

# CLIENT ACTION Bulletin

Employee Benefits

## DoL Issues Final Rule on Fiduciary/Conflicts of Interest

**SUMMARY** The Department of Labor has released a final rule redefining “fiduciary” under ERISA, focusing on individuals who provide investment advice or recommendations to retirement plan savers for a fee. The rule requires investment advisers to adhere to a fiduciary standard – that is, they must act in a client’s best interest – when advising retirement plan participants, such as on whether to rollover funds from an employer-sponsored 401(k) plan or on what funds to invest in for individual retirement accounts (IRAs). The agency concurrently published related guidance to exempt certain activities from the conflict-of-interest rule, allowing advisers to continue to receive fees or compensation if they comply with the fiduciary standard. The final rule generally applies beginning Apr. 10, 2017, although portions become effective Jan. 1, 2018.

The package of the final rule and related guidance on class exemptions and prohibited transaction exemption amendments is lengthy and complex; this *Client Action Bulletin* highlights the key areas covered for retirement plan sponsors. The rule applies to tax-qualified plans under ERISA; it does not affect 457 governmental plans or 403(b) tax-sheltered annuities under a governmental plan or a nonelecting church plan.

### DISCUSSION Implications for Plan Sponsors

The final rule primarily addresses financial/investment advisers/brokers and their operations, which were not considered fiduciaries under the 1975 rule and instead operated under a “suitability” standard that generally permits recommending products based on a client’s tolerance for risk. The new rule instead requires these advisers to comply with the ERISA fiduciary standard when advising clients for a fee, thereby likely altering the landscape for retirement plan participants who consider rolling over their account balances to individual retirement accounts (IRAs). Areas the final rule addresses include: types of investment products available; recommendations, advice, disclosure, and education; conflicts of interest; fees and commissions; and prohibited transaction exemptions.

**For employers that sponsor 401(k)** or other similar defined contribution retirement plans, the final rule exempts certain common practices from the fiduciary standards, deeming the following as not constituting investment advice or not providing investment recommendations to participants:

- *Investment education* – The final rule describes the types of information and activities that constitute investment education exempt from the fiduciary standard. Included are: information about the plan and its terms, as well as general financial, investment, and retirement information that does not address specific products or options. The rule permits asset allocation models and interactive investment materials that apply graphs, charts, and case studies, requiring that the models be based on generally accepted theories and disclose all material facts and assumptions. The models also must state that individuals should consider their own circumstances. Models may identify specific designated investment funds, as long as the plan’s fiduciary (who is not the investment fund provider) selected and periodically monitors the models and the investment alternatives. These models must also identify all of the plan’s other alternatives with similar risk and return characteristics and must point participants to where information about the other alternatives is available. A self-directed brokerage account option in a 401(k) plan is not considered investment education.
- *Communications by certain employees of the plan sponsor* – The final rule does not treat as fiduciary advice many routine communications that some of the plan sponsor’s employees may make to the plan’s fiduciary. Human resources, payroll, accounting, and financial department employees making recommendations to the plan’s named fiduciary (e.g., the plan sponsor and/or an affiliate) are not considered investment advisers who are subject to the fiduciary

standard unless they are paid fees or other compensation for the advice beyond their normal pay for work performed for the employer. These employees also may continue to communicate with participants about the plan and its options/features or discuss related issues without giving investment advice or recommendations, provided they are not registered or licensed advisers.

### Additional Issues for Plan Sponsors

Other key issues addressed include:

- *Call centers* – A single investment advice contract between the plan sponsor and any third-party (e.g., a call center) providing individualized investment advice for plan participants will be necessary, rather than an individual contract for each plan participant and the same third-party adviser. (See also, “Rollovers,” below.)
- *Rollovers* – An adviser to participants regarding rolling over 401(k) plan assets to an IRA is subject to the final rule’s fiduciary standards. Thus, call center employees must adhere to the fiduciary standards if they provide advice or recommendations on rollovers or other distributions to plan participants.
- *Investment platforms* – Third-party recordkeepers or administrators offering a menu of investment alternatives for a plan’s fiduciary to select from will avoid triggering the fiduciary status if the plan’s fiduciary is independent of the platform provider and if the investment platform provider states in writing that it is not providing impartial investment advice or giving advice in a fiduciary capacity. Marketing or making available an investment platform without considering the plan’s individualized needs, participants, or beneficiaries will not be considered making a recommendation.
- *Revenue sharing* – The final rule treats revenue sharing not as a fee or compensation, but as an “incidental economic advantage” that an employer may gain by sponsoring a retirement plan. Thus, a plan sponsor may use amounts generated by plan investments held in an ERISA budget account to pay for plan expenses.
- *Advisers to small plan sponsors (under \$50 million in assets) and participants* – Financial/investment firms and the individual advisers/brokers who work for them may continue their commission-based fees or other compensation structures when advising small plans under the “best interest contract exemption” (BICE). Under the BICE, the financial institution must acknowledge its fiduciary status for itself and its advisers, commit to putting their clients’ best interests first, and disclose conflicts of interest, among other requirements. The financial institution also must have policies and procedures designed to mitigate the harmful effects of conflicts of interest.
- *Seller’s exception and retirement plan fiduciaries* – A separate “seller’s exception” in the final rule permits investment advisers to avoid being classified as a fiduciary when marketing services to “independent fiduciaries with financial expertise,” including, retirement plan fiduciaries holding or having under management or control plan and nonplan assets totaling at least \$50 million.
- *Appraisals, including for employee stock ownership plans* – The final rule reserves for future regulatory development all appraisal and valuation issues.
- *Health savings accounts* – The final rule applies to benefits that include an investment component, such as HSAs, and not to group health, disability, dental, and term life insurance policies or benefits.

**ACTION** Plan sponsors should review the final rule and related guidance and take steps to ensure compliance with the new definition of fiduciary and the conflict-of-interest requirements. Seeking advice from legal and other professionals will be prudent, given the comprehensive standards and complex issues raised. Among the key areas to consider are: a review of contracts with investment advisers and third-party recordkeepers or administrators; employee training on fiduciary matters; communications with participants about the possible effects of the rule; and modifications to retirement plan educational materials to ensure that the information does not cross over into the realm of investment advice.

Although the rule will have the largest effect on defined contribution individual account plans, defined benefit plans that provide lump-sum distributions also will be affected, to the extent that advisers make recommendations on those distributions.

For additional information about the services Milliman provides, please contact your Milliman consultant. Milliman does not provide legal advice; please contact your legal adviser for specific information on how the new DoL fiduciary/conflict of interest rule may affect you.