DEPARTMENT OF LABOR

Employee Benefits Security Administration

29 CFR Part 2550

RIN 1210–AA92

Fiduciary Responsibility Under the Employee Retirement Income Security Act of 1974 Automatic Rollover Safe Harbor

AGENCY: Employee Benefits Security Administration, Labor.

ACTION: Proposed regulation.

SUMMARY: This document contains a proposed regulation that, upon adoption, would establish a safe harbor pursuant to which a fiduciary of a pension plan subject to Title I of the Employee Retirement Income Security Act of 1974, as amended (ERISA), will be deemed to have satisfied his or her fiduciary responsibilities in connection with automatic rollovers of certain mandatory distributions to individual retirement plans. This proposed regulation, if finalized, would affect employee pension benefit plans, plan sponsors, administrators and fiduciaries, and plan participants and beneficiaries.

DATES: Written comments on the proposed regulation should be received by the Department of Labor on or before April 1, 2004.

ADDRESSES: Comments (preferably at least three copies) should be addressed to the Office of Regulations and Interpretations, Employee Benefits Security Administration, Room N–5669, U.S. Department of Labor, 200 Constitution Avenue NW., Washington, DC 20210. Attn: Automatic Rollover Regulation. Comments also may be submitted electronically to *e-ori@dol.gov*. All comments received will be available for public inspection at the Public Disclosure Room, N–1513, Employee Benefits Security Administration, 200 Constitution Avenue NW., Washington, DC 20210.

FOR FURTHER INFORMATION CONTACT: Lisa M. Alexander or Kristen L. Zarenko, Office of Regulations and Interpretations, Employee Benefits Security Administration, (202) 693–8510. This is not a toll-free number.

SUPPLEMENTARY INFORMATION:

A. Background

Under the Internal Revenue Code of 1986, as amended (Code), tax-qualified retirement plans are permitted to incorporate provisions requiring an immediate distribution to a separating participant without the participant's consent if the present value of the participant's vested accrued benefit does not exceed $5,000.[1] A distribution by a plan in compliance with such a provision is termed a mandatory distribution, commonly referred to as a ''cash-out''. Separating participants may choose to roll the cash-out, which is an eligible rollover distribution,[2] into an eligible retirement plan,[3] or they may retain the cash-out as a taxable distribution. Within a reasonable period of time prior to making a mandatory distribution, plan administrators are required to provide a separating participant with a written notice explaining, among other things, the following: the Code provisions under which the participant may elect to have the cash-out transferred directly to an eligible retirement plan and that if an election is not made, such cash-out is subject to the automatic rollover provisions of Code section 401(a)(31)(B); the provision requiring income tax withholding if the cash-out is not directly transferred to an eligible retirement plan; and the provisions under which the distribution will not be taxed if the participant transfers the account balance to an eligible retirement plan within 60 days of receipt.[4]

As part of the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA),[5] section 401(a)(31) of the Code was amended to require that, absent an affirmative election by the participant, certain mandatory distributions from a tax-qualified retirement plan be directly transferred to an individual retirement plan[6] of a designated trustee or issuer. Specifically, section 657(a) of EGTRRA added a new section 401(a)(31)(B)(i) to the Code to provide that, in the case of a trust that is part of an eligible plan,[7] the trust will not constitute a qualified trust unless the plan of which the trust is a part provides that if a mandatory distribution of more than $1,000 is to be made and the participant does not elect to have such distribution paid directly to an eligible retirement plan or to receive the distribution directly, the plan administrator must transfer such distribution to an individual retirement plan. Section 657(a) of EGTRRA also added a notice requirement in section 401(a)(31)(B)(i) of the Code requiring the plan administrator to notify the participant in writing, either separately or as part of the notice required under section 402(f) of the Code, that the participant may transfer the distribution to another individual retirement plan.[8]

Section 657(c)(2)(A) of EGTRRA directed the Department of Labor (Department) to issue regulations providing safe harbors under which 1) a plan administrator's designation of an institution to receive the automatic rollover and 2) the initial investment choice for the rolled-over funds would be deemed to satisfy the fiduciary responsibility provisions of section 404(a) of ERISA. Section 657(c)(2)(B) of EGTRRA states that the Secretaries of Labor and Treasury may provide, and shall give consideration to providing, special relief with respect to the use of low-cost individual retirement plans for purposes of Code section 401(a)(31)(B) automatic rollovers and for other uses that promote the preservation of assets for retirement income.

Section 657(c)(2)(A) of EGTRRA further provides that the Code provisions requiring automatic rollovers of certain mandatory distributions to individual retirement plans will not become effective until the Department of Labor issues safe harbor regulations.

On January 7, 2003, the Department published a notice in the **Federal Register** requesting information on a variety of issues relating to the development of a safe harbor pursuant to section 657(c)(2)(A) and (B) of EGTRRA.[9] In response to this request for information (RFI), the Department received 17 comment letters. Copies of these comments are posted on the Department's Web site at *http://*

[1] Code sections 411(a)(11) and 417(e). *See* Code section 411(a)(11)(D) for circumstances where the amount of a cash-out may be greater than $5,000, based on a participant's prior rollover contribution into the plan.

[2] *See* Code section 402(f)(2)(A).

[3] *See* Code section 402(f)(2)(B).

[4] Code section 402(f)(1).

[5] Pub. L. 107–16, June 7, 2001, 115 Stat. 38.

[6] Section 401(a)(31)(B)(i) of the Code requires the transfer to be made to an ''individual retirement plan'', which section 7701(a)(37) of the Code defines to mean an individual retirement account described in section 408(a) and an individual retirement annuity described in section 408(b).

[7] Section 657(a)(1)(B)(ii) of EGTRRA defines an ''eligible plan'' as a plan which provides for an immediate distribution to a participant of any ''nonforfeitable accrued benefit for which the present value (as determined under section 411(a)(11) of the Code) does not exceed $5,000.'' The Treasury and the IRS have advised the Department that the requirements of Code section 401(a)(31)(B) apply to a broad range of retirement plans including plans established under Code sections 401(a), 401(k), 403(a), 403(b) and 457. The Department notes that the safe harbor proposed herein applies only to employee benefit pension plans covered under title I of ERISA. *See infra* fn. 15.

[8] Conforming amendments to Code sections 401(a)(31) and 402(f)(1) were also made by section 657 of EGTRRA.

[9] 68 FR 991. *http://www.dol.gov/ebsa/regs/fedreg/proposed/2003000281.htm.*

www.dol.gov/ebsa/regs/cmt_rolloverRFI.html.

Set forth below is an overview of the proposed safe harbor regulation and a review of the comments received in response to the RFI.

