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Questionable Response

Does FAQ 39 really address the brokerage window issue?

This past summer, the Employee Retirement Income Security Act (ERISA) community breathed a collective sigh of relief upon the reversal by the Department of Labor (DOL) of the treatment of brokerage windows as "designated investment alternatives" under the participant disclosure regulation. And, while the revocation of Question 30 in Field Assistance Bulletin (FAB) 2012-02—the DOL's disastrous attempt to explain the brokerage window exception—is good news, it may not be the end of the story. (For more about Question 30, see "Ball of Confusion," *PLANSPONSOR*, August 2012.) The rescission of the guidance means that the very issue the DOL was attempting to address is left up in the air. As plan fiduciaries try to move forward, it remains unclear exactly what type of arrangement constitutes a brokerage window or other similar arrangement.

Under ERISA Sections 404(a)(5) and 408(b)(2), the DOL established the designated investment alternative, defined as "any investment alternative designated by the plan into which participants and beneficiaries may direct the investment of assets held in, or contributed to, their individual accounts, but shall not include 'brokerage windows,' 'self-directed brokerage accounts' or similar plan arrangements that enable participants and beneficiaries to select investments beyond those designated by the plan." The second part of this definition came to be known as the "brokerage window exception."

After the regulations were published, practitioners began to ask the DOL how to interpret and implement various provisions of the regulations, including the brokerage window exception.

Question 30 Revisited

In Question 30, the DOL stated that there existed an unspecified level of fiduciary duty to monitor and make disclosures about investments selected by plan participants through a brokerage window. This duty seemed to exist regardless of whether a plan fiduciary had selected and designated a reasonable number of investment alternatives in addition to an available brokerage window or offered only a brokerage window. Question 30 created a virtual firestorm of controversy, igniting an intense lobbying effort to rescind it. Less than two months later, the DOL announced that it was "modifying and replacing Question 30 with a new Question 39."

With the release of Question 39, the DOL re-established the understanding held by most ERISA practitioners prior to the release of Question 30: that a plan fiduciary has a duty to select and monitor the provider of the brokerage window but not the investment alternatives purchased by the participants through the window, and that whether an investment alternative is designated depends upon whether it is specifically identified as available under the plan. However, the department made no attempt to explain the brokerage window exception or offer any guidance as to what type of arrangement would constitute a brokerage window.

There are generally five types of arrangements used in ERISA plans that are commonly referred to as brokerage windows: 1) an open window, which allows a participant to purchase any or almost any security traded on an exchange; 2) a mutual fund window, which allows a participant to purchase any or almost any registered open-ended mutual fund; 3) a supermarket or recordkeeper window, which allows a participant to purchase any fund or security maintained in a fund supermarket or on a recordkeeper's system; 4) a fund family window, which allows a participant to purchase any mutual fund offered by an issuer; and 5) a supplemental window, which makes available a selected set of investment alternatives beyond a set of core designated investment alternatives.

It is not clear which of these arrangements would qualify for the brokerage window exception. However, the more restrictions a plan fiduciary places on the arrangement and the fewer options offered through the window, the less like a true brokerage window it will appear. It is also unclear if, by changing the question stem of Question 39 from an investment platform "consisting of" a large number of investment alternatives—none of which have been designated—to an investment platform that "includes" a brokerage window, the DOL intends for the brokerage window exception to apply only where a brokerage window is offered in addition to a platform of core designated investment alternatives.

The DOL continues to promise additional guidance about the service provider disclosure regulation. It will be interesting to see whether that set of FAQs contains another surprise.

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