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The Department of Labor's Proposed Investment Selection Safe Harbor: a deeper dive

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In this article, the author analyzes in depth a new rule proposed by the US Department of Labor's Employee Benefits Security Administration titled, "Fiduciary Duties in Selecting Designated Investment Alternatives."

Introduction

The US Department of Labor's Employee Benefits Security Administration (DOL) has proposed a new rule[1] titled, "Fiduciary Duties in Selecting Designated Investment Alternatives" (the Proposed Safe Harbor Rule).[2] The Proposed Safe Harbor establishes a six-factor safe harbor framework designed to clarify the application of ERISA's[3] fiduciary duty of prudence to the selection of designated investment alternatives (DIAs) within 401(k) plans.[4]

Importantly, the Proposed Safe Harbor is asset neutral in that it affirms that ERISA Section 404(a)(1)(B) "does not require or restrict any specific type of designated investment alternative."[5] Moreover, the Proposed Safe Harbor establishes a six-factor safe harbor that a fiduciary must "objectively, thoroughly, and analytically consider and make determinations about" when selecting DIAs.[6] Where a fiduciary satisfies this standard with respect to a given factor, "its judgment regarding the factor or factors is presumed to be reasonable and is entitled to significant deference."[7]

Notably, compliance with the prudence safe harbor does not excuse fiduciaries from the duty of loyalty under ERISA Section 404(a)(1)(A) or the prohibited transaction rules under Section 406. Moreover, the Proposed Safe Harbor addresses investment selection only; the DOL has deferred the ongoing monitoring obligation to forthcoming interpretive guidance.

This article dives deeper into the Proposed Safe Harbor, detailing the specific illustrative examples provided by the DOL under each of the safe harbor's six factors and providing best practices for plan fiduciaries. Lastly, we discuss key developments to watch going forward.

The six Safe Harbor factors in practice

Performance

Under the Proposed Safe Harbor, the fiduciary must consider similar alternatives and determine that the DIA's risk-adjusted expected returns, over an appropriate time horizon and net of fees, further the plan's purposes.[8] The standard is maximizing

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returns for a given level of appropriate risk–not selecting the highest-returning strategy[9] This requirement is illustrated in the examples discussed below.

Consideration of returns (g)(1)

When a target date fund series offers lower expected returns but also lower expected risk compared to alternative series considered, including by incorporating alternative assets with low correlations to stocks and bonds to reduce return volatility, a fiduciary satisfies the performance requirement by selecting such series after evaluating the risk of potential investments and the risk capacity of the plan's participants. The fiduciary may rely on advice from a qualified third-party investment advice fiduciary in making this determination. This example establishes the principle that fiduciaries are not required to select the investment strategy with the highest returns; rather, the obligation is to maximize returns for a given level of appropriate risk, consistent with participants' likely needs over the anticipated investment horizon[10]

Consideration of time horizon (g)(2)

When evaluating three-target date fund series by reviewing 1-, 3-, 5- and 10-year historical performance data and placing the greatest weight on the 10-year data, a fiduciary satisfies the performance requirement by making its selection with the support of a qualified third-party investment advice fiduciary. This example confirms that fiduciaries are not required to prioritize short-term or most-recent performance data when selecting a DIA. Given the long-term nature of retirement savings, an appropriately long time horizon—such as 10 years—is a reasonable and prudent basis for evaluating and comparing investment performance[11]

Fees

The fiduciary must consider similar alternatives and determine that fees are appropriate given risk-adjusted returns and any other value the DIA provides.[12] The Proposed Safe Harbor provides five illustrative examples:

Higher fees with comparable risk-adjusted returns (h)(1)

Where a DIA carries higher fees than comparable alternatives offering similar risk-adjusted returns, a fiduciary does not act imprudently solely by selecting such DIA. Consistent with existing case law, the duty of prudence does not impose a categorical requirement to always choose the lowest-fee option. In this example, the fiduciary prudently identified exemplary customer service as the value proposition justifying the higher fee, demonstrating that a holistic assessment of value— not fee minimization alone—governs the selection process[13]

Failure to consider share class differences (h)(2)

