

Final Fiduciary Rule

Retirement Security Rule: Definition of an Investment Advice Fiduciary

Robert Gower, Brad Huss &
Yatindra Pandya

May 15, 2024, 10:00 AM PT

Housekeeping Items

Technical Issues

- ★ If you experience technical difficulties during this webinar, please call: 415-277-8050

Issues Accessing Materials

- ★ If you have any issues accessing materials, please call 415-277-8067 or email at webinars@truckerhuss.com

MCLE Credit

- ★ This program is eligible for Continuing Legal Education (CLE) credit. Please contact Franchesca Grande at fgrande@truckerhuss.com to receive a CLE certificate of completion.

Part I: History of the Fiduciary Rule

- ✦ In relevant part, ERISA Section 3(21) defines fiduciary to include any person who “renders investment advice for a fee or other compensation, direct or indirect,” with respect to the plan.
- ✦ Implication of fiduciary status
 - > Duty of Prudence and Loyalty.
 - > Conflicts of Interest.
 - > Prohibited Transactions.
- ✦ Broad statutory definition of “fiduciary”—29 U.S. Code § 1002, in relevant part:
 - > **(21)(A)(ii) he renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so,** or (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan. Such term includes any person designated under section 1105(c)(1)(B) of this title.

Part I: History of the Fiduciary Rule

1975 Regulation: Five-Part Test

★ 29 CFR § 2510.3-21 - Definition of "Fiduciary."

(c) Investment advice.

(1) A person shall be deemed to be rendering "investment advice" to an employee benefit plan, within the meaning of section 3(21)(A)(ii) of the Employee Retirement Income Security Act of 1974 (the Act) and this paragraph, only if:

(i) Such person renders advice to the plan as to the value of securities or other property, or makes recommendation as to the advisability of investing in, purchasing, or selling securities or other property; and

(ii) Such person either directly or indirectly (e.g., through or together with any affiliate)—

(A) Has **discretionary authority or control**, whether or not pursuant to agreement, arrangement or understanding, with respect to purchasing or selling securities or other property for the plan; or

(B) **[1] Renders any advice** described in paragraph (c)(1)(i) of this section **[2] on a regular basis** to the plan pursuant to a **[3] mutual agreement, arrangement or understanding, written or otherwise, between such person and the plan or a fiduciary with respect to the plan**, that such services will serve as a **[4] primary basis for investment decisions with respect to plan assets**, and that such person will render **[5] individualized investment advice to the plan based on the particular needs of the plan** regarding such matters as, among other things, investment policies or strategy, overall portfolio composition, or diversification of plan investments.

Part I: History of the Fiduciary Rule

Issues with 1975 Regulation Over Time

- ✦ In 1975, DOL issued a regulation that made the two-part statutory test of who is an investment advisor into a five-part test, adding requirements that the advice be given on a regular basis, be mutually understood to serve as the primary basis for an investment decision and be individualized for the investor. Ten years later, DOL issued a letter saying that rollover advice was not covered by ERISA.
- ✦ Over time, the DOL concluded “[A]s a result of the five-part test in the 1975 rule, many investment professionals, consultants, and financial advisers have no obligation to adhere to the fiduciary standards in Title I of ERISA or to the prohibited transaction rules, despite the critical role they play in guiding plan and IRA investments.”
- ✦ When the 1975 regulation was issued, the retirement marketplace was dominated by traditional defined benefit plans (as opposed to defined contribution plans).

Part I: History of the Fiduciary Rule

Issues with 1975 Regulation Over Time

- ✦ IRAs were authorized by ERISA in 1974 but were not widely used for decades.
- ✦ 401(k) plans were not in existence when the regulation was issued (first authorized in 1978 with regulations issued in 1984).
- ✦ In 1981, private defined benefit plans held more than twice the assets in private defined contribution plans, and roughly 10 times more than IRA assets.
- ✦ By 2023, the order had reversed:
 - > IRAs held \$13.0 trillion in assets.
 - > Private defined contribution plans held \$8.4 trillion.
 - > Private defined benefit plans held \$3.7 trillion in assets.
- ✦ Retirement Investors are projected to move \$4.5 trillion from defined contribution plans to IRAs from 2022 through 2027.

