
Reish & Reicher Comment on TDF Proposals

By Editor Test Sun, Jul 18, 2010

"We expect that the SEC proposals will be adopted much as proposed," says Fred Reish, the well-known ERISA lawyer. But a TDF expert says plan fiduciaries should do more than merely comply with them.

Reish & Reicher, the Los Angeles law firm that specializes in employee benefits and ERISA issues, has issued a bulletin on target date funds, with comments on last month's guidance on TDFs from the Securities and Exchange Commission and the Department of Labor.

"We expect that the SEC proposals will be adopted much as proposed. We also expect that the DOL's checklist and QDIA amendments will be consistent with the Bulletin and the SEC proposals," the bulletin, from Fred Reish (pictured at left) and his associates, said.

"The initial effect should be to educate plan sponsors and participants about asset allocation, glide paths and target date differences. We believe the long-term effect will be that plan sponsors and advisers will focus on the needs and characteristics of the covered workforce and the design differences of TDFs."

Reish and Reicher recommended that plan sponsors protect themselves by asking:

- Is the TDF line-up designed to be aggressive, moderate or conservative? Is that appropriate for the particular workforce?
- Is it appropriate if most participants are defaulted (*e.g.*, an automatically enrolled plan)?
- Does the glide path go "to retirement" or "through retirement?"
- If "through retirement," are the participants aware that the plan sponsor made that decision for them?

"From a legal perspective, the critical point is that fiduciaries need to engage in a prudent—and documented—process to make each of those decisions. A prudent process can produce a range of acceptable decisions. The failure to engage in a prudent process is a fiduciary breach," the attorneys said.

The SEC's Proposals

In summarizing the government's proposals for remedying the issues associated with target date funds, Reish & Reisher wrote:

- The SEC's proposal would require marketing materials for a target date fund that includes the target date in its name to disclose the asset allocation of the fund among types of investments.
- The types of investments—such as equity securities, fixed income securities, or cash—would need to appear with the fund's name the first time the fund's name is used.
- The SEC's proposal would require target date marketing materials to include a prominent table, chart, or graph that clearly depicts the asset allocations among types of investments over the entire

life of the fund.

- These proposals would also require a statement:
 - Explaining that asset allocation changes over time.
 - Noting the asset allocation eventually becomes final and stops changing.
 - Stating the number of years after the target date at which the asset allocation becomes final.
 - Providing the final asset allocation.
- The SEC's proposal would require target date marketing materials to include a statement informing the investor:
 - To consider the investor's risk tolerance, personal circumstances, and complete financial situation.
 - That an investment in the fund is not guaranteed and it is possible to lose money by investing in the fund, including at and after the target date.
 - Whether, and the extent to which, the intended percentage allocations may be modified without a shareholder vote.
 - In addition, funds would be required to add a statement in their marketing materials warning that the funds come with risks and should not be chosen based solely on investors' retirement dates.
- Further, the proposal would amend the commission's antifraud guidance to state that marketing statements suggesting that investments can be chosen based on a single factor or that investments are simple and require no monitoring can be misleading.

Another perspective

Ron Surz, president of PPCA Inc. and Target Date Solutions in San Clemente, Calif., who has written about target date funds for this publication, commented in recent days on the Reish & Reicher bulletin. He suggested that, for fiduciaries, merely complying with proposed SEC guidelines won't necessarily be enough to fulfill their responsibility to participants.

"Much of [the bulletin] reads as if the regulators think plan participants are choosing target date funds, but they're not. Even those who are not defaulted into target date funds do not really choose from among the various available target date funds. Their choice is limited to the funds that the sponsors make available to them, and this choice is, it would seem, typically made out of convenience," Surz wrote in an email to *R/IJ* and others.

"Fred's concluding remarks, advocating a prudent process, assume the best from fiduciaries, which is the right thing to do although I think it's more complicated than that.

"Here's what I think is going on... TDFs are a Qualified Default Investment Alternative (QDIA). Plan sponsors think any QDIA is a safe harbor, so they're all good—regulatory prudence. Or if they are concerned about picking a particular TDF, how can they go wrong with the name brands everyone else uses, like Fidelity, T. Rowe & Vanguard—procedural prudence. Also, *Plan Sponsor* magazine has determined that most plan sponsors base their TDF selection on their advisor's recommendation—delegated prudence.

“But at the highest level either plan sponsors, or their consultants, but preferably both, need to care about substantive prudence—picking the best. Regulatory checklists and required fund disclosures may give fiduciaries pause and should encourage substantive prudence. In other words a prudent process will hopefully lead to enlightenment, but the process alone is no guarantee.”

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