Dechert LLP

The Brave New Fiduciary World Has Arrived – The DOL Tries to Find a More Ideal Balance in the Final "Investment Advice" Rules

A legal update from Dechert's Employee Benefits and Executive Compensation and Financial Services Groups

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I. Introduction

The U.S. Department of Labor (the "DOL") on April 6, 2016 released the final version of its "investment advice" regulation and accompanying prohibited transaction exemptions (collectively, the "Final Rule"), a highly-anticipated milestone that is the culmination of a long and arduous process to adopt new rules relating to the definition of "fiduciary" under the Employee Retirement Income Security Act of 1974 ("ERISA") and the Internal Revenue Code of 1986 (the "Code"). The Final Rule covers not only retirement plans subject to ERISA, but, controversially, also individual retirement accounts ("IRAs")[1] and other non-ERISA plans.

The road to finalization was a long and winding one. In October 2010, the DOL issued a proposed rule (the "2010 Proposal"), which, in a highly unusual step, was withdrawn after intense criticism from a wide variety of sources. In April 2015, the DOL issued a re-proposed rule (the "2015 Proposal"), on which the DOL received thousands of comment letters.[2]

Contrary to industry expectations that the 2015 Proposal would remain relatively unchanged, the Final Rule contained substantial and significant alterations. With the issuance of the Final Rule, it appears that the DOL was indeed responsive to a number of concerns expressed by the market, although it is nevertheless expected to bring significant changes to the retirement investing industry.

The package of materials released in April 2016 consists of final versions of:

- The amended regulation that sets forth the rules for determining who is a "fiduciary" by reason of providing investment advice;
- A prohibited-transaction class exemption (a "PTE") known as the "Best Interest Contract" Exemption (the "BIC Exemption"), which is a new principles-based PTE for certain retirement advisers;
- A new PTE for "principal" transactions (the "Principal Transaction Class Exemption"); and
- Amendments to a number of existing PTEs.

On the day that the Final Rule was issued, Dechert published a high-level overview of the Final Rule discussing certain aspects in the Final Rule that were likely to be perceived as improvements over the 2015 Proposal. This OnPoint provides a more in-depth discussion of: (i) the definition of "fiduciary" under ERISA, (ii) the history of the developments that led up to the Final Rule, (iii) the amended regulation included with the Final Rule, (iv) the BIC Exemption, (v) the Principal Transaction Class Exemption and various existing PTEs that were amended in conjunction with the issuance of the Final Rule, (vi) the possible indirect impact of the Final Rule on non-fiduciary

[1] References to individual retirement accounts in the Final Rule generally encompass health savings accounts, Archer savings accounts and Coverdell education savings accounts.

[2] *See* Dechert OnPoint, The DOL Seeks an Ideal Balance in a Brave New World of "Investment Advice" Under ERISA (April 2015).

entities that may transact business with newly-minted fiduciaries, (vii) the potential application of the Final Rule to broker-dealers and (viii) the effective date of the Final Rule and certain grandfathering relief.

II. Executive Summary

The Final Rule is arguably the most significant change to the fiduciary rules governing retirement plans since ERISA was enacted, and it has the potential to disrupt many trends and practices by which financial products are currently marketed and sold to retirement investors. While the Final Rule is in many contexts daunting, the DOL's changes over the course of the regulatory process are responsive to a number of concerns expressed by the market.

The Final Rule expands dramatically the scope of who is a fiduciary in connection with retirement accounts. The basic structure of the Final Rule is to (i) establish the general principles under which one might be considered a fiduciary, (ii) set forth certain express clarifications under which fiduciary status expressly does not arise, (iii) provide exceptions under which certain parties that would otherwise be fiduciaries will not be considered fiduciaries and (iv) provide exemptions under which a fiduciary may proceed without engaging in a non-exempt prohibited transaction.

"Recommendations"

The threshold inquiry for determining fiduciary status under the Final Rule is whether a non-discretionary adviser is making a "recommendation." If the adviser gives non-discretionary advice that does not rise to the level of a "recommendation" within the meaning of the Final Rule, then the adviser will not be considered a fiduciary solely by reason of providing such advice. The Final Rule excludes certain types of communications and activities from the definition of "recommendation." In summary, the Final Rule clarifies that merely providing a platform of investment alternatives, investment education and/or marketing communications does not necessarily constitute a recommendation.

Certain Excluded Activities

Even if a particular set of facts indicates the existence of a covered recommendation, it does not necessarily follow that the person giving such recommendation is a fiduciary. In this regard, the Final Rule provides that certain activities will not, without more, cause a person to be treated as a fiduciary if certain conditions are satisfied, unless such person acknowledges fiduciary status with respect to that particular activity.

"Best Interest Contract" Exemption

In expanding ERISA's definition of "fiduciary," and thereby applying ERISA's fiduciary standards to parties that provide investment advice to retail investors, the DOL was faced with the challenge of designing rules that would accommodate a range of business arrangements and compensation practices (particularly in the context of the retail investment market), many of which would otherwise be characterized as prohibited transactions. The BIC Exemption is the primary mechanism by which the DOL seeks to protect retirement investors from conflicts of interest, while simultaneously allowing flexibility to permit compensation structures that are prevalent in the retail investment market. Where its conditions are met, the BIC Exemption generally provides relief so that "investment advice" fiduciaries may receive certain types of compensation that would otherwise be prohibited (i.e., commissions, sales loads, 12b-1 fees and revenue sharing payments).

While the requirements of the BIC Exemption may not always be palatable, financial services providers will hopefully be able to work through the requirements in a variety of situations. We note, however, that, even in cases in which

complying with the BIC Exemption is feasible, the provider should first get comfortable with a new fiduciary-based liability profile (either under ERISA, for ERISA clients, or under the "best interest" contract, for IRAs and other non-ERISA plans).

At the core of the BIC Exemption are the "Impartial Conduct Standards," which apply to all advisers and financial institutions providing advice to retirement investors. In the case of IRAs and other non-ERISA plans, the financial institution must generally enter into a contract giving rise to quasi-ERISA responsibilities of prudence and loyalty.

Widespread Impact

The impact of the Final Rule does not stop with those directly affected as a result of new-found fiduciary status. There is an important impact on certain market participants who themselves might not be fiduciaries, but whose business will be affected by those who are – notably, registered investment companies ("funds") and their sponsors. The Final Rule could significantly impact funds' intermediary-distribution channels, and may therefore lead to changes in demand for certain types of funds, share classes and intermediary-compensation arrangements. How intermediaries ultimately react to the Final Rule, and whether they react consistently, remains to be seen. Nevertheless, fund managers and underwriters must now interact and coexist with parties that will be fiduciaries and thus need to consider how their products and services can be adapted to meet the needs of their fiduciary counterparties.

Effective Date; Grandfather Relief

As described in Section IX, the Final Rule is initially effective on June 7, 2016, although with staged applicability over time, with grandfather relief for certain additional compensation based on investments that were made prior to the Final Rule's applicability date.

III. Background

A. *Statutory Definition of "Investment Advice" Fiduciary*

A person is an "investment advice" fiduciary to an employee benefit plan subject to ERISA or to an IRA or certain other non-ERISA plans if the person renders investment advice for a fee or other compensation (direct or indirect) with respect to any moneys or other property of a plan, or has any authority or responsibility to do so. The Final Rule directly impacts the fiduciary status of individuals and entities that provide non-discretionary advice (as opposed to investment managers and other discretionary advisers, who under the current rules, generally already are fiduciaries) and the times at which they may become fiduciaries.

Being an ERISA fiduciary implicates two critical sets of statutory requirements. First, an ERISA fiduciary is subject to general fiduciary duties, including duties of prudence and loyalty, which have been referred to as the "highest known to the law."[3] These general duties currently apply with respect to ERISA plans, but not with respect to IRAs and non-ERISA plans. Second, the "prohibited transaction" provisions of ERISA and Section 4975 of the Code, which include a number of self-dealing and other conflict-of-interest prohibitions, will apply so as to prohibit certain conduct (unless an exemption applies). The prohibited-transaction rules apply to ERISA plans, IRAs and a number of other non-ERISA plans.

[3] *E.g.*, *Donovon v. Bierwirth*, 680 F.2d 263, 271 n.8 (2d. Cir.) (citation omitted), *cert. denied*, 459 U.S. 1069 (1982).

Thus, for those considering acting in a fiduciary capacity, at least two general considerations arise: (i) the potential fiduciary will need to be comfortable that its anticipated conduct will not constitute or involve a non-exempt prohibited transaction, and (ii) the potential fiduciary should understand and be comfortable with the liability profile associated with being subject to ERISA's general fiduciary standards, including those of prudence and loyalty.

B. *History of "Investment Advice" Rulemaking Efforts*

1. The 1975 Regulation

The original "investment advice" regulations were promulgated in 1975 shortly after ERISA's enactment (the "1975 Regulation"). The 1975 Regulation set forth a five-part test for determining when a person would be treated as rendering "investment advice" for a fee and thus acting as a fiduciary. Under the 1975 Regulation, advice did not constitute "investment advice" that would make a person a fiduciary unless the person:

(i) rendered advice as to the value of securities or other property, or made recommendations as to the advisability of investing in, purchasing or selling securities or other property,

(ii) on a regular basis,

(iii) pursuant to a mutual agreement, arrangement or understanding with the plan or a plan fiduciary that

(iv) the advice would serve as a primary basis for investment decisions with respect to plan assets and that

(v) the advice would be individualized based on the particular needs of the plan.

The 1975 Regulation seemed to reflect a desire by the DOL to strike a balance between labeling certain non-discretionary advisers as fiduciaries, while at the same time not unduly discouraging the provision of services by desirable providers or putting unnecessary upward pressure on pricing.

2. Proposals Leading Up to the Final Rule

Since 1975, the retirement market has undergone a dramatic shift from primarily defined benefit plans, which generally are professionally managed, to "401(k)" and other defined contribution plans and IRAs, where participants (and beneficiaries), who may not be financially sophisticated, often make the investment decisions. Over this period, the variety and complexity of financial products available to the retirement market also increased significantly. However, despite these significant developments, the "investment advice" rules under ERISA had not been meaningfully revised since they were first issued in 1975.

