November 13, 2006

(Submitted electronically to e-ORI@dol.gov and sent via U.S. Mail to the following address):
Office of Regulations and Interpretations
Employee Benefits Security Administration, Room N-5669
U.S. Department of Labor
200 Constitution Avenue, N.W.
Washington, D.C. 20210

Attn: Default Investment Regulations

Ladies and Gentlemen:

Transamerica Retirement Services ("Transamerica"), appreciates this opportunity to comment on regulations for default investment alternatives under participant-directed individual account plans (the "Proposed Regulations") recently proposed by the U.S. Department of Labor's Employee Benefits Security Administration (the "Department").[1] The Proposed Regulations would implement provisions under the Pension Protection Act of 2006 (the "Pension Protection Act"), which added section 404(c)(5) under the Employee Retirement Income Security Act of 1974, as amended ("ERISA"). Section 404(c)(5) provides fiduciary relief to plan sponsors and other fiduciaries who invest the account balances of participants who fail to provide investment elections in a "qualified default investment alternative" ("QDIA") in accordance with regulations issued by the Department.

Transamerica, a marketing unit of Transamerica Life Insurance Company, and other of its affiliates design customized retirement plan solutions to meet the unique needs of small to midsized businesses. As of April, 2006, Transamerica ranked as a top-ten pension provider and, as of June 30, 2006, has more than 14,000 retirement plan clients totaling more than $11.95 billion in assets.

We congratulate the Department on quickly proposing regulations for default investment alternatives in response to requirements under the Pension Protection Act, and we commend the Department's efforts to facilitate the use of default investment alternatives that are likely to increase retirement savings over long periods of time. However, we encourage the Department to address several issues in connection with the Proposed Regulations.

- *Clarify that mutual fund redemption fees are not a "financial penalty."* The Department should confirm that redemption fees and other policies against frequent trading adopted by

[1] 71 Fed. Reg. 56806 (Sept. 27, 2006). The Proposed Regulations are required by section 624(b)(2) of the Pension Protection Act of 2006, Public Law 109-280.

registered investment companies would not violate the condition prohibiting financial penalties and restrictions against the ability of a participant to transfer from a QDIA under § 2550.404c-5(e)(2) of the Proposed Regulations.

- *Clarify circumstances in which a participant "did not direct the investment of assets."* The Proposed Regulations should be clarified so that a participant who may have previously provided investment instructions will be deemed to have "had the opportunity to direct the investment of assets in his or her account but did not direct the investment of assets," as specified by § 2550.404c-5(c)(2), if the participant fails to respond within a reasonable time to a request for new affirmative investment instructions. This would provide plan sponsors important flexibility in initially transitioning participant investments from existing default alternatives to QDIAs to obtain relief under section 404(c)(5). It also would facilitate the use of appropriate default investments in a range of situations on an ongoing basis.

- *Modify timing for notice in the case of "immediate participation" plans.* The Proposed Regulations should be revised to allow less than 30 days advance notice concerning the investment of assets in a QDIA in the case of participants eligible for automatic enrollment under "immediate participation" plans, because it is not workable to require notice in advance of a participant's actual employment commencement date.

- *Revise participant investment information requirements.* The Department should reconsider the requirement proposed under § 2550.404c-5(c)(4) to provide to each participant any materials provided to the plan relating to the participant's QDIA investment, because this requirement would be administratively burdensome for plans and confusing rather than helpful to participants. Instead, participants should receive a simplified disclosure document, such as a "fact sheet" containing key information about the QDIA.

- *Include capital preservation products as QDIAs.* Transamerica strongly agrees with comments that are being provided to the Department by others, including the American Council of Life Insurers and the American Benefits Council, urging the Department to include capital preservation products, including stable value and money market funds, among the types of investment products eligible to be QDIAs.

