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Past is Prologue: DOL Proposes to Change the Definition of "Investment Advice"

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On November 3, 2023, the Department of Labor (DOL or Department) published in the Federal Register its proposed, *Retirement Security Rule: Definition of an Investment Advice Fiduciary* (2023 Proposal).[1] This is the Department's latest attempt to define more broadly the term "investment advice" for purposes of Section 3(21)(A)(ii) of the Employee Retirement Income Security Act of 1974, as amended (ERISA) and Section 4975(e)(3)(B) of the Internal Revenue Code of 1986, as amended (Code). Many recommendations that are not investment advice today would be investment advice pursuant to the 2023 Proposal if finalized in its current form.

The purposes of this article are to (1) summarize the DOL's 1975 regulation and other guidance defining investment advice, (2) provide an overview of the Department's 2016 investment advice regulation, which was vacated by a federal appellate court, (3) explain changes to the Department's interpretation of its 1975 regulation in Prohibited Transaction Exemption 2020-02, and (4) discuss the 2023 Proposal. Understanding the DOL's efforts prior to the 2023 Proposal informs us as to how the DOL arrived at the 2023 Proposal. Indeed, many of the interactions with ERISA-covered plans, individual retirement accounts and other accounts subject to ERISA or Section 4975 of the Code that would be investment advice under the 2023 Proposal would have been investment advice under the 2016 regulation had it not been vacated.

Definition of "Investment Advice," the Five-Part Test and Deseret Advisory Opinion

Both ERISA and the Code provide that a person is a fiduciary if he or she "renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so."[2] The definition of investment advice under ERISA applies to accounts the assets of which are subject to the fiduciary provisions under Section 404 of ERISA and the prohibited transaction provisions in Section 406 of ERISA (ERISA Accounts).[3] The definition of investment advice in Section 4975 of the Code applies to ERISA Accounts as well as other accounts not subject to ERISA, but subject to the prohibited transaction provisions in Section 4975 of the Code (Qualified Accounts, and with ERISA Accounts, Accounts).[4] Such Qualified Accounts include individual retirement accounts and annuities formed under Sections 408 and 408A of the Code (IRAs) and other tax preferred accounts defined as a "plan" in Section 4975.[5]

In 1975, the Department promulgated a regulation (1975 Regulation) in which it defined the term "investment advice." The 1975 Regulation provides that a person provides "investment advice" if he or she—

1. renders advice to an Account as to the value of securities or other property, or makes recommendations as to the advisability of investing in, purchasing, or selling securities or other property;
2. on a regular basis;
3. pursuant to a mutual understanding;
4. that such advice will be a primary basis for investment decisions; and that
5. the advice will be individualized to the plan.

This is commonly known as the "5-Part Test" for determining fiduciary status with respect to the provision of "investment advice."[6] A regulation under the Code provides for the same 5-Part Test.[7]

The 1975 regulation does not specifically address whether a recommendation to take a distribution from an ERISA-covered plan and roll it over to another plan, including an IRA, is "investment advice." In 2005, the DOL issued Advisory Opinion 2005-23A to Deseret Mutual Benefit Administrators (Deseret Letter) in which the DOL provided its interpretation of the 5-Part Test in respect of when a person provides investment advice in connection with taking a distribution from an ERISA-covered plan (Plan) and rolling over the distribution proceeds to an IRA.[8] The Department stated that an investment adviser who was not otherwise a fiduciary with regard to the Plan would not be deemed a fiduciary with respect to the Plan solely on the basis of making a rollover recommendation to a plan participant, even if the adviser gave specific advice as to how to invest the distributed funds. In reaching this conclusion, the DOL stated that such a recommendation did not meet prong one of the 5-Part Test; that is, the recommendation is not a recommendation as to the advisability of investing in, purchasing, or selling securities. On the other hand, the Department stated that where a Plan officer who is already a fiduciary to the plan responds to questions regarding a Plan distribution or the investment of amounts withdrawn from the Plan, such fiduciary would be exercising discretionary management over the Plan, thus resulting in fiduciary status.