The DOL has made clear its view that the rigidity of the 1975 Regulation has hampered ERISA from protecting retirement assets as intended. Out of concern that the 1975 Regulation might not adequately protect individual retirement investors in a changed world, the DOL began to focus on finding a new approach. The 2010 Proposal, the first comprehensive proposal to amend the 1975 Regulation, was issued in October 2010, and would have expanded significantly the scope of who might be considered an ERISA fiduciary.

The 2010 Proposal aimed to recast the 1975 Regulation primarily by broadly expanding the types of and circumstances surrounding non-discretionary advice that would cause advice to constitute fiduciary "investment advice." Under the 2010 Proposal, an adviser could have become a fiduciary even without a "mutual" agreement

between the adviser and the retirement investor regarding the purpose of the advice and even if the advice did not serve as "a primary basis" for the investor's investment decisions.

Following significant concern and comments from the market, in September 2011 the DOL took the unusual step of announcing the withdrawal of the 2010 Proposal, although with an express intention to re-propose the rules at a later date. Eventually, in April 2015, with direct and public support from the President himself, the DOL issued new proposed rules that incorporated a number of changes intended to address industry concerns.

The President expressed concerns not only about conflicted advice generally, but also specifically about efforts by financial professionals to influence participants in employer-sponsored plans with respect to a decision as to whether to roll over retirement assets into IRAs. Regarding rollovers, certain DOL personnel have expressed great skepticism whether it generally is better for participants to be in individual retirement arrangements, such as IRAs, rather than being covered under employer-sponsored plans, which tend to have both economies of scale and at least some degree of fiduciary management.

The 2015 Proposal, like the 2010 Proposal, was highly focused on protecting retail investors, including IRA investors.[4] The DOL's approach was to use its authority over interpreting the Code's prohibited-transaction provisions to bring IRA providers potentially under the fiduciary tent.[5] Under the proposed BIC Exemption, the DOL's approach was to allow the provider to extricate itself from potential excise taxes by contractually agreeing to be subject to fiduciary duties very similar to ERISA's. Thus, the DOL was endeavoring to cause IRAs, which Congress has specifically excluded from the reach of ERISA's protection, to receive the benefits of ERISA-like safeguards.

IV. The Final Rule

A. *Overview*

The Final Rule is arguably the most significant change to the fiduciary rules governing retirement plans since ERISA was enacted,[6] and it has the potential to disrupt many current trends and market practices pursuant to which financial products are marketed and sold to retirement investors.[7] In redefining what communications constitute investment advice and what types of relationships are "fiduciary" in nature, the Final Rule attempts to achieve the DOL's goal of expanding certain of ERISA's protections generally to cover IRAs and other non-ERISA plans. Although IRAs and

[4] The 2015 Proposal generally retained the basic framework of the 2010 Proposal, with certain notable differences. While continuing to broaden the basic definition of "investment advice," the 2015 Proposal provided a more comprehensive list of "carve-outs" for conduct that would not be viewed as fiduciary. In addition, the 2015 Proposal included accompanying PTEs that would permit newly-minted fiduciaries under the DOL's revised approach to engage in certain conduct that would otherwise be prohibited. In particular, the DOL introduced a new "Best Interest Contract" exemption, which for many providers seemed to be emerging as a centerpiece of the DOL's new approach. The DOL also proposed amendments to incorporate a "best interest" standard into several existing PTEs.

[5] *See* footnote 8 below.

[6] The Final Rule does not purport to affect certain aspects of the existing fiduciary rules, such as (i) those relating to "plan assets" considerations and (ii) the exclusion from fiduciary status of traditional execution-only securities brokerage.

[7] We note that certain types of providers have been conducting business in a world that involves or at least implicates fiduciary issues, regardless of whether all of their conduct is fiduciary in nature. For example, trust officers may be well-versed in fiduciary concepts generally. The process of educating these types of market participants as to possibly expanded fiduciary duties may in some ways involve expanding an understanding of familiar principles, rather than introducing an entirely new paradigm. See also Section VIII.

other non-ERISA plans are not subject to ERISA, the DOL, under an applicable reorganization order, has rulemaking authority over the corresponding prohibited-transaction provisions of Section 4975 of the Code.[8]

B. *The General Structure of the Final Rule*

The Final Rule (i) establishes the general principles under which an adviser or financial institution might be considered a fiduciary, (ii) sets forth certain express clarifications under which fiduciary status expressly does not arise, (iii) provides for exceptions under which parties that would otherwise be fiduciaries will not be and (iv) issues exemptions under which a fiduciary can proceed without engaging in a prohibited transaction.

The threshold inquiry under the Final Rule is whether a non-discretionary adviser is making a "recommendation." If the adviser gives non-discretionary advice that does not rise to the level of a "recommendation" within the meaning of the Final Rule, then the adviser will not be considered a fiduciary solely by reason of providing such advice. The DOL identifies certain types of communications and activities that would expressly not be viewed as a recommendation and, therefore, would not give rise to fiduciary status. In addition, the DOL provides certain exceptions under which an adviser giving a recommendation will not be considered a fiduciary. Thus, if it is determined that a particular communication is a recommendation, it might still be possible to rely on one of the exceptions provided by the DOL to avoid the fiduciary status. If no exception from fiduciary status is applicable, the non-discretionary adviser would be a fiduciary under the Final Rule. The fiduciary may in that event proceed if (i) the conduct does not involve a prohibited transaction or (ii) the BIC Exemption or some other exemption is available.

C. *The "Too Soon" Question - Potential Impact of the Final Rule on Discretionary Fiduciaries*

As noted in Section III(A), the Final Rule at its core relates directly only to the provision of non-discretionary advice. However, all parties, including those in the business of providing discretionary advice (and who may already be considered fiduciaries), need to consider whether their sales and marketing activities may constitute fiduciary conduct. The relevant question is at what point in the process fiduciary status attaches.

If one is deemed a fiduciary during the sales-and-marketing phase, then even for a party that would willingly accept fiduciary status at the time the intended fiduciary relationship commences, fiduciary status may nevertheless arise sooner. That is to say, if a person is a fiduciary during the sales and marketing phase, then clear self-dealing issues may nevertheless arise at that time, possibly raising the need to seek relief under an exemption (such as the BIC Exemption). There are several possibilities. A provider may be a fiduciary in connection with efforts to market non-fiduciary products and services. In that case, fiduciary status may attach to a provider who otherwise would not have been a fiduciary. However, a provider willing to be a fiduciary (e.g., a provider seeking to become an investment manager) may become a fiduciary during the sales and marketing phase and before the intended fiduciary relationship commences.

As discussed in Section IV(D), the DOL did relax its approach to fiduciary status during the "hire me" phase. However, it is still possible under the Final Rule that certain types of sales and marketing efforts could involve a recommendation, thereby potentially triggering fiduciary status.

[8] *See* Reorg. Plan No. 4 of 1978, § 102(a) (transferring certain authority under Section 4975 of the Code from the Internal Revenue Service to the DOL), 3 C.F.R. part 332 (1978), confirmed by statute by P.L. 98-532 (1984).

D. *The Threshold Inquiry: Is There a Covered Recommendation?*

Under the Final Rule, the determination of whether a person is a fiduciary by virtue of giving non-discretionary "investment advice" involves asking the threshold question of whether that person has made a covered "recommendation." This fundamental point, which was part of neither the 2010 Proposal nor the 2015 Proposal, is central to the operation of the Final Rule. If there is no recommendation, then there is no fiduciary status and no other aspect of the Final Rule will apply.

Under the Final Rule, a recommendation is "a communication that, based on its content, context and presentation, would reasonably be viewed as a suggestion that the advice recipient engage in or refrain from taking a particular course of action." A covered recommendation is one that relates to:

- The advisability of acquiring, holding, disposing of or exchanging investment property;
- How to invest assets that are being rolled over, transferred or otherwise distributed from a plan or IRA;
- The management of investment assets through advisory accounts or otherwise (such as regarding investment policies or strategies, portfolio composition, selection of an investment adviser/manager or selection of investment account arrangements, in contrast to strictly taking orders for brokerage accounts); or
- Rollovers, transfers or other 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).

A person giving a covered recommendation will not be considered a fiduciary unless the recommendation is provided under one of the following three scenarios:

- The provider acknowledges fiduciary status;
- There is a written or verbal agreement, arrangement or understanding that the advice is based on the particular investment needs of the advice recipient; or
- The advice is directed to specific recipients regarding the advisability of a particular investment or management decision.

Although under general contract-law principles a "meeting of the minds" is necessary for an enforceable contract to arise, the DOL has specifically said that a meeting of the minds is not necessary for there to be fiduciary status under the Final Rule. Rather, an adviser may be considered a fiduciary if, under the circumstances surrounding the relationship, a reasonable person would understand that the nature of the relationship is one in which the adviser would be expected to consider the particular investment needs of the advice recipient. Similarly, fiduciary status may attach when the provider is reasonably understood to have held itself out as a fiduciary, even in the absence of express acknowledgement of fiduciary status. Accordingly, the determination of whether a recommendation has been made involves a case-by-case, fact-intensive analysis, and neither the provider's nor the recipient's own characterization of the advice is relevant. The Final Rule clarifies that the more individually tailored a communication is to a specific advice recipient, the more likely such communication will be viewed as a recommendation. A series of actions that are not themselves recommendations when viewed individually may amount to a recommendation when considered in the aggregate. It makes no difference to the characterization of the communication as a recommendation whether a communication was initiated by a person or a computer software program.

The Final Rule expressly states that providing a selective list of securities as "appropriate for a particular investor" would be a recommendation, even if no recommendation is made with respect to any one security. We note, however, that the Final Rule does not state that *every* provision of a selective list is a recommendation. Ultimately, there still needs to be a recommendation that the selective list is appropriate for a particular retirement investor in order for the provision of the list to constitute fiduciary advice.

