

DOL Issues RFI on Use of Brokerage Windows

On August 20, 2014, the DOL issued a Request for Information as part of its review of the use of brokerage windows in participant-directed individual account plans covered by ERISA. The stated purpose of the RFI is to increase the DOL's understanding of the prevalence and role of brokerage windows in these plans. The DOL is seeking information to determine what regulatory standards or guidance may be necessary to protect participant savings. The goal is to ensure participants are not exposed to undue risk and that fiduciaries understand the scope of their responsibilities when brokerage windows are part of the investment platform.

Background

Brokerage windows, including self-directed brokerage accounts or similar arrangements, allow participants to select investments beyond those specifically selected and monitored by the plan fiduciary. Plans generally offer brokerage windows in addition to a core set of investments to provide access to a broader set of investment vehicles than otherwise made available through the plan. Brokerage windows, and their expanded access, may be particularly attractive to the sophisticated investor.

As clarified in ERISA 404(a)(5) and subsequent questions and answers from the DOL, brokerage windows are not "designated investment alternatives" (DIAs) and not subject to the annual disclosure requirements. Rather, the plan fiduciary need only provide a description of the arrangement and a summary of the fees and expenses that may be charged to the individual's account (e.g., annual fees, brokerage fees, or commissions). In addition, participants must be furnished a statement of the dollar amount of the fees and expenses charged to their accounts in connection with the arrangement during the previous quarter.

The DOL's concern about brokerage options in qualified plans has been apparent for some time. On May 7, 2012, the DOL issued [Field Assistance Bulletin \(FAB\) 2012-02](#). The bulletin provided question-and-answer guidance on the final regulations for participant-level retirement plan fee disclosure. Q&A 30, which discussed brokerage platforms and windows, introduced a new interpretation of the obligations associated with offering a brokerage window that served to raise additional questions about the implications of offering such arrangements. Q&A 30 stated that, even if the plan fiduciary selected multiple DIAs as plan options, "if, through a



brokerage window or similar arrangement, non-designated investment alternatives available under a plan are selected by significant numbers of participants and beneficiaries, an affirmative obligation arises on the part of the plan fiduciary to examine these alternatives and determine whether one or more such alternatives should be treated as designated for purposes of the regulation.” “Designating” an investment alternative used in a brokerage window could require a plan fiduciary to give it the same level of oversight given to the core options under the plan. The DOL suggested that as few as five participants in a small plan, or 1% of the population in a plan that covered more than 500 participants, could trigger such treatment.

Comment. The DOL seems to have a particular concern about the use of non-designated investment alternatives as the exclusive means of investing in a plan to avoid any fiduciary or reporting obligations.

Q&A 30 generated concerns not only about the fee disclosure regulations, and how best to comply in situations where a brokerage window is offered to plan participants, but also about the fiduciary liability associated with offering such products. In response to concerns by employers and trade organizations, on July 30, 2012, the DOL issued [FAB 2012-2R](#), replacing Q&A 30 with a new Q&A 39. The replacement question eliminated the concept of a “safe harbor” and references to “an affirmative obligation” to determine whether popular investments in a brokerage window should be treated as DIAs. Instead, Q&A 39 confirmed that a brokerage window, self-directed brokerage account, or similar arrangement is not a DIA and whether an investment alternative is a DIA will depend on whether it is specifically identified as available under the plan. (See our [July 31, 2012 For Your Information](#).) Furthermore, fiduciaries of plans with such arrangements are still bound by ERISA's statutory duties of prudence and loyalty, including taking into account the nature and quality of services provided in connection with the arrangement. Although the revised FAB was a welcome relief, there was much speculation that the topic of brokerage windows would arise again.

Questions Presented in RFI

39 Questions

The DOL is seeking information to determine if additional regulatory standards or guidance may be necessary to protect participant savings.

The DOL has issued a [Request for Information](#) (RFI) comprised of 39 questions aimed at increasing its understanding of how many plans include brokerage windows in the investment lineup and how they are utilized. The DOL's objectives are to determine if participants are exposed to unnecessary risks and to ensure that plan fiduciaries understand their responsibilities. Based on the information collected from the RFI, the DOL will assess whether and to what extent additional guidance may be needed to protect participants' retirement savings. The RFI covers ten categories that focus on different aspects of brokerage windows. Respondents may choose to answer all or only some of the questions.

Defining “Brokerage Windows” — Scope

Brokerage windows vary in the number of investment options — hundreds or thousands of funds — and types of funds — stock funds, exchange-traded funds and other securities — offered to participants. The questions here focus on the most common arrangements and their benefits and drawbacks. The questions ask if any forthcoming guidance should be different depending on how a brokerage window is structured.

Plan Investment Offerings — Brokerage Windows and Designated Investment Alternatives

Next, the DOL questions what type of plan typically offers brokerage windows and whether the number of windows has been increasing or decreasing. The DOL is looking to see if there is a correlation between changes in the

number of DIAs offered by plans and changes in the number of plans offering brokerage windows. As a plan decreases the number of DIAs offered, is it more likely to add a brokerage window, or vice versa?

Participation in Brokerage Windows

The questions in this section look at brokerage window utilization statistics. Topics covered include the number of participants and the percentage of plan assets invested through the brokerage window, the percentage of assets in the window by participant, and any restrictions on the amount that can be invested. There is also a question about the demographic attributes of the participants who utilize the window.

