

Prohibited Transaction Class Exemption 77-4
Certain Transactions Between Investment Companies and Employee Benefit Plans
OMB Number 1210-0049
August 2016

SUPPORTING STATEMENT FOR PAPERWORK REDUCTION ACT OF 1995
SUBMISSIONS

A. Justification

1. *Explain the circumstances that make the collection of information necessary. Identify any legal or administrative requirements that necessitate the collection. Attach a copy of the appropriate section of each statute and regulation mandating or authorizing the collection of information.*

Section 408(a) of the Employee Retirement Income Security Act of 1974 (ERISA) and section 4975(c)(2) of the Internal Revenue Code of 1986 (the Code) authorizes the Secretary of Labor and the Secretary of the Treasury to grant a conditional or unconditional exemption of any fiduciary, disqualified person or class of fiduciaries, or orders of disqualified persons or transactions, from all or part of the restrictions imposed by sections 406 and 407(a) of ERISA and from taxes imposed by sections 4975(a) and (b) of the Code, by reason of section 4975(c)(1) of the Code. Under section 102 of Reorganization Plan No. 4, of 1978 (Reorganization Plan No. 4), the Secretary of Labor was given the authority to grant such exemptions.

This class exemption, which was originally granted on April 8, 1977, exempts from the prohibited transaction restrictions the purchase and sale by an employee benefit plan of shares from a registered, open-end investment company (mutual fund) when a fiduciary of the plan (e.g., an investment manager) is also the investment advisor for the investment company.

Section 406 of ERISA prohibits various transactions between a plan and certain related parties. Those parties in interest described in section 3(14) of ERISA and disqualified persons described in section 4975(e)(2) of the Code, such as plan fiduciaries, sponsoring employers, unions, service providers and affiliates, may not engage in a transaction described in section 406 of ERISA and section 4975(c) of the Code with a plan without an exemption. Specifically, these sections prohibits sales, leases, loans, or the provision of services between a party in interest and a plan, as well as a use of plan assets by or for the benefit of, or a transfer of plan assets to, a party in interest or a disqualified person, unless a statutory or administrative exemption applies to the transaction.

The Department of Labor has authority under Reorganization Plan No. 4, pursuant to section 408 of ERISA and section 4975(c) (2) of the Code to grant either individual or class exemptions. In order to grant an exemption under section 408 and section 4975(c) (2), the Department must determine that the exemption is:

- (1) administratively feasible,
- (2) in the interests of the plan and its participants and beneficiaries, and
- (3) protective of the rights of participants and beneficiaries of such plan.

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In order to ensure that the class exemption is not abused, that the rights of the participants and beneficiaries are protected, and that the exemption's conditions are being complied with, the Department often requires minimal information collection pertaining to the affected transactions.

2. *Indicate how, by whom, and for what purpose the information is to be used. Except for a new collection, indicate the actual use the agency has made of the information received from the current collection.*

There are three basic disclosure requirements incorporated within the class exemption. The first requirement is intended to put the plan on notice of possible fees associated with the redemption of open-end mutual fund shares. It requires disclosure of any redemption fees in the current prospectus of the open-end mutual fund (the prospectus in effect at the time of the plan's acquisition or disposal of such shares). The class exemption permits a plan to pay a redemption fee on the sale, by redemption, of open-end mutual fund shares only if the fee is paid to the open-end mutual company and the above noted disclosure is made.

The second requirement is that, at the time of the purchase or sale of such mutual fund shares, an independent fiduciary receive a copy of the current prospectus issued by the open-end mutual fund and full written disclosure of the investment advisory fees charged to or paid by the plan and the open-end mutual fund to the investment advisor. Pursuant to advisory opinion 2013-04A, the Department interprets the term "prospectus" in PTE 77-4 to include a "summary prospectus" if the summary prospectus meets the requirements of the Securities and Exchange Commission's revised disclosure provisions for mutual funds including a summary prospectus rule that were published in 2009. Pursuant to the SEC's revised disclosure provisions, mutual funds also are required to send the full prospectus to the investor upon an investor's request,¹ and to provide the full prospectus on-line at a specified internet site.² The hour and cost burden changes resulting from this revision are discussed in Items 12 and 13, below.

