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DOL Finalizes Investment Advice Rulemaking

The U.S. Department of Labor (DOL) released this week a new class exemption that would provide relief to registered investment advisers, broker-dealers, banks and insurance companies for the receipt of compensation as a result of providing investment advice, including rollover advice, to ERISA-covered plans and individual retirement accounts (IRAs). Also included in this rulemaking package is new guidance from the DOL on its recent reinstatement of the traditional five-part test when one becomes an investment advice fiduciary.

Here we provide a brief overview of this significant rulemaking.

Here are the key takeaways:

- Under the DOL's five-part test, for advice to constitute "investment advice," a financial institution or investment professional must (1) render advice to the plan as to the value of securities or other property, or make recommendations as to the advisability of investing in, purchasing, or selling securities or other property; (2) on a regular basis; (3) pursuant to a mutual agreement, arrangement, or understanding with the plan, plan fiduciary, or IRA owner, that; (4) the advice will serve as a primary basis for investment decisions with respect to plan or IRA assets; and that (5) the advice will be individualized based on the particular needs of the plan or IRA. If a financial services firm becomes a fiduciary to a plan under this test, then the resulting compensation from that advice would trigger the prohibited transaction restrictions, necessitating an exemption. While there are currently existing exemptions that can be utilized, they cover discrete transactions, whereas the DOL's new class exemption applies broadly, similar to how the DOL's 2016 *Best Interest Contract Exemption* was designed to function (see below on status of that exemption).

- The DOL indicates that advice to take a distribution of assets from a retirement plan is effectively advice to sell, withdraw, or transfer investment assets currently held in the plan, and, therefore, falls within the definition of fiduciary advice, assuming all five parts of the test are satisfied. DOL's treatment of most rollover recommendations as investment advice is a departure from its historical position, but pairs well with its 2016 rulemaking and the Securities and Exchange Commission's Regulation Best Interest. Note, however, that the DOL will not pursue claims for breach of fiduciary duty or prohibited transactions based on rollover recommendations made before the effective date of the new final exemption if the recommendations would not have been considered fiduciary communications under the reasoning of the DOL's historical guidance (*i.e.*, the Deseret Letter).

- The new exemption requires the investment advice to meet the *Impartial Conduct Standards*, namely: a best interest standard; a reasonable compensation standard; and a requirement to make no materially misleading statements about recommended investment transactions and other relevant matters. The exemption includes disclosure requirements, conflict mitigation, and a compliance review. Prior to engaging in a rollover recommended, financial institutions must provide documentation of the specific reasons for the rollover recommendation to the retirement investor, including the reasons it satisfies the best interest standard. This exemption is partly based upon the temporary enforcement policy announced in Field Assistance Bulletin (FAB) 2018-02.

- A financial institution's reliance on the new exemption also requires it to establish, maintain and enforce policies and procedures designed to ensure that they comply with the Impartial Conduct Standards.

- The exemption now includes a self-correction mechanism so that certain technical violations of the exemption's conditions do not cause the total loss of exemptive relief.

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- The exemption does not cover advice arrangements that rely solely on robo-advice; however, the exemption would cover hybrid robo-advice, namely, advice generated by computer models coupled with interaction with an investment professional.

- The DOL's new rulemaking package removes 2016's *Best Interest Contract Exemption and the Class Exemption for Principal Transactions in Certain Assets Between Investment Advice Fiduciaries and Employee Benefit Plans and IRAs*. Moreover, pre-existing prohibited transaction class exemptions that had been amended as part of the 2016 rulemaking (*e.g.*, 75-1, 77-4, 80-83, 83-1, 84-24 and 86-128) have been reinstated and published on the DOL's website in their original form.

- The new exemption will be effective and available to financial institutions beginning 60 days after the date of publication in the Federal Register; however, FAB 2018-02 remains in place for a year to smooth the transition.

Please be on the lookout for our full analysis of this important development after the holidays.