Questions and Answers of the Department of Labor for JCEB Technical Session on May 7, 2003

The following questions and answers are based on informal discussions between private-sector representatives of the Joint Committee on Employee Benefits (JCEB) and Department of Labor (DoL) officials. The questions were submitted by ABA members and the responses were given at a meeting of JCEB and government representatives. The responses reflect the unofficial, individual views of the government participants as of the time of the discussion, and do not necessarily represent agency policy. This report on the discussions was prepared by designated JCEB representatives, based on the notes and recollections of the JCEB representatives at the meeting, and has been reviewed by Labor Department staff who were at the meeting. The questions were submitted in advance to the agency, and it was understood that this report would be made available to the public.

QUESTION 1.

Under the prior claims procedure regulation, if there was a failure to respond in a timely manner, the claim was deemed denied. Under current 29 C.F.R. § 2560.503-1(e), if there is a failure to follow a reasonable claims procedure (which would include failing to respond in a timely manner), "a claimant shall be deemed to have exhausted the administrative remedies available…." Does deemed exhausted also mean deemed denied?

PROPOSED/SUGGESTED ANSWER 1.

No. Deemed denied means that the participant must go to the next level of appeal, if there is one, because the appeals procedures need to be exhausted before a participant can proceed to court, unless one of the exceptions to exhaustion is applicable. Deemed exhausted means that the participant can proceed directly to court.

DEPARTMENT OF LABOR ANSWER 1.

Staff agreed with the answer. The 1977 regulation "deeming" rule was designed to allow a participant to move to a later stage in the claims procedure process. Conversely, the new regulation "deeming" rule is designed to allow participants to get out of the ERISA claims process. For further details, *see* the DOL referenced Claim Procedure FAQ 11 on the DOL web site (http://www.dol.gov/ebsa/faqs/faq_claims_proc_reg.html).

QUESTION 2.

Would the standard of review be de novo? (Note, in some circuits, de novo review means a review of the administrative record without any deference. *E.g.*, *Perry v. Simplicity Engineering*, 900 F.2d 963 (6th Cir. 1990). In other circuits, de novo review is not limited to the administrative record. *E.g.*, *Moon v. American Home Assurance Co*., 888 F.2d 86, 89 (11th Cir. 1989)). Would the review be limited to the administrative record?

PROPOSED/SUGGESTED ANSWER 2.

The standard of review would be de novo, because there would be no decision by a fiduciary for the court to review. Whether the review is limited to the administrative record depends upon the facts and circumstances of the particular case. In other words, if the participant has made a complete submission to the plan fiduciary, and the participant is awaiting a decision, when the time period for decision-making runs, the participant would not be entitled to add to the administrative record. On the other hand, if the plan administrator refuses to make the appeals procedure available to a participant, then the administrative record could be supplemented, because the participant had been prevented otherwise from making that record.

DEPARTMENT OF LABOR ANSWER 2.

The question deals with the standard of review and the scope of the administrative record in court proceedings. The ERISA claims procedure regulation does not address this.

The ERISA claims procedure process (including appeals within that process) is governed by the claims regulations. This question deals with the standards applied in court. This question addresses a court rule, not the claims procedure. Staff is inclined to agree that in court the standard may depend upon facts and circumstances, but the Staff does not have an answer to the precise question. This is a matter left to the courts.

Staff suggested watching whether the Supreme Court grants *certiorari* in cases that permit it to resolve any perceived circuit conflict such as in *Regula v. Delta Family Care*, 266 F.3d 1130 (9th Cir. 2001).

QUESTION 3.

An employee retires and receives plan benefits; another employee leaves the employee of the same employer and has a break in service. Sometime after the employee retires and the other employee has a break in service, the plan is amended to provide that new employees starting will have a lower accrual rate. The employees, who retired and who had a break in service, return to work for this employer. Is it a cut-back to apply the lower accrual rate to the employee who has retired or the employee who returns after a break in service?

PROPOSED/SUGGESTED ANSWER 3.

No. It is not a cut-back to apply the lower accrual rate to either employee, as long as the lower accrual rate is not applied to any service earned prior to the retirement, the break in service, and/or the later of the date the amendment is adopted or effective.

DEPARTMENT OF LABOR ANSWER 3.

Staff declined to answer this question, stating that this was within the jurisdiction of the IRS.

QUESTION 4.

Field Assistance Bulletin 2002-2 seems to give multiemployer plan trustees a choice as to whether certain acts are settlor or fiduciary functions. Doesn't ERISA's functional test for fiduciary status make such a choice inconsistent with the statute?

PROPOSED/SUGGESTED ANSWER 4.