2016 Final Regulation

On April 8, 2016, the Department promulgated a regulation (2016 Regulation) redefining the term "investment advice" for purposes of ERISA and the Code.[9] The 2016 Regulation would have replaced the 1975 Regulation and would have resulted in many more financial institutions and their financial professionals being fiduciaries for purposes of ERISA and the Code by reason of providing "investment advice." However, the Court of Appeals for the Fifth Circuit vacated the 2016 Regulations effective June 21, 2018.[10]

The 2016 Regulation identified the following categories of recommendations that give rise to fiduciary status under the Code by reason of providing investment advice:

1. A recommendation as to the advisability of acquiring, holding, disposing of, or exchanging, securities or other investment property;
2. A recommendation as to how securities or other investment property should be invested after the securities or other investment property are rolled over, transferred, or distributed from the plan or IRA;
3. A recommendation as to the management of securities or other investment property, including, among other things, recommendations on investment policies or strategies, portfolio composition, selection of other persons to provide investment advice or investment management services, selection of investment account arrangements (e.g., brokerage versus advisory); or
4. Recommendations with respect to rollovers, transfers, or distributions from a plan or IRA, including whether, in what amount, in what form, and to what destination such a rollover, transfer, or distribution should be made.[11]

In addition to providing Covered Advice, one of the following relationship conditions must have been present in order for a person to be deemed providing investment advice under the 2016 Regulation:

1. He or she represented or acknowledged that he or she is acting as a fiduciary within the meaning of ERISA or the Code;
2. He or she rendered the advice pursuant to a written or verbal agreement, arrangement, or understanding that the advice is based on the particular investment needs of the advice recipient; or
3. He or she directed the advice to a specific advice recipient or recipients regarding the advisability of a particular investment or management decision with respect to securities or other investment property of the IRA.[12]

The 2016 Regulation provided for a number of exceptions in which a person would not provide a recommendation and thus not provide "investment advice" for purposes of ERISA and the Code. These situations included the following:

Counterparty Exception. The 2016 Regulation provided that there would be no investment advice if the recommendation to a plan or IRA to enter into a sale, purchase, loan, exchange or other transaction related to the investment of securities or other investment property was made to a fiduciary that is independent of the party making the recommendation, such independent fiduciary had under its management or control total assets of at least $50 million, and certain other conditions were met.[13]

Investment Education Exception. The provision of certain categories of investment-related information and materials to a plan or IRA owner was not investment advice so long as "the information and materials do not include (standing alone or in combination with other materials) recommendations with respect to specific investment products or specific plan or IRA alternatives, or recommendations with respect to investment or management of a particular security or securities or other investment property."[14] The exception included (i) general plan information, (ii) general financial, investment, and retirement information, and (iii) asset allocation models and interactive investment materials that met certain requirements.

Platform Providers and Selection and Monitoring Assistance Exceptions. The 2016 Regulation provided that the provision of a platform of investment options to plans (not IRAs) and the provision of information about the investment options on the platform was not a recommendation of such investment options if certain disclosure requirements were met.[15]

General Communications. The furnishing or making available to plans, plan participants and beneficiaries, IRAs or IRA owners general communications that a reasonable person would not view as an investment recommendation. The 2016 Regulation provided examples of such communications including general circulation newsletters, commentary in publicly broadcast talk shows, remarks and presentations in widely attended speeches and conferences, research or news reports prepared for general distribution, general marketing materials, general market data, including data on market performance, market indices, or trading volumes, price quotes, performance reports, or prospectuses.[16]

The result of the 2016 Final Regulation, but for its vacatur, would have been a substantial broadening of the definition of "investment advice" such that recommendations by financial institutions and their employees and representatives would be subject to the fiduciary duty and prohibited transaction provisions

of ERISA and/or the prohibited transaction provisions of the Code. For example, recommendations by broker-dealers and their representatives of securities and investment programs, recommendations by advisers to move assets from an ERISA-covered plan to an IRA or from one IRA to another IRA so that the adviser may provide advisory services, recommendations by insurance agents of certain insurance products, and recommendations of CD IRAs by bank employees would have been investment advice. Furthermore, while the sale of advisory services would not by itself give rise to fiduciary status, the coupling of such sales activities with a recommendation would result in fiduciary status. However, as noted above, an appellate court vacated the 2016 Regulation on March 15, 2018.[17]

Prohibited Transaction Exemption 2020-02 and DOL's Revised Interpretation of the 5-Part Test

On December 18, 2020, the Department published Prohibited Transaction Exemption 2020-02, *Improving Investment Advice for Workers & Retirees* (PTE 2020-02).[18] In the preamble to PTE 2020-02, the DOL changed its view expressed in the Deseret Letter and provided information regarding how it interprets the 5-Part Test. The Department affirmed this position in a series of Frequently Asked Questions it issued in April of 2021 (FAQs).[19]

PTE 2020-02 states "…that the analysis in the Deseret Letter was incorrect…" and that "…[a] recommendation to roll assets out of a Title I Plan is necessarily a recommendation to liquidate or transfer the plan's property interest in the affected assets and the participant's associated property interest in plan investments."[20] Therefore, a rollover recommendation did fall within part one of the test. Assuming the other four parts of the 5-Part Test are met, a rollover or transfer recommendation would be investment advice under ERISA and the Code.

