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Re: The DOL Clarifies QDIA Regulations

Dear Clients and Other Friends:

The Department of Labor recently issued amendments and clarifications with respect to its qualified default investment alternative (“QDIA”) regulations. The final QDIA regulations became effective December 24, 2007. Due to some awkward wording in the final regulations, however, there was considerable uncertainty about how to apply the QDIA rules.

The DOL has addressed some of these issues by amending the final QDIA regulations and by issuing Field Assistance Bulletin (“FAB”) 2008-03. The amendments were published in the Federal Register on April 30, 2008 (<http://www.dol.gov/ebsa/regs/fedreg/notices/E8-9371.htm>). The FAB was issued on April 29, 2008 (<http://www.dol.gov/ebsa/regs/fab2008-3.html>).

The amended regulations include these clarifications:

1. Stable Value Products, including Stable Value Funds – December 24, 2007 Grandfather Rule

The DOL clarified that typical stable value products, including stable value funds, qualify for the “grandfather” rule that treats them as QDIAs with respect to default investments made before December 24, 2007. It was clear that the DOL’s grandfather provision in the final QDIA regulations was intended to include the commonly used stable value products (otherwise, it had limited application). This amendment provides helpful clarification of the scope of the grandfather rule.

2. Plan Sponsor Committee as QDIA Manager

As amended, the QDIA regs. clarify that a committee comprised primarily of employees of the plan sponsor/employer and acting as named fiduciary is permitted to manage a QDIA. The QDIA regs. now provide that a QDIA can be a mutual fund or must be managed by an investment manager, plan trustee, plan sponsor or a committee comprised primarily of employees of the plan sponsor that is a named fiduciary.

3. No Prohibition of “Roundtrip” Restrictions During First 90 Days

The amendments clarify that “roundtrip” restrictions that only affect a participant’s ability to reinvest in the QDIA for a limited period of time, are permissible. Roundtrip restrictions that limit the ability to liquidate or transfer amounts from a QDIA or limit the ability to invest in other available investment funds are prohibited. To the extent defined by a mutual fund in its prospectus, especially with regard to timing and/or dollar amount limitations, “roundtrip” trades are those that involve a purchase and a redemption within a short period of time.

The DOL issued FAB 2008-03 (in a question and answer format) to describe the application of the final QDIA regs. and how they interact with ERISA. Issues covered include:

- A. A plan sponsor or committee that is named fiduciary of the plan and is primarily comprised of the plan sponsor’s employees is relieved of the liability for the decisions to invest all or part of a participant’s account in the QDIA but is not relieved of liability related to the management of the QDIA or the prudent selection or monitoring of the QDIA.
- B. QDIA fiduciary relief is available with respect to participants who on or after the effective date of the regs. (December 24, 2007), fail to give investment direction after being provided the required notice, regardless of whether the participant made an earlier affirmative election to invest in the plan’s default investment.
- C. The DOL clarified that nothing in the QDIA regs. precludes the use of separate, but simultaneously furnished, documents to satisfy the QDIA notice requirements. Such documents may include a prospectus or profile prospectus of a mutual fund that is a QDIA. Generally, participants must receive information concerning a QDIA either automatically or upon the request of a participant, as provided under the DOL’s 404(c) regs.
- D. The DOL is considering a separate regulatory initiative concerning the broader application of disclosure of investment materials by electronic means. In the meantime, the QDIA notice may be provided by electronic means consistent with current DOL or IRS guidelines.
- E. The annual notice requirements for qualified automatic contribution arrangements (QACAs) and eligible automatic contribution arrangements (EACAs) are satisfied if notice is provided at least 30, but not more than 90, days before the beginning of each year.
- F. EACAs that permit an employee to withdraw default contributions during the 90-day period following the date of the employee’s first deferral can satisfy the QDIA initial notice requirement (as well as the IRS’ special rule for employees who do not receive the annual notice because they are newly eligible) by

providing a notice on or before an employee's date of eligibility. The notice cannot, however, be given more than 90 days prior to eligibility. To satisfy this requirement an employer can provide this notice on the first day of plan participation.

- G. The QDIA notice can be included on a 401(k) plan safe harbor notice.
- H. A QDIA cannot be an investment fund or product with zero fixed income or zero equity. The investment fund model portfolio or investment management service must be "diversified so as to minimize the risk of large losses" and be designed to provide varying degrees of long-term appreciation and capital preservation through a "mix" of equity and fixed income exposures.
- I. The 120-day capital preservation QDIA is available only for plans that include an EACA. Plans are not required to provide a 120-day capital preservation QDIA. Any 120-day capital preservation QDIA must be offered by a state or federally regulated financial institution as required under the QDIA regs.

For a short summary of the final QDIA regs. requirements, including the recent clarifications included in the amendment to the final regs. and FAB 2008-03, see the DOL QDIA Fact Sheet available at <http://www.dol.gov/ebsa/newsroom/fsQDIA.html>.

Most employers will want to avail themselves of the available fiduciary relief for using one or more QDIAs under a 401(k) plan. It is important for plan sponsors to understand and follow the DOL's regulatory guidance as recently revised and clarified. If you would like more information about QDIA requirements, please contact us.

Sincerely,

Ted Rice

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