

The logo consists of the text 'Fi360' in a white, sans-serif font. The 'i' has a dot. The '3' is a simple numeral. The '6' has a loop at the bottom. The '0' is a simple circle. The text is centered within a white square frame.

Fi360

A Broadridge® Company

# 2020 Fi360 Webinar Series – Premier Sponsors



# It's Been a Hot Summer for the Regulation of Advice and There's No Sign of a Cooldown

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# Topics

- Covid-19 Impact
- Standards of Conduct
- Investment Selection
- Continuing Education for Advisors
- What to expect in the months ahead and how to prepare



# Covid-19 Impact on Investors\*

- Big drop in DC plan, IRA assets – February peak to March bottom
- Looming retirement crisis: More than half of unemployed older Americans may be forced into early retirement
- 71% of Americans expect pandemic to affect their retirement plans
  - 15% have delayed retirement; 24% considering delay
- Plans delayed switching plan service providers in 2Q; picked up in 3Q
- 2Q annuity sales down 24%
- Consumers go on spending boom instead of saving
- Half of Gen Z, Millennials say risk tolerance has increased since outbreak



\* Sources (in order of presentation): Center for Retirement Research, Boston College, June 2020; New School Retirement Equity Lab brief (8/5/20); TD Ameritrade survey, June 2020; LIMRA/Secure Retirement Institute (7/14/20); LIMRA, 2Q 2020 compared to 2Q 2019; Bloomberg News (8/19/20); E\*Trade survey (8/19/20).

# SEC Continues [Some] 'Business as Usual'



## SEC Relief

- Staff continue to work remotely
- Extended spring filing deadlines for Form ADV up to 45 days
- Additional relief on filing financial statements -- publicly traded and crowdfunding companies (small business issuers)
- Exemptive relief for muni advisors thru 12/31/20

## SEC Regulation

- Staff continues to examine firms remotely, enforce 12b-1 disclosures
- Requires disclosure of PPP loans by IA firms
- Regulatory alert related to Covid-19 compliance risks (8/12/20)
- Implemented Reg BI, Form CRS rules on time
  - Adds new FAQs on dual registrant status, account changes, titles

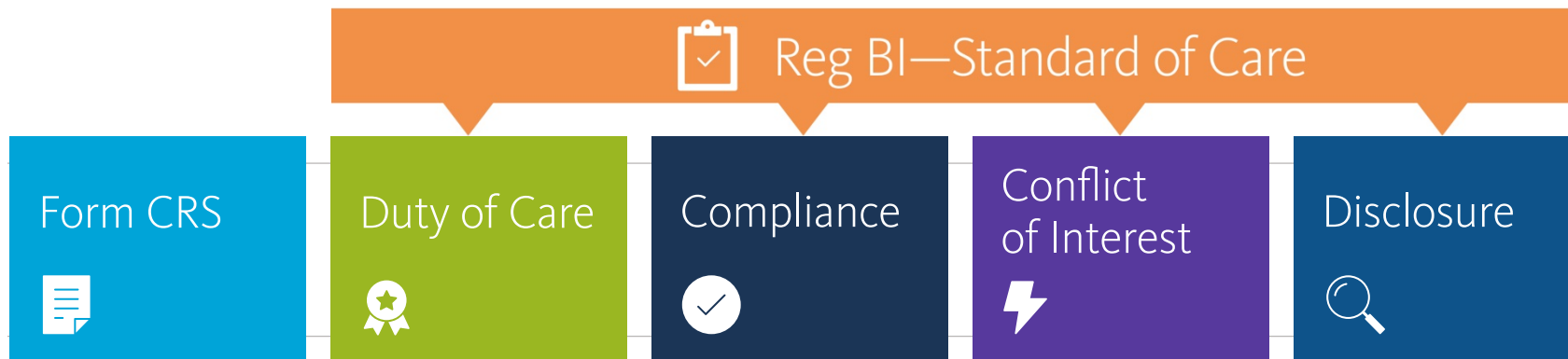


# Standards of Conduct

- SEC's Regulation Best Interest, Form CRS
- DOL's proposed new Prohibited Transaction Exemption for conflicted advice
- State initiatives:
  - Fiduciary rules
  - NAIC's model rule for annuity transactions; and
  - NASAA's proposed "policies and procedures" model rule for state-registered investment advisers



