U.S. Department of Labor **Employee Benefits Security Administration**
Washington, D.C. 20210

October 3, 2006

2006-08A
ERISA SEC
404(a)

Donald J. Myers, Esq.
Reed Smith LLP
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Washington, D.C. 20005-3373

Dear Mr. Myers:

This is in response to your request for an advisory opinion on behalf of JPMorgan Chase Bank, N.A. (JPMorgan) regarding the application of the fiduciary responsibility provisions of Title I of the Employee Retirement Income Security Act of 1974, as amended (ERISA). Specifically you have inquired whether a fiduciary of a defined benefit plan may, consistent with the requirements of section 404 of ERISA, consider the liability obligations of the plan and the risks associated with such liability obligations in determining a prudent investment strategy for the plan.

You represent that JPMorgan, as a plan fiduciary, proposes to "risk manage" the assets of defined benefit plans by better matching the risks of a plan's investment portfolio assets with the risks associated with its benefit liabilities, with a goal toward reducing the likelihood that liabilities will rise at a time when the assets decline. Defined benefit plan liabilities are determined by a number of factors, most significantly the demography of the participant population (participants' number of years of service and/or expected length of time for payment of retirement benefits) and the interest rates used to calculate the present value of the plan's obligations for funding and accounting purposes.

According to your letter, these liabilities most closely correlate with fixed-income assets, so that one approach for risk managing assets would be to invest directly in a portfolio of fixed-income securities with a duration of the plan's benefit obligations. However, you note that there may be aspects of a plan's obligations that correlate more closely with other types of investments, and it may not be possible to match liabilities precisely with fixed-income securities due to limitations in the fixed-income market. As a result, you indicate that a variety of approaches may be used in practice, depending on the facts and circumstances of the particular plan.

In developing an asset allocation that better matches the risk and duration characteristics of a plan's benefit liabilities, you explain that the focus of JPMorgan's services would be on reducing the risk of underfunding to the plan and its participants and beneficiaries by reducing volatility in funding levels. In this regard, you note that there may be incidental benefits to the plan sponsor from maintaining more consistent funding levels, such as reduced volatility on the sponsor's financial statements and reduced minimum contribution obligations. However, you also note that the principal benefit of decreased volatility would be the reduced need for the plan to rely on the plan sponsor to meet its funding obligations, protecting the plan participants and beneficiaries in the event of the sponsor's insolvency.

Taking into account the foregoing, you have requested the views of the Department on whether a fiduciary of a defined benefit plan may, consistent with the requirements of section 404 of ERISA, consider the liability obligations of the plan and the risks associated with such liability obligations in determining a prudent investment strategy for the plan.

Sections 403(c) and 404(a)(1)(A) of ERISA require plan fiduciaries to discharge their duties with respect to a plan solely in the interest of plan participants and beneficiaries and for the exclusive purpose of providing benefits to participants and beneficiaries and defraying the reasonable expenses of administering the plan. Section 404(a)(1)(B) of ERISA requires plan fiduciaries to act with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character with like aims. These fiduciary standards apply to the selection and monitoring of plan investments, including plan investments made pursuant to a particular investment strategy. The frequency and degree of monitoring, will, of course, depend on the nature of such investments and their role in the plan's portfolio.

The general standards of fiduciary conduct contained in sections 404(a)(1) apply to any investment by a plan covered by Title I, including investments made pursuant to the described risk management investment strategy. Accordingly, fiduciaries of the plan must act prudently, solely in the interest of the plan's participants and beneficiaries, and for the exclusive purpose of providing benefits and defraying reasonable plan administrative costs when deciding whether to invest in a particular investment or use a particular investment strategy.

With regard to investing plan assets, the Department has issued a regulation, at 29 CFR 2550.404a-1, interpreting the prudence requirements of ERISA as they apply to the investment duties of fiduciaries of employee benefit plans. The regulation provides that the prudence requirements of section 404(a)(1)(B) are satisfied if (1) the fiduciary making an investment or engaging in an investment course of action has given appropriate consideration to those facts and circumstances that, given the scope of the fiduciary's investment duties, the fiduciary knows or should know are relevant, and (2) the fiduciary acts accordingly. This includes giving appropriate consideration to the role that the investment or investment course of action plays with respect to that portion of the plan's investment portfolio within the scope of the fiduciary's responsibility.

The regulation further specifies the facts and circumstances that must be given appropriate consideration to include, but not be limited to, (A) a determination by the fiduciary that the particular investment or investment course of action is reasonably designed, as part of the portfolio (or, where applicable, that portion of the plan portfolio with respect to which the fiduciary has investment duties) to further the purposes of the plan, taking into consideration the risk of loss and the opportunity for gain (or other return) associated with the investment or investment course of action and (B) consideration of the following factors as they relate to such portion of the portfolio: (i) the composition of the portfolio with regard to diversification; (ii) the liquidity and current return of the portfolio relative to the anticipated cash flow requirement of the plan; and (iii) the projected return of the portfolio relative to the funding objectives of the plan.

Within the framework of ERISA's prudence, exclusive purpose and diversification requirements, the Department believes that plan fiduciaries have broad discretion in defining investment strategies appropriate to their plans. In this regard, the Department does not believe that there is anything in the statute or the regulations that would limit a plan fiduciary's ability to take into account the risks associated with benefit liabilities or how those risks relate to the portfolio management in designing an investment strategy.

For these reasons, a fiduciary would not, in the view of the Department, violate their duties under sections 403 and 404 solely because the fiduciary implements an investment strategy for a plan that takes into account the liability obligations of the plan and the risks associated with such liabilities and results in reduced volatility in the plan's funding requirements. Whether any particular investment strategy is prudent with respect to a particular plan will depend on all the facts and circumstances involved.

This letter constitutes an advisory opinion under ERISA Procedure 76-1. Accordingly, it is issued subject to the provisions of that procedure, including section 10 thereof relating to the effect of advisory opinions.

Sincerely,

Louis J. Campagna
Chief, Division of Fiduciary Interpretations
Office of Regulations and Interpretations