- *Coordinate the regulations with preemption relief under section 514(e).* Because preemption relief for automatic contribution arrangements under new ERISA section 514(e) includes reference to the Department's regulations under section 404(c)(5), we urge the Department to address several issues under section 514(e) as it finalizes the Proposed Regulations. As explained in more detail below, these include certain effective date issues, whether preemption will be available if a plan uses a default investment alternative other than a QDIA, and issues pertaining to notice requirements for automatic contribution arrangements under section 514(e)(3).

We discuss these comments in more detail below.

1. ***Clarify that mutual fund redemption fees are not a "financial penalty."***

Under § 2550.404c-5(e)(2) of the Proposed Regulations, a QDIA may not impose a financial penalty or otherwise restrict the ability of participants to transfer their investments to other investment alternatives available under the plan. However, as a result of recent Securities and Exchange Commission rulemaking, many registered investment companies have adopted policies to deter frequent trading that may harm shareholders, including redemption fees and other policies restricting frequent trading by the investment company's shareholders, including plan participants. If redemption fees and other restrictions imposed by investment companies violate § 2550.404c-5(e)(2) of the Proposed Regulations, the universe of investments available as QDIAs could be unduly restricted. For example, some otherwise appropriate registered investment companies, including certain balanced and lifecycle funds, could not be used as a QDIA because of their redemption fee policies. Further, the "core" investment alternatives under many plans include investment companies that impose redemption fees and other restrictions on frequent trading — these plans would not be able to offer a QDIA that is constructed using the plan's investment alternatives, including a target retirement date or balanced portfolio or managed account service that would use the investment alternatives offered under a plan.

Accordingly, Transamerica urges the Department to confirm that § 2550.404c-5(e)(2) of the Proposed Regulations does not prohibit the use of registered investment companies that impose redemption fees or other restrictions to address frequent trading as a QDIA, or in constructing a QDIA that uses the plan's current investment alternatives.

2. ***Clarify circumstances in which a participant "did not direct the investment of assets."***

The Proposed Regulations (at § 2550.404c-5(c)(2)) would require that a participant or beneficiary on whose behalf assets are being invested in a QDIA must have "had the opportunity to direct the investment of assets in his or her account *but did not direct the investment of assets*" *(emphasis added).* The Department explained that this requirement means that "no relief is available when a participant or beneficiary has provided affirmative investment direction concerning the assets invested on the participant's or beneficiary's behalf."[2] Transamerica requests that the Department review and clarify the circumstances in which it may be determined that a participant "did not direct the investment of assets" under the Proposed Regulations. Following are examples of why this flexibility is needed.

- There are a number of questions raised with respect to the implementation of the Proposed Regulations for plans that already have designated default investment alternatives for auto-enrollment or for other reasons. The Department has explained that, if an already designated default is a QDIA, fiduciaries may obtain relief under

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[2] 71 Fed. Reg. at 56808.

section 404(c)(5) for participants' future investments in the QDIA by delivering notice as described by the Proposed Regulations. However, many plans may be required to transfer participants' balances in existing default alternatives (such as money market or stable value options) to new investment alternatives that qualify as a QDIA. Further, it may be appropriate to replace a plan's QDIA from time to time based on cost, performance or other criteria. The Proposed Regulations do not currently provide specific procedures for transitioning participant account balances to a QDIA so that fiduciaries may obtain relief under section 404(c)(5), or for replacing a QDIA if required in the future.

- Some participants may initially provide affirmative investment instructions but then do not update their instructions or provide new instructions. For example, in DOL Advisory Opinion 96-02A (February 2, 1996), the Department addressed circumstances where plan fiduciaries were concerned about protecting plan assets in accounts of plan participants who could not be located to provide new investment instructions. The Department concluded that that a plan will not cease to be a "404(c)" plan merely because plan fiduciaries may override the last investment direction of a missing participant or beneficiary, where the fiduciaries determined that continuing to follow that last direction may not be prudent. It is unclear under the Proposed Regulations whether fiduciaries electing to override participants' prior instructions could obtain relief if the participants' accounts are invested in a QDIA.

