



DOL Field Assistance Bulletin 2007-1: Investment Advice to Plan Participants

It's rare to find a subject that lends itself to widespread agreement across all stakeholders, including law and policymakers in Washington, DC. Investment advice for retirement plan participants, however, is one such example. The benefits of having access to professional investment advice is clear; it's without question that advised participants are much more well diversified, appropriately allocated and aware of their retirement income needs. Indeed, Congress recognized as much, and the Pension Protection Act of 2006 directed the Department of Labor (DOL) to issue a prohibited transaction exemption to ensure that more participants receive access to professional investment advice. The final DOL rule is expected out this Fall.

Plan sponsors also benefit significantly from participant advice programs. To the extent a plan sponsor can demonstrate that the advice provider was prudently selected and is periodically monitored, ERISA provides absolute protection from liability for investment-related losses for participants who receive ongoing investment advice. This protection exists today where the advice is conflict-free, and the new DOL rules will afford the same protections (albeit with additional safeguards i.e., annual audits, specific disclosures, etc.) to plan sponsors for advice offered through advisers that may be conflicted under the current rules. DOL Field Assistance Bulletin 2007-1 sets forth additional guidance for plan sponsors.

Compliant participant advice programs protect retirement plan advisers as well. Many plan advisers are prohibited under ERISA from rendering investment advice that may affect their compensation or that of an affiliate. Variable 12b-1 fees, revenue sharing arrangements and affiliated products are common examples of unlevel compensation that could trigger a prohibited transaction. For this reason, the policies and procedures of many broker-dealers only allow registered representatives to provide investment education to plan participants. While there are a number of ways to structure meaningful education-based programs, plan sponsors do not receive the same protection they would if participants received ongoing investment advice from a prudently selected and monitored third-party.

There may be other reasons for a supervising firm to prohibit advisers from providing fiduciary services to plan participants such as preserving the advisers' ability to work more holistically with participants. For example, DOL Advisory Opinion 2005-23A cautions ERISA fiduciaries from using the authority that makes him/her a fiduciary to cause a participant to take action that results in greater compensation being paid to the fiduciary and/or his/her affiliates. The DOL's position is that an unsophisticated plan participant may simply "rubber stamp" any recommendation that a fiduciary adviser provides, including one to take assets out of the plan to invest in an IRA. To the extent this transaction results in greater compensation being paid to the adviser and/or his affiliates, the 2005 opinion warns that it may be a prohibited transaction. Inserting a third-party participant advice provider can insulate the adviser from this risk and leave him/her free to solicit IRA rollovers and discuss additional products and services with plan participants.¹

¹ Given the increasing demand from plan sponsors, and the above-referenced risk management benefits to broker-dealers and their advisers, we are working with a number of firms to conduct due diligence on third-party participant advice programs. We are seeing wide disparity among advice providers with respect to utilization. Many programs, which are not actively marketed and supported, report less than ten percent of participants on average actually use the service. The protections afforded to plan sponsors and advisers only extend to participants that receive ongoing advice, so utilization is a key factor that needs to be considered before recommending or implementing a participant advice solution.

WEST
613 Ocean Drive
Manhattan Beach
CA 90266

T: 310 210 1679

EAST
60 Thomas Park
South Boston
MA 02127
T: 617 834 0900
pension-resources.com

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Memorandum For: Virginia C. Smith
Director of Enforcement, Regional Directors

From: Robert J. Doyle
Director of Regulations and Interpretations

Subject: Statutory Exemption For Investment Advice

Background

Section 3(21)(A)(ii) includes within the definition of “fiduciary” a person that renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of a plan, or has any authority or responsibility to do so.⁽¹⁾ The prohibited transaction provisions of ERISA and the Internal Revenue Code (Code) prohibit an investment advice fiduciary from using the authority, control or responsibility which makes it a fiduciary to cause itself, or a party in which it has an interest that may affect its best judgment as a fiduciary, to receive additional fees. As a result, in the absence of a statutory or administrative exemption, fiduciaries are prohibited from rendering investment advice to plan participants regarding investments that result in the payment of additional advisory and other fees to the fiduciaries or their affiliates.

