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The DOL's New Investment Selection Proposal

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The Department of Labor's (DOL) issued proposed rulemaking titled Fiduciary Duties in Selecting Designated Investment Alternatives. If finalized, this rulemaking will create a new process-based safe harbor for fiduciary investment selection. Though this proposed rulemaking is being discussed largely through the lens of alternatives in defined contribution plans, at its core, this is not simply an "alternatives rule." It is a proposed framework for how ERISA fiduciaries should approach the selection of designated investment alternatives more generally, and it would provide fiduciaries a regulatory presumption of prudence in their investment selection decisions if six elements are met.

That broader point matters. For years, fiduciaries have operated in an environment shaped by general prudence principles, scattered sub-regulatory guidance, and litigation risk. The proposed rulemaking organizes those principles into a more defined and affirmative process-based construct. The proposal reaches significantly beyond private markets. It is intended to provide fiduciaries a clear roadmap how prudent investment selection decisions should be evaluated under ERISA and "entitles" fiduciaries' decisions made within said framework to "significant deference."

The proposal identifies six factors that fiduciaries should consider when selecting a designated investment alternative:

- expected performance or returns;
- fees and expenses;
- liquidity;
- valuation;
- meaningful benchmarking; and
- complexity.

Each of these considerations reflects concepts that most prudent fiduciaries already recognize. What is new is the extent to which the DOL is attempting to formally articulate them as the basis for a defense-friendly selection process. Whereas ERISA dictated the duty of prudence to fiduciaries, nowhere does it define a prudent process. The Department is finally answering the question, "what does a 'prudent process' entail?"

Importantly, when diving into the six elements, the proposed rule does not require fiduciaries to select the highest-return investment or the lowest-cost investment in isolation. Rather, the proposal recognizes that

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fiduciaries must evaluate investments in light of the relevant participant population, expected risk-adjusted returns, and the investment's overall characteristics. Likewise, fees must be assessed in relation to the investment's expected value, liquidity must be sufficient for both participant and plan needs, valuation must be suitable for plan administration, and benchmarks must be genuinely comparable to the strategy being evaluated – an element of litigation that we've seen plaintiff's counsel attempt to game over the years with apples-to-oranges comparisons. In addition, fiduciaries must be capable of understanding the investment's complexity or is strongly recommended to seek qualified 3(21) or 3(38) fiduciary assistance if they are not.

That last point is especially relevant in the alternatives discussion. The proposal expressly recognizes complexity as part of the fiduciary analysis and notes that reliance on a prudently selected ERISA 3(21) investment advice fiduciary or 3(38) investment manager is indicative of a prudent process. A complex investment does not become prudent merely because it is fashionable, institutionally common elsewhere, or wrapped in a familiar label. It is also not automatically prudent merely because there are valid investment-related reasons for its utilization. The full complexity of the vehicle has to be reviewed and understood within the context of its usage. And in a defined contribution context that means a world that's been built on transparency, liquidity, and daily valuation.

However, it is important to note that the proposed rulemaking does not create a safe harbor for ongoing monitoring after an investment has been selected. The proposal is directed to selection only, not retention. That distinction could prove important in litigation, particularly in a post-Hughes environment in which claims relating to monitoring and retention remain a central source of exposure. The practical result may be a sharper separation between selection claims, where fiduciaries may now have a more defined framework for defending process and monitoring claims, where ongoing oversight will still need to stand on its own record. But the DOL did make mention that additional guidance is likely in regards to ongoing monitoring – so more to come on that front.

The proposed rulemaking is an important development, but not because it should trigger a rush into alternatives. Rather it is a signaling of potential certainty for fiduciaries in their investment selection process. Even in light of the proposed rulemaking, adoption of alternatives in the defined contribution space is still early, product design is still evolving, and fiduciaries should proceed carefully and deliberately. The most plausible path for alternatives, if they expand meaningfully in defined contribution plans, is likely through professionally managed structures with modest allocations and strong governance, not through product-driven enthusiasm untethered from participant needs and outcomes.

In short, the real significance of the proposal is not that it may make alternatives easier to discuss, though it does do that. It is that it may provide a clearer, more structured basis for evaluating investment selection under ERISA. The headlines should be reading, "Fiduciaries May Finally Receive Regulatory Safe Harbor Protection for Undertaking Defined Prudent Processes."