"Advancing Your Investments"
NEW ENGLAND PENSION CONSULTANTS

November 13, 2006

Office of Regulations and Interpretations
Employee Benefits Security Administration
Room N-5669
U.S. Department of Labor
200 Constitution Avenue, N.W.
Washington, DC 20210

Attention: Default Investment Regulation

Dear Ladies and Gentlemen:

New England Pension Consultants, Inc. ("NEPC") is pleased to submit the following comments regarding the proposed regulation relating to Default Investment Alternatives for Participant Directed Individual Account Plans (the "Proposed Regulation"). The Proposed Regulation was published in notice form in the Federal Register on September 27, 2006 (the "Notice"). See Fed. Reg. Doc. 06-8282. The Notice states that comments must be received by November 13, 2006.

NEPC respectfully requests that the Department reconsider its requirement that a QDIA be managed by either an investment manager as defined in ERISA 3(38) of the Act or by an investment company registered under the Investment Company Act of 1940. We believe the definition of QDIA should be expanded to include custom-tailored investment options that are "managed" by the Authorized Plan Fiduciary.

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NEPC is one of the largest independent investment consulting firms with over 250 retainer clients overseeing over $250 billion in assets, including both defined benefit and defined contribution plans subject to ERISA, as well as foundations, endowments and other institutional investors. NEPC applauds the issuance of the Proposed Regulation, in particular, the recognition that it is appropriate to take a participant's age into account in developing a "qualified default investment alternative" ("QDIA"). However, NEPC is concerned that the Proposed Regulation will limit the ability of a plan sponsor or other responsible plan fiduciary (hereinafter referred to as the "Authorized Plan Fiduciary") to access the expertise of unbiased investment advisors who have historically provided retirement plan guidance. Moreover, under the Proposed Regulation, Authorized Plan Fiduciaries and plan participants will likely incur higher fees to ensure fiduciary compliance and in some instances could actually be denied access to better-managed investment options. These consequences will diminish the Authorized Plan Fiduciary's ability to offer participants the most appropriate investment solutions.

I. Background

Historically, defined benefit plans have served as the primary retirement vehicle for American workers. Authorized Plan Fiduciaries have traditionally turned to the investment consulting community to help manage plan assets and ensure that sufficient funds are available to meet pension obligations. Based upon the Annual Report of Pension Fund Consultants 2005 conducted by Thompson Financial, the 20 largest investment consulting firms advise on approximately $11 trillion in aggregate assets. The investment consulting community has been and continues to be responsible for the provision of informed advice to plan sponsors regarding the selection and review of investment managers and the development of appropriate asset allocation strategies.

Importantly, independent investment consultants such as NEPC are unbiased when providing investment advice. Such investment consultants are unwed to proprietary investment products and are incented only to offer investment solutions that are in the best interests of plan participants. Such independent investment consultants are employed to propose “best in class” investment managers that are complementary to one another and asset allocation solutions that optimize the trade-offs between risk and return. Moreover, consultants such as NEPC accept their role as fiduciaries providing investment advice to the plan within the meaning of ERISA.

As defined contribution plans have grown in popularity, Authorized Plan Fiduciaries have increasingly turned to the investment consulting community for investment advice. Investment consultants such as NEPC help select and review investment managers and offer investments with appropriate asset allocation strategies to help participants save properly for retirement. For many years, Authorized Plan Fiduciaries have made use of custom pre-mixed portfolios consisting of the existing core funds within the plan. These strategies have been designed to leverage the same principles that have been employed in defined benefit plans. Authorized Plan Fiduciaries have looked for ways to “DBify” their defined contribution plans in order to provide participants with the best opportunity to save adequately for retirement at risk levels appropriate to their demographic circumstances. Several of the principles employed to create custom strategies using DB plan techniques have included:

- Tailoring of asset allocation strategies for specific participant populations
- Use of best in class investments
- Inclusion of both active and passive strategies
- Use of non-mutual fund vehicles to leverage economies of scale and reduce fees

Use of these principles has allowed Authorized Plan Fiduciaries to create superior target date or lifecycle products. While several investment management firms offer high quality packaged mutual fund products, money managers, as a matter of product design, are biased to include their own proprietary products. Given this fact, investment managers are likely to include only those products in their families of funds regardless of the suitability of alternative products. In practice, no single mutual fund group claims to offer the best investment product in every asset class and few, if any, mutual fund groups offer every asset class an Authorized Plan Fiduciary might desire to include in an ideal target date offering. Specific Comments on the Proposed Regulation

