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DOL Interprets Five-Part Investment Advice Test and Issues Final Investment Advice Prohibited Transaction Exemption

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On December 15, 2020, the U.S. Department of Labor (the "DOL") issued its highly anticipated final prohibited transaction class exemption for fiduciary investment advice (the "Final Exemption"). The Final Exemption, which will be officially designated "Prohibited Transaction Exemption 2020-02," serves two broad functions. First, in the preamble, the DOL provides its "Final Interpretation" of the five-part test under its 1975 regulation defining who is an investment advice fiduciary under the Employee Retirement Income Security Act of 1974, as amended ("ERISA") and Section 4975 of the Internal Revenue Code (the "Code"). Second, in its operative text, the Final Exemption makes available prohibited transaction exemptive relief for such fiduciaries, subject to certain conditions.

The Final Exemption is the latest development in the DOL's longstanding efforts to regulate the provision of investment advice to ERISA plans and their participants and IRAs. However, while the exemption is described as "final," it is likely not the DOL's final pronouncement in this area. Because there will be a change of administration prior to the Final Exemption's effective date, it is very likely that new leadership at the DOL will reassess the Final Exemption, which could result, at the very least, in a delay of the effective date.

In this alert, we provide an overview of the Final Exemption. We begin with the DOL's interpretation of the five-part test, including its application to rollover advice. We then summarize the actual exemption and describe its coverage and conditions.

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I. Final Interpretation of Five-Part Test

The DOL's interpretation of the five-part test—which is arguably of greater significance than the exemption itself—does not appear in the Final Exemption's text; it is addressed in the preamble alone. Although refined to some degree in response to comments on the DOL's proposed exemption that preceded the Final Exemption, the DOL retains an expansive interpretation of certain prongs of the five-part test, which could result in a broadening of the universe of those considered to be investment advice fiduciaries. This broadening could, in turn, increase the need for prohibited transaction relief under ERISA and the Code.

A. The Five-Part Test

By way of background, the DOL established the definition of "investment advice" by regulation in 1975. 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 ERISA and the Code by reason of providing "investment advice," each of the five parts or "prongs" of the test must be met. Historically, the DOL has issued very little guidance on how to interpret each of the prongs. Financial services firms have often been able to interpret the five-part test in a manner that allows the firms and their employees, representatives and agents to not be fiduciaries. Additionally, DOL guidance issued in 2005 (discussed below) established that recommendations to take a distribution from a plan and rollover to an IRA was not investment advice for purposes of ERISA and the Code.

B. "Regular Basis" Prong

The DOL says the "regular basis" prong "broadly describes a relationship where advice is recurring, non-sporadic, and expected to continue." The DOL notes that objective evidence, "such as the parties agreeing to check-in periodically on the performance of the customer's post-rollover financial products" or a service provider holding itself "out to the customer as providing such ongoing services" could satisfy the regular basis requirement.

The DOL confirms that not all investment advice relationships satisfy the regular basis requirement. Specifically, the DOL "intends to preserve the ability of financial services professionals to engage in one-time sales transactions without becoming fiduciaries . . . including by assisting with a rollover." In this regard, parties intending such one-time, non-fiduciary relationships "can make clear in their communications that they do not intend to enter into an ongoing relationship to provide investment advice and act in conformity with that communication." Notably, the DOL emphasizes that actual conduct is determinative, and thus even after making such clarifications, fiduciary status could arise from an investment advice provider's actual conduct.

The DOL similarly confirms that certain "sporadic" interactions would not satisfy the regular basis prong. For example, the regular basis prong would not be satisfied in situations where a plan participant initially receives rollover assistance but "expresses the intent to direct his or her own investments," and then at some point in the future receives advice from the same adviser.

C. "Mutual Agreement" Prong

The DOL notes that if a mutual agreement or arrangement is not clearly demonstrated, it will consider the "reasonable understanding" of the parties to determine whether the "mutual agreement" requirement is satisfied. As with the other prongs of the five-part test, the DOL emphasizes that determining whether a mutual agreement exists depends on the facts and circumstances. In this regard, the DOL notes that it "intends to consider marketing materials in which Financial Institutions and Investment Professionals hold themselves out as trusted advisers" in determining whether the requirement is satisfied.

