Sunshine Act Meetings

This section of the FEDERAL REGISTER contains notices of meetings published under the "Government in the Sunshine Act" (Pub. L. 94-409) 5 U.S.C. 552b(e)(3).

COMMISSION ON CIVIL RIGHTS
September 1, 1987.
PLACE: 1121 Vermont Avenue, NW., Room 512, Washington, DC 20425.
DATE AND TIME: Friday, September 11, 1987, 9:00 a.m.-5:00 p.m.
STATUS OF MEETING: Open to the Public.

MATTERS TO BE CONSIDERED:
I. Approval of Agenda
II. Approval of Minutes of Last Meeting
III. Staff Director's Report
A. Status of Earmarks
B. Personnel Report
C. Activity Report
IV. Statement by Clarence M. Pendleton, Jr., Regarding the Flagstaff, Arizona Hearings on the Enforcement of the Indian Civil Rights Act of 1968
V. Report of Commission Subcommittee Regarding Proposed Projects
VI. SAC Recharters
VII. Discussion by SAC Chairs

PERSON TO CONTACT FOR FURTHER INFORMATION: Barbara Brooks, Press and Communications Division (202) 376-8312.
William H. Gillers, Solicitor, 376-8514.
[FR Doc. 87-20394 Filed 9-1-87; 11:56 am]

BILLING CODE 6335-01-M

FEDERAL DEPOSIT INSURANCE CORPORATION
Pursuant to the provisions of the "Government in the Sunshine Act" (5 U.S.C. 552b), notice is hereby given that at 10:30 a.m. on Thursday, August 27, 1987, the Board of Directors of the Federal Deposit Insurance Corporation met in closed session to consider (a) matters relating to the Corporation's assistance agreement with an insured bank; and (b) requests for financial assistance pursuant to section 13(c) of the Federal Deposit Insurance Act.

In calling the meeting, the Board determined, on motion of Director C. C. Hope, Jr. (Appointive), seconded by Director Robert L. Clarke (Comptroller of the Currency), concurred in by Chairman L. William Seidman, that Corporation business required its consideration of the matters on less than seven days' notice to the public; that no earlier notice of the meeting was practicable; that the public interest did not require consideration of the matters in a meeting open to public observation; and that the matters could be considered in a closed meeting pursuant to subsections (c)(4), (c)(6), (c)(8), (c)(9)(A)(ii), and (c)(9)(B) of the "Government in the Sunshine Act" (5 U.S.C. 552b(c)(4), (c)(6), (c)(8), (c)(9)(A)(ii), and (c)(9)(B).

The meeting was held in the Board Room of the FDIC Building located at 550 17th Street, NW., Washington, DC.

Federal Deposit Insurance Corporation.
Hoyle L. Robinson,
Executive Secretary.
[FR Doc. 87-20415 Filed 9-1-87; 12:25pm]
BILLING CODE 7535-01-M

NATIONAL CREDIT UNION ADMINISTRATION
PLACE: 1776 G Street, NW., Washington, DC 20456, 7th Floor, Filene Board Room.
STATUS: Open.

MATTERS TO BE CONSIDERED:
1. Approval of Minutes of Previous Open Meeting.
2. Economic Commentary.
3. Review of Central Liquidity Facility Lending Rate.
5. Central Liquidity Facility Agent Commitment Fees.
7. Appeal of Regional Director's Disapproval of Charter Application.
9. Request for Exemption from NCUA's Nonpreferential Treatment and Prohibited Fees Lending Rules.
12. College Student Credit Union Pilot Program.
13. Federal Credit Union Field of Membership and Chartering Policy.

RECESS: 11:30 a.m.

PLACE: 1776 G Street, NW., Washington, DC 20456, 7th Floor, Filene Board Room.
STATUS: Closed.

MATTERS TO BE CONSIDERED:
1. Approval of Minutes of Previous Closed Meetings.
2. Approval of Central Liquidity Facility Agent Member. Closed pursuant to exemptions (4), (8), and (9)(A)(ii).
3. Central Liquidity Facility Lines of Credit. Closed pursuant to exemptions (4), (8), and (9)(A)(ii).
4. Requests for Exemption from § 701.21(h)(2)(ii), NCUA Rules and Regulations. Closed pursuant to exemptions (6), (8), and (9)(A)(ii).
5. Appeals of Liquidating Agent Denial of Claims. Closed pursuant to exemptions (9), (7), (8), (9)(A)(ii), and (10).
6. Administrative Action under section 206(h)(1)(a) of the Federal Credit Union Act. Closed pursuant to exemptions (9), (9)(A)(ii), and (9)(B).
7. Board Briefings. Closed pursuant to exemptions (2), (8), (9)(A)(ii), and (9)(B).
8. Personnel Actions. Closed pursuant to exemptions (2) and (6).

FOR MORE INFORMATION CONTACT: Becky Baker, Secretary of the Board, Telephone (202) 357-1100.
Becky Baker, Secretary of the Board.
[FR Doc. 87-20436 Filed 9-1-87; 1:40 pm]
BILLING CODE 7535-01-M

Federal Register
Vol. 52. No. 171
Thursday, September 3, 1987
Part II

Department of Labor

Pension and Welfare Benefits Administration

29 CFR Part 2550
Proposed Regulation Regarding Participant Directed Individual Account Plans; Notice of Proposed Rulemaking
DEPARTMENT OF LABOR

Pension and Welfare Benefits Administration

29 CFR Part 2550

Proposed Regulation Regarding Participant Directed Individual Account Plans (ERISA Section 404(c) Plans)

AGENCY: Department of Labor.

ACTION: Notice of Proposed Rulemaking.

SUMMARY: This document contains a proposed regulation under section 404(c) of the Employee Retirement Income Security Act of 1974 (ERISA, or the Act). That section provides that where a participant or beneficiary of an employee pension benefit plan exercises control over assets in an individual account maintained for him under the plan, the participant or beneficiary is not considered a fiduciary by reason of his exercise of control and other plan fiduciaries are relieved of liability under Part 4 of Title I of ERISA for the results of the participant’s or beneficiary’s exercise of control. Section 404(c) specifically contemplates the issuance of regulations, and the proposal describes the circumstances in which section 404(c) applies to a transaction involving a participant’s or beneficiary’s exercise of control over his individual account. If adopted, the regulation will affect participants and beneficiaries as well as plan fiduciaries.

DATES: Written comments on the proposed regulation must be received by the Department of Labor (the Department) on or before November 2, 1987. The proposed regulation, if adopted, would apply to transactions occurring in plan years beginning after a date 90 days from the date the regulation is published in final form.

ADDRESSES: Written comments (preferably at least three copies) should be submitted to the Office of Regulations and Interpretations, Pension and Welfare Benefits Administration, Room N–4677, U.S. Department of Labor, Washington, DC 20210, and marked “Attention: Section 404(c) regulation.” All submissions will be available for public inspection in the Public Documents Room, Pension and Welfare Benefits Administration, Room N–4677, 200 Constitution Avenue NW, Washington, DC 20210.


SUPPLEMENTARY INFORMATION: This document contains a proposed regulation under section 404(c) of ERISA.1 That section provides that where a participant or beneficiary of an employee pension benefit plan that provides for individual accounts exercises control over assets in his account, then: (1) the participant or beneficiary shall not be deemed to be a fiduciary by reason of his exercise of control; and (2) no person who is otherwise a fiduciary shall be liable under the fiduciary responsibility provisions of ERISA for any loss, or by reason of any breach, which results from such participant’s or beneficiary’s exercise of control. A discussion of section 404(c) and a description of the proposed regulation follows.

A. General Considerations

The relief from the fiduciary responsibility provisions of ERISA that is provided by section 404(c) applies only to individual transactions that meet the criteria established by that section—i.e., the transaction must be under the kind of plan described in section 404(c) and the participant must have actually exercised control with respect to the transaction. Thus, a determination whether sections 404(c)(1) and 404(c)(2) apply can be made only on a case by case basis. The proposed regulation provides the general framework for such determinations.

It is the Department’s view that section 404(c) is similar to a statutory exception to the general fiduciary responsibility provisions of ERISA, and, accordingly, the person asserting applicability of the exception will have the burden of proving that the conditions of section 404(c) and any regulation thereunder have been met.2

The proposed regulation is organized in a manner similar to section 404(c) itself. Paragraph (a) describes the general standards of section 404(c). Paragraph (b) describes the kinds of plans that may provide for participant control. Paragraph (c) describes the application of paragraph (b) in certain special circumstances. Paragraph (d) describes the manner in which a participant must exercise control in order for the relief provided by section 404(c) to be available. Paragraph (e) describes the application of sections 404(c)(1) and 404(c)(2). Paragraph (f) defines certain terms that are used in the regulation. Paragraph (g) contains specific examples which illustrate the provisions of the proposal. Paragraph (h) establishes the effective date for the regulation.

B. ERISA Section 404(c) Plans

The proposed regulation defines an “ERISA section 404(c) plan” as an individual account plan described in section 3(34) of ERISA that permits a participant to make an independent choice, from a broad range of investment alternatives, regarding the manner in which any portion of the assets in that individual account are invested.3 The definition permits a plan to provide for participant control in many different ways and in varying degrees. For example, under the definition, a plan could meet the requirements for treatment as an ERISA section 404(c) plan notwithstanding that it only allows certain participants to exercise control over their individual account balances and notwithstanding that it only permits participants to exercise control over a specified portion of their account balances.4 However, if

---

1 29 U.S.C. 1104(c).
2 See Donovan v. Cunningham, 715 F.2d 1455, 1465–1467 (5th Cir. 1983) in which it was held that a fiduciary of an employee stock ownership plan had the burden of proof to show that the conditions to the availability of the statutory exemption found in section 404(e) of ERISA were met. As support, the court cited SEC v. Balaton Purine Co., 346 U.S. 119, 129 (1953). “At this point in time the Supreme Court has observed in a different context, it seems ‘fair and reasonable’ to place the burden of proof upon the person seeking to avoid the conditions to within a statute exception to a broad remedial scheme. SEC v. Balaton Purine Co., 346 U.S. 119, 123, 73 S.Ct. 881, 883, 97 L.Ed. 1444 (1953).” Id. at 1467–68, n.27.
3 This discussion deals only with the effect of such classifications on an ERISA section 404(c) plan. Certain circumstances such classifications may violate other provisions of law including conditions to qualification of a pension plan under section 404(e) of the Internal Revenue Code (the Code). That section provides that a qualified pension plan may not discriminate in favor of employees who are officers, shareholders or highly compensated. See section 401(a)(4) of the Code. In Rev. Rul. 70-279, 1970-2 C.B. 64, the Internal Revenue Service held that a profit sharing plan failed to meet the qualification requirements under section 401 of the Code because highly compensated employees were permitted to exercise control over assets in their individual accounts.
4 Section 404(c) refers to a pension plan that “provides for individual accounts.” The proposed regulation, however, limits coverage of section 404(c) to “individual account plans” described in section 3(34) of ERISA because the conference report accompanying ERISA, H.R. Rep. No. 1203, 93d Cong. 2d Sess., 305 (1974) (hereafter, the Conference Report) refers to individual account plans that provide for participant control and because section 404(c) seems to contemplate separate individual accounting so that each participant will bear the sole risk of loss attributable to his investment decision.
The proposed regulation also provides that a plan does not fail to qualify as an ERISA section 404(c) plan merely because it charges the participant's account with the reasonable expenses of carrying out his instructions provided the participant is informed that such charges will be made and that the participant is furnished periodic reports regarding the actual expenses incurred pursuant to the procedures established under the plan. 8

Pursuant to paragraph (b)(2)(ii) of the proposed regulation, an ERISA section 404(c) plan may impose certain limitations on the responsible fiduciary's duty to carry out a participant's investment instructions. For example, the proposal states that a plan fiduciary may refuse to implement an investment decision that would generate unrelated business income or unrelated debt-financed income to the plan that would be taxable under the Code. 9 The circumstances described in the proposal are not intended to be exhaustive and a plan may impose other reasonable limitations. However, such restrictions could so restrict a participant's opportunity to exercise control as to cause the plan to fail to meet the general requirement that an ERISA section 404(c) plan must provide for a broad range of investment alternatives. Thus, such restrictions should be taken into account in determining whether a particular plan meets the requirements for treatment as an ERISA section 404(c) plan and in determining the scope of the responsibilities of plan fiduciaries.

2. Broad Range of Investment Alternatives

a. In general. As noted above, the proposed regulation provides that a plan is an ERISA section 404(c) plan only if it offers a "broad range" of investment alternatives. This provision is derived from the discussion of section 404(c) in the Conference Report. 10 Whether a plan provides a broad range of investment alternatives is ultimately a factual question to be resolved in light of the facts and circumstances of the particular case. However, the proposed regulation establishes the minimum standards which a plan must meet in order to provide a sufficient range of investment options. 11

First, the alternatives available under the plan must be sufficient to permit the participant to pursue a variety of different investment objectives. These include: (1) Capital preservation and generation of income; (2) capital appreciation; and (3) liquidity with a high degree of assurance of repayment.

Third, the plan must provide a sufficient range of investments so that a participant may diversify investments so as to minimize the risk of large losses. There are two aspects to this requirement. First, the proposed regulation makes it clear that, within each of the investment objective categories discussed above, an ERISA section 404(c) plan must offer participants a sufficient number of investment alternatives so that a participant may diversify investments within each category to minimize the risk of large losses. Second, the regulation contains a more general requirement under which the plan as a whole must provide participants with the opportunity to diversify investments. The nature of the plan and the size of the participants' accounts may affect the number and type of investment options necessary to meet this requirement. For example, a plan which does not provide participants with an opportunity to

---

8 ERISA also imposes certain requirements which are not affected by a participant's exercise of control over the assets in his individual account; these requirements, of course, continue to apply to plan fiduciaries even though a plan is an ERISA section 404(c) plan. For example, the bonding requirements of section 412 of ERISA would apply to all persons (other than the participant) who handle plan funds under an ERISA section 404(c) plan.

9 As discussed below, paragraph (a)(b)(ii) of the proposed regulation describes certain categories of participant instructions with respect to which the provisions of section 404(c) do not apply. To ensure a reasonable opportunity to exercise control over assets in his account.

10 For example, if a plan's summary plan description contains a general description of the type of administrative charges that may be incurred along with the amount of such charge (and any change in that information is reflected in subsequent summaries of material modifications), the requirement of prior periodic disclosure of the existence of these charges generally would be met. Such disclosure would not, however, satisfy the requirement of periodic disclosure of the actual expenses incurred by the plan.

11 Of course, a plan which permits a participant to direct the investment of the assets in his account in any available investment will be considered to offer a broad range of investment alternatives. In cases where the plan limits the investment options available to participants, a determination whether the plan provides a broad range of investment alternatives would be made on a case by case basis, taking into account the factors described in the regulation.
invest in pooled investment funds might not meet the diversification requirement if the average size of the participants' accounts is such that pooled investment is the only management way in which to diversify account investments. In addition, the general diversification requirement should assure that participants have an opportunity to pursue "balanced" investment objectives involving a combination of investments from the specified categories discussed above. 12 13

Fourth, the plan must provide a participant the opportunity to invest some or all of his account balance in a relatively "safe" investment—i.e., a fully insured interest-bearing deposit in a bank or similar financial institution or a pooled investment fund the assets of which consist solely of cash and securities issued or guaranteed by the United States or one of its agencies. The principal investment objectives of such an investment fund must include a high level of current income consistent with the preservation of capital and a high degree of liquidity.