Several helpful express relief provisions are set forth under the Final Rule, including the following:

- *"Hire Me" – Certain Sales and Marketing Considerations*. The DOL has indicated that an adviser or financial institution may recommend that the customer hire the adviser (or its affiliate) for advisory or asset management services without having that marketing activity be a covered recommendation. This point is an extremely welcome one, as the scope of the sales and marketing activities that may have been considered to be fiduciary in nature under the 2015 Proposal appeared to be significantly overbroad. To illustrate how broad the 2015 Proposal might have been in this regard, there was concern that even simple responses to requests for proposals ("RFPs") could constitute fiduciary conduct; the DOL has largely allayed such concerns in the Final Rule.[9]

- *Appraisals and Valuations*. Appraisals, fairness opinions and other similar statements are not covered recommendations under the Final Rule; however, the DOL has noted that possible fiduciary ramifications of such statements may be addressed in a future regulatory initiative.

- *Certain Welfare-Benefit Insurance*. Advice regarding the purchase of health, disability or term life insurance policies is not a covered recommendation if such policies do not have an investment component. This provision was important to allay concerns that a whole host of persons marketing health and other insurance would now become ERISA fiduciaries under the Final Rule.

E. *Certain Express Clarifications of Non-Fiduciary Status*

The Final Rule excludes certain types of communications and activities from the definition of "recommendation." Under the 2015 Proposal, the DOL had characterized most of these exclusions as "carve-outs" from the general definition of "investment advice." The DOL noted in the preamble to the Final Rule that this structural change was made partly in response to concerns that the conduct and information described in some of these carve-outs did not meet the technical definition of investment advice, such that they should be excluded from that definition. In addition to this structural change, the DOL made certain substantive changes from the 2015 Proposal, including adding a new exclusion for general marketing communications. Generally, the Final Rule clarifies that merely providing a platform of investment alternatives, investment education or marketing communications will not necessarily constitute a recommendation.

While some activities may fit neatly into one of those exclusions, we note, from the outset, that the general rules applicable to the "recommendation" concept (as described in Section IV(D) above) may in many instances continue to apply, depending on the particular set of facts surrounding the activity. Thus, the conduct in question needs to constitute a recommendation before fiduciary status may be deemed to have arisen. While failing to qualify under an

[9] However, the "hire me" clarification may be of limited value where sales and marketing activity is accompanied by an investment recommendation (such as the recommendation to roll over money from a 401(k) plan into an IRA). Sales and marketing is also discussed in Section IV(C).

express exclusion puts clear additional pressure on the analysis, it remains the case that, absent a recommendation, there is no fiduciary status.[10]

1. Platform Providers and Selection/Monitoring Assistance

Under the Final Rule, the provision of a "platform" of investment alternatives to a plan fiduciary, without regard to the individualized needs of the plan or its participants and beneficiaries, is not considered a recommendation. In order to rely on this "platform" exclusion, the platform provider must be independent of the plan fiduciary and must disclose in writing that it is not providing impartial investment advice or acting in a fiduciary capacity.

In addition, certain common activities that "platform providers"[11] may carry out to assist plan fiduciaries in selecting and monitoring the investment alternatives are also not recommendations under the Final Rule if certain specific conditions are met. Generally, these activities include identifying investment alternatives that meet objective criteria specified by the plan fiduciary (such as expense ratios, fund size, and type of asset or credit quality), responding to RFPs, requests for information or similar solicitations with a sample line-up of investments based only on the size of the employer or plan or the current investment alternatives under the plan, and providing objective financial data regarding investment alternatives. A platform provider who identifies a line-up of investment alternatives must disclose any financial interest in any of the alternatives, as well as the precise nature of any such interest.

Consistent with the DOL's general focus on protecting "retail" investors in the Final Rule, this "platform" exclusion does not apply to platforms offered to IRAs or to individual participants of an ERISA plan (such as when brokerage products are offered to "401(k)" plan participants). Rather, any line-up of investments that are provided to an IRA owner without the benefit of an independent plan fiduciary's oversight should be assessed under the general criteria described above for determining whether a "recommendation" has been made.

Although tailoring platforms for a particular plan should be avoided to the extent feasible where reliance is being placed on this "platform" exclusion, the DOL provides some ability to vary platforms for different customers. In particular, platforms may be segmented based on objective criteria, such as the size of the plan, which the DOL views as a business practice rather than a fiduciary recommendation. However, the DOL cautions that, if the platform provider communicates to the plan fiduciary that a platform that has been designed for a particular market segment is also appropriate for the plan in particular, such communication will likely be considered a recommendation. In addition, the DOL notes that general advice on objective criteria that the plan fiduciary may wish to consider in evaluating and selecting investments typically would not rise to the level of a recommendation, but that the fiduciary status of such advice should be examined on a case-by-case basis under the general definition of a recommendation. As such, any given communication to customers should be analyzed with care to avoid the risk of "tainting" platform services that otherwise would be covered by the exclusion.

2. Investment Education

Certain investment-related information and materials are considered general investment education and are excluded from the scope of communications that are treated as a "recommendation" under the Final Rule. Such "investment

[10] In this regard, the risk-analysis considerations such as those noted in Section V(F)(1) may be relevant in analyzing platforms, particularly in the context of dealing with IRAs.

[11] The Final Rule does not precisely define what constitutes a "platform provider." It remains to be seen whether there will be further clarification of this point.

education" materials may be categorized generally as (i) plan information, (ii) general financial, investment and retirement information, (iii) asset allocation models and (iv) interactive investment materials.[12]

The scope of the "investment education" exclusion is in some respects quite broad. The exclusion applies regardless of who provides the information (e.g., plan sponsor or service provider) or who receives the information (e.g., plan fiduciary, plan participant or IRA owner), and regardless of the frequency or form of the information.

Additional guidance is provided in the Final Rule regarding the specific conditions and limitations applicable to each category of investment education materials to avoid the "recommendation" characterization. Some of the key conditions and limitations include:

- *Plan Information*. Plan information may not state whether any investment alternative or benefit distribution option is appropriate for the plan or a particular plan participant or IRA owner. However, a description of the various forms of distributions and annuity options, including the advantages and disadvantages and risks of different distribution forms, may be included.

- *General Financial, Investment and Retirement Information*. Such information may not relate to specific investment products, investment alternatives or distribution options available to the plan or IRA (or the plan participants or IRA owners), or any specific investment alternatives or services offered outside the plan or IRA. However, it is permissible to provide information regarding retirement-related risks (such as longevity, market/interest rates, inflation and health care) and general methods and strategies for managing retirement assets.

- *Asset Allocation Models*. These models may identify a specific "designated investment alternative" (as that term is defined in the participant disclosure regulation) if certain conditions are met that generally require identifying all the other designated investment alternatives with similar risk and return characteristics and indicating where information regarding those alternatives may be found. Identifying investment alternatives is permitted under the "asset allocation" exclusion only with respect to ERISA plans that are subject to independent fiduciary oversight; thus this relief is not available in the IRA context because there is no independent plan fiduciary to review and select investment options.

- *Interactive Investment Materials*. Subject to the same conditions that are applicable to asset allocation models (as described above), these interactive investment materials may select one or more specific investment alternatives if (i) the investment alternative is one of several specified by the plan participant, beneficiary or IRA owner or (ii) the investment alternative is a designated investment alternative under an ERISA plan subject to independent fiduciary oversight.

3. General Communications

In the Final Rule, the DOL has provided new exclusions from the definition of a "recommendation" for certain general communications that "a reasonable person would not view as an investment recommendation." These express exclusions were welcome, as the breadth of the 2015 Proposal had caused concern that an array of general public communication could constitute fiduciary conduct.

[12] These categories of investment education materials were previously permitted (without triggering fiduciary status) under Interpretive Bulletin 96-1.

These excluded communications include:

- General circulation newsletters;
- Commentary in publicly broadcast talk shows;
- Remarks and presentations in widely attended speeches and conferences;
- Research or news reports for general distribution and general marketing materials; and
- General market data (including data on market performance, market indices or trading volumes), price quotes, performance reports or prospectuses.

The DOL has clarified that any labels placed on the particular communication will not control and that, in each case, a separate determination should be made regarding whether a reasonable person would view the communication as a recommendation.

F. *Exceptions to Fiduciary Investment Advice*

Even if a particular set of facts indicates the existence of a covered recommendation, it does not necessarily follow that the person giving such recommendation is a fiduciary. The Final Rule provides that certain activities will not, without more, cause a person to be treated as a fiduciary if certain conditions are satisfied, unless such person acknowledges fiduciary status with respect to such activity. Thus, a person giving a covered recommendation may still be able to avoid fiduciary status if any of the exceptions described below are applicable. In certain situations, however, it may be worthwhile to modify or remove any aspects of current practices that could constitute a recommendation, which could eliminate the need to rely upon any of these exceptions.

1. Counterparty Transactions with Certain Independent Plan Fiduciaries

The Final Rule includes an exception for counterparty transactions that is broader than the so-called “seller’s carve-out” that was included in the 2015 Proposal. The counterparty exception covers any advice given to certain fiduciaries of a plan or IRA (or a “plan asset” entity) that are independent of the adviser with respect to an arm’s length transaction. Generally, this exception is not available for communications directed to retail investors, such as small retail employee benefit plans and IRA owners, because retail investors are not typically represented by an independent fiduciary. In order to rely on this exception, the adviser must know or reasonably believe that the fiduciary is (i) a bank, (ii) an insurance carrier, (iii) a registered investment adviser, (iv) a registered broker-dealer or (v) any other fiduciary with at least US$50 million of assets (including both plan and non-plan assets) under its management or control. In addition, the adviser seeking to rely on this exception must satisfy the following conditions (and the adviser may rely on written representations to satisfy the first and third conditions listed below):

- The adviser must know or reasonably believe that the fiduciary is capable of evaluating investment risks independently;
- The adviser must fairly inform the fiduciary that it is not undertaking to provide impartial investment advice or give advice as a fiduciary in connection with the transaction, and fairly inform the fiduciary of the existence and nature of the adviser’s financial interests in the transaction;

- The adviser must know or reasonably believe that the fiduciary is in fact a fiduciary under ERISA or the Code, or both, with respect to the transaction and is responsible for exercising independent judgment in evaluating the transaction; and

- The adviser must not receive a fee or other compensation directly from the plan, plan fiduciary, plan participant or beneficiary, IRA or IRA owner for the provision of investment advice (as opposed to other services) in connection with the transaction.