B. Overview of Proposal

1. Scope

Consistent with the directive in section 657(c)(2)(A) of EGTRRA, paragraph (a)(1) of § 2550.404a–2 provides that the proposed safe harbor applies only to the automatic rollover of a mandatory distribution described in section 401(a)(31)(B) of the Code. At present, such distributions are limited to nonforfeitable accrued benefits (generally referred to as vested benefits), the present value of which is in excess of $1,000, but less than or equal to $5,000. For purposes of determining the present value of such benefits, section 401(a)(31)(B) references Code section 411(a)(11). Section 411(a)(11)(A) of the Code provides that, in general, if the present value of any nonforfeitable accrued benefit exceeds $5,000, such benefit may not be immediately distributed without the consent of the participant. Section 411(a)(11)(D) of the Code also provides a special rule that permits plans to disregard that portion of a nonforfeitable accrued benefit that is attributable to amounts rolled over from other plans (and earnings thereon) in determining the $5,000 limit. Inasmuch as section 401(a)(31)(B) of the Code requires the automatic rollover of mandatory distributions, as determined under section 411(a)(11), which would include prior rollover contributions, the proposal provides safe harbor coverage for the automatic rollover of mandatory distributions containing such prior rollover contributions. One commenter on the RFI suggested that the safe harbor should extend to amounts of $1,000 or less. While the Department agrees with the commenter that similar considerations may be relevant to such rollovers, the Department did not adopt this suggestion in light of Congress's direction to provide a safe harbor for automatic rollovers of mandatory distributions described in section 401(a)(31)(B) of the Code.

Paragraph (b) of the proposed regulation provides that, if the conditions of the safe harbor are satisfied, fiduciaries will be deemed to have satisfied their fiduciary duties under section 404(a) of ERISA with respect to both the selection of an individual retirement plan provider and the investment of funds in connection with an automatic rollover of a mandatory distribution described in section 401(a)(31)(B) of the Code to an individual retirement plan, within the meaning of section 7701(a)(37) of the Code.

The proposal makes clear that the standards set forth in the proposed regulation apply solely for purposes of determining compliance with the safe harbor and that such standards are not intended to represent the exclusive means by which a fiduciary might satisfy his or her duties under ERISA with respect to automatic rollovers of mandatory distributions described in section 401(a)(31)(B) of the Code.

As noted above, section 657(c)(2)(B) of EGTRRA provides that the Secretary of the Treasury and the Secretary of Labor shall consider and may provide special relief with respect to the use of low-cost individual retirement plans. The Department considered the provision of such special relief and believes that the framework of the safe harbor encourages the use of low-cost individual retirement plans for purposes of rollovers under section 401(a)(31)(B) of the Code. The Department specifically invites public comment on whether, given the conditions of the proposal, further relief is necessary in this regard. If so, commenters are encouraged to specifically address what relief is necessary and why, as well as identify approaches to providing such relief.

2. Conditions

Safe harbor relief under the proposed regulation is dependent on a fiduciary satisfying six conditions. In general, the conditions address: (1) The amount of mandatory distributions; (2) qualifications for an individual retirement plan; (3) permissible investment products; (4) permissible fees and expenses; (5) required disclosures to participants and beneficiaries; and 6) prohibited transactions. Each of the conditions is discussed below.

The first condition, described in paragraph (c)(1) of the proposed regulation, provides that, for the automatic rollover of mandatory distributions, the present value of the nonforfeitable accrued benefit, as determined under section 411(a)(11) of the Code, does not exceed the maximum amount permitted under section 401(a)(31)(B) of the Code. This condition was discussed in ''Scope'', above.

The second condition, described in paragraph (c)(2) of the proposed regulation, provides that the mandatory distribution be directed to an individual retirement plan within the meaning of section 7701(a)(37) of the Code. Section 7701(a)(37) defines the term individual retirement plan to mean an individual retirement account described in section 408(a) of the Code and an individual retirement annuity described in section 408(b) of the Code. Accordingly, a bank, insurance company, financial institution or other provider of an individual retirement plan under the safe harbor is required to satisfy the requirements of the Code and regulations issued thereunder.[10] This approach is consistent with the majority of comments received in response to the RFI. These commenters argued that additional criteria are unnecessary and, if imposed, may only serve to limit the number of providers available or willing to establish and maintain the small rollover accounts covered by the safe harbor. Other commenters suggested that the fiduciaries should be required to consider an individual retirement plan provider's financial stability, taking into account such matters as credit ratings or insurance coverage. The Department is unaware of any problems attributable to weaknesses in the existing Code and regulatory standards for individual retirement plan providers. The Department, therefore, believes that, given the limited scope of the proposed safe harbor, existing Code and regulatory standards are sufficiently protective of separating participants and their beneficiaries who would become individual retirement plan account holders, without imposing unnecessary burdens on either plans or individual retirement plan providers.

The third condition, described in paragraph (c)(3) of the proposed regulation, defines the type of investment products in which a mandatory distribution can be invested under the safe harbor. Specifically, the proposal provides for the investment of mandatory distributions in investment products designed to preserve principal and provide a reasonable rate of return, whether or not such return is guaranteed, consistent with liquidity, and taking into account the extent to which charges can be assessed against an individual retirement plan. For this purpose, the product must be offered by

[10] For example, with respect to individual retirement accounts, 26 CFR 1.408–2(b)(2)(i) provides that the trustee of an individual retirement account must be a bank (as defined in section 408(n) of the Code and regulations thereunder) or another person who demonstrates, in the manner described in paragraph (e) of the regulation, to the satisfaction of the Internal Revenue Service, that the manner in which the trust will be administered will be consistent with section 408 of the Code and regulations thereunder. With respect to individual retirement annuities, 26 CFR 1.408–3 describes, among other things, requirements that must be met in order to maintain the tax-qualified status of such annuity arrangements.

a state or federally regulated financial institution, and must seek to maintain a stable dollar value equal to the amount invested in the product by the individual retirement plan.

For purposes of this condition, a ''regulated financial institution'' is defined in the proposal as a bank or savings association, the deposits of which are insured by the Federal Deposit Insurance Corporation; a credit union, the member accounts of which are insured within the meaning of section 101(7) of the Federal Credit Union Act; an insurance company, the products of which are protected by state guarantee associations; or an investment company registered under the Investment Company Act of 1940.

This condition reflects the Department's view that, given the nature and amount of the automatic rollovers, investments under the safe harbor should be designed to minimize risk, preserve assets for retirement and maintain liquidity. Such safe harbor investment products would typically include money market funds maintained by registered investment companies,[11] and interest-bearing savings accounts and certificates of deposit of a bank or a similar financial institution. In addition, safe harbor investment products would include ''stable value products'' issued by a regulated financial institution that are fully benefit-responsive to the individual retirement plan account holder. Such products must provide a liquidity guarantee by a financially responsible third party of principal and previously accrued interest for liquidations or transfers initiated by the individual retirement plan account holder exercising his or her right to withdraw or transfer funds under the terms of an arrangement that does not include substantial restrictions to the account holder's access to the assets of the individual retirement plan.

