

Department of Labor Permits Use of Summary Prospectus to Meet Section 404(c) Prospectus Delivery Requirements

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On September 8, the U.S. Department of Labor (the DOL) issued EBSA Field Assistance Bulletin No. 2009-3, which addresses whether a plan fiduciary may use a mutual fund's summary prospectus to satisfy its prospectus delivery obligations under regulations issued pursuant to the Employee Retirement Income Security Act (ERISA) section 404(c) (the 404(c) regulations). The DOL concluded that a Summary Prospectus may be used for this purpose.

Background

Section 404(c) of ERISA provides that, in the case of an individual account plan that permits participant-directed investments, no person that is otherwise a fiduciary shall be liable under ERISA's fiduciary rules for a loss that results solely from a participant's exercise of investment control. The 404(c) regulations require, among other things, that the participant be provided or have the opportunity to obtain sufficient information to make informed decisions about investment alternatives available under the plan.

In the case of a mutual fund investment, the 404(c) regulations provide that a participant be furnished with a copy of the most recent fund prospectus that was provided to the plan, either immediately before or immediately following the participant's initial investment in the fund. The 404(c) regulations also require that a participant be furnished (either directly or upon request) copies of, among other things, any prospectuses relating to the investment alternatives available under the plan, to the extent such information is provided to the plan.

Summary Prospectus Rule

In January 2009, the Securities and Exchange Commission (SEC) adopted amendments to its rules on mutual fund disclosure, including a new "Summary Prospectus" rule that provides an optional means for complying with the mutual fund prospectus delivery requirements. Under the Summary Prospectus rule, a person may satisfy the 404(c) regulations by sending or giving plan participants a Summary Prospectus, and by providing access to the statutory prospectus online at a specified Internet address. Mutual funds selecting this delivery option must also send a paper or electronic version of the statutory prospectus free of charge upon request.

The Summary Prospectus must include at the beginning or on the cover page, among other things, the mutual fund's name, the share classes to which the Summary Prospectus relates, and a required legend

containing an Internet address, email address, and toll-free telephone number where investors may obtain the statutory prospectus and other information free of charge. Furthermore, the Summary Prospectus must contain the key information required to appear at the beginning of the statutory prospectus, including a description of the investment objectives of the mutual fund, fee and expense information, principal investment strategies, associated risks, fund performance, investment advisers and subadvisers, purchase and sale of fund shares, and financial intermediary compensation.

Use of the Summary Prospectus to Comply with 404(c) Regulations

In the preamble to the 404(c) regulations, the DOL said that the prospectus delivery requirement is intended to ensure that participants are afforded the opportunity to review the prospectus for investments subject to prospectus delivery requirements under federal securities law. Although the DOL did not define the term “prospectus” in the 404(c) regulations, the DOL has now taken the view that the term “prospectus” encompasses the Summary Prospectus, because a Summary Prospectus includes the key information about a mutual fund that can assist plan participants in making informed investment decisions. Therefore, the DOL concluded, the delivery of a Summary Prospectus, both automatically and upon request, would satisfy the prospectus delivery requirements of the 404(c) regulations.

Observations

The DOL’s position on Summary Prospectuses is consistent with its previous view, expressed in a 2003 advisory opinion, that mutual fund profiles, an earlier type of alternative to a full statutory prospectus, could be used to satisfy the 404(c) regulations’ prospectus delivery requirements. The Summary Prospectus rule replaces the profile rule, reflecting recognition by the SEC that very few funds were using profiles. The SEC made several changes to the rules designed to address the problems that discouraged the use of profiles, so that more funds are expected to use the Summary Prospectus alternative.

Assuming funds prepare Summary Prospectuses, the ability of plan fiduciaries to deliver a Summary Prospectus in place of a full prospectus should greatly simplify and facilitate compliance with the 404(c) regulations’ prospectus delivery requirements. There have been concerns that full prospectuses are too long and unwieldy to be helpful to participants, resulting in a desire by plan fiduciaries to use simpler forms of disclosure that focus on the key information necessary to disclose to the participants, such as investment objectives, risks, and fees. The Summary Prospectus fulfills that need.

The current guidance does not address the issue of electronic delivery of prospectuses for section 404(c) purposes. Electronic delivery of the information required by section 404(c) is provided for under the terms of a 2002 DOL regulation, which permits electronic delivery to employees who have computer access at their workplaces, and to others subject to a consent requirement.

There are also prospectus delivery requirements under various DOL individual and class prohibited transaction exemptions. However, the current guidance only deals with the section 404(c) requirements.

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