EVERSHEDS SUTHERLAND

The Final Rule:
Next Steps After Vacatur

The nationwide vacatur of the Department of Labor (DOL) "investment advice" fiduciary definition and related exemptions (Final Rule) by the US Court of Appeals for the Fifth Circuit on March 15, 2018, did not bring an end to the challenges created by this extraordinary rulemaking. Both plan providers and plan sponsors will face significant responsibilities in unwinding the programs they had put in place to comply with the Final Rule—if the vacatur stands—and reinstating the predecessor ERISA regulation in their compliance programs, which apparently is to coincide with an uptick in "best interest" rulemaking by the Securities and Exchange Commission and among the states.

Considerations for Plan Providers

Retirement product and service providers should start the unwinding process with, yet again, a strategic reconsideration of how best to position their businesses in the evolving regulatory environment. Mainly the objections to the Final Rule from industry have not been to the "best interest" concept or to enhanced transparency, but rather to:

- the execution of those ideas by an agency with neither expertise in financial services nor accountability for the health of those industries;
- the disconnect between the Final Rule and the statute;
- by way of a specific example, the creation of a consequential legal remedy by regulation rather than legislation;
- a cost-benefit analysis that immediately proved to be materially inaccurate; and
- on a related point, the adverse effects of the Final Rule on the availability and costs of services particularly for small retirement investors, and ultimately to the coverage of the US retirement system.

It may be that providers will determine that at least some of the changes made to their business models in response to the Final Rule will permit them to better serve plans and retirement investors, or will be helpful in the changing regulatory context, or otherwise should be retained, perhaps with refinements.

With those strategic determinations, providers can then work back through the changes they developed in implementing the Final Rule and unwind or adjust them as appropriate. These include:

- **Documentation.** Different types of responses may be appropriate for different types of documentation, in part depending on the definitive date determined for vacatur of the Final Rule and the provider's ability to process these changes. For example, as the Final Rule was implemented, some documentation included self-executing unwind provisions in the event the Final Rule lost legal effect, others provided for unilateral unwinds, and still others were silent on this point. The affected documentation may include:
  a. client-facing agreements
  b. disclosures for plan sponsors and for participants or IRA owners
  c. websites
  d. marketing materials and illustrations, particularly including the disclaimers typical in these materials
  e. internal policies and procedures
  f. business-to-business agreements, e.g., selling agreements

- **Compensation structures**
- **Sales practices and procedures, including:**
  a. product/service shelf
  b. sales processes/standards
  c. sales supervision
- **Training.** The churn rate in "best interest" developments is proving to be a serious practical challenge, both for providers in designing effective training programs and for their personnel in keeping straight, understanding and operationalizing these developments.

Considerations for Plan Sponsors

Plan sponsors that developed infrastructure to collect and assimilate changes to their providers' business models and documentation in response to the Final Rule will turn again to those processes to understand and evaluate the changes made by providers in response to the vacatur.

Prohibited Transaction Considerations

Finally, plan providers, with oversight from plan sponsors, will need to reconstitute their prohibited transaction compliance programs in light of the reinstatement of the 5-part "investment advice" fiduciary definition and the pre-Final Rule system of exemptions. This also will be a multi-step process, and almost certainly will require guidance from DOL. In light of these developments, providers should consider the following:

- The ongoing accuracy of section 408(b)(2) disclosures, including any statement on whether fiduciary services are being provided, should be reviewed.
- Under the pre-existing system of exemptions, reasonable compensation was a condition for most, if not all, of the exemptive relief for investment products and services; the change in the Final Rule was to shift the onus for the reasonable compensation determination from the plan sponsor or retirement investor—i.e., from the party in a position to do "comparison shopping"—to the provider. In the process of reverting to the prior system, providers would be well served to be prepared to assist purchasers in making that determination.
- Providers should re-evaluate their current business models for circumstances in which fiduciary "investment advice" is being provided under the prior 5-part test and the availability of exemptive relief for any prohibited transaction issues presented.
- With the vacatur of the best interest contract exemption (BICE), the principal transaction exemption and amendments to other exemptions, a solution will be needed for transactions on or after the June 9, 2017, applicability date.
  – Providers that have in good faith been relying on the transaction relief under BICE, for example, may find themselves retroactively without clear exemptive relief, to the extent of conflicted fiduciary activity under the 5-part test; compliance with transition BICE generally would not in and of itself satisfy the full set of conditions under pre-existing exemptions.
  – There are limited arrangements for which BICE provided relief where there might not have been relief available under the prior system of exemptions.
  – Compliance since June 9 with one of the amended exemptions should constitute at least material compliance with the prior terms of that exemption, but further study will be required to identify whether there are any gaps in coverage.

The orderly administration of the prohibited transaction rules would seem to require guidance from DOL on these points, in a form that would be binding on not only the DOL and Internal Revenue Service but also on private litigants and (in light of the recent Massachusetts Securities Division complaint) state regulators. One approach may be for DOL to issue a temporary exemption for the period beginning on June 9 and ending on a reasonable date for transitioning back to compliance procedures based on prior exemptions.

