USI CONSULTING GROUP

ERISA § 404(c) COMPLIANCE

ERISA §404(c) provides limited relief from certain fiduciary responsibilities if participants or beneficiaries are allowed to exercise investment control over their individual accounts. Specifically, compliance with the requirements of §404(c) provides a defense for fiduciaries of a participant-directed investment plan in the event of plan losses that were a direct result of investment instructions given by participants or beneficiaries.

The §404(c) relief is available only if the plan fiduciary complies with the specific requirements of the §404(c) regulations. If a fiduciary represents to plan participants or beneficiaries that the plan is a §404(c) plan, but the fiduciary clearly is not complying with the §404(c) regulations:

- A court will most likely deny §404(c) protection; and
- The Department of Labor may prosecute for a breach of fiduciary duty.

The §404(c) regulations provide the following guidance to assist employers in complying with the requirements and obtain §404(c) relief. ***The regulations are lengthy and complicated and plan fiduciaries should consult with a benefit professional or legal counsel familiar with pension law to ensure compliance.***

General Requirements

- Duty to prudently select investment alternatives. The plan must offer at least three core investment alternatives which:

    i. are diversified,
    ii. have materially different risk and return characteristics,
    iii. enable a participant or beneficiary to structure a portfolio with risk/return characteristics within the range normally appropriate for participant or beneficiary, and
    iv. tend to minimize through diversification the overall risk to the participant's or beneficiary's portfolio.

- Duty to monitor investment alternatives. The plan fiduciary responsible for designating investment alternatives has a duty to periodically monitor and reevaluate the investment and fund manager designations.

- Opportunity for plan participants or beneficiaries to exercise control. The plan must give participants or beneficiaries:

    i. the opportunity to give investment instructions in writing or otherwise (with the right to receive written confirmation) to an identified plan fiduciary who is obligated to comply with the instructions; and
    ii. the right to give investment instructions with a frequency that is appropriate in light of market volatility.

- The participant's or beneficiary's exercise of control must be independent. For example, a fiduciary or plan sponsor should not:

    i. exert improper influence on the participant or beneficiary;
    ii. conceal material facts (unless disclosure would violate applicable federal or state laws); or
    iii. accept instructions from a participant or beneficiary known to be legally incompetent.

In some cases, plans provide that a participant who does not make an affirmative investment election will have his or her account invested in a "default investment" under a plan. The Qualified Default Investment Alternative ("QDIA") regulations issued in October of 2007 expanded ERISA 404(c) protection to plan fiduciaries for a plan's default investment provided certain conditions are met. If the conditions are met, plan participants are deemed to have "exercised control" over their plan accounts and plan fiduciaries are not held liable for investment losses that are a direct and necessary result of the investment of participant accounts in the default investment. A default investment fund will satisfy these rules if:

- » it falls within one of the four enumerated types of investment funds described in the regulations, which include life cycle, target date and balanced funds;
- » participants are provided with the opportunity to choose their own investments, but have not done so;
- » transfers out of the default investment are at least as favorable as for other investments and allowed at least quarterly;
- » informational materials (e.g. prospectuses, account statements, proxy voting materials) on the QDIA must be provided to participants and beneficiaries as listed below;
- » the plan must provide certain notices to participants regarding the QDIA; and
- » the plan must offer participants the opportunity to invest in "a broad range of investment alternatives" as indicated above.

Information That Must be Provided

- The plan fiduciary must give information to each participant or beneficiary that is generally sufficient to allow the participant or beneficiary to make informed investment decisions. The following information must be provided:

    1. An explanation that the plan is intended to be a 404(c) plan.
    2. An explanation that plan fiduciaries may be relieved of liability.
    3. A description of each investment alternative available under the plan.
    4. A general description of the investment objectives, risk and return characteristics, and the type and diversification of assets in the portfolio of each investment alternative.
    5. The identity of the designated investment manager, if any.
    6. An explanation about giving investment instructions, including to whom, when and any limitations on such instructions, and any restrictions on transfers or exercise of voting rights.
    7. A description of transaction fees, charges or expenses chargeable against the participant or beneficiary's account.
    8. The name, address and telephone number of the plan fiduciary responsible for providing additional information available upon request and the type of information available.
    9. Specified information regarding investments in employer securities.
    10. A copy of the most recent prospectus (provided to the plan) immediately following the initial investment in an option subject to the Securities Act of 1933.
    11. Materials provided to the plan that relates to the exercise of voting, tender, or similar rights that are passed through to the participant or beneficiary.

Information Provided Upon Request

- A participant or beneficiary must be provided with certain information upon request:

    1. A description of the annual operating expenses of each designated investment alternative, including fees and transaction costs which reduce a participant's or beneficiary's rate of return, and the aggregate amount of such expenses expressed as a percentage of average net assets of the designated investment alternatives.

    2. Copies of prospectuses, financial statements and reports, and other materials related to investment alternatives available under the plan to the extent such information is provided to the plan.

    3. A list of assets comprising the portfolio of each designated investment alternative and the value of each asset (or the proportion of the investment alternative which it comprises).

    4. The value of shares in designated investment options available under the plan, as well as the past and current investment performance, net of expenses.

    5. The value of shares of designated investment alternatives held in the account of a participant or beneficiary.