Empower Retirement/Great-West Investments announced a new potential approach to the QDIA in their white paper “In search of a more dynamic QDIA.” That paper explains the relevance of a dynamic approach QDIA (“Dynamic QDIA”) composed of two types of QDIA investment options. Participants at the early stages of their careers are defaulted into a target date fund, while those closer to retirement are defaulted into a managed account. Participants are automatically transferred from the target date fund to the managed account based on a designated trigger, for example, reaching age 45 or 50. On behalf of the plan fiduciary, Empower Retirement automates this transfer, includes the appropriate QDIA notices, and delivers a complete participant engagement strategy. A participant may opt out of the transfer and retain the ability to stay in the target date fund beyond the designated trigger.

In an effort to help plan fiduciaries understand the fiduciary considerations of a Dynamic QDIA approach, Empower Retirement/Great-West Investments engaged Groom Law Group to answer some common fiduciary questions.

FREQUENTLY ASKED QUESTIONS

1. Is the investment path in a Dynamic QDIA supported by current guidance from the Department of Labor (DOL)?

Yes. The Dynamic QDIA investment path begins with a default investment in a traditional target date QDIA. The path leads, at the right time, to a default investment in a managed account QDIA. The transfer from the target date QDIA to the managed account QDIA is triggered by an event designated by the plan fiduciary. The transfer itself is achieved through a “reset” (sometimes also referred to as a “re-enrollment”).

DOL’s QDIA regulation does not directly discuss resets. But DOL guidance (in the preamble to the QDIA Regulation and Field Assistance Bulletin 2008-03) sets forth concrete principles that clearly support resets. Specifically, that guidance extends QDIA relief to the investment of assets on behalf of any participant who fails to give investment direction following an appropriate QDIA notice. That relief is available regardless of whether a participant gave affirmative investment directions in the past. These principles have been applied to implement resets, and they have been tested in court in that same context. Specifically, the Sixth Circuit Court of Appeals cited the preamble’s language to uphold QDIA relief for a fiduciary who conducted a reset under the QDIA Regulation.

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2 Bidwell v. Univ. Med. Ctr., Inc., 685 F.3d 613 (6th Cir. 2012). In Bidwell, plan fiduciaries conducted a reset from a stable value fund to a QDIA target date fund. Subsequently, the market experienced a significant downturn and the transferred investments experienced significant losses. The court held that, in conducting the reset, the plan fiduciaries met the requirements of QDIA Regulation and thus the plan fiduciaries were not liable for the losses in affected participant accounts.
2. If a plan fiduciary adopts a Dynamic QDIA, is the fiduciary selecting two QDIAs or one QDIA with two different investment options?

The fiduciary is selecting and monitoring two QDIAs. A key feature of a Dynamic QDIA is the path from one type of QDIA (a target date investment fund) to another type of QDIA (a managed account). The transfer from the target date fund to the managed account QDIA qualifies for fiduciary protection under DOL guidance by treating the transfer as a reset from one QDIA to another QDIA. FAB 2008-03 is clear that nothing in the QDIA Regulation limits a plan to one QDIA, as long as each QDIA meets the requirements of the regulation. ¹

3. What are some of the fiduciary considerations a plan sponsor and committee should take into account when selecting and monitoring a QDIA?

A fiduciary must act solely in the interest of the plan’s participants and beneficiaries and must prudently select and monitor any QDIA. ² A fiduciary’s QDIA selection should result from a documented, objective, thorough, and analytical process that carefully considers the quality of competing investment providers and investment products, risk and return characteristics, and investment fees and expenses, and any other facts and circumstances a fiduciary knows (or should know) are relevant. ³

In the selection of any QDIA, a fiduciary must also consider the demographics of a plan’s participants. ⁴ A Dynamic QDIA allows a fiduciary to combine or “group” participants based on demographics to more closely align their needs with an appropriate QDIA. The preamble to the QDIA Regulation provides that a fiduciary may consider factors other than a participant’s age or target retirement date in selecting a target date QDIA. ⁵ As long as the fiduciary’s general ERISA fiduciary obligations are satisfied, the selection of any type QDIA allowed under the QDIA Regulation (including target date or managed account) works. ⁶

In addition to evaluating each QDIA as a prudent investment choice, a fiduciary who considers a Dynamic QDIA must consider what events are appropriate to trigger the reset or re-enrollment from the target date fund into the managed account fund. Factors that may be relevant include a participant’s age and retirement date. However, as stated above, other factors may be considered. See Q&A 6 for further discussion of this point.

