



The  
ERISA  
Industry  
Committee

**SUBMISSION OF  
THE ERISA INDUSTRY COMMITTEE  
TO THE  
EMPLOYEE BENEFITS SECURITY ADMINISTRATION  
U. S. DEPARTMENT OF LABOR**

**COMMENTS ON PROPOSED REGULATION:**

**DISCLOSURE REQUIREMENTS  
FOR  
PARTICIPANT-DIRECTED INDIVIDUAL ACCOUNT PLANS**

**September 8, 2008**

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**§§ 2550.404a-5 & 2550.404(c)-1,  
73 *Fed. Reg.* 43,014-44 (July 23, 2008)**

**September 8, 2008**

The ERISA Industry Committee (“ERIC”) is pleased to submit these comments on the Department’s proposed regulation creating new disclosure requirements for participant-directed individual account plans. The proposed regulation would require plan fiduciaries to disclose certain investment information, including fee and expense information, to participants and beneficiaries who have the right to direct the investment of their retirement accounts. Under the proposed regulation, the disclosure of this information would be a fiduciary obligation under § 404(a) of ERISA. Accordingly, the new disclosure requirements would apply to all participant-directed individual account plans, regardless of whether they rely on the fiduciary exception in ERISA § 404(c).

**ERIC’s Interest in the Proposed Regulation**

ERIC is a nonprofit association committed to the advancement of the employee retirement, health, incentive, and welfare benefit plans of America’s largest employers. ERIC’s members provide comprehensive retirement savings programs and other economic security benefits directly to some 25 million active and retired workers and their families. ERIC has a strong interest in proposals that affect its members’ ability to deliver high-quality, cost-effective benefits.

All of ERIC’s members sponsor individual account plans, including many of the largest individual account plans in the country. In the great majority of these plans, participants are responsible for directing how their accounts are allocated among the plan’s investment options. ERIC’s members share the Department’s view that participants should receive the information they need to make informed decisions about the investment of their retirement savings. ERIC’s mem-

bers also believe that the potential benefits of each disclosure requirement must be carefully weighed against the very real costs and administrative burdens imposed on plan fiduciaries, and against the risk that overloading participants with information will impair their ability to make sound investment decisions. ERIC's members have a vital interest in assuring that the regulation achieves its objectives in a way that is consistent with effective and efficient plan administration and communication. ERIC looks forward to working constructively with the Department to achieve this goal.

ERIC's members are still reviewing and evaluating the proposed regulation. ERIC will supplement these comments as necessary if its members identify additional issues that should be addressed.

### **Effective Date**

#### **1. The regulation should not become effective earlier than 12 months after Department issues the final regulation.**

The Department has proposed to make the regulation effective for plan years beginning on or after January 1, 2009. This proposed effective date is not realistic. As explained below, fiduciaries will need substantially more time to comply with the new disclosure requirements. ERIC recommends that the requirements become effective no earlier than the first plan year beginning at least 12 months after the final regulation is published in the *Federal Register*.

As the Department has recognized in the preamble of the proposed regulation, some of the required information (particularly for funds that are not registered under the securities laws) does not currently exist. Other information, although it might exist, is controlled by fund managers and other third parties and is not readily available to plan fiduciaries. Even where the information exists and is available, fiduciaries must develop systems that will gather information from multiple sources and display the information in the new comparative format required under the proposed regulation.

In order to comply with the new disclosure requirements, plan sponsors and fiduciaries must complete a number of complex tasks. These tasks will be particularly difficult for plans that have not been designed as § 404(c) plans; but even § 404(c) plans will have to gather new information and present it in new ways. For example, plan sponsors and fiduciaries must:

- amend plan and trust documents to allocate responsibility for satisfying the disclosure requirements;
- amend the charters and policies of administrative committees to reflect the new disclosure responsibilities;

- develop new information-gathering processes to collect and assemble performance data and fee and expense information from many different sources;
- create and test new software that will capture and transmit the required information;
- develop investment-related disclosure documents for in-house managed funds that are not subject to prospectus requirements;
- negotiate with the external managers of collective trusts, insured separate accounts, and other unregistered investment funds to make sure that they will provide required information in an appropriate format;
- identify appropriate performance benchmarks for designated investment options and gather information concerning the past performance of the benchmarks;
- modify existing Web sites and (in some cases) create new ones;
- develop investment-related communications that will be understandable to the average participant;
- develop new plan enrollment procedures and documents;
- revise the format of quarterly and annual benefit statements to incorporate required disclosures; and
- revise and print summary plan descriptions.

These steps cannot be taken in isolation. Plan fiduciaries must work with in-house staff and outside experts from many different disciplines, including legal, investment management, information technology, data security, human resources, and finance personnel. Fiduciaries also must work with third-party administrators, recordkeepers, and fund managers to coordinate the gathering and delivery of information, and to ensure that their different systems interact properly. The resources of plan service providers will be severely strained as large providers of investment, administrative, and recordkeeping services work with many different companies to bring thousands of plans—covering many millions of employees—into compliance simultaneously.

The cost of implementing these changes will be substantial. In order to avoid wasted effort and unnecessary expense, plan fiduciaries must wait until final regulations have been issued before they begin to develop compliance systems and procedures. In the next year or two, as fiduciaries and service providers work to comply with the new disclosure requirements for participant-directed plans, the same fiduciaries and service providers will be struggling to comply with the Department's new annual reporting requirements under ERISA § 104 and its new requirements for service contracts under ERISA § 408(b)(2), as well as continuing to

implement the changes enacted in the Pension Protection Act of 2006. Considering all of these factors, ERIC believes that 12 months is the minimum amount of time plan fiduciaries will need to implement the new disclosure requirements in an orderly way.

**2. The Department should make clear that ERISA’s fiduciary provisions did not previously require disclosure.**

The preamble of the proposed regulation includes the following statement:

The Department believes, *as an interpretive matter*, that ERISA section 404(a)(1)(A) and (B) impose on fiduciaries of all participant-directed individual account plans a duty to furnish participants and beneficiaries information necessary to carry out their account management and investment responsibilities in an informed manner.

73 *Fed. Reg.* at 43,015 (emphasis added). The preamble goes on to state that this fiduciary duty of disclosure “typically would have been satisfied” by plans that elected to comply with ERISA § 404(c). *Id.* In the case of plans that did not comply with the disclosure requirements under § 404(c), however, the Department “expresses no view” concerning the plans’ compliance during the period before the proposed regulation becomes effective. *Id.*

These statements are unwarranted. The proposed regulation is an exercise of the Department’s rulemaking authority under ERISA § 505, which permits the Department to “prescribe such regulations as [it] finds necessary or appropriate to carry out the provisions of [Title I].” The proposed regulation is not an interpretation of a disclosure obligation that ERISA’s fiduciary provisions currently impose.

The Department’s own rulemaking procedure recognizes that the proposed regulation imposes entirely new disclosure obligations. The Department considered a number of alternatives to the proposed regulation, including the possibility of “*establishing* a general, non-specific disclosure rule requiring that plan fiduciaries take steps to ensure that participants and beneficiaries of participant-directed individual account plans are provided sufficient information to make informed decisions about the management of their individual accounts.” 73 *Fed. Reg.* at 43,030 (emphasis added). There would be no need to “establish” such a rule if ERISA § 404(a) already imposed this obligation.