No. In Field Assistance Bulletin 2002-2, Staff explained, that "where relevant documents (e.g., collective bargaining agreements, trust documents, and plan documents) contemplate that the board of trustees of a multiemployer plan will act as fiduciaries in carrying out activities which would otherwise be settlor in nature, such activities would be governed by the fiduciary provisions of ERISA." That the documents create a measure of the standards for performing the function does not convert the function from that of a settlor to that of a fiduciary. Thus, even if a traditional settlor function will be measured by fiduciary standards (due to the language in a plan's governing documents), costs associated with that settlor function could not be paid for from plan assets.

DEPARTMENT OF LABOR ANSWER 4.

The Question and Proposed Answer reveal a basic misconception about the Field Assistance Bulletin. Multiemployer plan trustees do not have a "choice" as to whether they act in a settlor or fiduciary capacity. They are or are not acting in a fiduciary capacity depending upon the function they are performing. Nevertheless, the Field Assistance Bulletin clarifies that a trustee may perform settlor functions and be held to a fiduciary standard if the plan documents so state. If a trustee does perform a settlor function as a fiduciary, plan assets can be used to pay for that function.

QUESTION 5.

Why doesn't the claims procedure regulation expressly recognize that the provisions prohibiting the use of final and binding arbitration does not apply to Railway Labor Act-governed plans?

PROPOSED/SUGGESTED ANSWER 5.

This will be the subject of a technical correction to the regulation.

DEPARTMENT OF LABOR ANSWER 5.

Staff disagreed with the proposed answer, stating no technical correction is needed. They commented that the arbitration provisions in the claims procedure regulation do not affect the application of the rules on arbitration under the Railway Labor Act, pursuant to section 514(d) of ERISA.

QUESTION 6.

Can a retirement plan charge participants accounts (directly) the cost of issuing a check to the participant?

PROPOSED/SUGGESTED ANSWER 6.

Yes, to hold otherwise (where the plan bears the administrative costs) would produce untoward and unjust results, particularly in the case of a dwindling plan population. Basically, to hold otherwise, benefits those who quit early, as opposed to those who stay, as illustrated in the following example, where there are five participants, with one of them leaving at a time, where the cost of issuing the check to the departing participant is $72.

Participant	Actual Cost	Number of Participants	Cost Borne by Participant 5 ($72/number of participants)
1	$72	5	$14.40
2	$72	4	$18
3	$72	3	$24
4	$72	2	$36
4	$72	1	$72
Total Amount Borne by Participant 5			$169.40

Thus, if the costs must be borne by the plan, participant 5 ends up paying a total of $169.40, yet participant 1 only paid $14.40. This unequal allocation of the costs serves no rational purpose.

DEPARTMENT OF LABOR ANSWER 6.

The Department intends to publish guidance regarding this issue. Accordingly, Staff declined to respond to this question.

QUESTION 7.

Does requiring a participant to pay arbitration fees similar in amount to court filing fees unduly inhibit a claim for benefits under 29 C.F.R. § 2560.503-1(b)(3)?

PROPOSED/SUGGESTED ANSWER 7.

Yes. Requiring a participant to make any payment in order to invoke a statutory right of plan review unduly inhibits a claim for benefits under 29 C.F.R. § 2560.503-1(b)(3).

DEPARTMENT OF LABOR ANSWER 7.

Staff agreed with the proposed answer, stating that this would be a violation of (b)(3) regardless of the size of the payment. Staff noted that paragraph (b)(3) applies to claims for benefits under all ERISA covered plans, including pension plans. In addition, under paragraph (c)(3)(v) (relating to voluntary post-appeal procedures), no fee can be charged in health cases. Staff noted that paragraph (c) does not apply to pension claims.

QUESTION 8.

Is interest on delayed benefits equitable relief under section 502(a)(3) after *Knudson*?

PROPOSED/SUGGESTED ANSWER 8.

Interest on delayed benefits is equitable relief only to the extent that the interest to be paid has actually been earned by the plan on invested plan assets. Equitable relief would only allow for the disgorgement of “profits” earned on the investment of assets that would have otherwise been used to pay benefits.

DEPARTMENT OF LABOR ANSWER 8.

Interest on delayed benefits may constitute equitable relief under section 502(a)(3). The DOL's view on the availability of monetary relief under section 502(a)(3) is outlined in the DOL's *amicus* brief in *Ostler v. Oce*, which is available on the DOL web site. *See* http://www.dol.gov/sol/media/briefs/main.htm. *Knudson* is distinguishable from *Ostler* because *Ostler* involved a claim against a fiduciary and *Knudson* involved a claim against a non-fiduciary.

QUESTION 9.

Is interest on delayed benefits an implied plan benefit under 29 U.S.C. § 502(a)(1)(B)?

PROPOSED/SUGGESTED ANSWER 9.

No. *See Knudson*.

DEPARTMENT OF LABOR ANSWER 9.

No. *See Knudson*. Most courts analyze these issues under section 502(a)(3). *See*, *e.g.*, *Dunnigan v. Metropolitan Life Ins. Co*., 277 F.3d 223 (2d Cir. 2003).

QUESTION 10.

Is back pay an equitable remedy for ERISA section 510 claims after *Knudson*?