Whether the fiduciary is "independent" of the adviser for purposes of this counterparty exception will generally involve a determination as to whether there exists a financial interest, ownership interest or other relationship that would limit the ability of the fiduciary to carry out its fiduciary responsibility to the plan or IRA, and such determination will be based on all relevant facts and circumstances.

2. Swaps and Security-Based Swaps Transactions

The Final Rule contains an exception under which swap dealers, security-based swap dealers, major swap participants, major security-based swap participants and swap-clearing firms will not become fiduciaries as a result of communications to an employee benefit plan during the course of swap or security-based swap transactions regulated under the Dodd-Frank Act provisions in the Commodity Exchange Act or the Securities Exchange Act of 1934 and the applicable rules and regulations of the Commodity Futures Trading Commission and Securities and Exchange Commission (the "SEC"). In order to rely on this exception, a number of conditions must be satisfied, which are intended to ensure the independence of the plan fiduciary in evaluating the transaction. These conditions are similar to those that apply to the counterparty transaction exception discussed above.

Importantly, the swaps-transaction exception is not available for transactions with IRAs or for transactions involving other classes of investments such as futures, but the counterparty-transaction exception discussed above might be available for such transactions.

3. Employee Communications

The Final Rule continues to provide an exception for certain communications from employees of a plan sponsor or plan fiduciary. Two scenarios of employee communications are covered by the exception. Under the first scenario, an employee may provide advice to a plan fiduciary, another employee or independent contractor (other than in the advice recipient's capacity as a plan participant) without triggering fiduciary status, if the employee does not receive any direct or indirect compensation for the advice other than normal compensation for services performed as an employee. This first scenario is intended to address situations where employees working in a company's payroll, accounting, human resources or finance departments routinely develop reports and recommendations for the company and other named fiduciaries. This scenario broadly covers communications from employees of plan sponsors, affiliates of plan sponsors, plans, unions and plan fiduciaries.

The second scenario that is covered by the exception is intended to permit an employee of the plan sponsor (or an affiliate of such plan sponsor) to communicate information about the plan, such as distribution options, to another employee in his or her capacity as a plan participant. This exception is subject to the same no-additional-compensation requirement as applicable to the first scenario, and is further subject to certain conditions that are designed to prevent the exception from covering employees who are in fact employed to provide investment recommendations to plan participants.

This exception is consistent with our general sense that the DOL attempted in the Final Rule to address true conflicts of interest, not situations in which information may in some sense be inadequate under more general (prudence-type) fiduciary principles. Thus, it is not surprising that the DOL sought to accommodate employers (and their agents) and fiduciaries in connection with generic plan-type communications from their respective employees.

V. "Best Interest Contract" Exemption

A. *Overview*

The BIC Exemption is the primary mechanism by which the DOL seeks to protect retirement investors from conflicts of interest and, simultaneously, to permit flexibility with respect to certain compensation structures that are prevalent in the retail investment market. These types of compensation include commissions, sales loads, 12b-1 fees and revenue sharing payments.[13]

At the core of the BIC Exemption are the "Impartial Conduct Standards," which apply to all advisers and financial institutions advising retirement investors. The Impartial Conduct Standards include a reiteration of ERISA's generally-applicable fiduciary standard, and require the party giving investment advice to "act with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of like character." In addition, the Impartial Conduct Standards require that the adviser act "based upon the investment objectives, risk tolerance, financial circumstances and the needs of the retirement investor" and "without regard to the financial or other interests of the adviser, financial institution or any affiliate, related entity or other party." The Impartial Conduct Standards also provide that, in connection with a recommended transaction, (i) none of the adviser, the financial institution or any of their affiliates or related entities may receive direct or indirect compensation that is in excess of reasonable compensation and (ii) the fiduciary not make any materially misleading statements regarding the applicable fees, material conflicts of interest or any other matters relevant to a retirement investor's investment decision.

For retirement investors that are not ERISA plans (including IRAs), the Impartial Conduct Standards (among other provisions) must be incorporated into a written contract. The requirement of a written contract for non-ERISA-covered retirement investors is expressly intended to give such investors contractual remedies that are similar to the remedial provisions available to plans under ERISA.

While complying with the requirements of the BIC Exemption is likely to impose substantial cost and compliance burdens on financial institutions, the exemption offers the ability to proceed with certain familiar compensation structures that otherwise would be prohibited. Even with the availability of the BIC Exemption, however, certain compensation structures, and certain products and services, may nevertheless become impermissible.

B. *Scope of the BIC Exemption*

Under the BIC Exemption, relief may be available with respect to any "retirement investor," a term which includes

[13] In response to comments to the 2015 Proposal, the DOL incorporated a number of important adjustments into the final version of the BIC Exemption. For example, the BIC Exemption as finalized applies to recommendations concerning any asset, whereas, under the 2015 Proposal, it was available only to transactions involving an approved list of specified assets. Additional liberalizing changes between the 2015 Proposal and the Final Rule include, among others, dispensing with the requirements that ERISA plans be party to a contract with the financial institution and, where a contract is required (i.e., for IRAs and other non-ERISA plans), that an individual adviser employed by a financial institution be a party to such contract.

- Any participant or beneficiary of a plan subject to Title I of ERISA who has authority to direct the investment of assets in his or her plan account or to take a distribution of the plan account;
- Any participant or beneficiary of a "plan" described in Section 4975(e)(1)(A) of the Code, including IRAs, HSAs, Archer MSAs and Coverdell education savings accounts;
- The beneficial owner of an IRA acting on behalf of the IRA; and
- Any fiduciary of an ERISA plan, IRA or other non-ERISA plan that is not (i) a bank, registered investment adviser, registered broker-dealer or insurance company or (ii) another independent fiduciary that holds, manages or controls at least US$50 million of assets.

The BIC Exemption applies to recommendations given by "advisers" or "financial institutions" and their "affiliates," and any other "related party." An adviser is an employee, independent contractor or other registered representative of a "financial institution" who satisfies applicable law and licensing with respect to the receipt of compensation. A "financial institution" is a bank, insurance company, registered investment adviser or registered broker-dealer that employs or retains an "adviser." An "affiliate" is (i) any person that is, directly or indirectly, controlling, controlled by or under control with the adviser or financial institution, (ii) any officer, director, partner, employee or relative of the adviser or financial institution and (iii) any corporation or partnership of which the adviser or financial institution is an officer, director or partner. A "related entity" is any entity (other than an "affiliate") in which the adviser or financial institution has an interest that may affect the adviser's best judgment as a fiduciary.

C. *The BIC Exemption - Generally Applicable Requirements*

1. Requirements to be Documented in Writing

a. Written Contract or Statement

As a condition for relying upon the BIC Exemption in connection with a transaction recommended for an IRA or other non-ERISA plan, the financial institution must enter into a written contract with the retirement investor that includes an acknowledgement of fiduciary status, a statement of the Impartial Conduct Standards, warranties that the financial institution has complied with, and will comply with, the BIC Exemption and other required disclosures. In addition, the Final Rule does not require the adviser to be a party to the contract. Additional aspects of the contract requirement (or lack thereof, as the case may be) are discussed in Section V(F)(1).

As mentioned above, the BIC Exemption dispenses with the requirement that a financial institution enter into a contract with an ERISA plan as a condition to relying upon the BIC Exemption. The rationale for this is that ERISA plans and plan participants can avail themselves of ERISA's statutory remedial provisions.

b. Acknowledgement of Fiduciary Status

The financial institution must affirmatively state in writing that it and its advisers act as fiduciaries under ERISA or the Code, or both, with respect to the investment advice subject to the contract or, in the case of an ERISA plan, with respect to any investment advice regarding the plan or participant account. With respect to IRAs and non-ERISA plans, if this acknowledgment of fiduciary status does not appear in a contract with the retirement investor, the BIC Exemption is not satisfied with respect to transactions involving that retirement investor. With respect to ERISA plans, this acknowledgement must be provided to the retirement investor prior to or at the same time as the execution of the recommended transaction, but not necessarily as part of a contract (since no contract is required).

c. Statement of Impartial Conduct Standards

The Impartial Conduct Standards require the fiduciary to "act with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of like character based upon the investment objectives, risk tolerance, financial circumstances and the needs of the retirement investor without regard to the financial or other interests of the adviser, financial institution or any affiliate, related entity or other party." The Impartial Conduct Standards also require that, in connection with a recommended transaction, (i) none of the adviser, the financial institution or any of their affiliates or related entities receive direct or indirect compensation that is in excess of reasonable compensation and (ii) the fiduciary not make any materially misleading statements regarding the applicable fees, material conflicts of interest or any other matters relevant to a retirement investor's investment decision.