Title I, Part 1 of ERISA imposes detailed disclosure obligations on plan administrators, including an obligation to provide a summary plan description “sufficiently accurate and comprehensive to reasonably apprise . . . participants and

beneficiaries of their rights and obligations under the plan.” ERISA § 102(a). Courts have often pointed to these specific statutory disclosure requirements as evidence that ERISA § 404(a) does not impose a general fiduciary duty to disclose investment-related information. For example, in *DiFelice v. Fiduciary Counselors, Inc.*, 398 F. Supp. 2d 453, 463-64 (E.D. Va. 2005), the court described the state of the law as follows:

In view of the substantial disclosure obligations imposed expressly by ERISA, courts, in general, have been unwilling to read other provisions of ERISA, including § 404(a), as creating an implicit duty to disclose additional information. . . . [T]he Fourth Circuit has refused to use § 404(a) to supplement ERISA’s disclosure requirements based on the principle that specific provisions within a statute govern its general provisions and that this principle has “special force with regard to a reticulated statute such as ERISA.” *Faircloth v. Lundy*, 91 F.3d 648, 657 (4th Cir. 1996) (quoting *Bigger v. American Commercial Lines*, 862 F.2d 1341, 1344 (8th Cir. 1988)). Thus, compliance with the express disclosure requirements of ERISA will generally satisfy a fiduciary’s duty to provide information to participants.

*See also* *Nechis v. Oxford Health Plans, Inc.*, 421 F.3d 96, 102 (2d Cir. 2005) (“Nechis’s allegations with respect to disclosure violations [relying on § 404] are unavailing. Oxford has no duty to disclose to plan participants information additional to that required by ERISA . . . .”); *James v. Pirelli Armstrong Tire Corp.*, 305 F.3d 439, 451 (6th Cir. 2002) (“[N]o court of appeals has imposed fiduciary liability for a failure to disclose information that is not required to be disclosed.”); *Ehlmann v. Kaiser Foundation Health Plan of Texas*, 198 F.3d 552, 555 (5th Cir. 2000) (“While § 404 makes no reference to any duty to disclose, ERISA contains numerous other provisions detailing . . . disclosure duties . . . . That Congress and DOL were so capable of enumerating disclosure requirements when they wanted to means that the absence of one . . . was probably intentional.”); *Sprague v. General Motors Corp.*, 133 F.3d 388, 405 (6th Cir. 1998) (“It would be strange indeed if ERISA’s fiduciary standards could be used to imply a duty to disclose information that ERISA’s detailed disclosure provisions do not require to be disclosed.”); *Pedraza v. The Coca-Cola Company*, 456 F. Supp. 2d 1262, 1280 (N.D. Ga. 2006) (“No Court of Appeals has recognized an ERISA duty to make disclosures beyond ERISA’s detailed disclosure requirements.”). As the courts have recognized, a fiduciary does not have a general obligation to disclose investment-related information to plan participants, other than the statutory obligation to provide an accurate and up-to-date summary plan description.



The Department has estimated that 20% of the participants in non-§ 404(c) plans do not receive investment-related disclosure similar to the disclosure currently required under § 404(c). 73 *Fed. Reg.* at 43,027. Under the Department's own guidance, there is no reason to think that the fiduciaries of these plans are in breach of an implied duty of disclosure. The Department's existing regulation under § 404(c) states that the standards set forth in that regulation, including the disclosure requirements, "*are not intended to be applied* in determining whether, or to what extent, a plan which does not meet the requirements for an ERISA section 404(c) plan or a fiduciary with respect to such a plan satisfies the fiduciary responsibility or other provisions of Title I of the Act." 29 C.F.R. § 2550.404c-1(a)(2) (emphasis added).

The Department should recognize that the proposed regulation creates new disclosure obligations that have not applied to plan fiduciaries in the past (whether under a § 404(c) or non-§ 404(c) plan) and that will not apply in the future until the regulation becomes effective. Any suggestion that the regulation is an "interpretation" of existing law conflicts with current law and with the Department's regulation under § 404(c), on which fiduciaries have reasonably relied. Compare 73 *Fed. Reg.* at 43,015 with 29 C.F.R. § 2550.404c-1(a)(2).

The Department should disavow the suggestion in the preamble to the proposed regulation that past compliance or non-compliance with the § 404(c) disclosure standards has any bearing on plan fiduciaries' compliance with their obligations under ERISA § 404(a). Unless this suggestion is corrected, it will serve only to encourage costly litigation that does nothing to advance the interests of plan participants.

### **Scope of Disclosure Requirement**

- 3. If a fiduciary fails to disclose required information, the fiduciary is liable under ERISA only for investment losses that are caused by the fiduciary's breach of duty.**

ERISA § 404(c) creates an exception to ERISA's generally applicable fiduciary liability provisions. If a plan complies with the requirements of § 404(c), the participant is not deemed to be a fiduciary by reason of exercising investment control over his or her account, and no person who is otherwise a fiduciary is liable for any loss that results from the participant's exercise of control.

If a plan fails to comply with the disclosure requirements imposed by § 404(c), the plan will not qualify for § 404(c) protection. The loss of § 404(c) protection does not mean that the plan's fiduciaries are automatically liable for the plan's investment losses, however. Instead, in a non-§ 404(c) plan, the ordinary fiduciary principles of ERISA operate without reference to the special exception in § 404(c).

Under ERISA § 3(21), as long as the participants in a non-§ 404(c) plan have the authority to direct the investment of assets allocated to their accounts, the participants will have responsibility for their investment decisions. As the United States Court of Appeal for the Seventh Circuit explained,

Although section 404(c) and its accompanying regulation, 29 C.F.R. § 2550.404c-1, create a safe harbor for a trustee, we see no evidence that these provisions necessarily are the only possible means by which a trustee can escape liability for participant-directed plans. . . . [T]he statute, when read as a whole along with the accompanying regulations, permits a plan trustee to delegate decisions regarding the investment of funds to plan participants even if the plan does not meet the requirements for the section 404(c) safe harbor.

*Jenkins v. Yager*, 444 F.3d 916, 923 (7th Cir. 2006). The court rejected the plaintiff's assertion that the fiduciary "violated his fiduciary duty by failing to review each participant[s] investment directions throughout the year to ensure they were appropriate"; the court held that ERISA does not require fiduciaries "to investigate each participant's circumstances." *Id.* at 925.

In creating the new disclosure requirements under § 404(a), the Department has recognized that participants are responsible for the management and investment of their accounts in a participant-directed plan. If participants were not affected by their investment decisions, they would have no need for the investment-related disclosure mandated by the proposed regulation.

