U.S. Department of Labor

Employee Benefits Security Administration
Washington, D.C. 20210

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ERISA SEC.
404 and 406

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Dear Mr. DeMatties:

This is in response to your request on behalf of Citigroup Inc. and its affiliates (Citi) for the Department of Labor's views on the application of certain fiduciary responsibility provisions of Title I of the Employee Retirement Income Security Act (ERISA) to Citi's Action for Racial Equity Asset Manager Program (Racial Equity Program). The following summary is based on the materials and representations you provided and should not be treated as factual findings by the Department.

Citi's Racial Equity Program

The Racial Equity Program is a component of Citi's Action for Racial Equity (ARE). Citi states that ARE, announced in September 2020, is Citi's response to a set of social issues that it refers to as a "racial wealth gap" affecting the business environment in which Citi operates. Citi describes ARE as a comprehensive approach to increasing investment in Black-owned business, advancing racial equity practices in the financial services industry, providing greater access to banking and credit in communities of color, and expanding home ownership among Black Americans. Citi has announced more than $1 billion in strategic initiatives to help close the racial wealth gap and increase economic mobility in the United States.[1]

The Racial Equity Program involves a commitment by Citi to pay all or some portion of the investment management fees for "Diverse Managers" retained by Citi-sponsored employee benefit plans (Plans).[2] Citi's experience has been that Diverse Managers' market share lags their representation in the asset management industry for reasons unrelated to risk-adjusted returns. Citi states this underrepresentation exists even though studies show both that Diverse Managers perform as well as or better than median performers and also that diversity itself may mitigate volatility.[3] Citi's goal for the program is to help address such systematic disadvantages in the context of Citi's own employee benefit plans.

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[1] *See* https://www.citigroup.com/global/news/press-release/2020/citi-launches-more-than-1-billion-in-strategic-initiatives-to-help-close-the-racial-wealth-gap.

[2] The relevant employee benefit plans are expected to include defined benefit plans, defined contribution plans, and welfare benefit plans that hold investment assets.

[3] Knight Diversity of Asset Managers Research Series: Industry (2021), available at *https://knightfoundation.org/wp-content/uploads/2021/12/KDAM_Industry_2021.pdf*; National Association of Investment Companies, Examining the Returns 2019, The Financial Returns of Diverse Private Equity Firms, available at *https://naicpe.com/wp-content/uploads/2020/03/2019-NAIC-ExaminingTheResults-FINAL.pdf*.

Citi currently expects that an investment manager will qualify as a Diverse Manager for purposes of the program if it has a total minority/female ownership of at least a specific percentage set forth in the program, such as 50 percent. Whether any particular firm satisfies the percentage will be determined from an investment management firm database maintained by eVestment, a business unit of Nasdaq. Citi has no control, influence, or role in any aspect of that database or eVestment.[4]

Citi says the program will not apply to, and no payment of investment manager fees will be made under the program with respect to, any investment manager who is a party-in-interest under ERISA section 3(14) because of its affiliation with Citi, or in which Citi otherwise has an interest that might affect the Investment Committees' best judgment as a fiduciary or otherwise create a conflict of interest under ERISA's fiduciary and prohibited transaction provisions.

The program will involve a pre-determined aggregate amount that Citi allocates to its Plans on a plan-by-plan basis.[5] Citi intends to include conditions in the program designed to limit Citi's financial obligations under the program and to further Citi's purposes in adopting the program. Citi currently envisions a cap on the total amount available under the program, a cap on the amount available to individual Diverse Managers, a first-in-time selection mechanism to allocate amounts available under the program, and a limit on payment of incentive fees. Citi also expects that its agreement to pay for all or part of a Diverse Manager's fees will be set for a minimum of 3 years so that the respective Investment Committee can make decisions taking that duration into account. Citi further expects that modifications may be made occasionally based on Citi's experience with the program.

Citi expects to publicize the program's existence to the general public, including Citi Plan participants and beneficiaries, as part of Citi's reporting of its ARE initiatives. As such, the program may result in benefits to Citi in the sense that it may be viewed favorably by its employees, the general public, its shareholders, potential customers, business partners, and other interested parties. Citi also represents that neither ARE nor the program are designed to produce a monetary or other tangible financial benefit to Citi. Citi will not publicize any individual decisions or actions of any Investment Committee under the program, market the program to any of its customers, or otherwise take any steps intended to monetize the program.[6]

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[4] Citi states it is not affiliated with Nasdaq. The program may make use of a different database in the future, but Citi would continue not to have any control, influence, or role in any such database.