A. The Definition of a QDIA is too Restrictive.

Paragraph (e)(3) of the Proposed Regulation requires that a QDIA must either (i) be managed by an investment manager as defined in Section 3(38) of ERISA or (ii) be an investment company registered under the 40 Act (a "mutual fund"). In the preamble to the Proposed Regulation, the Department indicates that this requirement is based on its belief that, when plan fiduciaries are relieved of liability for underlying investment management/asset allocation decisions, "those responsible for the investment management/asset allocation decisions must be investment professionals who acknowledge their fiduciary responsibilities and liability under ERISA" or, alternatively, the plan's assets must be invested in a vehicle that is subject to alternative Federal and State regulation and oversight (i.e., a mutual fund).

NEPC agrees that the types of investment vehicles that meet the current definition of QDIA in the Proposed Regulation are appropriate subjects of the safe harbor relief provided by the Proposed Regulation. For the reasons discussed herein, NEPC respectfully submits that the definition of QDIA be expanded to include custom-tailored investment options "managed" by the Authorized Plan Fiduciary. NEPC's position stems from the current practice of many Authorized Plan Fiduciaries, to structure and operate one or more investment options under a participant-directed plan that consist of multiple collective or separately managed accounts ("institutional vehicles") and/or multiple mutual funds (such investment options are hereinafter referred to as "custom-tailored investment options") that are available as direct investment options under the plan.   In these cases, the Authorized Plan Fiduciary will work with its investment consultant to select a mix of institutional vehicles/mutual funds and develop asset allocation strategies for a series of target date funds or a series of lifestyle investments targeting specific demographic populations.

These investment options operate in exactly the same manner as a QDIA under the Proposed Regulation except that they are "managed" by the Authorized Plan Fiduciary, rather than by an investment manager. NEPC believes that allowing an Authorized Plan Fiduciary to utilize such custom-tailored investment options as QDIAs under the plan is both desirable and preferable because of the numerous benefits offered by custom-tailored investment solutions.

NEPC further submits that allowing such an alternative approach would be protective of the interests of the plan and its participants as long as the conditions set forth below are satisfied.

The potential benefits to be achieved by use of such a custom-tailored investment vehicle include the following:

1. An expanded QDIA definition will promote inclusion of "best in class" investments. An Authorized Plan Fiduciary, working with its independent investment consultant, structures and maintains a custom-tailored investment option, and has the flexibility to "mix and match" to utilize the "best in class" mutual funds and investment managers. Moreover, the Authorized Plan Fiduciary will typically consider the inclusion of institutional vehicles to lower overall investment expenses and make appropriate use of both active and passive strategies. By contrast, in many cases, the type of investment vehicle that will qualify as a QDIA under the Proposed Regulation will invest all of its assets in mutual funds that are sponsored by a single financial services organization.

2. An expanded QDIA definition will prevent unnecessary layers of fees. The need to hire an "investment manager" to assume full fiduciary responsibility for the operation of a QDIA is likely to give rise to a greater cost than the cost of a non-discretionary, independent investment consultant who would work with the Authorized Plan Fiduciary to structure and operate a comparable custom-tailored investment option. In addition, as noted above many of the so-called package products would invest all of the QDIA's assets in mutual funds which, as a general rule, bear higher expense ratios than institutional vehicles.

3. An expanded QDIA definition will allow the Authorized Plan Fiduciary to avoid disruption to the plan and continue an existing best practice – inclusion of custom-tailored investment options. Under the Proposed Regulation, in order to achieve the safe harbor, such a Plan Fiduciary would be required either to convert its existing investment options into QDIAs (as defined in the Proposed Regulation) or to establish additional investment options that qualify under the restrictive definition of a QDIA set forth in the Proposed Regulation. Changing investment options within a defined contribution plan can often involve additional costs and will require communication of the change to participants. As a result, either action will likely impose additional costs and burdens on the plan. Such actions may also create confusion and disruption from the perspective of the plan participants.

4. An expanded QDIA definition offers participants greater protection. If, in order to achieve the safe harbor provided by the Proposed Regulation, the Authorized Plan Fiduciary is required to engage, and delegate full investment discretion with respect to

the QDIA to, an investment manager, the Authorized Plan Fiduciary's liability will be limited to the prudence of its investment manager selection and retention decisions. By contrast, under the custom-tailored investment option approach, the Authorized Plan Fiduciary remains fully liable and responsible as an ERISA fiduciary for both the asset allocation and the institutional vehicle/mutual fund selection and retention decisions undertaken in connection with the structuring and operation of the investment option. Most would agree that larger plan sponsors combined with the fiduciary coverage of their consultant advisers offers more robust coverage than a single investment manager.