Although the Department may create a new duty of disclosure under ERISA § 404(a), the Department has no authority to impose strict liability for a fiduciary's breach of this duty. Under ERISA § 409(a), a fiduciary is liable only for losses that *result from* the fiduciary's breach. *Silverman v. Mutual Benefit Life Ins. Co.*, 138 F.3d 98, 104 (2d Cir. 1998) ("[Plaintiff] must show some causal link between the alleged breach of [the fiduciary's] duties and the loss plaintiff seeks to recover."); *Kuper v. Iovenko*, 66 F.3d 1447, 1459-60 (6th Cir. 1995) ("[T]o show that an investment decision breached a fiduciary's duty to act reasonably in an effort to hold the fiduciary liable for a loss attributable to this investment decision, a plaintiff must show a causal link between the [breach] and the harm suffered by the plan."; *Diduck v. Kasycki & Sons Contractors, Inc.*, 974 F.2d 270, 279 (2d Cir. 1992) ("[P]roof of a causal connection . . . is required between a breach of fiduciary duty and the loss alleged."). Accordingly, the plan fiduciaries who are responsible for satisfying the new disclosure requirements under ERISA § 404(a) will be liable only if their failure to disclose required information results in a loss to the plan. If a fiduciary fails to provide a participant with required information, but the information

was not material to the participant's investment decision, the fiduciary is not liable for any loss that results from the participant's decision. *Silverman*, 138 F.3d at 104; *In re Unisys Savings Plan Litig.*, 173 F.3d 145, 158-59 (3d Cir. 1999) (affirming judgment for plan where plaintiff "did not prove that any alleged failures to disclose caused the participants to suffer damages"); *Kuper*, 66 F.3d at 1459-60; *McDonald v. Provident Indemnity Life Ins. Co.*, 60 F.3d 234, 237-38 (5th Cir. 1995) (affirming judgment for plan where plaintiff proved breach of duty to disclose but failed to show a resulting loss to the plan). The final regulation should make this point clear.

**4. A fiduciary should not be liable for erroneous information furnished by others unless the fiduciary is aware of the error and fails to take reasonable measures to correct the error.**

The proposed regulation requires fiduciaries to obtain investment-related information from the managers of designated investment alternatives and to provide the information to participants and beneficiaries. Prop. Reg. § 2550.404a-5(d). In the case of registered mutual funds or other registered securities, much of the information might be included in a prospectus or other statutory disclosure document that is available to all investors. In contrast, if a plan offers designated investment alternatives that are not required to be registered under the securities laws, such as collective trusts or in-house managed funds, the fiduciaries must obtain the required information directly from the fund's managers.

A footnote in the preamble states that "fiduciaries shall not be liable for their reasonable good faith reliance on information furnished by their service providers with respect to those disclosures required by paragraph (d)(1)." 73 *Fed. Reg.* at 43,018 n. 7. This is an important statement that should be included in the regulation itself. Fiduciaries are increasingly subject to burdensome and expensive litigation involving investment-related disclosures over which they have little or no control. The final regulation should make clear that fiduciaries cannot be held responsible for information that they obtain from a third party and disclose in good faith. The statement concerning fiduciaries' limited responsibility should extend not only to the information described in paragraph (d)(1), which is provided in all cases, but also to the information described in paragraphs (d)(2) and (d)(3), which is provided subsequent to investment or upon request.

**5. The regulation should not use the word "monitor" to describe a fiduciary's duty periodically to review the performance of the plan's service providers and investment options.**

Proposed regulation § 2550.404a-5(f) and § 2550.404(c)-1(d)(2)(iv) state that the regulation does not relieve a fiduciary of its duty prudently to select and

monitor service providers, designated investment managers, and designated investment alternatives under a plan.

ERIC is concerned that the term “monitor” could be misinterpreted to imply that a fiduciary is required to keep plan service providers and investment funds under continuous supervision. For example, one meaning given for the word “monitor” in the *American Heritage Dictionary of the English Language* (Fourth Edition 2000) is “To keep close watch over; supervise: *monitor an examination.*” Similarly, one meaning given for this term in the *Oxford English Dictionary* (Online Edition) is “To observe, supervise, or keep under review; to keep under observation.”

ERIC does not believe that a fiduciary duty of continuous supervision is consistent with the Department’s intent or with the requirements of ERISA. When ERISA was first enacted, the Department described the ongoing responsibility of a fiduciary as follows: “*At reasonable intervals the performance of trustees and other fiduciaries should be reviewed by the appointing fiduciary . . .*” 29 C.F.R. § 2509.75-8, FR-17 (emphasis added). Similarly, in the preamble to the final § 404(c) regulations, the Department stated that a fiduciary has “a residual fiduciary obligation *to periodically evaluate* the performance” of look-through investment vehicles. 57 *Fed. Reg.* at 46,924 n. 27 (emphasis added).

ERIC recommends that the Department use the term “periodically review” rather than “monitor” to describe the ongoing duty of a fiduciary to determine whether the performance of plan service providers and investment funds is adequate. ERIC urges the Department to use this term consistently in the preamble of the final regulation as well as in § 2550.404a-5(f) and § 2550.404(c)-1(d)(2)(iv).

### **Time and Method of Disclosure**

ERIC appreciates the Department’s efforts to reduce administrative costs and burdens under the proposed regulation by combining some of the new disclosure requirements with existing requirements, such as the requirement under ERISA § 105(a)(1)(A) to deliver quarterly benefit statements. As explained below, the Department can materially improve the regulation by expanding its effort to harmonize the new disclosure requirements with existing administrative practices.

#### **6. A fiduciary should not be required to make the initial disclosure to a participant before the participant enrolls in the plan.**

The proposed regulation requires initial disclosure of plan-related and investment-related information “on or before the date of plan eligibility.” Prop. Reg. §§ 2550.404(a)-5(c)(1)(i), (c)(2)(i), (c)(3)(i) & -5(d)(1). Many plans provide that an employee becomes eligible to participate as soon as the employee is hired; but the employee might not choose to enroll in the plan until much later.

In a plan that provides for immediate eligibility, it will be impracticable for the fiduciary to provide investment information “on or before the date of plan eligibility.” Even if a plan prescribes a waiting period, so that an employee becomes eligible several months after he or she is hired, detailed information provided on the employee’s eligibility date often serves no purpose. If the employee has no immediate interest in participating in the plan, the employee usually discards any information provided on the eligibility date. It is only later, when the employee decides to enroll in the plan, that investment information becomes relevant and meaningful.

For these reasons, plan administrators typically provide detailed disclosure (including summary plan descriptions, prospectuses, and other plan-related and investment-related information) to an employee when the employee first enrolls in the plan. The enrollment date also is the earliest date on which the employee can actually select investment options for future contributions to the plan. As a result, the enrollment date is the date on which a fiduciary can most efficiently provide the initial disclosure, and it is also the date on which that disclosure will be most useful to the employee. The final regulation should make clear that initial disclosure of plan-related and investment-related information is required on or before the participant’s enrollment date rather than the plan eligibility date.

If a plan provides for automatic enrollment, the regulation should permit a fiduciary to provide initial disclosure of plan-related and investment-related information when the plan administrator establishes an account in the participant’s name. ERIC recognizes that this date is later than the date on which the fiduciary is required to provide the notice required by 29 C.F.R. § 2550.404c-5(c)(3) describing the plan’s qualified default investment alternative (“QDIA”). For the reasons explained above, however, the participant’s enrollment date often will be the earliest date on which it is practicable for the fiduciary to provide the initial disclosure of plan-related and investment-related information, especially in a plan that provides for immediate eligibility.

