

## Publications

# District Court Vacates DOL Interpretation of Investment Advice

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Does combining a recommendation to take a rollover from a retirement plan with post-rollover advice mean that advice is being provided on a “regular basis” under the Department of Labor’s (“DOL”) five-part test for fiduciary investment advice status?

In *American Securities Ass’n v. United States Dep’t of Labor*, a United States District Court answered “No” – recommendations to employee benefit plans must be analyzed separately from recommendations to IRAs to determine whether the regular basis prong of the five-part test has been met. No. 8:22-CV-330-VMC-CPT, 2023 WL 1967573 (M.D. Fla. Feb. 13, 2023). In so doing, the Court vacated the policy underlying guidance DOL issued in 2021 as one of a series of “[Frequently Asked Questions](#)” (or FAQs), which stated advice to rollover from a plan may be part of an ongoing advice relationship that satisfies the regular basis prong.

This decision is notable because it signals a growing divide between DOL and the courts over the definition of investment advice. Both the Obama and Trump Administrations took steps to expand the scope of those deemed to function as investment advice fiduciaries, but courts have disagreed with the DOL on both procedural and substantive grounds. DOL leadership under the Biden Administration has repeatedly stated its intent to issue a new regulation and consider changes to key prohibited transaction exemptions (“PTEs”), including PTE 2020-02 and PTE 84-24.

## I. Background

The DOL defined “investment advice” in a 1975 regulation on the term “fiduciary”. The regulation states that a person provides “investment advice” if he or she: (1) renders advice to a plan as to the value of securities or other property, or makes recommendations as to the advisability of investing in, purchasing, or selling securities or other property; (2) on a regular basis; (3) pursuant to a mutual understanding; (4) that such advice will be a primary basis for investment decisions; and that (5) the advice will be individualized to the plan. This is known as the “five-part test.” In order for a person to be a fiduciary for purposes of the Employee Retirement Income Security Act of 1974, as amended (“ERISA”) and the Internal Revenue Code of 1986, as amended (the “Code”) by reason of providing “investment advice,” each of the five parts or “prongs” of the test must be met.

The DOL finalized a regulation and several PTEs fundamentally reinterpreting the definition of investment advice during the Obama Administration, but the Fifth Circuit Court of Appeals vacated the rulemaking in 2018. The DOL then reinstated the five-part test and issued PTE 2020-02 to allow allegedly “conflicted” advice arrangements.

However, aside from describing PTE 2020-02’s terms, the DOL used the preamble of PTE 2020-02 to provide a novel interpretation of the five-part test. With respect to the regular basis prong, the DOL stated that when an advisor has not previously provided advice but expects to regularly make investment recommendations with respect to an IRA as part of an ongoing relationship, a recommendation to roll assets out of an ERISA plan into an IRA would be the start of an advice relationship that satisfies the regular basis prong. Thus, DOL stated that an initial recommendation without a prior relationship can satisfy the regular basis prong and therefore be considered fiduciary investment advice under the five-part test. The DOL took the view that “it is appropriate to conclude that an ongoing advisory relationship spanning both the Title I Plan and the IRA satisfies the regular basis prong.” The DOL reiterated this point in FAQ 7 of its 2021 FAQs.

PTE 2020-02 requires the investment professional providing advice to document the specific reasons why rollover advice is in the best interest of the retirement investor receiving the advice. In the preamble to PTE 2020-02 and FAQ 15 of the 2021 FAQs, the DOL discussed the factors that should be considered and documented in determining whether a rollover from an ERISA plan to an IRA may be in the interest of the retirement investor. These include:

- The retirement investor’s alternatives to a rollover, including leaving the money in his or her current employer’s plan, if permitted, and selecting different investment options;
- The fees and expenses associated with both the plan and the IRA;
- Whether the employer pays for some or all of the plan’s administrative expenses; and
- The different levels of services and investments available under the plan and the IRA.

On February 2, 2022, the Federation of Americans for Consumer Choice (“FACC”) filed suit against the DOL in the United States District Court for the Northern District of Texas seeking to set aside the DOL’s guidance on the five-part test set forth in the preamble to PTE 2020-02. The American Securities Association (“ASA”) quickly followed, filing this case on February 9, 2022. The ASA alleged that the policies underlying FAQs 7 and 15 in the DOL’s 2021 guidance were arbitrary and capricious in violation of the Administrative Procedure Act. Because FAQ 7 restated the DOL’s position set forth in the preamble to PTE 2020-02, the ASA and FACC’s lawsuits overlap – with both challenging the DOL’s new interpretation of the regular basis prong of the five-part test.

## II. The Court’s Decision

The Court in *ASA* held the DOL’s new interpretation of the regular basis prong, described in FAQ 7, was arbitrary and capricious because it contradicted the plain language of the DOL’s 1975 fiduciary investment advice regulation. The Court also determined that FAQ 7 constituted an unreasonable interpretation of ERISA’s statutory text. Relying on the analysis of the recent [\*Carfora v. Teachers Insurance Annuity Association of America\*](#) district court decision, the Court noted that ERISA’s statutory text and the 1975 regulation define fiduciary investment advice as advice given “to a particular plan.” The Court reasoned that in the context of a rollover, any investment advice that may be given after the rollover occurs is “inherently divorced from the ERISA-governed plan” and not captured within the analysis of whether the regular basis prong of the five-part test has been met with respect to the plan. Because the DOL’s interpretation described in FAQ 7 would combine advice given to the plan with advice given post-rollover, the Court held that FAQ 7 was unreasonable, and, as a result, vacated the policy underlying FAQ 7. In this respect, the Court noted that its decision to vacate the “policy” underlying FAQ 7 would extend to the corresponding discussion in the preamble to PTE 2020-02, in addition to FAQ 7 itself.

Separately, the Court upheld FAQ 15 as containing a permissible interpretation of PTE 2020-02. The Court reasoned that PTE 2020-02 requires a financial institution, when making a recommendation to rollover, to document the reasons it found the recommendation to be in the best interest of the retirement investor. While FAQ 15 specifies factors to document, the Court did not find any of the specified factors to be outside the scope of PTE 2020-02 or to impose new requirements. Indeed, the Court held that documenting the factors would be consistent with the impartial conduct standards of PTE 2020-02.

## III. Implications and Next Steps

Although only a district court decision – and one that may be appealed – the *ASA* decision is an important development in that it adds to the growing body of case law analyzing and interpreting the five-part test. Like in *Carfora*, the *ASA* decision interprets the “regular

basis” prong of the five-part test much more narrowly than the DOL. However, the decision does not discuss scenarios where a financial institution has been providing investment recommendations to an individual in a retirement account and then provides rollover advice to the individual. There, the DOL may assert that the regular-basis prong (and the five-part test in general) is met such that the recommendation to rollover will be considered fiduciary investment advice.

Importantly, the *ASA* and *Carfora* decisions highlight the fact that the DOL’s sub-regulatory interpretations do not have the force and effect of law. They are a clear indication that at least some courts are skeptical of efforts to fundamentally reinterpret a regulation that is almost 50 years old. Of course, neither of the decisions prevent the DOL from amending the investment advice regulation, and the DOL has included a fiduciary investment advice regulation on its regulatory agenda. However, given the Fifth Circuit’s 2018 decision, any formal regulations may also face a new challenge.