DOL FINAL RULE ON ADVICE UNDER THE PENSION PROTECTION ACT INCORPORATES PSCA COMMENTS

On October 25, 2011, the Department of Labor issued its final rule under a controversial provision in the Pension Protection Act of 2006 that creates a prohibited transaction exemption under ERISA whereby a plan investment manager affiliated with an advice provider may receive investment management fees as long as the adviser's compensation does not vary as a result of the advice to a participant or beneficiary (and several other requirements are met). The final rule generally follows a proposed rule published on March 2, 2010. An earlier final rule issued by the Bush administration on January 21, 2009, was subsequently withdrawn by the new administration.

The final rule is effective on December 27, 2011.

Perspective

PSCA does not expect widespread provision of advice under the rule, due to a lack of enthusiasm by both plan sponsors and advice providers. The final rule reiterates that it does not affect investment advice provided under other arrangements, such as the popular "SunAmerica model" in which an investment manager may provide advice based on an independent computer model. These other approaches are viewed as involving less fiduciary risk than monitoring and selecting an advice provider that is affiliated with plan investment managers. Advice providers have been unhappy with the original legislation and the DOL's position and cumbersome rules on both the fee-leveling and computer models. The retirement community has pretty much moved beyond this particular method of providing advice, which was first entertained several years ago. In PSCA's latest survey of 2010 plan experience, 57.6% of DC plans are offering investment advice.

PSCA's comments, filed jointly with the ERISA Industry Committee and the U.S. Chamber of Commerce, focused on collateral issues raised in the proposed rule. The DOL queried if it should determine what constitutes generally accepted investment theories under the computer model. The proposed rule also contained language under the computer rule viewed as banning the consideration of historical performance of individual plan investments. PSCA urged the DOL to reverse its position on these issues, and we are pleased to report that our efforts were successful.

Here are some highlights of the final rule:

- ***Investment theories*** – The DOL has determined that it does not have sufficient basis to determine generally accepted investment theories under the computer model. This is a great relief, in part because, despite language that any such determination would be restricted to the computer model, it is hard to understand how such a position would not affect the DOL's eventual position no other methods of providing advice.

- ***Historical performance*** – Under the proposed rule, the computer model had to avoid recommendations that "inappropriately distinguish among investment options on the basis of a factor that cannot confidently be expected to persist in the future." This provision was widely viewed to ban the consideration of historical performance in offering advice. The DOL denies that this was their intent. The final rule does not contain this language, but it does require that the computer model "appropriately weight the factors used in estimating future returns of investment options." This change provides relief to those who, like the treatment of investment theories, feel that the DOL's position will eventually spill over to other forms of advice.

- ***Fee-leveling*** – The proposed rule states that a fiduciary adviser cannot receive any fee that is "based in whole or in part on a participant's or beneficiary's selection of an investment option." The final rule replaces "based in whole or in part" with "that varies on the basis of" (the selection of a particular investment option). This change comports with statutory language, but its impact is undetermined. In the preamble, the DOL states that a bonus arrangement based on overall profitability of an organization, including an affiliated investment manager, may be permissible if advice and investment option components are excluded or are a negligible portion of the organization's profitability. The DOL noted that the auditor required under the rule would review and report on this issue as a condition of the exemption. This latter provision might not be embraced by advice providers.

- ***Employer stock and target date funds*** – The proposed rule permitted the computer model to not make a recommendation regarding an in-plan annuity, employer securities, and "asset allocation funds." The final rule retains the exemption only for in-plan annuities. The DOL explained that the change is based on reconsideration of their prior position that it is not feasible to develop a computer model capable of considering these investments. While limited to the computer model, the treatment of employer securities and asset allocation funds in other forms of advice might be reviewed by plan sponsors and advice providers because of this change.