The Department could clarify the Proposed Regulations to address these and similar situations by adding a provision that would permit plan fiduciaries to conclude that a participant (even if the participant may have previously provided affirmative investment instructions) will have "had the opportunity to direct the investment of assets in his or her account but did not direct the investment of assets" for purposes of § 2550.404c-5(c)(2) if the participant fails to respond within a reasonable time to a plan request for new affirmative investment instructions (such a request would include a notice with the information required by § 2550.404c-5(d)). This approach would provide plan sponsors much needed flexibility to transition participant investments from a currently designated default alternative to a QDIA and obtain relief under section 404(c)(5), even if plan records do not specify which participants have previously provided investment directions. On an ongoing basis, this approach also would facilitate the investment of participants' individual accounts in appropriate default investments.

3. Modify timing for notice in the case of "immediate participation" plans.

Under § 2550.404c-5(c)(3), the Proposed Regulations requires a participant or beneficiary to be furnished with a notice within a reasonable period of time of at least 30 days in advance of the first investment in a QDIA. However, this rule is unworkable for plans that provide for eligibility beginning on the employment commencement date or an eligibility waiting period of less than 30 days. Accordingly, the Proposed Regulations should be revised to include a special rule for "immediate participation" plans, which would require notice to be provided as far as practicable in advance of the first investment in a QDIA but such notice need not be provided before the participant's actual employment commencement date.

4. Revise participant investment information requirements.

We respectfully request that the Department reconsider § 2550.404c-5(c)(4) of the Proposed Regulations, which would require that —

> under the terms of the plan any material provided to the plan relating to a participant's or beneficiary's investment in a qualified default investment alternative (e.g., account statements, prospectuses, proxy voting material) will be provided to the participant or beneficiary.

As an initial matter, it is unclear why the "terms of the plan" must require that information be provided to a participant. This type of requirement may be a "trap" for an unwary plan sponsor, but would not ensure that plan participants whose accounts are allocated to a QDIA receive information that is helpful to their review of how their plan accounts are invested.

More importantly, this disclosure requirement could be unduly burdensome for plans, but would not provide plan participants with the type of information that they may find helpful in reviewing how their plan account balances are invested.

- First, as drafted, the Proposed Regulations would require plans to deliver a substantial volume of materials. With respect to a QDIA that is a registered investment company, a plan may receive (and would have to deliver to each participant) an annual prospectus and any prospectus updates, the investment company's semi-annual report to shareholders, and proxy materials. If a plan's QDIA is a managed account or plan portfolio made up of individual plan investment options, plans would have to deliver all of these documents for each of the plan investment options incorporated in the QDIA.

- Second, participant-directed plans typically do not provide for the pass-through of proxy-voting responsibility for shares of investment companies held by the plan. Delivering proxy materials to participants who are not eligible to vote would be at best confusing.

- Third, the language of the requirement in the Proposed Regulations relating to account statements is confusing. It is unclear whether participants' account statements are required, or if an account statement received by the plan to show the plan's holdings in a QDIA must be provided to plan participants. In addition, because other provisions of the Pension Protection Act impose new participant statement

> requirements for participant-directed plans, it should not be necessary to require participant account statements in the Proposed Regulations.

We respectfully suggest that the Department review this requirement and consider a rule that would result in plans delivering materials that will be helpful to participants rather than providing participants an overwhelming amount of information. Transamerica's experience is that plan participants who fail to provide investment elections for their plan account balances often do not have interest and/or expertise in investment matters. These participants are likely to find documents such as investment company prospectuses, semi-annual reports and proxy materials to be confusing rather than helpful. Further, we believe that plan communications to participants are more effective if the communications are presented in a shorter disclosure format limited to key information, as compared to more extensive and complex disclosure that may overwhelm participants and encourage them to ignore everything that is provided.

Therefore, we suggest that the Department revise this provision under the Proposed Regulations to require plans to deliver a simplified disclosure with respect to the QDIA, such as a "fact sheet" containing key information about the QDIA (e.g., the name of the investment company or designated investment manager, investment objective, type of assets, fees and expenses, and investment performance) and how additional information (including prospectuses and other documents) may be obtained.