The growth of participant directed individual account plans has increased recognition of the importance of investment advice to participants in such plans. Accordingly, employers and other fiduciaries have raised questions concerning their responsibilities in connection with offering investment advice programs. In response to these questions, the Department has issued various forms of guidance concerning when a person would be a fiduciary by reason of rendering investment advice and when the provision of investment advice may result in prohibited transactions.⁽²⁾

The Pension Protection Act of 2006 (PPA)⁽³⁾ amended both ERISA and the Code to add a statutory exemption relating to the provision of investment advice. Specifically, section 601 of the PPA added a statutory exemption under section 408(b)(14) of ERISA (and section 4975(d)(17) of the Code⁽⁴⁾). Section 408(b)(14) applies to the provision of investment advice under an “eligible investment advice arrangement,” as defined in paragraph (2) of section 408(g) (also added by the PPA), to participants and beneficiaries of a defined contribution plan that permits them to direct the investment of their accounts in the plan. If the conditions of section 408(g) are met, section 408(b)(14) exempts from the prohibited transaction rules the provision of investment advice, the investment transaction entered into pursuant to the advice, and the direct or indirect receipt of fees or other compensation by the fiduciary adviser or an affiliate in connection with the provision of advice or the transaction pursuant to the advice. An “eligible investment advice arrangement” is an arrangement that either provides that any fees (including any commission or other compensation) received by the fiduciary adviser for investment advice or with respect to the investment of plan assets do not vary depending on the basis of any investment option selected, or uses a computer model under an investment advice program that meets the requirements set forth in section 408(g)(3).

Paragraph (10) of section 408(g) addresses the responsibility and liability of plan sponsors and other fiduciaries in the context of investment advice provided pursuant to the statutory exemption. Subject to certain requirements, section 408(g)(10) provides that a plan sponsor or other person who is a plan fiduciary, other than a fiduciary adviser, is not treated as failing to meet the fiduciary requirements of ERISA

solely by reason of the provision of investment advice as permitted by the statutory exemption. This provision does not exempt a plan sponsor or a plan fiduciary from fiduciary responsibility under ERISA for the prudent selection and periodic review of the selected fiduciary adviser. The provision does make clear, however, that plan sponsors and other persons who are fiduciaries do not have a duty under ERISA to monitor the specific investment advice given by a fiduciary adviser to any particular recipient of the advice.

Since the enactment of section 408(b)(14) and 408(g) of ERISA, the Department has received a number of inquiries concerning the status of its prior guidance on investment advice and the scope of the statutory exemption for investment advice. This Bulletin provides guidance to EBSA's national and regional offices on the following specific issues.

Issues

1. Did enactment of the investment advice provisions of the Pension Protection Act of 2006 invalidate or otherwise affect prior guidance issued by the Department concerning investment advice?

No. It is the view of the Department that enactment of section 408(b)(14) and 408(g) allows the provision of investment advice to plan participants under circumstances that would, in the absence of an exemption, have constituted a prohibited transaction prior to the enactment of the PPA. Except for providing that persons who develop or market computer models described in section 408(g)(3) or who market investment advice programs using such models are fiduciaries, and requiring advisers to expressly acknowledge their fiduciary status,⁽⁵⁾ sections 408(b)(14) and 408(g) do not alter ERISA's framework for determining fiduciary status or recast otherwise permissible forms of investment advice as prohibited for purposes of section 406. For this reason, it is the view of the Department that the new provisions do not invalidate or otherwise affect prior guidance of the Department relating to investment advice and that such guidance continues to represent the views of the Department.⁽⁶⁾

Guidance of particular note in this regard includes: Interpretive Bulletin 96-1 (29 CFR § 2509.96-1), in which the Department identified categories of investment-related information and materials that do not constitute investment advice; Advisory Opinion Nos. 97-15A and 2005-10A, in which the Department explained that a fiduciary investment adviser could provide investment advice with respect to investment funds that pay it or an affiliate additional fees without engaging in a prohibited transaction if those fees are offset against fees that the plan otherwise is obligated to pay to the fiduciary; and Advisory Opinion 2001-09A in which the Department concluded that the provision of fiduciary investment advice, under circumstances where the advice provided by the fiduciary with respect to investment funds that pay additional fees to the fiduciary is the result of the application of methodologies developed, maintained and overseen by a party independent of the fiduciary, would not result in prohibited transactions.

