SEC gives participant-level disclosure a pass

By Marcia S. Wagner, Esq.

On October 20, 2010, the Department of Labor ("DOL") adopted regulations requiring plan administrators of participant-directed individual account plans to disclose plan and investment-related information to participants and beneficiaries on or before the date an individual can first direct the investment of his account and at least annually thereafter. After initial delays of the regulation's effective date, it is now anticipated that disclosures will need to begin by June 2012. At the time it was adopted, questions remained as to how the disclosure rule, particularly its requirements relating to the disclosure of investment performance, would be treated under the Securities and Exchange Commission's ("SEC") advertising rules for mutual funds, as set forth in SEC Rule 482. In a coordinated action, the DOL requested a no-action letter from the SEC on October 26, 2011, to which the SEC responded on the same day.

The DOL Rule. The DOL request noted that its regulation generally requires performance, benchmarking, and fee information for each plan investment option with varying returns, such as a mutual fund. Plans must disclose the average annual total return of the investment for 1, 5, and 10-year periods (or for the life of the investment option, if shorter) ending on the date of the most recently completed calendar year. Such information must be accompanied by a statement that an investment's past performance is not necessarily an indication of how the investment will perform in the future. Further, performance data, updated at least quarterly, must be made available via an Internet Web site address which may or may not link to a mutual fund company's Web address.

Money market funds are treated as subject to the DOL's investment performance disclosure rules so that plans must provide the above-mentioned historical return information. Under the DOL rule, investment-related information, including performance data, must be provided in a chart or other comparative format so as to help plan participants review and compare their investment options.

SEC Rule 482. The SEC's Rule 482 requires certain information to be included in mutual fund advertisements that include performance data. Such an advertisement with respect to an open-end investment company and certain separate accounts must contain a legend that goes beyond merely warning that past performance does not guarantee future results. In addition, the legend must identify a toll-free telephone number or Web site where an investor may obtain performance data current to the most recent month ended seven business days before the date of use. For purposes of Rule 482, the date of use is the entire period when the information might be used by investors, not merely the date of its publication.

Under the SEC rule, the legend for money market funds must also contain a statement that a money market fund is not insured by the Federal Deposit Insurance Corporation or any other government agency. Further, except in the case of money market funds not holding themselves out as maintaining a stable net asset value, the legend must indicate that although the fund seeks to preserve the value of an investment at $1.00 per share, it is possible to lose money by investing in the fund. Another special rule for money market funds is that quotations of total return must be accompanied by a quotation of current yield, calculated in accordance with specific SEC directions. The DOL rule does not require disclosure of current yield.

The SEC rule requires that performance information included in an advertisement include total return quotations to the most recent calendar quarter ending before its submission for publication and total return current to the most recent month ending seven business days prior to the date the information is provided telephonically or through a Web site address. Alternatively, total return quotations must be current to the most recent month ended seven business days before the date of use. In contrast, the DOL rule allows the use of performance quotations as of the end of the prior calendar year.

Notwithstanding the difference in content and timing of disclosure under the DOL and the SEC rules, the SEC concluded that "disclosure by a Plan Administrator to Plan participants ... that is required by and complies with the DOL Rule should not be viewed as inconsistent with the Rule 482 Timeliness Requirements or the Other Rule 482 requirements." The SEC also stated that the information furnished to plan participants in compliance with the DOL rule need not be filed with the Commission or certain national securities associations, as otherwise might be required. The SEC letter noted that the staff of the Financial Industry Regulatory Authority ("FINRA") has indicated that it intends to interpret FINRA's rules, particularly its rules relating to the filing of sales literature, in conformity with the SEC's position.

The SEC's position is welcome and was presumably to be expected. However, its limitations should be noted. First, it applies only to information furnished to plan participants or their beneficiaries by the plan administrator or its designee. In addition, the information covered by the no-action letter is solely that required by the participant-level disclosure regulation under 29 C.F.R. Section 2550.404a-5; the no-action letter does not cover information provided to plan fiduciaries by plan service providers under Section 408(b)(2) of ERISA that will presumably constitute some of the matter ultimately furnished to participants. ❖

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