In light of the foregoing, although the DOL seems to prefer level fees based on a fixed percentage of the value of an account's assets as an appropriate compensation mechanism for providing advice that reduces conflicts of interest with respect to recommendations made to retirement investors, variable compensation structures (such as commissions or transaction-based fees), which might ordinarily be prohibited under ERISA's self-dealing rules, are not necessarily foreclosed under the Final Rule.

d. Warranties

The written contract must include warranties to the retirement investor that the financial institution has adopted procedures that are reasonably and prudently designed to ensure that advisers adhere to the Impartial Conduct Standards. In addition, the warranties must include a statement that the financial institution requires that neither the financial institution nor any affiliates (or other related parties) use or rely upon compensation practices, quotas, appraisals or performance or personnel actions or other actions or incentives that would reasonably be expected to cause advisers to make recommendations that are not in the best interest of the retirement investor. While differential compensation is expressly permitted based upon the investment decision made by a retirement investor, the BIC Exemption requires that the financial institutions' policies and procedures do not, when viewed as a whole, cause a misalignment of the interests of advisers and retirement investors. Finally, the financial institution must warrant that it has specifically identified and documented all "material conflicts of interest" (defined as any financial interest of the adviser or financial institution that a reasonable person would conclude could affect the exercise of its best judgment in rendering advice to the retirement investor).

e. Certain Written Disclosures

The written contract (or for ERISA plans, the written statement) must contain the following disclosures or statements:

- *Statement of Standard of Care*. A statement of the best interest standard of care owed by the adviser and financial institution to the retirement investor, information regarding the services provided by the adviser and financial institution and a description of how the retirement investor will pay for services, whether directly or through third-party payments, including the nature of such payments (for example, commissions or transaction-based fees);

- *Conflicts Disclosure*. A description of the material conflicts of interests, a disclosure of all fees or charges that the adviser, the financial institution or its affiliates impose on the retirement investor, and a statement of the types of compensation that the adviser, financial institution and their affiliates expect to receive from third parties;

- *Description of Conflicts Policies*. A statement informing the retirement investor of the right to obtain copies of the financial institution's written description of its policies and procedures designed to prevent material conflicts of interest, as well as a specific disclosure of costs, fees and compensation (including third-party payments) regarding recommended transactions in sufficient detail to permit the retirement investor to make an informed judgment about the costs of the transaction and the significance and severity of the material conflicts of interest;

- *Website Link*. A link to the financial institution's website where updated versions of the financial institution's model contract disclosures and policies and procedures for the mitigation of conflicts can be obtained;

- *Disclosures Relating to Affiliations*. A disclosure of whether the financial institution offers proprietary products or receives third-party payments with respect to any recommended transaction, and a notification of the extent to which the adviser or financial institution limits its recommendations to proprietary products and any other limitations on the universe of investments that the adviser may offer for purchase, sale exchange or holding by the retirement investor;

- *Disclosures Relating to Ongoing Monitoring*. A statement of whether the adviser or financial institution will monitor the retirement investor's investments and alert the retirement investor to any recommended change in those investments, the frequency with which such monitoring will occur and the reasons for which the retirement investor will be alerted regarding those investments; and

- *Contact Information*. Contact information for a representative of the financial institution which the retirement investor can contact regarding the services or advice provided.

f. Prohibited Contract Terms

The contract between the financial institution and the retirement investor must not contain an exculpatory provision that disclaims or otherwise limits liability for any breach of the contract terms by the adviser or financial institution. In addition, the contract may not contain a provision that causes the retirement investor to waive or otherwise limit its right to participate in a class action or to limit damages that may be sought in an individual or class claim to liquidated damages for breach of contract. However, under the Final Rule, the contract may include a waiver of the retirement investor's ability to seek punitive damages or to rescind recommended transactions, if such a waiver is permitted under applicable state and federal law and if the retirement investor knowingly agrees to such a waiver.

g. Practical Considerations in Satisfying the Contract Requirements

The contract required for IRAs and other non-ERISA plans may be a master contract and its terms may be incorporated into separate documents in connection with opening an account or entering into an investment advisory or investment program agreement, an insurance or annuity contract or application, or another similar document. Thus, the contract may cover multiple recommendations, including advice rendered prior to the execution of the contract, as long as the contract is entered into prior to or at the same time as the execution of the recommended transaction. For new contracts, the retirement investor's assent must be demonstrated through a written or electronic signature. For retirement investors party to an investment or other contract entered into prior to April 10, 2017, assent may be evidenced either by affirmative consent (as described above) or a negative consent procedure under which the financial institution delivers a proposed contract amendment along with required disclosures to the retirement investor prior to January 1, 2018. If the retirement investor does not terminate the amended contract within 30 days after receiving the amendment documentation, the amended contract will become effective. If the retirement investor

does terminate the amended contract within that 30-day period, the BIC Exemption will provide relief for 14 days after the date on which the termination is received by the financial institution.

2. Other Requirements and Considerations Relating to the BIC Exemption

a. Policies and Procedures Relating to Conflicts

The financial institution must adopt policies and procedures that are reasonably and prudently designed to comply with the Impartial Conduct Standards. Specifically, the policies and procedures must not allow the financial institution (and, to the best of the financial institution's knowledge, must not allow any affiliate or related party) to use differential compensation, special awards, bonuses, contests, quotas, appraisals, performance or personnel actions or any other actions or incentives that would reasonably be expected to cause individual advisers to make recommendations that are not in the best interest of retirement investors. In designing such policies and procedures, the financial institution must specifically identify and document material conflicts of interest and adopt measures to prevent such conflicts of interest from causing violations of the Imprudent Conduct Standards.

In the Final Rule, the DOL enumerates several compensation arrangements that would generally not be seen as causing violations of the Imprudent Conduct Standards. Such arrangements include:

- Compensation related to advice provided in accordance with an unbiased computer model created by an independent third party, so long as the advice is not conveyed by an individual person;
- Compensation based upon the dollar amount of assets held by the retirement investor, regardless of how the retirement investor's assets are allocated between different investments;
- Compensation according to a fee schedule for its and its adviser's services, whereby the financial institution (i) may charge fees to the retirement investor in the case that payments from third-party providers do not satisfy such fees and (ii) must rebate fees to the retirement investor in the case that fees received from third-party providers exceed the financial institution's pre-determined fees; and
- Compensation based solely upon the time and expertise necessary to provide prudent advice with respect to the product, or other factors that would be neutral with respect to recommendations made to the retirement investor, but only if the financial institution also adopts a stringent supervisory structure to ensure that recommendations satisfy the Impartial Conduct Standards.

b. Proprietary Products and Third-Party Payments

Under the Final Rule, financial institutions and their advisers may continue to recommend proprietary products and other investment products that may cause third parties to make payments to the adviser or financial institution. Financial institutions and advisers that restrict their recommendations, in whole or in part, to proprietary products must comply with all other aspects of the BIC Exemption. Financial institutions must document any limitations they place on advisers' investment recommendations, the material conflicts of interest associated with the arrangements involving proprietary products, and the services that will be provided to retirement investors as well as third parties in exchange for compensation. A financial institution must reasonably conclude that the limitations will not cause the financial institution or its advisers to receive compensation in excess of reasonable compensation, and that the financial institution's policies, procedures and incentive practices will not cause the financial institution or its advisers to recommend imprudent investments or to otherwise fail to act impartially when making investment recommendations for retirement investors.

An institution's ability to offer proprietary products in a variety of contexts is another example of where the DOL had purported to aspire to allowing existing practices to continue, but where the proposed rules did not seem to allow a way forward. Under the final BIC Exemption, there now are paths that may, depending on the context and circumstances, be potentially viable. In this regard, we note that there has been some controversy over language in the Final Rule that could raise issues for institutions offering proprietary products "in whole or in part," and it seems possible that there may be some forthcoming clarification as to those issues.

c. Other Disclosure Requirements – "Point of Sale" Disclosures

In addition to the disclosures discussed above (in Section V(C)(1)(e)), a stand-alone "point of sale" disclosure must be provided prior to or at the time of the execution of a recommended transaction. The flexibility to delay the disclosure until the recommended transaction is executed is an example of the DOL's responsiveness to legitimate concerns that the disclosure requirements under the 2015 Proposal were unworkable.

The point-of-sale disclosure is a more streamlined disclosure that need only contain the following elements:

- A statement of the best interest standard of care;
- A statement that the retirement investor has the right to obtain copies of (i) the financial institution's written description of its policies and procedures designed to mitigate conflicts and (ii) a specific disclosure of the costs, fees and other compensation that are relevant to the retirement investor making an informed decision about the costs and the significance and severity of material conflicts of interest; and
- A link to the financial institution's website where updated versions of the financial institution's model contract disclosures and policies and procedures for the mitigation of conflicts can be obtained.

The Final Rule exempts the financial institution from repeating the above disclosures for products or investments that are subsequently recommended within one year, unless there is a material change in these disclosures. As a practical matter, it may be simpler for advisers and financial institutions to repeat the disclosures with each recommendation than to seek to track exactly when the earlier recommendations were made.

d. Other Disclosure Requirements – Website Disclosures

In addition to making point-of-sale disclosures and other written disclosures, as discussed above in Section V(C)(1)(e), the financial institution must maintain a website, updated not less than quarterly, that contains the disclosures mentioned above, the financial institution's current BIC Exemption model contract disclosure, and a summary of the policies and procedures adopted to avoid conflicts of interest. In addition, the website must include:

- A discussion of the financial institution's business model and the material conflicts associated with that business model;
- Disclosure of the financial institution's compensation and incentive arrangements with its advisers, including non-cash incentives and any incentives relating to attracting advisers to move from another financial institution or to stay at the financial institution;
- A list of all product manufacturers and all other parties with whom the financial institution maintains arrangements that cause third-party payments to be made to the adviser or financial institution, a statement

of any benefits that the financial institution provides to such other parties in exchange for the third-party payments and a statement of how any of these arrangements impact compensation of advisers; and

- A list of fees and service charges relating to retirement accounts.

e. Recordkeeping and Disclosure to the DOL

The financial institution must retain for six years all records necessary for the DOL and certain other entities (including plan fiduciaries, participants, beneficiaries and IRA owners) to determine whether the conditions of the BIC Exemption have been satisfied. Such records would include records concerning the financial institution's incentive and compensation practices for its advisers, the financial institution's policies and procedures designed to mitigate conflicts of interest, contracts entered into with retirement investors, and copies of disclosures intended to comply with the BIC Exemption.

Before receiving compensation in reliance on the BIC Exemption, the financial institution must notify the DOL by e-mail of its intention to rely on the BIC Exemption. The notice will remain in effect until revoked by the financial institution, and need not identify any particular plan or IRA. The DOL has stated that this requirement is integral to facilitating its audit and compliance assistance programs. If a financial institution restructures its operations so that a new legal entity is providing the investment advice or engaging the adviser, the new entity must file the notice with the DOL before relying on the BIC Exemption.

