The Asset Management Industry
SERVING INDIVIDUAL INVESTORS
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DOL Proposes Amendments to Investment Advice Fiduciary Regulation, Including Revised Definition of Investment Advice Fiduciary and Amendments to PTEs

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TO: ICI Members
Bank, Trust and Retirement Advisory Committee
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Investment Advisers Committee
Operations Committee
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SEC Rules Committee
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Disclosure
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Operations
Pension RE: DOL Proposes Amendments to Investment Advice Fiduciary Regulation, Including Revised Definition of Investment Advice Fiduciary and Amendments to PTEs

On October 31, 2023, the Department of Labor (DOL) released its long-awaited new regulatory package on fiduciary investment advice.[1] The package includes a proposal to amend the regulation defining who is a "fiduciary" under section 3(21) of ERISA and section 4975(e)(3) of the Internal Revenue Code ("Code") as a result of providing investment advice to a retirement investor. The package also includes proposed amendments to prohibited transaction exemptions (PTEs) 2020-02, 84-24, 75-1, 77-4, 80-83, 83-1, and

86-128).[2] As a general matter, the proposed definition of fiduciary advice sweeps very broadly, and the PTE amendments are intended to force most advice fiduciaries to rely on PTE 2020-02 to provide advice.

Comments on the proposed amendments currently are due by January 2, 2024. DOL intends to hold a public hearing approximately 45 days after the proposals' November 3 publication date (likely mid-December, before comment letters are due). ICI, together with 17 other organizations, submitted a joint trade letter (attached at the end of this memo) to urge DOL to extend the comment period and to hold the hearing only after the comment period has closed.[3]

Background

As a reminder, following the Fifth Circuit's 2018 vacatur[4] of the Obama era fiduciary rulemaking package (the "2016 Rule"),[5] DOL reinstated the 1975 fiduciary advice regulation's 5-part test in 2020.[6] Under the 5-part test (described in 29 CFR §2510.3-21(c)(1)), a person is a fiduciary only if they: (1) render advice as to the value of securities or other property, or make 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 a plan fiduciary that (4) the advice will serve as a primary basis for investment decisions with respect to plan assets, and that (5) the advice will be individualized based on the particular needs of the plan. In conjunction with the reinstatement, DOL also proposed and then finalized PTE 2020-02.[7] In the preamble to PTE 2020-02, DOL provided commentary regarding its updated interpretations of the 5-part test. DOL provided additional guidance regarding the application of the 5-part test in the form of FAQs issued in April 2021.[8]

In February 2023, a US District Court in Florida issued a ruling vacating DOL's interpretation articulated in the FAQ guidance, regarding when in the context of a rollover recommendation, an advice provider meets the regulatory 5-part test and is therefore considered a fiduciary under ERISA.[9] In addition to this lawsuit, another challenge to DOL's 2020 interpretation of the 5-part test, as articulated in the preamble to PTE 2020-02, is currently pending in a Texas federal court.[10] On November 2, 2023, the court in the Texas case granted the plaintiff's motion for leave to file a supplemental brief to show that this new proposal makes it clear that DOL's purpose and intent "is to ensure that every financial professional who sells an investment product to a Retirement Investor is deemed to be a fiduciary under ERISA and the Code."[11]

Proposed Amendment to the Definition of Investment Advice Fiduciary

Like the 2016 Rule, the proposal would significantly broaden the definition of who would be considered an investment advice fiduciary under paragraph (c) of the regulation, by effectively eliminating the regular basis, primary basis, and mutual agreement prongs of the current 5-part test as we know them. The proposal is intended to cover one-time recommendations (including rollover recommendations) if the elements of the proposed definition are satisfied.

Functional Definition

Under the proposed definition, a person would be an investment advice fiduciary under Title I and Title II of ERISA if:

1. The person provides investment advice or makes an investment recommendation to a

retirement investor (i.e., a plan, plan fiduciary, plan participant or beneficiary, IRA, IRA owner or beneficiary or IRA fiduciary)[12] [paragraph (c)(1)];
2. The advice or recommendation is provided "for a fee or other compensation, direct or indirect" as stated in ERISA §3(21)(A)(ii) [paragraph (e)]; and
3. The person makes the recommendation in one of the following contexts:
    a. 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 [paragraph (c)(1)(i)];
    b. 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 [paragraph (c)(1)(ii)]; or
    c. The person making the recommendation represents or acknowledges that they are acting as a fiduciary when making investment recommendations [paragraph (c)(1)(iii)].

The proposed amendments also include new provisions addressing the effect of written disclaimers of fiduciary status, the meaning of the statutory phrase "for a fee or other compensation, direct or indirect,"[13] and several new defined terms. The preamble provides more color on many aspects of the proposal, such as the meaning of "recommendation" and the three different contexts that result in fiduciary status for advice.

Three Contexts for Recommendations

As described above, the proposal contemplates three different contexts in which recommendations would be considered fiduciary advice.

Context 1: Discretionary Investment Authority

In regard to the first context (described in amended paragraph (c)(1)(i)), where an investment professional has discretionary authority or control with respect to investments, the proposal is nearly identical to the current definition.[14] Notably, however, the proposal would expand this category to cover discretionary authority or control with respect to purchasing or selling any investment property of the retirement investor, rather than just investment property of the plan (or IRA) itself.[15]

Context 2: Facts and Circumstances Determination

The second context (described in amended paragraph (c)(1)(ii)), is essentially the replacement test for the 5-part test, stripped of the current formulations of the "regular basis," "primary basis," and "mutual agreement" prongs.

To be considered fiduciary advice, the current 5-part test requires that the person provides advice to the plan "on a regular basis." The proposal's second context would instead capture individuals who make investment recommendations to investors "on a regular basis as part of their business." DOL explains in the preamble that this "updated regular basis requirement" would avoid sweeping so broadly as to cover, for example, human resource

employees of a plan sponsor.[16] As DOL explains, with this change, the definition would not automatically exclude one-time advice from treatment as fiduciary investment advice.

> By limiting the scope of those who may be an investment advice fiduciary to those who make investment recommendations as a regular part of their business, the Department believes that the proposed definition is appropriately tailored to those advice providers in whom retirement investors may reasonably place their trust and confidence. Whether someone gives investment recommendations on a regular basis as part of their business is an objective test based on the totality of facts and circumstances. [17]

The current 5-part test also requires a "mutual agreement" or "understanding" that the advice will serve as "a primary basis" for the investor's investment decision. The proposal's second context would replace these two prongs with a requirement that the advice be 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." [Paragraph (c)(1)(ii).]

DOL opines that the prior standard "over time has encouraged investment professionals to hold themselves out as trusted advisers while disclaiming fiduciary status in the fine print," and the revision will focus on "a reasonable understanding of the nature of their relationship."[18] DOL explains in the preamble that in determining whether the revised requirement is met, it intends to examine the ways investment advice providers market themselves and describe their services, including the titles they use.

> In the Department's view, an investment advice provider's use of such titles [such as financial consultant, financial planner, and wealth manager] routinely involves holding themselves out as making investment recommendations that will be based on the particular needs or individual circumstances of the retirement investor and may be relied upon as a basis for investment decisions that are in the retirement investor's best interest. [19]

DOL requests comments on whether particular titles convey that individualized recommendations are being provided (and if not, why such titles are used), and "whether other types of conduct, communication, representation, and terms of engagement of investment advice providers should merit similar treatment."[20]

Context 3: Fiduciary Representation or Acknowledgement

The third context (described in amended paragraph (c)(1)(iii)), where a person making the recommendation represents or acknowledges that they are acting as a fiduciary, is not in the current definition, but was included in the 2016 Rule.[21] In the preamble, DOL expounds that this context is not limited to representations of ERISA fiduciary status, but rather includes representations of any fiduciary status (e.g., under state or other federal law).

> [This context] is not limited to the circumstances in which the person specifically represents that they are a fiduciary for purposes of Title I or Title II of ERISA, or specifically cites any particular statutory provisions. It is enough that the investment advice provider told the retirement investor that the investment advice or investment recommendations were or will be made in a fiduciary

capacity. As with the other contexts identified in proposed paragraph (c)(1), this is intended to align fiduciary status with the retirement investor's reasonable expectations. A retirement investor who is told by a person that the person will be acting as a fiduciary reasonably and appropriately places their trust and confidence in such a person. [22]

Written Disclaimers of Fiduciary Status

The proposed definition also includes a new provision (paragraph (c)(1)(v)) providing that written statements disclaiming fiduciary status "will not control to the extent they are inconsistent with the person's oral communications, marketing materials, applicable State or Federal law, or other interactions with the retirement investor." Language in the preamble suggests that this provision would not limit a discretionary fiduciary's ability to define the parameters of the discretionary relationship.[23] It does appear, however, that if a firm's (or its affiliate's) marketing materials suggest a fiduciary relationship, then a disclaimer could not be used to define the relationship otherwise.