Part I: History of the Fiduciary Rule

Efforts to overhaul the 1975 Regulation

- ✦ 2010 Proposed Rule and Withdrawal
 - > To address gaps created by dramatic changes in the retirement marketplace, DOL issued its first proposal to mitigate financial conflicts of interest by updating the 1975 rule on October 22, 2010. After significant industry feedback, the October 2010 proposal was withdrawn in September 2011.
- ✦ 2016 Fiduciary Rule
 - > In 2016, the DOL issued a new regulation, two new prohibited transaction exemptions, and amendments to several others to address problems with the five-part test.
 - > The new regulation covered one-time advice, including rollover advice, and required that advisors act in the best interests of plans and participants.

Part I: History of the Fiduciary Rule

Efforts to overhaul the 1975 Regulation

- ✦ The 5th Circuit Vacates Rule
 - > Numerous District courts as well as the 10th Circuit uphold rule, but a challenge in the 5th Circuit resulted in the Rule being vacated. The 5th Circuit stated that DOL improperly untethered fiduciary status from notions of **trust and confidence**, and impermissibly extended protections to IRAs.
 - > The new Trump Administration did not petition for rehearing, or for certiorari to the Supreme Court.

- ✦ In 2020, the DOL released a proposal for a new class prohibited transaction exemption 2020-02, covering rollover advice to IRAs.

Part II: The Proposed Retirement Security Rule

Overview of Regulatory Package Design

- ✦ Proposed Retirement Security Rule (October 31, 2023).

- ✦ Amendments to PTE 2020-02, PTE 84-24, and other PTEs.
 - > Significantly, PTE 2020-02 (Improving Investment Advice for Workers & Retirees) would be expanded to also cover transactions involving pooled employer plans (PEPS), and robo-advice transactions, broadening the reach of the uniform standard.

Part II: The Proposed Retirement Security Rule

Three contexts in which a recommendation is fiduciary investment advice

- ✦ Under the proposed Retirement Security Rule, a person would be an “Investment Advice Fiduciary” if they provide a recommendation for a fee or other compensation in one of the following contexts:
 1. The person either directly or indirectly (e.g., through or together with any affiliate) has **discretionary authority or control**, whether or not pursuant to an agreement, arrangement, or understanding, with respect to purchasing or selling securities or other investment property for **the retirement investor**;

Part II: The Proposed Retirement Security Rule

Three contexts in which a recommendation is fiduciary investment advice

2. The person either directly or indirectly (e.g., through or together with any affiliate) makes investment recommendations to investors on a **regular basis as part of their business** and the recommendation is provided under circumstances indicating that the recommendation is based on the **particular needs or individual circumstances of the retirement investor** and may be relied upon by the retirement investor as a basis for investment decisions that are in the **retirement investor's best interest**; or
3. The person making the recommendation **represents or acknowledges** that they are **acting as a fiduciary** when making investment recommendations.

Part II: The Proposed Retirement Security Rule

Recommendation

- ✦ The phrase “recommendation of any securities transaction or other investment transaction or any investment strategy involving securities or other investment property” means recommendations:
 - > (i) As to the **advisability of acquiring, holding, disposing of, or exchanging**, securities or other investment property, as to **investment strategy**, or as to **how securities or other investment property should be invested** after the securities or other investment property are **rolled over, transferred, or distributed from the plan** or IRA;
 - > (ii) As to the **management** of securities or other investment property, including, among other things, recommendations on **investment policies or strategies, portfolio composition, selection of other persons to provide investment advice or investment management services, selection of investment account arrangements** (e.g., account types such as brokerage versus advisory) or **voting of proxies appurtenant to securities**; and
 - > (iii) As **to rolling over, transferring, or distributing assets from a plan** or IRA, including recommendations as to whether to **engage in the transaction**, the **amount**, the **form**, and the **destination of such a rollover, transfer, or distribution**.

