January 4, 2024

What’s a QDIA—and is it required?

How will you invest contributions on behalf of participants who don’t make an investment election? The answer to this question can affect your fiduciary liability—and your participants’ retirement readiness. One option that can help you address both is a qualified default investment alternative, or QDIA, for short.

Why you need a default investment fund

You have to select a default investment fund for your retirement plan because, although your participants (and beneficiaries) are able to choose the investments for their 401(k) deferrals and employer contributions from the plan's investment lineup, not all of them will. Additionally, if your plan offers automatic enrollment, you need to know how to invest these contributions.

The default fund is where money will be invested for a participant (or beneficiary) who hasn't provided explicit investment instructions. You can pick any fund in your plan's investment lineup as your default investment. Which one you choose will depend, in part, on whether you want the fund to qualify as a QDIA. Let's explore why this may matter to you.

What makes a default fund a QDIA

Not surprisingly, plan sponsors worry that investing participants' money without their direction may increase their fiduciary liability. This concern is why QDIAs were created. A QDIA is a default investment that limits a plan sponsor's fiduciary risk if certain requirements are met. Fiduciaries who select a QDIA as a default investment aren't liable for any investment loss that's a result of investing in the QDIA as long as:

- The plan allows participants and beneficiaries to select their own investments.
- The QDIA is managed by an investment manager, plan trustee, plan sponsor, or is an investment company registered under the Investment Company Act of 1940.
- The QDIA is a target-date fund (TDF) or lifecycle fund, balanced fund, or managed account.
- Participants and beneficiaries have the opportunity to opt out of the QDIA.
- Participants and beneficiaries are able to move money in and out of the QDIA as often as other participants and beneficiaries can change their investments.
- The QDIA doesn't impose fees or expenses when participants or beneficiaries transfer their money to another investment in the plan.
- The plan satisfies the QDIA notice requirements; participants and beneficiaries must receive a notice explaining when money will be invested in the QDIA, along with their rights, at least 30 days prior to their eligibility under the plan or making their

first investment, and annually thereafter (at least 30 days prior to the start of each plan year).

You're not required to use a QDIA—it's up to you to decide if it's right for your plan. Plan sponsors who use a QDIA aren't relieved of the distinct fiduciary duty to prudently select and monitor the QDIA.

Another potential benefit—increased retirement readiness

If you do choose a QDIA, it can potentially improve your participants' and beneficiaries' investment results over the long term, helping them make progress on their goals. That's because all the QDIA options include a growth component (stocks and similar investments), compared to money market and stable value funds, which focus solely on capital preservation.

Factors to consider when choosing your QDIA

TDFs are the most common QDIA, with 76% of surveyed plans with $5 million to $50 million in assets using them as their default.[1] But that doesn't automatically make it the right choice for your plan. You need to consider many factors, including:

- Your workplace demographics
- Employees' investment experience
- The desired level of personalization
- Fees and expenses

For example, if your employees have limited investment knowledge, it might make sense to choose a TDF because they're easier to understand than a managed account. If personalization is important, you might consider a managed account, as TDFs are typically "one size fits all."

A dynamic QDIA is another possibility. How does this work? Employees are defaulted into a TDF until they reach a certain age, such as age 40, at which point they're defaulted into a managed account where they can receive personalized investment advice.

Your financial professional can help you decide the best approach for your plan.

Turn the tables on participant inertia while reducing your fiduciary risk

Choosing your default fund requires careful consideration—not only because you have a fiduciary duty to act prudently, but because participants and beneficiaries tend to make few, if any, changes to their investment options. Once their money goes into the default investment, it's likely to stay there. So, you should consider a default fund that can help your participants build their retirement savings while minimizing your risk. A QDIA can help you with both.

1 "PLANSPONSOR 2021 DC Benchmarking Survey," © 2021 Asset International, Inc., November 2021.

Important disclosures

Although target-date funds are managed for investors on a projected retirement date timeframe, the fund's allocation strategy does not guarantee that investors' retirement goals will be met. The target date is the year in which an investor is assumed to retire and begin taking withdrawals.

This content is not intended to be an exhaustive review of fiduciary duties under ERISA. The objective is to highlight the key responsibilities of a plan fiduciary and present the challenges that plan fiduciaries may face in discharging their duties. John Hancock cannot provide legal advice concerning your plan or your role as plan fiduciary, and the information included should not be taken as such. If legal advice or other expert assistance is required, please consult your legal counsel.

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