The QDIA rules merely provide a safe harbor: a fiduciary may choose to satisfy the QDIA notice requirement and the other conditions of the safe harbor to the extent that it is practicable to do so, but the fiduciary is not required comply with the safe-harbor conditions. In discussing the problems that the QDIA notice-timing requirement presents for a plan with immediate eligibility and automatic enrollment, the Department noted that “if a fiduciary fails to comply with the final regulation for a participant’s first elective contribution because a notice is not provided at least 30 days in advance of plan eligibility, the fiduciary may obtain relief for later contributions with respect to which the 30-day advance notice requirement is satisfied.” 72 *Fed. Reg.* at 60,454 (Oct. 24, 2007). In contrast, however, the initial disclosure requirement in the proposed regulation under § 404(a) is mandatory: a fiduciary that fails to provide timely information will be in breach of a duty of dis-

closure. Because the Department has given fiduciaries no choice but to comply with the new disclosure requirement, the Department must ensure that the timing of the required disclosure is not unworkable or unreasonable.

Although the regulation should not require a fiduciary to give the initial plan-related and investment-related disclosure at the same time as the QDIA notice, the regulation should make clear that the fiduciary of a plan with automatic enrollment is permitted to give the initial disclosure at the same time as the QDIA notice. In some cases (for example, when a plan provides for delayed enrollment, or when new participants will be enrolled on a predetermined date in connection with a corporate acquisition), it will be both feasible and efficient to provide the initial disclosure and the QDIA notice at the same time.

**7. A fiduciary should not be required to make the initial disclosure to a beneficiary of a deceased participant before the beneficiary's account is established.**

The proposed regulation requires initial disclosure of plan-related and investment-related information to beneficiaries, as well as participants, "on or before the date of plan eligibility." Prop. Reg. §§ 2550.404(a)-5(c)(1)(i), (c)(2)(i), (c)(3)(i) & -5(d)(1). ERISA § 3(8) defines a "beneficiary" as a person designated by a participant (or by the terms of the plan) "who is or may become entitled to a benefit" under the plan.

It is not clear what the "date of plan eligibility" would be for a designated beneficiary. One possible interpretation is that a person becomes entitled to receive disclosure as soon as the person is designated as a beneficiary, even though the participant is still alive. A requirement to provide detailed investment disclosure to all designated beneficiaries of a living participant would be nonsensical, however, since the beneficiaries do not currently have (and might never obtain) the right to make investment decisions concerning the participant's account. The final regulation should make clear that a fiduciary is not required to provide disclosure to a designated beneficiary before the participant's death.

The most logical interpretation of "the date of plan eligibility," as it applies to a beneficiary, is that the proposed regulation refers to the date of the participant's death. If this is the intent of the proposed regulation, however, it creates a duty that fiduciaries will not be able to fulfill. A fiduciary cannot provide initial disclosure to a beneficiary *before* the date of the participant's death, since the identity of the beneficiary might change at any time. It will be equally impossible for a fiduciary to provide initial disclosure *on* the date of the participant's death. A fiduciary often does not learn of a participant's death immediately, especially if the participant is a former employee. Once the fiduciary receives notice of the participant's death, additional time will pass while the fiduciary obtains a death certificate con-

firming that the participant has died, identifies the participant's beneficiaries, locates the beneficiaries, and obtains Social Security numbers, addresses, dates of birth, and other information necessary to administer the plan properly.

When the plan administrator identifies the proper beneficiaries of a deceased participant and obtains essential information about the beneficiaries, the administrator instructs the plan's recordkeeper to establish a separate account in the name of each beneficiary. Plan administrators typically provide initial disclosure to a beneficiary when the beneficiary's account is established. A beneficiary cannot, as a practical matter, exercise any investment control over inherited assets until the assets are allocated to the beneficiary's account. Accordingly, the final regulation should state that a fiduciary must provide initial disclosure to a beneficiary on or before the date when the plan establishes an account in the beneficiary's name, rather than on the beneficiary's eligibility date.

Under ERISA § 206(d)(3)(J), a person who is an alternate payee under a qualified domestic relations order is treated as a beneficiary under the plan. It is not practicable for a fiduciary to provide initial disclosure to an alternate payee "on or before the date of plan eligibility," since the fiduciary often will not know that a qualified domestic relations order has been entered until the participant or alternate payee provides the plan with a copy of the final order. Accordingly, to the extent that the alternate payee has authority under the terms of the qualified domestic relations order to direct the investment of assets allocated to a separate account, initial disclosure to the alternate payee also should be required only when the plan establishes an account in the alternate payee's name.

**8. A fiduciary should be required to make annual disclosures of plan-related and investment-related information only to participants and beneficiaries who are enrolled in the plan.**

The proposed regulation requires a fiduciary to disclose plan-related and investment-related information to participants and beneficiaries on before the date of plan eligibility "and annually thereafter." Prop. Reg. §§ 2550.404(a)-5(c)(1)(i), (c)(2)(i), (c)(3)(i) & -5(d)(1). Under ERISA, persons who are "or may become" entitled to benefits under a plan are considered participants or beneficiaries. ERISA §§ 3(7) & 3(8). Accordingly, the proposed regulation appears to require a fiduciary to provide annual disclosures to employees who are eligible to participate but who have chosen not to enroll in the plan (and possibly also to the designated beneficiaries of participants who are still alive).

For the reasons we have explained above, it is not useful to a participant or beneficiary to receive information about theoretical investment rights a plan might provide at some future date when the participant or beneficiary establishes an individual account. This information is expensive to produce and distribute, and

individuals who are not enrolled in the plan routinely discard the information when they receive it. The final regulation should make clear that the annual disclosure requirement applies only to participants and beneficiaries who are enrolled in the plan and have an individual account.

**9. A fiduciary should not be required to provide a notice of a material change in the plan's investment options until at least 30 days after the change becomes effective.**

If there is a material change in the general investment rights under a plan, such as a material change in the designated investment alternatives or the rules for providing investment instructions, the fiduciary must furnish participants and beneficiaries with a description of the change not later than 30 days after the date of adoption of the change. Prop. Reg. § 2550.404a-5(c)(1)(ii). The preamble explains that the Department decided to tie the notice requirement to the date of adoption of a change because the Department believed that this rule would give participants and beneficiaries more time to consider the change before it became effective.

The regulation should require notice of a change not later than 30 days after the change becomes *effective*, rather than 30 days after the change is *adopted*. In some cases, a change is adopted far in advance of its effective date in order to give the plan administrator and third-party service providers ample time to implement the change. For example, a plan sponsor might adopt an amendment in February adding a new investment fund to the plan effective as of the following January. If participants are informed of this change in March (30 days after the February adoption date), the information will not be useful to them: they will have discarded the notice and forgotten the information long before the information becomes relevant to their investment decisions. In order to be effective, a communication concerning a plan change must be reasonably proximate to the effective date of the change. Whenever possible, fiduciaries generally provide notice of material changes a reasonable time before the changes become effective.

When a third party has the power to make a change that affects a designated investment alternative, the plan fiduciary will not always receive notice of the change within 30 days after it is adopted. For example, if the manager of an investment fund changes the fund's rules for processing investment instructions, the fund manager will inform investors before the change becomes effective, but not necessarily within 30 days after the change is adopted. Accordingly, in some circumstances a fiduciary will not be able to comply with a 30-day notice requirement that is tied to the adoption date of the change.

The notice requirement in the proposed regulation does not ensure that participants will receive notice of a change before it becomes effective. In some



cases, a change is effective as soon as it is adopted. For example, if a fiduciary determines that an investment manager is performing poorly, the fiduciary might have a duty to replace the investment manager immediately. In such a case, the adoption date and the effective date of the change are the same, and it will not be possible for the fiduciary to provide participants with advance notice of the change. A requirement that fiduciaries notify participants within 30 days after a material change becomes effective will protect participants' interest in receiving current information without imposing unrealistic obligations on fiduciaries.