The majority of the commenters on the RFI supported inclusion in the safe harbor of an investment product that favored retention of principal and income over growth. A number of commenters suggested that, in addition to such products, the safe harbor should include investment products identical or similar to those in which the participant had directed his or her investments prior to the mandatory distribution. Some argued that retaining such investments outside the plan might, in fact, result in some cost savings (*e.g.*, lower administrative expenses, avoiding termination charges, etc.). Some commenters also argued for inclusion of participant investments in qualifying employer securities as a safe harbor investment option. The Department does not believe that an investment strategy adopted by a participant while in a defined contribution plan or chosen by a plan fiduciary at a particular point in time would necessarily continue to be appropriate for the participant in the context of an automatic rollover, particularly given the relatively small account balances covered by the safe harbor. For this reason, the Department did not adopt these suggestions.

The fourth condition addresses the extent to which fees and expenses can be assessed against an individual retirement plan, including the investments of such plan. Most of the commenters on the RFI argued that the safe harbor should permit fees and expenses attendant to the establishment and maintenance of an individual retirement plan to be charged against the assets in the individual retirement plan and the safe harbor should not impose limits on such fees and expenses, noting that competition in the marketplace will serve to control costs. These commenters also noted that the costs attendant to maintaining individual retirement plans to handle mandatory distributions will be higher than for other types of accounts, because the amounts contributed are small, future contributions are unlikely, and the account holders generally will be passive or not in contact with the individual retirement plan providers.

There is nothing in the safe harbor that would preclude establishment, maintenance and other fees and expenses from being charged against the individual retirement plan of an account holder. On the other hand, the safe harbor does establish limits on the amount of such fees and expenses that can be charged against an individual retirement plan. While the Department agrees that competition in the marketplace may serve to keep administrative and investment management costs down, the Department nonetheless believes that, given the importance of cost considerations in connection with the selection of service providers by plan fiduciaries generally and the importance of protecting principal in connection with automatic rollover distributions, the safe harbor should contain some limits on the fees and expenses that may be assessed against an individual retirement plan established for mandatory distributions. In this regard, the Department attempted to strike a balance in the proposal between the application of a marketplace principle and the investment goal of preserving principal.

Under paragraph (c)(4) of the proposed regulation, fees and expenses attendant to an individual retirement plan, including investments of such plan, (*e.g.*, establishment charges, maintenance fees, investment expenses, termination costs and surrender charges) may not exceed certain limits. The first limit, provided in paragraph (c)(4)(i), is intended to ensure that fees and expenses charged to individual retirement plans established in connection with a mandatory distribution are not inconsistent with the marketplace. This limit provides that the fees and expenses charged to such plans may not exceed the fees and expenses charged by the provider for comparable individual retirement plans established for rollover distributions that are not subject to the automatic rollover provisions of section 401(a)(31)(B) of the Code.

The second limit, provided in paragraph (c)(4)(ii), is intended to protect the investment principal by providing that fees and expenses attendant to the individual retirement plan may be charged only against the income earned by the plan, with the exception of charges assessed for the establishment of the plan. The Department understands that in some instances providers will charge a one-time, typically small, fee to set up an individual retirement plan. While providers are not required to limit establishment charges to the income earned by individual retirement plans, these charges, nonetheless, may not exceed establishment charges assessed against comparable individual retirement plans established for rollover distributions that are not subject to the automatic rollover provisions of section 401(a)(31)(B) of the Code. If a provider, therefore, imposes no establishment or set-up charge on its comparable individual retirement plan customers, it may not impose a charge on plans established for rollover distributions under section 401(a)(31)(B) of the Code.

The fifth condition is intended to ensure that participants and beneficiaries are informed of the plan's procedures governing automatic rollovers, including an explanation about the nature of the investment product in which the mandatory distribution will be invested, and how

[11] Regarding money market mutual funds, prospectuses for such funds generally state that ''an investment in the [money market mutual] Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency. Although the Fund seeks to preserve the value of your [the investor's] investment at $1.00 per share, it is possible to lose money by investing in the Fund.''

fees and expenses attendant to the individual retirement plan will be allocated (*i.e.*, the extent to which expenses will be borne by the account holder alone or shared with the distributing plan or plan sponsor). In addition, the disclosure must identify a plan contact for further information concerning the plan's procedures, individual retirement plan providers, and the fees and expenses attendant to the individual retirement plan. In this regard, paragraph (c)(5) of the proposed regulation conditions safe harbor relief on the furnishing of this information to the plan's participants and beneficiaries in a summary plan description (SPD) or a summary of material modifications (SMM) in advance of an automatic rollover. For purposes of this condition, a plan contact can be identified by reference to a person, position or office, along with an address and phone number of the contact. It is anticipated that the contact, in response to requests from separated participants on whose behalf distributions have been made to an individual retirement plan, would be able to identify the individual retirement plan provider to whom a distribution was made for the particular participant.

One commenter on the RFI argued against the establishment of any new disclosure requirements under the safe harbor, given the requirements that already exist under the Code. Another commenter argued that the safe harbor should require individual notices to each separated participant on whose behalf an individual retirement plan is established informing him or her of the provider's name, address and phone number, and any other information needed by the account holder to take action with regard to the distributed funds.

This condition is consistent with the Department's statement in a footnote to Revenue Ruling 2000–36 requiring that plan provisions governing the default direct rollover of distributions, including the participant's ability to affirmatively opt out of the arrangement, must be described in the plan's SPD furnished to participants.[12] We believe this approach to disclosure similarly serves to ensure that participants and beneficiaries are provided, and have access to, sufficient information about automatic rollovers, while avoiding the imposition of unnecessary costs and burdens on pension plans and individual retirement plan providers.

Paragraph (c)(6) of the proposed regulation conditions safe harbor relief on the plan fiduciary not engaging in prohibited transactions in connection with the selection of an individual retirement plan provider or investment product, unless such actions are covered by a statutory or administrative exemption issued under section 408(a) of ERISA. In this regard, the Department is publishing a proposed class exemption in today's **Federal Register** that is intended to deal with prohibited transactions resulting from an individual retirement plan provider's selection of itself as the provider of an individual retirement plan and/or issuer of an investment held by such plan in connection with mandatory distributions from the provider's own pension plan. Specifically, the proposed exemption is intended to permit a bank or other regulated financial institution as defined therein to (1) select itself or an affiliate as the individual retirement plan trustee, custodian or issuer to receive automatic rollovers from its own plan and (2) select its own funds or investment products for automatic rollovers from its own plan. In the absence of this exemption, a bank or other financial institution would be required to direct automatic rollovers from its own plan for its own employees to a competitor as the individual retirement plan provider.

