Helping you manage your fiduciary responsibility and liability for your workplace retirement savings plan

Section 404(c) compliance means protection for plan fiduciaries.

Tax-qualified workplace retirement savings plans often permit participants to direct investments. Does this mean that the plan fiduciaries are not responsible for participant decisions? Not always. Sometimes participants have full control of investment decisions but the plan fiduciaries could still be “legally” responsible for the participants’ choices. Fortunately, plan fiduciaries do have an option that offers protection.

An effective method of managing risk associated with plan fiduciary responsibilities rests in Section 404(c) of the Employee Retirement Income Security Act of 1974, as amended (ERISA). This provision generally allows fiduciaries to be relieved of liability for participants’ investment decisions. The specific requirements to obtain Section 404(c) protection are set forth in a comprehensive final regulation issued in 1992 and amended in 2010 as part of the Department of Labor’s (DoL) efforts to improve disclosure to plan participants.

Briefly, the requirements:

- Offer a broad range of investments, including at least three options each of which is diversified and has materially different risk and return characteristics that in the aggregate enable the participant or beneficiary, by choosing among them, to achieve a portfolio with aggregate risk and return characteristics at any point within the range normally appropriate for the participant or beneficiary. Each of these when combined with investments in other alternatives tends to minimize through diversification the overall risk of a participant’s or beneficiary’s portfolio.

- Provide participants with the ability to transfer among investment options with a frequency appropriate for each investment’s market volatility, and the ability to transfer among three investment options, described above, at least once in any three-month period.

- Deliver to participants information about the plan, its investment
options, and its operations before participants make investment decisions.

- Provide additional information about each investment option to participants upon request, so they can make informed investment decisions.

**Key elements of Section 404(c) compliance: Section 404a-5 participant disclosure**

In addition to requirements regarding the range of investment options and participants’ control of their investments, complying with Section 404(c) regulation means that plans must disclose certain information to plan participants about the plan’s investment options. Some information must be provided automatically before participants exercise control and make investment elections, and other information must be provided upon request. All the information provided, whether automatically or upon request, is intended to provide plan participants with sufficient information to make investment decisions. However, the required information is virtually identical to the information that must be disclosed to all participants, including eligible participants not enrolled in the plan, under the DoL’s mandatory Section 404a-5 participant disclosure regulation. When a plan complies with the Section 404a-5 regulation, unless the plan offers employer securities (see page 5), the only additional disclosure is that the plan intends to comply with ERISA Section 404(c) and that plan fiduciaries may be relieved of liability for any losses resulting from a participant’s investment decisions.

It is important to make sure you are disclosing to your participants plan information and related fees as required by Section 404a-5. The disclosures under 404a-5 and 404(c) may be provided in print or electronically in accordance with DoL rules regarding electronic delivery. Fidelity’s communications, education, and business compliance professionals can assist plan sponsors with developing effective means of meeting these requirements.

This brochure takes a closer look at the requirements for Section 404(c) plan compliance and the benefits of Section 404(c) protection for plan fiduciaries.
Questions and answers to help understand the interplay between the Section 404a-5 and Section 404(c) regulations.

Q: What disclosures are required for 404(c) protection but are not required to be disclosed under the 404a-5 participant disclosure regulation?

A: Plans need to disclose to participants that the plan intends to comply with ERISA Section 404(c) and that plan fiduciaries may be relieved of liability for any losses resulting from a participant’s investment decisions. This disclosure is not required by the 404a-5 participant disclosure regulation. To the extent a plan offers company stock as an investment option, there are additional disclosures that must be made under the Section 404(c) regulation that are not required under the 404a-5 participant disclosure regulation (see Section 404(c) protection for employer stock investment options on page 5).

Q: Is 404(c) now mandatory?

A: No. Compliance with Section 404(c) is still optional. A plan must comply with the Section 404a-5 participant disclosure regulation but does not have to comply with the Section 404(c) regulation.

Q: If the plan complies with the 404a-5 participant disclosure regulation, but does not provide the additional disclosures that are only required by the Section 404(c) regulation, is there a breach of fiduciary duty?