PROPOSED/SUGGESTED ANSWER 10.

No, back pay is not an equitable remedy after *Knudson*. However, the remedies under ERISA section 510 are not limited to equitable remedies.

DEPARTMENT OF LABOR ANSWER 10.

This question is similar to Question and Answer 8. See the DOL's *amicus* brief in *Ostler v. Océ*, available at the DOL's website at http://www.dol.gov/sol/media/briefs/main.htm.

QUESTION 11.

When must Summary Plan Descriptions ("SPDs") be revised to reflect the change in the name of the PWBA to the EBSA?

PROPOSED/SUGGESTED ANSWER 11.

The next time SPDs are required to be updated.

DEPARTMENT OF LABOR ANSWER 11.

Staff felt that the suggested answer was basically right, subject to some caveats. First, if the plan's schedule for updating SPDs would provide an updated SPD before the date established under the law, the plan should reflect the new name in its next update and not wait until the required date. Second, if a copy of the SPD must be provided before the scheduled update because, for example, a participant or beneficiary requested it, the SPD provided must show the correct EBSA name, even if it is done using only a "sticker" or a hand-written correction on the text.

QUESTION 12.

The claims procedure regulation allows for, in the case of a post-service claim under a group health plan, up to a 15-day extension of the 30-day time limit to respond to an initial claim (Regulation section 2560.503-1(f)(2)(iii)). If the claimant is required to provide missing information, the claimant must be given at least 45 days to provide it. If the plan notifies the claimant on day 5 that it is taking a 15-day extension because it requires further information from the claimant and the claimant responds on day 10, when is the response due?

PROPOSED/SUGGESTED ANSWER 12.

The response should be due on day 50, which is the initial 30 day response period, plus the fifteen day extension, less the five-day period during which the participant provided additional information.

DEPARTMENT OF LABOR ANSWER 12.

Staff disagreed with the proposed answer. When the plan takes an extension to review the claim, the plan has 15 days to review the claim after the missing information is received by the plan. Therefore, in this case, the plan's response is due on day 25, even though that is before the end of the initial response period if no extension had been taken. This is the position taken in the FAQs posted on the EBSA website. *See* http://www.dol.gov/gov/ebsa/faqs/faq_claims_proc_reg.html.

In response to follow-up questions, Staff indicated that they presumed when missing information was requested that the plan had all other information needed and would be prepared to render a decision shortly after receiving the missing information. Staff had not contemplated that the plan might identify early in the process that one key piece of information was missing and request that data while continuing to review the file, possibly identifying other information needed at a later date. Staff also said that, if the plan asked for additional information but did not request an extension, the plan's response period would not be tolled while the plan waited for the additional information, because that is not the way the claims regulations are structured. Staff was asked whether the plan could request the missing information on day 5 and later request an extension, if the extension was later determined to be necessary. Staff reaction was that this approach probably would not be precluded by the regulation, subject to the rules in paragraph (b)(3), but staff preferred to give this question more consideration before providing a definitive response.

QUESTION 13.

Is qualified military service counted as service under a qualified plan for eligibility purposes?

PROPOSED/SUGGESTED ANSWER 13.

No, and the Department's website should be corrected to clarify this issue. The Department's website states that "an employee who would have become eligible to participate in a pension plan during that individual's time in the service should be placed in the plan retroactive to the date of initial eligibility." This suggests that an employee who has 975 hours of service for an employer plus two weeks of reserve duty would satisfy a 1,000 hour eligibility requirement.

In contrast, the statute provides that (i) an employee can't have a break in service due to military service, and (ii) military service counts for vesting and benefit accrual purposes. Nothing in the statute or legislative history suggests that qualified military service must be counted as eligibility service. Also, Rev. Proc. 96-49 section 2.03 states that IRC section 414(u) requires that "the employee's military service is treated as service with the employer for vesting and benefit accrual purposes," but does not say that military service must be treated as service for eligibility purposes.

DEPARTMENT OF LABOR ANSWER 13.

Although the Uniformed Services Employment and Reemployment Rights Act ("USERRA") is in the jurisdiction of the Veterans' Employment and Training Service, EBSA understands that qualified military service would be counted for eligibility purposes. Under USERRA section 4318(a)(2)(A) a reemployed person does not incur a break in service due to qualified military service. Since qualified military service is not counted toward (and would not give rise to) a break in service, it follows that such service should be counted as service for eligibility purposes.

QUESTION 14.

Does the use of rollover proceeds to indirectly acquire a business constitute a prohibited transaction? The situation involves an individual (Executive) who establishes a new company (Newco), which adopts a 401(k) plan. Executive is the sole director and officer of Newco. Executive rolls over to the Newco 401(k) plan funds from an eligible rollover plan. Executive then elects to invest the rollover proceeds in 100% of the stock of Newco, but does not get an appraisal of Newco in connection with the purchase. Newco uses the proceeds from the sale of stock directly or indirectly to acquire a target company. Once target or target's assets are acquired, new employees associated with target's business begin making 401(k) deferrals to the Newco plan, but will not have the option to direct investment in Newco stock because the offering will have closed.