5. An expanded QDIA definition is consistent with the Authorized Plan Fiduciary's responsibility to prudently select and monitor the QDIA option. As written, the QDIA investment manager guidance undermines ERISA's terms in that it requires a level of fiduciary oversight but places ultimate control of investment decisions in the hands of the required investment manager. The proposed rule should not undermine the employer's fiduciary oversight of the qualified plan investment process. Plan sponsors should have the ability to determine the investment allocation and manage the funds in the QDIA.

To further reinforce the degree of comfort sought by the Department in the Proposed Regulation, NEPC proposes incorporating the following conditions on the availability of QDIA status for an investment option that is managed by an Authorized Plan Fiduciary:

1. The Authorized Plan Fiduciary must receive ongoing, non-discretionary investment advice from a "qualified investment consultant." A "qualified investment consultant" would be defined to be a registered investment adviser under the Investment Advisers Act of 1940, a bank or an insurance company (all within the meaning of Section 3(38)) who has acknowledged in writing that it is acting as an ERISA fiduciary with respect to the plan in providing such investment advice to the Authorized Plan Fiduciary.

2. The qualified investment consultant must be engaged on an ongoing basis by the Authorized Plan Fiduciary and be responsible for monitoring all of the institutional vehicles/mutual funds that comprise each QDIA and making recommendations to the Authorized Plan Fiduciary for any changes it believes are necessary with respect to both the identity of any such institutional vehicles/mutual funds or the allocation of the QDIA's assets among them.

3. On at least an annual basis, the qualified investment consultant must prepare and submit to the Authorized Plan Fiduciary a written report summarizing its review and recommendations with respect to the retention or replacement of each institutional vehicle or mutual fund in the QDIA as well as its recommendations

as to any reallocation of the assets of the QDIA among such institutional vehicles and mutual funds.

4. All of the assets of the QDIA must be invested in (i) institutional vehicles that are managed by an entity that qualifies as an "investment manager" within the meaning of Section 3(38) of ERISA and/or (ii) mutual funds.

5. The qualified investment consultant must be independent of all institutional vehicles and mutual funds in the QDIA.

B. The Requirement that a QDIA must be Managed should be Clarified.

Under the Proposed Regulation a QDIA (other than a mutual fund) must be "managed" by an investment manager. Lifecycle or blended funds may consist of a mix and match of the direct investment options (e.g., mutual funds) that have already been selected by the Authorized Plan Fiduciary. Moreover, the investment manager of each core option is already the manager of its particular fund. In the event that the Department does not agree with NEPC's position, we respectfully ask for greater clarification of the investment manager definition. If custom-tailored investment options are offered, it seems plausible that the investment manager's required oversight could be limited to the determination of the offering's asset allocation or glide path. Limiting the responsibility of the investment manager to the glide path or asset allocation would prevent redundant layers of fiduciary responsibility. The removal of duplicative efforts and responsibility would also serve to limit the escalation of costs of offering custom-tailored investment solutions and thereby make such an approach somewhat more viable.

The Department's guidance currently suggests that Managed Account Services are includable within the definition of a QDIA. In many instances, the role of the managed account provider is limited to the asset allocation decision as opposed to the fund selection. The proposed QDIA guidelines on investment managers may be interpreted as the investment manager having responsibility for asset allocation as well as investment manager selection. The conflict should be corrected so that there is consistent guidance and clearly defined roles and responsibilities.

II. Conclusion

NEPC commends the Department's efforts with respect to the development of the QDIA guidelines. NEPC believes that expanding the QDIA definition to allow Authorized Plan Fiduciaries to serve as the "manager" of custom-tailored investment solutions is consistent with the Department's objectives as set forth in the preamble to the Proposed Regulation and would provide substantially the same degree of protection to plans and their participants as the Proposed Regulation. Further, NEPC believes that, in making this change, the Department will achieve its goals of creating cost-effective ways for plan participants to achieve better diversification within their defined contribution plans in a manner that is equally protective of the interests of the plans and their participants.

NEPC appreciates the opportunity to make this submission. Please feel free to contact me if you have any questions.

Sincerely,

Richard M. Charlton
Chairman and Chief Executive Officer
New England Pension Consultants