The Department also addressed in the preamble to PTE 2020-02 the other parts of the 5-Part Test. First, the Department addressed the "regular basis" requirement. The Department states "…that a single instance of advice to take a distribution from a Title I Plan and roll over the assets would fail to meet the regular basis prong. Likewise, sporadic interactions between a financial services professional and a Retirement Investor do not meet the regular basis prong."[21] In other words, for example, sales transactions involving a single recommendation would not meet the "regular basis" prong; rather, the recommendations must be "recurring, non-sporadic, and expected to continue."[22] Importantly, the Department went on to provide that "…advice to roll assets out of a Title I Plan into an IRA where the investment advice provider has not previously provided advice but will be regularly giving advice regarding the IRA in the course of a more lengthy financial relationship would be the start of an advice relationship that satisfies the regular basis prong."[23]

The Department in the preamble also interpreted the "mutual agreement" and "primary basis" prongs of the 5-Part Test. The Department stated it will look to the "the reasonable understanding of each of the parties" to determine whether there is a mutual agreement that the financial professional intends to make individualized recommendations that will be relied on by the investor as a primary basis for making investment decisions.[24] Finally, with regard to the "primary basis" prong, the Department stated that it "…does not intend to apply the five-part test to determine whether the advice serves as 'the' primary basis of investment decisions…but whether it serves as 'a' primary basis…"[25] The DOL goes on to provide that "[i]f…the parties reasonably understand that the advice is important to the Retirement Investor and could determine the outcome of the investor's decision, that is enough to satisfy the 'primary basis' requirement."[26]

The result of the DOL's revocation of the Desert Letter and interpretation of the "regular basis" prong in PTE 2020-02 is that more rollover and transfer recommendations became subject to ERISA or the Code, particularly when the person providing the recommendation provides ongoing advice.

However, such ongoing advice likely has to be in connection with an account subject to ERISA or Section 4975 of the Code in order to meet the "regular basis" requirement. Additionally, one-time recommendations and sporadic recommendations are not investment advice under the DOL's PTE 2020-02 interpretation.

The Department's interpretation of the 5-Part Test in PTE 2020-02 has been the subject of litigation. On February 2, 2022, the Federation of Americans for Consumer Choice (FACC) filed suit against the DOL in the US District Court for the Northern District of Texas seeking to declare that the DOL's interpretation exceeded the DOL's statutory jurisdiction, authority, or limitations and is arbitrary, capricious, and contrary to law.[27] A magistrate judge recommended that the court vacate the portions of PTE 2020-02 that provide a fiduciary's recommendation to take a distribution from an ERISA-covered plan and rollover to an IRA is the first recommendation of an ongoing advice relationship for purposes of the "regular basis" prong of the 5-Part Test.[28] In addition, the American Securities Association filed suit against the DOL in the US District Court for the Middle District of Florida for several of its positions in the DOL's FAQs.[29] Similar to the magistrate's recommendation in the *FACC* case, the court found that the DOL exceeded its authority vis-à-vis its position in FAQ 7 that a fiduciary's recommendation to take a distribution from an ERISA-covered plan and rollover to an IRA is the first recommendation of an ongoing advice relationship for purposes of the "regular basis" prong of the 5-Part Test.[30]

2023 Proposal Definition of "Investment Advice"

In issuing the 2023 Proposal, the Department recognized its interpretation of the 5-Part Test in PTE 2020-02 increased the number of situations in which financial institutions and financial professionals would provide investment advice, particularly with regard to rollovers.[31] The Department also recognized that in recent years other regulators have issued regulations or guidance intended to protect investors including the Securities and Exchange Commission's (SEC) Regulation Best Interest, the SEC Investment Adviser Interpretation and the NAIC Model Regulation adopted by a significant majority of state insurance regulators.[32] However, in the Department's view, it "as opposed to other regulators, remains uniquely positioned to create a regulatory definition of an investment advice fiduciary under ERISA that is uniformly applicable to all the types of investments that retirement investors make."[33] It noted "gaps" in the current regulatory regime including (1) Reg BI does not apply to recommendations to plans and plan fiduciaries, (2) the NAIC Model Regulation does not apply to recommendations "involving contracts used to fund retirement plan benefits covered by ERISA," and (3) the securities regulations do not cover certain types of plan and IRA investments such as "…real estate, fixed indexed annuities, certificates of deposit, and other bank products…"[34] The Department also states that it has the authority to issue a regulation defining "investment advice" for purposes of ERIA and the Code.[35]

In the 2023 Proposal, the Department provides that a financial intuition, financial professional or other "person"[36] will provide "investment advice" for purposes of ERISA and the Code if such person "for fee or other compensation, direct or indirect" does the following:

