

Comment Letter Regarding Small Pension Plan Security Proposal, February 2000

By Hand Delivery

February 7, 2000

Mr. John Keene
Office of Regulations and Interpretations
Room N-5669
Pension and Welfare Benefits Administration
U.S. Department of Labor
200 Constitution Avenue, NW
Washington, D.C. 20210

Re: Small Pension Plan Security Proposal

Dear Mr. Keene:

The Investment Company Institute¹ appreciates the opportunity to provide comments on the Department of Labor's proposed regulations on the small pension plan security amendments (RIN 1210-AA73) published in the Federal Register on December 1, 1999. Mutual fund companies are very active in the small plan market, providing both investment and plan administration services to such pension plans. Therefore, the mutual fund industry is interested in regulatory changes related to small pension plan administration.

The Institute commends the Department for its efforts to improve small plan security without imposing undue administrative burdens and costs on small employers. As the Department is aware, small employers are quite sensitive to these concerns. We further support the Department's efforts to assure that plan participants are able to obtain sufficient information about the investments of plan assets.

In general, the Institute supports the Department's proposal. We recommend, however, two changes. First, "qualifying plan assets" should include assets for which registered transfer agents maintain records. Second, the annual audit requirement should be waived for small pension plans whose participants and beneficiaries receive investment account statements, at least quarterly, directly from an independent qualifying plan recordkeeper, such as a financial institution or recordkeeping entity. Finally, in response to a request for comment, the Department should not require small pension plans to make available to participants and beneficiaries a schedule of plan assets similar to that required under Form 5500 for plans with 100 or more participants. Each of these points is discussed below.

I. Registered Transfer Agents

The proposed regulations would waive the annual audit requirement for small pension plans if at least 95% of plan assets are "qualifying plan assets" or if the person handling non-qualifying plan assets is bonded in an amount representing the value of the non-qualifying plan assets, and if the plan complies with certain disclosure and notice requirements. The proposed regulations use two categories to define "qualifying plan assets." The first category lists two types of assets that would be deemed "qualifying plan assets"—qualifying employer securities and qualifying plan loans. The second category defines "qualifying plan assets" as those assets held by certain types of organizations, including banks, insurance companies, registered broker-dealers and organizations authorized to act as a trustee under section 408 of the Internal Revenue Code.

It appears that the Department intended to include investments in mutual funds in the definition of "qualifying plan assets." Indeed, mutual funds are cited in the preamble to the proposed regulations.² We are nonetheless concerned that the proposed regulations

do not explicitly include investments in mutual funds in either of the two categories defining "qualifying plan assets," nor are they necessarily included indirectly.

Specifically, although some mutual funds (or affiliated trust companies) may be authorized to act as a section 408 trustee, not all are.³ Moreover, many small employer plans are "self-trusted." In these cases, the mutual fund company provides only investment services and/or other plan administrative services, including plan recordkeeping.⁴ In circumstances where the mutual fund complex does not act as trustee or custodian, it generally utilizes an entity that is not necessarily authorized to act as trustee under section 408 of the Code, such as a registered transfer agent, to process and record the small plan's transactional activity.

To assure that plan assets invested in mutual funds are deemed "qualifying plan assets" in circumstances where the mutual fund complex acts as trustee for the plan and in circumstances where it does not, we recommend that the Department add "registered transfer agents" to the list of institutions included in the definition of "qualifying plan assets." Specifically, we recommend that the proposed regulations be modified by inserting as a new §2520.104-46(b)(1)(ii)(D), the following language: "or, (D) Any assets for which a registered transfer agent maintains records."

By adding "assets for which a registered transfer agent maintains records" to the definition of "qualifying plan assets," the Department would make it clear that such investments would be deemed to be qualifying plan assets under the proposed regulations, i.e., counted toward the 95% plan asset test, whether or not the mutual fund complex provides trust or custodial services to the small pension plan. In addition, it is our understanding that, for purposes of the regulations, the Department intends to include institutions that are regulated, either by the federal government or by the states. Because registered transfer agents are regulated by the Securities and Exchange Commission, such entities would satisfy the Department's criterion of including only regulated entities in the regulation.⁵

II. Waiver for Plans in Which Participants Receive Quarterly Account Investment Statements Directly From a Qualifying Plan Recordkeeper

As noted above, one of the conditions for small pension plans to waive the annual audit requirement under the proposed regulations is that the plan is in compliance with certain disclosure and notice requirements. We recommend that the Department also waive the annual audit requirement for small plans if such plans' participants and beneficiaries regularly receive account statements from an independent service provider. By contracting with a third party service provider to provide plan participants and beneficiaries with regular investment account statements, small pension plan sponsors could sufficiently ensure the security and accountability of plan assets.