2. To what extent are the standards for selecting and monitoring a fiduciary adviser described in section 408(g)(10) different from the standards applicable to plan fiduciaries who offer an investment advice program with respect to which relief under the statutory exemption for investment advice (section 408(b)(14)) is not required?

It is the view of the Department that, with the exception of certain requirements in subparagraph (A)(i) – (iii) of section 408(g)(10) regarding compliance with the conditions of the statutory exemption, the same fiduciary duties and responsibilities apply to the selection and monitoring of an investment adviser for participants and beneficiaries in a participant directed individual account plan, regardless of whether the program of investment advice services is one to which the statutory exemption applies.

Subparagraph (A) of section 408(g)(10) provides that a plan fiduciary shall not be treated as failing to meet the requirements of Part 4 of title I of ERISA solely by reason of the provision of investment advice within the meaning of section 3(21)(A)(ii) or solely by reason of contracting or arranging for the provision of investment advice pursuant to an "eligible investment advice arrangement" but subject to subparagraph (B), which

addresses a fiduciary's duty to select and review the investment advice provider prudently. This principle is consistent with the Department's guidance provided in Interpretive Bulletin 96-1 regarding the provision of investment advice generally. See 29 CFR § 2509.96-1(e). Accordingly, it is the view of the Department that a plan sponsor or other fiduciary will not fail to meet the requirements of Part 4 of title I of ERISA solely by reason of offering a program of investment advice services to participants or beneficiaries that is not an "eligible investment advice arrangement."

Subparagraph (B) of section 408(g)(10), however, makes clear that, without regard to subparagraph (A), plan fiduciaries have a duty to prudently select and periodically monitor the advisory program. Subparagraph (B) of section 408(g)(10) further clarifies that fiduciaries have no duty to monitor the specific investment advice given by the fiduciary adviser to any particular recipient of advice. As with subparagraph (A), it is the view of the Department that the principles described in subparagraph (B) of section 408(g)(10) are consistent with those set forth in § 2509.96-1(e) and, therefore, equally applicable to plan fiduciaries who select a program of investment advice services with respect to which relief under the investment advice statutory exemption is not required.

Thus, it is the view of the Department that a plan sponsor or other fiduciary that prudently selects and monitors an investment advice provider will not be liable for the advice furnished by such provider to the plan's participants and beneficiaries, whether or not that advice is provided pursuant to the statutory exemption under section 408(b)(14).⁽²⁾

Although the Interpretive Bulletin does not address the monitoring of specific investment advice provided to a particular plan participant or beneficiary, the Department believes that fiduciaries selecting advisory programs are subject to the same fiduciary duty to prudently select and monitor investment advisers regardless of whether the advice arrangement was established under the section 408(b)(14) exemption. Accordingly, it is the view of the Department that, like fiduciaries offering exempted advice arrangements, fiduciaries offering programs of investment advice services with respect to which exemptive relief is not required have no duty to monitor the specific investment advice given by the investment advice provider to any particular recipient of the advice.

With regard to the prudent selection of service providers generally, the Department has indicated that a fiduciary should engage in an objective process that is designed to elicit information necessary to assess the provider's qualifications, quality of services offered and reasonableness of fees charged for the service. The process also must avoid self dealing, conflicts of interest or other improper influence. In applying these standards to the selection of investment advisers for plan participants, we anticipate that the process utilized by the responsible fiduciary will take into account the experience and qualifications of the investment adviser, including the adviser's registration in accordance with applicable federal and/or state securities law, the willingness of the adviser to assume fiduciary status and responsibility under ERISA with respect to the advice provided to participants, and the extent to which advice to be furnished to participants and beneficiaries will be based upon generally accepted investment theories.