# SEC's Regulation Best Interest - Framework





# SEC Staff Offers Mixed Reviews on Form CRS

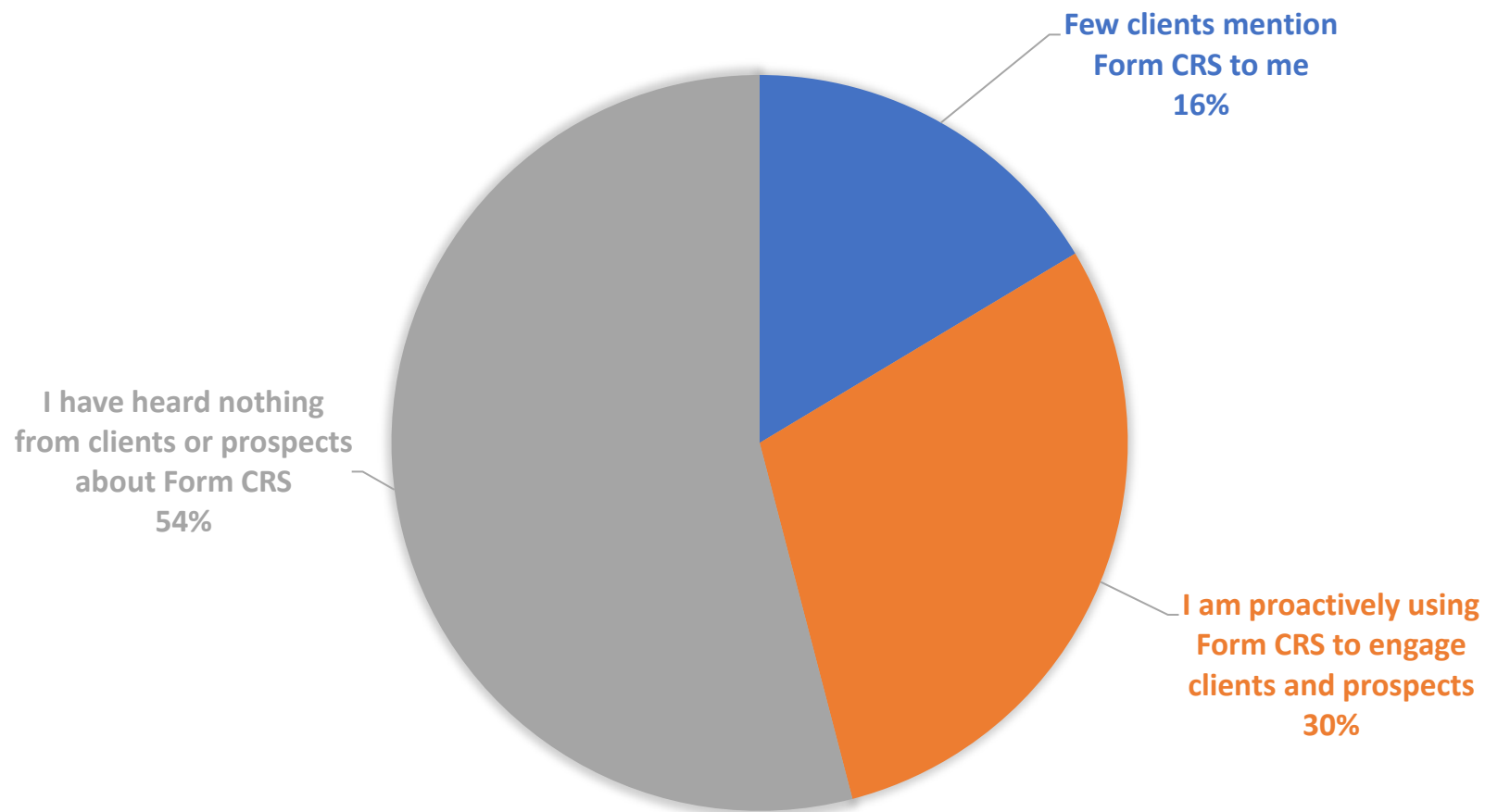
Special SEC review committee\* observed:

- Some content lacks “certain disclosures or could be clearer or otherwise improved.” Committee
  - Did not provide # of firms reviewed or examples
  - Will “engage with firms to share best practices and provide feedback” and
  - Host fall roundtable to share additional thoughts
- In interim, SEC staff recommends reviewing
  - Form CRS instructions
  - Form CRS adopting release
  - FAQs on Form CRS
- OCIE issued 4/7/20 risk alert that it may review Form CRS content, delivery and timing process

\* Statement by Staff Standards of Conduct Implementation Committee, 7/27/20



## POLLING QUESTION 1: HOW ARE CLIENTS REACTING TO FORM CRS?



# SEC's Regulation Best Interest – Firm Readiness\*

## GOVERNANCE

- Governance structures to lead and manage Reg BI and Form CRS compliance requirements

## SUPERVISION

- Inventory of changes
- Updates to Written Supervisory Procedures and Systems (WSPS)
- Identification of technology tools to monitor compliance

## DISCLOSURE – FORM CRS

- Creation
- Use of technology and vendors
- Delivery preferences and methods
- Supervision and audit of delivery

## CONFLICTS OF INTEREST

- Conflict inventories
- Limitations on products
- Eliminating sales contests
- Reviewing and updating disclosures
- Restricting use of the terms “Adviser” and “Advisor”

\* Based upon FINRA Preparedness Review results

# SEC's Regulation Best Interest – Standard of Care

## REG BI OBLIGATIONS

Disclosure 

Duty of Care 

Conflict of Interest 

Compliance 

Additional fiduciary best practices 

## Fi360'S FIDUCIARY PRECEPTS

Account for costs  
Manage conflicts of interest

Diversify to manage risk and return  
Prudently select fiduciary and non-fiduciary service providers  
Control and account for costs

Avoid or manage conflicts of interest

Follow laws and governing documents

Prepare and follow an investment policy statement  
Monitor service providers  
Monitor and assure conformity to fiduciary obligations

- 
- Fiduciary advisors can and should showcase fiduciary best practices
  - Dually registered advisors must clearly delineate fiduciary and non-fiduciary services in each client relationship
  - Non-fiduciary brokers should adhere to the fiduciary principles embedded in Reg BI but must steer clear of practices that require registration under the Advisers Act
-

# DOL's Proposed New PTE for Conflicted Advice

Provisions	Implications
Formally reinstates DOL's five-part test to establish fiduciary accountability	<ul style="list-style-type: none"><li>• This effectively happened in 2018 when the Fifth Circuit vacated the 2016 Fiduciary Rule</li><li>• Handicaps enforcement of fiduciary status</li></ul>
Creates a PTE that provides greater latitude for "investment advice fiduciaries" to receive compensation conflicts	<ul style="list-style-type: none"><li>• Requires acknowledgment of fiduciary status</li><li>• Mirrors the requirements of the BIC Exemption</li><li>• Applies to rollovers and certain principal transactions</li></ul>
Relies upon Impartial Conduct Standards (ICS) to protect investors	<ul style="list-style-type: none"><li>• Adhere to best interest standard</li><li>• Must not subordinate investor interests</li><li>• Receive only reasonable compensation</li><li>• Make no materially misleading statements</li><li>• Establish, maintain, and follow policies and procedures</li></ul>
Includes a "retrospective review" requirement to detect/prevent violations of ICS and PTE	<ul style="list-style-type: none"><li>• Written review, conducted at least annually</li><li>• Certified by financial institution's CEO or equivalent</li></ul>