Comment. The last questions in this section address the quality of decisions by, and outcomes from, participants using the window. One question seeks information on whether participants who do not invest in the brokerage window benefit from having the option in the plan. It is not clear what data is available to plan sponsors or providers to answer these questions.

Selecting and Monitoring Brokerage Windows and Service Providers

The DOL is interested in learning why plan sponsors add brokerage windows and how the vendor selection process works once the decision is made to implement a brokerage window. Specifically, are plan sponsors limited to the brokerage service affiliated with the recordkeeper or can they choose from several vendors, what challenges do they face, and are plan fiduciaries concerned about their responsibilities in this process? Several questions touch on the contractual details of brokerage window arrangements. As with several of the other sections, it seems that some of the questions are more targeted to service providers than to plan sponsors and fiduciaries.

DOL Wants to Know

How are plan fiduciaries monitoring the investments in the brokerage window? What are the costs and challenges involved? Is more guidance needed?

Fiduciary Access to Information about Brokerage Window Investments

Once the brokerage window is available to participants, how are plan fiduciaries monitoring the investments? Questions address the level of information available to plan fiduciaries, challenges in compiling information to monitor investments, and the costs associated with doing so.

Brokerage Window Costs

Qualified plans are permitted to charge fees to participants if the plan can show that expenses are reasonable. Other than situations where employers pay for recordkeeping costs outside the plan, participants generally pay for recordkeeping services through revenue sharing, annual fixed dollar fees, or fees based on asset size. When computing asset-based fees, the account balances of the brokerage window may or may not be considered. One then wonders whether the plan costs for participants in brokerage windows are being subsidized by core investments.

This section asks who pays for the brokerage window — participants, plan, or plan sponsor, to what extent the costs are subsidized by other participants, and how the costs of the brokerage window compare to the costs of other investments both inside and outside the plan. While service providers must disclose their fees to plan fiduciaries, the question here is how plan fiduciaries are evaluating and monitoring fees such as commissions and costs that generally cannot be controlled by participants.

Disclosure Concerning Brokerage Windows and Underlying Investments

Ensuring participants have sufficient information to make informed decisions about investing has always been a DOL concern. This section of the questionnaire addresses the adequacy of disclosure to participants — who should provide the information and whether more information should be provided to participants using the brokerage windows. A recent report by the US Government Accountability Office (GAO) recommended that the DOL consider requiring disclosure of performance and benchmarking information to plan sponsors and participants for managed accounts. The DOL asks if the suggested disclosure would be advisable for participants accessing managed accounts through brokerage windows.

Comment. Among the questions in this section, the DOL asks if “these disclosures regarding how the brokerage window differs from the plan’s designated investment alternatives typically include a description of the different risks and costs of investing through a brokerage window compared to investing in a designated investment alternative.” This question seems to encapsulate the line of thinking that may have driven the preparation of this RFI.

Role of Advisers

The next questions address how often plan fiduciaries use advisers in selecting the brokerage window and whether and how participants use advisers for investment selection. The RFI asks whether fiduciaries make advisers available to participants. If no advisers are made available, do participants actively seek out advisers for assistance and, if so, how often?

Comment. It isn’t clear how a fiduciary would know if a participant chose to seek assistance from an outside adviser.

Fiduciary Duties

Field Assistance Bulletins 2012-02 and 2012-02R confirmed that brokerage windows are not DIAs and do not require the extensive disclosure required of core investments in qualified plans. There is concern, however, that plan fiduciaries choosing to offer a brokerage window may need additional guidance to be in compliance with section 404(c). This section of the RFI focuses on whether there is a need for guidance on brokerage windows under ERISA’s fiduciary provisions and if not, why not.

Annual Reporting and Periodic Pension Benefit Statements

Plans that include a brokerage window are identified by the use of code 2R on line 8a of the Form 5500. A choice is available when completing Schedule H of the form to either split out the investments by the individual asset classes or combine them in the “other” category. The DOL asks if this provision should be expanded to require more detail and transparency around investments made through brokerage windows and, if so, what the cost and administrative burden would be for providing the additional information.

The participant fee disclosure regulations require quarterly benefit statements detailing transactions and costs for core investments and only mandate limited information for investments in brokerage funds. The last question asks how participant statements currently reflect brokerage window account balances.

In Closing

Brokerage windows are typically implemented for, and most used by, savvy investors and/or those using financial advisors. Investing in this type of vehicle puts the onus on employees to develop their own strategy and monitor

investments. For those willing to take on the extra responsibility and work, the brokerage window brings access to thousands of mutual funds, stocks, exchange-traded funds, and perhaps the opportunity for greater returns.

Based on some of the questions asked in the RFI, it appears that the DOL is particularly concerned about plan designs without any DIAs, in which the brokerage window is used as a means of skirting the disclosure rules. It is anticipated that the DOL will ultimately issue fiduciary guidelines and may impose limitations on the use of brokerage windows as an investment vehicle. Any guidance issued will likely introduce notices and other requirements that will increase the administrative burden and costs associated with administering brokerage windows.

Responses to the RFI are due by November 19, 2014 — instructions for submission are detailed in the RFI.

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