TREASURY | PARTNERS

401(k) Reenrollment

Seeking To Reduce Participant/Company Risk and Plan Costs

Although most defined contribution plans feature a range of prudent investment offerings, some participants make uninformed decisions, which can potentially lead to reduced returns or expose the portfolio to unnecessary risk. Common examples include concentrated investments or overly conservative or aggressive asset allocations.

In response to these types of situations, increasing numbers of plan sponsors are implementing a reenrollment strategy through which participants' current holdings are transferred into a qualified default investment alternative (QDIA). In many cases these QDIAs include age appropriate target date funds.

Along with addressing portfolio construction errors, this strategy may also limit the sponsor's fiduciary liability, because defaulting participants' assets into a QDIA affords plan sponsors relief from responsibility for investment losses. (Sponsors do, however, retain fiduciary responsibility for the selection and monitoring of investment options offered under the plan).

The key to achieving the fiduciary protection provided by QDIA regulations is that participants must be and are given the opportunity to direct the investment of assets in their accounts but, for whatever reasons, fail to take advantage of the opportunity.

Under the QDIA provision, participants who neglect to make an investment election are deemed to have exercised control over their investments—and plan fiduciaries will have ERISA Section 404(c) protection—if the following requirements are satisfied:

- Participants' assets are invested in a QDIA.
- Participants had the opportunity to direct the investment of the assets in their accounts, but did not do so.
- Participants receive a notice explaining their right to designate how contributions and earnings will be invested and explaining how, in the absence of any investment election, such contributions will be invested.
- This notice must be provided to plan participants at least 30 days before their initial enrollment in the QDIA, and then annually at least 30 days before the beginning of each plan year.
- Any documentation provided to the plan relating to participants' investments (e.g., account statements, prospectuses, proxy voting material) must also be provided to the participants.
- Participants are able to transfer assets out of the QDIA into any other investment alternative available under the plan, including their original asset allocation, without financial penalty.
- The alternatives must comprise a broad range of strategies, each of which must generally adhere to accepted investment theories, be diversified to minimize risk, and designed to provide long-term appreciation and capital preservation.

When properly designed and implemented, a QDIA can represent a valuable "reset button" in instances where a plan may no longer be consistent with the Investment Policy, or there has been a turnover among the members of the investment committee.

Another important advantage of instituting a reenrollment strategy is the potential for lowering overall plan costs and fiduciary risk.

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