

funding standard account it would constitute a transfer to reduce an obligation of the sponsor or employer to the plan. Therefore, in the absence of an applicable exemption, such a contribution would be prohibited under section 406(a)(1)(A) of ERISA and section 4975(c)(1)(A) of the Code. Such an in-kind contribution would constitute a prohibited transaction even if the value of the contribution is in excess of the sponsor's or employer's funding obligation for the plan year in which the contribution is made and thus is not used to reduce the plan's accumulated funding deficiency for that plan year because the contribution would result in a credit against funding obligations which might arise in the future.

(c) *Defined contribution and welfare plans.* In the context of defined contribution pension plans and welfare plans, it is the view of the Department that an in-kind contribution to a plan that reduces an obligation of a plan sponsor or employer to make a contribution measured in terms of cash amounts would constitute a prohibited transaction under section 406(a)(1)(A) of ERISA (and section 4975(c)(1)(A) of the Code) unless a statutory or administrative exemption under section 408 of ERISA (or sections 4975(c)(2) or (d) of the Code) applies. For example, if a profit sharing plan required the employer to make annual contributions "in cash or in kind" equal to a given percentage of the employer's net profits for the year, an in-kind contribution used to reduce this obligation would constitute a prohibited transaction in the absence of an exemption because the amount of the contribution obligation is measured in terms of cash amounts (a percentage of profits) even though the terms of the plan purport to permit in-kind contributions.

Conversely, a transfer of unencumbered property to a welfare benefit plan that does not relieve the sponsor or employer of any present or future obligation to make a contribution that is measured in terms of cash amounts would not constitute a prohibited transaction under section 406(a)(1)(A) of ERISA or section 4975(c)(1)(A) of the Code. The same principles apply to defined contribution plans that are not subject to the minimum funding requirements of section 302 of ERISA or section 412 of the Code. For example, where a profit sharing or stock bonus plan, by its terms, is funded solely at the discretion of the sponsoring employer, and the employer is not otherwise obligated to make a contribution measured in terms of cash amounts, a contribution of unencumbered real property would not be a prohibited sale or exchange between the plan and the employer. If, however, the same employer had made an enforceable promise to make a contribution measured in terms of cash amounts to the plan, a subsequent contribution of unencumbered real property

made to offset such an obligation would be a prohibited sale or exchange.

(d) *Fiduciary standards.* Independent of the application of the prohibited transaction provisions, fiduciaries of plans covered by part 4 of title I of ERISA must determine that acceptance of an in-kind contribution is consistent with ERISA's general standards of fiduciary conduct. It is the view of the Department that acceptance of an in-kind contribution is a fiduciary act subject to section 404 of ERISA. In this regard, sections 406(a)(1)(A) and (B) of ERISA require that fiduciaries discharge their duties to a plan solely in the interests of the participants and beneficiaries, for the exclusive purpose of providing benefits and defraying reasonable administrative expenses, and with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims. In addition, section 406(a)(1)(C) requires generally that fiduciaries diversify plan assets so as to minimize the risk of large losses. Accordingly, the fiduciaries of a plan must act "prudently," "solely in the interest" of the plan's participants and beneficiaries and with a view to the need to diversify plan assets when deciding whether to accept in-kind contributions. If accepting an in-kind contribution is not "prudent," not "solely in the interest" of the participants and beneficiaries of the plan, or would result in an improper lack of diversification of plan assets, the responsible fiduciaries of the plan would be liable for any losses resulting from such a breach of fiduciary responsibility, even if a contribution in kind does not constitute a prohibited transaction under section 406 of ERISA. In this regard, a fiduciary should consider any liabilities appurtenant to the in-kind contribution to which the plan would be exposed as a result of acceptance of the contribution.

[59 FR 66736, Dec. 28, 1994]

§ 2509.95-1 Interpretive bulletin relating to the fiduciary standards under ERISA when selecting an annuity provider for a defined benefit pension plan.

(a) *Scope.* This Interpretive Bulletin provides guidance concerning certain fiduciary standards under part 4 of title I of the Employee Retirement Income Security Act of 1974 (ERISA), 29 U.S.C. 1104-1114, applicable to the selection of an annuity provider for the purpose of benefit distributions from a defined benefit pension plan (hereafter "pension plan") when the pension plan intends to transfer liability for benefits to an annuity

provider. For guidance applicable to the selection of an annuity provider for benefit distributions from an individual account plan see 29 CFR 2550.404a-4.