**10. Fiduciaries should be given greater freedom to meet their disclosure obligations by providing electronic disclosure.**

The Department has coordinated its proposed disclosure requirements with the summary prospectus proposal of the Securities and Exchange Commission (the "Commission"). 73 *Fed. Reg.* at 43,015. The Commission proposes to allow registered mutual funds to send investors a summary prospectus and to provide a full statutory prospectus by posting it on an Internet Web site. *Enhanced Disclosure and New Prospectus Delivery Option for Registered Open-End Management Investment Companies*, Release No. 33-8861, 72 *Fed. Reg.* 67,790 (Nov. 30, 2007). Under the Commission's proposal, the fund would not be required to obtain the investor's affirmative consent to electronic delivery of the statutory prospectus. Instead, the summary prospectus would direct the investor to the fund's Web site and would explain that the investor could receive a paper copy of the statutory prospectus upon request. *Id.*

A large majority of individual account plans offer registered mutual funds as designated investment options. In 2007, 54% of the assets in 401(k) plans were invested in mutual funds. See Investment Company Institute, *The U. S. Retirement Market, 2007* (July 2008) (available at <http://www.ici.org/stats/mf/fm-v17n3.pdf>). Accordingly, the Department's effort to coordinate its disclosure rules with the Commission's rules is an important step to reduce duplicative and conflicting requirements. As the Department appears to recognize in the preamble, however, the Department's very restrictive rules governing electronic disclosure will present a substantial obstacle to any Internet-based disclosure of investment information to plan participants. See 73 *Fed. Reg.* at 43,017.

In the very short time allowed for comment on the Department's proposed participant disclosure regulation, ERIC has not had an opportunity to survey its members and develop detailed recommendations concerning the Department's electronic disclosure rules. ERIC notes, however, that the rules are largely unworkable to the extent that they require a participant's affirmative consent to the electronic delivery of information. A fiduciary may avoid obtaining a participant's consent only if access to the employer's electronic information system "is an integral part of [a participant's] duties." 29 C.F.R. § 2520.104b-1(c)(2). This restriction

makes it virtually impossible for an employer to provide disclosure electronically to workers who are not required to use a computer as part of their job. The administrative burden of collecting, storing, and updating individual consents on a participant-by-participant basis for thousands of employees is too great to be tenable, even though many of these workers might prefer to receive information electronically.

The Department should revise its rule to permit electronic disclosure without affirmative consent to participants who have reasonable access to electronic information at their principal work location. For example, if an employer establishes a password-protected email account for each employee and makes computer terminals with Internet access available in an employee break room or other readily accessible on-site location, the employer should be able to deliver information electronically without the employee's affirmative consent. As is currently the case for employees who use computers on the job, each employee would be notified of his or her right to receive a paper copy of documents on request.

The regulation also should provide that a fiduciary may satisfy the new disclosure requirements by providing electronic disclosure in accordance with the guidance issued by the Department of the Treasury and Internal Revenue Service at Treas. Reg. § 1.401(a)-21. In the preamble of the final QDIA regulation, the Department offered this alternative method of providing the QDIA notice. *72 Fed. Reg.* at 60,458; *see also* Dep't Lab. Field Assistance Bulletin 2008-03, Q&A-7 (Apr. 29, 2008). The same flexibility is both necessary and appropriate in the case of the new participant disclosure rules under § 404(a).

At present, the Internal Revenue Service's regulation states that fiduciaries *may not* rely on the Internal Revenue Service's electronic disclosure rules to satisfy any disclosure requirement under Title I of ERISA. Treas. Reg. § 1.401(a)-21(a)(3)(i). If, as ERIC suggests, the Department permits a fiduciary to rely on the Internal Revenue Service's electronic disclosure rules to satisfy the new participant disclosure requirements, this method should be authorized in the final regulation itself (or in a revised version of the Department's electronic disclosure regulation published at the same time): it should not merely be mentioned in the preamble of the final regulation.

In addition, regardless of whether the Department makes its general electronic disclosure requirements more feasible, the Department should make clear that the delivery of any document required under the securities laws will automatically satisfy the Department's electronic disclosure requirement if the document is delivered in a manner that satisfies the Commission's requirements for electronic disclosure of information to investors. For example, the Department's proposed participant disclosure regulation requires that participants receive limited information about a designated investment alternative directly, and that they be given an Internet Web site address where they can receive much more comprehensive infor-

mation. Prop. Reg. § 2550.404a-5(d)(1). This provision of the proposed regulation sensibly mirrors the Commission's summary prospectus proposal. The Department's efforts to avoid conflicting disclosure requirements are seriously undermined, however, by the fact that its own rules for electronic disclosure are far more restrictive than the Commission's proposed rules. The Department observes in the preamble that "plan fiduciaries may, in some cases, have to provide paper copies of the supplemental information listed in this requirement (i.e., information that would otherwise be accessible through the Internet Web site address) to participants who fail to affirmatively consent to receiving such information electronically." 73 *Fed. Reg.* at 43,017.

If the Commission, whose mission is to protect investors, determines that an investor's affirmative consent to electronic disclosure is not necessary, the Department should not superimpose such a requirement on prospectus information that is delivered in order to satisfy the participant disclosure rules in ERISA. The Department's final regulation should make clear that a fiduciary does not need to obtain affirmative consent from a participant or to comply with other aspects of the Department's electronic disclosure regulation in order to provide supplemental investment information concerning a registered mutual fund on a Web site. If the supplemental information is contained in a statutory prospectus that satisfies the Commission's electronic disclosure requirements, the same method of disclosure should automatically satisfy any requirement under the Department's regulation to provide plan participants with the information contained in the prospectus.

### **Employer Stock Funds and Other Single-Asset Funds**

#### **11. The investment-related disclosure requirements should not apply to employer stock funds that are regulated by the federal securities laws.**

When an employer allows participants in an individual account plan to invest their retirement savings in the employer's publicly-traded stock, the employer is required to register the plan under the securities laws and to provide participants with a statutory prospectus. *See* Securities Act of 1933, Rule 428, 15 U.S.C. § 77j; 17 C.F.R. § 230.428. The securities laws require publicly-traded U.S. companies to file annual reports (Form 10-K) and quarterly reports (Form 10-Q) with business descriptions, financial statements, and a detailed discussion of trends and other factors affecting financial condition and results. Issuers of registered securities also must file immediate updating Form 8-K reports to disclose events that fall within a broad variety of categories. In addition, before their annual shareholders' meetings, issuers must make proxy filings containing detailed disclosures regarding their management, executive compensation, insider transactions, and related matters.

The timing and content of these disclosures is regulated and enforced by the Securities and Exchange Commission, an agency whose mandate is to protect investors and preserve the integrity of the securities markets. Investors—including plan participants—who acquire a publicly-traded stock may assert claims under SEC Rule 10b-5 if the company’s disclosures are deficient. In construing and applying the securities laws, the courts have developed an extensive body of case law that attempts to strike an appropriate balance between the protection of investors against deficient disclosures, on the one hand, and the burdens to companies of excessive disclosure obligations and nuisance suits, on the other. Because the securities laws already impose comprehensive disclosure requirements regarding publicly-traded stock, it would be inappropriate (and unnecessary) for the Department to create overlapping and potentially inconsistent disclosure obligations under the fiduciary provisions of ERISA and to permit participants to enforce these obligations through lawsuits under ERISA.

