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CAB 10-27

Milliman

CLIENT ACTION Bulletin

Employee Benefits

DOL Proposes Enhanced Target Date Retirement Fund and Default Investment Disclosures

SUMMARY

The Department of Labor (DOL) has issued a proposed rule designed to enhance the details of target date, life-cycle, or similar fund (collectively, TDFs) disclosures in 401(k) and other plans that give participants the right to direct their own investments. The new proposed rule also would amend two final regulations – the 2007 qualified default investment alternative (QDIA) regulation and the 2010 participant-level disclosure regulation – to require plan fiduciaries to provide additional information on investments that are included in TDFs and QDIAs.

The proposed rule would apply to plans covered by ERISA, and thus would exclude plans offered by governmental entities and churches that do not elect to follow ERISA. The DOL proposes the changes to be effective 90 days after publishing a final rule.

DISCUSSION

Background

The DOL issued a final regulation in October 2007 on the kinds of QDIAs in which a plan sponsor may enroll participants who fail to affirmatively select a plan investment option. Under this rule, the plan sponsor is relieved from its fiduciary obligations for investing such participants' money into a default investment option if it provides these "defaulted participants" an initial and an annual notice disclosing certain information about the QDIA. TDFs are among the investment options that qualify as appropriate QDIAs (see ***Client Action Bulletin 07-13***).

The final participant-level disclosure regulation, issued in October 2010, requires plan administrators of participant-directed individual account plans to provide specific plan-related and investment-related information about each designated investment alternative under the plan, including any TDFs (see ***CAB 10-22***).

The proposed rule would amend both final regulations to require that all participants and beneficiaries – whether or not they are defaulted into a TDF – be given certain information about TDFs in the required initial and/or annual notices. In general, the proposed rule aims at providing information participants need to evaluate TDFs and how a specific TDF may meet their investment objectives.

New Disclosures for TDFs Proposed

For TDFs, the proposed rule would require:

- an explanation of the TDF's asset allocation, how it will change over time, and the point at which the investment will reach its most conservative asset allocation, including a chart, table, or other graphical representation;
- an explanation, if the fund by name includes or implies a target date, of the age group for whom the investment is designed, the relevance of that date, and any assumptions about a participant's contribution and withdrawal intentions on or after such date; and
- a statement that the participant may lose money by investing in a TDF, including losses near and following retirement, and that there is no guarantee that the investment will provide adequate retirement income.

The information above would have to be provided in the initial and annual notices if the TDF is the plan's QDIA; otherwise, the disclosure would be provided as an appendix to the chart comparing the plan's investment alternatives.

New QDIA Disclosures Proposed

The proposed rule would also require additional disclosures about QDIAs, including:

- the name of the QDIA issuer;
- the investment objectives or goals;
- a description of the investment's principal strategies and risks;
- historical performance data and, if applicable, any fixed return, annuity, guarantee, death benefit, or other ancillary features;
- a statement indicating that an investment's past performance is not necessarily an indication of its future performance; and
- a description of fees and expenses, including those charged directly against the amount invested in connection with acquisition, sale, transfer of, or withdrawal (e.g., sales loads, sales charges, deferred sales and surrender charges, and redemption fees, exchange, account, and purchase fees); any annual operating expenses (e.g., expense ratio); and any ongoing expenses in addition to annual operating expenses (e.g., mortality and expense fees).

The DOL intends to issue a series of tips to help plan fiduciaries obtain and evaluate relevant information when selecting and monitoring TDFs as investment options. The DOL also announced it would review its Apr. 9, 2002, final regulation that includes a safe harbor for the use of electronic media to provide information to plan participants and beneficiaries.

ACTION

Fiduciaries of 401(k) and other participant-directed individual account plans should review the DOL's proposed rule with an eye toward ensuring compliance in the near future. Plan administrators will be required to provide participants more detailed disclosures about TDFs and QDIAs if the provisions in the proposed rule are retained in the final regulation and thus, communications materials may have to be revised. Because much of the information is likely to be furnished by investment issuers, the DOL expects plan sponsors' burdens to lie in incorporating the additional information in the initial and annual notices. Plan sponsors also should bear in mind that the Securities and Exchange Commission has been examining appropriate disclosures and marketing efforts by TDF investment issuers and is working with the DOL to develop guidance for retirement plan fiduciaries. In addition, plan administrators should be mindful of ERISA's general fiduciary standards that, among other things, require appropriate steps be taken in selecting and monitoring investments.

Comments on the proposed regulation must be submitted to the DOL by Jan. 14, 2011.

For additional information on the DOL's proposed rule on TDF and QDIA disclosures, please contact your Milliman consultant.