1. Makes "a recommendation of any securities transaction or other investment transaction or any investment strategy involving securities or other investment property";
2. Makes such recommendation with respect to moneys or other property of an Account;
3. Makes the recommendation to the plan, a plan fiduciary, a plan participant or beneficiary, an IRA, an IRA owner or beneficiary or IRA fiduciary (Retirement Investor); and
4. Makes the recommendations under one of three circumstances or "contexts."[37]

The "contexts" to which the Department refers include the following:

1. The person "either directly or indirectly (for example, through or together with any affiliate) has discretionary authority or control…with respect to purchasing or selling securities or other investment property for the…" Retirement Investor;
2. The person "either directly or indirectly (for example, through or together with any affiliate) makes investment recommendations to investors on a regular basis as part of their business and the recommendation is provided under circumstances indicating that the recommendation is based on the particular needs or individual circumstances of the retirement investor and may be relied upon by the retirement investor as a basis for investment decisions that are in the retirement investor's best interest"; or,
3. The person "…represents or acknowledges that they are acting as a fiduciary when making investment recommendations."[38]

These "contexts" establish a relationship between a person and a retirement investor that are, in the DOL's view, sufficient to establish a fiduciary relationship under ERISA and the Code when the person makes a recommendation described in the 2023 Proposal.

The 2023 Proposal broadly defines the term "recommendation of any securities transaction or other investment transaction or any investment strategy involving securities or other investment property" broadly to include, among other things, (1) a recommendation as to the "advisability of acquiring, holding, disposing of, or exchanging, securities or other investment property," (2) a recommendation as to investment strategy, (3) a recommendation "as to how securities or other investment property should be invested after the securities or other investment property are rolled over, transferred, or distributed from the plan or IRA," (4) recommendations "as to the management of securities or other investment property (such as, "investment policies or strategies," "selection of other persons to provide investment advice or investment management services," and "selection of investment account arrangements"), and (5) recommendations regarding "rolling over, transferring, or distributing assets from a plan or IRA," which include "recommendations as to whether to engage in the transaction, the amount, the form, and the destination of such a rollover, transfer, or distribution."[39]

There are several notable aspects of the proposed definition of "investment advice." The above-described relationship conditions, particularly the second condition, mark a substantial departure from current law in respect of the current "regular basis" requirement. The 2023 Proposal provides that a person who makes recommendations to a Retirement Investor need only make recommendations "on a regular basis as part of their business," but current law requires that the "regular basis" prong of the 5-Part Test apply to each investor separately. Thus, under the current regulation, the person may make ongoing recommendations to some investors, but not others, and the person is only a fiduciary with regard to the persons to which recommendations are made. On the other hand, the 2023 Proposal would result in advice fiduciary status with regard to all of a person's investor clients (or, possibly, even some prospective investor clients) so long as the person provides investment advice to just some of its investor clients. Note that the 2023 Proposal appears to state that the "in the business of" requirement applies to all of the person's investor clients not just Retirement Investors. This relationship requirement would, among other things, result in one-time or sporadic recommendations, including those made in the context of a sales transaction, to be investment advice. This was the same result under the 2016 Regulation.

In addition to the "in the business of" requirement, the recommendation to a Retirement Investor must be "based on the particular needs or individual circumstances of the retirement investor" and "under circumstances that would suggest to the retirement

investor that the person makes the recommendation in the retirement investor's best interest." The "particular needs and individual circumstances" maintains, to some extent, the "individualized" prong in the current 5-Part Test. Suitability and similar determinations required under laws other than ERISA and the Code may, in the Department's view, result in an "individualized" determination because the Department appears to believe that presenting an investment or investment course of action as "appropriate" for a Retirement Investor is sufficient. For example, the Department states that providing a list of securities to a participant as "appropriate" to an investor's needs is a recommendation even if the person does not recommend a particular security on the list.[40] The Department intends that whether the Retirement Investor "may" view the recommendation as in its best interest is an objective test and based on the facts and circumstances. Delivery of disclosures stating that the person will act in the best interest (for example, Form CRS, Reg BI disclosure) or marketing materials stating the person acts in the best interest (or, possibly, acts as a trusted adviser) may meet the requirements of this relationship test.

The other two relationships that could result in advice fiduciary status are less nuanced, but equally important. If a person makes a recommendation as described above and that person, or its affiliate, provides discretionary asset management services, then the person provides investment advice. The premise behind this provision is that a Retirement Investor will logically assume that a recommendation would be made on a fiduciary basis if the person already provides discretionary asset management services and thus any such recommendation should be made in accordance with a fiduciary standard of conduct.[41] However, it is important to note that the proposed regulatory language states that an affiliate's provision of the discretionary asset management services is sufficient to make the provision of the recommendation a fiduciary. This could result in situations where, for example, an affiliate manages the assets of a collective investment trust the assets of which are plan assets for purposes of ERISA and thus recommendations made by a person at another affiliate could be investment advice under this provision. The 1975 Regulation includes a similar provision, but financial services companies and their advisers had not paid a great deal of attention to it until the 2016 Regulation.