Plan participants and beneficiaries who receive such disclosure at least every quarter would be able to efficiently and effectively track the contributions, distributions, earnings/losses and expenses related to their individual accounts, thus furthering the Department's goal of enhanced plan asset security. As the Department stated in the preamble to the proposed regulations, "...[W]ell informed participants and beneficiaries are often in the best position to be watchdogs over their own pension plans and can catch problems early." Participants with access to quarterly statements reflecting changes in their accounts would effectively enable them to monitor their own retirement savings.

In order to implement this recommendation, the Department should modify the proposed regulations by adding as new §2520.104-46(b)(1)(i)(A)(3) the following: or, (3) the plan's participants and beneficiaries receive, directly from an independent qualifying plan recordkeeper, an investment account statement, at least once every quarter, reflecting investment and other transactional activity in the participants' or beneficiaries' account." The Department should make it clear that this provision would be satisfied if the independent qualifying plan recordkeeper either delivers quarterly statements to participants in paper form or provides participants with electronic access to their individual account information at least quarterly via "800" numbers, automated voice response systems, website access and other similar technologies. In such cases, the Department should require that participants with electronic access to their account information via phone or the web be provided notice of such access and instructions on how to access such information. The purpose of this provision is to waive the audit requirement for plans whose participants receive or can access their account information on a regular basis. Therefore, the Department should ensure that the provision is sufficiently flexible to accommodate communication of account information using current and anticipated future technologies.

To maintain consistency within the regulation, the Department could define "qualifying plan recordkeeper" by referencing the entities already included in the proposed regulations' definition of "qualifying plan assets," §2520.104-46(b)(1)(ii), including banks, insurance companies, broker-dealers, those organizations authorized under section 408 of the Code to act as a trustee and registered transfer agents.

III. Requiring Small Plan Sponsors to File Schedules Similar to Those

Required Under Form 5500 For Large Plan Sponsors

In Section E of the proposed regulations, the Department requests comments on whether it should require small plans to "make available to participants and beneficiaries a schedule of the plan's assets held for investment purposes as of the end of the plan year similar to the schedule currently required as part of the Form 5500 annual report filed by pension plans with 100 or more participants." Currently, small pension plans are not required to file such schedules for Form 5500 purposes. The Institute believes that the disclosure requirements described in §2520.104-46(b)(1)(i)(B) of the proposed regulations would be sufficient to help ensure the security and accountability of small plan assets. Requiring small plan sponsors to prepare a schedule of plan assets similar to those filed by large plan sponsors for Form 5500 purposes is unlikely to provide sufficient additional benefits to plan participants and beneficiaries to justify the extra administrative cost and burden to the small plan sponsor of preparing such a schedule.

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If you have any questions or comments concerning our suggested modifications to the proposed regulations, please call me at (202) 218-3563 or Russ Galer at (202) 326-5835. In addition, we would like to schedule a meeting with representatives of the Department to further discuss our comments on the Department's small plan asset security proposal in the near future.

Sincerely,

Kathryn A. Ricard
Associate Counsel

cc: Robert Doyle
Joe Canary

ENDNOTES

¹ The Investment Company Institute is the national association of the American investment company industry. Its membership includes 8,018 open-end investment companies ("mutual funds"), 495 closed-end investment companies, and 8 sponsors of unit investment trusts. Its mutual fund members have assets of about \$6.802 trillion, accounting for approximately 95% of total industry assets, and over 78.7 million individual shareholders.

² The preamble states, "[I]n general, the Department believes that statements of plan assets prepared by certain regulated financial institutions (such as banks, insurance companies, mutual funds, and securities broker-dealers), if made available to participants and beneficiaries, provide a means by which participants and beneficiaries can independently confirm that the assets reported by the plan to be available to pay benefits as of the end of the plan year were, in fact, available according to the books and records of the institution holding the assets. Fed. Reg., Vol. 64, No. 230 pg. 67437 (December 1, 1999).

³ Many mutual funds engage an independent entity, such as an unaffiliated bank, to serve as IRA trustee or custodian.

⁴ In addition, we note that the proposed regulations do not address situations where an entity is authorized to act as custodian, and not a trustee, for a small pension plan. We believe the Department should modify the proposed regulations to include custodial arrangements in addition to trust arrangements.

⁵ Registered transfer agents are regulated by the Securities and Exchange Commission under section 17A of the Securities and Exchange Act of 1934, and the rules thereunder.