[5] Citi represents that out of the total $1 billion (or more) in strategic initiatives and business activities that ARE comprises, assets allocated to the program are expected to be immaterial for Citi as a financial accounting matter.

[6] Citi's submission states that disclosure required by law or in response to the request of any governmental inquiry would not be considered publicizing.

The Investment Committees' Selection of Investment Managers

Citi has appointed an Investment Committee for each plan involved in the program. The Investment Committees will serve as a named fiduciary within the meaning of ERISA section 402(a) with discretionary authority to manage and control their respective plan's investments.[7]

The Investment Committees' process for selecting an investment manager will involve a wide initial search of candidates based on the assets to be managed as well as certain pre-determined criteria, such as the candidates' credentials, assets under management, years in business, asset class experience, and other general factors that the Investment Committees believe are relevant considerations under applicable Department of Labor guidance.

Those manager candidates would then be filtered through a side-by-side comparison allowing for consideration of a range of factors, including proposed fees as well as historical performance, both before and net of fees. This filtering will result in a subset of candidates subject to additional diligence and comparisons. The result will be a short list of candidates to be interviewed, after which a final selection is then made by the Investment Committees. Citi says this screening process is undertaken by Investment Committee members, staff on behalf of the Investment Committees, and in certain cases the Investment Committees' third-party investment consultant acting in a fiduciary capacity pursuant to ERISA section 3(21)(A)(ii), or a combination.[8]

Citi expects that the program and related commitment to pay all or a portion of Diverse Managers' investment management fees would be factored into the process when the Investment Committees are considering proposed fees and performance as part of the side-by-side filtering process. To factor that commitment into the decision-making process, the Investment Committees would use the written program documents to determine which investment managers are eligible for the commitment, the overall amount and duration of the commitment, and the amount of the commitment available for each eligible manager.

Although Citi expects that each Investment Committee would take the program into account as one factor to consider in making investment manager selection and allocation decisions, the selection of any investment manager, including any Diverse Manager, will be made by the Investment Committees in their sole and complete discretion. The Investment Committees will be provided with a copy of this opinion of the Department along with a presentation by legal counsel serving the Committees. The presentation will include confirmation that the Investment Committees retain sole and complete discretion with respect to investment manager selection. A description of the program will be included in the Investment Committees' charters or investment policies adopted by the Investment Committees.

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[7] For purposes of this opinion, Citi intends the term "Investment Committee" to refer to the appointed named fiduciary of the applicable Plan and any fiduciary to which the named fiduciary has appropriately delegated fiduciary authority pursuant to ERISA section 402(c)(3) to select investment managers within the meaning of ERISA section 3(38).

[8] Citi did not ask for and the Department is not expressing an opinion on the sufficiency of the Investment Committees' search process as described in this letter.

Citi states it will not attempt to influence the Investment Committees in their decision-making process regarding use of the program. Citi further states that it will not consider the Investment Committees' use of the program (or lack thereof) when making any decision regarding the Investment Committees, including in the exercise of Citi's fiduciary responsibility to appoint and monitor the Investment Committees and their members. The program will not provide Citi with any rights regarding investment manager selections or allocations. The program will not mandate that the Investment Committees engage in any particular search or selection processes, and the Investment Committees will not be asked to explain program-related decisions regarding investment manager selection. There will not be numerical goals or similar requirements regarding engagement of Diverse Managers that Investment Committees must meet to receive reimbursements under the program.

Citi asked for the Department's opinion on whether: (1) Citi's activities under the Racial Equity Program are settlor functions not subject to the fiduciary requirements of ERISA, (2) the Racial Equity Program and any individual commitment under the program are financial factors a prudent fiduciary could consider among others in selecting an asset manager, and (3) the disclosure of the Racial Equity Program or any payment of fees under the program would result in ERISA section 404(c) being unavailable to an otherwise eligible plan. The Department's opinions on these three issues are set forth below.

Issue 1: Will Citi become a fiduciary with respect to the selection of investment managers under the Plans by reason of establishing the Racial Equity Program or by making payments to a Diverse Manager or reimbursing a Plan for a Diverse Manager's fee pursuant to its program commitments?