Additionally, if the person providing a recommendation states that he acts as a fiduciary or otherwise acknowledges fiduciary status, any recommendation would be fiduciary investment advice. The person need not specifically refer to ERISA or the Code in making a representation a fiduciary representation or acknowledgment. Additionally, such representations and acknowledgments need not be made in writing.[42] Specific statements disclaiming fiduciary status are permissible and may be helpful, but the Department states in the proposed regulatory language that such disclaimers "will not control to the extent they are inconsistent with the person's oral communications, marketing materials, applicable State or Federal law, or other interactions with the retirement investor."[43]

2023 Proposal-Investment Advice Exceptions

Conspicuously absent from the 2023 Proposal's regulatory language are specific carve outs or exceptions like those found in the 2016 Regulation. Rather, in the preamble, the DOL refers to several situations in which the language in the proposed regulation, particularly the relationship conditions, can be interpreted to exclude some conduct from the definition of investment advice.

The DOL states in the preamble that its longstanding guidance, Interpretive Bulletin 96-1 (I.B. 96-1), related to investment education would not be affected by the 2023 Proposal.[44] I.B. 96-1 provides safe harbors whereby a person can provide certain information about investments, plans, and IRAs, which will be viewed as investment education rather than investment advice and thus not be fiduciary advice for purposes of ERISA and the

Code. In effect, the I.B. 96-1 establishes how certain information can be provided without making a recommendation.

While there is no proposed regulatory language establishing a platform exception, the DOL states in the preamble that the offering of a platform of investments by a person would not necessarily result in the provision of investment advice.[45] In its view, whether the person provides investment advice will turn on whether the person makes a recommendation. A platform provider will likely provide a recommendation if the provider "presents the investments on the platform as having been selected for and appropriate for the investor (that is, the plan and its participants and beneficiaries)."[46] On the other hand, a platform provider does not provide a recommendation if it "merely identif[ies] investment alternatives using objective third-party criteria (for example, expense ratios, fund size, or asset type specified by the plan fiduciary) to assist in selecting and monitoring investment alternatives, without additional screening or recommendations based on the interests of plan or IRA investors…"[47] The DOL states a similar analysis would apply to pooled employer plans.[48]

The Department also states in the preamble that "wholesaling" of financial products by the financial institution that manufactures the product through an intermediary will not typically result in the provision of investment advice.[49] This would be the case "because they would not involve recommendations based on the particular needs or individual circumstances of the plan or IRA" as set forth in the relationship requirement of the proposed investment advice definition.[50] The Department made similar comments in this regard to the 2016 Regulation. In 2016, some wholesalers considered that they could be engaged in discussions with the Retirement Investor and thought such discussions could give rise to advice fiduciary status. That too could be an issue under the 2023 Proposal.

The Department also states that individuals like "human resource professionals discussing 401(k) investment options, and the car salesman who recommends a retiree cash in their 401(k) for a new convertible are not caught up in the definition."[51] Again, there are no specific exceptions stated in the proposed regulatory text, but the Department suggests such recommendations would not meet the relationship condition because human resource professionals and car dealerships are not "in the business of" providing investment advice.[52]

The 2023 Proposal does not provide for an exception for sophisticated investors. The DOL reiterated its position expressed in the 2016 Regulation that it does not equate investment sophistication with a larger amount of assets under management. Therefore, it refused to create an exception for recommendations made to investors that meet certain thresholds, for example, qualified purchasers, or qualified institutional buyers.[53] Additionally, unlike the 2016 Regulation that included a counterparty exception, the Department did not specifically address in the 2023 Proposal a situation in which an Account is represented by an independent and appropriately qualified investment professional such as a registered investment adviser with a certain amount of assets under management. The absence of a specific exemption will require a person who makes a recommendation to consider whether it may take the position that even if a person makes a recommendation to a third-party adviser, such recommendation would not be advice because the relationship condition did not apply. For example, the recommendation would not be investment advice because, arguably, the adviser representing the Retirement Investor should know that the person providing the recommendation is only selling its product or services and does not act in the retirement investor's best interest in doing so.

In both the 2016 Regulation and the 2023 Proposal, the DOL stated that a person would not be a fiduciary merely for marketing itself to provide investment advice or investment management services. This has come to be known as the "hire me" exception. However, the DOL cautions in

the preamble to the 2023 Proposal, as it did in the preamble to the 2016 Regulation, that "[t]here is a line between an investment advice provider making claims as to the value of its own advisory or investment management services in marketing materials, on the one hand, and making recommendations to retirement investors on how to invest or manage their savings, on the other."[54] Therefore, a person's touting his or her abilities as an investment adviser, broker or other financial professional would not be advice, but any recommendation with regard to how the person would invest the Account assets made at the time of the sales conversation would be investment advice. In practice, a person usually includes investment recommendations in sales conversations because making such recommendations is often necessary to convince the Retirement Investor to hire the person. Thus, the "hire me" exception as expressed in the 2023 Proposal is of little practical value to many.

