

BCG Newsletter January 2008

New Rules Concerning Qualified Default Investment Alternatives

The Pension Protection Act of 2006 (PPA) created the Qualified Default Investment Alternative (QDIA) to promote the offering of automatic enrollment 401(k) plans and to provide protection for plan fiduciaries where participants fail to direct the investment of their accounts. The QDIA provides employers a safe harbor from fiduciary risk when selecting an investment for a participant or beneficiary who fails to elect his or her own investment. Employers following the QDIA regulations will have no legal liability for market fluctuations when providing a QDIA for employees who do not choose their own investments. New regulations setting forth the rules for QDIA's are effective December 24, 2007.

Qualified Default Investment Alternatives

The PPA goal for the QDIA is that it meet a worker's long-term retirement savings needs, rather than just preserving capital. The final regulations provide four QDIA investment alternative mechanisms, rather than specific products. An example of a product for each category is provided.

- *Life Cycle or Target Date Fund.* A product with a mix of investments that takes into account the individual's age, retirement date, or life expectancy.
- *Balanced Fund.* A product with a mix of investments that takes into account the characteristics of the group of employees as a whole, rather than each individual.
- *Managed Account.* An investment service that allocates contributions among existing plan options to provide an asset mix that takes into account the individual's age or retirement date.
- *Capital Preservation Fund.* A capital preservation product for only the first 120 days of participation. After 120 days, the plan fiduciary must redirect the participant's investment into the above three QDIA categories (unless the participant opted-out of the plan or redirected investments during the 90 days).

Existing Stable Value Funds Grandfathered

Prior to PPA some plan sponsors adopted stable value products as their default investment. The final regulations "grandfather" these arrangements by providing relief for contributions invested in stable value products prior to the effective date of the final rule. The transition rule does not provide relief for future contributions to stable value products.

ERISA Supersedes State Law

The rule provides that ERISA supersedes any State law that would prohibit or restrict automatic contribution arrangements, regardless of whether such automatic contribution arrangements qualify for the safe harbor.

Additional QDIA Requirements

- With limited exception, a QDIA may not be invested in employer securities;
- A plan may not restrict the participant or beneficiary from transferring the funds in a QDIA to any other investment alternative available under the plan; the transfer must be permitted with the same frequency that applies to other plan investments, but not less than on a quarterly basis and may not impose any restrictions, fees or expenses inconsistent with these regulations;
- A QDIA must be a mutual fund, or managed by an investment manager as defined in ERISA, or a named fiduciary, such as the plan's trustee or sponsor, responsible for the management of the plan's investments.

Conditions for Fiduciary Liability Relief

- Assets must be invested in one of the QDIA investment categories above.
- The participant or beneficiary must first be given the opportunity to provide investment direction. If the participant or beneficiary fails to make an investment election, the QDIA may be used. If they respond after the QDIA is established, then the investment direction from the participant or beneficiary will supersede the QDIA.
- A notice must generally be provided at least 30 days in advance of the first investment in a QDIA and 30 days in advance of each subsequent plan year.
- Material provided to the plan for the QDIA investments must be furnished to participants and beneficiaries invested in the QDIA. For example, prospectuses, account statements, and proxy-voting materials. The rules for pass-through disclosure information provided to participants not invested in a QDIA will also apply to those invested in a QDIA. The information may be mailed directly from the provider to the participant or beneficiary.
- Participants and beneficiaries must have the opportunity to direct investments out of a QDIA at least as frequently as from other plan investments, but at least quarterly. During the first 90 days after the first automatic enrollment deferral is withheld, QDIA withdrawal requests will not be subjected to a surrender charge, liquidation or exchange fee, redemption fee, or similar expenses. However, on-going fees for the operation of the investment may be charged. After the 90-day period, the restrictions, fees and expenses of the plan will apply to a QDIA.
- The plan must offer a "broad range of investment alternatives" as defined in the regulations under section 404(c) of ERISA.

Fiduciary Prudence Requirement

The plan fiduciary must prudently select and monitor an investment fund, model portfolio, or investment management service within any category of QDIAs. For example, a plan fiduciary that chooses an investment management service must undertake a careful evaluation to prudently select among different investment services.

A more detailed explanation of these rules and how to take advantage of them will be sent to you soon.

2008 IRS LIMITS AFFECTING RETIREMENT PLANS

The following limits affecting retirement plans are in effect for 2008:

Defined Contribution Plan Limit on Annual Additions	\$46,000
Defined Benefit Plan Limit on Annual Benefits	\$185,000
Maximum Compensation for Allocation and Accrual Purposes	\$230,000
401(k), SARSEP, 403(b), and 457 Plan Deferrals/Catch-up	\$15,500/\$5,000
SIMPLE Deferrals/Catch-up	\$10,500/\$2,500
IRA Contributions/Catch-up	\$5,000/\$1,000
Compensation Defining Highly Compensated Employee (2008 amount for use in 2009 plan year tests)	\$105,000
Compensation Defining Key Employee/Officer	\$150,000
Social Security Taxable Wage Base (SSTWB)	\$102,000