# DOL's Proposed New "ICS" PTE – Current Status

- 30-day comment period closed August 6, 2020, despite requests from consumer, union, and other groups requesting more time
- A public hearing has been scheduled Sept. 3<sup>rd</sup> on the proposal.
- Rollover provision reversing Advisory Opinion 2005-23A ("Deseret letter") under fire from financial institutions; consumer groups argue that the 5-part test renders investor protections ineffective
- Would become effective 60 days after publication in Federal Register
- Guesstimates of timing
  - Final rule release anywhere from late this September to January
  - Compliance deadline one year after the rule is final



# NAIC Model Rule for Annuity Transactions

NAIC Rule	Regulation Best Interest
Adopted 2/13/20 by NAIC; state-by-state approval required. YTD adopted by Iowa, Arizona.	Effective 6/30/20
Covers annuity transactions by insurance cos. and agents; partial overlap with Reg BI covering variable annuities.	Covers advice on participant rollovers/distributions, investment strategies and securities transactions by brokerage firms and agents
Exempts transactions used to fund ERISA and other federal, state, or church retirement plans; settlements from personal injury litigation; or prepaid funeral contracts.	<u>Exempts</u> advice to nearly all retirement plans except SEP and SIMPLE IRAs; <u>covers</u> advice to individual participant accounts in addition to HSAs, MSAs, 529 plan accounts.
Additional suitability factors: insurance needs, existing annuity/insurance holdings; risk tolerance to accept non-guaranteed elements of annuity	In addition to Reg BI obligations, suitability factors include age, other investments, financial situation and needs, tax status, investment objectives, experience, time horizon, liquidity needs, and risk tolerance.
Compliance with Reg BI or Advisers Act, or comparable state laws, may satisfy NAIC rule.	No equivalent safe harbor under other laws.
Stipulates in Rule text that it does not create a fiduciary obligation.	Adopting release states, “We have declined to subject broker-dealers to a wholesale and complete application of the existing fiduciary standard under the Advisers Act.” However, the Rule text does not disclaim fiduciary status of a broker.



# Other State Initiatives



- Fiduciary rules for brokers pending:
  - NJ, NV
- Massachusetts fiduciary rule enforcement begins 9/1/2020; covers
  - BD firms and agents (RIAs already subject to fiduciary duty)
  - Only transactions, unless broker holds discretion or monitors
    - Also non-brokerage financial advice
    - Infers compensation must be reasonable
- NASAA's proposed "policies and procedures" model rule
  - Proposed 7/2/20; will require state-by-state adoption
  - Mirrors SEC Rule 206(4)-7, or "CCO Rule"
  - Obligations are "inherent to an investment adviser's fiduciary duty"





# Investment Selection

- ESG Investing
- Private Equity in Defined Contribution Plans



# ESG Investments – DOL’s Two-pronged Attack

- Proposed Rule “Financial Factors in Selecting Plan Investments”
  - To confirm that investment decisions must be based solely on financial considerations
  - Sets more stringent selection standards for ESG factor investing and adds documentation to “all things being equal” decision
  - Disqualifies use of ESG mandate in QDIAs
- Letter from EBSA to plan sponsors with ESG options in the plan menu asking for detailed information in a very short time period (e.g. 2 weeks)
- 30-day comment period