Congress has amended the securities laws a number of times in recent years to create requirements that plaintiffs must meet when bringing securities class action lawsuits alleging misrepresentation and to require that such suits be brought under the federal securities laws. In 1995, Congress enacted the Private Securities Litigation Reform Act (the “PSLRA”) to alter the procedures for bringing class actions alleging fraud in the sale of securities. *See* Pub. L. No. 104-67, 109 Stat. 737 (1995). Notably, the PSLRA established heightened pleading standards for plaintiffs bringing fraud or misrepresentation class actions under Rule 10b-5 and the Securities Exchange Act of 1934. In 1998, Congress enacted the Securities Litigation Uniform Standards Act (the “SLUSA”), Pub. L. No. 105-353, 112 Stat. 3227 (1998), to prevent plaintiffs from circumventing the PSLRA regime. *See* SLUSA § 2(2) & (3) (stating that the shift of securities class action suits from federal to state courts had prevented the PSLRA “from fully achieving its objectives”); *Spielman v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 332 F.3d 116, 123 (2d Cir. 2003) (“Driving enactment of SLUSA was Congress’ finding that litigants eluded PSLRA’s reach with relative ease.”).

If the Department imposes a new disclosure regime, enforceable under ERISA, on publicly-traded companies that are already subject to extensive disclosure requirements under the federal securities laws, the Department will seriously undermine Congress’s attempts to eliminate unmeritorious securities fraud lawsuits. Plaintiffs will be able to evade the heightened procedural requirements Congress has established for suits under the securities laws by asserting their claims under the fiduciary provisions of ERISA. A recent decision of the Supreme Court underscores this risk. In *Credit Suisse Securities (USA) LLC v. Billing*, 127 S. Ct. 2383 (2007), the Supreme Court rejected an attempt by the plaintiffs’ bar to circumvent the requirements of the securities laws by bringing an antitrust action in connection with an initial public offering. In so holding, the Court noted, “To permit an antitrust lawsuit risks circumventing [the PSLRA and SLUSA] requirements by

permitting plaintiffs to dress what is essentially a securities complaint in antitrust clothing.” *Id.* at 2396.

Under current law, a number of courts have recognized that alleged misstatements regarding company stock that are made to the general investing public are not actionable under ERISA, even where the statements are also made to plan participants who invest in an employer stock fund. As the court of appeals recently noted in *Kirschbaum v. Reliant Energy, Inc.*, 526 F.3d 243, 256-57 (5th Cir. 2008), ERISA liability attaches only if an “employer was acting as a fiduciary when it took [the challenged] action,” and corporate statements in SEC filings “do not constitute fiduciary communications,” even when they are later distributed to plan participants. *See, e.g., In re Syncor ERISA Litig.*, 351 F. Supp. 2d 970, 987 (C.D. Cal. 2004) (“[a] defendant does not act as a fiduciary simply because it made statements about its expected financial condition.”); *In re Tyco Int’l Multidistrict Litig.*, No. MDL 02-1335-PB, 2004 WL 2903889, at \*6 (D.N.H. Dec. 2, 2004) (“there is little evidence in the legislative history of either the Securities Act, which is the source of the disclosure requirements, or ERISA to support the view that an issuer of stock necessarily assumes fiduciary responsibilities in complying with its obligations under the securities laws if it chooses to allow its employees to invest in its stock as a part of an individual account plan”); *In re Honeywell International ERISA Litig.*, No. Civ. 03-1214, 2004 WL 3245931, at \*9 (D.N.J. Sept. 14, 2004) (“Even where a statement is made to an audience that includes plan participants, and even where that statement may be material to participants’ interests, the speaker does not incur fiduciary liability unless the statement was made in a fiduciary capacity.”); *In re WorldCom, Inc.*, 263 F. Supp. 2d 745, 766 (S.D.N.Y. 2003) (“Those who prepare and sign SEC filings do not become ERISA fiduciaries through these acts, and consequently, do not violate ERISA if the filings contain misrepresentations.”); *Crowley v. Corning, Inc.*, 234 F. Supp. 2d 222, 228 (W.D.N.Y. 2002) (the claim “that defendants made material misrepresentations and nondisclosures concerning Corning’s future performance . . . fails, since it is apparent from the amended complaint that such statements, regardless of truth or falsity, were not made by Corning in any fiduciary capacity regarding the Plan.”).

If the Department’s regulation requires a public company, as a matter of fiduciary duty, to disclose information to plan participants that the company is already required to disclose to all investors, the regulation will create a cause of action under ERISA to enforce requirements that Congress intended to be enforced exclusively under the federal securities laws. The creation of a parallel cause of action that permits plaintiffs to circumvent the heightened procedural requirements under PSLRA and SLUSA is precisely the position that the Supreme Court emphatically rejected in *Billig*. Accordingly, the final regulation should exempt employer stock funds from the new investment-related disclosure requirements to the extent that these funds are subject to disclosure requirements under the securities laws.

**12. If the regulation applies to employer stock funds and other single-asset funds, these funds should be subject to requirements that are more limited than those that apply to other funds.**

The proposed disclosure requirements are designed with mutual funds and other collective investment funds in mind. Many of the disclosure requirements are not applicable to a designated investment alternative that invests primarily in a single asset. The most common type of single-asset fund in a participant-directed plan is an employer stock fund; but these plans occasionally offer other single-asset funds (such as funds investing in the stock of a prior employer or a spin-off company) for which the proposed disclosure requirements also are inappropriate.

For example, the issuer of a single stock will not maintain a Web site that discloses “the investment’s principal strategies and attendant risks, the assets comprising the investment’s portfolio, the investment’s portfolio turnover,” and similar information. Prop. Reg. § 2550.404a-5(d)(1)(i)(B). The “type of management utilized by the investment” also is not relevant to an employer stock fund or other single-asset fund. Prop. Reg. § 2550.404a-5(d)(1)(i)(D). It is not always clear what broad-based market index a fiduciary should use as a benchmark against which to measure the performance of a single stock, especially if the stock is not publicly-traded. Prop. Reg. § 2550.404a-5(d)(1)(iii). Expense ratios are not relevant to an employer stock fund or other single-asset fund. Prop. Reg. § 2550.404a-5(d)(1)(iv)(B).

As explained in the preceding comment, ERIC believes that the new disclosure requirements should not apply to the stock of publicly-traded companies that are already subject to extensive disclosure requirements under the securities laws. To the extent that the regulation applies to employer stock funds and other single-asset funds, ERIC recommends that the Department limit the disclosure requirements for these funds to the information that is relevant to these funds and likely to be useful to participants.

### **Content of Disclosure**

ERIC commends the Department for its efforts to make investment-related disclosure useful to plan participants without imposing undue burdens and costs on plan fiduciaries and service providers. For example, ERIC agrees with the Department’s conclusion that it is not useful to participants to have information concerning administrative charges broken out on a service-by-service basis. *73 Fed. Reg.* at 43,016. ERIC’s members also appreciate the model comparative chart provided in the proposed regulation, which is a useful guide to the content and format of required disclosures. Prop. Reg. § 2550.404a-5, Appendix. These features should be retained in the final regulation.