A fiduciary fails to satisfy the prudence requirement when it selects a more expensive share class of a registered investment company without considering the differences in fee structures among available share classes, where a less expensive share class is identical in all other material respects. The fiduciary's failure to enlist a professional advisor, manager or consultant compounds the deficiency. This example confirms that a prudent selection process ordinarily would identify and select the lower-cost share class where no other differentiating value proposition exists.[14]

Lifetime income benefit option—additional fee justified (h)(3)

When selecting an asset allocation fund offered through a variable annuity contract which carries an additional fee above the expense ratio of a comparable existing fund, a fiduciary satisfies the fee requirement when it selects by consulting an investment advice fiduciary who analyzes the annuity market, break-even ages and the additional fee, and then critically evaluating and adopting that analysis to determine that the new alternative provides commensurate value. This example establishes that additional fees associated with a lifetime income feature can be appropriate where a thorough, expert-supported analysis confirms that the fee is justified by the value it delivers in furthering the purposes of the plan.[15]

Target date fund modification for risk mitigation—higher fees justified (h)(4)

When modifying a qualified default investment alternative target date fund to include hedge funds and private equity (increasing the expense ratio but providing downside protection and reduced volatility), a fiduciary satisfies the fee requirement when it enlists an investment advice fiduciary to produce a written report stochastically modeling the risk-adjusted returns of the modified fund and comparing it to similar alternatives. The fiduciary must independently consider and determine that the modification furthers the plan's purposes and that the higher expense ratio is appropriate in light of the estimated higher risk-adjusted expected returns, net of fees and

expenses, over an appropriate time horizon. Importantly, a modification of this magnitude is treated as tantamount to the selection of a new DIA, and is therefore subject to the full requirements of the proposed regulation.[16]

Active vs. Passive management—diversification benefits justify higher fees (h)(5)

Where both an actively managed and a passively managed fund are available within a particular strategy (even where the actively managed fund charges higher fees), a fiduciary may prudently select both options where, with the assistance of an investment advice fiduciary, it determines that offering both provides diversification benefits across the plan's investment menu that justify the higher fees of the active fund. This example confirms that fee comparisons need not be made in isolation and that the broader portfolio-level value of diversification is a legitimate and prudent basis for selecting a higher-fee investment alternative, consistent with modern portfolio theory and established case law.[17]

Liquidity

Fiduciaries may offer DIAs that include illiquid assets, recognizing that participants (particularly those with longer investment horizons) can benefit from the illiquidity premium.[18] However, fiduciaries must assess whether each DIA has sufficient liquidity to meet anticipated needs at both the plan and participant levels, ensure that liquidity promises to participants can be honored, and evaluate whether redemptions by other investors could adversely impact the alternative's liquidity.[19] Plans are not required to offer fully liquid options, but diligent liquidity analysis remains integral to the duty of prudence.[20] The Proposed Safe Harbor lists the following examples to illustrate this concept:

Participant-level liquidity—illiquid holdings in a designated investment alternative (i)(1)

When selecting a DIA that holds illiquid, non-publicly traded securities, a fiduciary satisfies the participant-level liquidity requirement by obtaining a written representation from the fund manager confirming that the alternative has adopted and implemented a liquidity risk management program substantially similar to that required of mutual funds under SEC Rule 22e-4. The fiduciary must critically read and review any such representation, independently or with the assistance of a qualified investment professional, and must have no reason to question it. For mutual funds, the regulatory requirement to maintain such a program is sufficient; for other vehicles (for example, collective investment trusts), a written representation or equivalent due diligence is required.[21]

Participant-level liquidity—guaranteed deferred annuity with liquidity restrictions (i)(2)

When selecting a guaranteed deferred annuity contract, under which participant contributions become fully committed after 90 days and early withdrawals trigger penalties and market value adjustments, a fiduciary satisfies the liquidity requirement by conducting an objective, thorough, and analytical investigation and concluding that the value of the guaranteed lifetime monthly payments and the certainty of the insurer's guarantee justify the liquidity restrictions. The fiduciary must affirmatively balance the lack of liquidity against the commensurate benefit of guaranteed income and longevity protection.[22]