(b) In General. Generally, when a pension plan purchases an annuity from an insurer as a distribution of benefits, it is intended that the plan's liability for such benefits is transferred to the annuity provider. The Department's regulation defining the term "participant covered under the plan" for certain purposes under title I of ERISA recognizes that such a transfer occurs when the annuity is issued by an insurance company licensed to do business in a State. 29 CFR 2510.3-3(d)(2)(ii). Although the regulation does not define the term "participant" or "beneficiary" for purposes of standing to bring an action under ERISA § 502(a), 29 U.S.C. 1132(a), it makes clear that the purpose of a benefit distribution annuity is to transfer the plan's liability with respect to the individual's benefits to the annuity provider.

Pursuant to ERISA section 404(a)(1), 29 U.S.C. 1104(a)(1), fiduciaries must discharge their duties with respect to the plan solely in the interest of the participants and beneficiaries. Section 404(a)(1)(A), 29 U.S.C. 1104(a)(1)(A), states that the fiduciary must act for the exclusive purpose of providing benefits to the participants and beneficiaries and defraying reasonable plan administration expenses. In addition, section 404(a)(1)(B), 29 U.S.C. 1104(a)(1)(B), requires a fiduciary to act with the care, skill, prudence and diligence under the prevailing circumstances that a prudent person acting in a like capacity and familiar with such matters would use.

(c) Selection of Annuity Providers. The selection of an annuity provider for purposes of a pension benefit distribution, whether upon separation or retirement of a participant or upon the termination of a plan, is a fiduciary decision governed by the provisions of part 4 of title I of ERISA. In discharging their obligations under section 404(a)(1), 29 U.S.C. 1104(a)(1), to act solely in the interest of participants and beneficiaries and for the exclusive purpose of providing benefits to the participants and beneficiaries as well as defraying reasonable expenses of administering the plan, fiduciaries choosing an annuity provider for the purpose of making a benefit distribution must take steps calculated to obtain the safest annuity available, unless under the circumstances it would be in the interests of participants and beneficiaries to do otherwise. In addition, the fiduciary obligation of prudence, described at section 404(a)(1)(B), 29 U.S.C. 1104(a)(1)(B), requires, at a minimum, that plan fiduciaries conduct an objective, thorough and analytical search for the purpose of identifying and selecting providers from which to purchase annuities. In conducting such a search, a fiduciary must evaluate a number of factors relating

to a potential annuity provider's claims paying ability and creditworthiness. Reliance solely on ratings provided by insurance rating services would not be sufficient to meet this requirement. In this regard, the types of factors a fiduciary should consider would include, among other things:

- (1) The quality and diversification of the annuity provider's investment portfolio;
- (2) The size of the insurer relative to the proposed contract;
- (3) The level of the insurer's capital and surplus;
- (4) The lines of business of the annuity provider and other indications of an insurer's exposure to liability;
- (5) The structure of the annuity contract and guarantees supporting the annuities, such as the use of separate accounts;
- (6) The availability of additional protection through state guaranty associations and the extent of their guarantees. Unless they possess the necessary expertise to evaluate such factors, fiduciaries would need to obtain the advice of a qualified, independent expert. A fiduciary may conclude, after conducting an appropriate search, that more than one annuity provider is able to offer the safest annuity available.

(d) Costs and Other Considerations. The Department recognizes that there are situations where it may be in the interest of the participants and beneficiaries to purchase other than the safest available annuity. Such situations may occur where the safest available annuity is only marginally safer, but disproportionately more expensive than competing annuities, and the participants and beneficiaries are likely to bear a significant portion of that increased cost. For example, where the participants in a terminating pension plan are likely to receive, in the form of increased benefits, a substantial share of the cost savings that would result from choosing a competing annuity, it may be in the interest of the participants to choose the competing annuity. It may also be in the interest of the participants and beneficiaries to choose a competing annuity of the annuity provider offering the safest available annuity is unable to demonstrate the ability to administer the payment of benefits to the participants and beneficiaries. The Department notes, however, that increased cost or other considerations could never justify putting the benefits of annuitized participants and beneficiaries at risk by purchasing an unsafe annuity.