D. *"BIC Lite" Transactions for which the General Requirements of the BIC Exemption are Relaxed*

The Final Rule provides special rules being referred to by some as "BIC Lite," under which, in instances where there is a "level fee fiduciary" or a "bank networking arrangement," the party giving the investment advice must merely (i) provide a written acknowledgement of its fiduciary status prior to or contemporaneously with the execution of the recommended transaction and (ii) comply with the Impartial Conduct Standards. A "level fee fiduciary" is, as the name implies, a fiduciary that receives a fee that is either based upon a fixed percentage of the assets held by the retirement investor or a set fee that otherwise does not vary with the particular investment recommended. To avail itself of the streamlined requirements, the adviser or financial institution must disclose the applicable fee to the retirement investor prior to the execution of the recommended transaction. A "bank networking arrangement" is an arrangement for the referral of retail, non-deposit investment products under which bank employees refer bank customers to an unaffiliated investment adviser, broker-dealer or insurance company. The bank's referral arrangement must satisfy applicable banking, securities and insurance regulations.

E. *Transactions for which the BIC Exemption Does Not Provide Relief*

The BIC Exemption may not be used to allow the receipt of any compensation prohibited by ERISA or the Code in the following situations:

- *"In-House" Plans*. The BIC Exemption does not apply to the receipt of compensation from a transaction involving an ERISA plan if the adviser, financial institution or any affiliate is the employer of employees covered by the ERISA plan. The BIC Exemption is not available for compensation received in a rollover from such an ERISA plan to an IRA, where the compensation is derived from transactions involving the ERISA plan, not the IRA (although an adviser or financial institution may provide advice to the beneficial owner of an IRA who is employed by the adviser, its financial institution or an affiliate, and receive prohibited

compensation as a result, provided that the IRA is not covered by Title I of ERISA and the conditions of the BIC Exemption are satisfied).[14]

- *Principal Transactions*. A principal transaction is a transaction in which the adviser or financial institution is purchasing from, or selling to, a plan on behalf of the financial institution's own account or on behalf of an account of a person that is controlling, controlled by or under common control with the financial institution. Principal transactions are not covered by the BIC Exemption unless they are "riskless principal transactions."

- *Robo-advice*. The BIC Exemption does not apply to compensation received as a result of investment advice generated solely by an interactive website in which software-based models provide advice based upon information supplied by the retirement investor (without any personal interaction between the retirement investor and an individual adviser), unless the financial institution is a "level fee fiduciary." Financial institutions that are not level fee fiduciaries that seek relief for providing robo-advice must comply with the statutory exemption under Section 408(b)(14) (and Section 408(g)) of ERISA and the applicable DOL regulations.

- *Adviser Discretion*. The BIC Exemption is not available where the adviser has or exercises any discretionary authority or discretionary control with respect to the recommended transaction.

F. *Certain Special Considerations Relating to the BIC Exemption*

1. "Take It or Leave It" - A Viable Way to Approach IRAs?

Critically, as outlined in Section IV(D), the Final Rule operates fundamentally around the threshold question of whether a "recommendation" has been made. If there is no recommendation, then there is no fiduciary status; if there is no fiduciary status, then there is no need to seek relief under the BIC Exemption.

When a provider seeks to assess its risk profile under the Final Rule, a critical initial question may be: is the provider (i) making a recommendation and then seeking exemptive relief under the BIC Exemption or (ii) taking the position that there is no recommendation and therefore no fiduciary conduct? The difference in the resulting risk profile can be significant.

If the provider is making a recommendation and seeking relief under the BIC Exemption, then several risks will arise under general fiduciary principles. In the case of an ERISA plan, the plan may claim that the adviser has breached its duties of prudence and loyalty. In the case of an IRA (or other non-ERISA plan), the IRA (or non-ERISA plan) may make similar contractual claims under the "best interest" contract that the financial institution will have entered into in order to satisfy the BIC Exemption.

But what if, on any particular facts and circumstances, the provider is taking the credible position that there has been no recommendation? How does the risk analysis change?

In the case of an ERISA plan, the plan will be able to argue that the provider was incorrect in its assertion that there was no recommendation, and, if the plan is successful in that argument, it will be able to recover if it is able to

[14] The BIC Exemption is also not available if the adviser or financial institution is a named fiduciary or plan administrator with respect to an ERISA plan, or any affiliate of such fiduciary or plan administrator, that was selected to provide advice to the plan by a fiduciary who is not "independent" of the adviser, the financial institution or any of their respective affiliates.

establish that there has been a breach of fiduciary duty by the provider. However, the situation is starkly different in the case of an IRA or non-ERISA plan.

In particular, if a provider takes the position, when dealing with an IRA, that it has made no recommendation, what are the IRA's rights in connection with asserting that there was a recommendation, that there consequently was fiduciary status, and that a fiduciary breach has occurred? The answer may well be that the IRA has no right under the Final Rule to assert any such claim. This result arises because (i) the IRA has no ERISA claim, because ERISA does not apply, and (ii) the IRA has no contract claim because, by hypothesis, the provider has proceeded on the basis that there has been no fiduciary status arising out of any recommendation and therefore has not offered to enter into a contract under the BIC Exemption. Left with neither a statutory claim nor a contract claim, the IRA is left without any claim at all by virtue of the Final Rule.[15] To be clear, there would be excise-tax risk (under Section 4975 of the Code) if (i) the provider were shown to be incorrect that it was not a fiduciary, and (ii) it were to be determined that a prohibited transaction occurred. But that claim would need to be pursued successfully by the Internal Revenue Service in order for there to be liability,[16] and, furthermore, the claim would not be a claim for damages by or for the benefit of the IRA at all, but would rather be a claim by the Internal Revenue Service for taxes.

This approach will, as a business matter, not be ideal for every provider, and, even where a provider may consider the approach, it may not be ideal for all of the provider's products and services. To be sure, many current business models do involve recommendations. To pursue this approach, the provider might need to take a "take it or leave it approach" to what the provider is offering, and such an approach might be difficult or possibly undesirable, from a client-relations and other business perspectives. Documentation might need to be clear that there is no recommendation, and training might need to be extensive to attempt to ensure that those interfacing with the client endeavor to confirm the lack of any recommendation.

It remains to be seen how willing institutions will be to structure their sales and marketing efforts as essentially a no-recommendation "take it or leave it" approach, and how comfortable they will be in taking the position that no recommendation has been made. However, there are factors that could make the approach more viable. For example, some providers may be willing to accept the risk of offering a particular product or service on a non-fiduciary basis while others may not. As another example, if competitors in the market move away from making recommendations with respect to any given product or service, then any given institution's or other person's movement away from making recommendations may as a practical matter become more feasible.

As noted in Section IV(A), an administrative reorganization gave the DOL interpretive authority over the Code's prohibited-transaction provisions. However, that reorganization neither caused ERISA's substantive rules to apply to, nor gave the DOL any enforcement authority over, IRAs and other non-ERISA plans. Thus, for IRAs and other non-ERISA plans, there is still no DOL enforcement, nor any generally applicable centralized legal fiduciary duty. Accordingly, the lack of any ability under the Final Rule of an IRA owner to bring a claim that a provider is acting in a fiduciary capacity could be relevant to the provider's risk assessment, if the provider wishes to consider proceeding on the basis that it is not making a recommendation.

[15] There may be a claim under state law, but that claim, if valid, would have existed even without regard to the Final Rule and, furthermore, the Final Rule would not seem to have any bearing on the validity of such a claim.

[16] The Internal Revenue Service, in order to prevail, would need not only to establish fiduciary status, but also to persuade a court that a non-exempt prohibited transaction actually occurred. Even then, an additional issue would center around what the applicable "amount involved" was and, therefore, what the correct amount of the excise tax is.

2. A "Bleed-Over" Effect for Disclosure and Training Practices?

Questions are emerging regarding the consequences of financial institutions relying on the BIC Exemption. For example, the degree to which the disclosure and training practices surrounding the BIC Exemption will "bleed over" and become incorporated into institutional practices regarding non-retirement accounts remains to be seen. There is a natural general trend to a "least common denominator" approach to disclosure and compliance training, which may work its way into implementation of compliance efforts surrounding the Final Rule.

Other relevant questions include:

- If a financial institution re-crafts its disclosure and training for retirement investors, will those changes be implemented across the board for other (non-retirement) customers?
- Will a financial institution be willing to give a customer one level of disclosure for the customer's retirement accounts and another (presumably lesser) level of disclosure for the customer's non-retirement accounts?
- If financial institutions do standardize their disclosure and training practices and extend them to non-retirement customers and accounts, how will this affect the regulatory efforts of the SEC?

The answers to these questions will presumably evolve as market practices develop in response to the Final Rule and as the SEC considers its approach.

VI. Other "Prohibited Transaction" Exemptions

Along with its revision of the definition of "investment advice," the DOL reconsidered a panoply of existing PTEs. It is noted that, because much advice given to IRAs and non-ERISA plans previously could not be categorized as "fiduciary" in nature, ERISA's scheme of prohibited transactions did not apply to a wide range of transactions involving IRAs and other non-ERISA plans. Under the Final Rule, many of these transactions will now be prohibited in the absence of an exemption, and, if a transaction is to go forward, the adviser or financial institution will need to comply with the requirements of the applicable PTE.

The DOL's general approach was to superimpose the "best interest" principles, and specifically the Impartial Conduct Standards, over the existing conditions of a number of existing PTEs. However, in one particular case, involving insurance companies, the scope of exemptive relief has been significantly narrowed, and in certain other cases existing relief has been revoked entirely.

A. *Principal Transaction Class Exemption*

1. Background

The DOL finalized a new class exemption that allows advisers and financial institutions to engage in "principal transactions" and "riskless principal transactions" involving certain investments with plans, participant and beneficiary accounts, and IRAs. A "principal transaction" is a transaction that involves a direct purchase or sale transaction between an ERISA plan, IRA or other non-ERISA plan and the account of the adviser or financial institution. A "riskless principal transaction" is one in which a financial institution, after having received an order from a retirement investor to buy or sell an investment product, purchases or sells the same investment product for the financial institution's own account to offset the contemporaneous transaction with the retirement investor.

The Principal Transaction Class Exemption was introduced because the DOL recognized that, with the sweeping changes to the fiduciary rules, certain purchases and sales of investments in principal transactions or riskless principal transactions between a plan and a fiduciary providing investment advice could constitute prohibited transactions even though such transactions are integral to the economically efficient distribution of fixed income securities. Specifically, the DOL recognized that principal transactions are essential to the distribution of debt securities and initially limited relief to that category of assets.