Covered Advice and Recommendation

The proposal's definition of investment advice in paragraph (c)(1) requires that there be a "recommendation of any securities transaction or other investment transaction or any investment strategy involving securities or other investment property." This phrase is defined in paragraph (f)(10), using language that almost exactly tracks language in the 2016 Rule.[24] The phrase includes recommendations:

1. As to the advisability of acquiring, holding, disposing of, or exchanging, securities or other investment property,[25] 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 [paragraph (f)(10)(i)];
2. 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)[26] or voting of proxies appurtenant to securities [paragraph (f)(10)(ii)]; and
3. 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 [paragraph (f)(10)(iii)].

One change from the language in the 2016 Rule is the inclusion of the phrase "as to investment strategy" in the category described in (f)(10)(i). Citing to the SEC's Regulation Best Interest release, DOL states that it "intends to interpret 'investment strategy' broadly, to include 'among others, recommendations generally to use a bond ladder, day trading . . . or margin strategy involving securities, irrespective of whether the recommendations mention particular securities.'"[27]

Like the 2016 Rule, the proposal (in both paragraphs (f)(10)(i) and (f)(10)(iii)) covers recommendations concerning the investment of securities to be rolled over or otherwise distributed from a plan or IRA. This codifies the position DOL articulated in both the 2016 Rule and the preamble to PTE 2020-02,[28] in which it officially withdrew DOL Advisory Opinion 2005-23A (the "Deseret Letter").[29] In the preamble, DOL explains its position that

in most cases, a recommendation regarding investments after a rollover "involves an implicit recommendation to the participant or beneficiary to engage in the rollover, transfer, or distribution," and even in the rare circumstance in which there is no implicit recommendation to rollover, advice on how to invest assets currently held in an ERISA-covered plan would fall under the statutory definition, "inasmuch as the assets at issue are still held by the plan."[30] DOL also clarifies that recommendations on distributions or recommendations to entrust plan assets to a particular IRA provider would be covered by the proposed definition, and, more specifically, would be covered by Title I of ERISA, including the enforcement provisions of section 502(a).[31] Similarly, a recommendation that involves moving assets out of a plan or IRA and into an account not covered by either Title I or II of ERISA, could still be advice under Title I or II.[32]

As in the 2016 Rule, under the second category of recommendation described above (paragraph (f)(10)(ii)), the specific reference to "other" persons in the context of recommending someone to provide investment advice or investment management services, appears to be an attempt to clarify that advisers can promote their own advice or management services (i.e., the "hire me" situation) without it being considered fiduciary advice. In the preamble, DOL confirms that "[t]outing the quality of one's own advisory or investment management services would not trigger fiduciary obligations."[33]

However, DOL cautions that a recommendation to "hire me" could cross the line into fiduciary advice if coupled with a recommendation of how to invest or otherwise manage retirement assets. In this regard, DOL states that "when a recommendation to 'hire me' effectively includes a recommendation on how to invest or manage plan or IRA assets (e.g., whether to roll assets into an IRA or plan or how to invest assets if rolled over), that recommendation would need to be evaluated separately under the provisions in the proposed regulation."[34]

Unlike the 2016 Rule, the proposal's definition in paragraph (f)(10)(ii), adds a reference to the voting of proxies appurtenant to securities. DOL explains that since the exercise of ownership rights is a fiduciary responsibility, advice on the exercise of those rights is fiduciary advice, provided the conditions of the rule are met. DOL provides some clarification on the application of rule in this context, explaining that:

> guidelines or other information on voting policies for proxies that are provided to a broad class of investors without regard to a client's individual interests or investment policy and that are not directed or presented as a recommended policy for the plan or IRA to adopt, would not rise to the level of a covered recommendation under the proposal. Similarly, a recommendation addressed to all shareholders in an SEC-required proxy statement in connection with a shareholder meeting of a company whose securities are registered under Section 12 of the Exchange Act, for example, soliciting a shareholder vote on the election of directors and the approval of other corporate action, would not, under the proposed rule, constitute fiduciary investment advice from the person who creates or distributes the proxy statement. [35]

DOL does not include appraisals, fairness opinions, or similar statements as to the value of securities or other property in the categories of covered advice, as it did in its 2015 proposal. Rather, like the 2016 Rule, DOL states that valuations will be considered in a future separate rulemaking.[36]

Definition of Recommendation

Unlike the 2016 Rule, the text of the proposal does not define the term "recommendation" itself.[37] The preamble indicates that "[f]or purposes of the proposed rule, the Department views a recommendation as a communication that, based on its content, context, and presentation, would reasonably be viewed as a suggestion that the retirement investor engage in or refrain from taking a particular course of action"—which essentially is identical to the definition from the 2016 Rule.[38] After this broad articulation of what is a recommendation, DOL also explains in the preamble that it "intends to take an approach similar to that taken by the SEC and FINRA in the broker-dealer context," and "would consider a recommendation for purposes of the SEC's Regulation Best Interest as a recommendation for purposes of this proposed regulation."[39] In that regard, the preamble notes that, for purposes of determining under Regulation Best Interest whether a recommendation has been made, the SEC has stated that relevant factors include whether the communication "reasonably could be viewed as a 'call to action'" and "reasonably would influence an investor to trade a particular security or group of securities."[40] This standard as described in the Regulation Best Interest release appears to contemplate more than a mere "suggestion."

DOL includes a number of clarifying points in the preamble which were included in the text of the 2016 Rule, based on existing FINRA and SEC guidance:

- Whether a recommendation has been made is an objective rather than subjective inquiry.
- The more individually tailored the communication is to a specific advice recipient or recipients, the more likely the communication will be viewed as a recommendation. DOL cautions that "the fact that a communication is made to a group rather than an individual would not be dispositive of whether a recommendation exists."[41]
- Providing a selective list of securities to a particular advice recipient as appropriate for that investor would be a recommendation even if no recommendation is made with respect to any one security.
- A series of actions that individually may not constitute a recommendation, may amount to a recommendation when considered in the aggregate.[42]

No Carveouts or Exclusions, Including for Counterparties, Swaps, Platform Providers and PEPs

While the scope of the proposed definition is just as expansive as the 2016 Rule, the proposal does not incorporate important carveouts from the 2016 Rule. The 2016 Rule included exclusions for certain activities that, by themselves, would not be considered fiduciary advice, except in cases where the advice provider represents or acknowledges fiduciary status.[43] It also outlined four different types of activity that will not be considered a "recommendation."[44]

One important exclusion was for "transactions with independent fiduciaries with financial expertise," intended to cover advice to a fiduciary of a plan or an IRA who is independent from the advice provider, with respect to an arm's length sale, purchase, loan, exchange, or other transaction related to the investment of securities or other property. DOL declined to include a similar exclusion in this proposal, explaining that "[t]o the extent counterparties wish to avoid fiduciary status, they can avoid structuring their relationships to fall within the circumstances described in [proposed paragraph (c)(1)(ii)]."[45] Further, in the context of "wholesaling" activity,

> the Department believes that communications to financial intermediaries would typically fall outside the scope of proposed paragraph (c)(1)(ii) because they

> would not involve recommendations based on the particular needs or individual circumstances of the plan or IRA serviced by the intermediary…. In general, however, the Department envisions that proposed paragraph (c)(1)(ii) would apply broadly to recommendations to plan and IRA fiduciaries acting on behalf of plans and IRAs. [46]

The 2016 Rule also included an exclusion for swap dealers, security-based swap dealers, major swap participants, security-based major swap participants, and swap clearing firms who make recommendations to plans. Here, DOL declined to include an explicit exclusion in the proposal. Instead, DOL states that:

> [t]he disclosures required of plans' counterparties under the business conduct standards would not generally constitute a ''recommendation'' as defined in the proposal, or otherwise compel the dealers or major participants to act as fiduciaries in swap and security-based swap transactions... [47]

DOL warned, however, that dealers or major participants in swaps or security-based swaps could cross the line into fiduciary advice if (in addition to providing the mandatory disclosures to plans required under applicable business conduct standards) they choose to make specific recommendations to plan clients.[48]

The 2016 Rule had included an exception for platform providers, described as marketing or making available to a plan fiduciary, without regard to the individualized needs of the plan, a platform or similar mechanism from which a plan fiduciary may select or monitor investment alternatives, including qualified default investment alternatives, into which plan participants may direct the investment of their accounts.[49] The proposal does not include a similar exception. In the preamble, DOL notes that platform providers may provide advice in connection with their platform offerings or they may simply provide general financial information, such as historical performance of the investments available on the platform. The preamble explains that, to determine whether a platform provider is providing advice:

> the inquiry may turn on whether the provider presents the investments on the platform as having been selected for and appropriate for the investor (i.e., the plan and its participants and beneficiaries). In this regard, platform providers who merely identify investment alternatives using objective third-party criteria (e.g., expense ratios, fund size, or asset type specified by the plan fiduciary) to assist in selecting and monitoring investment alternatives, without additional screening or recommendations based on the interests of plan or IRA investors, would not be considered under the proposal to be making a recommendation. [50]