Part II: The Proposed Retirement Security Rule

Industry Response and Criticisms

✦ Same as 2016 rule, the DOL ignored the 5th Circuit decision.

"...commenters err in asserting that this rulemaking is simply a repeat of the 2016 Rulemaking, or in contending that the final rule fails to take proper account of the nature of the relationship between the advice provider and the advice recipient."

✦ Lack of authority of DOL to regulate, especially on IRAs and rollovers.

✦ SEC's Regulation Best Interest and NAIC model regulation of investment advisors solved the problem.

✦ Overly broad definition of "Investment Advice Fiduciary".

Part II: The Proposed Retirement Security Rule

Typical industry response and criticisms

- ✦ May turn routine sales conversations into fiduciary advice (“Hire Me”).
- ✦ Distinction between investment education v. investment advice unclear.
- ✦ No special rule exempting “sophisticated investors” (i.e., large institutional investors), as was seen (and generally well received) in 2016 Rule.
- ✦ “Harmful” to investors (e.g., increased cost, decreased choice).
- ✦ Most industry trade associations, financial services and insurance companies demanded that DOL withdraw the Proposed Rule.

Part III: The Final Retirement Security Rule

Two contexts in which a recommendation is Fiduciary Investment Advice

- ★ The DOL designed the Final Rule to appropriately define an investment advice fiduciary to comport with reasonable investor expectations of **trust and confidence**.

- ★ A person is an “Investment Advice Fiduciary” if they provide a recommendation for a fee or other compensation to a “retirement investor” in one of the two following contexts:
 1. Objective facts and circumstances test.

 2. Acknowledgment of fiduciary status.

Part III: The Final Retirement Security Rule

Two contexts in which a recommendation is Fiduciary Investment Advice

1. The person either directly or indirectly (e.g., through or together with any affiliate) makes professional investment recommendations to investors on a regular basis as part of their business and the recommendation is made under circumstances that would indicate to a reasonable investor in like circumstances that the recommendation:
 - is based on review of the retirement investor's **particular needs** or **individual circumstances**,
 - reflects the **application of professional or expert judgment** to the retirement investor's particular needs or individual circumstances, and
 - **may be relied upon** by the retirement investor as **intended to advance the retirement investor's best interest**; or

Part III: The Final Retirement Security Rule

Two contexts in which a recommendation is Fiduciary Investment Advice

2. If the person **represents or acknowledges** that they are **acting as a fiduciary** under Title I of ERISA, Title II of ERISA, or both with respect to the recommendation, they meet the facts and circumstances test.
- ★ Notably, the Final Rule drops expansion of the discretionary management prong in the Final Rule, which many commenters on the Proposed Rule found confusing.

Part III: The Final Retirement Security Rule

Two contexts in which a recommendation is Fiduciary Investment Advice

- ✦ The DOL added a new defined term of a “retirement investor”.
- ✦ A “retirement investor” means a **plan, plan participant or beneficiary, IRA, IRA owner or beneficiary, plan fiduciary** within the meaning of ERISA section (3)(21)(A)(i) or (iii) and Code section 4975(e)(3)(A) or (C) **with respect to the plan, or IRA fiduciary** within the meaning of Code section 4975(e)(3)(A) or (C) **with respect to the IRA.**

Part III: The Final Retirement Security Rule

Two contexts in which a recommendation is Fiduciary Investment Advice

- ✦ Whether a person has made a “recommendation” is a threshold element in establishing the existence of fiduciary investment advice.
- ✦ For purposes of the Final Rule, whether a recommendation has been made will turn on the facts and circumstances of the particular situation, including whether the communication reasonably could be viewed as a “call to action.”
- ✦ The “call to action” standard intentionally follows the SEC’s framework established in Regulation Best Interest.