As explained below, ERIC believes that there are additional areas in which the regulation can be modified to make required disclosures more meaningful to participants and less burdensome to fiduciaries.

**13. Separate disclosure of administrative expenses should be required only if the administrative expenses are not included in the plan's investment-related expenses.**

The proposed regulation requires a plan to provide participants and beneficiaries, at least quarterly, with a statement that includes the dollar amount actually charged to their accounts for administrative expenses. Prop. Reg. § 2550.404a-5(c)(ii)(A). Not all administrative expenses are charged directly to a participant's account, however. Instead, many plans calculate certain categories of administrative expenses as an aggregate amount and subtract this amount from the net asset value of the plan's investment funds. Plans that use this method record administrative expenses as basis-point reductions in investment returns.

It would be very difficult and time-consuming for a fiduciary to convert these aggregate percentages to dollar amounts allocated to individual accounts. Participants move their money into and out of the plan's investment funds frequently, sometimes as often as daily. Participants also contribute new money to the plan's investment funds in each payroll period. In contrast, a plan might charge administrative expenses to an investment fund only once a month, once a quarter, or even once a year. There is no practical way for a plan fiduciary to convert administrative expenses charged periodically at the fund level to dollar amounts allocated to participants' accounts.

ERIC believes that this problem can be addressed by a simple conforming change that might more accurately reflect the intent of the proposed regulation. In paragraph (c)(i), the proposed regulation states that a fiduciary must provide an explanation of administrative expenses "to the extent not otherwise included in investment-related fees and expenses." The final regulation should include the same limitation in paragraph (c)(ii)(A), to make clear that a plan must report the dollar amount of administrative expenses charged to a participant's account only to the extent that this amount is not otherwise included in the investment's expense ratio. To the extent that a plan deducts administrative expenses (charged in basis points) from investment returns or net asset values, these expenses would be disclosed under paragraph (d)(1)(iv)(B) as part of the total annual operating expenses of each designated investment alternative.

**14. The final regulation should eliminate the redundant reference to identification of designated investment managers.**

The proposed regulation requires a § 404(c) plan to disclose all of the information required in the new disclosure rules under § 404(a), plus certain additional information. One item of additional information required under § 404(c) is “[i]dentification of any designated investment managers.” Prop. Reg. § 2550.404c-1(b)(2)(i)(B)(2). However, “identification of any designated investment managers” is also an item of plan-related information that must be disclosed by all plans, including § 404(c) plans, in order to comply with the new requirements under § 404(a). Prop. Reg. § 2550.404a-5(c)(1)(i)(E). To avoid confusion, the redundant disclosure requirement under § 404(c) should be eliminated from the final regulation.

**15. A fiduciary should be permitted (but not required) to disclose composite performance data for new funds.**

For designated investment alternatives with variable returns, the proposed regulation requires fiduciaries to disclose performance data for the preceding 1-year, 5-year, and 10-year periods “if available.” Prop. Reg. § 2550.404a-5(d)(1)(ii). The preamble explains that funds that have not been in existence for 1, 5, or 10 years “are expected to explain that the data is not available for this reason.”

Under the current § 404(c) regulation, fiduciaries are required to disclose, upon request, information concerning past and current investment performance “on a reasonable and consistent basis.” 29 C.F.R. § 2550.404c-1(b)(2)(i)(B)(2)(iv). If a fund is new and therefore lacks actual past performance data, fiduciaries sometimes disclose representative composite data. For example, if a new fund combines several existing funds, the fiduciary might disclose the composite past performance of the combined funds.

This information can be useful to plan participants who wish to evaluate the fund, provided that the information is clearly labeled as composite data and is used only when actual past performance data is not available. The final regulation should permit fiduciaries to disclose composite data under these conditions. At the same time, however, the final regulation should make clear that fiduciaries are not required to provide composite data for new funds. There will be many circumstances in which a fiduciary will not be able to develop composite data that provides a meaningful indication of a new fund’s past performance. The final regulation should continue to allow the fiduciary to explain that performance data is not available for a fund that has not been in existence for 1, 5, or 10 years.



**16. A fiduciary should not be required to compare the performance of an investment alternative with the performance of a benchmark when no relevant benchmark is available.**

The proposed regulation requires a fiduciary to compare the performance of a designated investment alternative over a 1-year, 5-year, and 10-year period with the performance of “an appropriate broad-based securities market index” over the same periods. Prop. Reg. § 2550.404a-5(d)(1)(iii). This comparison will be useful to participants in cases where an appropriate benchmark is available.

In many cases, however, there is no relevant benchmark against which a fiduciary can measure the performance of a designated investment alternative. For example, stable value funds, target date funds, and many customized proprietary funds are not comparable to any broad-based market index. Any attempt by a fiduciary to compare these funds with a benchmark is more likely to mislead than to inform plan participants. The final regulation should make clear that a fiduciary is required to compare a fund’s performance with the performance of a benchmark only if a relevant benchmark is available.

**17. A fiduciary should be permitted to select from a wider range of benchmarks, and to measure characteristics other than the rate of return.**

The proposed regulation requires a fiduciary to compare the “average annual total return” of a designated investment alternative with the “returns” of “an appropriate broad-based securities market index.” Prop. Reg. § 2550.404a-5(d)(1)(iii). The standards for benchmarks are far too narrow: they fail to take into account the range of investment objectives and characteristics of the funds offered under participant-directed individual account plans.

A benchmark is a standard of comparison of a fund to an appropriate measure of performance that will give plan participants one basis on which to assess the quality of an investment option. A broad-based securities market index will constitute the most appropriate benchmark in many cases because in many cases fund managers themselves manage a fund against a similar benchmark.

However, a broad-based securities market index is not the most appropriate (or even one of several possible appropriate) benchmarks in all cases. The proposed regulation should be revised to permit plan fiduciaries to use different types of benchmarks where the fiduciary determines that a particular benchmark is most appropriate for the investment option, or where an appropriate broad-based securities market index suitable for use for the particular investment option does not exist. An alternative benchmark might be an index, a different portfolio, a tar-

get return, an external determinable variable, or a range of returns derived from a specified universe.

In addition, the regulation should permit plan fiduciaries to use benchmarks that are designed to evaluate investment characteristics other than rate of return, such as risk. For example, some participant-directed individual account plans offer investment options that are based on an absolute return strategy. Absolute return funds seek to produce a positive return regardless of market conditions. There is no market benchmark to outperform in the case of an absolute return strategy. Instead, the return objective for an absolute return strategy is usually stated in one of three ways: first, return relative to a cash rate such as the London Interbank Offered Rate (“LIBOR”), plus a certain premium; second, a “real” return objective, or a return over the rate of inflation; or, third, an absolute return target such as 8%, or a range such as 8% to 12%.

The magnitude of the target return objective for an absolute return strategy can be established based on the how well a manager is expected to perform against a risk target. The manager’s targeted level of risk is stated in the most commonly used measure of either volatility or standard deviation. For a mandated standard deviation risk target of 12%, the fund’s annual return target would be set (likely at anywhere from 6% to 12%) based on how well the manager is expected to perform using the mandated level of risk, as measured by various mathematical formulae, such as Sharpe ratios or information ratios. The extent to which the manager attains the return target is the benchmark by which the manager’s performance would be assessed.