A: Failure to comply with the mandatory 404a-5 participant disclosure regulation is potentially a breach of fiduciary duty. However, as adherence to Section 404(c) regulation is optional, the consequence of not meeting all its requirements is that plan fiduciaries may not enjoy the protection afforded by Section 404(c).

Q: Is a prospectus still required to be provided upon an initial investment into a mutual fund in order to obtain 404(c) protection?

A: No. The “confirming prospectus” requirement was removed from the Section 404(c) regulation and was not made a requirement of the Section 404a-5 participant disclosure regulation. However, the Section 404a-5 participant disclosure regulation does require a prospectus (and similar documents provided by nonregistered options) to be provided upon participant request.

Q: Are investment descriptions, including objective and risk, still required to be proactively provided to participants for each designated investment option in order to obtain 404(c) protection?

A: No. The “fund description” requirement was removed from the Section 404(c) regulation and was not made a requirement of the Section 404a-5 participant disclosure regulation. However, the Section 404a-5 participant disclosure regulation does require “fund descriptions” to be made available on a Web site. In addition, this information would need to be provided in paper upon participant request.
The advantages of Section 404(c) compliance become more apparent in a volatile market. The increased risk of participants initiating lawsuits to address declines in their retirement savings plan accounts makes fiduciaries more aware of the need for the protection that Section 404(c) offers. Employers and fiduciaries may become more focused on, and committed to meeting, the ERISA requirements for Section 404(c) protection for their plans in today’s market environment.

Once a plan has been established as a Section 404(c) plan, an ongoing effort is required to maintain the protections afforded under Section 404(c).

Fidelity has dedicated teams of professionals who work with clients to help them achieve Section 404(c) compliance. In its role as provider of recordkeeping and administrative services, Fidelity can help plans comply with 404(c) by providing many of the required disclosures via our Participant Disclosure Service.

There is no guarantee that plan fiduciaries can avoid liability altogether for losses, even if the plan is Section 404(c) compliant, because certain fiduciary responsibilities cannot be passed along to participants. For example, the plan sponsor is still responsible for selecting and monitoring the investment options offered through a plan. However, compliance with ERISA Section 404(c) remains among the best methods for plan sponsors and fiduciaries to manage and minimize risk.

In today’s environment, Section 404(c) compliance and protections make sense
Section 404(c) protection for employer stock investment options

When employer stock is offered, there are additional requirements that need to be met in order for fiduciaries to obtain 404(c) protection for participant investment decisions related to the employer stock investment.

- Employer securities must be publicly traded on a generally recognized exchange with sufficient frequency and volume to enable prompt trades.
- Participants must be provided with the same information as other shareholders.
- Voting, tender, and other rights must be passed through to participants.
- Confidentiality of the purchase, holding, or sale of employer securities, as well as the exercise of voting, tender, or other shareholder rights, must be maintained.

- A description of the procedures for maintaining confidentiality must be provided, and a plan fiduciary must be designated to monitor compliance with the procedures.
- An independent fiduciary must be appointed in situations where there is the potential for undue employer influence on participants, such as a tender offer.

Keep in mind that these are not requirements of the Section 404a-5 participant disclosure regulation.

In today's environment, achieving Section 404(c) compliance for employer stock investment options can provide a measure of protection for plan sponsors and fiduciaries.

Are you ready for the protections available under ERISA Section 404(c)?

ERISA Section 404(c) may offer plan fiduciaries a measure of protection against litigation related to qualified workplace retirement savings plans. Fidelity is ready to help plan sponsors work to make their retirement plans Section 404(c) compliant.

As you work with Fidelity to manage the responsibilities and risk associated with sponsoring a qualified workplace retirement savings plan, you will understand the value of Section 404(c) protection and the steps necessary to comply.

Contact your Fidelity representative to discuss any questions you may have.
This article does not address protection under the special rules added to ERISA Section 404(c) by the Pension Protection Act of 2006 (PPA). The PPA added ERISA Section 404(c)(4), containing rules for fiduciary protection for mapping of assets, and ERISA 404(c)(5), containing rules for fiduciary protection for qualified default investment alternatives.

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