Plan-level liquidity—illiquid holdings with redemption restrictions (i)(3)

A fiduciary satisfies the plan-level liquidity requirement when selecting a DIA that holds illiquid assets and imposes redemption restrictions (such as advance notice requirements or incremental redemptions) by following one of two paths:

- **Path 1:** Relying on a mutual fund's regulatory obligation to maintain a written liquidity risk management program under the Investment Company Act,[23] or for non-mutual fund vehicles, obtaining a written representation of a substantially similar program (or conducting equivalent due diligence), provided the fiduciary critically reviews the representation and has no reason to question it.
- **Path 2:** Conducting an independent objective, thorough and analytical evaluation, with or without a third-party investment advice fiduciary, to assess how long it would take the fund to liquidate illiquid assets without value reduction, what redemption restrictions are in place and whether the fund can appropriately balance liquidity needs against its ability to achieve risk-adjusted returns and maintain asset allocation targets even under significant redemption pressure.[24]

Combined participant- and plan-level liquidity—fund with quarterly plan-level redemptions and daily participant liquidity (i)(4)

When selecting a fund that restricts plan-level redemptions to quarterly intervals but provides daily liquidity to individual participants, and which allocates a portion of holdings to illiquid private assets, a fiduciary satisfies both participant- and plan-level liquidity requirements by obtaining written representations that the fund has adopted a liquidity risk management program substantially similar to mutual fund requirements. The fiduciary must critically review those representations with the assistance of a third-party investment advice fiduciary. The fiduciary must also conduct an objective, thorough and analytical evaluation concluding that the redemption structure is appropriate for the plan's needs and that the plan-level liquidity tradeoff is justified by the expected increase in risk-adjusted returns net of fees.[25]

Valuation

The fiduciary must assess whether the DIA maintains adequate procedures to ensure valuations are conducted accurately and on a timely basis.[26] The Proposed Safe Harbor lists the following examples:

Publicly traded securities (j)(1)

Where asset values are readily, accurately and timely determinable, fiduciaries may rely on valuations derived from a national securities exchange or similar public exchange. A fiduciary that relies on such exchange-based valuations is deemed to have satisfied the objective, thorough and analytical valuation determination requirement. This conclusion is not altered solely because a fund manager, acting in good faith, adopts alternative valuation procedures during a documented temporary emergency (for example, where following standard procedures would allow investors to redeem at an inflated valuation, causing significant harm to remaining investors).[27]

Mixed portfolio—public and non-public securities (j)(2)

Where a DIA holds both publicly traded and non-publicly traded securities, a fiduciary may satisfy the valuation requirement by receiving a written representation that non-public securities are valued at least quarterly through a conflict-free, independent process using FASB ASC 820 Fair Value Measurement standards. The fiduciary must critically read and understand those representations and have no information that would give reason to question them.[28]

Mutual funds (j)(3)

For mutual funds holding a mix of publicly traded and non-publicly traded securities, fiduciaries may satisfy the valuation requirement by reviewing the fund's publicly available audited financial statements and valuation-related disclosures (prepared under the Investment Company Act and rule 2a-5), confirming compliance with applicable pricing and valuation requirements, reviewing the fund's Form N-1A prospectus to verify board independence and consulting a qualified investment professional if necessary, provided the fiduciary has no reason to question the accuracy of those statements.[29]

Continuation funds with conflicts of interest (j)(4)

Where a DIA is a continuation fund acquiring assets from a vehicle managed or controlled by the same manager or an affiliate, the risk of a conflicted or self-serving valuation is particularly acute. A fiduciary that agrees to a proprietary valuation methodology relying on inputs provided by the manager's affiliates, rather than requiring an independent, conflict-free process, fails to meet the valuation consideration and determination requirement. Even where plan assets are not held directly under ERISA, fiduciaries must take appropriate steps to understand and mitigate conflicts of interest that could negatively impact risk-adjusted returns, and must affirmatively determine that such conflicts have not and will not render the valuation inaccurate.[30]

Notably, a continuation fund using a proprietary valuation methodology that relies on inputs from affiliates of the manager does not satisfy this factor— one of the most significant signals for private markets practitioners. The DOL has expressly requested public comment on whether additional safeguards should be mandated for continuation funds and similar vehicles.[31]

Performance benchmarking

The fiduciary must assess whether each DIA is measured against a "meaningful benchmark," that is, an investment, strategy, index or other comparator that shares similar mandates, strategies, objectives and risks.[32] No single

benchmark will be appropriate across all DIAs on a plan menu.[33] Three examples discussed below illustrate this factor.