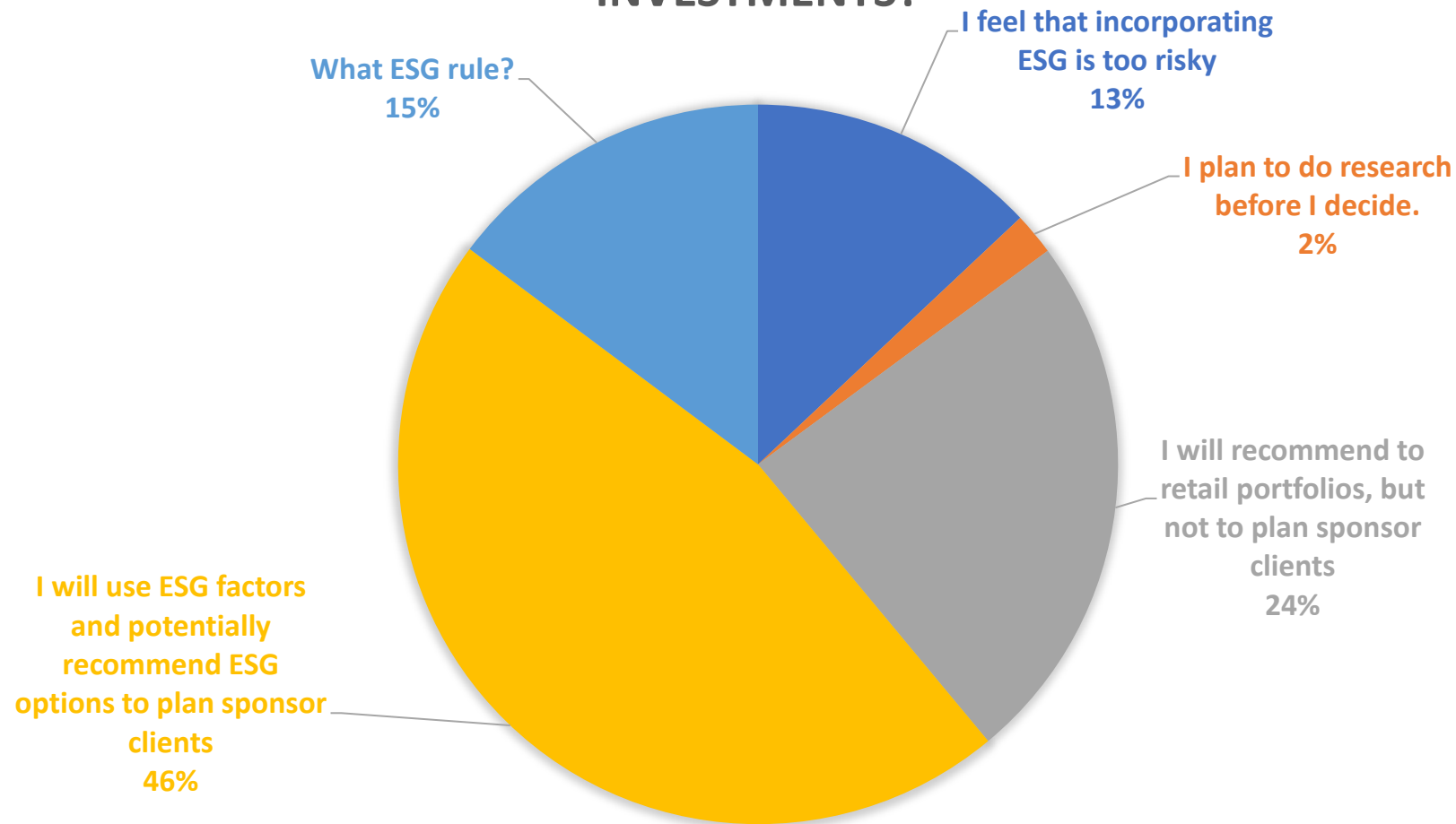


# ESG Investments – Current status of DOL Actions

- 30-day comment period ended July 31
- Comments have been overwhelmingly negative; many faulting a flawed premise that investing using ESG factors detracts from results
- Morningstar comments cited internal research that ESG-focused funds generally have outperformed over the past 1-, 3-, and 5-year periods and noted that the question should be why wouldn't a plan sponsor consider using ESG factors (other than added regulatory burdens)
- DOL has stated that the proposed rule and EBSA letter are unrelated



## POLLING QUESTION 2: IF DOL'S ESG RULE IS ENACTED, WILL YOU BE LESS LIKELY TO CONSIDER ESG FACTORS IN PLAN INVESTMENTS?