C. Miscellaneous Issues

In response to the Department's RFI, a number of commenters identified possible legal impediments that fiduciaries, banks and other financial institutions might encounter in connection with automatic rollovers. These impediments included perceived conflicts with state laws on signature requirements and escheat, Code requirements, and requirements under the USA PATRIOT Act.[13]

With regard to Code requirements that may possibly conflict with or impede the establishment of individual retirement plans for purposes of automatic rollovers of mandatory distributions under section 401(a)(31)(B) of the Code, the Department has been informed that staff of the Department of the Treasury and the Internal Revenue Service are reviewing the current rules and regulations affecting such distributions and that guidance addressing the application of these rules to the automatic rollover of mandatory distributions is anticipated in advance of or simultaneously with the Department's issuance of a final safe harbor regulation.

With regard to the provisions of the USA PATRIOT Act (Act), a number of commenters pointed out that the customer identification and verification provisions of the Act may preclude banks and other financial institutions from establishing individual retirement plans without the participation of the participant or beneficiary on whose behalf the fiduciary is required to make an automatic rollover. In most of the situations where a fiduciary is required to make an automatic rollover to an individual retirement plan, the participant or beneficiary is unable to be located or is otherwise not communicating with the plan concerning the distribution of plan benefits. Accordingly, if the customer identification and verification provisions of the Act were construed to require participant or beneficiary participation when an individual retirement plan is established on his or her behalf, fiduciaries will be unable to comply with the automatic rollover requirements of the Code and utilize this safe harbor. Commenters also noted that such an interpretation of the Act would limit the ability of fiduciaries to make distributions from terminating defined contribution plans on behalf of missing plan participants and beneficiaries.

In response to these issues, Treasury staff, along with staff of the other Federal functional regulators,[14] have advised the Department that they interpret the customer identification and verification (CIP) requirements of section 326 of the Act and implementing regulations to require that banks and other financial institutions implement their CIP compliance program with respect to an account, including an individual retirement plan, established by an employee benefit plan in the name of a former participant (or beneficiary) of such plan, only at the time the former participant or beneficiary first contacts such institution to assert ownership or exercise control over the account. CIP compliance will not be required at the time an employee benefit plan establishes an account and transfers the funds to a bank or other financial institution for purposes of a distribution of benefits from the plan to a separated employee.[15] In January 2004, Treasury staff, along with staff of the other Federal functional regulators, issued guidance on this matter in the form of

[12] Revenue Ruling 2000–36, 2000–2 C.B. 140.

[13] Pub. L. No. 107–56, October 26, 2001, 115 Stat. 272.

[14] The term ''other Federal functional regulators'' refers to the other agencies responsible for administration and regulations under the Act.

[15] It is the Department's understanding that this interpretation applies to a broad spectrum of employee benefit plans including those covered by title I of ERISA and those established under Code provisions.

a question and answer, published in a set of ''FAQs: Final CIP Rule,'' on the regulators'' Web sites.[16]

Issues raised by commenters concerning the possible application of state laws are beyond the scope of this regulation.

D. Effective Date

As discussed above, section 657(c)(2)(A) of EGTRRA provides that the requirements of section 401(a)(31)(B) of the Code requiring automatic rollovers of mandatory distributions to individual retirement plans do not become effective until the Department issues final safe harbor regulations. Inasmuch as it appears clear that Congress did not intend fiduciaries to be subject to the automatic rollover requirements under the Code in the absence of a safe harbor, the Department believes the effective date of the rollover requirement must be determined by reference to the effective date of the final safe harbor regulation, that is the date on which plan fiduciaries may avail themselves of the relief provided by the safe harbor. In this regard, the Department is proposing to make the final safe harbor regulation effective 6 months after the date of publication in the **Federal Register** in order to afford plan fiduciaries adequate time to amend their plans, distribute required disclosures and identify institutions and products that would afford relief under the final safe harbor regulation.

E. Request for Comments

The Department invites comments from interested persons on all aspects of the proposed safe harbor provided herein, including the proposed effective date. Comments (preferably at least three copies) should be addressed to the Office of Regulations and Interpretations, Employee Benefits Security Administration, Room N–5669, U.S. Department of Labor, 200 Constitution Avenue NW., Washington, DC 20210. Attn: Automatic Rollover Regulation. Comments also may be submitted electronically to *e-ori@dol.gov*. All comments received will be available for public inspection at the Public Disclosure Room, N–1513, Employee Benefits Security Administration, 200 Constitution Avenue NW., Washington, DC 20210.

The Department has limited the comment period to 30 days in order to issue a final regulation on the earliest possible date, taking into account Congress's expectation that regulations would be issued in June 2004. The Department believes that, in light of the earlier published request for information and the limited number of issues presented for consideration by the proposal, the provided 30-day comment period affords interested persons an adequate amount of time to analyze the proposal and submit comments thereon.

F. Regulatory Impact Analysis

Summary

The purpose of this proposed regulation is to establish conditions under which a fiduciary will be deemed to satisfy the fiduciary obligations under section 404(a) of ERISA in connection with the automatic rollover of a mandatory distribution as described in amended Code section 401(a)(31)(B). The EGTRRA amendment is estimated to have significant costs and benefits in that it annually will provide 241,000 former participants with preserved retirement savings of about $249 million and immediate tax savings of about $71 million. Included in those 241,000 participants are 98,000 who are assumed to be passive or non-responsive. Establishing individual retirement plans for these participants for automatic rollovers of mandatory distributions will reduce ordinary plan administrative expenses attributable to those participants by an estimated $9.5 million in the first year.

The amendment will generate one-time administrative compliance costs of an estimated $139 million, and individual retirement plan establishment and maintenance fees totaling $14.4 million in the first year. Automatic rollovers of mandatory distributions may give rise to other costs as well, such as investment expenses, termination charges, and surrender charges, but the magnitude of some of those expenses will relate to the actual investment products selected. The range of possible costs that relate to investment products is considered too broad to support meaningful estimates.

The savings that will arise from this safe harbor are expected to substantially outweigh its costs and transfers. The guidance provided by this proposed regulation is expected to result in an aggregate savings of administrative compliance costs for plans of about $92 million by lessening the time required to select an individual retirement plan provider, investment product, and fee structure that are consistent with the provisions of Code section 401(a)(31)(B) and ERISA section 404(a) with respect to automatic rollovers of mandatory distributions. Other benefits not quantified here are expected to accrue to fiduciaries through greater certainty and reduced exposure to risk, and to former plan participants through the proposed regulatory standards concerning individual retirement plan providers, investment products, preservation of principal, rates of return, liquidity, and fees and expenses.

One-time costs associated with modifying a summary plan description or summary of material modifications to satisfy the safe harbor conditions are expected to amount to about $13 million.

The proposed safe harbor will preserve the principal amounts of automatic rollovers of mandatory distributions by ensuring that the various fees and expenses that apply to the individual retirement plans established for mandatory distributions are not more costly than those charged by the provider to individual retirement plans for comparable rollover distributions that are not subject to the automatic rollover provisions of Code section 401(a)(31)(B). If adopted as proposed, this guidance may also result in a transfer of individual retirement plan costs to other individual retirement plans or to plan sponsors to the extent that earnings and available profit are less than the fees that the individual retirement plan provider would ordinarily charge for comparable individual retirement plans.