Countdown to Applicability Date

-367 days	April 8, 2016	Final Rule published
-307 days	June 7	Effective Date – Final Rule officially became law
-277 days	July 7	Technical corrections to BICE, PTE 2016-02 released
-228 days	August 25	District court hearing in DC litigation
-201 days	September 21	District court hearing in Kansas litigation
-165 days	October 27	First FAQs issued by DOL
-157 days	November 4	Decision in DC litigation for DOL
-153 days	November 8	Election Day
-147 days	November 14	Appeal filed in DC litigation
-144 days	November 17	District court hearing in Texas litigation
-133 days	November 28	Decision in Kansas litigation for DOL on preliminary injunction
-94 days	January 6, 2017	HR 355, delaying Final Rule for 2 years, introduced by Rep. Wilson
-89 days	January 11	SEC no-action letter issued on new mutual fund share classes
-87 days	January 13	Second FAQs issued by DOL
-81 days	January 19	Class exemption (PTE) for insurance intermediaries proposed by DOL
-80 days	January 20	Inauguration Day; White House moratorium on regulations not in effect
-66 days	February 3	Presidential memorandum directing DOL study of Final Rule
-61 days	February 8	Decision in Texas litigation for DOL
-60 days	February 9	DOL proposal to delay Applicability Date transmitted to OMB
-52 days	February 17	Decision in Kansas litigation for DOL on summary judgment
-51 days	February 18	End of comment period on proposed insurance intermediary PTE
-47 days	February 22	Appeal filed in Kansas litigation
-45 days	February 24	Appeal filed in Texas litigation by US Chamber; other plaintiffs filed appeals on February 28
-39 days	March 2	60-day delay to Applicability Date proposed by DOL
-38 days	March 3	District court hearing in Minnesota litigation
-24 days	March 17	Comments due on proposed 60-day delay
-6 days	April 4	Applicability Date delayed to June 9
Original Deadline	April 10	Original Applicability Date
-53 days	April 17	Comments due on DOL study of Final Rule
-44 days	April 26	Financial CHOICE bill, subordinating DOL fiduciary rule to an SEC rule, introduced by Rep. Hensarling
-36 days	May 4	Financial CHOICE bill reported out of House committee

-18 days	May 22	June 9 Applicability Date confirmed by DOL; third FAQs and enforcement policy released
-8 days	June 1	Informal request for public comment on standards for broker-dealers and investment advisers issued by SEC Chair Clayton
-1 day	June 8	Financial CHOICE bill passed in House; bills introduced in House and Senate (HR 2823 and S 1321) to rescind and replace Final Rule
New Deadline	**June 9**	**Revised Applicability Date – Final Rule fully applicable; all PTE relief available, with limited transition conditions for financial institutions relying on the BICE and Principal Transaction PTE and deferral of most PTE 84-24 revisions**
+20 days	June 29	RFI for further public comment on Final Rule released by DOL
+40 days	July 19	HR 2823 reported out of House committee
+42 days	July 21	Due date for RFI responses related to January 1, 2018, date
+45 days	July 24	House DOL appropriations bill (HR 3358), which would nullify Final Rule, reported out of committee
+52 days	July 31	5th Circuit argument on appeal of Texas litigation
+55 days	August 3	Fourth FAQs issued by DOL
+59 days	August 7	Due date for substantive responses to RFI
+60 days	August 8	60-day benchmark for 408(b)(2) disclosure updates related to Final Rule
+83 days	August 30	Proposal released to extend transition relief to July 1, 2019
+98 days	September 15	Due date for comments on proposed extension of transition relief
+111 days	September 27	HR 3857 to repeal and replace Final Rule introduced by Rep. Wagner
+126 days	October 12	HR 3857 reported out of House committee
+172 days	November 27	Extension of transition relief released by DOL
+206 days	January 1, 2018	Original expiration date for transition relief
+222 days	January 17	10th Circuit argument on appeal of Kansas litigation
+251 days	February 15	Massachusetts files Scottrade complaint
+278 days	March 13	Decision for DOL by 10th Circuit in Kansas litigation
+280 days	March 15	Decision for plaintiffs by 5th Circuit in Texas litigation
+281 days	March 16	DOL suspends enforcement of Final Rule pending review
+288 days	March 23	Parties voluntarily dismiss DC Circuit appeal of DC litigation
+752 days	**July 1, 2019**	**Revised expiration date for transition relief**

For More Information

For resources and commentary regarding the Final Rule, visit Eversheds Sutherland's dolfiduciaryrule.com.

- Text of and supporting materials for the Proposed and Final Rule
- Pleadings in the pending litigations challenging the Final Rule
- Articles, presentations and client alerts
- Videocasts about the Final Rule

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