2. Basic Requirements of the Principal Transaction Class Exemption

The Principal Transaction Class Exemption permits an adviser or financial institution to engage in the purchase or sale of a "principal traded asset" (*i.e.*, an asset held in its own account) in a principal transaction or riskless principal transaction with a plan, participant or beneficiary account, or IRA, and receive a mark-up, mark-down or other similar payment as a result of the adviser's or financial institution's advice. For purposes of the Principal Transaction Class Exemption, "principal traded asset" is defined as (i) for purposes of a purchase by a plan or IRA, a debt security, a certificate of deposit or an interest in a unit investment trust, and (ii) for purposes of a sale by a plan or IRA, all securities or other investment property. The type of transactions originally intended to be exempt under the 2015 Proposal involved the purchase or sale of debt securities (*e.g.*, bonds) which may only be available from a limited number of financial institutions (which also act as advisers); however, given the conditions and requirements of the Principal Transaction Class Exemption as finalized, the DOL decided to expand the scope of relief to include certificates of deposit and interests in unit investment trusts. A financial institution can obtain relief under the Principal Transaction Class Exemption if it (i) customarily purchases or sells "principal traded assets" for its own account in the ordinary course of business and (ii) is a registered broker-dealer, registered investment adviser or a bank or similar financial institution.

The Principal Transaction Class Exemption is not available if:

- The adviser is a "discretionary" fiduciary; or
- The plan is covered by Title I of ERISA and either (i) the adviser, financial institution or an affiliate is the employer of the employees covered by the plan or (ii) the adviser or financial institution is a named fiduciary or administrator of the plan or an affiliate thereof that was selected to provide investment advice to the plan by a fiduciary who is not "independent."

3. Other Requirements of the Principal Transaction Class Exemption

Advisers and financial institutions seeking relief under the Principal Transaction Class Exemption are subject to certain conditions described below, which, in many respects, are similar to the conditions set forth under the BIC Exemption described above. For example:

- Under the Principal Transaction Class Exemption, financial institutions are required to enter into written contracts with non-ERISA investors prior to or at the same time as the execution of the principal transaction or riskless principal transaction. Such a written contract can be entered into as a new stand-alone contract or its terms may be incorporated into an investment advisory agreement, account opening agreement or similar document. Advisers and financial institutions may amend existing contracts by negative consent (identical to the process described in the BIC Exemption). No written contracts are required with ERISA plans.

- The Principal Transaction Class Exemption generally incorporates from the BIC Exemption (with certain adjustments) the Impartial Conduct Standards and the requirement to give affirmative warranties and certain disclosures, and also prohibits certain exculpatory provisions that are also prohibited under the BIC Exemption.

B. *Amendment of PTE 77-4: Purchases and Sales of Affiliated Mutual Fund Shares*

PTE 77-4 generally allows, subject to certain conditions, the purchase and sale of mutual fund shares where the mutual fund adviser or one of its affiliates is a fiduciary to the ERISA plan or IRA. Under the prior version of PTE 77-4, the exemption would only apply if the plan investor did not pay (i) any sales commission in connection with the purchase, (ii) an investment management, investment advisory or similar fee with respect to the plan assets invested, or (iii) a redemption fee in connection with the disposition of the shares to the investment company unless the redemption fee is disclosed in the applicable mutual fund prospectus and is paid only to the investment company.

Under the Final Rule, the DOL amended PTE 77-4 so that purchases and sales of mutual fund shares under these circumstances are permissible so long as certain BIC-type conditions are satisfied. Specifically, PTE 77-4 as amended requires the adviser and financial institution to uphold the Impartial Conduct Standards, not receive more than reasonable compensation and not make certain types of materially misleading statements. However, amended PTE 77-4 does not require the adviser and financial institution to make the warranties that are otherwise generally required for full compliance with the BIC Exemption.

C. *Amendments of Other PTEs to Incorporate a "Best Interest" Standard*

Similar to the DOL's approach to amending PTE 77-4, a number of other PTEs were amended so as to import into those PTEs the standards of the BIC Exemption and apply those standards to transactions that were not subject to such standards under the prior versions of those PTEs, as follows:

- PTE 80-83 provides relief for fiduciaries using the proceeds of securities purchased in a public offering to retire indebtedness;

- PTE 83-1 provides relief for the sale in the initial issuance of, and continued holding by a plan of, mortgage pool certificates where the mortgage pool sponsor, trustee or insurer of the pool is a party in interest to the plan;

- PTE 75-1 Part III, provides relief for the purchase of securities in an underwriting from a person other than the fiduciary where the fiduciary is a member of the underwriting syndicate for the security; and

- PTE 75-1 Part IV, provides relief for the purchase of securities from a fiduciary who is a market maker with respect to the security that is the subject of the transaction.

As amended, advisers and financial institutions that wish to rely upon any of the above PTEs will now be required to comply with the impartial conduct standards established under the BIC Exemption. In addition to the above amendments to PTE 75-1, the DOL revoked certain aspects of PTE 75-1 (discussed in Section VI(F)) and also expanded relief under Part V of PTE 75-1 to permit a party giving investment advice to receive a reasonable fee for extending credit to a retirement investor to avoid a failed purchase or sale of securities. To obtain this relief, the terms of the extension of credit must be comparable to those that would have been negotiated in an arm's length transaction between unaffiliated parties, and the fiduciary (and its affiliates) cannot be the cause of the failed transaction.

D. *Amendment of PTE 86-128: Affiliated Brokerage*

PTE 86-128 provides relief for fiduciaries that use their authority to cause a plan to pay a fee to themselves or an affiliate and for fiduciaries that receive commissions for acting as agents in agency cross transactions involving "plan assets." The DOL made a number of material changes to PTE 86-128:

- PTE 86-128 can no longer be relied upon by an investment advice fiduciary (as opposed to a discretionary fiduciary) to an IRA to permit receipt of a fee for effecting or executing securities. Investment advice fiduciaries with respect to IRAs must now instead rely upon the BIC Exemption for these transactions; however, investment advice (as well as discretionary) fiduciaries with respect to ERISA plans may continue to rely upon this exemption.

- Importantly, the fiduciary must now satisfy the Impartial Conduct Standards. In addition, fiduciaries must abide by recordkeeping requirements that would enable an enforcement agency or retirement investor to review compliance with the terms of the PTE. Such recordkeeping requirements obligate fiduciaries to retain records for six years, commensurate with the recordkeeping requirements applicable under the BIC Exemption and other PTEs.

- The types of commissions a fiduciary is permitted to receive under PTE 86-128 are limited to brokerage commissions and sales loads. Other types of payments in connection with the transaction (including 12b-1 fees, revenue sharing and administrative and marketing fees) will no longer be eligible for relief under PTE 86-128.

- Relief is expanded so that, in addition to fiduciaries and their affiliates, commissions may be received by related entities.

- Certain conditions of PTE 86-128 will not apply if the fiduciary returns to the retirement investor all profits earned by the fiduciary (and its affiliates and other certain related entities). In addition, certain disclosure and express authorization requirements generally applicable under PTE 86-128 will not apply to pooled funds if certain other conditions are met, including where the authorizing fiduciary receives certain detailed information stating that future express authorization will not be required.

E. *Amendment of PTE 84-24: Certain Insurance Products*

PTE 84-24 generally allows agents, brokers and pension consultants to receive commissions in connection with the purchase of an insurance or annuity contract and the receipt of commissions in connection with the sale by a principal underwriter of shares of a mutual fund. In addition, PTE 84-24 allows an insurance broker or pension consultant to effect transactions for the purchase of insurance or annuity contracts or mutual fund shares using the assets of an ERISA plan or IRA. As amended in conjunction with the release of the Final Rule, PTE 84-24 will no longer permit an adviser or financial institution to receive commissions with respect to the sale to an ERISA plan or IRA of an annuity other than a "fixed rate annuity contract" or mutual fund shares. A fixed rate annuity contract generally includes an immediate or deferred annuity contract the benefits of which do not vary, whether in whole or in part, based upon the investment experience of a separate account, an index, investment model or other vehicle which would generate returns that would fluctuate over time.

Thus, PTE 84-24 will no longer be applicable with respect to variable and index annuities, and an insurance company seeking to sell those products to an ERISA plan or IRA would instead generally need to comply with the BIC

Exemption. The partial revocation of this aspect of PTE 84-24 is motivated by the DOL's perception that, when a retirement investor is in the market for such products, the BIC Exemption provides the appropriate conditions for relief.

Thus, under the Final Rule, PTE 84-24 now provides relief only for the financial institution's or other adviser's receipt of (i) insurance commissions in connection with the purchase of a fixed rate annuity contract by, or otherwise effecting a purchase of a fixed rate annuity contract with the assets of, an ERISA plan or IRA, and (ii) mutual fund commissions in connection with the purchase of mutual fund shares, or otherwise effecting a transaction for the purchase of mutual fund shares by an ERISA plan (but not an IRA). This relief is also available in the context of a rollover, and PTE 84-24 does permits the fiduciary adviser to be related to the IRA owner.

Insurance companies may be disappointed by the withdrawal of relief previously available with respect to purchases of annuities other than fixed rate annuity contracts. While it is true that complying with the BIC Exemption may be more burdensome, those insurance companies that will pursue relief under the BIC Exemption will not be alone in those efforts. Insurers and their brokers selling variable and index annuities will no longer have a special compliance path. However, it is not clear that insurance-company compensation models will always be reasonably amenable to complying with the BIC Exemption. Thus, it remains to be seen how insurance companies will proceed regarding variable and index annuities.

The insurance industry is an example of a group that was adversely affected by the progression from the proposed fiduciary rules to the Final Rule.

F. *Revocation of Certain Relief*

In applying its overarching mission of mitigating the potential for conflicts of interest, the DOL believed that certain PTEs should no longer be available. Thus, in connection with issuing the Final Rule, the DOL withdrew exemptive relief under PTE 75-1, Part II, for the purchase of mutual fund shares (as opposed to other types of securities) if the fiduciary is not affiliated with the mutual fund or its underwriter. The DOL believed that appropriate relief for such transactions that involve the assets of ERISA plans was granted under PTE 86-128, described in Section VI(D). To the extent that the transaction involves the assets of an IRA or other non-ERISA plan, the fiduciary must rely upon the BIC Exemption.

