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New Guidance on Default Investments for Retirement Plans

by B. David Joffe

The Department of Labor ("DOL") has issued correcting amendments to its final regulations regarding qualified default investment alternatives ("QDIAs"). They are effective April 30, 2008, and apply retroactively to the effective date of the final regulations, December 24, 2007.

The corrections change three areas of the final regulations:

- Modifying the "grandfather" relief for stable-value funds;
- Limitations on so-called "round-trip restrictions;" and
- The scope of who can manage a QDIA to now include a committee that is a named fiduciary of the plan.

The DOL also issued Field Assistance Bulletin No. 2008-03 providing guidance on QDIAs in the form of 22 questions and answers covering the scope of the final regulations, notice requirements, the 90-day limitation on fees and restrictions, 120-day capital preservation QDIAs, and grandfather relief for stable-value funds.

Stable-Value Funds

In perhaps the most significant correction, the DOL acknowledged that its description of stable-value products and funds in the final regulations limited the availability of grandfather relief for stable-value funds. Despite several references in the preamble to the grandfather relief for stable-value funds, the regulations appeared to exclude virtually all stable-value funds commonly offered in the market. The previous regulations required that the stable-value fund be "designed to guarantee principal and a rate of return generally consistent with that earned on intermediate investment grade bonds." It also provided that principal and rates of return had to be guaranteed by a State or federally regulated financial institution.

Under the amended regulation, the stable-value fund must only be "designed to preserve principal" and "provide a rate of return generally consistent with that earned on intermediate investment grade bonds." Further, such investment product or fund must now invest "primarily" in investment products that are backed by State or federally regulated financial institutions. As a result, the requirements in the regulations more closely match the nature of stable-value funds that have been commonly used by plans.

Round-Trip Restrictions

The final regulations limit the restrictions that can be imposed on participants or beneficiaries withdrawing or transferring from a QDIA in the 90-day period beginning with the first contribution. The withdrawal or transfer generally cannot be subject to restrictions, fees or expenses, except for certain ongoing administrative and investment fees. In the supplementary information to the final regulations explaining the restrictions, the DOL indicated that a "round-trip" restriction on the ability of the participant or beneficiary

to reinvest in a fund within a defined period of time was not permissible. In light of short-term trading restrictions for most funds, this restriction potentially posed a significant restriction on QDIAs.

As part of the correcting amendments, the DOL modified the supplementary information by indicating that the round-trip restriction was too broad and should not have been included as an example of an impermissible restriction. Most round-trip restrictions generally affect only a participant's ability to reinvest in the QDIA for a period of time without penalty—not the ability to withdraw or transfer the funds out of the QDIA after the initial investment; funds imposing such restrictions should be acceptable as QDIA options under the revised regulation. However, the DOL did note that, if the round-trip restriction would affect a participant's or beneficiary's ability to liquidate or transfer from the QDIA or restrict their ability to invest in any other investment, such a restriction would be impermissible.

Committee-Managed QDIA

The DOL also amended the final regulations regarding persons who may manage a QDIA. Under the regulations, the language includes a "plan sponsor" who is a "named fiduciary" of the plan. The DOL indicates that it understood the language to broadly accommodate employers that manage their plan investments in-house, including by committee. However, it now acknowledges that the reference to a "plan sponsor" raised concerns as to whether a committee that is a named fiduciary of the plan and is comprised primarily of employees of the plan sponsor can manage a QDIA when that committee, pursuant to plan documents, is a named fiduciary. To address this issue, the DOL amended the final regulations to make clear that such a committee of the plan sponsor may manage a QDIA.

If you have any questions about the correcting amendments or QDIAs, please contact one of the Employee Benefits and Executive Compensation attorneys at Boult, Cummings, Conners & Berry PLC:

Martha L. Boyd
615.252.2357
mboyd@boultcummings.com

Charles M. Cain II
615.252.2330
ccain@boultcummings.com

Andrew Elbon
615.252.2378
aelbon@boultcummings.com

B. David Joffe
615.252.2368
djoffe@boultcummings.com

Gordon Earle Nichols
615.252.2387
gnichols@boultcummings.com

John M. Scannapieco
615.252.2352
jscannapieco@boultcummings.com

Roundabout Plaza, 1600 Division Street, Suite 700 Nashville, TN 37203
615.244.2582 www.boultcummings.com