DOL suggests that the same analysis is likely to apply with respect to pooled employer plans (PEPs). DOL explains that pooled plan providers (PPPs):

> are in a unique statutory position in that they are granted full discretion and authority to establish the plan and all of its features, administer the plan, act as a fiduciary, hire service providers, and select investments and investment managers. When a PPP or another service provider interacts with an employer about investment options under the plan, whether they have made a recommendation under the proposal will turn, in part, on whether they present the investments as selected for, and appropriate for, the plan, its participants, or beneficiaries. [51]

No Proposed Changes to the IB 96-1 Guidance Delineating Education and Advice

DOL's Interpretive Bulletin (IB) 96-1 provides guidance on the circumstances under which the provision of investment-related information to participants and beneficiaries of an individual account plan will constitute education and not the rendering of fiduciary investment advice. Where the 2016 Rule had incorporated an updated[52] version of IB 96-1 into the text of the rule (as an exclusion from "recommendation" for investment education), the current proposal would make no change to IB-96-1. DOL confirms that it believes the IB continues to provide accurate information, and notes in particular the important example of providing information on the benefits of participating in the plan and the benefits of increasing contributions. The preamble also indicates that, although the IB specifically applies in the context of participant-directed individual account plans, DOL believes that the guidance is valid in the IRA context as well.[53] DOL requests comments about whether the guidance in the IB is sufficient and whether its provisions should be incorporated into the text of the final rule.

Scope

The proposal includes provisions from the existing regulation and 2016 Rule regarding the scope of fiduciary duty and the execution of securities transactions. The scope provision confirms that being an investment advice fiduciary with respect to certain assets of a plan or IRA does not make the person an investment advice fiduciary for all of the assets of the plan or IRA. The securities transactions provision specifies that the execution of certain securities transactions by broker-dealers at the direction of plan clients or unrelated parties is not fiduciary advice.

Squaring the Proposal with the Fifth Circuit's 2018 Decision

In vacating the 2016 Rule, the Fifth Circuit emphasized the importance of the existence of a relationship of trust and confidence between the fiduciary and client for a fiduciary relationship to exist. The court also noted the importance of the difference between mere sales conduct, which does not usually create a fiduciary relationship under ERISA, and investment advice for a fee, which does.[54]

In the preamble, DOL includes frequent use of the terms "trust and confidence." DOL, however, generally characterizes the proposed definition as capturing the contexts in which retirement investors could reasonably place their trust and confidence in the advice provider (seemingly a one-way view of trust and confidence, rather than a two-way relationship). DOL flatly disagrees with the court's distinction between sales activity and advice, saying "the Department rejects the purported dichotomy between a mere 'sales' recommendation to a counterparty, on the one hand, and advice, on the other, in the context of the retail market for investment products."[55]

In light of the fact that the proposal does not comport with the Fifth Circuit's decision, DOL seems to be aware that it may be sued over the eventual final rule, noting that it "is considering whether this proposal could continue to work even if certain aspects of the proposal were struck down by a court" and "whether any aspects of this proposal could be severable."[56] DOL requests comments on this question.

Proposed Changes to PTEs

As noted above, in addition to proposing a new definition of investment advice fiduciary, the proposal would implement significant changes to several PTEs that the asset

management industry relies on. These include PTEs 2002-02, 84-24, 75-1, 77-4, 80-83, 83-1, and 86-128. As a threshold matter, the proposed amendments generally shift fiduciary investment advice under the purview of PTE 2020-02. While PTE 84-24 remains available to a narrow category of investment advice arrangements (and would largely mirror an amended PTE 2020-02), a party currently relying on one of the other PTEs for investment advice arrangements likely will be limited to using PTE 2020-02 going forward.[57]

Proposed Changes to PTE 2020-02

Overview of Current PTE 2020-02

PTE 2020-02 offers broad relief for registered investment advisers, broker-dealers, insurance companies, banks (i.e., "Financial Institutions"), and individual investment professionals who are their employees or agents (i.e., "Investment Professionals"),[58] permitting them to receive compensation as a result of providing fiduciary investment advice; provided they satisfy the requirements of the exemption.[59] It allows investment advice fiduciaries under both ERISA and the Code to receive compensation (including as a result of advice to roll over assets from a plan to an IRA) and to engage in certain principal transactions, that would otherwise violate the prohibited transaction provisions of ERISA and the Code.[60]

PTE 2020-02 is not available for:

- transactions involving ERISA-covered plans if the Investment Professional, Financial Institution, or an affiliate is either (i) the employer of employees covered by the plan, or (ii) is a named fiduciary or plan administrator, or an affiliate thereof, who was selected to provide advice to the plan by a fiduciary who is not independent of the Financial Institution, Investment Professional, and their affiliates;
- transactions that result from robo-advice arrangements that do not involve interaction with an Investment Professional; or
- transactions in which the Investment Professional is acting in a fiduciary capacity other than as an investment advice fiduciary.

PTE 2020-02 currently does not apply in the context of PEPs.

Financial Institutions and Investment Professionals providing advice pursuant to PTE 2020-02 must comply with a number of conditions, including adhering to certain "Impartial Conduct Standards";[61] providing specified disclosures including a written acknowledgement of fiduciary status and explanation of services and material conflicts of interest; establishing and maintaining written policies and procedures prudently designed to both ensure compliance with the above referenced impartial conduct standards and mitigate conflicts of interest that could otherwise cause violations of those standards; documenting and disclosing the specific reasons that any rollover recommendations are in the retirement investor's best interest; and conducting an annual retrospective compliance review.

Proposed Amendments to PTE 2020-02 ("Proposed PTE 2002-02")

The proposal accords significantly enhanced importance to PTE 2020-02. First, as discussed above, the proposed definition of investment advice fiduciary would significantly expand those parties that are deemed to be providing fiduciary investment advice. Second, the

proposal amends the scope of several PTEs currently available to investment advice fiduciaries such that most investment advice arrangements would now fall exclusively under the scope of PTE 2020-02. Third, PTE 2020-02 would now be available for PEPs and robo-advice.

The proposal makes a number of changes that would, as DOL describes them, maintain the core conditions of the current PTE 2020-02 while providing "more certainty for Retirement Investors receiving advice and Financial Institutions[62] and Investment Professionals[63] complying with the exemption's conditions."[64]

To this end, Proposed PTE 2020-02 would:

- Expand the coverage of PTE 2020-02 to allow its use by PPPs in connection with advice to PEPs, and for robo-advice arrangements that do not involve human interaction;
- Require additional disclosures to retirement investors regarding the costs of a transaction, as well as the significance and severity of any conflicts of interest;
- Provide more guidance for Financial Institutions and Investment Processionals as to the types of practices that are likely prohibited under PTE 2020-02;
- Require affirmative reporting to the IRS, correction of, and payment of applicable excise taxes on non-exempt prohibited transactions; and
- Expand the situations under which an institution would be disqualified from replying on PTE 2020-02.

DOL asserts in the preamble that Proposed PTE 2020-02 would not:

- require a contract for investment advice to IRAs (unlike the now vacated Best Interest Contract exemption from the 2016 Rule);
- Create any new causes of action; or
- Require Financial Institutions to provide enforceable warranties to retirement investors.[65]

DOL poses a number of questions regarding the proposed expansion of PTE 2020-02 as to which it is requesting comment. We highlight a few of these below.

Expanded Coverage to Include PEPs and Robo-Advice

As noted above, PTE 2020-02 currently is not available in the context of advice from a PPP to a PEP.[66] DOL proposes to expand coverage to advice provided by an Investment Professional, Financial Institution, or affiliate thereof that is a PPP. DOL explains this expansion by noting that, among other things, at the time PTE 2020-02 was put in place the rules for PPP registration had not yet been finalized.[67] Notably, this expansion to PPPs would not provide relief for a PPP's decision to retain an affiliated or related party as an advice provider.

The proposal also would extend the availability of PTE 2020-02 to robo-advice arrangements that do not involve interaction with an investment advice professional by removing the existing exclusion of such pure robo-advice arrangements. DOL recognizes that robo-advice models may involve a combination of pure computer model advice and some level of human Investment Professional interaction.[68] Expanding PTE 2020-02 to include pure robo-advice arrangements would, in DOL's view, simplify compliance for Financial Institutions as they could operate a robo-advice program with available Investment Professional assistance without having to separately evaluate whether the

Investment Professional is providing fiduciary investment advice. DOL requests comments on several questions regarding current use of computer models, including Financial Institutions' use of artificial intelligence.[69]

Scope of Covered Principal Transactions

DOL proposes to narrow the scope of Covered Principal Transactions under PTE 2020-02 by carving out in-kind transactions and adding a definition of "Riskless Principal Transaction" (which is not considered a "Covered Principal Transaction" and is eligible for the more general provisions of the exemption). A Riskless Principal Transaction would be defined in proposed section V(l) as a transaction where a Financial Institution receives an order from a retirement investor to buy or sell assets, and contemporaneously sells or buys such asset for its own account to offset this transaction. DOL emphasizes that parties should take care in determining whether a product is eligible for treatment as a Covered Principal Transaction or a Riskless Principal Transaction.[70] If a principal transaction is later determined to not fall under one of these definitions, the transaction was not eligible for PTE 2020-02 and may need to be reversed.