PROPOSED/SUGGESTED ANSWER 14.

No, the situation described is not a prohibited transaction because the requirements of section 408(e) of ERISA are satisfied. An appraisal of Newco stock is not necessary because the value of Newco immediately after the acquisition Newco's value will equal the amount of money paid for Newco's stock.

DEPARTMENT OF LABOR ANSWER 14.

This question, despite being specific in certain respects, did not provide sufficient facts to allow Staff to analyze the issue and provide an answer. Staff invited the questioner to submit a request for an advisory opinion.

QUESTION 15.

If a plan sponsor does not pay the plan's record keeper the contractually agreed administrative fees, can the record keeper refuse to turn over the plan records?

PROPOSED/SUGGESTED ANSWER 15.

Assuming that the record keeper is not a fiduciary of the plan, then any right of the plan to get the records would be based upon contractual obligations, not ERISA. However, arguably, the record keeper is a plan fiduciary to the extent that it exercises control over the plan's records, which are essential to the administration of the plan.

DEPARTMENT OF LABOR ANSWER 15.

Staff declined to answer the question in this forum because too many assumptions would be needed to make a complete analysis.

QUESTION 16.

Employee terminates employment with a vested deferred benefit, and the defined benefit plan distributes an annuity contract to her. The employee later marries and then is divorced. Is this annuity contract subject to the QDRO rules?

PROPOSED/SUGGESTED ANSWER 16.

Once the benefit is distributed from the plan, the QDRO rules no longer apply.

DEPARTMENT OF LABOR ANSWER 16.

Staff agrees with the proposed answer. Where a former employee's benefit has been completely distributed from a plan, a domestic relations order that addresses division of the assets already distributed is not subject to ERISA's QDRO provisions.

QUESTION 17.

Are discount vision programs (offering discounts on exams, hardware and laser surgery) offered only to employees of certain employers "welfare benefit plans?"

PROPOSED/SUGGESTED ANSWER 17.

No. This is analogous to "premium only plans" (which are a variant of cafeteria plans under I.R.C. section 125, the only function of which is to permit participants to pay contributions with pre-tax dollars). *See* Advisory Opinion 96-12A.

DEPARTMENT OF LABOR ANSWER 17.

It depends on the extent of the employer's involvement in the program. *See* 29 CFR 2510.3-1(j). For example, there would be no employee welfare benefit plan covered by Title I if the vision benefit provider unilaterally set the discount for employees of certain employers and the only employer involvement was, without endorsing the program, agreeing to allow the provider to advertise the program to employees. Staff disagreed with the proposed answer's analogy of the discount vision program to the "premium only plans" under Code section 125 as referenced in Adv. Op. 96-12A (July 17, 1996).

QUESTION 18.

Can an employer issue a single Summary Annual Report (SAR) that covers more than one tax-qualified retirement plan?

PROPOSED/SUGGESTED ANSWER 18.

Assuming that the information for each plan is clearly identified, a Summary Annual Report may cover more than one plan.

DEPARTMENT OF LABOR ANSWER 18.

A single document may include SARs for more than one plan, as long as the SAR of each plan is a separate completed copy of the prescribed SAR form, 29 CFR 2520.104b-10(d), and the format of the single document is not misleading.

QUESTION 19.

Is it necessarily inappropriate for an ESOP to retain the same valuation firm to value the stock and issue a fairness opinion as is retained by the majority shareholders for a merger of the companies sponsoring the ESOP? (Assume the valuation firm is truly independent of the company and the shareholders.)

PROPOSED/SUGGESTED ANSWER 19.

While not inappropriate per se, the fiduciaries should scrupulously examine the possible conflicts of interests that may exist prior to approving any such arrangement.

DEPARTMENT OF LABOR ANSWER 19.

Staff indicated that this question is difficult to answer as posed because of the number and type of facts needed to be examined in order to determine the actual independence of the valuation firm and the motivation of the parties. Staff noted that Code § 401(a)(28) has independence requirements separate from the conflict of interest provisions in part 4 of Title I of ERISA. Despite the supposed independence of the valuation firm, plan fiduciaries must examine closely whether the valuation firm, because it has already taken a position on the value and fairness of the transaction for the companies, is able to provide an unbiased evaluation, or whether prudence would necessitate the plan's retention of an independent fiduciary to evaluate the proposed transaction. *See*, Donovan v. Bierwirth. In addition, ESOP fiduciaries are cautioned that the plan may not assume any of the expenses for the fairness opinion or other aspects of the valuation that are settlor, as opposed to fiduciary in nature. *See* DOL Advisory Opinion 2001-01A (Jan. 18, 2001) and hypothetical examples thereunder.

QUESTION 20.