Where pooled investment funds are available as investment options, the underlying securities held in the investment funds may be considered in evaluating the extent to which a participant is able to diversify investments so as to minimize the risk of large losses. 13 14

The Department notes that, in view of the importance of these provisions defining a broad range of investment opportunities available for participation direction, it will carefully consider comments describing other options that the commentator believes satisfy the requirements of section 404(c) of ERISA and its legislative intent.

b. Access to information regarding investment options. The proposed

regulation states that only those investment options as to which sufficient information is available to the participant to permit informed investment decisions will be taken into account in determining whether a plan provides a broad range of investment alternatives. 14 This provision does not require plans to limit the available investment alternatives to those which meet these information requirements, but rather requires only that participants under an ERISA section 404(c) plan may at least be able to choose from a broad range of investments with respect to which such information is available. Thus, a plan can offer investment alternatives for which no information is available and still meet the broad range of investment alternatives requirement if it also offers a sufficient number of investment alternatives about which information is available. Paragraph (g)(1) of the proposal illustrates the operation of this provision.

C. Special Rule for Designated Pooled Investment Funds and Designated Investment Managers

1. Designated Pooled Funds. It appears that some individual account plans limit a participant's investment options by permitting participants to choose from a variety of different kinds of specified pooled investment funds. These funds frequently are identified in the plan document and may be the only investment options available to the participant. In many cases, all of the available funds are managed by the same investment manager or by affiliated investment managers. The Department has concluded that, in such cases, these plans should be treated as ERISA section 404(c) plans because they permit participant control and provide for a broad range of investment alternatives. However, these plans appear to differ in at least two respects from other participant-directed plans.

First, these plans offer participants designated pooled funds to the exclusion of other investments. Participants are required to choose from funds that have different investment objectives, but once they invest in a fund they do not have control over individual investment decisions made by the pooled fund's manager. Moreover, in many cases, the participant has no choice with respect to the investment managers who do make individual investment decisions. For these reasons, the Department believes that it is important that any regulation under section 404(c) of ERISA clearly reflect plan fiduciaries' ongoing duty to consider the suitability of the designated funds in these circumstances in order to protect the interests of participants.

Second, because a participant may have limited funds in his account, investment in pooled funds may frequently be the only way in which the participant can diversify his account. Thus, the Department believes that it is essential that a sufficient variety of funds be available to enable the participant to pursue—through investment in the designated funds—each of the investment objectives discussed above in connection with the general requirement that the plan permit a participant to choose from a broad range of investments.

In view of the foregoing, the proposed regulation provides that a plan whose investment alternatives include any specified pooled investment fund is an ERISA section 404(c) plan only if (in addition to the plan's compliance with the requirements of paragraph (b)): (1) An independent plan fiduciary is required to designate the pooled investment funds offered as investment options, and (2) the fiduciary designates at least four funds, each of which is managed in furtherance of a different one of the four investment objectives (preservation of capital, capital appreciation, liquidity, and balanced funds). 15 For purposes of this rule, an

12 Even if a plan offers a diverse group of investments in each of the categories of investments discussed above, it may not meet the general diversification standard of the proposed regulation. For example, a plan may fail to provide a participant an opportunity to diversify his account if all of the available options relate to one industry.

This is made clear in an example included in the regulation (paragraph (g)(2)). The Department's position is also consistent with the position taken in the Conference Report with regard to a fiduciary's obligation to diversify investments. There, the conference stated that for efficiency and economy plans may invest all their assets in a single bank or other pooled investment fund, but that the pooled fund must be diversified investments, and, in such circumstances, the diversification rule is to be applied to the plan by examining the diversification of the investments in the pooled fund. Conference Report at 305.

For purposes of diversification, an investment in a closed-end management company will not be considered investment in a pooled investment fund unless the investment is in the common stock issued by that company. 13

13 The requirement that sufficient information must be available to permit informed investment decisions applies not only to the initial participant investment decision but also to subsequent decisions with regard to that investment. Thus, for example, in order for an investment option to meet this requirement, information regarding the current value of the investment would need to be readily available on a regular basis as well as information regarding the financial condition of the issuer. A participant must also be given sufficient information to make informed decisions with regard to all incidents of ownership of that investment in order for an investment to be taken into account for purposes of the broad range requirement. In the case of a security, such information would include information sufficient to permit the participant to make investment decisions in exercising any voting rights attendant to such ownership. One of the examples (paragraph (g)(1)) illustrates that this standard would be met where the investment options available under the plan include a broad range of publicly-offered securities for which market quotations are readily available and where the plan and its legislative intent.

14 For purposes of this rule, an

Continued
affiliates of such fiduciary, such exercise of control will not be “independent” (regardless of whether it meets the other requirements of the regulation) unless the terms of the transaction are fair and reasonable to the participant at the time of the transaction. A transaction will be deemed to be fair and reasonable to the participant if the participant pays no more than, or receives no less than, adequate consideration as defined in section 3(18) of the Act in connection with the transaction. These standards are adopted from established principles relating to the circumstances under which consent of a beneficiary of a trust will relieve a trustee from liability for breach of his fiduciary duties.1

2. Absence of Affirmative Instructions. Generally, the proposed regulation contemplates that a participant will give affirmative instructions regarding the investment of assets in his individual account. However, the regulation does indicate that section 404 may apply in cases where the participant has not given such affirmative instructions if certain conditions are met. Such passive investment options are limited to the relatively “safe” investments required by paragraph (b)(1)(i) of the proposal to be included in each ERISA section 404(c) plan—i.e., fully insured interest-bearing deposits in a bank or similar financial institution or a pooled investment fund the assets of which consist solely of cash and securities issued or guaranteed by the United States or one of its agencies. It is contemplated that such a passive investment designation will serve primarily as a “suspense” fund in which

“independent” plan fiduciary is a fiduciary that is not affiliated with any of the specified investment funds or with any investment manager of such a fund. Under these rules, a plan that limits participants’ choices to a “family of funds” managed by a single investment manager could be treated as an ERISA section 404(c) plan.

2. Designated Investment Managers. It is also possible that an individual account plan may limit a participant’s investment options by providing participants with the opportunity to appoint one or more specified investment managers to make individual investment decisions on behalf of participants.16

The Department has concluded that any such plan should also be subject to a special rule in order to assure that a plan fiduciary assumes a continuing obligation to assess the suitability of the designated investment managers. Thus, the proposed regulation provides that a plan whose investment alternatives include the selection of one or more designated investment managers is an ERISA section 404(c) plan only if an independent fiduciary is required to designate the investment managers from which the participant may select. This rule is similar to the first of the two special rules for designated pooled funds. Since, however, a participant’s account assets would be managed individually under this kind of plan, the Department has concluded that the general rules in paragraph (b) are sufficient to assure that participants are free to pursue their desired investment objectives by choosing from a broad range of investment alternatives.

Paragraphs (g)(2) and (g)(3) of the proposed regulation illustrate the operation of the special requirements for designated pooled investment funds and designated investment managers.

Finally, the Department emphasizes that the rules for pooled funds are not intended to negate the relief that section 404(c) is intended to provide. In this respect, the independent fiduciary generally would discharge his oversight duties by prudently selecting the

investment funds (or investment managers), periodically evaluating their performance, and determining, based on that evaluation, whether the funds should continue to be available as participant investment options. In making these decisions the fiduciary would, of course, consider the special characteristics of ERISA section 404(c) plans.

D. Exercise of Control by a Participant

1. Generally. In view of the transactional nature of the relief provided by section 404(c), the proposed regulation makes it clear that a determination whether a participant has in fact exercised control must necessarily be made on a case by case basis, taking into account the relevant facts and circumstances.

The proposed regulation makes it clear that sections 404(c)(1) and 404(c)(2) apply only where the participant’s exercise of control has been independent. This is consistent with the Conference Report discussion of section 404(c).17 In this regard, the proposed regulation describes certain factors that indicate the absence of independent control. These are: (1) Improper influence by a plan fiduciary or plan sponsor with respect to the transaction; (2) concealment from the participant by a plan fiduciary of material nonpublic facts regarding the transaction that are known by the plan fiduciary;18 and (3) the legal incompetence of the participant where the plan fiduciary accepting his instructions knows him to be incompetent.19

The proposed regulation also provides that where a participant exercises control over the assets in his account to engage in a sale or an exchange of property or a loan with a plan fiduciary (other than a plan sponsor, or an affiliate as discussed below)20 or an

16 Conference Report, at 305.
17 As provided in paragraph (d)(5) of the proposed regulation, it is contemplated that generally a fiduciary would have no affirmative obligation to advise participants regarding the suitability of various investment options.
18 With respect to the third factor, the Department does not intend to impose an affirmative duty on the implementing fiduciary to evaluate the participant’s competence. However, the Department is of the opinion that the implementing fiduciary should not be able to invoke section 404(c) to avoid liability for losses resulting from the imprudent instructions of a participant where the fiduciary has actual knowledge of the incompetence.
19 Paragraph (e)(2)(ii)(D) of this regulation provides that section 404(c) does not relieve a fiduciary of the duty of prudently selecting a participant instruction which results in a transaction between the plan and a plan sponsor or an affiliate or the acquisition or sale of any employee securities or employer real property.

18 Conference Report, at 305.
19 As provided in paragraph (d)(5) of the proposed regulation, it is contemplated that generally a fiduciary would have no affirmative obligation to advise participants regarding the suitability of various investment options.
20 With respect to the third factor, the Department does not intend to impose an affirmative duty on the implementing fiduciary to evaluate the participant’s competence. However, the Department is of the opinion that the implementing fiduciary should not be able to invoke section 404(c) to avoid liability for losses resulting from the imprudent instructions of a participant where the fiduciary has actual knowledge of the incompetence.
21 Paragraph (e)(2)(ii)(D) of this regulation provides that section 404(c) does not relieve a fiduciary of the duty of prudently selecting a participant instruction which results in a transaction between the plan and a plan sponsor or an affiliate or the acquisition or sale of any employee securities or employer real property.

21 Restatement (Second) of Trusts section 216 (1959) provides:

Section 216. Consent of Beneficiary

(1) Except as stated in Subsections (2) and (3), a beneficiary cannot hold the trustee liable for omission of the trustee as a breach of trust if the beneficiary prior to or at the time of the act or omission consented to it.

(2) The consent of the beneficiary does not preclude him from holding the trustee liable for a breach of trust, if—

(a) the beneficiary was under an incapacity at the time of such consent or of such act or omission; or

(b) the beneficiary, when he gave his consent, did not know of his rights and of the material facts which the trustee did not reasonably believe that the beneficiary knew; or

(c) the consent of the beneficiary was induced by improper conduct of the trustee.

(3) Where the trustee has an adverse interest in the transaction, the consent of the beneficiary does not preclude him from holding the trustee liable for a breach of trust not only under the circumstances stated in Subsection (2), but also if the transaction to which the beneficiary consented involved a bargain which was not fair and reasonable.

See also III Scott, Trusts section 216 (3rd ed. 1967); Bogert, Trusts section 941 (2d ed. 1960).
plan assets are held until such time as a participant makes an investment decision. Therefore, the kinds of investments that may be used for this purpose are limited to those which can be liquidated in a reasonably short period of time and which are most likely to conserve the principal amount deposited, even though the rate of return on assets invested in this way may not be as favorable as other investment opportunities.

The Department is concerned that amounts may accumulate in a suspense account over an extended period of time because the participant is not adequately informed of his opportunity to direct investment of his account assets. Accordingly, the proposed regulation also provides that a participant will be deemed to have exercised control with respect to such automatic allocations only if reasonable procedures are established under the plan which are designed to inform participants of the nature of the passive investment options and the anticipated rate of return of each option and to elicit affirmative instructions.

The proposal also states that the special rules contained in paragraph (c) for plans that offer investment alternatives that include one or more designated pooled investment funds are not applicable to an ERISA section 404(c) plan merely because the plan provides for a "passive" investment fund pursuant to paragraph (d)(4)(ii) of the proposal.

Finally, the proposed regulation specifically states that fiduciaries of an ERISA section 404(c) plan generally have no obligation to advise the participant regarding the suitability of making an investment or of the advisability of retaining an investment that has already been made.

E. Effect of a Participant's Independent Exercise of Control

1. Participant not treated as a fiduciary. As provided in section 404(c)(1), the proposed regulation states that a participant is not considered to be a fiduciary solely because he exercises control over assets in his individual account. This provision has two primary effects. First, because a participant is not a fiduciary, he would not violate the prohibited transaction provisions of Title I of ERISA if he exercises control over assets in his account to engage in a transaction with a party in interest. Second, other fiduciaries generally would have no co-fiduciary liability under section 406 of the Act with respect to participant investment decisions under ERISA section 404(c) plans.

2. Other fiduciary responsibilities. The proposed regulation discusses in more detail the consequences to other plan fiduciaries of a participant's exercise of control. Section 404(c) provides that plan fiduciaries are relieved of liability for losses, or with respect to breaches of the requirements of Title I, which "result" from a participant's exercise of control over individual account assets. Thus, given the transactional nature of the relief provided by section 404(c), it is necessary to determine in any particular case whether alleged losses or violations resulted from a participant's investment decision.

In the Department's view, section 404(c) was not intended to apply in those situations where losses are attributable to intervening breaches of fiduciary responsibility by the plan official implementing the participant's instructions. Thus, the proposed regulation states that a fiduciary is relieved of responsibility only for the direct and necessary consequences of a participant's exercise of control.

Accordingly, if a participant gives investment instructions to a plan fiduciary, and, due to the imprudence of the fiduciary in carrying out the instructions, the participant suffers a loss, then the fiduciary is liable for such loss because it resulted from a breach of his duties as a fiduciary rather than from the participant's exercise of control.

Similarly, if a participant gives investment instructions that may be carried out in more than one way, and the fiduciary chooses a method of carrying out the instructions that results in a breach of his obligations as a fiduciary, then he is liable for any resulting losses because such losses would not be a necessary consequence of the participant's exercise of control. Thus, if a participant directs a fiduciary to acquire certain securities, but does not specify the manner in which the acquisition is to be effected, and the fiduciary causes a party in interest to execute the transaction, the fiduciary would be liable with respect to the resulting prohibited transaction (unless an exemption is otherwise available) notwithstanding the participant's exercise of control.

The proposal also specifically states that the individual investment decisions of an investment manager are not direct and necessary results of the participant's designation of the investment manager or of investment in a pooled investment fund managed by the investment manager. In the Department's view, this provision is consistent with the general rule describing the scope of the relief provided by section 404(c)(2). However, the proposed regulation also provides that this rule should not be construed to impose co-fiduciary liability on a fiduciary who would otherwise be relieved of liability under section 404(c).

Thus, if a participant chooses an investment manager who imprudently invests plan assets, the investment manager will not be relieved of liability because his imprudence resulted from a direct and necessary result of the participant's exercise of control.

However, other plan fiduciaries would be relieved of liability under section 405, even if, for example, they had knowledge of the investment manager's imprudent decisions. A fiduciary that designates an investment manager or pooled fund in the manner contemplated by paragraph (c) of the regulation, would, however, be required to take any known imprudence of the manager into account in determining whether to continue the designation of that manager.

As noted above, liability results from the investment manager's imprudent exercise of discretionary authority over plan assets because, once a participant has invested in a pooled investment fund, the participant no longer has control over the individual investment decisions concerning the assets which are invested in the fund.
It is important to note that the proposed rule relating to individual investment decisions of an investment manager relates only to the scope of the relief provided by section 404(c)(2); it is not intended to create fiduciary duties which would not otherwise exist. Thus, even though the individual decisions of the investment manager of an investment company registered under the Investment Company Act of 1940 would not be considered to "result" from a participant’s decision to invest in the company, the manager would have no liability under ERISA for any losses because mutual fund investment advisers are excluded from the statutory definition of "fiduciary" in ERISA (see sections 3(21)(B) and 401(b)(1) of ERISA).

3. Limitations. There are four exceptions to the general rule in the proposed regulation regarding the relief provided to a fiduciary. Under these exceptions, a plan fiduciary will not be relieved of liability with respect to a participant’s instructions which: (a) would not be in accordance with the documents and instruments governing the plan; (b) would cause a fiduciary to maintain the indicia of ownership of any assets of the plan outside of the jurisdiction of the United States (other than as permitted by section 404(b) of the Act); (c) would result in a direct or indirect acquisition, sale, or lease of property (including employer securities or employer real property) between a participant and a plan sponsor or an affiliate of the sponsor or a direct or indirect loan to a plan sponsor or any affiliate of the sponsor. In addition, a plan fiduciary will not be relieved of liability with respect to any sale, acquisition or lease of employer securities or employer real property whether or not the transaction involves the employer.