Further discussion of costs and benefits and the data and assumptions underlying these estimates will be found below.

Executive Order 12866 Statement

Under Executive Order 12866, the Department must determine whether a regulatory action is ''significant'' and therefore subject to the requirements of the Executive Order and subject to review by the Office of Management and Budget (OMB). Under section 3(f) of the Executive Order, a ''significant regulatory action'' is an action that is likely to result in a rule (1) having an annual effect of the economy of $100 million or more, or adversely and materially affecting a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or State, local or tribal governments or communities (also referred to as ''economically significant''); (2) creating serious inconsistency or otherwise interfering with an action taken or planned by another agency; (3) materially altering the budgetary impacts of entitlement grants, user fees, or loan programs or the rights and obligations of recipients

[16] *See* FAQs: Final CIP Rule at: *http://www.occ.treas.gov/10.pdf http://www.fincen.gov/finalciprule.pdf http://www.ots.treas.gov/docs/25188.pdf http://www.fdic.gov/news/news/financial/2004/FIL0404a.html*

thereof; or (4) raising novel legal or policy issues arising out of legal mandates, the President's priorities, or the principles set forth in the Executive Order. OMB has determined that this action is significant under section 3(f)(4) because it raises novel legal or policy issues arising from the President's priorities. Accordingly, the Department has undertaken an analysis of the costs and benefits of the proposed regulation. OMB has reviewed this regulatory action.

1. Costs and Benefits of the EGTRRA Amendment

The impact of the amendment to Code section 401(a)(31) is distinguishable from the impact of the proposed regulation, and is expected to affect, in the aggregate, fiduciaries, plan participants, and certain regulated financial institutions. Fiduciaries will incur initial administrative expenses to select providers and investment products. Plan participants who may otherwise receive a cash distribution and pay ordinary income tax and penalties on the amount distributed will not pay those taxes because the amounts would have been retained in the pension system to earn additional tax-deferred income for retirement. As a result of the amendment, certain costs and fees will also be incurred by pension plans in connection with automatic rollovers and the investments for individual retirement plans. Finally, certain regulated financial institutions will receive additional deposits and earnings potential, and incur costs and charge fees for account maintenance.

After the effective date of the amendment, plans that currently mandate immediate distributions for amounts of greater than $1,000 but not exceeding $5,000 will, absent an affirmative election of a different alternative, make direct transfers of these distributions to an individual retirement plan. To implement this change, fiduciaries and their professional service providers will need to review the new requirements and select individual retirement plan providers and investment products. The amount of time required for this activity will vary, but based on 680,000 retirement plans and an assumed hourly rate of $68, the aggregate cost of each hour is over $46 million. An effort involving an average of 3 hours would result in an aggregate one-time cost of about $139 million. For this estimate we have conservatively assumed that all plans provide for such mandatory distributions and will need to take action to implement procedures for automatic rollovers to individual retirement plans. The proportion of pension plans that provide for such mandatory distributions is not known, but is believed based on anecdotal evidence to be very high. This total cost may be lessened to the extent that fewer plans will need to address the automatic rollover requirement, or that the assistance of service providers to multiple plans results in greater efficiency.

The Census Bureau's 1996 Survey of Program Participation (SIPP), Wave 7 Pension Benefits Module collected information as to the number, uses, and values of lump sum distributions from private pension plans in 1997. The survey responses show whether a distribution was mandatory or voluntary, and whether the amount involved was ''Rolled over into another plan, an IRA, or an individual retirement annuity'' (''rolled over''). The number of lump sum distributions between $1,001 and $5,000 that were characterized as mandatory and put to other specific uses enumerated in the survey instrument (''lump sums'') has been used for the purpose of this analysis to approximate the number of participants in plans with mandatory distribution provisions that might fail to make an affirmative election. The number of automatic rollovers of mandatory distributions that will occur because of the Code amendment may be smaller than the number of lump sums because some of these participants may have made an affirmative election. It seems reasonable to assume that distributions rolled over would have involved an affirmative election, and that the number of participants making affirmative elections will be largely unchanged. The number of lump sums is assumed to represent an upper bound of the number of participants potentially affected by the automatic rollover provisions of Code section 401(a)(31)(B).

SIPP data show that in 1997 about 143,000 mandatory lump sum distributions of $1,001 to $5,000 were made. Using the midpoint of the reported groupings of distribution amounts (*e.g.*, $1,500 for $1,001 to $1,999) the total amount of retirement savings distributed was about $415 million, or an average of $2,900 per former participant. The account balances and present values of accrued benefits (''accounts'') of an additional 98,000 participants were left in plans during the same year for reasons that are not known. Although there is some uncertainty with respect to this assumption, this number has been used here as a proxy for a number of participants that did not receive mandatory distributions because they were passive or non-responsive. Assuming that the accounts of these participants were comparable in size and would also be automatically rolled over after the amendment is effective, the aggregate amount of automatic rollovers of mandatory distributions to individual retirement plans for 241,000 participants would be about $699 million per year ($415 million plus $284 million). Only $415 million of this total represents retirement savings that would not otherwise have been preserved, given that the $284 million was already maintained in retirement plans.

The amount of some mandatory distributions subject to the automatic rollover requirements of section 401(a)(31)(B) of the Code may be more than $5,000. This can occur where the present value of the nonforfeitable accrued benefits immediately distributable includes additional funds attributable to prior rollover contributions (and the earnings thereon).

The Department did not attempt to estimate the number or dollar amount of mandatory distributions eligible for relief under the proposed safe harbor regulation that may exceed $5,000. Adequate data to support such estimates are not currently available.

The Department believes it is probable that the number of mandatory distributions containing prior rollover contributions that will be subject to the automatic rollover requirement of section 401(a)(31)(B) of the Code will be small but the number of plans affected and the dollar amount of some of these mandatory distributions might be large.

A large majority of 401(k) plan participants are in plans that accept rollover contributions, according to the Bureau of Labor Statistics. There is some evidence, however, that rollovers into qualified plans are infrequent, which suggests that the number of participants whose accounts include amounts attributable to prior rollover contributions may be small. The number of such participants that will eventually become the owners of an automatic rollover individual retirement plan will be further limited by a number of factors, on which no data are available. Some plans will not mandate distribution of accounts that include prior rollover contributions and therefore exceed $5,000. Some accounts of participants with prior rollover contributions will accumulate more than $5,000 of additional contributions, thereby becoming ineligible for mandatory distributions. Some participants whose accounts do not accumulate more than $5,000 will

affirmatively direct, upon leaving employment, the disposition of their accounts. Compared with other participants, those with prior rollover contributions, especially those with large rollover contributions, may be more likely to accumulate more than $5,000 from new contributions and more likely to affirmatively direct the disposition of their accounts.

