

Employee Benefit ■ Plan Review

Department of Labor Proposes to Amend and Resurrect the Fiduciary Rule

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In the wake of the 2018 decision by the U.S. Court of Appeals for the Fifth Circuit in *Chamber of Commerce v. U.S. Department of Labor*, which vacated the U.S. Department of Labor's (DOL) fiduciary rule, the DOL has once again issued proposed rules¹ in its longstanding effort to clarify the scope of the duty of a person who renders "investment advice for a fee or other compensation" for purposes of defining a "fiduciary."

FIDUCIARY STATUS

It is no surprise that the DOL continues to seek modifications to its regulations that relate to fiduciary standards for individuals providing investment advice, which date back to 1975. The DOL's proposed rule broadens its application beyond the fiduciary rule to impose fiduciary status on many previously excluded persons, as the DOL has consistently indicated its view that participants need greater protections for the investment advice they receive with respect to retirement plan assets, including rollovers.

Significantly, in addition to the proposed rules, the DOL also released proposed amendments to class prohibited transaction exemptions (PTEs) available to fiduciaries providing investment advice.

Over the past several years, the DOL has continuously worked to revamp fiduciary regulations first released in 1975, when defined benefit plans were prevalent and 401(k) plans were uncommon. A DOL Fact Sheet² covering the proposed rules outlines the DOL's primary goal for a "new definition of an investment advice fiduciary to better protect retirement investors who make decisions about their retirement savings based on advice they receive."

The DOL is also proposing amendments to prohibited transaction exemptions so that fiduciaries who use them must follow consistent and protective compliance requirements, including an obligation to act in retirement investors' best interest.

FIDUCIARY TEST

Under the Employee Retirement Income Security Act of 1974 (ERISA), an individual becomes a fiduciary to the extent that they render investment advice (or have the authority to do so) for a fee or other direct or indirect compensation with respect to any moneys or other property of a benefit plan. A fiduciary has various core duties including, among others, the duty of care, loyalty to plan participants and beneficiaries, prudence in exercising responsibility, and avoiding prohibited transactions and

conflicts of interest. It is a significant designation that comes with personal liability.

The current DOL regulations provide a five-part test to interpret when a person would be considered a fiduciary based on the rendering of “investment advice for a fee.”³ The proposed rules change that five-part test to a two-part test such that a person now will be a fiduciary if they:

- Provide investment advice or make an investment recommendation to a retirement investor (e.g., a benefit plan participant, an IRA owner, a benefit plan administrator) for a fee or other compensation, and
- If the person makes investment recommendations on a regular basis as part of their business and the recommendation is provided under circumstances in which it can be inferred that the retirement investor may rely upon it for investment decisions that are in the retirement investor’s best interest.

The DOL opines that these updates are “designed to ensure that ERISA’s fiduciary standards uniformly apply to all advice that retirement investors receive concerning investment of their retirement assets in a way that ensures that retirement investors’ reasonable expectations are honored when receiving advice from financial professionals who hold themselves out as trusted advice providers.”

OTHER CHANGES

It is important to note that other changes include the following:

- One-time recommendations relating to rollovers of plan assets from an employer-sponsored retirement plan to an IRA or annuities would be considered “investment advice” if other parts of the test are met, and
- Amendments to several PTEs so that fiduciaries who use them must follow rigorous compliance requirements including an obligation to act in retirement investors’ best interest.

There are several definitional changes that highlight the DOL’s intent to expand the coverage of the fiduciary rule. The DOL’s proposal is consistent with other regulatory efforts to update rules relating to financial professionals that provide investment advice or recommendations. In 2019, the U.S. Securities and Exchange Commission (SEC) issued its “Regulation Best Interest,” which established a best interest standard applicable to broker-dealers when recommending any securities transaction or investment strategy involving securities to retail customers.

The SEC also issued guidance in 2019 reaffirming and clarifying the fiduciary duties of investment advisers under the Investment Advisers Act. The DOL’s proposal appears to be an effort to clarify and better coordinate ERISA fiduciary standards with the SEC’s 2019 Regulation Best Interest to better protect the qualified assets of participants and beneficiaries.

The DOL’s preamble and media headlines suggest that the proposed rule targets junk fees relating to retirement plans. However, it appreciably understates the potential scope of the proposal which threatens to impose significant changes to the

way broker-dealers, institutional asset managers, insurance agents, and other financial firms who market retirement products conduct their businesses.

CONCLUSION

It is unclear whether the DOL’s most recent effort to clarify and broaden fiduciary standards will stick, and a vigorous comment period and litigation are likely to follow. However, it would be prudent for anyone who provides investment advice, and who may now be an ERISA fiduciary, to assume and be prepared for its implementation. 🌟

NOTES

1. <https://www.dol.gov/sites/dolgov/files/ebsa/temporary-postings/retirement-security-rule-definition-of-an-investment-advice-fiduciary.pdf>.
2. <https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/fact-sheets/retirement-security-proposed-rule-and-proposed-amendments-to-class-pte-for-investment-advice-fiduciaries#:~:text=The%20proposal%20states%20that%20investment,confidence%20in%20the%20advice%20provider.#:~:text=The%20proposal%20states%20that%20investment,confidence%20in%20the%20advice%20provider.>
3. Under the five-part test, a person will be an “investment advice fiduciary” if such person (1) renders advice to a plan as to the value of securities or other property or makes 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 or plan fiduciary that (4) the advice serves as a primary basis for investment decisions with respect to such plan assets and (5) the advice will be individualized based on the particular needs of the plan.

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