Target date fund—inappropriate benchmark (k)(1)

Where a large capitalization US equity index is selected as a performance benchmark for a target date fund, a fiduciary fails to satisfy the benchmark requirement. A large cap index is not a meaningful comparator because it tracks different securities than the target date fund holds and adjusts its constituents based on market capitalization changes rather than a time-to-retirement glide path. This example establishes the principle that a performance benchmark must share similar traits with the DIA, including mandates, strategies, objectives and risks, and that a fiduciary cannot use a less suitable benchmark when a more appropriate one is available.[34]

Asset allocation fund with private equity sleeve— composite benchmark and reliance on investment advice fiduciary (k)(2)

Where a prudent, unaffiliated investment advice fiduciary constructs a composite benchmark that measures risk-adjusted expected returns, net of fees, across the fund's sleeves, a fiduciary satisfies the benchmark requirement. The composite benchmark must blend broad-based securities market indices for public stock and bond holdings in proportion to their weight in the fund. For the private equity sleeve, the benchmark must use commonly accepted private equity methodologies, such as internal rate of return and public market equivalent methods. The fiduciary must read, critically review and understand the investment advice fiduciary's written explanation of the composite benchmark. This example illustrates that named fiduciaries may rely on the expertise of an investment advice fiduciary in benchmark construction, provided they actively engage with and understand that fiduciary's analysis.[35]

Target date fund—custom composite benchmark (k)(3)

Where a custom composite benchmark blends multiple broad-based securities market indices in proportions that reflect a target date fund's asset allocation strategy to evaluate a target date fund holding only publicly traded stocks and bonds, a fiduciary satisfies the benchmark requirement by selecting such benchmark. The fiduciary must read, critically review and understand the benchmark description, and must compare the fund's historical performance against the benchmark's historical returns to evaluate risk-adjusted expected returns, net of fees. This example confirms that fiduciaries may appropriately rely on blended index benchmarks where the custom composite shares similar traits, including mandates, strategies, objectives and risks with the DIA.[36]

Complexity

The fiduciary must evaluate whether it possesses sufficient expertise and capacity to understand the DIA to a degree necessary to fulfill its ERISA duties, or whether it must engage qualified professional assistance.[37] Where such assistance is required, the fiduciary must exercise prudence in selecting the professional. Two examples illustrate this factor:

Complex fee structures (l)(1)

When reviewing a pooled investment vehicle with private asset target positions that employ variable fee structures (including management fees, performance fees and carried interest), a fiduciary satisfies the complexity requirement under either of two scenarios:

- The fiduciary conducts thorough due diligence on the fees and expenses, engaging a qualified third-party investment advice fiduciary where appropriate, and concludes that the fee structure will deliver increased value that outweighs the variability and potential unpredictability of the amount and timing of the fees.
- The fiduciary obtains written representations from the fund manager confirming that the manager will internalize the underlying fees, with the plan paying only an appropriate flat fee based on assets under management.[38]

Managed account service—failure to understand participant needs (l)(2)

A managed account service may be designed to create a customized portfolio targeted to each participant's unique financial circumstances. Where a fiduciary selects such a service as the plan's qualified default investment alternative, but does not understand the design of the service and does not seek professional advice, the fiduciary fails to satisfy the complexity requirement. In this example, the fiduciary provides only the age of each participant to the service and does not provide, or permit participants to

provide, additional information about their unique financial circumstances. As a result, the service creates a portfolio for each participant that is materially similar to the portfolio that the participant would obtain through the plan's target date fund, which has substantially lower fees. This example demonstrates a flawed selection process in which the fiduciary appears to not understand how the DIA delivered value to the plan and therefore failed to operationalize it accordingly.