Clearly, the Department took a different tact in the 2023 Proposal. Rather than creating specific exceptions to the term "investment advice," the DOL provides that financial institutions and other providers to Retirement Investors should look to the regulatory language and preamble language to identify possible exceptions. This can be favorable to providers because they may have more flexibility in crafting exceptions. On the other hand, the lack of explicit regulatory exceptions leaves providers open to legal challenges by the DOL or a court.

DOL Proposed Changes to Prohibited Transaction Exemptions

The primary purpose of this article is to explain the Department's proposed definition of investment advice. However, readers should be aware that the DOL also proposed on November 3, 2023 substantial changes to current prohibited transactions on which advice providers currently rely. The common underlying theme of the proposed amendments is to require fiduciary advice providers to address fiduciary conflicts described in Section 406(b) of ERISA and Section 4975(d) of the Code through the use of PTE 2020-02, rather than other, long-standing prohibited transaction exemptions. The conditions with which fiduciaries must comply to rely on PTE 2020-02 are more substantial than those found in these other exemptions.

Prohibited Transaction Exemption 84-24 (PTE 84-24), in part, provides an exemption for fiduciary conflicts that arise when insurance companies, agents and brokers recommend that the assets of an Account be used to purchase insurance (for example, variable annuities, fixed annuities, fixed indexed annuities, and life insurance).[55] The Department proposes to amend PTE 84-24 so that only a limited group, called "Independent Producers," may rely on the exemption for this purpose.[56] Additionally, the DOL proposes to amend the exemption to include many of the conditions found in PTE 2020-02 including a "Best Interest" standard of conduct, which will apply to such Independent Producers.[57] All other sellers of insurance that provide investment advice as defined in the 2023 Proposal will have to rely on PTE 2020-02.

Additionally, PTE 84-24 and Prohibited Transaction Exemption 77-4 (PTE 77-4)[58] currently exempt fiduciary prohibited transactions that arise when a fiduciary advice provider recommends mutual funds that are underwritten by affiliates or are advised by the advice provider or its affiliate, respectively. The Department proposes to amend the exemptions so that they may no longer be used for this purpose although they are still available to exempt other prohibited transactions not relevant here.[59] Fiduciary advice providers would have to rely on PTE 2020-02.

Prohibited Transaction Exemption 86-128 (PTE 86-128) currently exempts fiduciaries from prohibited transactions that arise when their investment advice results in the receipt of commissions.[60] The DOL proposes to amend PTE 86-128 so that the advice provider could no longer rely on PTE 86-128 with respect to IRAs and thus must rely on PTE 2020-02.[61]

Impact on Providers

If the Department issues a final regulation that defines "investment advice" in the manner described in the 2023 Proposal, a large number of persons will provide investment advice and those persons who already provide investment advice under current law will likely provide advice in more circumstances. The following are some situations in which a fiduciary advice relationship might arise:

- The recommendation to take a distribution from an Account (and the form of distribution) could be investment advice in all circumstances, not just when a recommendation is made to rollover or transfer to an IRA so that advice might be provided on an ongoing basis. Thus, for example, a recommendation by an insurance agent to take a distribution so the Retirement Investor can purchase life insurance outside of an Account could be investment advice.
- One-time or sporadic recommendations to purchase securities or other investment property with the assets of an Account could be investment advice. For example, a broker-dealer's one-time sale of securities to an Account, even an Account owned by a sophisticated counterparty, could be investment advice. Thus, a broker-dealer's capital markets group may provide investment advice in addition to the retail group. Additionally, a solicitor's recommendation of an investment manager or unregistered fund to a Retirement Investor could be investment advice.
- The sale by an asset manager of its investment management services could be investment advice if accompanied by a recommendation regarding how the manager will manage the assets once the Retirement Investor hires the manager. Also, an asset manager's recommendation of one or more funds (registered or unregistered) managed by it as the means to provide such management services could be investment advice.
- Recommendations to purchase insurance products with Account assets, even if only a one-time recommendation, could be investment advice.
- One-time recommendations by retail bankers to purchase IRA CDs and recommendations by such bankers to take distributions from ERISA Accounts and IRAs and rollover or transfer to an IRA CD likely will be investment advice.