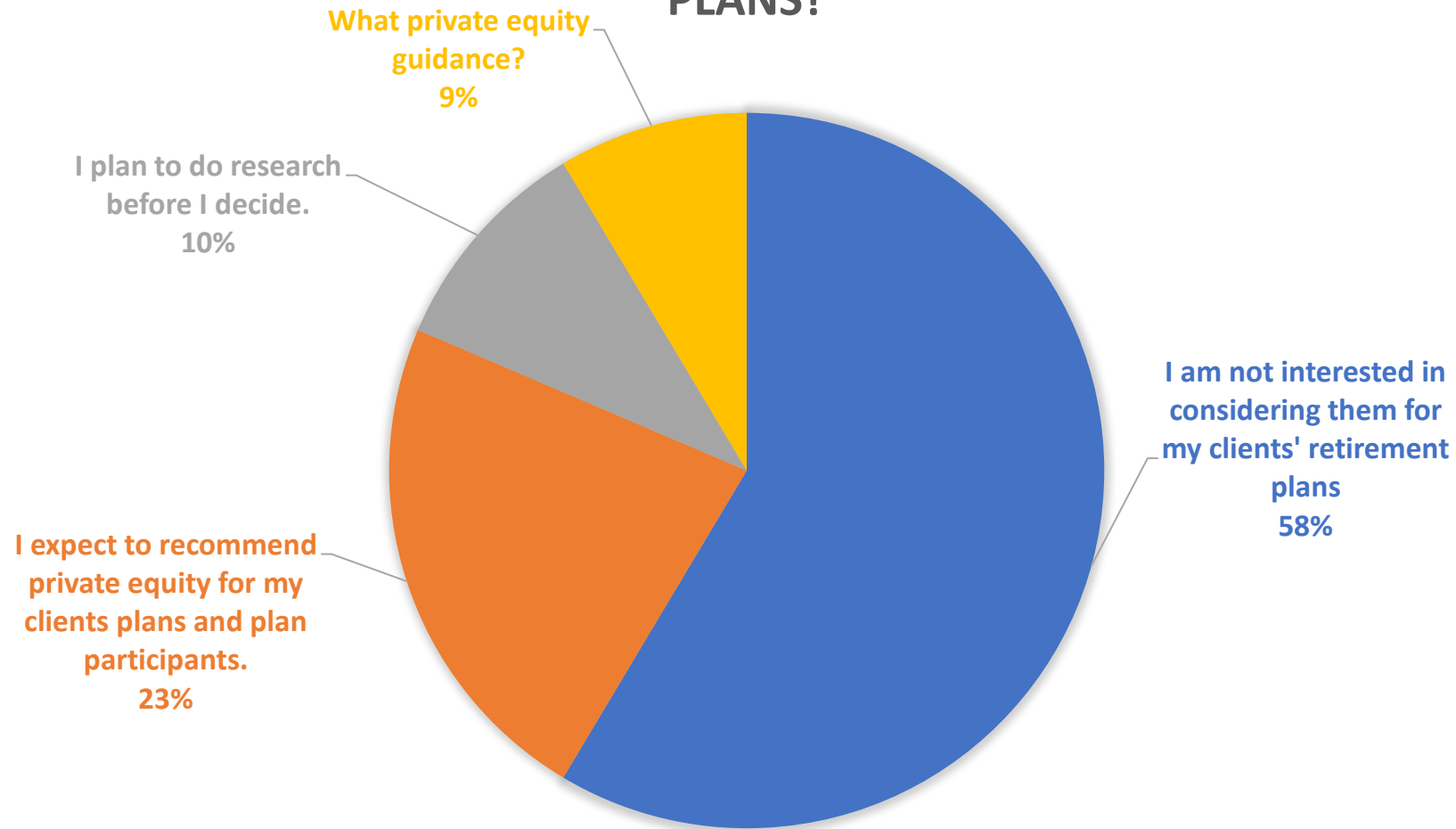


# Private Equity in Defined Contribution Plans

- DOL Information Letter issued June 3, 2020 responds to Pantheon Ventures and Partners Group (developers of private equity investments in collective trust form) about using private equity as a designated investment alternative in an ERISA individual account plan
- Concludes that offering a professionally managed asset allocation fund would not be a fiduciary breach if used in a manner consistent with applicable ERISA standards
- Provides guidance about appropriate selection and monitoring capabilities and practices



# WHAT ARE YOUR THOUGHTS ABOUT USING PRIVATE EQUITY AS A DESIGNATED INVESTMENT ALTERNATIVE IN 401(K) PLANS?



# Continuing Education

- NASAA's model rule proposal to establish a CE program for IARs
  - Pending adoption; would need state-by-state approval
  - 12 hours annual CE
    - 6 hours investments
    - 6 hours ethics or "professional responsibility"
  - Existing FINRA firm element CE, professional designation programs would count (subject to 3<sup>rd</sup> party review)
  - Exempt from CE rule some designations (CFA, CFP, PFS, etc.)
  - Job task survey by NASAA to determine appropriate topics
- CFP Board's Ethics CE requirement focusing on its new Code and Standards





# What to expect after November elections

Regulation	Republican Administration	Democrat Administration
SEC Reg BI	Rule retained; enforcement focus	Rule reinterpreted or replaced to require fiduciary accountability
DOL “ICS” PTE Rule	Rule finalized; possible loosening of rollover provisions	Five-part test replaced; “regular” and “primary basis” deleted
Qualified Plans	Support industry initiatives that include tax breaks for new plans, encourage annuities as DIAs	Automatic 401(k) on federal level; tax credit for lower, middle-income worker contributions