Enhanced Impartial Conduct Standards

The proposal would enhance aspects of the impartial conduct standards requirements of PTE 2020-02. These standards include a best interest standard, a reasonable compensation standard, and a no misleading statements requirement. The proposal would retain the current best interest standard. Of note, however, DOL proposes to add an example to section II(a)(1) of PTE 2020-02 stating that, in choosing between two available investments, the Investment Professional may not recommend a product that is worse for the retirement investor but better or more profitable for the Investment Professional or the Financial Institution. The preamble explains that: "[i]n other words, the requirement for Investment Professionals not to subordinate the Retirement Investor's interests to their own is not satisfied if the Investment Professional merely considers the Retirement Investor's interests along with its own and the Financial Institution's in choosing which product to recommend to a Retirement Investor."[71]

It is unclear from the proposal why DOL believes this example is needed, other than DOL's noting that the standard in this example is consistent with applicable SEC standards for both investment advisers and broker-dealers. DOL also emphasizes that this example is not intended to foreclose payment on a transactional basis, investment advice on proprietary products, or advice based on investment menus that are limited to proprietary products.[72]

DOL also clarified in the proposal that the best interest standard does not impose an "unattainable obligation…to somehow identify the single 'best' investment…assuming such advice were even possible at the time of the transaction."[73]

DOL is not proposing any changes to the reasonable compensation and best execution aspects of the impartial conduct standards.

The proposal would clarify the no misleading statements requirement such that "materially misleading" includes omitting information that is needed to make a statement not misleading in light of the circumstances under which it is made. Put another way, the Financial Institution and Investment Professional must consider whether the information given to a retirement investor provides the data the retirement investors would need or

would want to know about a recommended investment, and whether such information is provided in a manner that the retirement investor can understand.[74]

Additional Required Disclosures

Proposed PTE 2020-02 includes numerous enhanced disclosure requirements that would impact the information provided to retirement investors. These enhancements are as follows.

- The required pre-transaction disclosure would be enhanced to clarify that the Financial Institution and its Investment Professional are providing fiduciary investment advice to the retirement investor, and are fiduciaries under ERISA and/or the Code when making an investment recommendation. [Proposed section II(b)(1).] DOL is proposing this change due to concerns that some parties are utilizing "artful phrasing" that does not affirmatively state that they are making a recommendation as a fiduciary. Notably, a disclosure that a party "may" be a fiduciary or is a fiduciary "to the extent" that they meet the applicable definition no longer would be permitted.[75]
- A new written statement of the best interest standard of care owed to the retirement investor. [Proposed section II(b)(2).]
- The written description of the services to be provided and material conflicts would be expanded to include information as to whether the retirement investor will pay for services, and if so how (directly/indirectly, through commissions or transaction-based payments, etc.). [Proposed section II(b)(3).] DOL appears to contemplate some level of customization in these disclosures, as Proposed PTE 2020-02 would require that this information "be written in plain English, taking into consideration a Retirement Investor's level of financial experience."[76]
- A new written statement that a retirement investor can request (free of charge) specific information regarding costs, fees, and compensation, described in dollar amounts, percentages, formulas, or other means reasonably designed to present full and fair disclosure that is materially accurate in scope, magnitude, and nature, with sufficient detail to enable an informed judgment about the costs of the transaction and about the significance and severity of conflicts of interest.[77] [Proposed section II(b)(4).]
- The required documentation and disclosure for rollover recommendations would be significantly broader, and must include the alternatives to a rollover, the fees and expenses associated with the plan and the recommended investment, whether an employer or other party pays plan administrative expenses, and the different levels of services and investments available under the plan and the recommended investment or account.[78] [Proposed section II(b)(5).]
- Errors or omissions in a disclosure that were made while acting in good faith and with reasonable diligence may be corrected by providing the required information as soon as practicable, but not later than 30 days after the date an error or omission is discovered or reasonably should have been discovered. [Proposed section II(b)(6).]

In the preamble, DOL includes model language that can be used to satisfy sections II(b)(1), (2) and (4).[79] DOL also requests comment as to whether Financial Institutions should be required to provide additional disclosure to the investing public, including via a public website containing the required pre-transaction disclosure and other information.[80]

Additional Requirements for Financial Institution Policies and Procedures

Proposed PTE 2020-02 leaves in place the policies and procedures requirements of the

current PTE 2020-02, with two changes. First, DOL proposes to add to the text of PTE 2020-02 examples of actions that Financial Institutions may not take: "Financial Institutions may not use quotas, appraisals, performance or personnel actions, bonuses, contests, special awards, differential compensation,[81] or other similar actions or incentives that a reasonable person would conclude are likely, to result in recommendations that are not in Retirement Investors' Best Interest."[82] Second, Financial Institutions would now be required to provide copies of their policies and procedures to DOL upon request, within 10 business days.

In the preamble, DOL cautions paying close attention to conflicts of interest within an institution itself. For example, apparently neutral criteria (such as an Investment Professional receiving the same percentage of a Financial Institution's compensation for recommended investment products) may effectively transmit the conflict from the institution to the professional as the professional's compensation would be increased in direct proportion to the firm's profitability.[83]

The preamble also provides greater detail on how a Financial Institution can satisfy the policies and procedures requirement in the context of offering a limited menu of investment products, such as proprietary funds or funds that generate third-party payments.[84] DOL sets forth a detailed list of practices, as an example of "one way a Financial Institution could satisfy the policies and procedures requirement, but not the only way."[85] These include:

- Documenting its limitations on the universe of recommended investments and the conflicts associated with the receipt of third-party payments or the sale/promotion of proprietary products;
- Documenting any services provided in exchange for third-party payments;
- Reasonably concluding that the product limitations and conflicts will not result in compensation to the Financial Institution or Investment Professionals in excess of reasonable compensation;
- Reasonably concluding (and documenting in writing) that the product limitations and conflicts will not cause recommendations of imprudent investments;
- Informing the investor in writing about the specific product limitations that apply (DOL notes that it would not be sufficient to state that the Financial Institution or Investment Professional "may" limit recommendations to proprietary products or products that generate third-party payments);
- Clearly explaining its fees, compensation, and associated conflicts to the investor in plain English;
- Ensuring that all recommendations are based on the Investment Professional's consideration of certain characteristics of the investor, such as investment objectives, risk tolerance, financial circumstances, and other needs;
- Ensuring that at the time of the recommendation, the amount of compensation expected to be paid (directly or indirectly) to the Investment Professional, Financial Institution, or affiliates/related entities, for services in connection with the recommended transaction is not in excess of reasonable compensation; and
- Ensuring that the recommendation meets the prudence and loyalty requirements of the Impartial Conduct Standards.

The preamble invites comment on the need for additional guidance on recommendations of proprietary products and the type of guidance that would be most useful.[86]

Updated Retrospective Review

PTE 2020-02 requires that at least annually a Financial Institution conduct a retrospective review reasonably designed to assist the institution in detecting and preventing violations of and in complying with PTE 2020-02. Proposed PTE 2020-02 would require that, as part of the retrospective review, a senior executive officer of the Financial Institution certify that it has reported (or will report, as applicable) any non-exempt prohibited transactions in connection with fiduciary investment advice to the IRS on Form 5330, corrected such transactions, and paid any resulting excise taxes. [Proposed section II(d)(3)(B).]

Expanded Events of Disqualification

DOL proposes to expand the circumstances that would render a party ineligible to rely on PTE 2020-02, generally for a period of 10 years. First, DOL would expand ineligibility to include disqualifying actions by affiliates of a Financial Institution. DOL explains that this change addresses concerns that a party facing ineligibility may simply change its corporate form and continue relying on PTE 2020-02.[87] Moreover, DOL believes this expansion could better foster a culture of compliance throughout an organization.[88] Second, the proposal would expand the types of convictions that would lead to ineligibility. PTE 2020-02 currently bases ineligibility on criminal convictions arising out of the provision of investment advice to retirement investors. Proposed PTE 2020-02 casts a much wider net, including (among other things) conviction (irrespective of a pending appeal) of a range of felonies[89] by a US federal or state court, or conviction in a "foreign court of competent jurisdiction" of substantially equivalent crimes. Additionally, the proposal would expand the circumstances under which DOL can issue a Financial Institution or Investment Professional a notice of ineligibility to rely on PTE 2020-02[90] to include engaging in a systematic pattern or practice of failing to (i) correct prohibited transactions, (ii) report those transactions to the IRS, and (iii) pay applicable excise taxes.