As this example illustrates, a “broad-based securities market index” will not always be the most appropriate performance standard for a designated investment alternative, and the simple rate of return on the benchmark will not always be the correct measurement of the investment’s performance. The final regulation should be sufficiently flexible to permit plan fiduciaries to select the benchmarks and measure the characteristics that are most appropriate for each designated investment alternative offered to plan participants.

**18. A fiduciary should be permitted to compare the performance of an investment alternative with the performance of an appropriate customized benchmark.**

The proposed regulation states that the performance benchmark must be “an appropriate broad-based securities market index.” Prop. Reg. § 2550.404a-5(d)(1)(iii). The Department observed in the preamble that plans offering registered investment funds probably would choose the benchmark already used in the fund’s prospectus. 73 *Fed. Reg.* at 43,017. The Department sought comments “on wheth-

er and how the proposed requirement may need to be modified . . . for ERISA plan investment options that are not subject to the securities laws.” *Id.*

The participant-directed individual account plans of large employers often offer customized funds that are designed for the plans of that employer. These funds are exempt from the prospectus delivery requirements under the securities laws. For example, these funds might consist of interests in several registered investment funds offered by different mutual fund families, or they might consist of a pool of assets managed by an in-house or outside investment manager. In some cases, a plan will offer designated investment options that consist of portfolios of other options offered under the plan. For example, a plan might offer fund-of-funds investment options that combine the plan’s domestic equity fund, international equity fund, and stable value fund in different proportions. Many lifestyle and target date funds managed by in-house investment professionals adopt this approach.

A customized fund often requires a customized benchmark. For example, if a customized small-cap equity fund holds a 20% interest in each of five registered small-cap equity funds offered by different mutual fund families, the most appropriate benchmark for the fund might give a 20% weighting to the benchmark used in the prospectus for each of the five underlying funds. Similarly, if a customized fund consists of a portfolio of different percentage interests in separate funds that also are designated investment options under the plan, the appropriate benchmark for the portfolio might combine the benchmarks of the separate funds that make up the portfolio. The final regulation should make clear that a fiduciary may use a benchmark that combines the performance of two or more separate benchmarks that reflect the asset allocation of the components of the fund-of-funds investment option, provided that each underlying benchmark satisfies the standards in the regulation.

**19. Disclosure of unit values or individual assets in an investment fund should not be required.**

The proposed regulation requires a fiduciary to disclose, upon request, “[a] statement of the value of a share or unit of each designated investment alternative as well as the date of valuation.” Prop. Reg. § 2550.404a-5(d)(4)(iii). The fiduciary must also disclose, upon request, “[a] list of the assets comprising the portfolio of each designated investment alternative which constitute plan assets . . . and the value of each such asset (or the proportion of the investment which it comprises).” Prop. Reg. § 2550.404a-5(d)(4)(iv).

The information that the fiduciary is required to disclose is “based on the latest information available to the plan.” Prop. Reg. § 2550.404a-5(d). The unit value of mutual funds and other collective investment funds changes daily. Accordingly, any information available to a fiduciary concerning unit value will be out of

date by the time the fiduciary is able to provide it to a plan participant. In the case of registered investment funds and publicly-traded securities, the information that a participant can obtain over the Internet will be more current than the information the participant can obtain by contacting a plan fiduciary. To the extent that a participant wishes to know the value of investments he already holds, he will receive this information in the quarterly benefit statement required under ERISA § 105(a)(1)(A).

Similarly, it is not clear why a participant would need a list of the assets constituting a collective trust or other look-through investment vehicle. (In the case of a registered mutual fund, the underlying assets would not be “plan assets” and would not be subject to disclosure in any event.) In the preamble to the current regulation under § 404(c), the Department explained that a fiduciary generally could satisfy this requirement by disclosing the plan asset information in the plan’s most recent annual report on Form 5500. *57 Fed. Reg.* at 46,912. ERISA § 104(b) already permits a participant to obtain a copy of the annual report, however. Accordingly, no purpose is served by creating a separate disclosure requirement under § 404(a).

ERIC recognizes that these requirements are carried over, in substantially similar form, from the current regulations under § 404(c). 29 C.F.R. § 2550.404c-1(b)(2)(i)(B)(2)(iii) & (iv). In the sixteen years since the final § 404(c) regulations were published, however, employers and the Department have had an opportunity to evaluate the current disclosure requirements and to weigh the potential benefits to plan participants against the administrative burden imposed on plan sponsors and service providers. ERIC believes that the disclosures required by these provisions are not useful (and might be misleading) to plan participants. The burden of assembling and presenting this information upon request far outweighs any benefit it might be thought to provide. In addition, under the current § 404(c) regulation, a fiduciary that is unable to provide this information upon request merely forfeits the protection of a safe harbor. In contrast, under the proposed regulation, a fiduciary that is unable to list every asset in a look-through investment vehicle is exposed to liability for breach of a duty of disclosure. Accordingly, ERIC urges the Department to eliminate these disclosure requirements from the final regulation.

**20. The regulation should clarify that funds offered through mutual fund windows are not “designated investment alternatives.”**

The proposed regulation requires a plan fiduciary to make detailed disclosures concerning a plan’s designated investment alternatives. The proposed regulation explains that the term “designated investment alternative” does not include “‘brokerage windows,’ ‘self-directed brokerage accounts,’ or similar plan arrangements that enable participants and beneficiaries to select investments beyond those

designated by the plan.” Prop. Reg. § 2550.404a-5(h)(1). ERIC believes that the Department has appropriately excluded these arrangements from the disclosure requirements for designated investment alternatives, and that this exclusion should be retained in the final regulation.

The term “brokerage window” does not have a uniform definition. Some people use this term as an alternate name for a self-directed brokerage account, an arrangement that permits participants to invest (through a designated stockbroker) in any asset available to individual investors, including investments not typically offered under participant-directed plans. Many plans, in order to avoid potential legal or administrative problems, impose certain restrictions on the types of assets a participant can acquire through a self-directed brokerage account. For example, a plan might prohibit a participant from investing in illiquid assets, real property, commodities, derivatives, or similar assets.

In contrast, some people use the term “brokerage window” as an alternate name for a “mutual fund window,” an arrangement that offers plan participants access to a large (but not unlimited) number of registered mutual funds. For example, a mutual fund window might allow participants to choose among five hundred registered mutual funds offered by an array of different providers, but would not give participants unlimited access to all of the approximately 8,000 different mutual funds available to investors.

ERIC believes that the Department intended to exclude both types of arrangement from the definition of “designated investment alternative.” Although a plan that offers a mutual fund window might be thought to have “designated” as an investment option each of the many funds available through the window, it is not practicable for fiduciaries to provide the kind of detailed disclosure contemplated in the proposed regulation with respect to hundreds of different funds. Accordingly, if plans are to continue to offer mutual fund windows (which are popular and beneficial to participants), it must be clear that the funds available through the window are not “designated investment alternatives.” ERIC requests that the Department clarify this point in the final regulation.

ERIC appreciates the opportunity to present these comments. If the Department has any questions about our comments, or if we can be of further assistance, please let us know.

Sincerely,

Mark J. Ugoretz  
President  
THE ERISA INDUSTRY COMMITTEE