The Conference Report expresses concern regarding participant-directed investments which may inure to the direct or indirect benefit of a plan sponsor and indicates that the Department should impose special standards with respect to such investments. The proposed regulation does not provide relief under section 404(c) with respect to these investments because the Department does not believe that the information necessary to determine if it is appropriate to apply section 404(c) to participant-directed investments which may benefit a plan sponsor, or to determine the kinds of safeguards that might be appropriate to assure that participants are not subjected to undue influence with respect to such investments.

Nonetheless, the Department recognizes that many participant-directed plans do permit investments in such property and that the Conference Report might be read to contemplate that section 404(c) would apply to at least some participant decisions to invest in property acquired from an employer and in employer securities and employer real property. Thus, the Department specifically invites comments addressing the issue. Such comments should assist the Department in developing a final rule which will limit the potential for the exercise of improper influence by the plan sponsor, but not unduly restrict participant investment options. The Department is particularly interested in comments describing current practices with respect to property acquired from or sold to plan sponsors, the benefits of such investments and the safeguards which exist with respect to such investments.

With respect to employer securities, the Department is particularly interested in commentators’ views concerning whether a participant’s investments should be limited to a specified percentage of his account balance and/or whether such investments should be limited to publicly-offered securities.

Investment in employer real property, however, appears to be less liquid and may be less appropriate as a participant investment alternative. Accordingly, comments describing any participant investment alternatives that involve employer real property, the safeguards (such as investment limitations) that exist with respect to such investments, and the benefits to the participant of this particular type of real estate investment will be particularly helpful.

4. Prohibited transactions. Finally, the proposed regulation makes it clear that, if the conditions to the availability of the relief described in section 404(c)(2) otherwise are met, a fiduciary would be relieved from direct liability (in addition to any co-fiduciary liability) for engaging in a prohibited transaction in violation of section 406 of ERISA if the prohibited transaction is a direct and necessary consequence of the participant’s exercise of control. However, the proposed regulation also makes it clear that the relief provided by section 404(c)(2) extends only to the provisions of part 4 of Title I of ERISA (relating to fiduciary responsibility).

Therefore, even if a prohibited transaction is a direct and necessary consequence of a participant’s exercise of control, nothing in section 404(c) of ERISA would relieve a “disqualified person” described in section 4975(e)(2) of the Code (including a fiduciary) from liability for the taxes imposed by sections 4975(a) and (b) of the Code with respect to such prohibited transaction. In this respect, the Department notes that, although Reorganization Plan Number 4 of 1978 generally transfers the authority of the Secretary of the Treasury to grant exemptions from the provisions of section 4975 of the Code to the Secretary of Labor, authority to issue exemptions for transactions with respect to which a fiduciary is relieved of liability under section 404(c) is expressly left with the Secretary of the Treasury.

Accordingly, the Department has no authority to provide exemptive relief for a disqualified person’s liability for the excise taxes imposed by section 4975 of the Code with respect to a prohibited transaction that results from a participant’s exercise of control pursuant to section 404(c).

Reporting and Disclosure

The proposal also does not address the reporting and disclosure provisions of ERISA with respect to their applicability to ERISA section 404(c) plans. The Department does, however, specifically invite comments discussing the application of the existing reporting and disclosure requirements of ERISA to
such plans and whether it would be appropriate for the Department to develop an alternative method of compliance under section 110 of ERISA for ERISA section 404(c) plans.

Effective Date

In general, the proposed regulation would be effective with respect to transactions occurring in plan years beginning after a date 90 days from the date the regulation is published in final form. Transactions before that date would be governed by section 404(c) of the Act without regard to the regulation.

Technical Revisions

Pursuant to recent amendments to the rules for publication of the Office of the Federal Register, this proposal contains a proposed amendment of the authority citation for Part 2550 of Chapter XXV of Title 29 of the Code of Federal Regulations.

Executive Order 12291 Statement

The Department has determined that the proposed regulatory action would not constitute a “major rule” as that term is used in Executive Order 12291 because the action would not result in: an annual effect on the economy of $100 million; a major increase in costs or prices for consumers, individual industries, government agencies, or geographical regions; or significant adverse effects on competition, employment, investment, productivity, innovation, or on the ability of United States based enterprises to compete with foreign based enterprises in domestic or export markets.

Regulatory Flexibility Act Statement

The Department has determined that this regulation would not have a significant economic effect on small plans. In conducting the analysis required under the Regulatory Flexibility Act, it was estimated that the total annual cost to the approximately 15,600 small plans which may be affected by the regulation would be just over $6 million, or a cost of approximately $410 per plan. This does not reflect an actual increase in costs to most plans with participant directed account features since the regulations are intended to reflect, to a large extent, current administrative practices by these plans.

Paperwork Reduction Act Statement

This proposed regulation contains several paperwork requirements. The regulation has been forwarded for approval to the Office of Management and Budget under the provisions of the Paperwork Reduction Act of 1980 (P.L. 96-511). A control number has not yet been assigned.

Statutory Authority


List of Subjects in 29 CFR Part 2550


In view of the foregoing the Department proposes to amend Part 2550 of Chapter XXV of Title 29 of the Code of Federal Regulations as follows:

PART 2550—RULES AND REGULATIONS FOR FIDUCIARY RESPONSIBILITY

1. By revising the authority citation for Part 2550 to read as set forth below and the authority citations following all the sections in Part 2550 are removed.


§ 2550.404(c)-1 also issued under 29 U.S.C. 1104.

§ 2550.404(c)-3 also issued under 29 U.S.C. 1107.

§ 2550.412-1 also issued under 29 U.S.C. 1112.

§ 2550.414b-1 also issued under 29 U.S.C. 1114.

Secretary of Labor’s Order No. 1-86.

2. By adding a new § 2550.404(c)-1 to read as follows:

§ 2550.404(c)-1 ERISA Section 404(c) Plans.

(a) In General. Section 404(c) of the Act provides that if a pension plan that provides for individual accounts permits a participant or beneficiary to exercise control over the assets in his account and that participant or beneficiary in fact exercises control over assets in his account, then the participant or beneficiary shall not be deemed to be a fiduciary by reason of his exercise of control and no person who is otherwise a fiduciary shall be liable for any loss, or by reason of any breach, which results from such exercise of control. This section describes the kinds of plans that are “ERISA section 404(c) plans,” the circumstances in which a participant is considered to have exercised independent control over the assets in his account as contemplated by section 404(c), and the consequences of a participant’s exercise of control over the assets in his account.

(b) ERISA section 404(c) plans—(1) In general. An “ERISA section 404(c) plan” is an individual account plan described in section 3(34) of the Act that:

(i) Provides an opportunity for a participant or beneficiary to exercise control over the assets in his individual account (see paragraph (b)(2));

(ii) Provides a participant or beneficiary an opportunity to choose, from a broad range of investment alternatives, the manner in which some or all of the assets in his account are invested (see paragraph (b)(3));

(iii) Provides a participant or beneficiary an opportunity to invest some or all of the assets in his account in an investment which is either:

(A) An interest-bearing deposit in a bank or similar financial institution, which deposit has a high degree of liquidity and is fully insured against loss by the United States or an agency of the United States, or

(B) A pooled investment fund the assets of which consist solely of cash and securities issued or guaranteed by the United States or one of its agencies and the principal investment objectives of which include a high level of current income consistent with the preservation of capital and a high degree of liquidity; and

(iv) Meets the requirements of paragraph (c), in the case of a plan under which the investment alternatives available to a participant or beneficiary include investment in one or more designated pooled investment funds or the selection by a participant of one or more designated investment managers.

(2) Opportunity to exercise control. (i) A plan provides a participant or beneficiary the opportunity to exercise control over assets in his account if, under the terms of the plan, the participant or beneficiary has a reasonable opportunity to give written investment instructions (or oral instructions followed by a written confirmation of such instructions returned to the participant) to an identified plan fiduciary who is obligated to comply with such instructions.

(ii) A plan does not fail to provide an opportunity for a participant or beneficiary to exercise control over his individual account merely because it—

(A) Imposes reasonable restrictions on the frequency with which the
participant or beneficiary may give investment instructions;  
(B) Charges the participant or beneficiary’s account for the reasonable expenses of carrying out his instructions, provided reasonable procedures are established under the plan to inform participants that such charges are made and to inform each participant periodically of the actual expenses associated with respect to his individual account; or  
(C) Permits a fiduciary to decline to implement participant instructions which would generate income that would be taxable to the plan.  
(iii) Paragraph (d) of this section describes the circumstances under which a participant or beneficiary will be considered to have exercised independent control with respect to a particular transaction.  
(3) Broad range of investment alternatives.  
(i) A plan offers a broad range of investment alternatives only if the available alternatives are sufficient to provide the participant or beneficiary with a reasonable opportunity to:  
(A) Materia lly affect the potential return on amounts in his individual account with respect to which he is permitted to exercise control and the degree of risk to which such amounts are subject;  
(B) Choose from a diversified group of investments within each of the following categories:  
(1) Investments which can reasonably be expected to result in the generation of a high level of income while preserving capital in the long term;  
(2) Investments which can reasonably be expected to result in capital appreciation, or  
(3) Investments which can reasonably be expected to result in the generation of a high level of current income consistent with the preservation of capital and a high degree of liquidity; and,  
(C) Diversify the investments of that portion of his individual account with respect to which he is permitted to exercise control so as to minimize the risk of large losses, taking into account the nature of the plan and the size of participants' accounts.  
(ii) Diversity and pooled investment funds. Where pooled investment funds are available as investment options to participants or beneficiaries, the following investment alternatives of the pooled investment funds shall be considered in determining whether the plan satisfies the requirements of paragraphs (b)(3)(i)(B) and (b)(3)(ii)(C) (relating to diversification of investments).  
(iii) In determining whether a plan provides a broad range of investment alternatives, only those investment alternatives are to be taken into account to which sufficient information is available to the participant or beneficiary to permit informed investment decisions.  
(c) Special Rule for Designated Pooled Investment Funds and Investment Managers—(1) In general. A plan under which the investment alternatives available to a participant or beneficiary include investment in one or more designated pooled investment funds (other than a fund described in paragraph (b)(1)(iii) or (d)(4)(ii)) or the right to choose from one or more designated investment managers, shall be treated as an ERISA section 404(c) plan only if it meets the requirements of this paragraph in addition to the requirements of paragraph (b).  
(2) Pooled investment funds.  
(i) A plan under which the investment alternatives available to a participant or beneficiary include investment in designated pooled investment funds is an ERISA section 404(c) plan only if, under the plan, an independent fiduciary is required to designate a diversified group of pooled investment funds (as described in paragraph (c)(2)(iii)).  
(ii) For purposes of this paragraph (c)(2), a “diversified group” of pooled investment funds is a group of at least four funds each of which has a different one of the following primary objectives:  
(A) The generation of the highest level of income consistent with the preservation of capital over the long term;  
(B) Capital appreciation;  
(C) A balance between capital appreciation and preservation of capital and generation of income; and  
(D) The generation of a high level of current income consistent with the preservation of capital and a high degree of liquidity.  
(3) Designated investment managers.  
A plan under which the investment alternatives available to a participant or beneficiary include the right to appoint a designated investment manager is an ERISA section 404(c) plan only if, under the plan, an independent fiduciary is required to designate the investment manager(s) which the participant or beneficiary may appoint.  
(4) Independent fiduciary.  
For purposes of this paragraph (c), a fiduciary is an independent fiduciary if he is not affiliated with any designated pooled investment fund or any investment manager with respect to which such a fund or with any designated investment manager.  
(d) Exercise of control—(1) In general.  
(e) of this section applies only with respect to a transaction where a participant or beneficiary has exercised independent control in fact with respect to the investment of assets in his individual account under an ERISA section 404(c) plan.  
(2) Independent control. Whether a participant or beneficiary has exercised independent control in fact with respect to a transaction depends on the facts and circumstances of the particular case. However, a participant’s or beneficiary’s exercise of control is not independent in fact if:  
(i) The participant or beneficiary is subject to improper influence by a plan fiduciary or the plan sponsor with respect to the transaction;  
(ii) A plan fiduciary has concealed material non-public facts regarding the transaction from the participant or beneficiary; or  
(iii) The participant or beneficiary is legally incompetent and the responsible plan fiduciary accepts the instructions of the participant or beneficiary knowing him to be legally incompetent.  
(3) Transactions involving a fiduciary.  
In the case of a sale, exchange or leasing of property (other than a transaction described in paragraph (e)(2)(ii)(D)) between an ERISA section 404(c) plan and a plan fiduciary or an affiliate of such a fiduciary, or a loan to a plan fiduciary or an affiliate of such a fiduciary, the participant or beneficiary will not be deemed to have exercised independent control unless the transaction is fair and reasonable to him. For purposes of this paragraph (d)(3), a transaction will be deemed to be fair and reasonable to a participant or beneficiary if he pays no more than, or receives no less than, adequate consideration (as defined in section 3(18) of the Act) in connection with the transaction.  
(4) Absence of affirmative direction.  
Generally, an affirmative investment direction by a participant or beneficiary is required to establish that a participant or beneficiary has exercised independent control with respect to an investment. However, a participant or beneficiary shall be deemed to have exercised independent control with respect to investments of any amount in his individual account over which he is permitted to exercise control, but as to which he has not given affirmative investment instructions, if:  
(i) Reasonable procedures are established under the plan—  
(A) To inform participants of the manner in which individual account assets will be invested in the absence of affirmative instructions and the
anticipated rate of return on such investments; and
(B) To elicit affirmative investment instructions from the participant; and
(ii) Amounts with respect to which no affirmative investment instructions have been received are invested in an investment vehicle described in paragraph (b)(1)(iii).

(5) No obligation to advise. In general, a fiduciary has no obligation under part 4 of Title I of the Act to provide advice to a participant or beneficiary with respect to an investment made pursuant to the participant's or beneficiary's independent exercise of control under an ERISA section 404(c) plan. See paragraph (d)(2)(ii), however, with respect to the effect of a fiduciary's concealment of material, nonpublic facts regarding a transaction.

(e) Effect of independent exercise of control—(1) Participant or beneficiary not a fiduciary. If a participant or beneficiary of an ERISA section 404(c) plan exercises independent control over assets in his individual account in the manner described in paragraph (d), then such participant or beneficiary is not a fiduciary of the plan by reason of such exercise of control.

(2) Limitation on liability of plan fiduciaries. (i) If a participant or beneficiary of an ERISA section 404(c) plan exercises independent control over assets in his individual account in the manner described in paragraph (d), then no other person who is a fiduciary with respect to such plan shall be liable for any loss, or with respect to any breach of part 4 of Title I of the Act, that is the direct and necessary result of the participant's or beneficiary's exercise of control.

(ii) Paragraph (e)(2)(i) does not apply with respect to any instruction which, if implemented—
(A) Would not be in accordance with the documents and instruments governing the plan insofar as such documents and instruments are consistent with the provisions of Title I of ERISA;
(B) Would cause a fiduciary to maintain the indicia of ownership of any assets of the plan outside the jurisdiction of the district courts of the United States other than as permitted by section 404(b) of the Act and 29 CFR 2550.404b-1;
(C) Would jeopardize the plan's status as a trust described in section 401(a) of the Internal Revenue Code; or
(D) Would result in a direct or indirect sale, exchange, or lease of property between a plan sponsor or any affiliate of the sponsor and the plan;

(2) Loan to a plan sponsor or any affiliate of the sponsor;
(3) Acquisition or sale of any employer security (as defined in section 407(d)(1) of the Act); or
(4) Acquisition, sale, or lease of any employer real property (as defined in section 407(d)(2) of the Act).