Part III: The Final Retirement Security Rule

DOL clarifications (response to concerns)

- ✦ Makes clear that fiduciary status does not extend to sales pitches and casual conversations.
- ✦ Similarly, mere investment information or education, without an investment recommendation, is not treated as fiduciary advice.
- ✦ Specifically, the Final Rule includes a new paragraph (c)(1)(iii) that provides confirmation that sales pitches and investment education can occur without ERISA fiduciary status attaching.

Part III: The Final Retirement Security Rule

Updates to PTE 2020-02

- ✦ PTE 2020-02 provides relief for investment advice related to rollovers from a plan or IRA.
- ✦ Expands PTE 2020-02 to robo-advice and pooled employer plans (PEPs).
- ✦ In streamlining other PTEs, the DOL made them unavailable to investment advice fiduciaries, so PTE 2020-02 is in most circumstances the only option for relief.
- ✦ Requires acknowledgment that financial institutions and their investment professionals are providing fiduciary investment advice to the Retirement Investor and are fiduciaries with respect to the recommendation.
- ✦ Required standard of care—For clarity, the DOL updated the standard of care for financial institutions and their investment professionals to a “Care Obligation” and a “Loyalty Obligation.”

Part III: The Final Retirement Security Rule

Alignment with SEC Regulation Best Interest

- ★ The Final Rule is closely aligned with the SEC's standards under both the Advisers Act and under Regulation Best Interest, which was adopted subsequent to the Chamber opinion and is rooted in fiduciary principles.
- ★ "The Department intends that whether a recommendation has been made will be construed in a manner consistent with the SEC's framework in Regulation Best Interest."
- ★ SEC—whether a recommendation is made turns on the facts and circumstances of the particular situation.
- ★ DOL declines to include a definition of Recommendation in line with SEC approach in Regulation Best Interest.

Part IV: Key Takeaways for Plan Fiduciaries

Sales Pitches and Investment Advice

- ✦ “Hire Me” communications—exception to fiduciary status?
- ✦ “Normal activity of marketing themselves” without making a recommendation is not advice. Where is the line?
 - > Making claims as to the value of its own advisory or investment management services in marketing materials.
 - > Making recommendations to retirement investors on how to invest or manage their savings.
- ✦ Disclaimers in context of Requests for Proposal are not prohibited.
- ✦ “Persons can tout their own services and provide other information (including information about their affiliates' services), but to the extent “hire me” communications include covered investment recommendations, those recommendations are evaluated separately under the provisions of the final rule.”

Part IV: Key Takeaways for Plan Fiduciaries

Investment information or education

- ✦ Expressly carves-out investment information or education absent a recommendation from fiduciary status.
- ✦ Providing educational information and materials such as those described in IB 96–1 will not result in the provision of fiduciary investment advice. IB-96-1 provides examples of four broad categories of information and materials that do not constitute investment advice:
 - > plan information,
 - > general financial and investment information,
 - > asset allocation models, and
 - > Interactive investment materials.

(Whether provided on an individual or group basis, in writing or orally, or via video or computer software.)

Part IV: Key Takeaways for Plan Fiduciaries

Investment information or education

- ✦ Other examples of non-fiduciary investment education.
 - > Safe Harbor 402(f) Notice. The safe harbor notice provides a significant amount of information on rollovers.
 - > A general conversation about retirement planning, such as providing a company's retirement plan options to a retirement investor, would not rise to the level of a recommendation.
 - > General methods and strategies for managing assets in retirement. For example, systemic withdrawal payments, annuitization, guaranteed minimum withdrawal benefits.
- ✦ However, a recommendation to take a distribution, even if it is not accompanied by a recommendation of a specific investment, is a "recommendation."
 - > For example, if an advisors says, "after reviewing your plan, I think you should roll over into an IRA"—that is not investment education.

Part IV: Key Takeaways for Plan Fiduciaries

Sophisticated Advice Recipients

- ✦ Sophisticated Advice Recipients—“Sophisticated Investor.”
- ✦ No carve-out for a “Sophisticated Investor” in the Final Rule.
- ✦ “preferable to retain the facts and circumstances test set forth in this rule for all recommendations.”
- ✦ For example, when a financially sophisticated retirement investor engages in an arm's length transaction with a counterparty . . . it is appropriate to consider whether a reasonable investor *in like circumstances* would rely on the recommendation as intended to advance the investor's best interest.

