

# The Final DOL Fiduciary Rule and Putting Investors First

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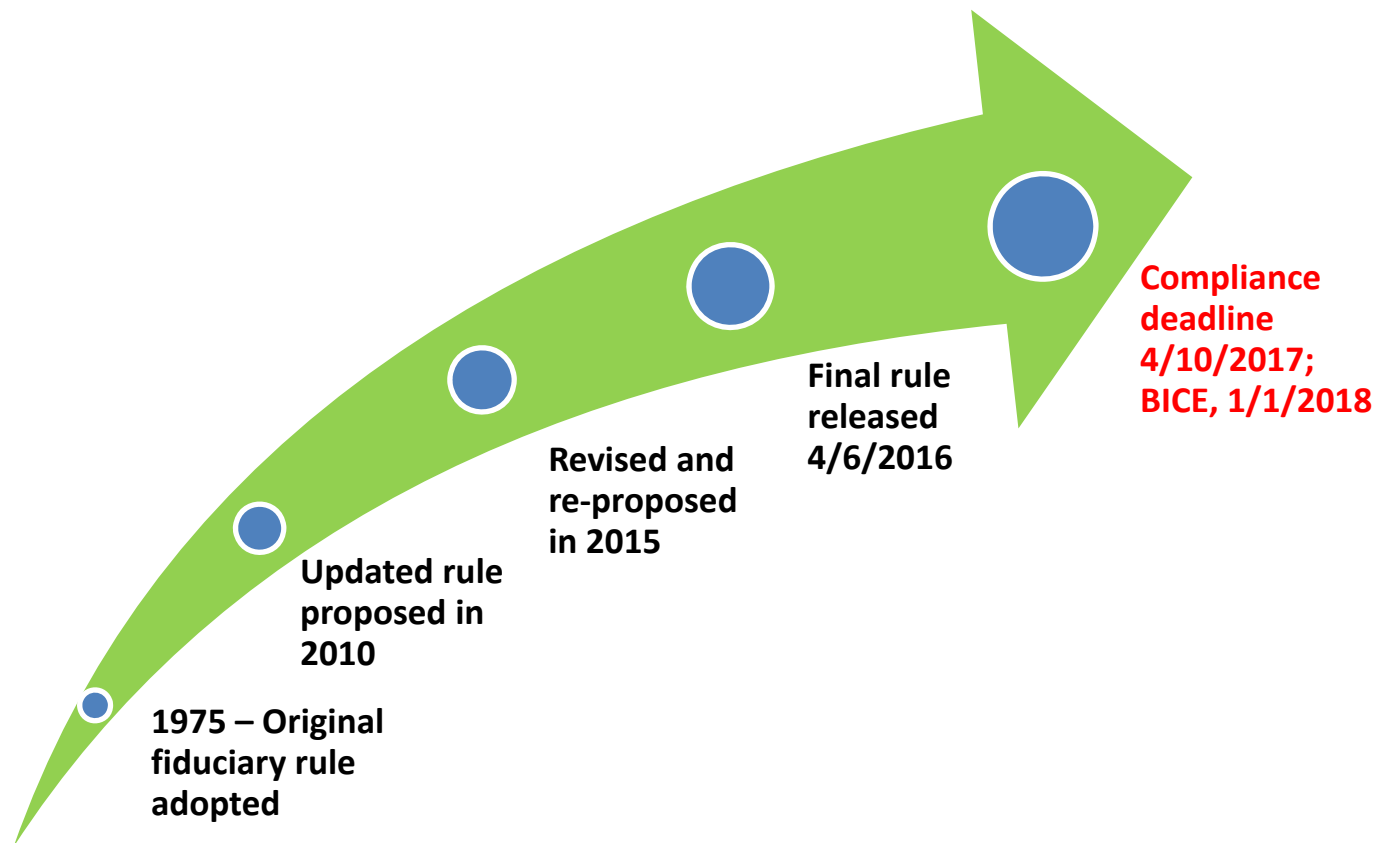
# Topics

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- Overview
  - Chronology
  - What the Rule hopes to accomplish
  - Coverage and exclusions
  - Definition of an investment fiduciary adviser
- Non-fiduciary communications
- Prohibited Transaction Exemptions
- Key Takeaways

# Fiduciary Rule Chronology

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# What the Rule hopes to accomplish

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*“Instead of ensuring that trusted advisers give prudent and unbiased advice in accordance with fiduciary norms, the current regulation erects a multi-part series of technical impediments to fiduciary responsibility.”*

[DOL Notice of Rulemaking, April 2015]

## Fiduciary Rule Coverage

### ERISA Plans

401(k)

Non-ERISA Plans (Covered under IRC sec. 4975)

Archer MSAs

Coverdell education savings accounts (Coverdell ESAs)

Health Savings Accounts (HSAs)

Keogh plans

Savings Incentive Match Plans for Employees (SIMPLEs)

Simplified Employee Pensions (SEPs)

Some 403(b) plans

IRAs (Covered under IRC sec. 4975)

Traditional and Roth IRAs

## Fiduciary Rule Exclusions

529 plans

Certain 403(b) plans

Certain SARSEPs

Sec. 457 plans

Governmental plans

Church plans

Products without an investment component

Term-life insurance

Health insurance

Disability insurance

# Original Fiduciary Adviser Definition

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1. Renders investment advice
2. Receives compensation, direct or indirect
3. Advice is individualized
4. Provided on a regular basis
5. Serves as primary basis for decision-making

This 5-part test narrowed the statutory definition.

# Two Clarifying Questions

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- What is investment advice?
- Who is a fiduciary investment adviser?