DOL also proposes to standardize a 6-month wind-down period after a conviction or ineligibility notice. DOL expresses concern that the current framework, with different timeframes for ineligibility followed by a 1-year wind down period, results in too long a time frame during which noncompliance and inappropriate conduct could continue.[91]

PTE 2020-02 currently provides that a Financial Institution convicted of a crime may petition DOL to be allowed to continue to rely on the exemption. DOL proposes to amend this process to limit such petitions to disqualification due to foreign convictions, under the theory that for US federal and state convictions the advice provider already has been accorded due process by a US court.[92]

Expanded Recordkeeping Requirements Under Consideration

While the proposal does not change the recordkeeping provision of PTE 2020-02, DOL in the preamble seeks feedback on an alternative approach to the recordkeeping requirement that would significantly expand the parties entitled to access records.[93] These additional parties would include any fiduciary of a plan that engaged in a transaction pursuant to PTE 2020-02, any contributing employer or employee organization to a plan that engaged in a transaction pursuant to PTE 2020-02, and any participant or beneficiary of a plan or beneficial owner of an IRA acting on behalf of an IRA that engaged in a transaction pursuant to PTE 2020-02.

Proposed Amendments to PTE 84-24 ("Proposed PTE 84-24")

DOL proposes to significantly scale back the availability of PTE 84-24. PTE 84-24 currently provides relief for the purchase of annuities and the purchase/sale of investment company

securities by a plan or IRA, and the receipt by an insurance agent or an investment company principal underwriter of sales commissions paid in connection with the transaction. DOL proposes to push virtually all advice-related transactions that currently can avail themselves of PTE 84-24 into PTE 2020-02, with the exception of certain sales of non-security annuities/insurance products through independent insurance agents.[94] To the extent that Proposed PTE 84-24 continues to be available for advice through independent insurance agents, most of the requirements of PTE 84-24 would be replaced with provisions that generally mirror the requirements of Proposed PTE 2020-02.

Availability for Certain Non-Advice Mutual Fund Transactions

DOL proposes to leave in place the ability to use PTE 84-24 for certain transactions involving annuities and securities issued by an investment company that do not involve a fiduciary's provision of investment advice (e.g., transactions by non-fiduciaries and nondiscretionary trustees).[95] With respect to mutual funds, PTE 84-24 would remain available for receipt of certain commissions by a principal underwriter for effecting or executing the purchase of securities issued by an investment company, but would no longer be available for recommending affiliated funds. [Proposed section III(b) and (c).] The proposal also would narrow the types of sales commissions covered by the exemption. With respect to mutual funds in particular, the proposal would define a new term—"Mutual Fund Commission"—to include only a commission or sales load paid by either the plan or the investment company for the service of effecting or executing the purchase of investment company securities, and specifically excludes 12b-1 fees, revenue sharing payments, administrative fees, and marketing fees. [Proposed section X(h).]

PTE 84-24 also would continue to be available for the purchase, with plan assets, of securities issued by an investment company from, or the sale of such securities to, an investment company or an investment company principal underwriter, when such investment company, principal underwriter, or the investment company investment adviser is a fiduciary or a service provider (or both) with respect to the plan solely by reason of: (1) the sponsorship of a preapproved plan; or (2) the provision of nondiscretionary trust services to the plan; or (3) both (1) and (2). [Proposed section III(f).]

Sections IV and V of Proposed PTE 84-24 would apply several conditions to the covered mutual fund transactions, including a reasonable compensation requirement, various disclosure requirements, and a requirement that the principal underwriter is not: a trustee of the plan (other than a nondiscretionary trustee), a plan administrator, a discretionary asset management fiduciary to the plan, or an employer of employees covered by the plan.

Availability for Advice by Independent Insurance Agents

As amended, PTE 84-24 would remain available for investment advice provided to a retirement investor only by an independent insurance agent (an "Independent Producer"). [Proposed section III(g).] The exemption would provide relief only for the agent's receipt of fully disclosed sales commissions on non-securities annuity contracts or other insurance products not regulated by the SEC. Any related or alternative forms of compensation would not qualify for the exemption.[96] PTE 84-24 would not be available where the Independent Producer or the insurer and any affiliate thereof is the employer of employees covered by the plan or the plan's named fiduciary or administrator (with an exception where selected by an independent fiduciary). [Proposed section VI(c)(1).]

Proposed PTE 84-24 would not provide relief for the insurer. While the insurer would be

responsible for supervising Independent Producers and for performing retrospective reviews, it would not itself be a fiduciary. To the extent the insurer is an investment advice fiduciary because it is providing investment advice under ERISA or the Code, it would need to rely on PTE 2020-02. DOL explains that this limitation is due in part to the fact that under PTE 84-24 the insurance company would not be assuming fiduciary status in overseeing the conduct of Independent Producers.[97] Moreover, PTE 84-24 would apply separately with respect to each insurance company. As such, to the extent PTE 84-24 were no longer available due to an insurer's failure to comply with the exemption, an Independent Producer may still rely on the exemption (and receive compensation) in connection with the sale of other insurance companies' products.[98]

Impartial Conduct Standards

PTE 84-24 would be amended to require that the Independent Producer in providing fiduciary investment advice adhere to the same Impartial Conduct Standards as those in PTE 2020-02—a Best Interest standard, a requirement that the Independent Producer's compensation not exceed reasonable compensation, and a prohibition on misleading statements. [Proposed section VII(a).] Proposed PTE 84-24 expands on these requirements to reflect the circumstances of the exemption. "Best Interest," as defined in section X(b), requires that the advice the Independent Producer provides to a retirement investor not place the financial or other interests of the Independent Producer, insurer or an affiliate, or any other party ahead of those of the retirement investor. Reasonable compensation is limited to an Independent Producer's receipt as compensation in connection with the transaction only an Insurance Sales Commission—as defined in section X(g), a sales commission paid to the Independent Producer by the insurance company or an affiliate for recommending and/or effecting the purchase or sale of an insurance or annuity contract. The prohibition on misleading statements applies to the Independent Producer, and permits the agent to provide materials including those prepared by the insurer, provided that such materials are not misleading to the agent's knowledge.[99] Similar to proposed PTE 2020-02, "materially misleading" would include omitting necessary information.

Disclosures

Similar to PTE 2020-02, the Independent Producer providing fiduciary investment advice to a retirement investor must provide certain disclosures. [Proposed section VII(b).] These disclosures include a written acknowledgement that the Independent Producer is a fiduciary under Title I of ERISA and/or the Code, a written statement of the Best Interest standard of care, a written description of the services they will provide and the products they are licensed and authorized to sell, including any limits on the range of insurance products recommended, and a written statement of their material conflicts of interest and the amount of the insurance commission that will be paid to them in connection with the purchase of the recommended annuity by a retirement investor. The retirement investor also must be informed in writing of their right to obtain specific information regarding costs, fees, compensation. DOL includes proposed model language that would satisfy certain of these disclosures.[100]

As under PTE 2020-02, DOL is interested in comments regarding whether it should require insurers or Independent Producers to maintain a public website containing the pre-transaction disclosure and other information.[101]

Documentation

The Independent Producer also would have to make certain specific disclosures before the sale of a recommended annuity. Of note, the Independent Producer would have to document its conclusion that the recommended annuity is in the retirement investor's Best Interest, and provide this documentation to both the retirement investor and the insurer. [Proposed section VII(b)(6).] Where a recommendation is made in connection with a rollover, before engaging in the rollover or making a post-rollover recommendation the Independent Producer must consider and document its rollover-related conclusions in a manner similar to PTE 2020-02, and provide this documentation to the retirement investor and the insurer. [Proposed section VII(b)(7).]

Insurance Company Policies and Procedures

Proposed PTE 84-24 depends on oversight by an insurer that must ensure that appropriate policies and procedures designed to ensure compliance with the Impartial Conduct Standards are both adopted and implemented (as is the case for PTE 2020-02), and to "carefully police" Independent Insurers' recommendations of its insurance products.[102] This includes reviewing these recommendations before an annuity is issued to a retirement investor. [Proposed section VII(c)(1).] Policies and procedures also must include a prudent process both for determining whether to authorize an Independent Producer to sell the insurer's annuity contracts to retirement investors, and for taking actions to protect retirement investors from Independent Producers who either have failed or are likely to fail to adhere to the Impartial Conduct Standards, or who lack the necessary education, training, or skill to do so. [Proposed section VII(c)(3).]

In mitigating conflicts of interest, the policies and procedures must identify and eliminate quotas, appraisals, bonuses, contests, special awards, differential compensation, riders, or other features that a reasonable person would conclude are likely to incentivize Independent Producer to make recommendation that do not meet the Impartial Conduct Standards. [Proposed section VII(c)(2).] To this end, an insurer would not be able to offer incentive vacations, trips, or even educational conferences; if qualification for these items is based on sales volume or satisfaction of sales quotas.[103] DOL views these types of incentives as creating an undue conflict of interest. Moreover, specific to educational conferences in DOL's view these opportunities should be equally offered to all sales agents as training is a necessary component of providing Best Interest advice.