Reaction to the 2023 Proposal

Much as with the 2016 Regulation, the financial services industry and others who work with Retirement Investors reacted strongly to the 2023 Proposal. The Department held online hearings on December 12 and December 13, 2023 at which approximately 40 witnesses testified. Many of those witnesses challenged the 2023 Proposal as too broad, unnecessary in light of other regulatory efforts by different agencies, contrary to the Fifth Circuit's decision vacating the 2016 Regulation, and for other reasons. However, some witnesses believed the DOL's rule is necessary to protect investors and to fill in gaps left by other regulatory regimes.[62] Additionally, the DOL requested written public comments and received approximately 500 comments on the proposed definition of investment advice (and hundreds more on the proposed changes to the prohibited transaction exemptions). Many of those comments reflected dissatisfaction with the 2023 Proposal and the DOL's attempt to once again change the definition of investment advice.

Members of Congress have also expressed concerns with the 2023 Proposal. On January 10, 2024, the House Financial Services Subcommittee on Capital Markets held a hearing entitled, "Examining the DOL Fiduciary Rule: Implications for Retirement Savings and Access." The Subcommittee heard from several witnesses, many of which disapproved of the DOL's proposed rulemaking. A letter signed by some members of the Subcommittee, both Republicans and Democrats, addressed to the Acting Assistant Secretary of Labor expressed concerns with the regulation.[63] Congress has some options with regard to the 2023 Proposal including passing legislation eliminating the DOL's ability to use its budget

to implement or enforce the rule or a Congressional Review Act (CRA) challenge.[64] President Biden, so long as he is in office, would likely veto any such legislation.

Possible Legal Challenges

The Department's 2023 Proposal, if finalized, will result in legal challenges by financial industry participants and other constituencies. As discussed above, the US Chamber of Commerce convinced the Fifth Circuit to vacate the 2016 Regulation. Additionally, a case challenging the DOL's interpretation of the 5-Part Test in the preamble to PTE 2020-02 is pending in the District Court for the Northern District of Texas. Separately, the District Court for the Middle District of Florida vacated, the Department's interpretation of the 5-Part Test reflected in Frequently Asked Question guidance issued by the Department. Given this litigation history (and the views expressed in the above-discussed hearing testimony and comment letters), the DOL will be sued once it promulgates a final regulation that is substantially similar to the 2023 Proposal.

The question then becomes whether the DOL would win a legal challenge to a final regulation, particularly if such case would be heard by the Fifth Circuit on appeal. The Department recognizes, throughout the 2023 Proposal's preamble, the Fifth Circuit's decision, particularly the court's position that there should be a relationship of "trust and confidence" in order for fiduciary duties to apply.[65] The Department believes that it has made enough changes from the 2016 Regulation to the 2023 Proposal to address the issues raised by the Fifth Circuit. It states in the preamble, "The Department's proposal is also intended to be responsive to the Fifth Circuit's emphasis on relationships of trust and confidence. The current proposal is much more narrowly tailored than the 2016 Final Rule…the proposal provides that fiduciary status would attach only if compensated recommendations are made in certain specified contexts, each of which describes circumstances in which the retirement investor can reasonably place their trust and confidence in the advice provider."[66] However, that position is questionable as indicated by the above-discussed hearing testimony and comment letters. Additionally, in effect, many of the activities that would have been investment advice under the 2016 Regulation would be investment advice under a final regulation consistent with the 2023 Proposal notwithstanding the DOL's changes to the proposed regulatory language.

Conclusion

In conclusion, the Department believes that the 5-Part Test, its interpretation of the 5-Part Test in PTE 2020-02, and other regulators' efforts are not sufficient to protect the interests of Retirement Investors. Therefore, the Department has again proposed a regulation that will change the definition of "investment advice" for purposes of ERISA and Section 4975 of the Code. If the DOL finalizes the 2023 Proposal as currently stated, more financial institutions, their employees and representatives, and other persons will be fiduciaries by reason of providing investment advice or will be advice fiduciaries to a greater extent than they already are under current law. The DOL will be inclined to issue a final regulation as early in 2024 as possible in order to limit the likelihood of a successful challenge of the regulation under the CRA. Undoubtedly, the final regulation will be challenged in a lawsuit, but the outcome of that suit may not be known for a year or two. Thus, financial services companies may have to deal with a final regulation in the interim unless a change in Administration and DOL leadership causes a different result.

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NOTES

1 88 Fed. Reg. 75890 (Nov. 3, 2023).