(iii) The individual investment decisions of an investment manager who is designated directly by a participant or who manages a pooled investment fund in which a participant has invested are not direct and necessary results of the designation of the investment manager or of investment in the pooled investment fund. However, this paragraph (e)(2)(iii) shall not be construed to result in liability under section 405 of ERISA with respect to a fiduciary (other than the investment manager) who would otherwise be relieved of liability by reason of section 404(c)(2) of the Act and this paragraph (e).

(3) Prohibited transactions. The relief provided by section 404(c) of the Act and this section applies only to the provisions of Part 4 of Title I of the Act. Therefore, nothing in this section relieves a disqualified person from the taxes imposed by sections 4975(a) and (b) of the Internal Revenue Code with respect to the transactions prohibited by section 4975(c)(1) of the Code.

(f) Definitions. For purposes of this section:

(1) "Pooled investment fund" means:
(i) An investment company described in section 3(a) of the Investment Company Act of 1940.
(ii) A common or collective trust fund or a pooled investment fund maintained by a bank.
(iii) A pooled separate account of an insurance company qualified to do business in a State, or
(iv) Any entity whose assets include plan assets by reason of a plan's investment in the entity;
(2) "Adequate consideration" has the meaning given it in section 3(18) of the Act and in any regulations under this title;
(3) "Investment manager" includes any person described in section 3(38) of the Act and any person who exercises discretionary authority or control over the assets of a plan or a pooled investment fund or who provides investment advice with respect to such assets for a fee;
(4) An "affiliate" of a person includes the following:
(I) Any person directly or indirectly controlling, controlled by, or under common control with the person;
(II) Any officer, director, partner, employee, an employee of an affiliated employer, relative (as defined in section 3(15) of ERISA), brother, sister, or spouse of a brother or sister, of the person; and
(iii) Any corporation or partnership of which the person is an officer, director or partner.

For purposes of this paragraph (f)(4), the term "control" means, with respect to a person other than an individual, the power to exercise a controlling influence over the management or policies of such person.

(g) Examples. The provisions of this section are illustrated by the following examples. Examples (5) through (12) assume that the participant has exercised independent control with respect to his individual account under an ERISA section 404(c) plan described in paragraph (b) and has not directed a transaction described in paragraph (e)(2)(ii).

(1) Plan A is an individual account plan described in section 3(34) of the Act under which a plan participant may direct the plan administrator to invest any portion of his individual account in any asset which it is administratively feasible for the plan to hold and the acquisition of which would not result in disqualification of the plan under the Internal Revenue Code. Plan A provides that the plan administrator is obligated to effect participant investment instructions when requested but must decline to implement any participant instructions which would not be in accordance with plan documents or which would cause a fiduciary to hold the indicia of ownership of any plan assets outside the jurisdiction of the district courts of the United States. In addition, Plan A provides that the administrator is required to forward to the participant any proxy solicitations, periodic reports, and other communications with respect to participant directed investments in publicly-offered securities. Plan A is an ERISA section 404(c) plan. Although a participant in Plan A would be permitted to direct an investment as to which there is not sufficient information available to permit an informed investment decision, it nonetheless provides a broad range of investment alternatives as to which such information is available (i.e., publicly-offered securities).

Finally, Plan A is an ERISA section 404(c) plan notwithstanding that it does not meet the requirements of paragraph (c) because it does not limit the choices of pooled funds or investment managers to designated funds or to designated brokers.

(2) Plan B is an individual account plan described in section 3(34) of the Act. Plan B provides for participant directed investments in the following manner: Under the plan, participants may direct investments only in shares of mutual funds designated by the plan's named fiduciary or in a government securities investment fund described in paragraph (b)(1)(i) and designated by the plan's named fiduciary. The plan document requires the named fiduciary to designate a "diversified group" of mutual funds (as...
described in paragraph (g)(5) as permissible participant investments. Pursuant to the terms of the plan, the appropriate plan fiduciary designates diversified income, growth, balance, and cash equivalency funds all of which are managed by one investment manager. Absent other relevant circumstances, ERISA section 404(c) plan because: (i) Under the terms of the plan, participants and beneficiaries have a reasonable opportunity to give investment instructions to a plan fiduciary who is obligated to carry out those instructions (as described in paragraph (b)(2)(ii); (ii) the investment alternatives available to a participant or beneficiary allow him to significantly affect the potential return on his individual account balance, and (iii) the participant or beneficiary is permitted to diversify the investments of his account since the income, growth, balance, and cash equivalency pooled investment funds are each diversified (see paragraph (b)(2)(ii)). The plan is required to meet the requirements of paragraph (c) because the pooled investment funds in which participants may invest are limited to designated funds, but Plan B satisfies the requirements of paragraph (c) because it provides the participant a choice to diversify his account to include fixed income obligations, but does not designate a cash equivalency fund. Plan B is not a section 404(c) plan because the plan fiduciary has not specified as least one fund within each of the four categories of funds described in paragraph (b)(2). If, however, the appropriate fiduciary designates a cash equivalency fund, Plan B would then be an ERISA section 404(c) plan.

(3) Assume that Plan B contains the same provisions as those described in paragraph (g)(2). However, the appropriate plan fiduciary designates one diversified growth fund, one diversified balanced fund, and one diversified balanced fund, but does not designate a cash equivalency fund. Plan C is not a section 404(c) plan because the plan fiduciary has not specified at least one fund within each of the four categories of funds described in paragraph (b)(2). If, however, the appropriate fiduciary designates a cash equivalency fund, Plan B would then be an ERISA section 404(c) plan.

(4) Assume that Plan C contains a diversified account plan described in section 3(34) of the Act, permits a participant to give investment instructions to the plan administrator in the same manner as Plan A (see paragraph (g)(1)). Plan C, however, contains only diversified funds, to which his account balance is subject, and (iii) the participant or beneficiary is permitted to diversify the investments of his account since the income, growth, balance, and cash equivalency pooled investment funds are each diversified (see paragraph (b)(2)(ii)). The plan is required to meet the requirements of paragraph (c) because the pooled investment funds in which participants may invest are limited to designated funds, but Plan B satisfies the requirements of paragraph (c) because it provides the participant a choice to diversify his account to include fixed income obligations, but does not designate a cash equivalency fund. Plan B is not a section 404(c) plan because the plan fiduciary has not specified as least one fund within each of the four categories of funds described in paragraph (b)(2). If, however, the appropriate fiduciary designates a cash equivalency fund, Plan B would then be an ERISA section 404(c) plan.

(5) A participant, P, independently exercises control over assets in his individual account plan by directing a plan fiduciary, F, to invest 100% of his account balance in a single stock. P is not a fiduciary with respect to the plan by reason of his exercise of control and F will not be liable for any losses that may necessarily result from P’s investment instruction.

(6) Assume the same facts as in paragraph (5), except that P directs F to purchase the stock from B, who is a party in interest with respect to the plan. Neither P nor F has engaged in a transaction prohibited under section 406 of the Act because he is not a fiduciary with respect to the plan by reason of paragraph (b)(2)); (ii) the investment alternatives available to a participant or beneficiary allow him to significantly affect the potential return on his individual account balance, and (iii) the participant or beneficiary is permitted to diversify the investments of his account since the income, growth, balance, and cash equivalency pooled investment funds are each diversified (see paragraph (b)(2)(ii)). The plan is required to meet the requirements of paragraph (c) because the pooled investment funds in which participants may invest are limited to designated funds, but Plan B satisfies the requirements of paragraph (c) because it provides the participant a choice to diversify his account to include fixed income obligations, but does not designate a cash equivalency fund. Plan B is not a section 404(c) plan because the plan fiduciary has not specified at least one fund within each of the four categories of funds described in paragraph (b)(2). If, however, the appropriate fiduciary designates a cash equivalency fund, Plan B would then be an ERISA section 404(c) plan.

(7) Assume the same facts as in paragraph (5), except that P does not specify the use of B and F chooses to purchase the stock from C. In the absence of an exemption, F has engaged in a prohibited transaction described in 406(a)(1) of ERISA because the participant was not given the opportunity to diversify his investments.

(8) Pursuant to the terms of the plan, plan fiduciary F designates three reputable investment managers which participants may appoint to manage assets in their individual accounts. Participant P selects M, one of the designated managers, to manage assets in his account. M prudently manages P’s account for 6 months after which he incurs losses in managing the account through his imprudence. M has engaged in a breach of fiduciary duty because M’s imprudent management of P’s account is not a direct or necessary result of P’s exercise of control.

(9) Participant P, in exercising control over the assets in his individual account, directs a plan fiduciary F to purchase a limited partnership share in a limited partnership managed by Y. Participant P instructs plan fiduciary F to purchase the limited partnership share in his individual account. F provides P with a confidential report which is pessimistic concerning the prospects of the investments made by the partnership. Without disclosing the contents of the report, F executes P’s instructions. Participant P has not exercised independent control in fact with respect to the transaction because F has concealed a material nonpublic fact (the pessimistic report) from P (see paragraph (d)(2)(ii)).

(h) Effective date. This section is effective with respect to transactions occurring in plan years beginning after [90 days after publication of a final rule]. Transactions occurring before that date would be governed by section 404(c) of the Act without regard to the regulation.
Part III

Department of Labor

Employment and Training Administration

20 CFR Part 602
Federal-State Unemployment Compensation Program; Unemployment Insurance Quality Control Program; Final Rule
DEPARTMENT OF LABOR
Employment and Training Administration
20 CFR Part 602
Federal-State Unemployment Compensation Program; Unemployment Insurance Quality Control Program
AGENCY: Employment and Training Administration, Labor.
ACTION: Final rule.

SUMMARY: The Secretary of Labor is issuing the final regulation to establish a permanent Quality Control program for the Federal-State unemployment insurance system. The Quality Control program will be a major tool to assess the timeliness and accuracy of State administration of unemployment insurance in order to improve program performance and revenue collection, and to reduce inaccurate benefit payments and claims denials, administrative errors, and abuse in the unemployment insurance system.


FOR FURTHER INFORMATION CONTACT: Carolyn M. Golding, Director, Unemployment Insurance Service, Employment and Training Administration, U.S. Department of Labor, Room S-4231, Francis Perkins Building, 200 Constitution Ave. NW., Washington, DC 20210. Telephone: (202) 535-0660 (this is not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background
Recent reviews of benefit payments and revenue collections indicate potentially serious problems in the Federal-State Unemployment Insurance (UI) system. The Random Audit program, which evaluated benefit payments in 48 States, found a percentage of errors in making payments which needs to be reduced. In addition, audits of benefits payment control, tax accounting and cash management activities indicated the need for improvement in all of these functions. To address these needs, a Quality Control (QC) program will be initiated; QC will expand upon previous efforts, notably the Random Audit program, and provide the basis for diagnosing problems and taking corrective actions.

QC Will Be Mandatory
The QC program will be the principal means by which the Federal-State UI partners evaluate the administration of a State's UI law and achieve improvement in program operations. Its design relies heavily on the experience of the Random Audit program, which was voluntary for the States. Given the importance of ensuring the accurate and timely payment of benefits to eligible UI claimants and the accurate and prompt collection of UI revenues, however, participation of the States in the QC program will be mandatory.

Section-by-Section Regulatory Highlights
Subpart A, General Provisions, sets out the purpose and scope of the QC program, including the laws to which the regulation applies.
Subpart B, Federal Requirements, defines the authority under which these regulations are issued. It also explains the Secretary of Labor's (Secretary) interpretation of the authority allowing the Department of Labor (Department) to make the QC program mandatory.

The Department does not believe that a mandatory QC program will require any State to go beyond its current law to fulfill the methods of administration requirement in section 303(a)(1) of the Social Security Act (SSA) (42 U.S.C. 503(a)(1)) as the QC program is an expansion/enhancement of other Federal-State UI evaluation programs, such as Random Audit and Quality Appraisal, which have been operative in State agencies for some time. States are encouraged, however, to review their laws to ensure that an adequate legal basis exists for implementing QC.

Subpart C, State Responsibilities, contains requirements which ensure the objectivity of the State's QC unit and eliminates potential conflicts of interest.

Subpart D, Federal Responsibilities, defines the management and oversight responsibilities required of the Department to be excessive in relating authority to recapture QC granted funds in cases other than those in which the benefits of operating a QC program might be deemed by the Department to be excessive in relating to the overall results obtained.

Subpart E, QC Grants to States, provides that: (1) The Secretary has the authority to recapture QC funds expended which are not necessary for the proper and efficient administration of the QC program; and (2) after notice and a hearing, the Secretary may withhold all Title III grants from a State that fails to implement a QC program in accordance with Part 602. However, under Part 602, there is no sanction or incentive to influence achievement of any specific error rate, although errors revealed by the QC operation might result in questions being raised about methods of administration or other Federal requirements.

Consultation for Development of the Proposed Rule
The Department published an Advance Notice of Proposed Rulemaking in the Federal Register on September 26, 1984, at 49 FR 38083, to inform interested persons of its intentions to establish a permanent QC program for the UI system. During the 30-day comment period, the Department received five letters with comments. Prior to and after the request for formal comments, the Department held numerous meetings with those involved in the UI system to solicit ideas and reactions to the proposed design of the QC system.

In June 1985, the Secretary of Labor directed the undertaking of a wide-ranging policy review. The purpose of the review was to explore fully and
formally the basic policy decisions forming the framework of the QC system and to ensure full participation of the many groups involved in UI administration.

The Secretary's review was announced in a notice published in the Federal Register on August 6, 1985, at 50 FR 31767 and a public meeting was announced to be held on August 21, 1985, at 50 FR 31792, inviting viewpoints, suggestions, and alternative approaches from Governors, employer groups, organized labor, and State Employment Security Administrators. Each group was asked to comment specifically on nine (9) design issues which were described in the Federal Register on August 6, 1985, at 50 FR 31767.

Listed below are decisions on the nine design issues which were reached after consideration of the 61 comments received.

1. **System Operations.** The QC system will provide mixed Federal/State division of responsibilities.
2. **Coverage.** QC will be mandatory for the States.
3. **Access to Data.** States will be required to release QC results annually using a standard format, retaining the option of release by States before any national release.
4. **Scope.** QC investigations will be conducted State-wide at Federally-established sample levels. Beyond the minimum sampling effort, States will be given the flexibility to examine subjects more closely through such choices as increased sample size, augmented sampling, or special studies.
5. **Investigative Objectives.** Case reviews of the QC sample claims will focus on both outcomes and process.
6. **Purpose.** The QC program will focus on correcting, not just measuring problems. Data to support operational corrections will be required and data to affect policy and legislative changes will be optional.
7. **Methodology.** QC will feature a prescribed minimum sample size specified for each State, standard definitions and methodology, and will offer flexibility for additional State-designed sampling and special studies (subject to Departmental approval).
8. **Error Correction Strategies.** The Department will encourage corrective action and foster it through technical assistance, but will not mandate corrective action.
9. **Programs Included.** QC will cover both paid and denied claims under all major regular benefit programs as well as revenue activities and it will be gradually extended to other programs such as Extended Benefits and Trade Readjustment Allowances.

In response to the Secretary's review of QC, representatives of several District of Columbia-based public interest groups including the Interstate Conference of Employment Security Agencies, Inc. (ICESA), the National Conference of State Legislatures, the National Federation of Independent Businesses, the Council of State Chambers of Commerce, UBA Inc. (United Benefit Advisor, Inc.), the U.S. Chamber of Commerce, and the American Federal of Labor-Congress of Industrial Organizations (AFL-CIO), suggested a series of QC principles. These consensus principles (described later under Major Themes) were adopted as policy by the Department and issued in Unemployment Insurance Program Letter (UIPL) No. 4-86, on December 29, 1985.