4. Must a plan fiduciary always choose the QDIA with the lowest expense ratio, or fees?

No. As with all investment options in a plan, a plan fiduciary must carefully consider all relevant factors and not just fees when selecting a QDIA. Whether a particular investment is a prudent choice is an inherently factual question based on the facts and circumstances of the situation. ⁷ The impact of fees and expenses is merely one of many factors to be considered in selecting a QDIA.

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¹ 3 FAB 2008-03 at Q&A-16.
² ERISA § 404(a)(1)(B) and QDIA Regulation, Preamble at 72 Fed. Reg. 60453.
³ QDIA Regulation, Preamble at 72 Fed. Reg. 60453 and 29 C.F.R. § 2550.404a-1(b).
⁴ Id. at 60461 (requiring consideration of age, target retirement date, or life expectancy in selecting target date QDIA and allowing fiduciary to consider other factors); Id. at 60462 (requiring consideration of age of participant population when selecting plan wide QDIA and allowing consideration of other relevant factors); Id. at 60462 (requiring investment management service QDIA to consider age, target retirement date/plan’s normal retirement date, or life expectancy).
⁵ Id.
⁶ FAB 2008-03 at Q&A 16 (stating that “Nothing in the QDIA regulation limits the ability of a plan sponsor to use more than one QDIA, so long as all the requirements of the regulation are satisfied with respect to each QDIA.”).
⁷ 29 C.F.R. § 2550.404a-1(b).
A Dynamic QDIA path includes a transfer to a managed account. With respect to fees, the transfer will likely result in a higher expenses because a managed account typically is more customized than a target date fund. Many plan fiduciaries view a managed account investment as providing more tailored return/risk characteristics for a participant than could be achieved with a target date fund alone. Plan fiduciaries may reasonably conclude that a particular managed account could be expected to deliver better results on a net of fee basis over a reasonable period of time or that a particular managed account is an appropriate approach to managing downside risk as the participant nears retirement age. Thus, a plan fiduciary may conclude that the benefits of a managed account offset the additional fees. The DOL recognizes that whether a particular investment option is a prudent choice is a fiduciary determination that must be based on the facts and circumstances of the individual situation.

5. What changes to participant communication and disclosures should be considered from an ERISA perspective for a plan fiduciary to gain the protection available for QDIA investments? From an ERISA perspective, in the context of a Dynamic QDIA, is any specific communication required before a participant is transferred from one QDIA to the other?

The disclosure requirements are the same for all types of QDIs. To qualify for relief under the QDIA Regulation, a fiduciary must give a specific notice at least 30 days in advance of the first investment in any QDIA and annually thereafter. The initial investment in the target date fund, and the transfer to the managed account, are each separate QDIA notice events. Generally, that advance notice must describe the circumstances under which contributions and accounts will be invested in a QDIA, the investment objectives of the QDIA, and the right to direct investments out of the QDIA.

Plan sponsors should determine if the plan documents should be amended to implement a Dynamic QDIA and the ongoing resets that will take place under a Dynamic QDIA. Also, participant-facing documents, including the summary plan description, should be updated to describe the circumstances under which the reset will take place.

Low engagement rates are an inherent characteristic of default investment vehicles like a QDIA, because default investment vehicles are for participants who are not actively engaged in directing their own investments. Therefore, in addition to meeting the QDIA notice requirements under the QDIA Regulation and amending relevant plan documents, we recommend reaching out to participants in multiple ways to ensure that the concept of the Dynamic QDIA is well communicated. Additional and alternative communications might include, for example, emails or a telephone call as a participant approaches the event that will trigger the transfer from one QDIA to another. These additional communications ensure that the participant has the opportunity to opt out. Further, if properly tailored, these communications can increase the likelihood that a participant will understand the features of his or her new managed account and take maximum advantage of those features.

Empower Retirement/Great-West Investments may be able to help you meet the notice requirements. You should also review these and other QDIA requirements with your counsel.

10 This is a general discussion of the QDIA notice requirements in 29 C.F.R. §2550.404c-5. Please refer to the regulations for specific information on how to comply with the notice and other requirements for relief.
6. What should a fiduciary consider in selecting the event that will trigger a move into a managed account?

Identifying the pool of plan participants positioned to receive the greatest benefit from a managed account is a helpful step to determining the appropriate trigger for the managed account reset. Accordingly, fiduciaries should consider their plan demographics when selecting one or more trigger events.

Age is commonly used as a trigger for changing investment characteristics and as such may be the criterion a fiduciary prefers. Considerations a fiduciary may weigh in determining an appropriate trigger for the move to a managed account will depend on the facts and circumstances. The following may be relevant:

- Participants who are within fifteen to twenty years of the normal retirement date may benefit from a managed account due to diverging circumstances such as plans to retire early or to keep working, health status, savings, and other obligations — particularly if the managed account takes these factors into account in investment allocation. Some or all relevant factors, such as age, deferral rate, projected retirement age, and accumulated balance may be readily available from the recordkeeping system.

