives" as defined in the Department's regulation under section 404(c) of ERISA."

Exceptions for Capital Preservations Investments

- One exception allows investments in capital preservation products or funds to be treated as an in vestment in a QDIA for a 120 day period.
- The rule views it appropriate to include capital preservation products as a "limited-duration" QDIA to give plan sponsors the flexibility of using a near risk-free investment alternative for the investment contributions during the period of time when employees are most likely to opt out of plan participation.
- The rule also states that at the end of the 120-day period, capital preservation products would cease to be QDIA with respect to any assets of the participant that continued to be invested in such products.
- The second exception states that stable value products and funds should be addressed as QDIAs solely for purposes of investments in such products or funds made prior to the effective date of the regulation.

Notification Requirements

- The rule sets a time period for the 30-day advance notice requirement from the date of plan eligibility to better coordinate the notice requirements with the tax code provision governing permissible withdrawals.
- It also requires that the notice to participants be written in a manner that is "understood by the average plan participant."
- The rule does not include a model notice but has mentioned working with the Department of Treasury to develop such language.

Miscellaneous Issues

- "Preemption – Provides for preemption of federal law (ERISA) over state law regarding any pension plan that provides for automatic contribution arrangements, regardless of whether such plan includes an automatic contribution arrangement as defined in the regulation.
- Penalties – Provides for the development of implementing regulations to assess civil penalties for plan violations.
- Small Plan QDIAs – Provides for the consideration of providing guidance for small plans regarding prudent section of QDIAs."

Again, a complete version of the DOL's final ruling can be accessed at
www.dol.gov/ebsa/regs/fedreg/final/07-5147.htm.

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Department of Labor, Employee Benefits Security Administration: Default Investment Alternatives Under Participant Directed Individual Account Plans, GAO-08-256R, November 13, 2007: http://www.gao.gov/decisions/majrule/d08256R.htm.

Regulation Relating To Qualified Default Investment Alternatives In Participant-Directed Individual Account Plans: https://www.youth2work.gov/ebsa/newsroom/fsQDIA.html.

U.S Department of Labor: www.dol.gov/ebsa/regs/fedreg/final/07-5147.htm.