ERISA requires fiduciaries with respect to a covered plan to comply with strict fiduciary standards in the performance of their plan duties. ERISA section 3(21) defines the term "fiduciary" to include, among others, any person who has or exercises discretionary authority or control in the administration or management of an employee benefit plan or its assets. The Department has long recognized there is a class of discretionary so-called "settlor" activities that relate to the formation, rather than the management, of plans. These functions include decisions relating to the establishment, design, and termination of plans and, except in the context of multiemployer plans, generally are not fiduciary activities governed by ERISA.[9]

In the context of "settlor" functions, the Department has addressed the discretion enjoyed by plan sponsors in determining, as a matter of plan design, the extent to which reasonable plan expenses are to be paid by the plan or the plan sponsor.[10] Plan sponsor decisions on plan document provisions governing whether and under what circumstances the sponsor will pay fees and

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[9] *See* Advisory Opinion 2003-04A("[While] such decisions may be settlor functions, activities undertaken to implement the decisions generally are fiduciary in nature and must be carried out in accordance with the fiduciary responsibility provisions."). *See also* Advisory Opinion 2001-01A; Information Letter to Kirk F. Maldonado from Elliot I. Daniel (March 2, 1987); Information Letter to John N. Erlenborn from Dennis M. Kass (March 13, 1986).

[10] *See* Advisory Opinion 97-03A ("If the plan document provides that the employer will pay any of such expenses, and if the employer has reserved the right to amend the plan document, ERISA would not prevent the employer . . . from amending the plan to require, prospectively, that the relevant expenses be paid by the plan."). *See also* DOL Guidance on Settlor v. Plan Expenses (Jan. 18, 2001), n. 5, at www.dol.gov/agencies/ebsa.

expenses that could otherwise appropriately be paid by the Plan are settlor decisions not subject to ERISA fiduciary standards.

Accordingly, based on Citi's representations regarding the program, the Department would not view Citi as a fiduciary with respect to the selection of investment managers under the Plans solely by reason of establishing the program or by paying or reimbursing the Plans for Diverse Managers' fees pursuant to its program commitments and in accordance with plan documents. The Department's opinion in this respect is based on the program as described by Citi and does not address the circumstances in which Citi's involvement is different from or exceeds the role described in this letter.

Further, Citi is responsible for the selection and monitoring of Investment Committee members as Plan fiduciaries. Citi is a fiduciary with respect to that exercise of discretionary authority or control regarding the management of the Plan.[11] Although Citi represents that an Investment Committee's use of the program will not impact Citi's decisions regarding selection and monitoring of Investment Committee members, whether Citi's actions in this regard are consistent with ERISA's fiduciary standards involves questions that are inherently factual. Pursuant to section 5.01 of ERISA Procedure 76-1, the Department ordinarily does not issue opinions on such matters, and this letter should not be read as expressing any view on those issues.

Issue 2: Will the Investment Committees be deemed to have violated ERISA sections 403, 404 or 406, by reason of taking Citi's fee payment commitment into account in decisions regarding the selection of or allocation of investment assets to a Diverse Manager?

ERISA section 403(c)(1) provides, subject to certain exceptions not here relevant, that the assets of an employee benefit plan shall never inure to the benefit of any employer and shall be held for the exclusive purpose of providing benefits to participants and beneficiaries and defraying reasonable expenses of administering the plan.

ERISA section 404(a)(1)(A) requires that plan fiduciaries discharge their duties to the plan solely in the interest of the participants and beneficiaries and for the exclusive purpose of providing them benefits and defraying reasonable expenses of administering the plan. ERISA section 404(a)(1)(B) requires fiduciaries to discharge their duties to a plan 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 with like aims.

ERISA section 406(b) provides that plan fiduciaries shall not: (1) deal with the assets of the plan in their own interest or for their own account, (2) in their individual or in any other capacity act in any transaction involving the plan on behalf of a party whose interests are adverse to the interests of the plan or the interests of its participants or beneficiaries, or (3) receive any

[11] Interpretive Bulletin 75-8, D-4.

consideration for their own personal account from any party dealing with such plan in connection with a transaction involving the assets of the plan.