- Participants who have significant assets available for retirement outside of the plan may benefit from a managed account that considers those assets to achieve an overall balanced portfolio. A plan sponsor may identify these participants based on income, tenure, or even account balance within the plan.

7. What other steps should a fiduciary take in selecting a trigger?

A fiduciary should document a prudent process to determine that a transfer to a managed account is appropriate for the transferred population. Documenting that decision process would include recording the due diligence (such as research and evaluation) and fiduciary deliberations given to factors such as the investment manager’s qualifications, the manager’s track record and investment methodology, the investment objectives and risk/return characteristics of the managed account profile, and any other pertinent characteristics of the managed account. The record should also document the due diligence and fiduciary deliberation given to selecting the appropriate criteria that will trigger a move to a managed account (such as those set forth above). This does not mean that the fiduciary must undertake to determine whether the managed account is the most prudent QDIA for a particular group of participants in the plan.11 The fiduciary must, however, determine that the QDIA is appropriate for that group of participants.

8. Can you describe a plan reset/re-enrollment and why it might be in the best interest of plan participants? Why might this concept also apply when a plan maps participants into a managed account as a result of changing recordkeepers?

A plan reset/re-enrollment event results in the directed investment of every account in a plan — either by the participants themselves or by a QDIA default. A reset encourages and reminds participants and beneficiaries to consider and refresh stale investment directions — that is, to actively manage their accounts. Participants who do not respond to the QDIA notices are defaulted to a QDIA with an appropriate mix of return and capital preservation.

QDIA relief also benefits participants in “mapping” situations. “Mapping” occurs when an existing investment option under the plan is discontinued — either as a result of the elimination of a single fund or a comprehensive change in investment line-up.12 Amounts invested in the discontinued investment option are defaulted to a QDIA if participants fail to provide investment direction after an appropriate QDIA notice.

In both reset/re-enrollment and mapping cases, participants and beneficiaries who are not actively monitoring their investments may not have investment directions that are appropriate under current circumstances. Participants and beneficiaries who fail to respond to the QDIA notice will have their investments “reset” to a QDIA which may be more appropriate to their circumstances. When a move to a QDIA results in an investment that is more appropriate for a participant given his or her age or retirement date, etc., the participant should benefit over the long term. Of course, a fiduciary must meet the requirements of the QDIA Regulation to obtain relief.

9. What fiduciary relief would a plan fiduciary receive using this approach?

If the conditions of the QDIA Regulation are met, the participant is treated as having exercised control over the defaulted investment direction to the QDIA. As a result, the fiduciary will not be liable for the investment outcomes that occur as a result of the direction of the amounts to the QDIA. A plan fiduciary remains obligated, however, to prudently select and monitor a QDIA alternative in accordance with ERISA’s general fiduciary rules.

10. What other steps must a plan fiduciary take when implementing a Dynamic QDIA?

QDIA relief is conditioned, in part, upon providing appropriate notice to participants and beneficiaries. A plan administrator should already have procedures to identify participants and beneficiaries who do not have current addresses on file.13 If a plan administrator does not have these procedures in place, now is a good time to consider adopting and implementing such procedures. That way, if a participant who is defaulted to a QDIA later claims he or she did not receive the notice at his or her current address, the plan administrator will have documentation of the efforts to locate missing participants and beneficiaries.

CONCLUSION

The Dynamic QDIA is an innovative default investment fund strategy that should prove to be beneficial to participants as they near retirement. The strategy defaults participants who are in the early or middle stages of their careers into a target date fund QDIA. As those participants age, typically their resources and obligations become more divergent from one participant to another. As those resources, obligations, and objectives diverge, those participants are transferred into managed account QDIA that provides a more tailored investment approach. Provided that the conditions of the QDIA Regulation are met, the path from the target date fund QDIA to the managed account QDIA may be treated as a reset/or re-enrollment triggered by a certain event, such as reaching age 45 or 50.

12 QDIA relief under ERISA § 404(c)(5) and is available both to the selection of plan investments for which participants fail to give directions (such as initial investments or resets) and to changes in investment options — generally referred to as “mapping.” Mapping relief is also available under ERISA § 404(a)(4)(A) in the event of “certain qualified changes in investment options.” Under ERISA § 404(c)(4), new investments must be reasonably similar to the investments before the change. This discussion is limited to mapping relief under the QDIA rules of ERISA § 404(c)(5).

13 FAB 2004-02 provides guidance on locating missing participants and beneficiaries.
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