The proposed regulation was written to conform to the consensus principles plus the decisions on the design issues. Decisions which deal with procedural subjects are reflected in The Benefits Quality Control State Operations Handbook (Benefits QC Handbook) which the Department prepared and issued separately for comment.

**Comments Received in Response to the Notice of Proposed Rulemaking**

The proposed rule (new Part 602) to establish the QC program was published for comment in the Federal Register on July 25, 1986 at 51 FR 28840. On August 12, 1986, the Department extended the period for comments on the proposed rule until September 9, 1986, at 51 FR 28840.

The Department received timely comments from 33 organizations and individuals. An additional seven organizations submitted comments after the close of the comment period. The majority of comments were from State Employment Security Agencies (SESAs); comments were also received from other interested parties such as public interest groups. All comments received timely were given careful consideration in preparing the final regulation in this document.

**Major Themes in the Comments**

Three major themes were present in the comments: (1) questioning the Secretary's authority to mandate a QC program as a requirement under the Federal law; (2) a desire for more specificity in the regulation; and (3) the desire that the regulation reflect the consensus recommendations previously accepted by the Department which were submitted by ICESA on behalf of several District of Columbia-based public interest groups.

The first major area of concern, the Secretary's authority to mandate the program, is addressed in section-by-section analysis that follows. The request for specificity, the second major theme, reflected States' expressed desire to be protected from any undue exercise of Departmental discretion outside the regulatory process. Ten commenters expressed concern about the failure of the proposed regulation to specify all of the requirements of the QC program. After carefully considering these comments, the Department has concluded that the regulatory approach taken, that of issuing a broad and brief implementing regulation supported by detailed operating procedures in handbooks, is the most appropriate way of establishing the program. The regulation establishes and defines the program while the handbooks provide the necessary level of detail and flexibility needed to initiate and operate the QC program. This approach is considered appropriate because it allows for phasing in QC and making handbook changes based on early experience. It is also consistent with the Administration's desire to limit detailed regulations where possible. The Department committed itself to gathering the maximum possible public and State input before modifying and issuing the regulation in this document and the operations' handbooks.

Although they will not be published in the Federal Register, handbooks containing detailed operating procedures have been and will continue to be broadly circulated for comment before being issued or modified by the Department.

In a related group of responses, thirteen commenters identified particular sections of the regulation that they believed did not provide sufficient specificity for the States (e.g., contents of the questionnaire, timing/contents of the annual release of data). The Department does not want to make these sections more specific because of the need for flexibility to make the QC program more comprehensive in succeeding years. These items will be part of the handbooks and will be circulated widely for comment before being issued or modified by the Department.

The third theme was that the consensus principles be included in the regulation. These principles were suggested by representatives of the previously listed District of Columbia-based public interest groups. They were outlined in an issuance from the Department that was sent to all interested parties (UIPL No. 4-86). Six
commenters requested that the consensus principles be incorporated in the body of the regulation. Another fourteen requested that certain specific principles be included.

Although the principles are already embodied in the operations handbooks and other implementing instructions, the Department agrees they should be specifically included in the regulation as well. The principles, with the sections of the regulation modified to embody them indicated in brackets, follow:

1. All States would perform "Core QC." That is, a minimum of 400 weeks claimed cases, per State per year, would be investigated to determine whether the payments were proper. [§ 602.21(b)] Only those data elements that relate to eligibility for UI benefits would be collected. [§ 602.21(c)(5)] [This principle was accepted in modified form by the Department to (1) substitute "cases of weeks paid" for "weeks claimed cases" and (2) include the collection of demographic data necessary to conduct proportions tests to validate the selection of representative samples.]

2. QC would be expanded to include the review/investigation of claims that had been denied and employer tax collection activities. In addition, other categories of UI payments (interstate benefits, combined wage claims, and Federal UI benefits) should eventually be included in the program. [§ 602.1]

3. States would not be required to furnish information to the Federal Government about individuals whose claims are audited unless that information were provided without revealing the identity of the individuals. [§ 602.21(f)] [This principle was accepted in modified form by the Department to specify that only Core QC which assesses the benefit payment operations by investigating paid claims, has been designed and tested thus far, the Department wrote the regulation broadly to provide authority for what is planned as a comprehensive QC program. Also, by its acceptance of consensus principle number two, the Department is committed to expand the QC program to include the investigation of claims that have been denied and employer revenue collection activities (Revenue QC) which would include any other UI revenues, such as payments in lieu of contributions and EUCA reimbursements.]

4. The collection of demographic data elements that do not relate to an individual’s eligibility for UI benefits would not be a part of QC. [§ 602.21(c)(3)] [This principle was accepted in modified form by the Department to include the collection of demographic data necessary to conduct proportions tests to validate the selection of representative samples.]

5. Obtaining information needed for QC by telephone rather than in face-to-face interviews would be tested on a limited basis. [§ 602.21(g)] [This principle was accepted in modified form by the Department to provide also for three other areas: (1) substitute "cases of weeks paid" for "weeks claimed cases" and (2) include the collection of demographic data necessary to conduct proportions tests to validate the selection of representative samples.]

6. A portion of additional resources would be used for analysis of data generated by QC, to increase the number of claims sampled in areas where more information is needed, and for corrective action. [§ 602.40(b)] [This principle was accepted in modified form by the Department to specify that the Department may allocate additional resources, if available, to States for analysis of data generated by the QC program, to increase the number of claims sampled in areas where more information is needed, and for corrective action.]

7. No sanctions nor funding "incentives" would be used to force the achievement of specified error rates. [§ 602.43]

8. States would be required to release the results of the QC program at the same time each year, providing calendar year results using a standardized format to present the data. States would have the opportunity to release this information prior to any release at the national level. [§ 602.21(g)]

Section-by-Section Analysis of Comments

Subpart A—General Provisions

Section 602.1 Purpose.

Section 602.2 Scope.

Eleven commenters said that the inclusion of Denials and/or Revenue in the QC regulation is inappropriate or premature at this time. While it is true that only Core QC which assesses the benefit payment operations by investigating paid claims, has been designed and tested thus far, the Department wrote the regulation broadly to provide authority for what is planned as a comprehensive QC program. Also, by its acceptance of consensus principle number two, the Department is committed to expand the QC program to include the investigation of claims that have been denied and employer revenue collection activities (Revenue QC) which would include any other UI revenues, such as payments in lieu of contributions and EUCA reimbursements.

One commenter suggested that QC be investigated to determine whether the payments were proper. [§ 602.21(b)] [This principle was accepted in modified form by the Department to specify that only Core QC which assesses the benefit payment operations by investigating paid claims, has been designed and tested thus far, the Department wrote the regulation broadly to provide authority for what is planned as a comprehensive QC program. Also, by its acceptance of consensus principle number two, the Department is committed to expand the QC program to include the investigation of claims that have been denied and employer revenue collection activities (Revenue QC) which would include any other UI revenues, such as payments in lieu of contributions and EUCA reimbursements. Two commenters proposed that States be allowed the option to participate in whichever components of the QC program (benefits, denials, or revenue) they believe that they need. While States may have ideas of which areas of their programs require attention, the Random Audit experience demonstrated to the Department the value of such a program nationwide.

Subpart B—Federal Requirements

Section 602.10 Federal law requirements.

Section 602.11 Secretary’s interpretation.

Five commenters questioned the authority of the Secretary to mandate a QC program. One commenter said that requiring a State to operate a QC program goes far beyond the intent of section 303(a)(6) of the SSA, which gives the Secretary authority to require reports. Legal authority to establish QC derives from both sections 303(a)(1) and 303(a)(6) of the SSA. As described in the regulation, the Secretary interprets these sections to authorize QC among the “methods of administration . . . as are found by the Secretary of Labor to be reasonably calculated to insure full payment of unemployment compensation when due,” as well as authorizing the Secretary to require verifiable reports of its QC implementation and operations. The methods of administration requirement (section 303(a)(1), SSA) has from the beginning of the program been interpreted as pertaining to all UI operations, including revenue and benefit operations.

One commenter suggested that QC would be more successful and States would be more cooperative if it were voluntary, as was Random Audit. Observations of QC as operated since March 30, 1986 and its predecessor, Random Audit, both of which were voluntary, have revealed less than adequate adherence by several States to methodology necessary to ensure valid results.

Another commenter suggested that § 602.21(a), which says in the proposed rule, “the Secretary interprets section 303(a)(1), SSA, to require that a State law [provide for] such methods of administration . . . , and collection [and handling] of unemployment revenues [and reimbursements], with the greatest
accuracy feasible" is sufficient, and that § 602.11(d) requiring a State law authorizing QC is unnecessary. Section 602.11(d) has been improperly interpreted by this commenter. Section 602.11 sets forth the Secretary of Labor's basic interpretations of sections 303(a)(1) and 303(a)(6) as they relate to the QC program. As stated earlier in the Section-by-Section Regulatory Highlights, the Secretary has no reason to believe that a mandatory QC program will require any State to amend its law. Without § 602.11(d), a State might construe their methods of administration requirement to be sufficient without the establishment of a QC program.

To clarify that QC involves both conformity and compliance, additions were made to both § 602.10(d) and 602.11. An additional sentence in § 602.11(c) states, "Further, conformity of the State law with those requirements is required by section 303(a) and section 601.5 of this chapter."

Subpart C—State Responsibilities

Nine commenters stated that corrective action should be funded and/or required by the Federal government and that technical assistance should be made available to help correct the errors detected by QC. Concerning funding of corrective actions, State initiatives in response to Random Audit data and to QC data collected on a voluntary basis have demonstrated that many corrective actions can be taken with existing resources as part of ongoing management oversight. Should it develop that necessary actions nationwide cannot be supported with available resources, the Department will use the information from QC findings in budget development to seek funding for such necessary corrective actions. However, such data is expected to be available only after QC has operated for some time in each State. The regulation was modified by the addition of § 602.40(b) to authorize the Department to allocate additional resources, if available, for corrective action, as called for in consensus principle number six.

The Department finds no need to impose an explicit requirement that SESAs implement corrective action. It believes that SESAs want to operate the best possible UI program and also have a strong incentive to improve their operations and lower taxes for the benefit of their own States' employers whose taxes finance UI. Rather than promulgating such a requirement, the Department is committed to providing technical assistance to the States to help correct errors detected by QC. To this end, the Department funded an analyst position in each State so that SESAs may develop additional expertise to help determine where their problems lie.

Section 602.20 Organization.

Two commenters opposed direction by the Department of the States' organizational structure. The limits imposed by the regulation are intended to protect the integrity of the program while preserving the States' prerogatives. The SESA is free to locate the QC unit wherever it wishes so long as it is independent of, and not accountable to, any unit performing functions the QC unit evaluates. The Department allows the SESA full flexibility to locate the unit within this constraint.

One commenter questioned the wisdom of prohibiting the QC unit from being within the UI Division, reportable to the UI Director, or under the authority of the State Commissioner of Labor. This is an apparent misinterpretation of the requirements intended to ensure independence from operational units being evaluated. The regulation would prohibit the QC unit from reporting to a manager whose sole or predominant responsibility is to manage an area, e.g., benefit payment operations, being evaluated. Depending upon the organizational structure of the State, therefore, the QC unit could report to the State Commissioner of Labor, the SESA Administrator, or the UI Director.

Section 602.21 Standard methods and procedures.

Section 602.21 has been renamed to more aptly describe the subjects included and reorganized to achieve a more logical order. Following is a table showing the new section title and topics covered in each subsection compared to the location of the same material in the proposed rule.

<table>
<thead>
<tr>
<th>Final rule</th>
<th>Proposed rule</th>
</tr>
</thead>
<tbody>
<tr>
<td>602.21(a)</td>
<td>[In reference to using standard methods and procedures established by the Department].</td>
</tr>
<tr>
<td>602.21(b)</td>
<td>[In reference to taking official actions on inaccuracies detected through QC investigations].</td>
</tr>
<tr>
<td>602.21(c)</td>
<td>[In reference to informing claimants/employees of effect of QC findings].</td>
</tr>
<tr>
<td>602.21(d)</td>
<td>[In reference to the use of questionnaires being requested].</td>
</tr>
</tbody>
</table>

One commenter contended that QC is not cost effective because of high unit cost, that sampling should be reduced from 12 months to one month, and that QC should be incorporated into the UI Quality Appraisal system (the existing system used to assess performance in UI benefits, appeals, and revenue collections). The Department recognizes the expense of operating a QC program, but the investment in QC, when compared to the overall administrative costs of the UI program (less than two percent) and to benefit outlays (two tenths of one percent), is very worthwhile. Studies of alternative investigative methods have been and will continue to be undertaken in order to identify the most cost-effective procedures. Despite the costs of the QC program, it is expected to realize savings that would more than offset costs. The QC and Quality Appraisal programs have been examined, and duplications have already been eliminated. Ultimately the two assessment systems will be merged into a single system which preserves Quality Appraisal's useful features.

Section 602.21(a) [In reference to using standard methods and procedures established by the Department].

Ten commenters objected to the inflexibility of the prescribed methodology and the absence of alternative methodology. Consensus principle number five on this subject states that the Department will test collecting information by telephone rather than in face-to-face interviews, and this language, modified to provide also for tests of collecting data by mail, has been added to the regulation at § 602.30(b). Furthermore, in keeping with the commitment to test alternative methodologies, the Department has approved and supported one SESA's proposal for such a test. Other SESAs'
proposals for conducting their own tests are also welcomed.

Two commenters stated that the required methods and procedures should be established only after consultation and should be specified in the regulation. The methods and procedures are not specified in the regulation due to the nature of the regulatory approach taken with the QC program. The Department has sought and used input from SESAs in the development of QC methodology and will continue to do so. State comments on two draft versions of the benefits QC State Operations Handbook (Benefits QC Handbook) have led to several modifications in the methodology. Future revisions to the Benefits QC Handbook also will be circulated for comment before being issued. After agreeing to the consensus principles, the Department made additional changes to the methodology.

Section 602.21(b) [In reference to representative sample minimums set by DOL]*

Five commenters were concerned that the regulation does not specify minimum sample sizes but gives the Department the authority to establish minimum sample sizes outside the regulatory process. Two expressed the opinion that States should have input on the number of cases sampled to reflect State-specific factors affecting the time it takes to complete an investigation. Two others proposed that States should be allowed to reduce the sample pull below existing Benefits QC Handbook limits if necessary due to illnesses, vacancies, leave, etc. In contrast, another commenter believed that the sample sizes will be too small to make valid estimates.

The Department concurs in consensus principle number one that each State sample a minimum of 400 cases and has amended the regulation to incorporate that principle. The principle, as incorporated, has been modified for technical accuracy. The term "cases of weeks paid", which are covered in Core QC, has been substituted for the suggested language of "weeks claimed cases" as contained in the consensus principles.

The Department believes that 400 cases per year is the minimum needed to establish sufficiently precise QC inferences to be made from the data obtained each quarter. Samples below these minimums run the risk of significantly reducing the usefulness and reliability of data from an entire quarter. Two commenters suggested that special studies could be at State discretion, with no mandatory application to the national data perspective. SESAs have discretion to determine what should be studied. However, the Department must reserve the right to review State proposals to ensure that they are technically valid and consistent with QC objectives.

Another commenter suggested that nonscientific, ad hoc studies are inexpensive and useful and should be included. The Department recognizes that nonscientific, ad hoc studies have been performed for years by SESAs. Such studies are encouraged so long as the minimum requirements for QC are met.

Section 602.21(c) [In reference to completing prompt and in-depth case investigations to determine degree of accuracy and timeliness]*

Two commenters objected to the addition to the regulation of timeliness as a subject of assessment without first consulting the States. Reference to timeliness in this section refers not to QC case completion, but to more general UI applications such as claim payment timeliness. This language has been included to permit future applications of the QC program beyond those in the existing design of the QC case investigations; e.g., utilization of capabilities built into the QC system to eliminate the need for periodic reports which provide data from which the minimum requirements for QC are met.