Insurance Company Retrospective Review

An insurer must at least annually conduct a retrospective review reasonably designed to achieve compliance with, and detect and prevent violations of, the Impartial Conduct Standards. [Proposed section VII(d)(1).] While this is similar to the retrospective review proposed under PTE 2020-02, the review also must include a prudent determination of whether individual Independent Producers should be permitted to continue to sell the insurer's annuity contracts to retirement investors. This review need not be as extensive as an initial evaluation of an Independent Producer.[104] The review must be provided to an insurer senior executive officer, who must annually certify that the officer has reviewed the retrospective review report, among other things. [Proposed section VII(d)(2) and (4).] Of note, this certification must include a confirmation that the insurer has filed, or will file, Form 5330 with IRS to report any prohibited transactions it discovered in connection with investment advice covered under Code section 4975(e)(3)(B), and that any such prohibited transactions have been reported to DOL. Moreover, the Insurer must retain the report and supporting data for six years to make available to DOL upon request. [Proposed section VII(d)(6).]

Self-Correction

Proposed PTE 84-24 would provide a means for the Independent Producer to make corrections needed to avoid non-exempt prohibited transactions. [Proposed section VII(e).] Self-correction would be allowed where the Independent Producer (i) has either refunded any charge to the retirement investor or rescinded a mis-sold annuity and cancelled the contract and waived any surrender charges, (ii) notifies DOL of the violation and of the refund/rescission within 30 days of correction, (iii) makes the correction no later than 90 days after they learn of or reasonably should have learned of a violation, and (iv) notifies the person at the insurer responsible for conducting the retrospective review during the applicable review cycle, and the correction is specifically set forth in the written retrospective review report.

Events of Disqualification

Proposed PTE 84-24 includes events of disqualification similar to Proposed PTE 2020-02, as described earlier. [Proposed section VIII.] Different criteria would apply as to Independent Producers and insurers.

Recordkeeping Requirement

DOL proposes an expanded recordkeeping requirement that it views as "intended to protect the rights of plan participants, beneficiaries, and IRA owners by ensuring that they and the Department are provided with sufficient information to determine whether the exemption conditions have been satisfied."[105] DOL notes that the proposed recordkeeping requirement is consistent with that in other class exemptions—including Proposed PTE 2020-02. The expanded requirement would require that the applicable party maintain records necessary for any of the following persons "to determine whether the conditions of this exemption have been met with respect to a transaction for a period of six years from the date of the transaction in a manner that is reasonably accessible for examination."[106] Persons entitled to access would include authorized DOL/IRS/state or federal regulator employees, any fiduciary of a plan engaged in a transaction pursuant to PTE 84-024, any contributing employer or employer organization to a plan that engaged in a transaction pursuant to this exemption, or a participant or beneficiary of a plan or, beneficial owner of an IRA acting on behalf of the IRA, that engaged in a transaction pursuant to PTE 84-24. [Proposed section IX(a)(2).]

Proposed Amendments to PTEs 75-1, 77-4, 80-83, 83-1, and 86-128

DOL proposes to amend each of the above PTEs to add the following restriction.

Exception. No relief from the restrictions of ERISA section 406(b) and the taxes imposed by Code section 4975(a) and (b) by reason of Code sections 4975(c)(1)(E) and (F) is available for fiduciaries providing investment advice within the meaning of ERISA section 3(21)(A)(ii) or Code section 4975(e)(3)(B) and regulations thereunder.[107]

As such, these PTEs no longer would be available for fiduciaries providing fiduciary investment advice as outlined above. DOL's stated intent is to provide "a single standard of care (which is currently found in PTE 2020-02) that would apply universally to all fiduciary investment advice, regardless of the specific type of product or advice provider, will provide greater protection for retirement investors and create a level playing field among investment advice providers."[108]

PTE 77-4, which currently is available for the sale and recommendation of proprietary mutual funds to plans and IRAs (in the context of both fiduciary advice and discretionary fiduciary services), would continue to be available for use in the discretionary investment management context. The proposal would not make any other changes to PTE 77-4.

In addition to shifting all fiduciary investment advice activities (as redefined) to PTE 2020-02, DOL proposes what it describes as administrative amendments to some of these exemptions. Some notable proposed changes are described below.

Proposed Amendments to PTE 75-1

The proposal would eliminate Part 1(b) and (c) of PTE 75-1, which provide exemptive relief for certain non-fiduciary services that are provided by broker-dealers in securities transactions. DOL views this relief as duplicative of statutory exemptions under ERISA section 408(b)(2) and Code section 4975(d)(2).[109]

The proposal would revoke Part II(2), which provides exemptive relief for mutual fund purchases between fiduciaries and plans or IRAs. DOL views this exemption as not protective of retirement investors.[110] In lieu of this exemption, DOL views Proposed PTE 2020-02 as more protective for the provision of investment advice on the purchase or sale of a mutual fund security. DOL also notes that PTE 77-4 is available for fiduciaries receiving non-commission compensation for investment management on the purchase or sale of a mutual fund security.[111] With respect to the remaining transactions covered by Part II (principal transactions), the proposal would shift the responsibility for maintaining records demonstrating compliance with the PTE from the plan to the broker-dealer, reporting dealer, or bank engaging in the covered transaction. Similar to the proposed amendments to the QPAM Exemption,[112] the records must be made available to specified persons (including employees of DOL and IRS, plan fiduciaries, and plan participants and beneficiaries).

Part V, which permits a broker-dealer to extend credit to a plan or IRA in connection with a purchase or sale of securities, would be amended as it was under the 2016 amendments to permit investment advice fiduciaries to receive compensation in connection with such as extension of credit where credit is extended to avoid a failed securities transaction. This relief is conditioned on the fiduciary or an affiliate not having caused the failure.

Proposed Amendments to PTE 86-128

PTE 86-128 allows a fiduciary to receive reasonable compensation when executing an agency securities transaction. DOL proposes changes to PTE 86-128 not related to the provision of fiduciary investment advice. First, DOL proposes (as it did in 2016) to delete section IV(a), which carves out from the conditions of PTE 86-128 certain plans (including IRAs) that do not cover employees. DOL views this change as increasing the safeguards available to these retirement investors.[113] Without this carve-out, investment advice fiduciaries to IRAs would need to look to other exemptive relief such as PTE 2020-02. DOL notes that fiduciaries that exercise full discretionary authority or control with respect to IRAs could continue to rely on PTE 86-128, as long as they comply with all of the exemption's conditions.[114] Second, DOL also proposes to amend PTE 86-128, at proposed section IV(b) (currently IV(c)), to clarify that discretionary trustees may utilize the recapture of profits exception whereby all profits earned on a securities transaction are returned to the plan.

Next Steps

DOL has proposed what would represent significant and wholesale changes to how many entities conduct business when providing fiduciary investment advice and to business activity not previously viewed as fiduciary investment advice. ICI will work with member companies to develop comments on the proposal.

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Notes

[1] DOL's news release is available at https://www.dol.gov/newsroom/releases/ebsa/ebsa20231031, DOL's fact sheet is available at 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, and a blog post by Assistant Secretary Lisa Gomez is available at https://blog.dol.gov/2023/10/31/a-long-overdue-update-for-retirement-savings-protections. In addition, the White House released a blog post at https://www.whitehouse.gov/cea/written-materials/2023/10/31/fiduciary-rule/ and a fact sheet at https://www.whitehouse.gov/briefing-room/statements-releases/2023/10/31/fact-sheet-president-biden-to-announce-new-actions-to-protect-retirement-security-by-cracking-down-on-junk-fees-in-retirement-investment-advice/. The main themes of the package (as described in the Administration's promotional materials) are eliminating "junk fees," ensuring that rollover recommendations are covered, addressing recommendations of rollovers to fixed indexed annuities, and closing the gaps for those not covered by the SEC's Regulation Best Interest.

[2] The proposal to amend the regulation defining the term Investment Advice Fiduciary was published at 88 Fed. Reg. 75890 (November 3, 2023), available at https://www.govinfo.gov/content/pkg/FR-2023-11-03/pdf/2023-23779.pdf. The proposal to amend PTE 2020-02 was published at 88 Fed. Reg. 75979 (November 3, 2023), available at https://www.govinfo.gov/content/pkg/FR-2023-11-03/pdf/2023-23780.pdf. The proposal to amend PTE 84-24 was published at 88 Fed. Reg. 76004 (November 3, 2023), available at https://www.govinfo.gov/content/pkg/FR-2023-11-03/pdf/2023-23781.pdf. The proposal to amend the five additional PTEs was published at 88 Fed. Reg. 76032 (November 3, 2023), available at https://www.govinfo.gov/content/pkg/FR-2023-11-03/pdf/2023-23782.pdf.