Best practices for plan fiduciaries

The Proposed Safe Harbor establishes a six-factor, process-based safe harbor for satisfying ERISA's duty of prudence when selecting DIAs, including asset allocation funds with exposure to alternative assets. While the safe harbor is not prescriptive, it makes clear that fiduciary protection flows from disciplined process, careful documentation and ongoing engagement. In light of the risks associated with alternative investments, including complexity, liquidity constraints, valuation challenges and heightened litigation scrutiny, plan fiduciaries should consider the following best practices.

Conduct objective and thorough due diligence

Plan fiduciaries should conduct an objective, thorough and analytical review of any investment that provides exposure to alternative assets. This evaluation should address, at a minimum, the investment's structure, strategy, underlying assets, risk profile, expected risk-adjusted returns, fee arrangements, valuation methodologies and liquidity characteristics. Fiduciaries should consider a reasonable range of comparable alternatives and assess how the investment fits within the plan's broader investment menu or asset allocation strategy.

Critically, fiduciaries should document each step of the due-diligence process, including materials reviewed, questions asked of managers, advice received from investment professionals and the fiduciaries' independent conclusions. The proposed rule repeatedly emphasizes that contemporaneous documentation is central to demonstrating compliance with ERISA's prudence standard.

Ensure meaningful participant disclosure and education

Where alternative assets are made available—directly or indirectly— through a designated investment alternative, fiduciaries should ensure that participants receive clear, accurate and comprehensible information regarding the nature of the investment. This includes disclosures addressing investment objectives, material risks, fee structures, liquidity limitations, valuation practices and any unique operational features.

Beyond formal disclosures, fiduciaries should consider whether participant education tools are appropriate to help participants understand how alternative investments behave across market cycles and how they may differ from traditional public-market funds. Providing robust disclosures and educational materials can help participants make informed decisions and may mitigate litigation risk based on alleged disclosure deficiencies.

Monitor dias on an ongoing basis

Although the Proposed Safe Harbor focuses on selection, it expressly reaffirms that fiduciaries retain an ongoing duty to prudently monitor designated investment alternatives after placement on the plan menu. Fiduciaries should periodically review performance relative to meaningful benchmarks, fee levels, liquidity experience, valuation practices and operational integrity.

Monitoring should be calibrated to the nature of the investment. For example, investments with limited liquidity or longer investment horizons may warrant different performance expectations than fully liquid public-market funds. Fiduciaries should be prepared to take corrective action, including modification or removal, if an investment no longer serves the plan's objectives or if superior alternatives emerge.

Evaluate plan design and vehicle selection

Plan sponsors should carefully consider how alternative assets are offered within the plan. Consistent with the proposed rule's emphasis on process and participant protection, fiduciaries may wish to limit exposure to alternative assets through professionally managed asset allocation vehicles such as target date funds, balanced funds or collective investment trusts, rather than offering stand-alone alternatives.

Fiduciaries should also consider appropriate sizing—for example, limiting alternative asset exposure to a modest portion of a diversified portfolio—and whether plan demographics, participant turnover and investment horizons support the inclusion of less liquid or more complex strategies.

Assess liquidity at both the participant and plan level

Liquidity analysis is a core component of the proposed safe harbor. Fiduciaries must evaluate whether DIAs provide sufficient liquidity to meet reasonable participant-level and plan-level needs, taking into account expected contribution patterns, withdrawals, loans and transfers.

Where investments include illiquid assets, fiduciaries should understand redemption terms, notice requirements, gating provisions and liquidity risk-management practices. Fiduciaries should also assess whether liquidity constraints are adequately balanced by expected risk-adjusted returns and whether liquidity promises made to participants can be fulfilled under stressed conditions.

Maintain robust records and governance practices

Fiduciaries should maintain comprehensive records documenting all decisions related to the selection, retention and monitoring of investments with alternative asset exposure. This includes documenting the rationale for decisions, reliance on internal expertise or external advisors, reviews of conflicts of interest and steps taken to address risks identified during due diligence or monitoring.