Could an investment banking firm issue a fairness opinion and an appraisal of the value of the stock to an employee benefit plan in connection with a transaction in which the investment banking firm only gets paid if the deal is actually consummated?

PROPOSED/SUGGESTED ANSWER 20.

No. The investment banking firm has an irreconcilable conflict of interest.

DEPARTMENT OF LABOR ANSWER 20.

Staff agreed with proposed answer that the investment banking firm had an irreconcilable conflict of interest.

QUESTION 21.

Would the following statute be preempted with respect to claims for benefits under an employee benefit plan? California Civil Code section 1542 provides:

> A general release does not extend to claims which the creditor does not know or suspect to exist in his favor at the time of executing the release which, if known by him, must have materially affected his settlement with the debtor.

PROPOSED/SUGGESTED ANSWER 21.

No. This statute does not "relate" to employee benefit plans in any meaningful manner.

DEPARTMENT OF LABOR ANSWER 21.

Staff declined to answer this question, but suggested reviewing the Department's *amicus* brief in the *Egelhoff* case on its website. *See* http://www.dol.gov/sol/media/briefs/main.htm.

QUESTION 22.

Can a self-funded health plan explicitly exclude benefits for expenses caused by the acts of a third party, but provide that the plan administrator, may, in its discretion, elect to advance payment for such expenses with the agreement that upon any recovery, the participant will reimburse the plan. Specifically, is this arrangement a prohibited transaction in that it could be considered a loan or an extension of credit to the participant?

PROPOSED/SUGGESTED ANSWER 22.

This would be a prohibited extension of credit.

DEPARTMENT OF LABOR ANSWER 22.

Staff agrees with the proposed answer. There have been some analogous individual exemptions in this area, although the Staff does not believe the situations are similar enough to invoke the expedited exemption procedure.

QUESTION 23.

Are plan sponsors or plan administrators or employers required to share with persons who are eligible for COBRA the actuarial data that was the basis for determining the amount of the premiums for a self-insured plan?

PROPOSED/SUGGESTED ANSWER 23.

No.

DEPARTMENT OF LABOR ANSWER 23.

Staff stated the underlying actuarial data used to calculate the COBRA premium is not required to be disclosed under ERISA sections 104(b)(2) or 104(b)(4).

QUESTION 24.

A plan receives a notice of a tax levy from the IRS for one of the Section 401(k) plan participants. Is there any fiduciary obligation to investigate the tax levy, or not?

PROPOSED/SUGGESTED ANSWER 24.

No. A fiduciary should be able to treat a tax levy the same way that it treats a Qualified

Domestic Relations Order. *See* Ad Op. 99-13A.

DEPARTMENT OF LABOR ANSWER 24.

In evaluating a tax levy, the plan may apply the same principles set forth in Adv. Op. 99-13A regarding a fiduciary's duty to investigate the validity of qualified domestic relations orders. In Adv. Op. 99-13A regarding QDROs, Staff stated, in general, that the plan administrator may rely on the validity of the QDRO unless the plan administrator has received evidence calling into question the validity of the order and whether the order was fraudulently obtained. When made aware of such evidence, the administrator must take reasonable steps to determine its credibility. If the administrator determines that the evidence is credible, the administrator must decide how best to resolve the question of the validity of the order without inappropriately spending plan assets or inappropriately involving the plan in the State domestic relations proceeding. The appropriate course of action will depend on the actual facts and circumstances of the particular case and may vary depending on the fiduciary's exercise of discretion.

QUESTION 25.

Do contributions of accrued vacation benefits or paid time off pursuant to a “leave-sharing” plan involve plan assets?

PROPOSED/SUGGESTED ANSWER 25.

Assuming that the vacation benefits or paid time off plan constitute a “payroll practice,” no plan assets issues are implicated.

DEPARTMENT OF LABOR ANSWER 25.

Staff generally agrees with the Proposed Answer. However, if the “leave-sharing” plan is a separate program, it also must constitute a payroll practice. If the “leave-sharing” plan is a Title I plan, it could, in those circumstances, involve plan assets.

QUESTION 26.

The claims procedure regulation requires an “appropriate named fiduciary” to review appeals of adverse benefit determinations under an employee benefit plan. The November 2000 amendments to the claims procedure regulation eliminated the special rule that treated an insurance company as the appropriate named fiduciary for this purpose to the extent that benefits under plan were provided or administered by the insurance company. Nevertheless, as a matter of practice, it is still common for an insurance company or HMO (or a subcontractor such as an entity that provides utilization review services) to handle all aspects of claims decision-making, without being specifically designated as a named fiduciary. It's also common for the only documentation for the plan to be the plan sponsor's contracts with the insurance company or HMO and the certificates of coverage provided to participants. If the designation of fiduciary issue is addressed at all in these documents, it's common for the plan sponsor to be designated as the named fiduciary of the plan for all purposes. The plan sponsor's actual role is usually limited to helping participants with problems they might have in filing claims or resolving claims disputes with the insurance company or HMO.

