

ERISA Section 404(c) Checklist

ERISA Section 404(c) applies to individual account plans, specifically: profit sharing plans; money purchase pension plans; and 401(k) plans. Although the 404(c) regulations are lengthy and formidable, they provide the basic overarching guidelines to assist employers in complying with the requirements so they can avail themselves of the 404(c) relief. Although plan participants will not be deemed fiduciaries by reason of their exercise of investment control, the plan fiduciaries will not be liable for losses on individual transactions when:

- The participants actually exercised control with respect to the transaction.
- The losses were directly and necessarily a result of investment instructions given by the participants.

The requirements can be met even if:

- Only certain participants may exercise control (assuming this is not discriminatory).
- Participants may exercise control over a portion of their account balance.

Moreover, Section 404(c) relief is available when alternate payees exercise control over assets allocated to them within a plan under a QDRO.

Requirements:

The opportunity of plan participants to exercise control requires that they may give investment instructions by any means but must have the opportunity to receive written confirmation. Those instructions must be given to an identified plan fiduciary is obligated to comply and may be identified by position or function. Moreover, the fiduciary must give certain information to the participants.

Information That Must Be Provided. The information must be generally sufficient to enable the participant to make informed investment decisions. Information that must be provided includes:

1. An explanation that the plan is intended to be a 404(c) plan.
2. An explanation that the fiduciaries may be relieved of liability.
3. A description of each investment alternative available under the plan, which can be general when the plan permits any investment, but should encourage participants to review information on the investment.
4. Each designated alternative must include a general description of the investment objectives and risk and return characteristics, and information regarding the type and diversification of assets in the portfolio of the designated alternative.
5. The identity of any designated investment manager.
6. An explanation of the circumstances under which participants may give investment instructions including limitations on such instructions; restrictions on transfer; limitations on voting rights; and information on penalties or adjustments related to fund transfers.
7. A description of transaction fees and expenses chargeable against the participant's account.
8. Information on indemnification of the plan fiduciary responsible for giving information on request.
9. Information regarding investments in employer securities including a description of the procedure to provide for confidentiality and identity of the fiduciary charged with monitoring compliance with the confidentiality requirement.
10. A copy of most recent prospectus provided to the plan if the investment is subject to the Securities Act of 1933 (this can be given immediately before or after investment).
11. After investment, participants must be provided with plan materials related to the exercise of voting, tender, or similar rights. If there are plan provisions regarding the exercise of such rights, participants must receive a description of or reference to such provisions. While the plan is not required to pass through such rights, Section 404(c) relief is not available to the extent that plan fiduciaries exercise the rights.

Information to Be Provided on Participant Request. Participant must be provided certain information on request. This material must be based on the latest information available to the plan, including:

1. A narrative of the annual operating expenses of each designated investment alternative, including investment manager fees, administrative fees, and transaction costs, which reduce the rate of return to the participant. The aggregate amount of such expenses must be expressed as a percentage of average net assets of the designated investment alternative. If the information is already in the prospectus, providing the prospectus is sufficient.
2. Copies of prospectuses, financial statements and reports, and other materials related to the investment alternatives to the extent the information is provided to the plan.
3. Regarding the designated investment alternatives: (a) a list of assets comprising the portfolio of the alternative that includes plan assets and the value of the assets, and (b) if the asset is a fixed rate investment contract, the name of the issuer of the contract, the term of the contract, and the rate of return on the contract.
4. The value of shares or units and past and current investment performance of each available alternative, net of expenses.
5. The value of the shares or units held in the particular participant's account.

Timing of Providing Information. The eleven items under "Information that must be provided" (above) must be provided before investment. Other information must be given in sufficient time for the participant to take the information into account prior to making an investment decision.

Carrying Out Investment Instructions. The plan may impose a reasonable charge for carrying out investment instructions so long as it has a procedure to inform participants periodically of the actual expenses incurred with respect to their accounts. The fiduciary may decline to follow instructions that would result in a prohibited transaction, or would generate income taxable to the plan (UBTI). The fiduciary is not relieved of liability when a participant instruction, if implemented, would:

1. Not be in accordance with the plan document.
2. Cause the indicia of ownership of plan assets to be outside the U.S.
3. Jeopardize the plan's tax qualified status.
4. Plausibly result in a loss in excess of a participant's account balance.
5. Result in a prohibited transaction.

Since the fiduciary is not relieved of fiduciary responsibility in the above events, it can decline to carry out investment instructions that would cause them.

Frequency of Giving Instructions. Participants must be given the opportunity to change their investments as often as the volatility of the investment requires ("general volatility rule"). They must be able to change core investment alternatives at least every three months, subject to the general volatility rule ("core" investments are those that constitute a broad range of investment alternatives).

If any investment alternative permits changes more frequently than once every three months, at least one core investment must permit the same frequency of change, and the investment into which participants can transfer must be income producing, low risk, and liquid. Non-core investments are not subject to the three month requirement but are subject to general volatility rule.

"Broad Range of Investment Alternative" Requirement. This requirement is met if investments are sufficient to permit participants a reasonable opportunity to materially affect the potential return and degree of risk on their investments. The participants must also have an opportunity to choose from at least three investments that:

- Are diversified.
- Have materially different risk and return characteristics.
- In the aggregate, enable the participant to achieve aggregate risk and return characteristics at any point within the range "normally appropriate for the participant."
- Each of which, when combined with the other alternatives, tends to minimize, through diversification, the overall risk of the portfolio.

Finally, participants must be given the opportunity to diversify the investments to minimize the risk of large losses, taking into account the nature of the plan and the size of participant accounts.