

November 2007

## **Department of Labor Issues Final Rules On Qualified Default Investment Alternatives Under Participant Directed Individual Account Plans**

Last year, the DOL issued proposed regulations, as directed by the Pension Protection Act of 2006, providing guidance on fiduciary relief for plan fiduciaries who invest participant accounts in default investment alternatives in the absence of affirmative participant investment direction. The DOL has now issued its final regulations, effective December 24, 2007, implementing the safe harbor for default investment alternatives. Under the final regulations, default investments may be used in the following situations:

- the failure of a participant to provide investment direction following automatic enrollment in a 401(k) plan,
- the failure of a participant or beneficiary to provide investment direction following the elimination of an investment alternative or a change in service provider,
- the failure of a participant or beneficiary to provide investment direction following a rollover from another qualified plan, or
- any other failure of a participant to provide investment instruction.

The following conditions must be satisfied in order to satisfy the safe harbor requirements:

- assets must be invested in a "qualified default investment alternative" (QDIA),
- 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,
- 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 regulations limit the fees that can be imposed on a participant who opts out of participation in the plan or who decides to direct their investments, and
- the plan must offer a "broad range of investment alternatives" as defined in the DOL's regulation under section 404(c) of ERISA.

The final regulations define a QDIA in the same manner as the proposed regulations but now provide a limited role for capital preservation funds. Plan fiduciaries must continue to prudently select and monitor QDIAs. The four categories of QDIAs are:

Lifestyle or Target Retirement Date Fund - offers a mix of investments based upon the participant's age or target retirement date,

Professionally Managed Account – where assets are invested by an investment manager among existing investment options offered under the plan, based on such factors as the participant's age or target date of retirement,

Balanced Fund - offers a mix of equity and fixed income investments that focuses on what is appropriate for participants of the plan as a whole instead of the individual, and

Capital Preservation Products – generally, stable value and money market funds designed to preserve principal and provide a reasonable rate of return ***but these investments may only be used for the first 120 days of participation in a plan.*** However, the final regulations grandfather such arrangements by providing relief for contributions invested prior to the effective date of the final rule.

In addition, a QDIA (1) must either be managed by an investment manager, plan trustee, or plan sponsor who is a named fiduciary, or a registered investment advisor, (2) may not, with limited exception, invest participant contributions in employer securities, and (3) may be offered through variable annuity contracts or other pooled investment funds.

With respect to participant notices, each participant whose account will be invested in a QDIA must be provided with an initial notice at least 30 days prior to the first investment in the QDIA or 30 days prior to the date the participant first becomes eligible to participate in the plan. Annual notices must be provided at least 30 days prior to the start of each plan year.

If these requirements are satisfied, then a plan fiduciary is relieved of liability for any losses resulting from a participant's investment in a QDIA. Also, this relief is available even if a plan does not satisfy all of the requirements for ERISA Section 404(c) relief.

If you have any questions about the final regulations, selecting a QDIA, adding an automatic enrollment feature to your 401(k) plan, or require assistance with the contents of participant notices, please call us.

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