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Proposed Change to the Fiduciary Rule: An Opportunity For Introspection

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The Department of Labor recently published long-promised revisions to the rules regulating investment advisers who advise retirement plans and their fiduciaries, participants and beneficiaries, as well as IRAs and their owners and beneficiaries (“Advice Recipients”). The new proposed fiduciary regulations (the “2015 Proposed Rule”) are the Department of Labor's most recent attempt to modernize long-standing labor rules that have been in place since before the creation of the 401(k) plan and the widespread use of IRAs. The Department of Labor initially attempted in 2010 to revise the same fiduciary regulations, but withdrew those regulations after receiving significant push-back from stakeholders.

Crux of the Issue

The crux of the issue is that plan fiduciaries must act in the best interest of their Advice Recipients. Under ERISA and the Internal Revenue Code, a prohibited transaction occurs if a fiduciary uses plan or IRA assets for their own advantage. For example, a fiduciary adviser who receives compensation from a third party (i.e., the plan recordkeeper or platform provider) to recommend a particular investment to an Advice Recipient may be engaging in a prohibited transaction. Fiduciaries who are a party to a prohibited transaction may be subject to penalties and law suits from plan participants.

In the past, investment advisers have navigated this issue by serving in a non-fiduciary consulting capacity with respect to their Advice Recipients. The current long-standing regulations generally treat an adviser as a fiduciary only if the adviser enters into an *agreement* with an Advice Recipient to *regularly* provide *individualized* investment advice that will serve as the *primary basis* upon which the Advice Recipient will make *investment* decisions (this is generally referred to as the “five-part test”). Each element of the five-part test must be satisfied in order for an adviser to be considered a fiduciary.

Investment consultants take the position that they are not fiduciaries under the five-part test because they either do not provide *regular* advice to the Advice Recipient or the advice they provide is not the primary basis of the Advice Recipient's investment decision. Plans that use investment consultants who do not assume fiduciary responsibility should be aware that the 2015 Proposed Rule may ultimately characterize these consultants as fiduciaries.

Expands Fiduciary Activity

Under the 2015 Proposed Rule an adviser will be a fiduciary to an Advice Recipient even if the adviser does not regularly provide investment advice to the Advice Recipient and even if the advice is not the primary basis for the Advice Recipient's investment decision. Instead, under the 2015 Proposed Rule, an adviser may become a fiduciary if the adviser receives a fee for the advice *and* the adviser either (i) represents or acknowledges that he or she is acting as a fiduciary with respect to the Advice Recipient or (ii) agrees in writing or verbally to provide the Advice Recipient with advice that is individualized or specifically directed to the Advice Recipient.

Under the 2015 Proposed Rule investment advice generally includes:

- A recommendation to acquire, hold, dispose or exchange an investment, including in connection with a participant's distribution or rollover from a plan or IRA;
- A recommendation with respect to the management of an investment, including in connection with a participant's distribution or rollover from a plan or IRA;
- An appraisal, fairness opinion, or similar oral or written statement concerning the value of an investment in connection with a transaction involving a plan or IRA; or
- A recommendation to hire another service provider who will provide investment advice.

Under the 2015 Proposed Rule a “recommendation” includes an adviser's suggestion for the Advice Recipient to take a particular course of action with respect to an investment under the Advice Recipient's control.

Common Plan Administration Carve-Outs

Notwithstanding the apparent breadth of 2015 Proposed Rule, the rule does contain a number of helpful carve-outs summarized below that identify common situations in which an adviser will not be considered a plan fiduciary.

- Providing a plan or IRA with an investment platform, provided that the recordkeeper or platform provider notifies the Advice Recipient that it is not providing investment advice or serving as a fiduciary.
- Identifying investment options that satisfy the pre-established investment criteria of an independent plan fiduciary (e.g. expense ratios, size of fund, type of asset, etc.) and/or providing benchmarking information to the independent plan fiduciary.
- Providing basic investment information that assists a plan in complying with reporting and disclosure requirements.
- Providing investment education that is limited to investment concepts (e.g., risk and return, diversification and dollar-cost averaging) and objective questionnaires, worksheets and interactive software.
- Selling investments to an Advice Recipient who has the requisite

investment background and who is properly informed that the broker is not undertaking to impartially advise the plan. This carve out generally only applies to larger retirement plans.

The Proposed 2015 Rule also provides a means by which an adviser who falls with the definition of a fiduciary may continue to receive conflict of interest compensation by satisfying certain safeguards and disclosure requirements.

Take Aways

The definition of a fiduciary under the 2015 Proposed Rule is quite broad and, if adopted, will certainly expand the number of advisers who are treated as adviser fiduciaries to retirement plans and IRAs. However, even if the 2015 Proposed Rule is not adopted, Advice Recipients should take this opportunity to review their relationship with their current investment adviser. If an adviser is not currently a fiduciary, but provides recommendations with respect to investments, consider asking the adviser whether he or she is able to be a fiduciary and whether changes will be required to the relationship if the rule is finalized. These questions may spark a helpful conversation that clarifies the adviser's role and informs the Advice Recipient of whether changes to the relationship may be required (even if the rule is not finalized).
