The Fiduciary Rule: New Uncertainty

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The US Department of Labor (DOL) has officially delayed by 60 days the implementation of an Obama Administration regulation (Fiduciary Rule) that would have significantly broadened the ways an investment manager, broker-dealer or other service provider could be considered an investment advice fiduciary to retirement plans under the US Employee Retirement Income Security Act of 1974 (ERISA).

Those service providers in the foreign exchange industry most at risk of becoming investment advice fiduciaries under the Rule are those who discuss their products and services with ERISA fiduciaries or participants of retirement plans, as well as the owners of individual retirement accounts. A noteworthy aspect of the Rule is that sales pitches and other marketing materials can, under certain circumstances, inadvertently create investment advice fiduciary relationships under ERISA. Discussions regarding strategies may also be swept up by the Rule.

Before proceeding with a discussion of the delay, it is important to note that investment managers, such as an overlay manager, may already acknowledge ERISA fiduciary status in written contracts with their clients. However, these managers would likely be agreeing to act as a fiduciary only with respect to the buying and selling of currency products on behalf of their client. The fiduciary status for these types of discretionary relationships are unaffected by the Rule. These investment managers should still examine the applicability of the Rule to them because the Rule could require them to adhere to the stringent ERISA standard of care in respect of the communications that got them hired as the investment manager in the first place.

As previously noted, communications with plan fiduciaries (as either prospective or current clients) about the provider's products and services may very well be ensnared by the Fiduciary Rule's scope come June 9, 2017, necessitating the creation and implementation of compliance policies and controls to guard against entering into non-exempt prohibited transactions.

There are a number of exemptions available to service providers deemed ERISA fiduciaries under the Rule, each of which contain a number of technical requirements (some more onerous than others). One condition of these exemptions is the "Impartial Conduct Standards". Helpfully, the DOL created a phased implementation scheme: (1) from June 9, 2017-December 31, 2017, providers can generally satisfy the exemptions by complying with the Impartial Conduct Standards; and (2) starting January 1, providers will need to adhere to the Impartial Conduct Standards, as well as the numerous other conditions of the applicable exemption.

Impartial Conduct Standards refer to three key behaviours: (1) the investment advice/fiduciary communications are made in accordance with ERISA's duties of prudence and loyalty; (2) the

investment advice fiduciary receives no more than reasonable compensation in connection with the advice, as further described in separate regulations; and (3) the investment advice fiduciary avoids making any materially misleading statements regarding any aspect of the communication, including any conflicts of interest that the investment advice fiduciary may have. Service providers who are investment advice fiduciaries under the Rule should be methodical and detailed in documenting how these criteria were met in its communications with the ERISA plan fiduciary, participant or IRA owner. Moreover, fiduciary investment advisors should identify and mitigate conflicts of interest, including with respect to compensation structures.

Finally, it is important to understand how the Rule is subject to the political winds in the US. The Rule has been delayed because of a directive issued by president Donald Trump in early February for the DOL to re-examine its legal and economic analysis used by the DOL when it devised the final framework of the Rule last year. Substantive changes to the Rule are on the table. The DOL currently has open a comment period that ends on April 17, during which stakeholders are strongly encouraged to submit updated economic data on the costs and savings associated with the Rule, as well fresh ideas on whether and how the Rule should be modified.

From mid-April to the end of the year, the DOL will review the comment letters and take one of three actions: (1) have the Rule and the accompanying exemptions go into full effect on January 1, 2018; (2) revise portions of the Rule and/or exemptions, which could lead to another delay or a battery of streamlined exemptions to ease compliance; or (3) repeal of the Rule. The outcome is in part driven by the approach Alex Acosta, the nominee to head the DOL, takes, once he is confirmed by the Senate, which could happen this month.

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