

BenAlert

Benefit Trends and Legislative Updates



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Howitt Insurance Services is pleased to provide you with periodic updates on benefit trends and legislative updates. As part of our valuable services, we want to ensure that you are in compliance and well-informed of the ongoing changes in our industry.

Department Of Labor Releases Final Regulations on 401(k) Plan Default Investment Vehicles

October 30, 2007

The Department of Labor has issued final regulations that provide a safe harbor to qualified plan fiduciaries to guide their selection of default investment alternatives for plan participants. Default investment alternatives are investments that are automatically provided by plan sponsor fiduciaries when participants who are given the opportunity to direct the investment of their defined contribution plan accounts (401k) do not make an investment election. This regulation will be applicable to 401k plans that use automatic enrollment for newly-eligible employees as well as plans that do not receive an election from participants. The final regulations are effective December 24, 2007.

Effective December 24, 2007, these final regulations go beyond the scope of automatically enrolled employees and will be applied by the Dept. of Labor to situations beyond automatic enrollment, including:

- the failure of a participant or beneficiary to provide investment direction following the elimination of an investment alternative or a change in service provider;
- the failure of a participant or beneficiary to provide investment instruction following a rollover from another plan; and
- any other failure of a participant to provide investment instructions.

If prudent default investment alternatives are in plan fiduciaries will be able to afford themselves of the protections afforded by ERISA section 404(c) with respect to these investments. The regulation states four specific categories of investment alternatives that can be used for the default investments:

- Investment funds, products, or model portfolios that offer a mix of equity and fixed income exposure based on the participant's age, target retirement date, or life expectancy (a "lifecycle" fund).
- Investment funds, products, or model portfolios that offer a mix of equity and fixed income exposure appropriate for the plan population as a whole (a "balanced" fund). In determining whether a fund is "appropriate," the fiduciary must recognize the average age of the population and is not precluded from considering other factors as well.
- An investment management service that allocates the assets of each participant's individual account through a mix of equity and fixed income exposures offered as investment alternatives under the plan, based on the participant's age, target retirement date, or life expectancy.
- Stable value or money market funds, can be used only for the first 120 days following the date of the participant's first elective contribution under an automatic enrollment plan (as defined in Code section 414(w)). This category is also available for default investments before the December 2007 effective date of the regulation.

The default investment must be managed by a registered investment manager, a mutual fund family or bank trust department.

Participants defaulted into the default alternative must have the same options to change their investments as other participants. For the first 90 days after the participant's initial investment into the default alternative, no restrictions, fees, or expenses may be imposed on the account if the participant elects to change investments, other than investment management and similar types of fees and expenses.

Once a participant makes an affirmative election to change any of the default investments to another investment option available under the plan, the participant is deemed to have made an affirmative election to leave the remainder of the account invested in the default alternative.

Employer Securities

Generally, investment in employer stock will not be an acceptable default alternative. But a regulated pooled investment vehicle (such as a common or collective trust fund) or a mutual fund can hold employer securities as part of its diversified portfolio.

Important: Notice Requirement

Each participant whose account will be invested in the default alternative must receive an initial notice at least 30 days in advance of the first investment in the default alternative or 30 days in advance of the participant's first date of plan eligibility. If the notice is provided late, the safe harbor is still available for investments made 30 days or more after the provision of the notice, even if the safe harbor is not available for earlier investments. In the case of a plan with automatic enrollment and a right to make a permissible withdrawal under Code section 414(w), the notice can be provided at any time on or before the date of plan eligibility. The annual notice cannot simply be included in a summary plan description, but can be included with other plan informational materials such as enrollment forms.

In addition to the initial notice, the plan administrator must provide an annual notice at least 30 days in advance of each plan year. The annual notice cannot simply be included in a summary plan description or summary of material modifications, but can be included with quarterly statements or other materials being furnished to plan participants and beneficiaries.

Participants whose accounts are invested in a default alternative must be provided with the same information about their investments as is required for other plan investment alternatives.

Immediate Action Required

Plan fiduciaries must immediately identify whether their defined contribution plans will have contributions going into default investments after the effective date of the regulation (pre-effective date contributions in default investments generally will be covered by the regulation if the investments are in stable value or money market funds, or other investment alternatives covered by the three regulatory categories). If so, one or more default investment alternatives must be selected by December 24, 2007 in compliance with the final regulation.

If any default investments are maintained under the plan (either old or new contributions), the fiduciaries must ensure compliance with the notice requirements of the final regulation.

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