Further, as explained in regulation 29 CFR 2550.408b-2(e)(1), if a fiduciary uses the authority, control, or responsibility that makes them a fiduciary to cause the plan to enter into a transaction involving the provision of services when such fiduciary has an interest in the transaction that may affect the exercise of their best judgment as a fiduciary, a transaction described in section 406(b) of ERISA would occur. The Department treats that transaction as a separate transaction from the transaction involving the provision of services and it would not be exempted by section 408(b)(2) of ERISA.[12]

The selection of a plan investment manager is an exercise of discretionary authority with respect to the management and administration of the plan within the meaning of ERISA section 3(21), and, therefore, is subject to ERISA's fiduciary responsibility standards and prohibited transaction provisions. In selecting a service provider, including investment managers, ERISA section 404 requires a fiduciary to engage in an objective process designed to elicit information necessary to assess the service provider's qualifications, the quality of the services offered, and the reasonableness of the fees in light of the services provided.[13]

The Department has stated that plan fiduciaries must fully understand a service provider arrangement, including the quality and the cost of the services and any associated risks, before entering into the arrangement. In addition, the selection process should be designed to avoid self-dealing, conflicts of interest, or other improper influence. The fiduciary should not consider any one factor, such as the lowest bid for services, to the exclusion of any other relevant factor, such as the quality of the services.

Subject to those principles and based on Citi's representations about the program, in the Department's view, the Investment Committees' members will not violate their fiduciary duties under ERISA section 403(c)(1) or 404 solely by virtue of considering as one factor in the selection process that an investment manager's fees otherwise payable by the Plan will be reduced or paid in full by Citi under the program.[14] Rather, the Department would view appropriate consideration of the program and any commitments under it as another relevant

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[12] ERISA section 406(a)(1)(C) and (D) prohibit a fiduciary with respect to a plan from causing a plan to engage in a transaction which the fiduciary knows or should know constitutes a direct or indirect furnishing of goods, services, or facilities between a plan and a party in interest; or transfer to, or use by or for the benefit of, a party in interest, of any assets of the plan. ERISA section 408(b)(2) exempts from the prohibitions of section 406(a) any contract or reasonable arrangement with a party in interest, including a fiduciary, for office space, or legal, accounting or other services necessary for the establishment or operation of the plan, if no more than reasonable compensation is paid therefor. The Department's regulations clarify the terms "necessary service" (29 CFR 2550.408b-2(b)), "reasonable contract or arrangement" (29 CFR 2550 .408b-2(c)), and "reasonable compensation" (29 CFR 2550.408b-2(d) and 2550.408c-2) as used in section 408(b)(2). Whether the conditions of ERISA section 408(b)(2) are met in this case involves questions that are inherently factual in nature, upon which the Department generally will not opine.

[13] *See* Information Letter to Diana Orantes Ceresi from Bette J. Briggs (Feb. 19, 1998); Information Letter to Theodore Konshak from Bette J. Briggs (Dec. 1, 1997).

[14] Under each Plan, reasonable costs, fees, and expenses incurred in connection with the administration and operation of the Plan are permitted to be paid from Plan assets.

financial factor in evaluating the fees to be incurred by the Plan in choosing among investment managers.

Further, the fact that Citi may pay a portion of the Diverse Manager's fee would not, in and of itself, create an adversity of interests that would result in the Investment Committees violating ERISA section 406(b)(2).[15] The Department also would not view the Investment Committees' members' best judgment as fiduciaries as being influenced merely because they were aware of the program's potential for generating reputational benefits to Citi.[16] However, it would be inconsistent with the duties and prohibitions of ERISA sections 403, 404 and 406 for Investment Committee members to exercise their fiduciary authority for the purpose of advancing Citi's corporate public policy goals. Determining whether Investment Committee members satisfy their fiduciary duties and obligations in any particular instance ultimately would depend on an evaluation of the relevant facts and circumstances.

In that regard, it is important to emphasize that this letter should not be read as expressing the view that it is inconsistent with ERISA's fiduciary standards for an Investment Committee to ever consider diversity, equity, and inclusion factors as material to the merits of choosing a particular investment manager from a financial perspective.[17] Citi did not ask for an opinion on that subject, and this letter does not address the issue. Similarly, this letter should not be read as expressing the view that a program like the one described in this letter is required for a fiduciary to select a diverse manager.

Issue 3: Will the inclusion of information regarding the Racial Equity Program and payment of fees under the program in disclosures required under 29 CFR 2550.404c-1 result in ERISA section 404(c) being unavailable to an otherwise eligible plan?

Citi asked the Department to confirm that certain disclosures regarding the program's existence and payment of fees under the program are allowed under 29 CFR 2550.404c-1(b)(2)(B)(2) and will not constitute "improper influence by a plan fiduciary or the plan sponsor" with respect to participants' or beneficiaries' exercise of independent control for purposes of 29 CFR 2550.404c-1(c)(2)(i).