In contrast to the above, a fiduciary's decision to purchase more risky, lower-priced annuities in order to ensure or maximize a reversion of excess assets that will be paid solely to the employer-sponsor in connection with the termination of an over-funded pension plan would violate the fiduciary's duties under ERISA to act solely in the interest of the plan participants and beneficiaries. In

such circumstances, the interests of those participants and beneficiaries who will receive annuities lies in receiving the safest annuity available and other participants and beneficiaries have no countervailing interests. The fiduciary in such circumstances must make diligent efforts to assure that the safest available annuity is purchased.

Similarly, a fiduciary may not purchase a riskier annuity solely because there are insufficient assets in a defined benefit plan to purchase a safer annuity. The fiduciary may have to condition the purchase of annuities on additional employer contributions sufficient to purchase the safest available annuity.

(e) *Conflicts of Interest.* Special care should be taken in reversion situations where fiduciaries selecting the annuity provider have an interest in the sponsoring employer which might affect their judgment and therefore create the potential for a violation of ERISA § 406(b)(1). As a practical matter, many fiduciaries have this conflict of interest and therefore will need to obtain and follow independent expert advice calculated to identify those insurers with the highest claims-paying ability willing to write the business.

[60 FR 12329, Mar. 6, 1995, as amended at 72 FR 52006, Sept. 12, 2007; 73 FR 58447, Oct. 7, 2008]

§ 2509.99-1 Interpretive Bulletin Relating to Payroll Deduction IRAs.

(a) *Scope.* This interpretive bulletin sets forth the Department of Labor's (the Department's) interpretation of section 3(2)(A) of the Employee Retirement Income Security Act of 1974, as amended, (ERISA) and 29 CFR 2510.3-2(d), as applied to payroll deduction programs established by employers¹ for the purpose of enabling employees to make voluntary contributions to individual retirement accounts or individual retirement annuities (IRAs) described in section 408(a) or (b) or section 408A of the Internal Revenue Code (the Code).

(b) *General.* It has been the Department's long-held view that an employer who simply provides employees with the opportunity for making contributions to an IRA through payroll deductions does not thereby establish a "pension plan" within the meaning of section 3 (2) (A) of ERISA. In this regard, 29 CFR 2510.3-2 (d) sets forth a safe harbor under which IRAs will not be considered to be pension plans when the conditions of the regulation are satisfied. Thus, an employer

¹The views expressed in this Interpretive Bulletin with respect to payroll deduction programs of employers are also generally applicable to dues checkoff programs of employee organizations.

may, with few constraints, provide to its employees an opportunity for saving for retirement, under terms and conditions similar to those of certain other optional payroll deduction programs, such as for automatic savings deposits or purchases of United States savings bonds, without thereby creating a pension plan under Title I of ERISA. The guidance provided herein is intended to clarify the application of the IRA safe harbor set forth at 29 CFR 2510.3-2 (d) and, thereby, facilitate the establishment of payroll deduction IRAs.

(c) *Employee communications.* (1) It is the Department's view that, so long as an employer maintains neutrality with respect to an IRA sponsor in its communications with its employees, the employer will not be considered to "endorse" an IRA payroll deduction program for purposes of 29 CFR 2510.3-2(d).² An employer may encourage its employees to save for retirement by providing

²The Department has specifically stated, in its Advisory Opinions, that an employer may demonstrate its neutrality with respect to an IRA sponsor in a variety of ways, including (but not limited to) by ensuring that any materials distributed to employees in connection with an IRA payroll deduction program clearly and prominently state, in language reasonably calculated to be understood by the average employee, that the IRA payroll deduction program is completely voluntary; that the employer does not endorse or recommend either the sponsor or the funding media; that other IRA funding media are available to employees outside the payroll deduction program; that an IRA may not be appropriate for all individuals; and that the tax consequences of contributing to an IRA through the payroll deduction program are generally the same as the consequences of contributing to an IRA outside the program. The employer would not be considered neutral, in the Department's view, to the extent that the materials distributed to employees identified the funding medium as having as one of its purposes investing in securities of the employer or its affiliates or the funding medium in fact has any significant investments in such securities. If the IRA program were a result of an agreement between the employer and an employee organization, the Department would view informational materials that identified the funding medium as having as one of its purposes investing in an investment vehicle that is designed to benefit an employee organization by providing more jobs for its members, loans to its members, or similar direct benefits (or the funding medium's actual investments in any such investment vehicles) as indicating the employee organization's involvement in the program in excess of the limitations of 29 CFR 2510.3-2 (d).