

## ***ERISA SECTION 404(c) EMPLOYER GUIDELINES***

The ERISA Section (Sec.) 404(c) regulations allow you, as an employer, to significantly shift the responsibility for selecting retirement plan investments directly to plan participants and beneficiaries. Compliance with ERISA Sec. 404(c) is not mandatory in order to maintain a qualified retirement plan or a Title I 403(b) retirement plan. You could, therefore, choose to operate your plan without regard to these guidelines. Provided the requirements of ERISA Sec. 404(c) and the underlying regulations are met, however, you will be substantially free from any liability for the performance of the investments selected by plan participants and beneficiaries.

To take advantage of the relief offered by ERISA Sec. 404(c), you must take certain steps to alert and educate plan participants and beneficiaries about their investment responsibilities and options. These *ERISA Section 404(c) Employer Guidelines* are designed to give you a brief background to help you comply with the requirements of ERISA Sec. 404(c).

This set of guidelines is not designed to serve as a replacement for tax or legal advice. You should seek the assistance of a competent professional advisor if you have any questions regarding your plan's compliance with ERISA Sec. 404(c).

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### **The Purpose of ERISA Section 404(c)**

To understand the relief offered by ERISA Sec. 404(c), you must first have a basic understanding of the ERISA fiduciary rules. Under ERISA, the term "fiduciary" basically includes anyone who has discretionary authority over any aspect of plan administration. Persons who are considered fiduciaries of a plan are held to very strict standards of plan performance in an effort to protect plan participants and beneficiaries against fraud and mismanagement of plan assets. You, the employer, are deemed to be a fiduciary under ERISA.

It is important to note that compliance with the ERISA Sec. 404(c) regulations is completely voluntary and does not absolve you from all fiduciary responsibility. Rather, the 404(c) regulations prescribe the requirements which a participant-directed investment program must meet for you to absolve yourself of fiduciary responsibility with respect to plan participants' investment selections. One of your remaining fiduciary responsibilities under the plan is to select a range of prudent investments. The fiduciary who is responsible for plan investments must diversify the investments so as to minimize the risk of loss. You remain responsible for determining the investment alternatives available to plan participants and beneficiaries. You must choose such investments prudently and monitor their performance and their characteristics on an ongoing basis.

### **Basic Requirements Under ERISA Section 404(c)**

Under ERISA Sec. 404(c), for you to be absolved of liability with respect to the plan participants' investment selection, plan participants and beneficiaries must exercise "control in fact." The exercise of control over plan assets requires that plan participants and beneficiaries be allowed to

- choose among a broad range of investment alternatives consisting of at least three diversified investment categories, each of which is characterized by materially different risk and return factors;
- diversify investments generally both among and within the investment categories;
- receive sufficient information to make informed investment decisions; and
- give investment instruction as frequently as the market volatility of the particular investment dictates—in any event, no less frequently than quarterly.

### **Broad Range of Investments**

You are responsible for selecting the investment options from which the plan participants may choose. While there is no maximum number of investments that you may allow, to meet the requirements under ERISA Sec. 404(c), you must offer at least three "core" investment options. Regardless of how many investment options you allow, they must cover a broad range. In other words, the investment options must allow a plan participant to put together an investment portfolio that would place him on the risk/return range normally available for those in his circumstances, while also allowing him to minimize the overall risk of large losses by diversifying.

### **Investment Diversification**

You must choose core investment options that are materially different from each other in terms of risk and return to minimize the risk of loss. Additionally, the investment option itself must be diversified. For example, if a stock fund is offered, the various stocks in that fund must vary in terms of risk and likely return. While employer stock may be offered by a plan under ERISA Sec. 404(c), the employer stock cannot be one of the core investment options.

### **Employee Disclosures and Investment Information**

To take advantage of the relief offered by ERISA Sec. 404(c), you must inform plan participants and beneficiaries, in writing, that the plan participants and beneficiaries will be responsible for selecting their own investments.

In addition to the disclosure described above, you must provide investment information to plan participants and beneficiaries. The information must be sufficient to enable a plan participant to make an informed investment decision and must be provided in accordance with the requirements under the plan participant disclosure regulations (DOL Reg. 2550.404a-5). In general, this will require you to provide basic investment education to your employees covering such concepts as setting investment objectives, evaluating risk and return, dollar cost averaging, volatility, risk tolerance, asset allocation, and explaining the specific characteristics of the investments available under your plan. (Check with your plan sponsor or investment provider for assistance and for materials that you can use to explain to your employees the basic principles of investing.)

### **Investment Instructions**

**Frequency.** Plan participants and beneficiaries must be allowed to transfer their retirement plan dollars from one investment to another within the plan. The regulations require that investment changes be allowed

1. as often as the volatility of the investments require, and
2. at least quarterly for any core investment options.

In addition, if any noncore investment option allows for a change more frequently than quarterly, at least one of the core investment options must allow for the same frequency of changes.

As an alternative, you may provide an “income producing, low risk, liquid fund, sub-fund or account” into which plan participants can transfer from a noncore investment option as long as the plan participants can then transfer the assets to a core investment option as soon as they are allowed to change investment elections under that core investment option.

**Restrictions.** You may place some restrictions on changes of investment. For example, you could require that plan participants and beneficiaries move retirement plan dollars in increments of at least 10 percent of their balance. Also, you can refuse to conduct investment changes for a plan participant or beneficiary who is legally incompetent or investment changes that would result in a prohibited transaction. You should be cautious about imposing too many limitations, however. Limitations may be viewed as an infringement upon an individual’s exercise of control. If you do not permit sufficient control, you may not qualify for ERISA Sec. 404(c) protection.

**Reasonable Charges.** You may charge reasonable expenses for carrying out investment instructions provided that procedures are established under the plan to periodically inform the plan participants and beneficiaries of the actual expenses incurred with respect to their individual accounts.

### **Coordination with Participant Disclosure**

New ERISA Sec. 404(c) requirements will apply for plan years beginning on or after November 1, 2011. The final plan participant disclosure regulations under ERISA Sec. 404(a) state that you will satisfy the ERISA Sec. 404(c) notice requirements if

- you provide the plan participants with an explanation stating that the plan is an ERISA Sec. 404(c) plan;
  - you provide the plan participants with all of the information required to be disclosed under the participant disclosure regulations (see the *Participant Fee Disclosure and 404(c) Employee Information Sheet* for this information); and
  - when your plan offers employer securities as an investment alternative, you provide the plan participants with a description of the procedures established to provide for the confidentiality of information regarding holding and voting those securities, including contract information for the responsible fiduciary.
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