The third requirement is that the independent fiduciary be notified of any changes in the fees and approves in writing the plan's purchase or sale of affected mutual fund shares, or the plan's continued possession of any such mutual fund shares that it had acquired before the fee changes.

Without the class exemption an open-end mutual fund could not sell shares to or purchase shares from a plan when the fiduciary with respect to the plan is also the investment advisor for the mutual fund. Such purchases and sales may serve the interest of both the

¹ 17 CFR § 230.498(f).

² 17 CFR § 230.498(b)(1)(A).

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plans and the industry, provided that procedures designed to protect the interests of participants and beneficiaries from potential abuse are built into the transactions. Therefore, the exemption requires disclosure of any redemption fees in the current prospectus and approval of the advisory fees by a second fiduciary so that the plan fiduciary can make informed judgments with respect to the prudence of the transactions.

3. *Describe whether, and to what extent, the collection of information involves the use of automated, electronic, mechanical, or other technological collection techniques or other forms of information technology, e.g., permitting electronic submission of responses, and the basis for the decision for adopting this means of collection. Also, describe any consideration for using information technology to reduce burden.*

Under 29 C.F.R. § 2520.104b-1(b) of ERISA, “where certain material, including reports, statements, and documents, is required under Part I of the Act and this part to be furnished either by direct operation of law or an individual request, the plan administrator shall use measures reasonably calculated to ensure actual receipt of the material by plan participants and beneficiaries.” Section 2520.104b-1(c) establishes the manner in which disclosures under Title I of ERISA made through electronic media will be deemed to satisfy the requirement of § 2520.104b-1(b). Section 2520-107-1 establishes standards concerning the use of electronic media for maintenance and retention of records. Under these rules, all pension and welfare plans covered under Title I of ERISA may use electronic media to satisfy disclosure and recordkeeping obligations, subject to specific safeguards.

The Government Paperwork Elimination Act (GPEA) requires agencies to allow customers the option to submit information or transact with the government electronically, when practicable. Where feasible, and subject to resource availability and resolution of legal issues, EBSA has implemented the electronic acceptance of information submitted by customers to the federal government.

4. *Describe efforts to identify duplication. Show specifically why any similar information already available cannot be used or modified for use for the purposes described in Item 2 above.*

The Department of Labor and the Department of the Treasury collectively issued this class exemption in order to eliminate duplicative disclosure requirements.

5. *If the collection of information impacts small businesses or other small entities describe any methods used to minimize burden.*

The disclosure requirements included in the class exemption ensure that the transactions involving the open-end mutual fund allow existing business practices to continue. Because of the nature of the potential conflict of interest for individuals who manage

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these open-end mutual funds, the disclosure requirements make no distinction between small and large mutual fund companies. In addition, mutual fund companies are managed by very large fund complexes which are not small entities.

6. *Describe the consequence to Federal program or policy activities if the collection is not conducted or is conducted less frequently, as well as any technical or legal obstacles to reducing burden.*

The disclosure requirements of the class exemption are only mandatory if open-end mutual funds sell their shares to or purchase their shares from plans when the investment advisor for the plan is also the investment advisor for the open-end mutual fund. The frequency is dependent on the occurrence of such transactions, not on a predetermined time period.

Pursuant to AO 2013-04A the Department is interpreting the term “prospectus” in PTE 77-4 to include a “summary prospectus” if certain conditions are met that are discussed in Item 2, above.

7. *Explain any special circumstances that would cause an information collection to be conducted in a manner:*

- *requiring respondents to report information to the agency more often than quarterly;*
- *requiring respondents to prepare a written response to a collection of information in fewer than 30 days after receipt of it;*
- *requiring respondents to submit more than an original and two copies of any document;*
- *requiring respondents to retain records, other than health, medical, government contract, grant-in-aid, or tax records for more than three years;*
- *in connection with a statistical survey, that is not designed to produce valid and reliable results that can be generalized to the universe of study;*
- *requiring the use of a statistical data classification that has not been reviewed and approved by OMB;*
- *that includes a pledge of confidentiality that is not supported by authority established in statute or regulation, that is not supported by disclosure and data security policies that are consistent with the pledge, or which unnecessarily impedes sharing of data with other agencies for compatible confidential use; or*
- *requiring respondents to submit proprietary trade secret, or other confidential information unless the agency can demonstrate that it has instituted procedures to protect the information's confidentiality to the extent permitted by law.*

There are no special circumstances that require the collection to be conducted in a manner inconsistent with the above.