Section 602.21(c)(1) [In reference to informing claimants and employers in writing of the effect of QC investigations]*

Section 602.21(c)(1) was clarified to explain that States must inform claimants in writing that the information obtained from a QC investigation may affect their eligibility for benefits. Each State must also inform employers in writing that the information obtained from a QC investigation of revenue may affect their tax liability.

Section 602.21(c)(2) [In reference to the use of the questionnaire being required]*

Eleven commenters stated that the collection of demographic data beyond that necessary for determination of eligibility is inappropriate or should be optional for the States. The Department accepts this position, which is also contained in consensus principles number one and four, and has revised the regulation to so state and identify the demographic data that are necessary to conduct proportions tests for the purpose of validating the selection of representative samples: Claimants' date of birth, sex, and ethnic classification.
Section 602.21(c)(4) [In reference to concluding all findings of inaccuracy as detected through QC investigations with appropriate official actions].

The language in this section has been revised to more accurately set forth the requirement that appropriate official actions be taken when inaccuracies are detected through QC investigations. The term “determination” used in the proposed rule is too narrow in definition as an inaccuracy may be properly concluded with some other appropriate action. Moreover, State finality laws may preclude action.

Section 602.21(d)(1) and (2) [In reference to classifying QC case findings].

One commenter stated that there is too much detail regarding the classification of cases, which should more appropriately be located in the Benefits QC Handbook. In contrast, another commenter suggested that the regulation should define “error.” The Department believes that a proper balance between the regulation and the operational handbooks will be maintained by the regulation setting forth the major classification of case findings [e.g., proper payments, overpayments, underpayments, or proper denials] while the handbooks prescribe the detailed categories and definitions of error.

Section 602.21(f) [In reference to furnishing information and reports].

Two commenters were concerned that the regulation does not make clear what data are to be transmitted, why they are to be transmitted weekly, or how they are to be used. They believe that the statement “for statistical and other analysis” is too general and does not support State integrity. In keeping with the broad regulatory approach described earlier, the Department does not believe it should specify in the regulation which QC data are to be collected and transmitted; such detail is contained in the Benefits QC Handbook. However, the Department has modified the regulation at § 602.30 to identify examples of how the data are to be used. Section 602.30 was amended to state that a QC data base will be combined with other data for statistical and other analyses such as assessing the impact of economic cycles, funding levels, and workload levels on program accuracy and timeliness.

Five commenters stated that weekly transmission of data was inappropriate. The Department finds that weekly transmission is desirable because Federal oversight responsibility involves ensuring that cases are sampled properly and completed in a timely manner to ensure reliability of data. Prompt entry and transmission of QC data are necessary to enable the Department to conduct proportions tests at frequent intervals in order to minimize the possibility that large blocks of data might be invalidated.

Seven commenters received a need to ensure privacy of claimant’s Social Security numbers. Based on these comments, the Department’s desire to incorporate consensus principle number three, and compliance with the Privacy Act of 1974 (5 U.S.C. 552(a)), the Department has modified the regulation. Containing even more restrictive language than presented in consensus principle number three, the regulation now specifies that States will be required to furnish information and reports to the Department of Labor, including weekly transmissions of case data entered into the automatic QC system and annual reports, without, in any way, identifying individuals to whom such data pertain. The States are being provided with software which will ensure that identifiers for all data transmitted from States will be encrypted so that individual claimants cannot be identified from information furnished to the Department. The Department does not maintain any records or establish any identifiers on individual persons under the QC program; therefore, no system of records is being established which would be subject to the Privacy Act.

Section 602.21(g) [In reference to releasing results of the QC program].

Five commenters requested that the timing/format of the annual release of QC data be specified in regulation. Four additional commenters requested that the release of QC data to the public should be controlled by the States.

Two others believed that publication of QC results by the Department in a standardized format may lead to unfair and unrealistic comparisons between States. Nine commenters stated that flexibility on release of information was necessary. One commenter said that the annual release of data should include full disclosure of the States’ work search requirements, while another saw a need to differentiate between “correctable” and “non-correctable” improper payments. Two commenters stated that QC results should be published at the national level only as a composite-of-performance rate of all States, and that individual State data should be released by the Department only if a State fails to release its own data within 90 days of a composite release.

In response to these varied comments, the Department has agreed to consensus principle number eight that States will release calendar year results of the QC program at the same time each year, using a standardized format to present the data. States will have the opportunity to release this information prior to any release at the national level. This language has been added to the regulation. Specific dates and procedures will be promulgated through the Benefits QC Handbook, rather than in regulation, consistent with the regulatory approach previously described. The Department is committed to ensuring that significant concerns on the subject continue to be identified and addressed. Although there are no general plans to publish handbook sections in the Federal Register, proposals related to releasing the QC data will use this mechanism to ensure that all interested parties have the opportunity to comment.

Section 602.22 Exceptions.

One commenter suggested that the final rule should stipulate that States can petition the Department for exclusion from QC. As stated in the background statement of the proposed regulation, published at 51 FR 26846 on July 25, 1986, and repeated in the section titled QC Will Be Mandatory above, “Given the importance of ensuring accurate and timely payment of benefits to eligible UI claimants and accurate and prompt collection of UI contributions, however, participation of the States in the QC program will be mandatory.” At this time it is anticipated that the only jurisdiction that may be excepted from Core QC would be the Virgin Islands. The Department has determined, therefore, that a procedure for requesting exemptions is not necessary. However, the regulation has been revised to clarify that cost effectiveness will be considered in excepting States from participation in QC. Moreover, any exceptions will be discussed with the individual State in advance of any final decision.

Subpart D—Federal Responsibilities

Section 602.30(a) [In reference to the establishment of methods and procedures].

Two commenters stated that the required methods and procedures should be established only after consultation with the States and should be specified in the regulation. Response to this comment is included in the earlier discussion of § 602.21(a).
Section 602.30(b) [In reference to alternative methodologies].

In response to the ten commenters objecting to the inflexibility of the prescribed methodology and the absence of alternative methodology, the Department has added a section to the regulation concerning consensus principle number five, alternative methodologies. Complete reponse to this comment is found in the earlier discussion of § 602.21(a) [In reference to using standard methods and procedures established by the Department].

Section 602.30(c) [In reference to the Department maintaining a computerized data base].

Four commenters were concerned about the need, cost, and security of Federal data bases and of access to State data bases. The need for a Federal data base and its uses are addressed in § 602.21(f) above. Prior to the transmission of case data, States will encrypt each claimant's social security number, thereby preventing identification of any individual's record. This should ensure the maintenance of privacy in the data base. While the Department recognizes the cost of maintaining a Federal data base, its use and potential savings outweigh the expense. More discussion of QC cost benefit is found in § 602.21 above.

SESA's are presumed to have established appropriate security and password procedures to prohibit unauthorized access to either the SESA mainframe or the QC microcomputers. There will be no mandatory access by the Department to any data in the SESA mainframe in the operation of the QC program under this part, although access to such data may be required in connection with audits conducted under State or Federal authority.

Section 602.31 Oversight.

Two commenters stated that the Department should have the responsibility to establish uniform, standard methods and procedures, but monitoring of the State operational procedures should be limited to ensuring only that States meet conformity and compliance requirements. The QC program is based on the Secretary's interpretations of section 303 of the SSA, which contains the "methods of administration" requirement. All departures from these requirements pose a potential conformity/compliance issue.

Subpart E—Grants to States

Section 602.40 Funding.

Three commenters stated that the regulation should ensure, and the Department should provide, sufficient funds in order for States to meet the Federal QC requirements. This would not be appropriate subject matter for regulation, because the Department is dependent on Congress for appropriation levels and cannot guarantee, in regulation, specified funding. Furthermore, it should not be necessary for any State to use State resources for implementing and maintaining a QC program, as adequate resources have been provided for such purpose.

One commenter requested that the regulation should stipulate that State revenues not be used for QC. To prohibit States from using State revenues for QC could be counterproductive. The Department would not want to discourage States from taking the initiative to expand QC to meet their own needs.

In response to the six commenters wishing the consensus principles to be explicitly incorporated in the regulation, the Department has added § 602.40(b). This new section, embodying a slightly modified version of consensus principle number six, states that the Department may allocate additional resources, if available, to States for analysis of data generated by the QC program, to increase the number of claims sampled in areas where more information is needed, for pilot studies for the purpose of expanding the QC program, and for corrective action. The revision to the exact language of consensus principle number six acknowledges that allocations can only be made if funds are available and provides some Departmental discretion in making the allocation.

Section 602.41 Proper expenditure of QC granted funds.

One commenter pointed out that subjecting QC funds to recapture seems inconsistent with the Administrative Financing Initiative (AFI). There is no inconsistency between financing and proper expenditure requirements with respect to QC and the four short-term changes made thus far under the Department's AFI which was published in the Federal Register at 51 FR 18052. Should future changes in administrative financing pose any issue, a reconciliation will be effected.

Sections 303(a)(6) and (9), SSA, require that State laws include provisions for:

... the expenditure of all moneys received pursuant to section 302 of this title solely for the purposes and in the amounts found necessary by the Secretary of Labor for the proper and efficient administration of such State law; and

... The replacement, within a reasonable time, of any moneys received pursuant to section 302 of this title, which, because of any action or contingency, have been lost or have been expended for purposes other than or in amounts in excess of, those found necessary by the Secretary of Labor for the proper administration of such State law.

These provisions authorize the Department to take exception to and require reimbursement for any expenditure made which is not in compliance with requirements placed on States for the operation of QC. This reference is set forth in the regulation to notify States that an interim step will be taken before proceeding with any action to withhold all grants.

Another commenter observed that effective review of the use of QC granted funds will be difficult unless they are identified as a separately budgeted item. SESEAs will be responsible for operating the QC program in accordance with the QC requirements. The Department will be responsible for ensuring that SESEAs program performance is adequate. It will only be necessary for the Department to review SESEAs use of grant funds if program performance is inadequate.

Section 602.42 Effect of failure to implement a Quality Control program.

Twelve commenters questioned the authority of the Secretary to withhold grants for failure to implement QC in accordance with Federal requirements. The Social Security Act makes the Secretary responsible for ensuring that SESEAs adopt such methods of administration as will ensure full payment of unemployment compensation when due, and makes provision for grants withdrawal to ensure conformity/compliance. The Random Audit experience has revealed the existence of problems in the payment of benefits and has demonstrated that this approach is feasible for estimating the extent of improper payments. The Secretary has determined that implementation of QC will be the most efficient means of fulfilling these responsibilities.

It is the intent of the Department to ensure that an effective QC program is implemented by providing adequate funding and offering technical assistance to SESEAs as needed. Consistent with other aspects of WI administration, withdrawal of grants would be a last resort.
Four commenters were concerned that conformity/compliance issues could be raised for failure to run the QC program within the strict guidelines of the QC methodology. They suggested that the regulation should clarify that administrative funding would not be withheld unless a State “refuses” to participate in QC. It was further suggested that the Department should give States quarterly written assurance that their QC program is in compliance with Federal rules, and if deficiencies are found by the Department, they should be specifically defined for corrective action.

The language from the proposed regulation is being maintained to be consistent with that of section 303(a)(1) SSA, and the Secretary’s interpretation as set out in the regulation. Failure to comply substantially with QC methodology could result in proceeding under section 303(b), SSA. However, the intent of the regulation is not to withhold administrative funding for technical deficiencies beyond the SESA’s control. The Department will be conducting routine compliance monitoring of the State QC programs and providing regular feedback to the States. If problems are found, it will be in the interest of all parties involved to resolve them. As with all such matters, the Department will work cooperatively with a State before taking any formal conformity/compliance action. The regulation states that “the Department of Labor shall, for purposes of determining eligibility for grants... annually review the adequacy of the administration of a State’s QC program.” This is deemed sufficiently frequent for official notification to the SESAs.

One commenter proposed that definition of the word “implementation” was necessary. For purposes of this regulation, implementation refers to the act of establishing a QC program in accordance with the regulation and the prescribed methodology in the QC operations’ handbooks. (Thus far only the Benefits QC Handbook has been written and issued.) Further definition does not appear appropriate or necessary.

Section 602.43 No incentives or sanctions based on specific error rates.

Two commenters said that the regulation should state that no sanctions or funding incentives will be used to force achievement of specified error rates. This position also was stated in consensus principle number seven. The Department has revised the regulation, substituting the word “influence” for “force”, to incorporate this principle.

**Appendix A—Standard for Claims Determinations—Separation Information**

Three commenters asserted that Appendix A is not needed and should be deleted from the regulation. The appendix is intended to support the QC requirement that appropriate action resulting from QC investigations be issued officially. This ensures that findings are subject to the same possible challenges by claimants as other agency actions. The inclusion of Appendix A in the regulation is mandated by the Office of the Federal Register’s rule on incorporation by reference.

Another commenter was concerned that Appendix A changes procedural instructions, which if not followed could result in sanctions. Procedural instructions are not affected by inclusion of Appendix A, which is presently contained in the Employment Security Manual, and is a requirement independent of the QC regulation.

**Other Comments Which Are Not Section Specific**

Eleven commenters contended that the problem with UI is that it is systematically underfunded. Furthermore, they content that if the requirements of Gramm-Rudman legislation are implemented, it is implicit that the QC program will be fully funded, while funding for the payment of benefits and collection of revenues will be reduced. This would result in QC having a higher priority than the operation of the basic UI program. The Department believes that QC is essential at any time, regardless of budget constraints. Moreover, QC could reveal the impact of such variables as budget and workload fluctuations. Such information would be invaluable in future budget discussions.

One commenter believed that the QC rule represents a potential for substantial interference in State UI administrative processes and objected to the potential use of QC to enforce non-statutory Federal work-search standards upon States without making those standards explicit. The Department does not intend to impose or enforce non-statutory work-search standards. The QC program will not interfere with the administrative processes of SESAs, since the QC program methodology simply verifies the degree to which SESAs are applying their own State laws and official operational procedures. Thus, it will yield a great deal of information which will assist SESA managers in operating the UI program or assessing the need to revise their own UI law and policies.

One commenter requested a delay of the implementation of the QC program, originally limited to the audit of benefit payments, until other elements of UI administration, notably denials and revenue collections, can be included. After a thorough review of the QC program, a decision was made to proceed with the revised QC program. As described in UIPL No. 4-86, which presented the aforementioned consensus principles as Departmental policy, the revised QC program was implemented voluntarily in March 1986. Such implementation was called for in consensus principle number one. Consistent with consensus principle number two, the Core QC program will be expanded to include the investigation of claims that have been denied and employer revenue collection activities. The QC denials pilot was launched in five States in October 1986 and Revenue QC is currently being designed.

Two commenters contended that QC should be designed to improve quality through corrective action rather than to be a longitudinal research project which provides for statistics and data compilation. The Department concurs that the objective of the QC program is to improve program operations. Any longitudinal research will be dealt with separately.

One commenter stated that the QC program should easily meet the definition of a “major rule” as outlined in the published proposal. Executive Order 12291 on Federal Regulations defines the requirements for classification as a “major rule”. As stated in the preamble of the proposed rule and repeated below, this rule is not classified as a “major rule” because it is not likely to result in (1) an annual effect on the economy of $100 million or more; (2) a major increase in costs or prices for consumers, individual industries, Federal, State, local government agencies, or geographic regions; or (3) significant adverse effects on competition, employment, investment, productivity, innovation, or the ability of United States-based enterprises to compete with foreign-based enterprises in domestic or export markets.

**Other Comments Which Are Not Applicable to the Regulation**

Individuals or groups who made the following comments will receive direct responses from the Department since they do not apply to the regulation:

One commenter noted language in the QC State Operations Handbook which required a log-in account to be established on the SESA mainframe computer for the sole purpose of
allowing data file transfer from the SESA computer to the QC microcomputer. This assumes a QC-to-mainframe link. This commenter believes that the Secretary does not have the authority to mandate such internal operations.

Another commenter was opposed to telephone transmission of QC data between State and National Office during nonworking hours.