The Department invites comments on the potential economic impact of the safe harbor established by this proposed regulation in connection with the mandatory distributions of accounts valued at more than $5,000.

The Joint Committee on Taxation's May 26, 2001 estimates of budget effects for this provision of EGTRRA indicated revenue losses on the order of about $30 million per year, which suggests a substantially lower estimate of the aggregate preservation of retirement savings, amounting to about $83 million for private plan participants. The reason for this difference is unknown. Interpreting these differing estimates as ends of a range, ordinary income tax and penalty savings are expected to amount to between $30 million and $112 million per year, while aggregate retirement savings are expected to increase by between $83 million and $415 million per year. For purposes of discussion, midpoint values of $71 million and $249 million are used here. These savings for former participants and distributions of amounts previously retained in plans also represent increased deposits to regulated financial institutions.

The establishment and maintenance of individual retirement plans for automatic rollovers of mandatory distributions will generate costs to individual retirement plans that may be defrayed by administrative fees to the extent that the individual retirement plan providers charge them. Certain investments may also generate fees. Some individual retirement plan providers may have termination fees, and some investments may have surrender charges associated with them that would be incurred at a later time when a former participant chose to exercise control over the account. With interpretive guidance, fiduciaries and the regulated financial institutions will have increased certainty regarding the limitations on costs, fees, and charges for individual retirement plans. In the absence of the proposed safe harbor and the fiduciary's desire to make use of the safe harbor, such costs and fees could be paid by plan sponsors or charged to individual retirement plans. However, it has been assumed here that in the absence of guidance, most fees would be charged against individual retirement plans. Aggregate annual establishment fees for rollovers arising from the amendment each year are estimated to range from a negligible amount to $2.4 million at the upper end of a range based on typical establishment fees for comparable individual retirement plan rollovers that range from no charge to $10 per account. Annual maintenance fees, which typically range from $7 to $50, with a mid-point of $29, are estimated to range from $1.7 million to $12 million, implying a mid-point estimate of $6.9 million, for individual retirement plans established in the first year. Assuming that individual retirement plans continue to be established at a constant rate of 241,000 plans per year and that, at an upper bound, no account holders assume control of their plans, maintenance fees would continue to grow at an average rate of $6.9 million annually.

As noted earlier, although establishment and maintenance fees are relatively predictable based on comparable individual retirement plans for rollover distributions available in the marketplace, the types of investment products available and the actual choices that may be made by fiduciaries are considered to be too variable to support a meaningful estimate of investment fees, termination charges, and surrender fees.

Plans will benefit from administrative cost savings under the Code amendment for those 98,000 accounts that previously remained in pension plans but are assumed to be subject to mandatory rollover provisions under EGTRRA. Ordinary administrative costs that typically range from $45 to $150 per participant will be saved when accounts are rolled over, reducing plan expenses by about $4.4 million to $14.7 million, or an average of $9.5 million in the first year. Assuming an annual rollover of 98,000 accounts that would have remained in pensions plans, cost savings to plans would continue to increase at an average of $9.5 million per year. The cost savings realized in each year will continue to accumulate through the future years that the accounts would otherwise have remained in the pension plan.

For the estimated 8 percent of these accounts that were in defined benefit plans, a small savings of approximately $144,000 would be realized from reduced funding risk and corresponding premium payments to the Pension Benefit Guaranty Corporation (PBGC).

2. Benefits and Costs of the Proposed Regulation

The proposed regulation will benefit fiduciaries by affording them greater assurance of compliance and reduced exposure to risk. Specificity as to the types of entities that may receive the rollovers, the investment choices, and the limitations on fees will lessen the time required to comply with the EGTRRA amendment. The substantive conditions of the safe harbor will benefit former participants by directing their retirement savings to individual retirement plans, providers, regulated financial institutions, and investment products that minimize risk and offer preservation of principal and liquidity. The limitation of fees and expenses will also benefit individual retirement plan account holders. Fees and expenses for the individual retirement plans will be limited under the safe harbor to those that would be charged by the provider to comparable individual retirement plans established for rollover distributions that are not subject to automatic rollover provisions of the Code, thereby preserving principal. The limitation of maintenance fees to the extent of income earned will also serve to maintain principal.

The benefits of greater certainty for fiduciaries and protection of participants cannot be specifically quantified. The proposed regulation is, however, expected to reduce one-time startup administrative compliance costs by as much as $92 million by narrowing the range of individual retirement plan providers and investment products fiduciaries might otherwise consider, assuming a savings of 2 of the 3 hours that compliance would otherwise require.

No estimate is made for the impact of the limitation on fees charged to the subject individual retirement plans compared to those charged by individual retirement plan providers for comparable individual account plans established for rollover distributions that are not subject to section 401(a)(31)(B) of the Code because the Department is not aware of a basis for judging whether and in what magnitude providers would charge different fees absent the safe harbor.

The proposal may affect the manner in which fees and expenses would otherwise have been allocated among plan sponsors and individual retirement plans. Under section 2550.404a–2(c)(4)(ii) of the proposed regulation, fees and expenses may be charged only against the income earned by the individual retirement plan. In some instances, particularly in the case of

smaller individual retirement plans and when interest rates are low, the credited interest, together with any profit the individual retirement plan provider might otherwise derive from holding the plan, may not cover the cost incurred by the provider to maintain the plan. The Department believes that in these circumstances individual retirement plan providers will offset or subsidize any such uncovered costs either through increased maintenance fees on larger automatic rollovers, through increased administrative charges to plan sponsors, or possibly both. Because such uncovered costs (if any) derive from a provision of this proposed regulation, any associated offsets or subsidies would be attributable to it as well. The Department would welcome comments on the probable incidence and magnitude of any such uncovered costs and associated offsets or subsidies.

Plans will incur costs in connection with the proposed safe harbor to modify summary plan descriptions or provide a summary of material modifications. This cost is estimated to be about $13 million.

3. Alternatives

In preparation for drafting the proposed regulation, the Department published an RFI (68 FR 991) requesting comment on issues relating to the development of safe harbors for automatic rollovers and assistance in drafting regulations. The Department received 17 comments from the general public, service providers, and professional associations involved with pension planning, investing, and retirement accounts. Commenters opined on potential costs, issues of fiduciary liability and prohibited transaction relief, technical considerations involving state and federal laws, disclosures to participants, and draft language for the proposed regulation. Responses to the RFI informed the drafting process by permitting the Department to consider alternatives for achieving the regulatory objective at the initial stages. A more detailed discussion of the comments and the considerations given the alternatives by the Department is provided earlier in the preamble.