Does the Department take the position that the insurance company, HMO, or subcontractor effectively has the authority to make final claims determinations and therefore is a fiduciary of the plan? *See* 63 Fed. Reg. at 48390, 48392 note 5 (Sept. 9, 1998). If so, does the Department take the position that the insurance company, HMO, or subcontractor can be treated as the appropriate named fiduciary even if it is not specifically named as such? Or does the Department take the position that the appropriate named fiduciary is the plan administrator within the meaning of section 3(16) of ERISA if no other fiduciary is specifically named for this purpose? *See* 63 Fed. Reg. at 48392 (text). Or does the Department take the position that an appropriate named fiduciary has not been identified, and the plan is not in compliance with the claims regulations?

PROPOSED/SUGGESTED ANSWER 26.

If the insurance company, HMO, or subcontractor effectively has the authority to make claims determinations (final or otherwise), it is a fiduciary of the plan. However, unless it is specifically identified as a named fiduciary within the meaning of section 402(a)(2) of ERISA, it cannot be the appropriate named fiduciary for this purpose. If it is not specifically identified as a named fiduciary for this purpose, the appropriate named fiduciary is the named fiduciary whose authority encompasses this aspect of plan administration. Typically, this will be the plan administrator, and typically the plan administrator will be the plan sponsor. Whether the plan complies with other aspects of the claims regulations will depend upon the facts.

DEPARTMENT OF LABOR ANSWER 26.

This is a claims regulation question that will not go away. The DOL removed the 1977 regulation identification of insurance companies as “appropriate fiduciaries” because they thought it didn't add anything to the functional fiduciary principles.

The DOL did not intend to disturb established fiduciary principles when they deleted this regulatory language. The new regulation requires that appeals be decided by an appropriate named fiduciary. The person exercising discretionary authority or discretionary responsibility in making decisions on appeal, pursuant the plan’s claims procedures, is effectively a “named fiduciary,” whether the plan documents fail to state that the person is a named fiduciary or indeed a fiduciary. This principle was articulated by the Department in DOL Interpretive Bulletin 75-8 and recognized by the Supreme Court in *Varity Corp*. v. *Howe*, 116 S.Ct. 1065, 1077 (1996).

QUESTION 27.

The HIPAA privacy regulations generally allow a group health plan to share protected health information (“PHI”) with the plan sponsor only if the plan sponsor puts certain safeguards into place to protect the privacy of the information. These requirements generally do not apply if the group health plan is fully insured and the group health plan (and therefore the plan sponsor) does not create or receive PHI other than information regarding participant enrollment and certain limited “summary health information,” or if the participant authorizes the disclosure. If a plan sponsor anticipates receiving PHI from an insurance company or HMO only occasionally, in order to help a participant with a problem he or she has in filing a claim or resolving a claim dispute with the insurance company or HMO, it is easier for the plan sponsor to insist that the participant authorize the disclosure than to implement all of the safeguards otherwise required by the privacy regulations. Is such a practice permitted under the claims procedure regulation?

PROPOSED/SUGGESTED ANSWER 27.

Such a practice is permitted under the claims procedure regulations as long as participants are not entitled to appeal adverse benefit determinations to the plan sponsor as the appropriate named fiduciary. (*See* Question 26 above.) If participants are entitled to appeal adverse benefit determinations to the plan sponsor or an employee of the plan sponsor, such a practice is not permitted, because if would impermissibly interfere with that right. *See* 29 C.F.R. § 2560.503-1(b)(3) (claims procedures may not be administered in a way that unduly inhibits or hampers the initiation or processing of claims).

DEPARTMENT OF LABOR ANSWER 27.

Staff stated that this was an HHS issue, but there was no conflict with the DOL claims regulation.

QUESTION 28.

The HIPAA privacy regulations preempt state laws to the extent that they prevent a covered entity from complying with the HIPAA privacy regulations. Effectively, this means that states are free to enact laws that protect the privacy of protected health information ("PHI") to a greater extent than the HIPAA privacy regulations. However, the HIPAA privacy regulations do not interfere with the normal ERISA preemption rules. Do the ERISA preemption rules preempt state laws that impose more stringent privacy requirements on ERISA plans, plan sponsors, and plan service-providers?

PROPOSED/SUGGESTED ANSWER 28.

The Department expects that such laws generally would be preempted unless they are saved as laws regulating insurance. The HIPAA privacy regulations generally allow a group health plan to share PHI with the plan sponsor only if the PHI will be used for plan administration purposes. Therefore, state laws that are more stringent than the HIPAA privacy regulations must affect plan administration in some way. State laws that affect plan administration create a risk that a plan will have to be administered in different ways in different states and therefore typically are preempted by ERISA.

DEPARTMENT OF LABOR ANSWER 28.

The Department of Labor has not taken a position on this issue and would analyze this issue on a case by case basis.