# What is Investment Advice?

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- Two types of recommendations that are advice:
  - Advisability of acquiring, holding, disposing of, or exchanging, securities or other investment property or how to invest after a rollover, transfer or distribution from a plan or IRA
  - Recommendation as to management of securities or other investment property
- Advice involves a call to action specific to the recipient; giving rise to fiduciary accountability
- Content, context, and presentation are important



# More About “Management” Advice

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- Investment policies and strategies
- Portfolio composition
- Selection of other investment advisers or managers
- Selection of account arrangements (broker/adviser)
- Plan or IRA rollovers, transfers, or distributions
  - Whether to do so
  - In what amount
  - In what form
  - To what destination

# Fiduciary Investment Adviser

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Paid person(s) who provide, directly or indirectly, investment advice that:

1. Represents/acknowledges acting as fiduciary;
2. Is pursuant to an agreement, arrangement, or understanding that is individualized; or
3. Pertains to the advisability of particular investment or management decisions regarding plan or IRA investment property.

# Important Big Picture Concepts

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- The rule is not just about conflicts
  - Duty of Loyalty (conflicts)
  - Duty of Care (prudence)
- DOL keys in on the term ‘recommendation’
  - Advice is a communication that a person would reasonably view as a suggestion to take a particular course of action; advice = fiduciary
  - Education and other communications without a call to action are non-fiduciary; formerly known as carve-outs
- Appraisals may be subject to fiduciary rulemaking later

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# Non-fiduciary Communications

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1. Platform providers
2. Investment education
3. Counterparty transactions
4. Swaps
5. Plan sponsor employees

# Platform Providers

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- Recordkeepers, TPAs, and the like that make available platforms of investment vehicles
- Must be independent of the plan fiduciary
- State intention to not be a fiduciary, and do not become a functional fiduciary under the rule
- Not limited by plan size
- Not available for plan participants or beneficiaries or IRA accountholders

# Investment Education

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- Involves providing specific types of information
  - Descriptions of investments or plan alternatives without specific recommendations
  - General financial, investment, or retirement information
  - Asset allocation models
  - Interactive investment materials
- May come from sponsor, fiduciary, or others
- Frequency, form, and account types are not limited
- Selection and monitoring of education providers are fiduciary obligations

# Investment Education Limitations

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Asset allocation models and interactive materials may not identify specific investments, unless:

- The alternative is a Designated Investment Alternative (DIA) of a plan
- The alternative is subject to oversight by a plan fiduciary independent of the person who developed or markets the investment alternative or distribution option
- Models/materials identify all comparable alternatives
- Models/materials are accompanied by directions to find more information about the alternatives



# Counterparty Transactions

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- Sales to independent fiduciaries with financial expertise (bank, insurance company, federal or state registered investment adviser, broker-dealer, or other person with at least \$50 million under management or control)
- Inform fiduciary of no intent to provide impartial advice
- Have reason to believe fiduciary is capable of expert evaluation
- Not available for sales directly to IRA accountholders

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# Prohibited Transaction Exemptions

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- Best interest contract exemption (BICE or BIC Exemption)
- Principal transaction exemption
- Existing PTEs

# BICE – Key Features

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- BIC exemption permits
  - Variable and indirect compensation for brokers, firms
  - Binding arbitration for IRA and non-ERISA plan disputes
  - Class action suits available for systemic abuse
- Also covers investment, rollover advice to
  - Participants
  - IRAs
  - Small plans (under \$50M in assets)
- New – indexed annuities included (fixed annuities still covered in PTE 84-24)

# BICE – Requirements

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- Acknowledge fiduciary status
- Adhere to impartial conduct standards
  - Prudent investment advice
  - Charge only reasonable compensation
  - Avoid misleading statements
  - Contract for participants, beneficiaries and IRAs
- Implement policies and procedures reasonably and prudently designed to prevent violations
- Refrain from sales incentives
- Disclose fees, compensation and conflicts of interest
- Notify DOL

# BICE - Limitations

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- Proprietary products subject to ‘finding’
  - Firm makes written finding that products are OK
  - Subject to impartial conduct standards
  - Disclose conflicts
  - Product compensation is reasonable
- Ban on complex, illiquid products removed
  - All product recommendations subject to prudence standard
- Not available to advisors with discretion

# BICE - Grandfathering Provisions

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- For receipt of compensation for pre-rule transactions in which a firm or advisor receives a continuing revenue stream:
  - Recommendations prior to the effective date are permitted as long as they do not result in increased compensation to the firm or advisor
  - Prior transactions must have satisfied ERISA's reasonable compensation standard
  - Any advice provided on grandfathered products after the compliance date must then conform to BICE

# Level-Fee Exemption

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- Available to advisors charging flat fees, AUM
- No BICE required for Level-to-Level rollovers; statutory protection for investors
- Conditions of safe harbor under BICE
  - Acknowledge fiduciary status
  - Subject to impartial conduct standards
  - Document reasons why recommendation in best interest of client



# BICE Blueprint

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- Carefully define an engagement agreement for each client
  - Scope, service expectations and limitations
- Establish Impartial Conduct Standards (serve clients' best interests, reasonable compensation, no misrepresentations)
  - Compliance manual
  - Policies and procedures guide
  - Exceptional product and service provider due diligence
- Avoid/mitigate conflicts of interest
- Disclose fees, compensation, and conflicts of interest
- Maintain thorough documentation

# Key Takeaways

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- It's not just about conflicts – care/prudence are essential
- A communication suggesting a particular course of action is advice – giving paid investment advice makes you a fiduciary
- Those who now routinely operate as level-fee fiduciaries will not be greatly impacted by the Rule
- Conflicted compensation requires BICE – a significant burden
- Products will change dramatically
  - Compensation removed; costs reduced
  - Quality improved
- Fewer advisors, all fiduciaries, competing as professionals

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# Questions

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