[3] The letter, submitted on November 8, 2023, argued that a 60-day comment period (falling over multiple federally recognized holidays) is simply too short to allow interested parties to provide meaningful input and requested a 60-day extension. The letter further noted that setting a public hearing date before the close of the comment period

communicates that the hearing is merely a "check the box" exercise, rather than an effort to receive helpful feedback.

[4] For an overview of the Fifth Circuit decision, see ICI Memorandum No. 31137, dated March 16, 2018, available at https://www.ici.org/memo31137.

[5] For an overview of the 2016 Rule, see ICI Memorandum No. 29837, dated April 13, 2016, available at https://www.ici.org/memo29837.

[6] See ICI Memorandum No. 32581, dated July 6, 2020, available at https://www.ici.org/memo32581.

[7] For a summary of the finalized PTE 2020-02, see ICI Memorandum No. 32999, dated December 18, 2020, available at https://www.ici.org/memo32999.

[8] For a summary of the FAQ guidance, see ICI Memorandum No. 33485, dated April 19, 2021, available at https://www.ici.org/memo33485.

[9] See ICI Memorandum No. 35053, dated March 1, 2023, available at https://www.ici.org/memo35053. The court disagreed with DOL's position that, for the "regular basis" prong of the test, a recommendation to roll over from a plan to an IRA can be the beginning of an intended future ongoing relationship. The court's holding relies on the 5-part test's requirement that the advice is provided on a regular basis "to the plan" (i.e., the plan holding the assets at the time of the recommendation). DOL did not appeal this decision.

[10] Note that a magistrate judge has made a recommendation to the district court, recommending that the court vacate the portions of PTE 2020-02's text and preamble that allow consideration of Title II investment advice relationships when determining Title I fiduciary status.

[11]According to the court's filing entry on PACER granting the request, the plaintiffs may file a supplemental brief, of no more than 10 pages, by December 4, 2023 and DOL may file a response brief, of no more than 10 pages, by January 5, 2024.

[12] The term "IRA" includes any account or annuity described in Code section 4975(e)(1)(B) through (F), including, for example, an individual retirement account described in section 408(a) of the Code and a health savings account described in section 223(d) of the Code.

[13] The proposal defines "for a fee or other compensation, direct or indirect" similar to how it defined it in the 2016 Rule. Compare section (e) of the proposal with section (g)(3) of the 2016 Rule. Further, in the preamble, DOL explains that "compensation is treated as paid 'in connection with or as a result of' the provision of advice only if it would not have been paid but for the recommended transaction or the provision of advice, or if the investment advice provider's eligibility for the compensation (or its amount) is based in whole or part on the recommended transaction or the provision of advice." 88 Fed. Reg. at 75909.

[14] See section (c)(1)(ii)(A) of current definition.

[15] See 88 Fed. Reg. at 75901 for DOL's justification for this change.

[16] 88 Fed. Reg. at 75902.

[17] 88 Fed. Reg. at 75902. "The Department invites comment on this approach, including the extent to which the Department should consider the investor's understandings as to whether the adviser regularly makes investment recommendations as part of their business. The Department seeks comment regarding examples of financial professionals who may be reasonably viewed by investors as giving investment advice but would not in fact meet the requirements laid out in this provision." [emphasis added]

[18] 88 Fed. Reg. at 75902.

[19] 88 Fed. Reg. at 75903.

[20] 88 Fed. Reg. at 75903. The SEC's initial 2018 package included a proposal that would have restricted broker-dealers and their associated persons from using the term "adviser" or "advisor" when communicating with a retail investor unless they were registered as, or supervised persons of, an investment adviser. See ICI Memorandum No. 31185, dated April 26, 2018, available at https://www.ici.org/memo31185. Instead of adopting that rule, in the final Regulation Best Interest, the SEC took the position that the use of the term "adviser" or "advisor" in a name or title by (1) a broker-dealer that is not also registered as an investment adviser or (2) an associated person that is not also a supervised person of an investment adviser, presumptively would violate Regulation Best Interest's Disclosure Obligation. See ICI Memorandum No. 31815, dated June 19, 2019, available at https://www.ici.org/memo31815.

[21] Section (a)(2)(i) of the 2016 Rule would have imposed fiduciary status on a person who: "Represents or acknowledges that it is acting as a fiduciary within the meaning of the Act or the Code."

[22] 88 Fed. Reg. at 75903.

[23] DOL explains that its "intent in including this paragraph in the proposal is to permit parties to define the nature of their relationship, but also to ensure that any disclaimer be consistent with oral communications or actions, marketing material, State and Federal law, and other interactions based on all relevant facts and circumstances. When the disclaimer is at odds with the investment advice provider's oral communications, marketing material, State or Federal law, or other interactions, the disclaimer is insufficient to defeat the retirement investor's legitimate expectations." 88 Fed. Reg. at 75903. According to footnote 108, "[t]his discussion of disclaimers applies to the regulation proposed herein, defining an investment advice fiduciary, and would not extend to a circumstance in which a financial professional has investment discretion over a retirement investor's assets."

[24] Compare section (f)(10) of the proposal to sections (a)(1)(i) and (ii) of the 2016 Rule.

[25] Like the 2016 Rule, the proposal clarifies in paragraph (f)(11) that "investment property" does not include health insurance policies, disability insurance policies, term life insurance policies, or other property to the extent the policies or property do not contain an investment component.

[26] DOL points out in the preamble that this reference to the selection of an investment account arrangement is consistent with the SEC's Regulation Best Interest and the Adviser's Act's fiduciary obligations (although note that this was included in the 2016 Rule before Regulation Best Interest was issued). 88 Fed. Reg. at 75905.

[27] 88 Fed. Reg. at 75905.

[28] See ICI Memorandum No. 32999, dated December 18, 2020, available at https://www.ici.org/memo32999.

[29] Under the Deseret Letter, DOL stated that it is not fiduciary advice to make a recommendation as to distribution options even if that advice is accompanied by a recommendation as to how the distribution should be invested.

[30] 88 Fed. Reg. at 75905. DOL further states "[c]ertainly, a prudent and loyal fiduciary generally could not make a recommendation on how to invest assets currently held in a plan after a rollover, without even considering the logical alternative of leaving the assets in the plan or evaluating how that option compares with the retirement investor's likely investment experience post-rollover. A fiduciary would violate ERISA's 404 obligations if it recommended that a retirement investor roll the money out of the plan without proper consideration of how the money might be invested after the rollover."

[31] 88 Fed. Reg. at 75906.

[32] 88 Fed. Reg. at 75906.

[33] 88 Fed. Reg. at 75906. Further, DOL states that it "does not intend to suggest, however, that a person could become a fiduciary merely by engaging in the normal activity of marketing themselves as a potential fiduciary to be selected by a plan fiduciary or IRA owner, without making a recommendation of a securities transaction or other investment transaction or any investment strategy involving securities or other investment property."

[34] 88 Fed. Reg. at 75906. DOL further argues that its approach is consistent with the SEC's approach in Regulation Best Interest. See footnote 115, citing to Questions on Regulation Best Interest, available at https://www.sec.gov/tm/faq-regulation-best-interest.

[35] 88 Fed. Reg. at 75906.

[36] 88 Fed. Reg. at 75908.

[37] The 2016 Rule, at paragraph (b)(1), defined "recommendation" as "a communication that, based on its content, context, and presentation, would reasonably be viewed as a suggestion that the advice recipient engage in or refrain from taking a particular course of action."

[38] 88 Fed. Reg. at 75904.

[39] 88 Fed. Reg. at 75904.

[40] 88 Fed. Reg. at 75904, citing Regulation Best Interest release, which cited relevant FINRA guidance.

[41] 88 Fed. Reg. at 75904.

[42] 88 Fed. Reg. at 75904.

[43] The activities excluded under the 2016 Rule included: transactions with independent fiduciaries with financial expertise, swap and security-based swap transactions, and employees.

[44] The 2016 Rule's exclusions from "recommendation" included: platform providers, selection and monitoring assistance, general communications, and investment education.

[45] 88 Fed. Reg. at 75907.

[46] 88 Fed. Reg. at 75907.

[47] 88 Fed. Reg. at 75908.

[48] 88 Fed. Reg. at 75908.

[49] The 2016 Rule specified that the plan fiduciary must be independent of the platform provider and the platform provider must provide a written disclosure. The platform provider exclusion did not apply with respect to IRAs.

[50] 88 Fed. Reg. at 75908.

[51] 88 Fed. Reg. at 75908.

[52] The IB covers the furnishing of (1) plan information, (2) general financial, investment and retirement information, (3) asset allocation models, and (4) interactive investment materials. The 2016 Rule included a clarification that the provision of certain general information that helps an individual assess and understand retirement income needs (such as longevity and inflation risk) or explains general methods for the individual to manage those risks, both within and outside the plan, would not result in fiduciary status. The 2016 Rule also clarified that the distinction between non-fiduciary education and fiduciary advice applies equally to information provided to plan fiduciaries, as well as to information provided to plan participants and beneficiaries and IRA holders, and that it also applies equally with respect to participant-directed plans and other plans. The 2016 Rule also included new requirements regarding when asset allocation models and interactive investment materials may identify a specific investment alternative.