Paperwork Reduction Act

This Notice of Proposed Rulemaking is not subject to the requirements of the Paperwork Reduction Act of 1995 (44 U.S.C. 3501 *et seq.*) because it does not contain a ''collection of information'' as defined in 44 U.S.C. 3502(3). It is expected that this proposed rule will result in a modification of retirement plan Summary Plan Descriptions, an information collection request approved separately under OMB control number 1210–0039. However, this modification is not considered to be substantive or material in the context of that information collection request as a whole. In addition, the methodology for calculating burden under the Paperwork Reduction Act for the Summary Plan Description takes into account a steady rate of change in Summary Plan Descriptions that is estimated to accommodate the change that would be made by this proposed rulemaking. As a result, the Department has not made a submission for OMB approval in connection with this rulemaking.

Regulatory Flexibility Act

The Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*) (RFA) imposes certain requirements with respect to Federal rules that are subject to the notice and comment requirements of section 553(b) of the Administrative Procedure Act (5 U.S.C. 551 *et seq.*) and which are likely to have a significant economic impact on a substantial number of small entities. Unless an agency determines that a proposed rule is not likely to have a significant economic impact on a substantial number of small entities, section 603 of the RFA requires that the agency present an initial regulatory flexibility analysis at the time of the publication of the notice of proposed rulemaking describing the impact of the rule on small entities and seeking public comment on such impact. Small entities include small businesses, organizations and governmental jurisdictions.

For purposes of analysis under the RFA, the Employee Benefits Security Administration (EBSA) proposes to continue to consider a small entity to be an employee benefit plan with fewer than 100 participants. The basis of this definition is found in section 104(a)(2) of ERISA, which permits the Secretary of Labor to prescribe simplified annual reports for pension plans which cover fewer than 100 participants. Under section 104(a)(3), the Secretary may also provide for exemptions or simplified annual reporting and disclosure for welfare benefit plans. Pursuant to the authority of section 104(a)(3), the Department has previously issued at 29 CFR 2520.104–20, 2520.104–21, 2520.104–41, 2520.104–46 and 2520.104b–10 certain simplified reporting provisions and limited exemptions from reporting and disclosure requirements for small plans, including unfunded or insured welfare plans covering fewer than 100 participants and which satisfy certain other requirements.

Further, while some large employers may have small plans, in general small employers maintain most small plans. Thus, EBSA believes that assessing the impact of this proposed rule on small plans is an appropriate substitute for evaluating the effect on small entities. The definition of small entity considered appropriate for this purpose differs, however, from a definition of small business which is based on size standards promulgated by the Small Business Administration (SBA) (13 CFR 121.201) pursuant to the Small Business Act (15 U.S.C. 631 *et seq.*). EBSA therefore requests comments on the appropriateness of the size standard used in evaluating the impact of this proposed rule on small entities. The Department does not expect that the financial institutions potentially impacted by this proposal will be small entities.

EBSA has preliminarily determined that this rule will not have a significant economic impact on a substantial number of small entities. In support of this determination, and in an effort to provide a sound basis for this conclusion, EBSA has prepared the following initial regulatory flexibility analysis.

Section 657(c)(2)(A) of EGTRRA directed the Department to issue regulations providing safe harbors under which a plan administrator's designation of an institution to receive automatic rollovers of mandatory distributions pursuant to section 401(a)(31)(B) of the Code and the initial investment choice for the rolled-over funds would be deemed to satisfy the fiduciary responsibility provisions of section 404(a) of ERISA. This EGTRRA provision further provided that the Code provisions requiring automatic rollovers of certain mandatory distributions to individual retirement plans would not become effective until the Department issued safe harbor regulations. Before issuing this proposal, the Department requested comments on the potential design of the safe harbor.

The conditions set forth in this proposed regulation are intended to satisfy the EGTRRA requirement that the Department prescribe regulations providing for safe harbors, while meeting the objectives of offering greater certainty to fiduciaries concerning their compliance with the requirements of ERISA section 404(a), and of preserving assets of former plan participants for retirement income purposes. In describing the financial institutions, investment products, and fee arrangements that fall within the safe harbor, the Department has attempted to strike a balance between the interests of

fiduciaries, individual retirement plan providers, and the investment goal of preserving principal.

The proposed rule would impact small plans that include provisions for the mandatory distribution of accounts with a value exceeding $1,000 and not greater than $5,000. It has been assumed for the purposes of this analysis that all plans include such provisions, although the number may actually be somewhat lower. On this basis, it is expected that the proposal will affect 611,800 small plans. The proportion of the total of 241,000 participants estimated to be affected annually by the amendment to Code section 401(a)(31)(B) that were in small plans is not known. Similarly, there are no available data on the number of participants that will separate from employment with account balances of more than $5,000 (because of prior rollover contributions) that may be, depending on the provisions of the distributing plans, automatically rolled over under EGTRRA. It is assumed that all 611,800 small plans will need to address compliance with the Code amendment and section 404(a) of ERISA.

As described above, the costs and benefits of the Code amendment and safe harbor proposal are distinguishable, and estimated separately. As also noted, the proposed regulation is expected to substantially reduce the cost of compliance with the Code amendment. The initial cost of the Code amendment for small plans is expected to be about $124 million. The one-time savings from the proposed regulation is estimated at about $83 million for small plans compared with $9 million for large plans, due to the significantly larger number of small plans. The condition of the safe harbor requiring disclosure of specific information in a summary plan description or summary of material modification is expected to result in costs of about $11 million. Preparation of this information is in most cases accomplished by professionals that provide services to employee benefit plans. Where fiduciaries prepare these materials themselves, it is assumed that persons at the professional level of budget analysts or financial managers will complete the necessary work.

The benefits of greater certainty afforded fiduciaries by the safe harbor are substantial but cannot be specifically quantified.

Prior to publication of this proposed regulation, the Department published an RFI requesting comments and suggestions from the general public on developing guidelines to assist fiduciaries in selecting institutions and investment products for individual retirement plans. The Department specifically requested in the RFI that commenters, ''address the anticipated annual impact of any proposals on small businesses and small plans (plans with fewer than 100 participants).'' The Department received three comments that pertained specifically to small plans, the first of which cautioned that plan sponsors would be deterred from sponsoring plans with a mandatory distribution provision by placement of any additional burdens on them. Another comment indicated that, because of technological improvements, the burden on small plans would be manageable. Finally, a third commenter noted that annual costs would not be any higher for small plans.

To the Department's knowledge, there are no federal regulations that might duplicate, overlap, or conflict with the proposed regulation for safe harbors under section 404(a) of ERISA.

Congressional Review Act

The notice of proposed rulemaking being issued here is subject to the provisions of the Congressional Review Act provisions of the Small Business Regulatory Enforcement Fairness Act of 1996 (5 U.S.C. 801 *et seq.*) and, if finalized, will be transmitted to the Congress and the Comptroller General for review.

Unfunded Mandates Reform Act

Pursuant to provisions of the Unfunded Mandates Reform Act of 1995 (Pub. L. 104–4), this rule does not include any Federal mandate that may result in expenditures by State, local, or tribal governments, or the private sector, which may impose an annual burden of $100 or more.