One commenter suggested that local office managers' comments be obtained whenever mispayments are detected in a QC investigation.

Four commenters suggested establishment of a National Clearinghouse on Corrective Strategies for the purpose of exchanging ideas and experiences under the QC program.

Another commenter suggested that State staff need more training on interpreting QC data.

Untimely Comments

As noted above, a number of comments were received after the comment period had ended. While these comments are not addressed specifically in this document, the comments were examined, and most were found to present nothing of substantial import not addressed in the timely comments discussed above. Those individuals or groups which presented additional issues or concerns will receive direct responses from the Department.

Technical and Conforming Changes

In addition to the changes noted above, other technical and conforming changes have been made to improve the accuracy and completeness of the regulations.

Authority

Section 302(a), SSA, requires the Secretary of Labor to certify payment of granted funds to each State in:

such amounts as the Secretary of Labor determines to be necessary ... for the proper and efficient administration of ... the State’s unemployment compensation laws.

Section 303(a)(1), stipulates that the Secretary shall make no certification for payment of granted funds unless he finds the State law includes provision for:

... such amounts as the Secretary of Labor determines to be necessary ... for the proper and efficient administration of ... the State’s unemployment compensation laws.

Section 303(a)(6), SSA, the Secretary has authority to require States to make reports. Under this section, the Secretary has the authority to require the States to make reports concerning their implementation and operation of the QC program.

Classification—Executive Order 12291

The rule in this document is not classified as a “major rule” under Executive Order 12291 on Federal Regulations, because it is not likely to result in (1) an annual effect on the economy of $100 million or more; (2) a major increase in costs or prices for consumers, individual industries, Federal, State, or local government agencies, or geographic regions; or (3) significant adverse effects on competition, employment, investment, productivity, innovation, or the ability of United States-based enterprises to compete with foreign-based enterprises in domestic or export markets.

Accordingly, no regulatory impact analysis is required.

Paperwork Reduction Act

The Department has complied with the provisions of the Paperwork Reduction Act of 1980, 44 U.S.C. Chapter 35. Approval of recordkeeping requirements at §§ 602.21(c)(2), 602.21(e), and 602.21(f) are under OMB control number 1205-0245.

Regulatory Flexibility Act

This rule will have no “significant economic impact on a substantial number of small entities” within the meaning of 5 U.S.C. 605(b). This rule implements an internal QC program, and has no significant economic impact on any small entities. The Secretary of Labor has certified to the Chief Counsel for Advocacy of the Small Business Administration to this effect. Accordingly, no regulatory flexibility analysis is required.

Catalog of Federal Domestic Assistance

This program is listed in the Catalog of Federal Domestic Assistance at number 17.225, Unemployment Insurance.

List of Subjects in 20 CFR Part 602

Labor, Unemployment compensation, Reporting and recordkeeping requirements.

Words of Issuance

For the reasons set out in the preamble, Part 602 is added to Title 20, Chapter V, of the Code of Federal Regulations to read as set forth below.


William B. Brock,
Secretary of Labor.

PART 602—QUALITY CONTROL IN THE FEDERAL-STATE UNEMPLOYMENT INSURANCE SYSTEM

Subpart A—General Provisions

Sec. 602.1 Purpose.

Subpart B—Federal Requirements

602.10 Federal law requirements.

602.11 Secretary’s interpretation.

Subpart C—State Responsibilities

602.20 Organization.

602.21 Standard methods and procedures.

602.22 Exceptions.

Subpart D—Federal Responsibilities

602.30 Management.

602.31 Oversight.

Subpart E—Quality Control Grants to States

602.40 Funding.

602.41 Proper expenditure of Quality Control granted funds.

602.42 Effect of failure to implement Quality Control program.

602.43 No incentives or sanctions based on specific error rates.

Appendix A To Part 602—Standard For Claim Determinations—Separation Information.

Authority: 42 U.S.C. 1302.

Subpart A—General Provisions

§ 602.1 Purpose.

The purpose of this part is to prescribe a Quality Control (QC) program for the Federal-State unemployment insurance (UI) system, which is applicable to the State UI programs and the Federal unemployment benefit and allowance programs administered by the State Employment Security Agencies (SESA) under agreements between the States and the Secretary of Labor (Secretary). QC will be a major tool to assess the timeliness and accuracy of State administration of the UI program. It is designed to identify errors in claims processes and revenue collections (including payments in lieu of contributions and Extended Unemployment Compensation Account collections), analyze causes, and support the initiation of corrective action.

§ 602.2 Scope.

This part applies to all State laws approved by the Secretary under the Federal Unemployment Tax Act (section 33528 Federal Register / Vol. 52, No. 171 / Thursday, September 3, 1987 / Rules and Regulations
3304 of the Internal Revenue Code of 1954, 26 U.S.C. section 3304), to the administration of the State laws, and to any Federal unemployment benefit and allowance program administered by the SSSAs under agreements between the States and the Secretary. QC is a requirement for all States, initially being applicable to the States and the Secretary. QC is a requirement for all States, initially being applicable to the largest permanently authorized programs (regular UI including Combined-Wage-Claims) and federally-funded programs (Unemployment Compensation for Ex-Servicemen and Unemployment Compensation for Federal Employees). Other elements of the QC program (e.g., interstate, extended benefit programs, benefit denials, and revenue collections) will be phased in under a schedule determined by the Department in consultation with State agencies.

Subpart B—Federal Requirements

§ 602.10 Federal law requirements.

(a) Section 303(a)(1) of the Social Security Act (SSA), 42 U.S.C. 503(a)(1), requires that a State law include provision for:

Such methods of administration...as are found by the Secretary of Labor to be reasonably calculated to assure full payment of unemployment compensation when due.

(b) Section 303(a)(6), SSA, 42 U.S.C. 503(a)(6), requires that a State law include provision for:

The making of such reports, in such form and containing such information, as the Secretary of Labor may from time to time require, and compliance with such provisions as the Secretary of Labor may from time to time find necessary to assure the correctness and verification of such reports.

(c) Section 303(b), SSA, 42 U.S.C. 503(b), provides in part that:

Whenever the Secretary of Labor, after reasonable notice and opportunity for hearing to the State agency charged with the administration of the State law, finds that in the administration of the law there is—

(2) A failure to comply substantially with any provision specified in subsection (a); the Secretary of Labor shall notify such State agency that further payments will not be made to the State until the Secretary of Labor is satisfied that there is no longer any such denial or failure to comply. Until he is so satisfied, he shall make no further certification to the Secretary of the Treasury with respect to such State...

(d) Certification of payment of grants to a State is withheld only when the Secretary finds, after reasonable notice and opportunity for hearing to the State agency—

(1) That any provision required by section 303(a) of the Social Security Act is no longer included in the State unemployment compensation law, or

(2) That in the administration of the State unemployment compensation law there has been a failure to comply substantially with any required provision of such law.

§ 602.11 Secretary's interpretation.

(a) The Secretary interprets section 303(a)(1), SSA, to require that a State law provide for such methods of administration as will reasonably ensure the prompt and full payment of unemployment benefits to eligible claimants, and collection and handling of income for the State unemployment fund (particularly taxes and reimbursements), with the greatest accuracy feasible.

(b) The Secretary interprets sections 303(a)(1) and 303(a)(6), SSA, to authorize the Department of Labor to prescribe the standard definitions, methods and procedures, and reporting requirements for the QC program and to ensure accuracy and verification of QC findings.

(c) The Secretary interprets section 303(b)(2), SSA, to require that, in the administration of a State law, there shall be substantial compliance with the provisions required by sections 303(a)(1) and (6). Further, conformity of the State law with those requirements is required by section 303(a) and § 601.5(a) of this chapter.

(d) To satisfy the requirements of sections 303(a)(1) and (6), a State law must contain a provision requiring, or which is construed to require, the establishment and maintenance of a QC program in accordance with the requirements of this part. The establishment and maintenance of such a QC program in accordance with this part shall not require any change in State law concerning authority to undertake redeterminations of claims or liabilities or the finality of any determination, redetermination or decision.

Subpart C—State Responsibilities

§ 602.20 Organization.

Each State shall establish a QC unit independent of, and not accountable to, any unit performing functions subject to evaluation by the QC unit. The organizational location of this unit shall be positioned to maximize its objectivity, to facilitate its access to information necessary to carry out its responsibilities, and to minimize organizational conflict of interest.

§ 602.21 Standard methods and procedures.

Each State shall—

(a) Perform the requirements of this section in accordance with instructions issued by the Department, pursuant to § 602.30(a) of this part, to ensure standardization of methods and procedures in a manner consistent with this part;

(b) Select representative samples for QC study of at least a minimum size specified by the Department to ensure statistical validity (for benefit payments, a minimum of 400 cases of weeks paid per State per year);

(c) Complete prompt and in-depth case investigations to determine the degree of accuracy and timeliness in the administration of the State UI law and Federal programs with respect to benefit determinations, benefit payments, and revenue collections; and conduct other measurements and studies necessary or appropriate for carrying out the purposes of this part; and in conducting investigations each State shall:

(1) Inform claimants in writing that the information obtained from a QC investigation may affect their eligibility for benefits and inform employers in writing that the information obtained from a QC investigation of revenue may affect their tax liability.

(2) Use a questionnaire, prescribed by the Department, which is designed to obtain such data as the Department deems necessary for the operation of the QC program; require completion of the questionnaire by claimants in accordance with the eligibility and reporting authority under State law.

(3) Collect data identified by the Department as necessary for the operation of the QC program; however, the collection of demographic data will be limited to those data which relate to an individual's eligibility for UI benefits and necessary to conduct proportions tests to validate the selection of representative samples (the demographic data elements necessary to conduct proportions tests are claimants' date of birth, sex, and ethnic classification); and

(4) Conclude all findings of inaccuracy as detected through QC investigations with appropriate official actions, in accordance with the applicable State and Federal laws; make any determinations with respect to individual benefit claims in accordance with the Secretary's "Standard for Claim Determinations—Separation Information" in the Employment Security Manual, Part V, sections 6010–6015 (Appendix A of this part);

(d) Classify benefit case findings resulting from QC investigations as:
(1) Proper payments, underpayments, or overpayments in benefit payment cases, or
(2) Proper denials or underpayments in benefit denial cases;
(e) Make and maintain records pertaining to the QC program, and make all such records available in a timely manner for inspection, examination, and audit by such Federal officials as the Secretary may designate or as may be required or authorized by law;
(f) Furnish information and reports to the Department, including weekly transmissions of case data entered into the automated QC system and annual reports, without, in any manner, identifying individuals to whom such data pertain; and
(g) Release the results of the QC program at the same time each year, providing calendar year results using a standardized format to present the data as prescribed by the Department; States will have the opportunity to release this information prior to any release by the Department.

§602.22 Exceptions.
If the Department determines that the QC program, or any constituent part of the QC program, is not necessary for the proper and efficient administration of a State law or in the Department's view is not cost effective, the Department shall use established procedures to advise the State that it is partially or totally excepted from the specified requirements of this part. Any determination under this section shall be made only after consultations with the State agency.

Subpart D—Federal Responsibilities
§602.30 Management.
(a) The Department shall establish required methods and procedures (as specified in §602.21 of this part); and provide technical assistance as needed on the QC process.
(b) The Department shall consider and explore alternatives to the prescribed sampling, study, recordkeeping, and reporting methodologies. This shall include, but be limited to, testing the obtaining of information needed for QC by telephone and mail rather than in face-to-face interviews.
(c) The Department shall maintain a computerized data base of QC case data which is transmitted to the Department under §602.21, which will be combined with other data for statistical and other analysis such as assessing the impact of economic cycles, funding levels, and workload levels on program accuracy and timeliness.

§602.31 Oversight.
The Department shall review QC operational procedures and samples, and validate QC methodology to ensure uniformity in the administration of the QC program and to ensure compliance with the requirements of this part. The Department shall, for purposes of determining eligibility for grants described in §602.40, annually review the adequacy of the administration of a State's QC program.

Subpart E—Quality Control Grants to States
§602.40 Funding.
(a) The Department shall use established procedures to notify States of the availability of funds for the operation of QC programs in accordance with this part.
(b) The Department may allocate additional resources, if available, to States for analysis of data generated by the QC program, to increase the number of claims sampled in areas where more information is needed, for pilot studies for the purpose of expanding the QC program, and for corrective action.

§602.41 Proper expenditure of Quality Control granted funds.
The Secretary may, after reasonable notice and opportunity for hearing to the State agency, take exception to and require repayment of an expenditure for the operation of a QC program if it is found by the Secretary that such expenditure is not necessary for the proper and efficient administration of the QC program in the State. See Actions 303(a)(8), 303(a)(9) and 303(b)(2), SSA, and 20 CFR 601.5. For purposes of this section, an expenditure will be found not necessary for proper and efficient administration if such expenditure fails to comply with the requirements of Subpart C of this part.

§602.42 Effect of failure to implement Quality Control program.
Any State which the Secretary finds, after reasonable notice and opportunity for hearing, has not implemented or maintained a QC program in accordance with this part will not be eligible for any grants under Title III of the Social Security Act until such time as the Secretary is satisfied that there is no longer any failure to conform or to comply substantially with any provision specified in this part. See sections 303(a)(1), 303(a)(6), and 303(b)(2), SSA, and 20 CFR 601.5.

§602.43 No incentives or sanctions based on specific error rates.
Neither sanctions nor funding incentives shall be used by the Department to influence the achievement of specified error rates in State UI programs.

Appendix A to Part 602—Standard for Claim Determinations—Separation Information


6010 Federal Law Requirements. Section 303(a)(1) of the Social Security Act requires that a State law include provision for:
“Such methods of administration...as are found by the Secretary to be reasonably calculated to insure full payment of unemployment compensation when due.”

Section 303(a)(4) of the Social Security Act requires that a State law include provision for:
“Opportunity for a fair hearing before an impartial tribunal, for all individuals whose claims for unemployment compensation are denied.”

Section 303(a)(4) of the Federal Unemployment Tax Act and section 303(a)(5) of the Social Security Act require that a State law include provision for:
“Expenditure of all money withdrawn from an unemployment fund of such State, in the payment of unemployment compensation.”

Section 303(b) of the Federal Unemployment Tax Act defines “compensation” as “cash benefits payable to individuals with respect to their unemployment.”

6011 Secretary’s Interpretation of Federal Law Requirements. The Secretary interprets the above sections to require that a State law include provisions which will insure that:
A. Individuals who may be entitled to unemployment compensation are furnished such information as will reasonably afford them an opportunity to know, establish, and protect their rights under the unemployment compensation law of such State, and
B. The State agency obtains and records in time for the prompt determination and review of benefit claims such information as will reasonably and securely the payment of benefits to individuals to whom benefits are due.

6012 Criteria for Review of State Law Conformity with Federal Requirements: In determining the conformity of a State law with the above requirements of the Federal Unemployment Tax Act and the Social Security Act as interpreted by the Secretary, the following criteria will be applied:
A. Is it required that individuals who may be entitled to unemployment compensation be furnished such information of their potential rights to benefits, including the manner and places of filing claims, the reasons for determinations, and their rights of appeal, as will reasonably afford them an opportunity to know, establish, and protect their rights under the law of the State?
B. Is the State agency required to obtain, in time for prompt determination of rights to benefits such information as will reasonably afford
insure the payment of benefits to individuals to whom benefits are due?

C. Is the State agency required to keep records of the facts considered in reaching determinations of rights to benefits?

C-3 Determinations Requirements Designed To Meet Department of Labor Criteria:

A. Investigation of claims. The State agency is required to obtain promptly and prior to a determination of an individual's right to benefits, such facts pertaining thereto as will be sufficient reasonably to assure the payment of benefits when due.