Part IV: Key Takeaways for Plan Fiduciaries

Call center support activity

- ✦ Most activity will be exempted.
- ✦ Rendering professional investment recommendations on a regular basis must be part of business (so recordkeepers without investment advisory / proprietary fund arms probably exempted).
- ✦ Recommendation must be “based on review of the retirement investor’s particular needs or circumstances.”
- ✦ Recommendation must go so far as a “call to action.”
 - > “Advice providers can just as easily hold themselves out as trusted advisers in phone communications as in other contexts.”
- ✦ Final Rule should be relief for recordkeepers.

Part IV: Key Takeaways for Plan Fiduciaries

Rollovers

- ✦ Updates to PTE 2020-02—harmonize standard with SEC language.
- ✦ Care and loyalty obligations must be honored—this may slow rollovers out of plans, but at the same time go a long way to stopping predatory rollover practices.
- ✦ Small account balances are exempted (not participant driven under statutory framework).
- ✦ Again, rendering professional investment recommendations on a regular basis must be part of business (so recordkeepers without investment advisory / proprietary fund arms may be exempted).

Part IV: Key Takeaways for Plan Fiduciaries

408(b)(2) Disclosures

- ✦ Plan Fiduciaries need to know who is a fiduciary.
- ✦ Plan Fiduciaries have an affirmative duty to keep their eyes open and to take reasonable remedial action when they become aware of actual or potential breaches committed by their fellow fiduciaries.
- ✦ All fiduciaries have potential liability for the actions of their co-fiduciaries.
- ✦ Just because fiduciary advisors do not have to acknowledge status in writing does not mean that Plan Fiduciaries do not have knowledge of such advisor's fiduciary status.

Part IV: Key Takeaways for Plan Fiduciaries

Legal advice not investment advice

- ✦ Recommendations from counsel pertaining to legal advice regarding whether to accept a rollover, whether to accept rollover providers, etc. are legal recommendations, and not fiduciary recommendations.
- ✦ Similarly, tax advice with respect to a rollover recommendation is not a fiduciary recommendation, however, the advisor must take precautions not to cross the line into a “call to action.”
- ✦ (*See generally*, 29 C.F.R. § 2509.75-5 D-1 Q (“attorneys, accountants, actuaries and consultants performing their usual professional functions will ordinarily not be considered fiduciaries” but “if the factual situation in a particular case falls within one of the categories described in” ERISA § 1002(21), “such persons would be considered to be fiduciaries”.)

Part V: Legal Challenges

2018 Fifth Circuit Ruling voiding 2016 Version of the Rule

- ★ In *Chamber of Commerce v. DOL*, the Fifth Circuit Court of Appeals vacated the 2016 version of the Fiduciary Rule in its entirety.
- ★ Section 706(2) of the federal Administrative Procedure Act provides that a federal court reviewing a federal agency action shall—
- ★ (2) hold unlawful and set aside agency action, findings, and conclusions found to be—
 - > (A) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law
 - > (C) in excess of statutory jurisdiction, authority, or limitations, or short of statutory right;
- ★ The Fifth Circuit found that the 2016 Fiduciary Rule was both arbitrary and capricious and in excess of the DOL's statutory authority.
- ★ The Fifth Circuit further found that the 2016 version was an unreasonable interpretation under the long standing deferential standard of review under the Supreme Court decision in *Chevron, USA, Inc. v. Nat. Resources Defense Council*.

Part V: Legal Challenges

Federation of Americans for Consumer Choice Inc. v. DOL

- ✦ On May 2, 2024, a trade association representing insurance agents and agencies that market traditional fixed rate annuities and fixed index annuities as well as several individual insurance agents filed suit in a Texas District Court seeking to vacate the 2024 Fiduciary Rule and the amendment to PTE 84 - 24 in their entirety under the Administrative Procedures Act on the grounds that they are contrary to law and arbitrary and capricious.
- ✦ The plaintiffs also seek preliminary and permanent injunctive relief to prevent the DOL from attempting to enforce the 2024 Fiduciary Rule and amended PTE 84-24.

