NAGDCA NOTES

A Brief Look: Investment Advice Within Your Defined Contribution Plan

Plan sponsors now have the ability to provide participants in their defined contribution plans an advisory service which will assist participants in the selection of investments within the plan. In addition, these services can provide Managed Accounts which will create diversified investment portfolios and rebalance them over the course of the participant's life. Furthermore, the uncertainty of liability on the part of plans sponsors for the advice of this service appears to have been settled in a manner that should put plan sponsors' fears to rest. Plan sponsors will not be liable for the advice to participants from properly selected service providers. Plan sponsors will need to prudently select or monitor the advice service providers in the same manner as is required when they select investment options for their plans.

This new lease on offering investment advice came in a key provision of the Pension Protection Act of 2006 (PPA). Even though the PPA relates to ERISA provisions, for many years public pension plans have used ERISA rulings and regulations as a model to oversee their governmental plans. With the passing of the PPA, investment providers now have alternatives to provide advice to participants; (1) they can use an independent financial expert ("fiduciary adviser") who will provide the methodology i.e. the DOL Advisory Opinion or (2) they can develop their own service or in house computer model but will need to comply with the disclosure and audit provisions of PPA. Plan sponsors can select the investment advisory service which is best for their plan participants with less confusion whether it complies with the PPA or the DOL advisory Opinion.

"Who exactly qualifies as a **fiduciary adviser** you might ask? The advisor must be named as a plan fiduciary providing investment advice to a participant or beneficiary, and must also be one of the following:

- registered as an investment adviser under the Investment Advisers Act of 1940 or under laws of the state in which the fiduciary maintains its principal office and place of business
- a bank, a similar financial institution supervised by the United States or a state, or a savings association, but only if the advice is provided through a trust department subject to periodic examination and review by federal or state banking authorities
- an insurance company qualified to do business under state law
- registered as a broker or dealer under the Securities Exchange Act of 1934
- an affiliate under the Investment Company Act of 1943, of any of the preceding
- an employee, agent or registered representative of any of the preceding who satisfies the requirements of applicable insurance, banking and securities laws relating to the provision of advice

To qualify as an eligible investment adviser arrangement, it must use a **qualified computer model** under an investment advice program that:

- applies generally accepted investment theories which take into account the historic returns of different asset classes over defined periods of time
- uses relevant information about the participant, which may include age, life

(859) 514-9161 • Fax: (859) 514-9166 • www.nagdca.org

National Association of Government
Defined Contribution Administrators Inc.

expectancy, retirement age, risk tolerance, other assets or sources of income, and preferences as to certain types of investments
- uses prescribed objective criteria to provide asset allocation portfolios comprised of investment options available under the plan
- operates in a manner not biased in favor of investments offered by the fiduciary adviser or a person with a material affiliation or contractual relationship with the fiduciary adviser or a person with a material affiliation or contractual relationship with the fiduciary adviser
- takes into account all investment options under the plan in specifying how a participant's account balance should be invested, and not be inappropriately weighted with respect to any investment option"
- is certified under the rules created by the Department of Labor

However, even with the passing of these new provisions which provide specific safeguards, it is extremely important that plan administrators practice due diligence in evaluating fiduciary advisers who are offering investment advice to their participants.

Neither NAGDCA, nor its employees or agents, nor members of its Executive Board, provide tax, financial, accounting or legal advice. This memorandum should not be construed as tax, financial, accounting or legal advice; it is provided solely for informational purposes. NAGDCA members, both government and industry, are urged to consult with their own attorneys and/or tax advisors about the issues addressed herein.

Ashton, Bruce; The New Participant Investment Advice Law:
www.reish.com/publications/article_detail.cfm?ARTICLEID=603

Gordon, Catherine; New Pension Law Expands Investment Advice Options:
www.completetax.com/taxguide/news/06-100planadvice.asp

Investment Advice to Defined Contribution Plan Participants – Update on Impact of Department of Labor Advisory Opinion 2001-09A and the Pension Protection Act of 2006:
http://www.nagdca.org/users/epubs/brochures/investmentAdvice.cfm