2 ERISA § 3(21)(A)(ii); I.R.C. § 4975(e)(3)(B).

3 ERISA § 4.

4 I.R.C. §§ 4975(c)(1), 4975(e)(1).
5 *Id*.
6 29 C.F.R. § 2510-3.21(c), 40 Fed. Reg. 50842 (Oct. 31, 1975).
7 26 C.F.R. §54.4975-9(c), 40 Fed. Reg. 508640 (Oct. 31, 1975).
8 DOL Adv. Op. 2005-23A (Dec. 7, 2005).
9 Definition of the Term "Fiduciary"; Conflict of Interest Rule—Retirement Investment Advice, 81 Fed. Reg. 20946 (April 8, 2016).
10 Chamber of Commerce of the U.S. v. U.S. Dept. of Labor, 885 F.3d 360 (5th Cir. 2018)
11 29 C.F.R. § 2510.3-21(a)(1)(i) & (ii).
12 29 C.F.R. § 2510.3-21(a)(2).
13 29 C.F.R. § 2510.3-21(c).
14 29 C.F.R. § 2510.3-21(b)(2)(iv).
15 29 C.F.R. § 2510.3-21(b)(2)(i) & (ii).
16 29 C.F.R. § 2510.3-21(b)(2)(iii).
17 Chamber of Commerce, 885 F.3d at 360.
18 85 Fed. Reg. 82798 (Dec. 18, 2020).
19 New Fiduciary Advice Exemption: PTE 2020-02 Improving Investment Advice for Workers & Retirees Frequently Asked Questions, *https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/faqs/new-fiduciary-advice-exemption*.
20 85 Fed. Reg. at 82803.
21 85 Fed. Reg. at 82805.
22 *Id*.
23 *Id*.
24 *Id*. at 82805-82806.
25 *Id*. at 82806.
26 *Id*. at 82808.
27 Compl., Fed'n of Ams. for Consumer Choice v. U.S. Dep't of Labor, No. 3:22–CV–00243–K–BT.
28 Findings, Conclusions, and Recommendations of the United States Magistrate Judge, Fed'n of Ams. for Consumer Choice v. U.S. Dep't of Labor, No. 3:22–CV–00243–K–BT, 2023 WL 5682411, at *27–29 (N.D. Tex. June 30, 2023).
29 Compl., Am. Sec. Ass'n. v. U.S. Dep't of Labor, No. 8:22–CV–330VMC–CPT, 2023 WL 1967573 (M.D. Fla. Feb. 13, 2023).
30 Am. Sec. Ass'n. v. U.S. Dep't of Labor, 2023 WL 1967573, at * 22–23.
31 *Retirement Security Rule*, 88 Red. Reg. at 75896.
32 88 Fed. Reg. at 75896-75897.
33 *Id*. at 75900.
34 *Id*.
35 *Id*.
36 Section 3(9) of ERISA defines a "person" as an "individual, partnership, joint venture, corporation, mutual company, joint-stock company, trust, estate, unincorporated organization, association, or employee organization."
37 88 Fed. Reg. at 75977 (as proposed, 29 C.F.R. § 2510.3-21(c)(1)).
38 *Id*. (as proposed, 29 C.F.R. § 2510.3-21(c)(1)(i)-(iii)).
39 *Id*. at 75978 (as proposed, 29 C.F.R. § 2510.3-21(f)(10)).
40 *Id*. at 75904.
41 *Id*. at 75901.
42 *Id*. at 75903.
43 *Id*. at 75977 (as proposed, 29 C.F.R. § 2510.3-21(c)(1)(v)).
44 *Id*. at 75911.
45 *Id*. at 75907.
46 *Id*. at 75908.
47 *Id*.
48 *Id*.
49 *Id*. at 75907.
50 *Id*.
51 *Id*. at 75961.
52 *Id*.
53 *Id*. at 75907.
54 *Id*. at 75906.
55 49 Fed. Reg. 13208 (Apr. 3, 1984).
56 Proposed Amendment to Prohibited Transaction Exemption 84–24, 88 Fed. Reg. 76004 (Nov. 3, 2023).
57 *Id*. at 76009.
58 42 Fed. Reg. 18732 (Apr. 8, 1977).
59 Proposed PTE 84-24, 88 Fed. Reg. at 76005-6; Proposed Amendment to Prohibited Transaction

Exemptions 75–1, 77–4, 80–83, 83–1, and 86–128, 88 Fed. Reg. 76032, 76044 (Nov. 3, 2023).

60 51 FR 41686 (November 18, 1986), as amended at 67 FR 64137 (October 17, 2002).

61 88 Fed. Reg. at 76035.

62 Department of Labor, Employee Benefit Security Administration, December 12, 2023, Hearing Transcript, *https://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/public-comments/1210-AC02/hearing-transcript-day-1.pdf*; Department of Labor, Employee Benefit Security Administration, December 13, 2023, Hearing Transcript, *https://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/public-comments/1210-AC02/hearing-transcript-day-2.pdf*.

63 *https://hill.house.gov/news/documentsingle.aspx?DocumentID=9239*.

64 35 U.S.C. § 801, *et. seq*.

65 85 Fed. Reg. at 75895.

66 *Id*. at 75901.