Federalism Statement

Executive Order 13132 (August 4, 1999) outlines fundamental principles of federalism and requires the adherence to specific criteria by federal agencies in the process of their formulation and implementation of policies that have substantial direct effects on the States, the relationship between the national government and the States, or on the distribution of power and responsibilities among the various levels of government. This proposed rule would not have federalism implications because it has no substantial direct effect on the States, on the relationship between the national government and the States, or on the distribution of power and responsibilities among the various levels of government. Section 514 of ERISA provides, with certain exceptions specifically enumerated, that the provisions of Titles I and IV of ERISA supersede any and all laws of the States as they relate to any employee benefit plan covered under ERISA. The requirements implemented in this proposed rule do not alter the fundamental provisions of the statute with respect to employee benefit plans, and as such would have no implications for the States or the relationship or distribution of power between the national government and the States.

List of Subjects in 29 CFR Part 2550

Employee benefit plans, Exemptions, Fiduciaries, Investments, Pensions, Prohibited transactions, Real estate, Securities, Surety bonds, Trusts and trustees.

For the reasons set forth in the preamble, the Department proposes to amend Subchapter F, Part 2550 of Title 29 of the Code of Federal Regulations as follows:

SUBCHAPTER F—FIDUCIARY RESPONSIBILITY UNDER THE EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974

PART 2550—RULES AND REGULATIONS FOR FIDUCIARY RESPONSIBILITY

1. The authority citation for part 2550 is revised to read as follows:

Authority: 29 U.S.C. 1135; sec. 657, Pub. L. 107–16, 115 Stat. 38; and Secretary of Labor's Order No. 1–2003, 68 FR 5374 (Feb. 3, 2003). Sec. 2550.401b–1 also issued under sec. 102, Reorganization Plan No. 4 of 1978, 43 FR 47713 (Oct. 17, 1978), 3 CFR, 1978 Comp. 332, effective Dec. 31, 1978, 44 FR 1065 (Jan. 3, 1978), 3 CFR, 1978 Comp. 332. Sec. 2550.401c–1 also issued under 29 U.S.C. 1101. Sec. 2550.404c–1 also issued under 29 U.S.C. 1104. Sec. 2550.407c–3 also issued under 29 U.S.C. 1107. Sec. 2550.408b–1 also issued under 29 U.S.C. 1108(b)(1) and sec. 102, Reorganization Plan No. 4 of 1978, 3 CFR, 1978 Comp. p. 332, effective Dec. 31, 1978, 44 FR 1065 (Jan. 3, 1978), and 3 CFR, 1978 Comp. 332. Sec. 2550.412–1 also issued under 29 U.S.C. 1112.

2. Add § 2550.404a–2 to read as follows:

§ 2550.404a–2 Safe harbor for automatic rollovers to individual retirement plans.

(a) *In general.* (1) Pursuant to section 657(c) of the Economic Growth and Tax Relief Reconciliation Act of 2001, Public Law 107–16, June 7, 2001, 115 Stat. 38, this section provides a safe harbor under which a fiduciary of an employee pension benefit plan subject to Title I of the Employee Retirement Income Security Act of 1974, as amended (the Act), 29 U.S.C. 1001 *et seq.*, will be deemed to have satisfied his or her fiduciary duties under section 404(a) of

the Act in connection with an automatic rollover of a mandatory distribution described in section 401(a)(31)(B) of the Internal Revenue Code of 1986, as amended (the Code).

(2) The standards set forth in this section apply solely for purposes of determining whether a fiduciary meets the requirements of this safe harbor. Such standards are not intended to be the exclusive means by which a fiduciary might satisfy his or her responsibilities under the Act with respect to automatic rollovers of mandatory distributions described in section 401(a)(31)(B) of the Code.

(b) *Safe harbor.* A fiduciary that meets the conditions of paragraph (c) of this section is deemed to have satisfied his or her duties under section 404(a) of the Act with respect to both the selection of an individual retirement plan provider and the investment of funds in connection with an automatic rollover of a mandatory distribution described in section 401(a)(31)(B) of the Code to an individual retirement plan, within the meaning of section 7701(a)(37) of the Code.

(c) *Conditions.* With respect to an automatic rollover of a mandatory distribution described in section 401(a)(31)(B) of the Code, a fiduciary shall qualify for the safe harbor described in paragraph (b) of this section if:

(1) The present value of the nonforfeitable accrued benefit, as determined under section 411(a)(11) of the Code, does not exceed the maximum amount under section 401(a)(31)(B) of the Code;

(2) The mandatory distribution is to an individual retirement plan within the meaning of section 7701(a)(37) of the Code;

(3)(i) The mandatory distribution is invested in an investment product designed to preserve principal and provide a reasonable rate of return, whether or not such return is guaranteed, consistent with liquidity, and taking into account paragraph (c)(4) of this section. For this purpose, the product must be offered by a state or federally regulated financial institution, as defined in paragraph (c)(3)(ii) of this section, and must seek to maintain a stable dollar value equal to the amount invested in the product by the individual retirement plan, and

(ii) For purposes of this section, a regulated financial institution shall be: a bank or savings association, the deposits of which are insured by the Federal Deposit Insurance Corporation; a credit union, the member accounts of which are insured within the meaning of section 101(7) of the Federal Credit Union Act; an insurance company, the products of which are protected by state guarantee associations; or an investment company registered under the Investment Company Act of 1940;

(4)(i) Fees and expenses attendant to the individual retirement plan, including investments of such plan, (*e.g.*, establishment charges, maintenance fees, investment expenses, termination costs and surrender charges) shall not exceed the fees and expenses charged by the individual retirement plan provider for comparable individual retirement plans established for rollover distributions that are not subject to the automatic rollover provisions of section 401(a)(31)(B) of the Code, and

(ii) Fees and expenses attendant to the individual retirement plan may be charged only against the income earned by the individual retirement plan, with the exception of charges assessed for the establishment of the individual retirement plan;

(5) Participants have been furnished a summary plan description, or a summary of material modifications, that describes the plan's automatic rollover provisions effectuating the requirements of section 401(a)(31)(B) of the Code, including an explanation that the mandatory distribution will be invested in an investment product designed to preserve principal and provide a reasonable rate of return and liquidity, a statement indicating how fees and expenses attendant to the individual retirement plan will be allocated, and the name, address and phone number of a plan contact (to the extent not otherwise provided in the summary plan description or summary of material modifications) for further information concerning the plan's automatic rollover provisions, the individual retirement plan provider and the fees and expenses attendant to the individual retirement plan; and

(6) Both the fiduciary's selection of an individual retirement plan and the investment of funds would not result in a prohibited transaction under section 406 of the Act, unless such actions are exempted from the prohibited transaction provisions by a prohibited transaction exemption issued pursuant to section 408(a) of the Act.

Signed at Washington, DC, this 24th day of February, 2004.

Ann L. Combs,

Assistant Secretary, Employee Benefits Security Administration, Department of Labor.

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