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8. *If applicable, provide a copy and identify the date and page number of publication in the Federal Register of the agency's notice, required by 5 CFR 1320.8(d), soliciting comments on the information collection prior to submission to OMB. Summarize public comments received in response to that notice and describe actions taken by the agency in response to these comments. Specifically address comments received on cost and hour burden.*

Describe efforts to consult with persons outside the agency to obtain their views on the availability of data, frequency of collection, the clarity of instructions and recordkeeping, disclosure, or reporting format (if any), and on the data elements to be recorded, disclosed, or reported.

Consultation with representatives of those from whom information is to be obtained or those who must compile records should occur at least once every 3 years -- even if the collection of information activity is the same as in prior periods. There may be circumstances that may preclude consultation in a specific situation. These circumstances should be explained.

The Department's notice, required by 5 CFR 1320.8(d), which provided the public with 60 days to comment on the information collection, was published in the Federal Register on May 26, 2016 (81 FR 33550). No comments were received.

9. *Explain any decision to provide any payment or gift to respondents, other than remuneration of contractors or grantees.*

No payments or gifts are provided to respondents.

10. *Describe any assurance of confidentiality provided to respondents and the basis for the assurance in statute, regulation, or agency policy.*

There is no promise of confidentiality of the information. The class exemption requires that the information concerning the possible payment of redemption fees be included in the open-end mutual fund's prospectus and, therefore, available to the plan and interested parties.

11. *Provide additional justification for any questions of a sensitive nature, such as sexual behavior and attitudes, religious beliefs, and other matters that are commonly considered private. This justification should include the reasons why the agency considers the questions necessary, the specific uses to be made of the information, the explanation to be given to persons from whom the information is requested, and any steps to be taken to obtain their consent.*

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There are no questions of a sensitive nature pertaining to sexual behavior and attitudes, religious beliefs, or other matters that are commonly considered private. Therefore, this is not applicable to the requirements of this class exemption.

12. *Provide estimates of the hour burden of the collection of information. The statement should:*
- *Indicate the number of respondents, frequency of response, annual hour burden, and an explanation of how the burden was estimated. Unless directed to do so, agencies should not conduct special surveys to obtain information on which to base hour burden estimates. Consultation with a sample (fewer than 10) of potential respondents is desirable. If the hour burden on respondents is expected to vary widely because of differences in activity, size, or complexity, show the range of estimated hour burden, and explain the reasons for the variance. Generally, estimates should not include burden hours for customary and usual business practices.*
 - *If this request for approval covers more than one form, provide separate hour burden estimates for each form and aggregate the hour burdens in Item 13.*
 - *Provide estimates of annualized cost to respondents for the hour burdens for collections of information, identifying and using appropriate wage rate categories. The cost of contracting out or paying outside parties for information collection activities should not be included here.*

The class exemption has three basic disclosure requirements. The first is to incorporate within the open-end mutual fund's prospectus, in effect at the time of the plan's acquisition of the open-end mutual fund's shares and at the time of disposition of such shares, a one-line notice of possible fees associated with the redemption of such shares. The second requires at the time of purchase or sale of such mutual fund shares that the plan's independent fiduciary receive a copy of the current prospectus issued by the open-end mutual fund and a full and detailed written statement of the investment advisory fees charged to or paid by the plan and the open-end mutual fund to the investment advisor. The third requires that the independent fiduciary is notified of any changes in fees. As discussed in Item 2 above, the Department has revised the second requirement by interpreting the term prospectus in PTE 77-4 to include a "summary prospectus" if certain conditions are met. For purposes of this PRA analysis, the Department assumes that all mutual funds using the exemption will send the summary prospectus.