State Initiative	More fiduciary and other investor protection rulemakings, legislation	Potentially less state activity if federal protections increase
Proposed DOL ESG Rule	Withdrawn, revert to existing guidance	Revert to pre-2018, more encouraging, stance on ESG
DOL Private Equity Interpretation Letter	Retained	Reined in by replacement of the five-part test and stronger protections
State Model Laws: CE and Policies & Procedures	Widely adopted	Widely adopted





# Make Impartial Conduct Standards Your Focus

- Establishing Prudence – Methods and Merits
  - Procedural prudence – the extent to which the fiduciary assembled, evaluated, and acted upon pertinent information in a professional manner; i.e., applying sound decision-making methodology
  - Substantive prudence – whether the fiduciary reached objectively sound decisions; i.e., the merits of the decision made



# Demonstrating Prudence: Why? How? What?

- Why? Purpose; decision to be made, for example ...
  - Account type to choose
  - Investment selection
  - Whether to roll a plan distribution to an IRA
- How? Process; choices and the decision-making methodology
  - Alternatives
  - Factors, their relative weights, and the formula to “score” alternatives
- What? Decision; objectively, what should be done

“Why” and “How” demonstrate procedural prudence, using a sound process.  
“What” demonstrates substantive prudence, coming to the right conclusion.



# Attributes of a Profession – The Path We Are On

- Service orientation (recognized obligation to the public)
- Standard of conduct that places clients interests first (fiduciary standard)
- Body of knowledge (sophisticated academic foundation)
- Sanctioning authority (government and/or professional organizations)
- Pathway to the profession (recognized curriculum to become a practitioner)



# Questions



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THANK  
YOU

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