The DOL also revoked Parts I(b) and I(c) of PTE 75-1, which had previously provided relief for (i) effecting securities transaction by a non-fiduciary party-in-interest that was acting as an agent in the transactions and (ii) the furnishing of non-fiduciary advice regarding the value of securities or a wide range of investment-related research regarding securities, including reports concerning issues, industries, economic analysis and portfolio strategy. The DOL indicated that it believed that the statutory provisions applicable with respect to such advice and information are sufficient.

VII. Possible Indirect Effect on Non-Fiduciaries

A. *In General*

The impact of the Final Rule does not stop with those directly affected as a result of new-found fiduciary status. There is an important impact on certain market participants who might not be fiduciaries, but whose business will be affected by those who are. These entities must interact and coexist with parties that will now be fiduciaries, and may need to consider how their products and services can be adapted to meet the needs of their fiduciary counterparties.

One critical way in which the Final Rule might impact the market is in connection with the potential indirect effect on sponsors of investment funds and other financial products, where those sponsors deal with platform providers and other intermediaries who may be directly affected by the Final Rule. For example, assume that a person offering a menu of funds would not have been a fiduciary prior to the Final Rule, but is willing to proceed on the basis that it will be a fiduciary under the Final Rule. That person may be required to consider a number of possible alternatives. They may seek to reduce conflicts of interest in an effort to comply with the BIC Exemption, or they may seek relief under the streamlined BIC Lite provisions available for certain transactions involving level fee fiduciaries. Alternatively, that person may seek to eliminate conflicts altogether and assert that it is in compliance with its new-found fiduciary status without needing to rely upon an exemption. In any such case, the manager of the funds might need to reconsider the structure of the funds so that any compensation flowing from the fiduciary's use of the funds is somewhat or entirely level, or otherwise does not raise conflicts of interest for the fiduciary.

Another example may involve the provision of free products, information or services by an advice provider to a fiduciary. Are the free items available to the fiduciary even if the fiduciary does not transact business with the provider? If not, do they put the fiduciary into a conflict position in connection with the fiduciary's consideration of the use of that provider? If so, the provider may want to consider reviewing its practices, so that the provider does not make it more difficult for the fiduciary to continue to do business with the provider.

B. *Certain Considerations Relating to Funds*

With respect to funds in particular, the Final Rule is expected to have a significant impact on intermediary distribution channels. Prior to the issuance of the Final Rule, intermediaries that provided recommendations regarding investment products to retail retirement investors were generally not considered fiduciaries under ERISA, but instead were only subject to suitability requirements *(i.e.*, a requirement to determine that an investment is suitable for a particular client). Under the Final Rule, the universe of ERISA fiduciaries has been expanded to include intermediaries that make such recommendations, including recommendations relating to the decision of whether to roll over assets from an employer-sponsored plan into an IRA. As ERISA fiduciaries, these intermediaries are subject to duties of prudence and loyalty and are limited in their ability to receive fees with respect to investment products they recommend, including sales commissions, 12b-1 fees, revenue sharing payments, and sub-transfer agency payments, absent an exemption. The application of the prohibitions and the exemptions relating to fund intermediaries is still unclear at this point in time and market practices will continue to develop.

Given the burdens associated with complying with the BIC Exemption discussed above, some intermediaries may not be willing to rely on the exemption to continue to receive the types of compensation they receive under their current distribution arrangements. In addition, even where an intermediary is willing to comply with the conditions of the exemption, the intermediary must recognize that it is still a fiduciary. As such, the fiduciary should understand that compliance with the exemption does not mean that the intermediary's receipt of compensation cannot be questioned, but rather that such compensation is not automatically prohibited. The Final Rule may therefore prompt intermediaries to seek changes to their distribution arrangements, thereby indirectly impacting funds. For example, intermediaries may now seek to be compensated at the client level rather than by funds and their sponsors (*i.e.*, payments at the IRA account level rather than 12b-1 and revenue sharing payments).

How intermediaries react to the Final Rule, and whether they react consistently, remains to be seen. However, given the fiduciary standards to which intermediaries may be subject, possible trends following the implementation of the Final Rules may include changes in demand for certain types of funds or share classes due to intermediaries' appetite for products that implicate fewer issues under the Final Rules; an increased focus on the differences among share classes, including the differences in fees and the services provided for those fees; an increased focus on the

differences in fees among funds (*e.g.*, passive vs. actively managed strategies, equity vs. fixed income); and movement toward low-cost, passive strategies in retirement plans. These trends may be seen in the retirement market as well as in other markets, as intermediaries may be unable to justify choosing different funds or share classes for their non-retirement investors than they choose for the retirement investors for which they serve as fiduciaries.

It is also important to note that fund distributors and transfer agents could be deemed fiduciaries if they were to provide "recommendations" as part of their functions to shareholders invested in retirement accounts. These recommendations could take the form of call-center responses to inquiries from shareholders and fund websites that may be deemed to provide investment advice (see also Section IV(F)(3), discussing employee communications).

VIII. Potential Considerations For Broker-Dealers

Although many broker-dealers who will become subject to the Final Rule are dually-registered as investment advisers, and as such have already been dealing with some level of fiduciary obligation, to the extent that they provide covered services to ERISA plans or other retirement investors, they will need to modify their procedures to reflect their new, ERISA-type fiduciary obligations.[17]

IX. Effective Date; Grandfather Rule

The Final Rule becomes effective on June 7, 2016 (60 days after publication in the Federal Register), although its actual applicability is delayed until April 10, 2017 (roughly the first anniversary of the Final Rule's issuance), and with a general delay in the applicability of the BIC Exemption until January 1, 2018. The DOL has indicated that it will provide further guidance regarding implementation of the Final Rule on a rolling basis in the form of FAQs starting in the summer of 2016.

The Final Rule includes a grandfathering provision that allows for additional compensation based on investments that were made prior to the Final Rule's applicability date, although all advice provided after the applicability date must satisfy the Impartial Conduct Standards. It is possible that some newly-minted fiduciaries under the Final Rule might consider ceasing to accept new IRA contributions before the applicability date, in order to avoid the compliance obligations under the Final Rule.

X. Conclusion

Surely, we now have a brave new fiduciary world in the ERISA galaxy. The Final Rule is undeniably one of the most important developments under ERISA since its enactment in 1974, and will affect an incredibly broad array of activities undertaken by professionals in the financial services industry ranging from large financial institutions to

[17] It is also noted that a broker-dealer's institution of a level fee structure, whether specifically to come within the BIC Lite rules (noted in Section V(D)) or otherwise, may raise questions regarding whether the broker-dealer is receiving "special compensation" for providing advisory services, thereby jeopardizing the ability of the broker-dealer to rely on the broker-dealer exception from the definition of an "investment adviser" in the Investment Advisers Act of 1940. Section 202(a)(11)(C) thereof excepts from the definition of an "investment adviser" any broker or dealer whose performance of advisory services is solely incidental to the conduct of its business as a broker or dealer, if no special compensation is received by the broker or dealer for providing investment advice. The term "special compensation" has generally been defined to include any compensation other than commissions, mark-ups and mark-downs. Although in 2005 the SEC adopted a rule that deemed brokers charging asset-based brokerage fees not to be investment advisers based solely on the receipt of special compensation (SEC Rel. No. 2376 (Apr. 12, 2005)), that rule was later vacated (by *Financial Planning Ass'n v. SEC*, 482 F.3d 481 (D.C. Cir. 2007)).

individual asset managers. The DOL clearly chose to strike a new balance regarding fiduciary status when it released the Final Rule. It remains to be seen whether the new balance is an ideal one.

In many ways, the Final Rule can be seen as continuing an existing legislative and regulatory trend towards increased disclosure and heightened fee-transparency. Rather than serving effectively to prohibit desirable products and services, the Final Rule seems genuinely to be structured to permit institutions to proceed as fiduciaries, if they are willing to accept a “best interest” gloss over what previously had been non-fiduciary conduct.

In this regard, as important as the Final Rule is, it may not be as utterly transformative as the proposals leading up to it may have been. The DOL, in considering the fallout from the 2010 Proposal and the 2015 Proposal, made numerous important changes and, as a result, it is anticipated that the Final Rule will in many cases present workable alternatives. In addition, the DOL has indicated some willingness to make still further changes and clarifications to facilitate the implementation of the Final Rule. Ultimately, it remains to be seen just how the market will eventually react to the various changes that have now been incorporated into the Final Rule.

This update was authored by:

Andrew L. Oringer
Partner, New York
+1 212 698 3571
andrew.oringer@dechert.com

Susan M. Camillo
Partner, Boston
+1 617 728 7125
susan.camillo@dechert.com

Stephen H. Bier
Partner, New York
+1 212 698 3889
stephen.bier@dechert.com

Julien Bourgeois
Partner, Washington, D.C.
+1 202 261 3451
julien.bourgeois@dechert.com

Susan K. Grafton
Partner, Washington, D.C.
+1 202 261 3399
susan.grafton@dechert.com

Christopher P. Harvey
Partner, Boston
+1 617 728 7167
christopher.harvey@dechert.com

Jack W. Murphy
Partner, Washington, D.C.
+1 202 261 3303
jack.murphy@dechert.com

Andrew Braid
Associate, Philadelphia
+1 215 994 2613
andrew.braid@dechert.com

Sarah Burke
Associate, New York
+1 212 698 3620
sarah.burke@dechert.com

Stephanie A. Capistron
Associate, Boston
+1 617 728 7127
stephanie.capistron@dechert.com

Chelsea M. Childs
Associate, Boston
+1 617 728 7128
chelsea.childs@dechert.com

Young Eun Lee
Associate, New York
+1 212 641 5634
youngeun.lee@dechert.com

Christine Ayako Schleppegrell
Associate, Washington, D.C.
+1 202 261 3357
christine.schleppegrell@dechert.com

Aryeh Zuber
Associate, New York
+1 212 698 3522
aryeh.zuber@dechert.com