Open-end mutual funds are required by the SEC to provide a current summary prospectus (every prospectus must be updated at least every 16 months) to present and prospective shareholders, and therefore they must update their prospectus after their annual audit and whenever substantial changes occur. Open-end mutual funds are required by SEC rules to incorporate in the prospectus a statement of any fees charged for the redemption of shares. Since the funds are required by the SEC to prepare a prospectus, this requirement of the class exemption adds no paperwork burden.

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There is some paperwork burden associated with the provision of information regarding the investment advisory fees. The investment advisor normally accomplishes this disclosure by preparing a one or two page written document; the advisor then reproduces and mails this document to each independent fiduciary. The Department estimates that it would take an average of 30 minutes annually per mutual fund complex to prepare or update the disclosure since each investment advisor can prepare one fee schedule for all of the plans it provides investment management services to and then reproduce and send a copy to the independent fiduciary of each plan. The independent fiduciary also must receive a copy of the already prepared prospectus. Since this can be mailed with the fee information, it imposes no separate burden. The notification of changes in fee rates would not add paperwork burden because it would be a standard business practice.

According to the Investment Company Institute (ICI), 873 complexes managed and distributed mutual funds in 2015.³ The Department assumes that all of these complexes also offer investment management services to pension plans. A 2013 Deloitte/ICI survey finds that 37 percent of 401(k)s have a mutual fund company as their service provider.⁴ Based upon ICI analyses and Form 5500 data that examines the percentage of plans that are invested in registered investment companies, the Department estimates that 24.7 percent of defined benefit plans have mutual fund companies as money managers.⁵ Applying these percentages to the universe of pension plans that filed a Form 5500 in 2013 yields a total of approximately 246,580 plans (235,687 defined contribution and 10,894 defined benefit plans) with service provider relationships with mutual fund companies.⁶

The Department assumes that every mutual fund complex will make use of the class exemption for all their client plans. Each plan would have one independent fiduciary, required under the class exemption to receive the disclosure material. The Department also estimates that ten percent of plans will then request a full prospectus. The Department estimates that it will take no more than 5 minutes (1/12 of an hour) to distribute the materials to each plan. In sum, we calculate the total burden hours for this exemption as follows:

Preparation: ½ hr. x 873 mutual fund firms = 437
Distribution (summary): 1/12 hr. x 246,580 plans = 20,548

³ 2016 *Investment Company Fact Book*, Investment Company Institute 2016.

⁴ Deloitte. *Defined Contribution/401(k) Fee Study*. Investment Company Institute. August 2014.

⁵ Based on Form 5500 Data 2000-2010, defined benefit plans are approximately 33 percent less likely than defined contribution plans to be invested in a registered investment company.

Also see Holden, Sarah. "The Economics of Providing 401(k) Plans: Services, Fees, and Expenses" *Investment Company Institute*, September 2010.

⁶ Table A1 of the Private Pension Plan Bulletin, Abstract of 2013 Form 5500 Annual Reports. There are 681,154 pension plans, of which 44,163 are defined benefit plans and 636,991 are defined contribution plans.

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Distribution (full): 1/12 hr. x 24,658 plans = 2,055
 Total burden hours = 23,040

Mutual fund complexes, rather than the plans they provide services to, would bear the burden and are expected to perform the services in-house. The mutual fund complexes are estimated to incur costs of \$167.32 per hour for financial professional staff time to prepare the disclosure material and \$55.21 per hour in clerical time to distribute the material.⁷ Total equivalent costs are estimated to be approximately \$1,321,030.⁸

Activity	Burden Hours	Equivalent Burden Cost
Preparing and Updating the Disclosure	437	\$73,119
Distributing the Summary Prospectus	20,548	\$1,134,455
Distributing the Full Prospectus	2,055	\$113,457
Total	23,040	\$1,321,030

13. *Provide an estimate of the total annual cost burden to respondents or recordkeepers resulting from the collection of information. (Do not include the cost of any hour burden shown in Items 12 or 14).*

The information under this class exemption must be provided by mutual fund complexes to their client pension plans. The Department assumes that the disclosure material will be prepared by in-house staff of the mutual fund complexes; therefore, the only cost burden will be for materials and postage. Based on the Department’s interpretation that the term “prospectus” includes a summary prospectus, the Department assumes that respondents will send the summary disclosure at a cost of \$0.77 in materials and postage (\$0.47 postage and \$0.30 in materials).⁹ The Department estimates that 51.8 percent of the disclosures will be distributed electronically at no additional cost.¹⁰ Based on the

⁷ For a description of the Department’s methodology for calculating wage rates, see <http://www.dol.gov/ebsa/pdf/labor-cost-inputs-used-in-ebsa-opr-ria-and-pra-burden-calculations-march-2016.pdf>.