[53] 88 Fed. Reg. at 75911.

[54] The court stated, "Congress does not 'hide elephants in mouseholes.' … Had Congress intended to abrogate both the cornerstone of fiduciary status—the relationship of trust and confidence—and the widely shared understanding that financial salespeople are not fiduciaries absent that special relationship, one would reasonably expect Congress to say so." Chamber of Commerce v. United States Department of Labor, 885 F.3d 360 (5th Cir. 2018) [pages 25-26], available at https://www.ca5.uscourts.gov/opinions/pub/17/17-10238-CV0.pdf.

[55] 88 Fed. Reg. at 75907.

[56] In deciding to vacate the rule in its entirety, the Fifth Circuit noted that "DOL makes no argument concerning severability of the provisions making up the Fiduciary Rule and BICE exemption apart from the illegal arbitration waiver. In any event, this comprehensive regulatory package is plainly not amenable to severance." Chamber of Commerce, 885 F.3d. 360 (5th Cir. 2018).

[57] The statutory exemptions in ERISA section 408(b)(14) and (g) for the provision of investment advice remain in place.

[58] More specifically, "Investment Professionals" are individual investment professionals who are employees, agents, independent contractors, or representatives of a Financial Institution.

[59] ICI Memorandum No. 32999, dated Dec. 18. 2020, available at https://ww/ici.org/memo32999.

[60] PTE 2020-02 "extends broadly to [a fiduciary's] receipt of reasonable compensation as a result of the provision of fiduciary investment advice," and DOL specified this would cover "a wide variety of payments that would otherwise violate the prohibited transaction rules, including, but not limited to, commissions, 12b-1 fees, trailing commissions, sales loads, mark-ups and mark-downs, and revenue sharing payments from investment providers or third parties." 85 Fed. Reg. at 82798, 82799, 82800.

[61] The Impartial Conduct Standards include a best interest standard (intended to be aligned with the conduct standards in the SEC's Regulation Best Interest and the fiduciary duty of registered investment advisers under securities laws), a reasonable compensation standard, and a requirement to not make any materially misleading statements about recommended investment transactions and other relevant matters.

[62] "Financial Institutions" generally are registered investment advisers, broker-dealers, insurance companies, and banks.

[63] "Investment Professionals" generally are individual investment professionals who are employees, agents, independent contractors, or representatives of a Financial Institution.

[64] 88 Fed. Reg. at 75980.

[65] 88 Fed. Reg. at 75980.

[66] This is because the current PTE cannot be used when the Financial Institution or Investment Professional is the employer of employees covered by the plan or is a named fiduciary or a plan administrator of the plan (unless selected by an independent fiduciary to provide advice). 88 Fed. Reg. at 75982. In issuing the final PTE in 2020, DOL addressed commenters' requests that DOL specifically address the application of advice to PEPs. In declining to do so, DOL indicated its belief that it was premature to address issues related to PEPs, given their novel and unique nature. Note that ICI's comment letter on the PTE as proposed in 2020 urged DOL to clearly permit advice in connection with a PEP, as well as to expand coverage to robo-advice. See ICI Memorandum No. 32665, dated August 7, 2020, available at https://www.ici.org/memo32665.

[67] 88 Fed. Reg. at 75982.

[68] 88 Fed. Reg. at 75982.

[69] While DOL does not reference the SEC's recent proposal regarding conflicts of interest associated with the use of predictive data analytics and other "covered technologies" by broker-dealers and investment advisers, DOL could be influenced by SEC activity in this area. For an overview of the SEC's proposal, see ICI Memorandum No. 35390, dated August 2, 2023, available at https://www.ici.org/memo35390.

[70] 88 Fed. Reg. at 75981.

[71] 88 Fed. Reg. at 75983.

[72] 88 Fed. Reg. at 75983.

[73] 88 Fed. Reg. at 75984.

[74] 88 Fed. Reg. at 75984.

[75] 88 Fed. Reg. at 75984.

[76] Proposed section II(b)(3). DOL notes in the preamble that it anticipates Financial Institutions will be able to satisfy this written disclosure requirement in part through disclosures required by other regulators, including those disclosures required under Regulation Best Interest for broker-dealers and Form CRS for registered investment advisers. 88 Fed. Reg. at 75985.

[77] While a Financial Institution is not required to retain detailed cost and fee information as to every specific transaction, DOL is proposing to require that sufficient information be retained to meaningfully respond to such requests. 88 Fed. Reg. at 75985.

[78] The preamble states that this requirement extends to recommended rollovers from a plan to another plan or IRA, from an IRA to a plan, from an IRA to another IRA, or from one type of account to another (e.g., from a commission-based account to a fee-based account). 88 Fed. Reg. at 75985.

[79] 88 Fed. Reg. at 75985.

[80] 88 Fed. Reg. at 75986.

[81] As a reminder, the 2016 BIC exemption included a similar list of prohibitions. It further included language clarifying that "neutral factors tied to the differences in the services delivered" (as opposed to the difference in the amounts the service provider receives in connection with a particular investment) appear to be required for differential compensation at the adviser level. See BIC exemption section II(d)(3).

[82] Proposed section II(c)(2).

[83] 88 Fed. Reg. at 75987.

[84] 88 Fed. Reg. at 75987.

[85] 88 Fed. Reg. at 75987.

[86] 88 Fed. Reg. at 75987.

[87] 88 Fed. Reg. at 75989.

[88] 88 Fed. Reg. at 75989.

[89] Relevant convictions include those for:

any felony involving abuse or misuse of such person's employee benefit plan position or employment, or position or employment with a labor organization; any felony arising out of the conduct of the business of a broker, dealer, investment adviser, bank, insurance

company or fiduciary; income tax evasion; any felony involving larceny, theft, robbery, extortion, forgery, counterfeiting, fraudulent concealment, embezzlement, fraudulent conversion, or misappropriation of funds or securities; conspiracy or attempt to commit any such crimes or a crime in which any of the foregoing crimes is an element; or a crime that is identified or described in ERISA section 411. [Proposed section III(a)(1)(A).]

[90] The current bases for DOL issuing a notice of ineligibility would largely be carried over. These include engaging in a systematic pattern or practice of violating the conditions of the exemption in connection with otherwise non-exempt prohibited transactions; intentionally violating the conditions of the exemption in connection with otherwise non-exempt prohibited transactions; and providing materially misleading information to DOL in connection with the conditions of the exemption. These correspond to proposed section III(a)(2)(A), (B), and (D).

[91] 88 Fed. Reg. at 75989.

[92] 88 Fed. Reg. at 75989.

[93] 88 Fed. Reg. at 75990.

[94] DOL explains that proposed PTE 84-24 would "provide a narrowly tailored, alternative exemption allowing independent insurance agents to receive commissions from insurance companies with respect to annuity recommendations. 88 Fed. Reg. at 76005. DOL's stated objective "is to provide a level playing field for all investment advice fiduciaries." Id.

[95] 88 Fed. Reg. at 76006.

[96] 88 Fed. Reg. at 76007. Referring to the 2016 amendments, DOL expresses concern that the PTE has been interpreted too broadly to cover non-commission payments and fees. See footnote 11.

[97] 88 Fed. Reg. at 76006.

[98] 88 Fed. Reg. at 76006.

[99] 88 Fed. Reg. at 76009. See Proposed section VII(b)(6) (note that the subsections within section VII(b) are misnumbered and this should be subsection (b)(8)).

[100] 88 Fed. Reg. at 76010.

[101] 88 Fed. Reg. at 76009.

[102] 88 Fed. Reg. at 76010.

[103] 88 Fed. Reg. at 76011.

[104] 88 Fed. Reg. at 76012.

[105] 88 Fed. Reg. at 76008.

[106] Proposed section IX(a).

[107] 88 Fed. Reg. at 76034. This statement only would apply to Parts III and IV of PTE 75-1.

[108] 88 Fed. Reg. at 76034.

[109] 88 Fed. Reg. at 76034.

[110] As evidence of this determination, DOL cites to the preamble of its 2016 amendments. 88 Fed. Reg. at 76034, see footnote 12.

[111] In the preamble, DOL requests comment regarding whether fiduciaries providing discretionary investment management services on the purchase or sale of a mutual fund security in a principal transaction need the relief currently provided by PTE 75-1, Part II(2), and, if so, what conditions would be appropriate. 88 Fed. Reg. at 76035.

[112] For a summary of proposed amendments to PTE 84-14, a longstanding exemption governing financial institutions acting as qualified professional asset managers (or QPAMs), see ICI Memorandum No. 34239, dated August 3, 2022, available at https://www.ici.org/memo34239.

[113] 88 Fed. Reg. at 76035.

[114] 88 Fed. Reg. at 76035.