QUESTION 29.

Under 29 C.F.R. § 2550.404c1(d)(2)(ii)(E)(4)(vi), the protection of ERISA section 404(c) is unavailable with respect to investments in employer securities unless "voting, tender and similar rights with respect to such securities are passed through to participants and beneficiaries." Plan participants are commonly given the right to direct plan fiduciaries with respect to voting on items that are scheduled to be presented to the shareholders at an annual meeting. For a variety of logistical or administrative reasons, plan participants cannot be given the right to direct voting with respect to unscheduled items that might be presented at the shareholders meeting. Rather, in even the most ideal situations, plan participants may only be allowed to choose between abstaining or delegating the right to vote on unscheduled items to a designated plan fiduciary who will cast the vote on unscheduled items in its discretion (which is not truly a "pass through").

In this context, if an unscheduled item actually comes before the shareholders meeting, is ERISA section 404(c) protection lost?

PROPOSED/SUGGESTED ANSWER 29.

No. As long as the plan passes through the vote with respect to items that are scheduled to come before the shareholders, 404(c) protection is not lost simply because, for logistical reasons, plan participants cannot be given an effective voice with respect to unscheduled items.

DEPARTMENT OF LABOR ANSWER 29.

Staff indicated that 404(c) protection is transactional. In the context of this fact situation, there would be no 404(c) relief with respect to the fiduciary's decisions (or votes) regarding the unscheduled items, but 404(c) relief would be available with respect to the voting on scheduled items. Moreover, 404(c) relief with respect to the employer stock investments in general would not be lost because of the inability to pass through the vote on unscheduled items.

QUESTION 30.

The regulations under ERISA section 404(c) include special requirements if the plan wants to extend the 404(c) defense to investments in qualifying employer securities. *See* 29 C.F.R. § 2550.404c-1(d)(2)(ii)(E)(4)(i) through (ix). Assume that the plan is a typical 401(k) plan which is an eligible individual account plan that offers seven mutual fund investment options and an employer stock fund (virtually all of the fund must be invested in employer stock that is a qualifying employer security). What is the significance of the 404(c) defense with respect to investments in employer securities, made by employee elections to invest in the employer stock fund, if the plan satisfies these special requirements and all of the other applicable requirements under the 404(c) regulations?

PROPOSED/SUGGESTED ANSWER 30.

Because the participant's investment election is an asset allocation decision that relates to diversification, 404(c) compliance is irrelevant to an investment decision with respect to an employer stock fund. ERISA section 404(a)(2) already gives the plan's investment fiduciaries a "free ride" on diversification. Moreover, 404(c) offers no protection with respect to other aspects of the prudence rules because the plan's investment fiduciaries retain the responsibility, in any case, for the prudence of making available and retaining the employer stock fund. On the other hand, 404(c) would provide a defense with respect to the participant's exercise of ancillary fiduciary functions, such as directing the voting of the employer stock.

DEPARTMENT OF LABOR ANSWER 30.

Staff disagreed with the suggestions included in the proposed answer that 404(c) relief was of little value in the context of employer stock investments. While 404(c) relief may not be needed with respect to the diversification issue, the relief is of assistance with respect to the other elements of the prudence requirements.

QUESTION 31.

Assume a typical 401(k) plan which offers participants the right to direct the investment of their accounts among eight mutual fund investment options, and assume that the plan complies with all requirements of the regulations under ERISA section 404(c) except one (although it should not matter, assume the one rule the plan does not satisfy is the requirement of 29 C.F.R. § 2550.404c-1(b)(2)(i)(B)(1)(vi)). Although the plan has not satisfied all of the requirements of the regulations under 404(c), participants are nevertheless permitted to, and do, direct the investment of their accounts. A participant becomes unhappy with his asset allocation decisions and sues the plan's investment fiduciaries for violation of the prudence rules in investing his account. Do the investment fiduciaries remain liable for investing the account because the plan did not satisfy all of the requirements of the 404(c) regulations?

If the investment fiduciaries do still remain liable, what is the standard applied to determine whether the plan's investment fiduciaries violated the prudence rules? [Note that at this point we are not determining the amount of the loss or damages, if any.] At least three approaches appear possible. (1) Look at the participant's allocation decision and attribute that decision to the fiduciaries. If the decision is prudent, the fiduciaries have been prudent. (2) Look at the participant's decision making process (if you can) and attribute that to the fiduciaries. If the process is prudent, then the fiduciaries are protected even if the resulting asset allocation decision would be one that experts would deem to be imprudent (assuming that the prudence rules admit of this possibility). (3) Look at what the fiduciaries actually did to invest the employee's account, which is nothing. Since the investment fiduciaries necessarily retained responsibility for allocating the participant's account among the investment funds, yet completely ignored that responsibility, they automatically violated the ERISA prudence rules.

PROPOSED/SUGGESTED ANSWER 31.