5. Include capital preservation products as QDIAs.

We understand that the Department is receiving comments requesting that capital preservation products, including stable value and money market funds, be among the types of investment products included as eligible to be QDIAs, including comments from the American Council of Life Insurers and the American Benefits Council. Transamerica strongly agrees and urges the Department to include capital preservation products among the types of products allowed to be used as QDIAs.

6. Coordinate the regulations with preemption relief under section 514(e).

Congress included in the Pension Protection Act section 902(f), which provides preemption from conflicting state regulation for "automatic contribution arrangements" under new ERISA section 514(e). For this purpose, an automatic contribution arrangement is an arrangement under which "contributions are invested in accordance with regulations prescribed by the Secretary under section 404(c)(5)." Section 514(e) was effective as of August 17, 2006, the date of enactment of the Pension Protection Act.

Because new ERISA section 514(e) references the Department's regulations under section 404(c)(5), we request that the Department address several issues that are raised by new section 514(e) when finalizing the Proposed Regulations. In this regard, the preemption of state anti-wage garnishment laws, including certain criminal prohibitions against payroll withholding without employee consent, arguably may depend on whether a plan has complied with the Department's final regulations under section 404(c)(5).

First, we urge the Department to address an effective date issue. Specifically, although ERISA section 514(e) was effective as of August 17, 2006, it has not been possible for any employer to comply with its requirements because the Department has not issued final regulations under 404(c)(5). The Department can resolve this by specifying in its final regulations under 404(c)(5) that employers who adopt automatic contribution arrangements on or before the Proposed Regulations are finalized will be deemed to have complied with ERISA section 404(c)(5) effective as of August 17, 2006 (or the adoption date of the arrangement, if later) so long as contributions under the employer's automatic contribution arrangement are invested in accordance with the 404(c)(5) regulations after the regulations are effective, including a grace period. For this purpose, a grace period of at least one year would allow plan sponsors to incorporate an appropriate QDIA into their plans and comply with the notice and other conditions under final 404(c)(5) regulations.

Second, the Department has specifically recognized that its Proposed Regulations should not be construed to indicate that the use of investment alternatives not identified as a QDIA would be imprudent or not permissible.[3] If the Department agrees that investment alternatives other than QDIAs defined by the Proposed Regulations may be prudent, there is no reason to deny an employer the benefit of preemption for its automatic contribution arrangement if an alternative default is used. Therefore, we urge the Department to clarify in finalizing the Proposed Regulations that, for purposes of obtaining preemption relief under section 514(e), the default need not meet requirements under § 2550.404c-5(e) (which defines conditions for QDIAs), but other requirements of the final 404(c)(5) regulations must be met.

Finally, new ERISA section 514(e)(3) requires that the plan administrator of an automatic contribution arrangement must "within a reasonable period before such plan year, provide to each participant to whom the arrangement applies for such plan year notice of the participant's rights and obligations under the arrangement . . ." Transamerica requests that the Department clarify several issues with respect to this requirement.

- We believe that this notice requirement is not a condition to obtain preemption relief under ERISA section 514(e) based on the specific language of section 514(e) as well as the fact that Congress implemented a separate penalty under ERISA section 502(c)(4) that would apply if the notice is not provided. We request that the Department confirm this view.

- Because final regulations under 404(c)(5) have not been issued, we request that the Department clarify that any good faith effort to provide notice for plan years

[3] 71 Fed. Reg. at 56907.

beginning as of August 17, 2006 and until the section 404(c)(5) regulations are effective, will meet the notice requirement under section 514(e)(3).

- The Department should clarify that notice under section 514(e)(3) may be included with any notice required under § 2550.404c-5(c)(3) and will meet the "reasonable period" requirement under section 514(e)(3) if provided within the time frames described by the Proposed Regulations.

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We appreciate the opportunity to comment and hope that these comments will be helpful to the Department as it finalizes the Proposed Regulations. We welcome any questions that you may have about these comments.

Sincerely,

Catherine Collinson
Senior Vice President, Strategic Planning