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DOL Proposes Further Disclosures for Target Date Funds and Default Investments

On November 30, 2010, the Department of Labor (DOL) [proposed new regulations](#) requiring plan fiduciaries to provide enhanced disclosures about target date funds to retirement plan participants directing their own investments. The proposal would also amplify the investment information that must be disclosed about a plan's qualified default investment alternative (QDIA), even if it is not a target date fund. DOL proposes that these amendments would be effective 90 days following publication of the final rule in the Federal Register. Comments on the proposed regulations must be received no later than January 14, 2011.

Background

This new development represents the intersection of two different DOL regulatory initiatives. DOL has for several years been in the process of considering and then requiring enhanced disclosures for participants who direct the investment of their own retirement plan accounts.

- In October 2007, DOL issued [a final QDIA regulation](#), providing relief for fiduciaries of participant-directed individual account plans who invest participant accounts in certain designated investment alternatives in the absence of affirmative investment directions by the participant. Under this rule, which includes target date funds as a type of fund that may be used as a plan's QDIA, a fiduciary may be relieved from liability under the Employee Retirement Income Security Act (ERISA) § 404(c) for loss or fiduciary breach resulting from the investment of a participant's account in a QDIA when the participant has an opportunity to but does not direct the investment of his or her account. Relief is available under the final regulation only if the fiduciary provides participants with initial and annual notices disclosing certain information about the plan's QDIA.
- In October 2010, DOL issued [a final participant disclosure regulation](#), which takes the position that the ERISA § 404(a) fiduciary rules are satisfied only if certain plan- and investment-related disclosures are made to participants in a participant-directed individual account plan. Thus, this final regulation applies to all participant-directed individual account plans, not just a plan intended to qualify for relief under ERISA § 404(c). The regulation provides detailed and expansive guidance on the types of plan- and investment-related information that must be furnished, as well as when and how often such information should be provided. When issuing the participant disclosure regulation, DOL reserved rules on target date fund disclosures for future guidance.

Simultaneously, DOL and the Securities and Exchange Commission (SEC) have jointly been considering issues raised by the performance of target date funds in late 2008 and early 2009.

- In May 2010, DOL and the SEC published [a joint investor bulletin](#) addressed to retirement plan participants considering an investment in target date funds.
- In June 2010, the SEC [proposed rules](#) for the information that must be provided in connection with the advertising and marketing of target date funds registered under the Investment Company Act of 1940.

The agencies have announced that they also intend to (i) jointly publish a target date fund compliance checklist for retirement plan fiduciaries and (ii) continue to examine how target date funds are marketed.

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Additional Disclosures for Target Date Funds

In the disclosure to all participants in participant-directed plans under DOL's October 2010 regulation, DOL's new proposal would require the following additional information for a designated investment option that is a target date, life-cycle or similar fund:

- An explanation of the fund's asset allocation, how it will change over time, and the point in time when the fund will reach its most conservative asset allocation, including an illustrative chart, table, or similar graphic;
- For funds that include or imply a target date in their name, the age group for whom the investment is designed, the relevance of the date, and any assumptions about a participant's or beneficiary's contribution and withdrawal intentions on or after that date; and
- A statement that the participant or beneficiary may lose money by investing in the fund, including losses close to and following retirement, and that there is no guarantee that investment in the fund will provide adequate retirement income.

This information would be provided as an appendix to the chart comparing the plan's investment alternatives (including the target date fund), which is already required under the October 2010 regulation.

Where a target date fund or portfolio is the plan's QDIA, the proposal would require this additional information be included in the initial and annual QDIA notices to participants specified in the October 2007 QDIA regulation.

These requirements generally do not apply by their terms to individual retirement accounts (IRAs).

Proposed SEC Rules for Target Date Fund Disclosures

The SEC's June 2010 proposal is similar in concept to the DOL proposal but differs in certain details. Funds subject to both proposals would need to meet the DOL and SEC requirements cumulatively.

- The SEC proposal also addresses the concern that a fund containing a target date in its name may lead to investor misunderstanding about the fund. To alleviate potential confusion, the SEC proposal would require marketing materials for any such a target date fund to include, alongside the fund's name, the asset allocation of the fund at the target date.
- The SEC proposal also requires inclusion of a table, chart or other graphic illustrating how the investment's asset allocation will change over time. The SEC proposal contains more detailed requirements than the DOL proposal with respect to the information that this graphic must contain. For instance, the SEC proposal specifically requires that fund marketing materials include the fund's asset allocation at the inception of the fund, on the target date, and at the landing point. The SEC proposal also provides that specific dates generally must be used to show the asset allocation over time (as opposed to referencing the number of years before a participant's retirement date, although this would generally be permitted when advertising multiple target date funds sharing a common glide path), and that intervals of no longer than five years may be used for this purpose.
- Like the DOL proposal, the SEC proposal requires a statement that a target date fund is not a guaranteed investment. The SEC proposal further requires a statement that a target date fund should not be selected based solely on age or retirement date and that a target date fund's stated asset allocation may be subject to change.

Additional Disclosures for All QDIAs

For the initial and annual QDIA notices, DOL's October 2007 QDIA regulation currently requires only the following investment-related information: "a description of the qualified default investment alternative, including a description of the investment objectives, risk and return characteristics (if applicable), and fees and expenses attendant to the investment alternative." To better conform the QDIA disclosure to the October 2010 participant disclosure requirement, DOL's proposal would clarify that investment-related information for any QDIA must include all of the following:

- The name of the investment's issuer;
- The investment's objectives or goals;
- The investment's principal strategies (including a general description of the types of assets held by the investment) and principal risks (as required by the applicable SEC form);
- The investment's historical performance data (e.g., one-, five- and 10-year returns) 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 indicator of future results; and
- The investment's attendant fees and expenses, including:
 - Any fees charged directly against the amount invested in connection with acquisition, sale, transfer, or withdrawal (e.g., sales loads, sales charges, deferred sales charges, redemption fees, surrender charges, exchange fees, account fees, and purchase fees);
 - Any annual operating expenses, such as the expense ratio; and
 - Any additional ongoing expenses, such as mortality and expense fees.

DOL specifically requested comments on the extent to which these requirements should conform to the October 2010 regulation and whether they should incorporate by reference the participant disclosure regulation's more specific standards for investment-related information. For instance, under the rules as currently proposed, a QDIA notice would not be required to reference a broad-based securities index as a benchmark for the QDIA, while such information generally would be required under the participant disclosure regulation.

Additional proposed amendments would further align the QDIA disclosure requirements with the participant disclosure regulation. For instance, the current requirement under the QDIA regulation that participants be provided with information regarding voting rights, as well as annual prospectuses, would remain, but the requirement would cross-reference the participant disclosure regulation. Thus, as a condition for QDIA relief, prospectuses would be required to be furnished upon request to a participant invested in a QDIA, as would copies of financial statements, statements of share valuations, and a list of the assets comprising the QDIA. Additionally, the QDIA notice would be required to alert participants to the availability of additional information about both the QDIA and the plan's other investment alternatives. Currently the QDIA regulation only requires the plan to make available comprehensive information about the plan's investment alternatives *other* than the QDIA.



If you have any questions about this development, please feel free to contact any of the attorneys listed below or the Sutherland attorney with whom you regularly work.

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