In monitoring investment advisers, we anticipate that fiduciaries will periodically review, among other things, the extent to which there have been any changes in the information that served as the basis for the initial selection of the investment adviser, including whether the adviser continues to meet applicable federal and state securities law requirements, and whether the advice being furnished to participants and beneficiaries was based upon generally accepted investment theories. Fiduciaries also should take into account whether the investment advice provider is complying with the contractual provisions of the engagement; utilization of the investment advice services by the participants in relation to the cost of the services to the plan; and participant comments and complaints about the quality of the furnished advice. With regard to comments and complaints, we note that to the extent that a complaint or complaints raise questions concerning the quality of advice being provided to participants, a fiduciary may have to review the specific advice at issue with the investment adviser.

Subparagraph (C) of section 408(g)(10) makes clear that plan assets can be used to pay reasonable expenses in providing investment advice to participants and beneficiaries. Again, this provision is consistent with the long held view of the Department, as set forth in § 2509.96-1(e), provided that the service provider rendering investment advice is selected and monitored prudently. Consistent with this guidance, fiduciaries selecting programs of investment advice services with respect to which exemptive relief is not required may use plan assets to pay reasonable expenses in providing investment advice (and/or investment education) to plan participants and beneficiaries.

3. For purposes of an “eligible investment advice arrangement” within the meaning of section 408(g)(2)(A)(i), is an affiliate of a fiduciary adviser subject to the level fee requirement?

The investment advice exemption provided by section 408(b)(14) applies only to investment advice provided by a “fiduciary adviser” under an “eligible investment advice arrangement.” Section 408(g)(2)(A)(i) includes within the meaning of “eligible investment advice arrangement” an arrangement that, among other things, provides that any fees (including any commission or other compensation) received by the fiduciary adviser for investment advice or with respect to the sale, holding, or acquisition of any security or other property for purposes of investment of plan assets do not vary depending on the basis of any investment option selected.

The term “fiduciary adviser” is defined in section 408(g)(11)(A) to mean a person who is a fiduciary of the plan by reason of providing investment advice *and* who is a registered investment adviser, a bank or similar financial institution, an insurance company, or a registered broker dealer; an affiliate⁽⁸⁾ of such registered investment adviser, bank, insurance company, or broker dealer; *or* an employee, agent or registered representative of any such entity.

It is clear from section 408(g)(2)(A)(i) that only the fees or other compensation of the fiduciary adviser may not vary. In this regard we note that, in contrast to other provisions of section 408(b)(14) and section 408(g), section 408(g)(2)(A)(i) references only the fiduciary adviser, not the fiduciary adviser or an affiliate. Inasmuch as a person, pursuant to section 408(g)(11)(A), can be a fiduciary adviser only if that person is a fiduciary of the plan by virtue of providing investment advice, an affiliate of a registered investment adviser, a bank or similar financial institution, an insurance company, or a registered broker dealer will be subject to the varying fee limitation only if that affiliate is providing investment advice to plan participants and beneficiaries.

Also, consistent with past Departmental guidance (see discussion of issue 1), if the fees and compensation received by an affiliate of a fiduciary that provides investment advice do not vary or are offset against those received by the fiduciary for the provision of investment advice, no prohibited transaction would result solely by reason of providing investment advice and thus there would be no need for a prohibited transaction exemption.⁽⁹⁾ It is the view of the Department, therefore, that, for purposes of section 408(g)(2)(A)(i), Congress did not intend for the requirement that fees not vary depending on the basis of any investment options selected to extend to affiliates of the fiduciary adviser, unless, of course, the affiliate is also a provider of investment advice to a plan.