⁸ Preparation: 437 hours at \$167.32 per hour = \$73,119; Distribution: 22,603 hours at \$55.21 per hour = \$1,247,912.

⁹ The Department estimates that, on average, mutual fund complexes will send 6 pages at \$0.05 a page, which costs \$0.47 to send first class mail.

¹⁰ According to data from the National Telecommunications and Information Agency (NTIA), 33.4 percent of individuals age 25 and over have access to the internet at work. According to a Greenwald & Associates survey, 84 percent of plan participants find it acceptable to make electronic delivery the default option, which is used as the proxy for the number of participants who will not opt out that are automatically enrolled (for a total of 28.1 percent receiving electronic disclosure at work). Additionally, the NTIA reports that 38.9 percent of individuals age 25 and over have access to the internet outside of work. According to a Pew Research Center survey, 61 percent of internet users use online banking, which is used as the proxy for the number of internet users who will opt in for electronic disclosure (for a total of 23.7 percent receiving electronic disclosure outside of work). Combining the 28.1 percent who receive electronic disclosure at work with the 23.7 percent who receive electronic disclosure outside of work produces a total of 51.8 percent who will receive electronic disclosures overall.

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foregoing, the summary disclosures will be mailed to 118,852 plans at a cost of approximately \$91,516.¹¹

The Department estimates that ten percent of plans will request a full prospectus and that 51.8 percent will be sent electronically at no additional cost. Mailing the full prospectus to the remaining 22,520 plans will cost \$2.15 in materials and postage (\$1.15 postage and \$1.00 in materials) resulting in a cost of approximately \$25,553.¹² The total cost of this ICR is approximately \$117,069.

14. *Provide estimates of annualized cost to the Federal government. Also, provide a description of the method used to estimate cost, which should include quantification of hours, operational expenses (such as equipment, overhead, printing, and support staff), and any other expense that would not have been incurred without this collection of information. Agencies also may aggregate cost estimates from Items 12, 13, and 14 in a single table.*

There is no cost to the Federal government. This class exemption does not result in any information being filed with or reported to the Federal government.

15. *Explain the reasons for any program changes or adjustments reported in Items 13 or 14.*

Although no program changes have been made that would require revision of the prior paperwork burden estimates, the Department is adjusting its estimates of the hour and cost burden of this exemption in two respects. First, the Department is revising its estimate of the number of respondents and responses, based on more recent ICI and Form 5500 data. Second, the Department is revising its estimate of the wage and postage costs due to increased labor costs and inflation.

16. *For collections of information whose results will be published, outline plans for tabulation, and publication. Address any complex analytical techniques that will be used. Provide the time schedule for the entire project, including beginning and ending dates of the collection of information, completion of report, publication dates, and other actions.*

This is not a collection of information for statistical use, and there are no plans to publish the results of this collection.

17. *If seeking approval to not display the expiration date for OMB approval of the information collection, explain the reasons that display would be inappropriate.*

¹¹ 246,580 disclosures * 48.2 percent mailed = 118,852 plans receiving paper disclosures; 118,852 plans * \$0.77/plan = \$91,516.

¹² 24,658 disclosures * 48.2 percent mailed = 11,885 plans receiving paper disclosures; 11,885 plans * \$2.15/plan = \$47,734.

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The OMB expiration date will be published in the Federal Register following OMB approval.

18. *Explain each exception to the certification statement identified in Item 19, "Certification for Paperwork Reduction Act Submission."*

Not applicable.

B. Collections of Information Employing Statistical Methods

Not applicable. The use of statistical methods is not relevant to this collection of information