The investing fiduciaries cannot use 404(c) as a defense, unless all the requirements of the regulation are complied with. Consequently, the correct answer is (3). In effect, if a plan allows participants to direct the investment of their accounts, but does not satisfy all of the applicable requirements of the 404(c) regulations, then the plan's investment fiduciaries necessarily retain responsibility for any "loss" suffered by the plan as a result of the participant's direction of his account (with respect to any fund for which all of the requirements have not been satisfied). This is a strict liability standard.

DEPARTMENT OF LABOR ANSWER 31.

Staff indicated that when any of the requirements of 29 CFR 2550.404c have not been met, the defense to liability under section 404(c) is not available. Whether the plan fiduciaries are liable under section 409 of ERISA for losses to a participant based on a participant's allocation decisions would then be determined by application of the fiduciary principles in part 4 of Title I of ERISA.

QUESTION 32.

Assume a typical 401(k) plan which offers participants the right to direct the investment of their accounts among eight mutual fund investment options. Assume further that the plan complies with all requirements of the regulations under ERISA section 404(c) except the requirement of 29 C.F.R. § 2550.404c-1(b)(2)(i)(B)(*1*)(*viii*) regarding the furnishing of prospectuses. The facts are that the plan's record keeper and nonfiduciary third-party administrator is Big Mutual Fund Company ("BMC") , and five of the mutual funds offered under the plan are BMC's own mutual funds ("BMC funds"). However, the other three funds are so-called "outside funds," two of which are Small Mutual Fund Company funds ("SM funds") and one of which is a Middling Mutual Fund Company fund ("MM fund"). BMC has arrangements with SM and MM to offer their funds under plans administered by BMC.

Although in the course of doing business with SM Fund Co. and MM Fund Co., BMC receives from time to time prospectuses for the two SM funds and the MM Fund, BMC does not make a practice of furnishing such prospectuses to participants who invest in those funds. Participants make investment elections either by telephoning BMC and speaking with a live operator or using a voice response system, or by using the BMC website. After a participant makes an investment election, BMC immediately mails the participant a written confirmation of the election, and includes a prospectus for any BMC fund in which the participant has newly invested. However, neither BMC nor anyone else furnishes the participant (either immediately prior to or immediately following, hard copy or electronically) a prospectus for any SM fund or MM fund in which the participant may have newly invested. Note that the 401(k) plan's investment committee also receives copies of prospectuses for the SM funds and the BMC funds, and lets participants know they are available from the employer's human resources department at any time upon request. In addition, the H.R. department gives each employee, at the time the employee first becomes eligible to participate in the plan, a package containing then-current prospectuses for each mutual fund available as an investment option under the plan. Does 404(c) offer any protection with respect to the participant's election to invest in one of the SM funds or the MM fund under these circumstances?

PROPOSED/SUGGESTED ANSWER 32.

No, under normal circumstances. The prospectuses BMC receives for SM funds and MM funds in course of its dealings with SM Fund Co. and MM Fund Co. are deemed to be received by the plan, as are the prospectuses received by the plan's investment committee. Since these prospectuses for these funds are not automatically given to participants who newly invest in the SM funds and MM fund, the plan does not generally satisfy all of the requirements of the 404(c) regulations with respect to participants' directed investments in these funds. The only exception would be in the case of a participant who invests in one or more of these funds immediately after having received the initial package of prospectuses upon first becoming eligible to participate in the plan.

DEPARTMENT OF LABOR ANSWER 32.

In general, the staff agrees with the proposed answers that there is no 404(c) protection for the funds where the participant does not receive a prospectus.

THE PRECEDING QUESTIONS AND ANSWERS ARE BASED ON INFORMAL DISCUSSIONS BETWEEN PRIVATE-SECTOR REPRESENTATIVES OF THE JCEB AND DEPARTMENT OF LABOR OFFICIALS. THE QUESTIONS WERE SUBMITTED BY ABA MEMBERS AND THE RESPONSES WERE GIVEN AT A

MAY 7, 2003 MEETING OF JCEB AND GOVERNMENT REPRESENTATIVES. THE RESPONSES REFLECT THE UNOFFICIAL, INDIVIDUAL VIEWS OF THE GOVERNMENT PARTICIPANTS AS OF THE TIME OF THE DISCUSSION, AND DO NOT NECESSARILY REPRESENT AGENCY POLICY. THIS REPORT ON THE DISCUSSIONS WAS PREPARED BY DESIGNATED JCEB REPRESENTATIVES, BASED ON THE NOTES AND RECOLLECTIONS OF THE JCEB REPRESENTATIVES AT THE MEETING, AND HAS BEEN REVIEWED BY LABOR DEPARTMENT STAFF WHO WERE PRESENT AT THE MEETING. THE QUESTIONS WERE SUBMITTED IN ADVANCE TO THE AGENCY, AND IT WAS UNDERSTOOD THAT THIS REPORT WOULD BE MADE AVAILABLE TO THE PUBLIC.