This requirement embraces five separate elements:

1. It is the responsibility of the agency to take the initiative in the discovery of information. This responsibility may not be passed on to the claimant or the employer. In addition to the agency's own records, this information may be obtained from the worker, the employer, or other sources. If the information obtained in the first instance discloses no essential disagreement and provides a fair determination, no further investigation is necessary. If the information obtained from other sources differs essentially from that furnished by the claimant, the agency, in order to meet its responsibility, is required to inform the claimant of such information from other sources and to afford the claimant an opportunity to furnish any further facts he may have.

2. Evidentiary facts must be obtained as distinguished from ultimate facts or conclusions. That a worker was discharged for misconduct is an ultimate fact; that he destroyed a machine upon which he was working is a primary or evidentiary fact; and the sort of fact that the requirement refers to.

3. The information obtained must be sufficient reasonably to assure the payment of benefits when due. In general, the investigation made by the agency must be complete enough to provide information upon which the agency may act with reasonable assurance that its decision is consistent with the unemployment compensation law. On the other hand, the investigation should not be so exhaustive and time-consuming as unduly to delay the payment of benefits and to result in excessive costs.

4. Information must be obtained promptly so that the payment of benefits is not unduly delayed.

5. If the State agency requires any particular evidence from the worker, it must give the worker a reasonable opportunity to obtain such evidence.

B. Recording of facts. The agency must keep a written record of the facts considered in reaching its determinations.

C. Determination notices.

1. The agency must give each claimant a written notice of:

a. Any monetary determination with respect to his benefit year.

b. Any determination with respect to purging a disqualification if, under the State law, a condition or qualification must be satisfied with respect to each week of disqualification; but in lieu of giving written notice of each determination for each week in which it is determined that the claimant has met the requirements for purging, the agency may inform the claimant that he has purged the disqualification for a week by notation of his applicant identification card or otherwise in writing.

c. Any other determination which adversely affects the claimant's right to benefits, except that written notice of determination need not be given with respect to:

(1) A written notice of a week for which the claimant's weekly benefit amount is reduced in whole or in part by earnings if, the first time in the benefit year that there is such a reduction, he is required to be furnished a dispute concerning the denial or reduction, etc., or (b) there is a change in the State law or in the application therefor affecting the denial or reduction;

(2) Any week in a benefit year subsequent to the first week in such benefit year in which benefits were denied, or reduced in whole or in part for reasons other than earnings, if denial or reduction for such subsequent week is based on the same reason and the same facts as for the first week, and if written notice of determination is required to be given to the claimant with respect to such first week, and with such notice of determination, is required to be given a booklet or pamphlet containing the information set forth below in paragraphs 2f(2) and 2h. However, a written notice of determination is required if: (a) there is a dispute concerning the reduction with respect to any week (e.g., as to the amount or as computed as the appropriate reduction, etc.), or (b) there is a change in the State law or in the application therefor affecting the denial or reduction; or

(2) Any week in a benefit year subsequent to the first week in such benefit year in which benefits were denied, or reduced in whole or in part for reasons other than earnings, if denial or reduction for such subsequent week is based on the same reason and the same facts as for the first week, and if written notice of determination is required to be given to the claimant with respect to such first week, and with such notice of determination, is required to be given a booklet or pamphlet containing the information set forth below in paragraphs 2f(2) and 2h. However, a written notice of determination is required if: (a) there is a dispute concerning the reduction with respect to any week (e.g., as to the amount or as computed as the appropriate reduction, etc.), or (b) there is a change in the State law or in the application therefor affecting the denial or reduction; or

(2) Any week in a benefit year subsequent to the first week in such benefit year in which benefits were denied, or reduced in whole or in part for reasons other than earnings, if denial or reduction for such subsequent week is based on the same reason and the same facts as for the first week, and if written notice of determination is required to be given to the claimant with respect to such first week, and with such notice of determination, is required to be given a booklet or pamphlet containing the information set forth below in paragraphs 2f(2) and 2h. However, a written notice of determination is required if: (a) there is a dispute concerning the reduction with respect to any week (e.g., as to the amount or as computed as the appropriate reduction, etc.), or (b) there is a change in the State law or in the application therefor affecting the denial or reduction; or

(2) Any week in a benefit year subsequent to the first week in such benefit year in which benefits were denied, or reduced in whole or in part for reasons other than earnings, if denial or reduction for such subsequent week is based on the same reason and the same facts as for the first week, and if written notice of determination is required to be given to the claimant with respect to such first week, and with such notice of determination, is required to be given a booklet or pamphlet containing the information set forth below in paragraphs 2f(2) and 2h. However, a written notice of determination is required if: (a) there is a dispute concerning the reduction with respect to any week (e.g., as to the amount or as computed as the appropriate reduction, etc.), or (b) there is a change in the State law or in the application therefor affecting the denial or reduction; or

(2) Any week in a benefit year subsequent to the first week in such benefit year in which benefits were denied, or reduced in whole or in part for reasons other than earnings, if denial or reduction for such subsequent week is based on the same reason and the same facts as for the first week, and if written notice of determination is required to be given to the claimant with respect to such first week, and with such notice of determination, is required to be given a booklet or pamphlet containing the information set forth below in paragraphs 2f(2) and 2h. However, a written notice of determination is required if: (a) there is a dispute concerning the reduction with respect to any week (e.g., as to the amount or as computed as the appropriate reduction, etc.), or (b) there is a change in the State law or in the application therefor affecting the denial or reduction; or

(2) Any week in a benefit year subsequent to the first week in such benefit year in which benefits were denied, or reduced in whole or in part for reasons other than earnings, if denial or reduction for such subsequent week is based on the same reason and the same facts as for the first week, and if written notice of determination is required to be given to the claimant with respect to such first week, and with such notice of determination, is required to be given a booklet or pamphlet containing the information set forth below in paragraphs 2f(2) and 2h. However, a written notice of determination is required if: (a) there is a dispute concerning the reduction with respect to any week (e.g., as to the amount or as computed as the appropriate reduction, etc.), or (b) there is a change in the State law or in the application therefor affecting the denial or reduction; or

(2) Any week in a benefit year subsequent to the first week in such benefit year in which benefits were denied, or reduced in whole or in part for reasons other than earnings, if denial or reduction for such subsequent week is based on the same reason and the same facts as for the first week, and if written notice of determination is required to be given to the claimant with respect to such first week, and with such notice of determination, is required to be given a booklet or pamphlet containing the information set forth below in paragraphs 2f(2) and 2h. However, a written notice of determination is required if: (a) there is a dispute concerning the reduction with respect to any week (e.g., as to the amount or as computed as the appropriate reduction, etc.), or (b) there is a change in the State law or in the application therefor affecting the denial or reduction; or

Note.—This procedure may be applied to determinations made with respect to any subsequent weeks for the same reason and on the basis of the same facts: (a) that claimant is unable to work, unavailable for work, or is disqualified under the labor dispute provision; and (b) reducing claimant's weekly benefit amount because of income other than earnings or offset by reason of overpayment.

2. The agency must include in written notices of determinations furnished to claimants sufficient information to enable them to understand the determinations, the reasons therefor, and their rights to protest, request reconsideration, or appeal.

The written notice of monetary determination must contain the information specified in the following items (except h) unless an item is specifically not applicable.

A written notice of any other determination must contain the information specified in as many of the following items as are necessary to enable the claimant to understand the determination and to inform him of his appeal rights. Information not specifically applicable to the individual claimant must be contained in the written notice of determination. Information of general application such as (but not limited to) the explanation of benefits for partial unemployment, information as to deductions, seasonality factors, and information as to the manner and place of taking an appeal, extension of the appeal period, and where to obtain information and assistance may be contained in a booklet or leaflet which is given the claimant with his monetary determination.

a. Base period wages. The statement concerning base-period wages must be in sufficient detail to show the basis of computation of eligibility and weekly and maximum benefit amounts. (If maximum benefits are allowed, it may not be necessary to show details of earnings.)

b. Employer name. The name of the employer who reported the wages is necessary so that the worker may check the wage transcript and know whether it is correct. If the worker is given only the employer number, he may not be able to check the accuracy of the wage transcript.

c. Explanation of benefit formula—weekly and maximum benefit amounts. Sufficient information must be given the worker so that he will understand how his weekly benefit amount, including allowances for dependents, and his maximum benefit amount were figured. If benefits are computed by means of a table contained in the law, the table must be furnished with the notice of determination whether benefits are granted or denied.

The written notice of determination must show clearly the weekly benefit amount and the maximum potential benefits to which the claimant is entitled.

The notice to a claimant found ineligible by reason of insufficient earnings in the base period must inform him clearly of the reason for ineligibility. An explanation of the benefit formula contained in a booklet or pamphlet should be given to each claimant at or prior to the time he receives written notice of a monetary determination.

d. Benefit year. An explanation of what is meant by the benefit year and identification of the claimant's benefit year must be included in the notice of determination.

e. Information as to benefits for partial unemployment. There must be included either in the written notice of determination or in a booklet or pamphlet accompanying the notice an explanation of the claimant's rights to partial benefits for any week with respect to which he is working less than his normal customary full-time workweek because of
Deductions from weekly benefits.

(1) Earnings. Although written notice of determinations deducting earnings from a claimant's weekly benefit amount is generally not required (see paragraph 1c(1) above), where written notice of determination is required (or given) it shall set forth the amount of earnings, the method of computing the deduction in sufficient detail to enable the claimant to verify the accuracy of the deduction, and his right to protest, request redetermination, and appeal. Where a written notice of determination is given to the claimant because there has been a change in the State law or in the application of the law, an explanation of the change shall be included.

Where claimant is not required to receive a written notice of determination, he must be given a booklet or pamphlet the first time in his benefit year that there is a deduction for earnings which shall include the following information:

The method of computing deductions for earnings in sufficient detail to enable the claimant to verify the accuracy of the deduction;

(b) That he will not automatically be given a written notice of determination for a week with respect to which there is a deduction for earnings (unless there is a dispute concerning the reduction with respect to a week or there has been a change in the State law or in the application of the law affecting the deduction) but that he may obtain such a written notice upon request;

(c) A clear statement of his right to protest, request redetermination, and appeal from any deduction which might affect determinations for subsequent weeks that a benefit amount, the reason for the deduction, and his right to protest, request redetermination, and appeal.

(2) Other deductions.

(a) A written notice of determination is required with respect to the first week in claimant's benefit year in which there is a reduction from his benefits for a reason other than earnings. This notice must describe the deduction made from claimant's weekly benefit amount, the reason for the deduction, the method of computing it in sufficient detail to enable him to verify the accuracy of such deduction, and his right to protest, request redetermination, or appeal.

(b) A written notice of determination is not required for subsequent weeks that a deduction is made for the same reason and on the basis of the same facts. If the notice of determination pursuant to (2)(a) or a booklet or pamphlet given him with such notice explains (i) the several kinds of deductions which may be made under the State law (e.g., retirement pensions, vacation pay, and governmental); (ii) the method of computing each kind of deduction; (iii) the sufficient detail to enable claimant will be able to verify the accuracy of deductions made from his weekly benefit payments; (iii) any limitation on the amount of any deduction or the time in which any deduction may be made; (iv) that he will not automatically be given a written notice of determination for subsequent weeks with respect to which there is a deduction for the same reason and on the basis of the same facts, but that he may obtain a written notice of determination upon request; (v) his right to protest, request redetermination, or appeal with respect to subsequent weeks for which there is a reduction from his benefits for the same reason, and on the basis of the same facts even though he does not automatically receive a written notice of determination; and (vi) that if the State law requires written notice of determination in order to effectuate a protest, redetermination, or appeal, he must be so advised and advised also that he must request a written notice of determination before he takes any such action.

(c) Seasonality factors. If an individual's determination is affected by seasonality factors under the State law, an adequate explanation must be made. General explanation of seasonality factors which affect determinations for subsequent weeks for which a benefit amount may be included in a booklet or pamphlet given claimant with his notice of monetary determination.

D. Disqualification or Ineligibility.

If a disqualification is imposed, or if the claimant is declared ineligible for one or more weeks, he must be given not only a statement of the period of disqualification or ineligibility and the amount of wage-credit reductions, if any, but also an explanation of the reason for the ineligibility or disqualification. This explanation must be sufficiently detailed so that he will understand why he is ineligible or why he has been disqualified, and what he must do in order to requalify for benefits or purge the disqualification. The statement must be individualized to indicate the facts upon which the determination was based, e.g., state, "It is found that you left your work with Blah Blah Blah, though you were tired of working, the separation was voluntary, and the reason does not constitute good cause," rather than merely the phrase "voluntary quit." Checking a box as to the reason for the disqualification is not a sufficiently detailed explanation. However, this statement of the reason for the disqualification need not be a restatement of all facts considered in arriving at the determination.

Appeal rights.

The claimant must be given information with respect to his appeal rights.

(1) The following information shall be included in the notice of determination:

(a) A statement that he may appeal, or if the State law requires or permits a protest or redetermination before an appeal, that he may protest or request a redetermination.

(b) The place or places to which the appeal, protest, or request for redetermination may be mailed or hand-delivered.

(2) The following information must be included either in the notice of determination or in separate informational material referred to in the notice:

(a) The manner in which the appeal, protest, or request for redetermination must be filed, e.g., by signed letter, written statement, or on a prescribed form, and the place or places to which the appeal, protest, or request for redetermination may be mailed or hand-delivered.

(b) An explanation of any circumstances (such as nonworkdays, good cause, etc.) which will extend the period for the appeal, protest, or request for redetermination beyond the date stated or identified in the notice of determination.

(c) That any further information claimant may need or desire can be obtained together with assistance in filing his appeal, protest, or request for redetermination from the local office.

If the information is given in separate material, the notice of determination would adequately refer to such material if it said, for example, "For other information about your appeal, protest, [redetermination] rights, see page ___ of the booklet or pamphlet heretofore furnished to you."
1. Information required to be given. Employers are required to give their employees information and instructions concerning the employees' potential rights to benefits and concerning registration for work and filing claims for benefits. The information furnished to employees under such a requirement need not be elaborate; it need only be adequate to insure that the worker who is separated or who is working less than full time knows he is potentially eligible for benefits and is informed as to what he is to do or where he is to go to file his claim and register for work. When he files his claim, he can obtain more detailed information.

In States that do not require employers to furnish periodically to the State agency detailed reports of the wages paid to their employees, each employer is required to furnish to his employees information as to (a) the name under which he is registered by the State agency, (b) the address where he maintains his payroll records, and (c) the workers' need for this information if and when they file claims for benefits.

2. Methods for giving information. The information and instructions required above may be given in any of the following ways:

a. Posters prominently displayed in the employer's establishment. The State agency should supply employers with a sufficient number of posters for distribution throughout their places of business and should see that the posters are conspicuously displayed at all times.

b. Leaflets. Leaflets distributed either periodically or at the time of separation or reduction of hours. The State agency should supply employers with a sufficient number of leaflets.

c. Individual notices. Individual notices given to each employee at the time of separation or reduction in hours.

It is recommended that the State agency's publicity program be used to supplement the employer-information requirements. Such a program should stress the availability and location of claim-filing offices and the importance of visiting those offices whenever the worker is unemployed, wishes to apply for benefits, and to seek a job.


If the State law provisions do not conform to the suggested requirements set forth in sections 6013 and 6014, but the State law contains alternative provisions, the Bureau of Employment Security, in collaboration with the State agency, will study the actual or anticipated effects of the alternative provisions. If the Administrator of the Bureau concludes that the alternative provisions satisfy the criteria in section 6012, he will so notify the State agency. If the Administrator of the Bureau does not so conclude, he will submit the matter to the Secretary. If the Secretary concludes that the alternative provisions satisfy the criteria in section 6012, the State agency will be so notified. If the Secretary concludes that there is a question as to whether the alternative provisions satisfy the criteria, the State agency will be advised that unless the State law provisions are appropriately revised, a notice of hearing will be issued as required by the Code of Federal Regulations, title 20, section 601.5.

[FR Doc. 87-20151 Filed 9-2-87; 8:45 am]
BILLING CODE 4510-30-M