Strong governance practices—including clear investment policies, defined roles and responsibilities and regular committee reviews—are essential complements to recordkeeping. Together, these practices form the evidentiary backbone of the process-based safe harbor contemplated by the DOL Proposed Safe Harbor Rule.

Selection and monitoring of service providers

Ultimate responsibility for the selection and monitoring of service providers remains with the plan fiduciary. The plan fiduciary should consider whether existing engagement agreements and investment policy statements appropriately reflect fiduciary expectations under the DOL Proposed Safe Harbor Rule. The plan fiduciary may wish to revisit how information provided by advisers and managers is evaluated, challenged and documented.

What to watch next

- DOL's regulatory agenda includes a separate project to revise the foundational 1979 Investment Duties Regulation, signaling the Proposed Safe Harbor is part of a broader ERISA investment duties modernization effort.
- Fiduciaries must also satisfy Section 404(c)'s requirements for a broad range of investment alternatives—a dual-compliance framework that the Proposed Safe Harbor does not address.
- DOL is seeking comment on whether participant profiles or characteristics should be added as a seventh safe harbor factor.
- The Supreme Court's ultimate ruling on Anderson v. Intel Corp.39 will shape how courts receive the meaningful benchmark doctrine embedded in the safe harbor.

The implications of the Proposed Safe Harbor for plan sponsors, and the millions of retirement savers who depend on prudent fiduciary decision-making, are far-reaching. With the comment period closing on June 1, 2026, and the regulatory landscape for ERISA investment duties continuing to evolve, now is the time to act. Whether you need to evaluate your current plan menu against the six-factor safe harbor framework, assess fiduciary compliance exposure, prepare comment letters or develop governance and documentation practices aligned with the DOL's heightened expectations, our team stands ready to provide strategic counsel at every stage.

Notes

1. https://www.federalregister.gov/documents/2026/03/31/2026-06178/ fiduciary-duties-in-selecting-designated-investment-alternatives.

2. The Proposed DOL regulation explains that a DIA "refers generally to the investment options of the plan's menu chosen by a fiduciary and available to participants and beneficiaries for investment of their retirement benefits." Id. at 20.

3. https://www.dol.gov/agencies/ebsa/laws-and-regulations/laws/erisa.

4. Proposed DOL regulation, supra n.1.

5. Id. This includes investments in foreign adversaries, OFAC-sanctioned entities, and investments violating civil rights laws are categorically impermissible.

6. Id. at 26.

7. Id. Importantly, fiduciaries need not satisfy the safe harbor's requirements on their own. The DOL Proposed Investment Selection Safe Harbor Rule permits fiduciaries to rely on recommendations of a prudently selected investment advice fiduciary under ERISA Section 3(21)(A)(ii) or by delegating compliance to an investment manager under ERISA Section 3(38).

8. Id. at 27.

9. Id. See also, Anderson v. Intel Corp., 137 F.4th 1015, 1024 (9th Cir. 2025), confirms that "ERISA fiduciaries are not required to adopt a riskier strategy simply because that strategy may increase returns."

10. Id. at 29.

11. Id. at 30.

12. Id.at at 29. ERISA is not violated solely because the fiduciary does not select the lowest-fee alternative.

13. Id. at 30.

14. Id. at 30-31.

15. Id. at 31-32.

16. Id. at 32-33.

17. Id. at 33-34.

18. Id. at 34.

19. Id.

20. Id.

21. Id. at 35-36.

22. Id. at 36-37.

23. https://www.govinfo.gov/content/pkg/COMPS-1879/pdf/COMPS-1879.pdf.

24. DOL Proposed Regulation, supra n.1 at 37-39.

25. Id. 39-40.

26. Id. at 40.

27. Id. at 40-41.

28. Id. at 41-42.

29. Id. at 42-43.

30. Id. at 43-44.

31. Id. at 44.

32. Id. at 44-45.

33. Id.

34. Id. at 45-46.

35. Id. at 46-47.

36. Id. at 47-48.

37. Id. at 48-49.

38. Id. at 50.

39. Anderson v. Intel Corp. (No. 25-498), available at https://www.supremecourt.gov/docket/docketfiles/html/public/25-498.html.

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