Citi states that a Plan may offer a "private label fund" for which the respective Investment Committee may select the investment manager. In such a case, the Investment Committee will calculate the total annual operating expenses (*e.g.,* expense ratio) for the fund in accordance with the Department's regulation at 29 CFR 2550.404a-5(h)(5) without regard to Citi's commitment to pay all or part of a Diverse Manager's fee (*i.e.,* treating the commitment as analogous to a form of reimbursement). Citi expects that the expense ratio reflecting Citi's commitment to pay

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[15] *See* Advisory Opinion 83-44A.

[16] *See generally* Letter to William B. Posner from Robert J. Doyle (Sept. 8, 1989) (an investment conferring a non-economic benefit on an IRA owner best characterized as a feeling of psychic well-being will not give rise to a transfer of assets to or use of plan assets by or for the benefit of the IRA owner); Advisory Opinion 2000-10A("[A] violation of section 4975(c)(1)(D) or (E) will not occur merely because the fiduciary derives some incidental benefit from a transaction involving IRA assets."); Lockheed Corp. v. Spink, 517 U.S. 882 (1996).

[17] *See e.g.,* Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights, 87 Fed. Reg. 73822, 73859, 73867-73869 (December 1, 2022)(regulation codified at 29 CFR 2550.404a-1).

some or all of an investment manager's fee pursuant to the program will also be included in the disclosure along with a statement explaining Citi's commitment to reimburse all or a portion of the investment manager's fees.

ERISA section 404(c) provides conditional relief from certain provisions of Part 4 of Title I of ERISA for fiduciaries of a pension plan that permits participants and beneficiaries to exercise control over the assets in their individual accounts.[18] The Department's implementing regulation at 29 CFR 2550.404c-1(b)(2) describes the circumstances under which a plan provides a participant or beneficiary an opportunity to exercise control over assets in their account. Among other things, pursuant to subparagraph 2550.404c-1(b)(2)(B)(2), an identified plan fiduciary (or a person or persons designated by the plan fiduciary to act on their behalf) must provide the participant or beneficiary with the disclosures required by regulation 29 CFR 2550.404a-5. Further, section 2550.404c-1(c)(2)(i) provides that a participant's or beneficiary's exercise of control is not independent in fact if, among other conditions, the participant or beneficiary is subjected to improper influence by a plan fiduciary or the plan sponsor with respect to the transaction.

Paragraph (d)(1)(iv)(A)(2) of 29 CFR 2550.404a-5 requires disclosure of the total annual operating expenses of the investment alternative expressed as a percentage (*e.g.,* expense ratio), calculated in accordance with paragraph (h)(5) of the regulation. Paragraph (h)(5)(ii) of the regulation requires the calculation of total annual operating expenses before any waivers or reimbursements. However, paragraph (d)(2)(ii) of 29 CFR 2550.404a-5 states that nothing in the regulation precludes a plan administrator from including additional information that the plan administrator determines appropriate for comparisons of investment alternatives, provided such information is not inaccurate or misleading.

[18] Section 404(c) does not relieve a fiduciary from the duty to prudently select and monitor designated investment alternatives offered under the plan. *See* 29 CFR 2550.404c-1(d)(2)(iv). *See also* Hughes v. Northwestern University, 142 S. Ct. 737, 742 (2022) ("[E]ven in a defined-contribution plan where participants choose their investments, plan fiduciaries are required to conduct their own independent evaluation to determine which investments may be prudently included in the plan's menu of options.").

In the Department's view, the treatment of the investment manager's fee in the calculation and disclosure of the fund's total annual operating expenses as described above would not fail to meet 29 CFR 2550.404c-1(b)(2)(B)(2). Further, the disclosure of the program's existence and payments under the program as described above would not, in the Department's view, result in "improper influence" by the Investment Committees or Citi for purposes of subparagraph (c)(2)(i) of 29 CFR 2550.404c-1.[19]

This letter constitutes an advisory opinion under ERISA Procedure 76-1. Accordingly, it is issued subject to the provisions of that procedure, including section 10 thereof, relating to the effect of advisory opinions. This opinion relates solely to the application of the provisions of Title I of ERISA addressed in this letter.

Sincerely,

Karen Lloyd
Chief, Division of Fiduciary Interpretations
Office of Regulations and Interpretations

[19] You also seek confirmation that the disclosures described above would satisfy the 404(c) regulation to the extent the Department views the program's existence as a "material non-public fact" for purposes of 29 CFR 2550.404c-1(c)(2)(ii). In light of the foregoing discussion of the public nature of the program, the Department would not consider the program's existence to be a non-public fact for purposes of the 404(c) regulation.