Part V: Legal Challenges

Federation of Americans for Consumer Choice Inc. v. DOL

- ✦ Citing the Fifth Circuit opinion in *Chamber of Commerce*, plaintiffs contend that, in using the term “fiduciary” in ERISA and the Internal Revenue Code, Congress intended to incorporate the well-established common law meaning that fiduciary status requires the existence of a “special relationship of trust and confidence.”
- ✦ Plaintiffs further contend:
 - > The 2024 Rule’s definition of an investment advice fiduciary is virtually indistinguishable from the 2016 Fiduciary Rule that was struck down by the Fifth Circuit.
 - > The new Rule defines fiduciary investment advice to be coterminous with standard sales practices.
 - > The new Rule turns any financial professional who recommends a product to an investor in the course of rolling over assets from an employer-based ERISA plan to an IRA into a fiduciary with respect to that recommendation.

Part V: Legal Challenges

Federation of Americans for Consumer Choice Inc. v. DOL

- ✦ Plaintiffs also allege that the DOL:
 - > Has deep-rooted misunderstandings and bias against annuities and the insurance sales channel through which they are sold.
 - > Rushed the 2024 Rule through at extraordinary speed and without any substantial consideration of the consequences or the effect it will have on the insurance industry in particular.
 - > Provided an unreasonably short 60-day time period for comments on the proposal.
 - > Held its public hearing in the midst of the 60-day comment period, with the result that interested parties could not review and react to other parties' comments.
 - > Rebuffed multiple requests to allow more time for public comments.

Part V: Legal Challenges

Possible responses to the FACC lawsuit against the DOL

- ✦ DOL took great care to define “Investment Advice Fiduciary” under a facts and circumstances test that indicates a relationship (from investor’s perspective) of trust and confidence.
- ✦ DOL conducted data-driven cost-benefit analysis.
- ✦ The rule will not decrease consumer choice and will lower costs particularly for low and moderate income retirees.
- ✦ Preamble to Final Rule makes clear that sales pitches and casual conversations are not investment advice under the facts and circumstances test.
- ✦ DOL’s regulatory authority over IRAs, including exemptions for prohibited transactions under the IRC, is not as limited as plaintiffs allege.
- ✦ A joker in the deck is whether the Supreme Court will overturn *Chevron* deference that protects reasonable agency interpretations of statutes.

Contact

- ✦ Robert Gower, Esq.
Trucker ♦ Huss, APC
135 Main Street, 9th Floor
San Francisco, CA 94105
(415) 788-3111
rgower@truckerhuss.com
www.truckerhuss.com
- ✦ Yatindra Pandya, Esq.
Trucker ♦ Huss, APC
135 Main Street, 9th Floor
San Francisco, CA 94105
(415) 788-3111
ypandya@truckerhuss.com
www.truckerhuss.com

- ✦ Brad Huss, Esq.
Trucker ♦ Huss, APC
135 Main Street, 9th Floor
San Francisco, CA 94105
(415) 788-3111
bhuss@truckerhuss.com
www.truckerhuss.com

Disclaimer

- ★ These materials have been prepared by Trucker ♦ Huss, APC for informational purposes only and constitute neither legal nor tax advice
- ★ Transmission of the information is not intended to create, and receipt does not constitute, an attorney-client relationship
- ★ Anyone viewing this presentation should not act upon this information without first seeking professional counsel
- ★ In response to IRS rules of practice, we hereby inform you that any federal tax advice contained in this writing, unless specifically stated otherwise, is not intended or written to be used, and cannot be used, for the purpose of (1) avoiding tax-related penalties or (2) promoting, marketing or recommending to another party any tax-related transaction(s) or matter(s) addressed herein