We further note that although section 408(g)(11)(A) generally limits “fiduciary advisers” to certain types of entities, it also permits employees, agents, or registered representatives of those entities to also qualify as fiduciary advisers if they satisfy the requirements of applicable insurance, banking, and securities laws relating to the provision of the advice. *See* section 408(g)(11)(A)(vi). As with affiliates, such an individual must, for purposes of section 408(g)(11)(A), not only be an employee, agent, or registered representative of one of those entities, but also must provide investment advice in his or her capacity as employee, agent, or registered representative. It is the view of the Department that when an individual acts as an employee, agent or registered representative on behalf of an entity engaged to provide investment advice to a plan, that individual, as well as the entity, must be treated as the fiduciary adviser for purposes of section 408(g)(11)(A).⁽¹⁰⁾ In such instances, therefore, both the individual and the entity would be treated as fiduciary advisers and subject to the limitations of section 408(g)(2)(A)(i).⁽¹¹⁾

In general, a party seeking to avail itself of a statutory or administrative exemption from the prohibited transaction provisions bears the burden of establishing compliance with the conditions of the exemption. With regard to the exemptive relief accorded an “eligible investment advice arrangement” within the meaning of section 408(g)(2)(A)(i), it is the expectation of the Department that parties offering investment advisory services will maintain, and be able to demonstrate compliance with, policies and procedures designed to ensure that fees and compensation paid to fiduciary advisers, at both the entity and individual level, do not vary on the basis of any investment option selected. Moreover, it is anticipated that compliance with such policies and procedures will be reviewed as part of the annual audit required by section 408(g)(5)(A) and addressed in the report referred to in section 408(g)(5)(B).

Questions concerning the information contained in this Bulletin may be directed to the Division of Fiduciary Interpretations, Office of Regulations and Interpretations, 202.693.8510.

Footnotes

1. See also 29 CFR § 2510.3-21(c).
2. See Interpretative Bulletin relating to participant investment education, 29 CFR § 2509.96-1 (Interpretive Bulletin 96-1), AO 97-15A (May 22, 1997), AO 2001-09A (December 14, 2001), and AO 2005-10A (May 11, 2005).
3. Pub. L. 109-280, 120 Stat. 780 (Aug. 17, 2006).
4. Under Reorganization Plan No. 4 of 1978 (43 FR 47713, October 17, 1978), 5 U.S.C. App.1, 92 Stat. 3790, the authority of the Secretary of the Treasury to issue rulings under section 4975 of the Code has been transferred, with certain exceptions not here relevant, to the Secretary of Labor. Therefore, the references in this Bulletin to specific sections of ERISA should be taken as referring also to the corresponding sections of the Code.
5. ERISA section 408(g)(11)(A)(flush language), 408(g)(10)(A), 408(g)(6)(A)(vii).
6. See also August 3, 2006 Floor Statement of Senate Health, Education, Labor and Pensions Committee Chairman Enzi (who chaired the Conference Committee drafting legislation forming the basis of H.R. 4), regarding investment advice to participants in which he states, “It was the goal and objective of the Members of the Conference to keep this advisory opinion [AO 2001-09A, SunAmerica Advisory Opinion] intact as well as other pre-existing advisory opinions granted by the Department. This legislation does not alter the current or future status of the plans and their many participants operating under these advisory opinions. Rather, the legislation builds upon these advisory opinions and provides alternative means for providing investment advice which is protective of the interests of plan participants and IRA owners.” 152 Cong. Rec. S8, 752 (daily ed. Aug. 3, 2006) (statement of Sen. Enzi).
7. We note, however, that a fiduciary may have co-fiduciary liability under ERISA section 405(a) if, for example, it knowingly participates in a breach committed by another fiduciary.
8. Under section 408(g)(11)(B) the term affiliate of another entity means an affiliated person of the entity (as defined in section 2(a)(3) of the Investment Company Act of 1940 (15 U.S.C. 80a-2(a)(3))).
9. See AO 97-15A and AO 2005-10A.
10. No inferences should be drawn regarding the extent to which such an entity is responsible as principal for the acts of the individual fiduciary adviser providing the investment advice.
11. For purposes of section 408(g)(2)(A)(i), the Department interprets the requirement that fees received by a fiduciary adviser not vary on the basis of any investment option selected as meaning that the fees or other compensation (including salary, bonuses, awards, promotions or any other thing of value) received, directly or indirectly from an employer, affiliate or other party, by a fiduciary adviser (or used for the adviser’s benefit) may not be based, in whole or part, on the investment options selected by participants or beneficiaries.