Notably, the DOL reaffirms that contractual terms or written statements "disclaiming a mutual understanding or forbidding reliance on the advice as a primary basis for investment decisions" are not determinative with respect to whether a mutual agreement exists. In particular, the DOL cautions that "[a] financial services provider should not, for example, expect to avoid fiduciary status through a boilerplate disclaimer buried in the fine print, while in all other communications holding itself out as rendering best interest advice that can be relied upon by the customer in making investment decisions."

D. "Primary Basis" Prong

With respect to the "primary basis" prong, the DOL interprets the five-part test to require that advice be "a" rather than "the" primary basis of investment decisions, as reflected in the actual regulatory text. In this regard, the DOL notes that the primary basis prong does not require "proof that the advice was the single most important determinative factor" in an investment decision. Rather, it takes the view that the primary basis prong is met as long as it is reasonably understood that "the advice is important to the Retirement Investor and could determine the outcome of the investor's decision." Additionally, the DOL expressed its view that the "primary basis" prong could be met even if an investor consults with multiple financial professionals. Indeed, any one of those professionals may meet this prong of the test "…[i]f, in each instance, the parties reasonably understand that the advice is important to the Retirement Investor and could determine the outcome of the investor's decision…"

E. Rollover Advice

1. Status of Deseret Advisory Opinion

A key aspect of the DOL's interpretation of the five-part test is its confirmation that Advisory Opinion No. 2005-23A (the "Deseret Opinion") no longer reflects its views regarding fiduciary status in the context of rollover recommendations. Specifically, the DOL now clarifies that its statement in the Deseret Opinion that advice to take a distribution of assets from an ERISA plan is not advice to sell, withdraw, or transfer investment assets is incorrect. According to the DOL, the "better view" is that a recommendation to roll assets out of an ERISA plan *is* advice with respect to moneys or other property of a plan, which must be further evaluated in the context of the full five-part test. Since each prong of the five-part test would need to be satisfied, the DOL acknowledges "that not all rollover recommendations can be considered fiduciary investment advice." In this regard, the DOL "acknowledges that a single instance of advice to take a distribution from a Title I Plan and roll over the assets would fail to meet the regular basis prong." In response to concerns about potential liability for past reliance on the Deseret Opinion for rollover transactions, the DOL confirms that it "will not pursue claims for breach of fiduciary duty or prohibited transactions against any party, or treat any party as violating the applicable prohibited transaction rules" for conduct between 2005 and February 16, 2021 (the effective date of the Final Exemption).

2. Extent of Fiduciary Relationship

The DOL says that rollover advice can mark "the beginning of an ongoing relationship," and that, in those circumstances, the entire advisory relationship, "including the first instance of advice," will be considered fiduciary in nature. This position, when published in the proposed exemption, generated some concern within the regulated community regarding the extent to which a relationship would be considered "fiduciary" if the relationship touched multiple retirement accounts (*i.e.*, a Title I plan and an IRA). Specifically, several commenters argued that advisory relationships should be viewed as specific to each retirement account, and that by ignoring the precise timing for the start and end of such relationships, the DOL's interpretation could result in "retroactive" fiduciary status.

In response to such comments, the DOL notes that its view "merely recognizes that the rollover recommendation can be the beginning of an ongoing advice relationship," and that in such situations, fiduciary status should extend "to the entire advisory relationship, including the first—and often most important—advice on rolling the investor's retirement savings out of the Title I Plan in the first place." The DOL further notes that its position does not result in "retroactive" fiduciary status because fiduciary status is ultimately "determined by the facts as they exist at the time of the recommendation, including whether the parties, at that time, mutually intend an ongoing advisory relationship."

In addressing advice provided to multiple retirement accounts, the DOL notes that it disagrees that the regular basis prong of the five-part test "must first be met with respect to the Title I Plan, and then again with respect to the IRA." Instead, the DOL takes 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." In justifying this position, the DOL argues that "[i]t is enough . . . that the same financial services provider is giving advice to the same person with respect to the same assets (or proceeds of those assets), pursuant to identical five-part tests."

II. Final Exemption

Broadly speaking, the Final Exemption allows financial institutions to give fiduciary investment advice to ERISA plans, ERISA plan participants, and IRAs and to receive otherwise prohibited compensation resulting from that advice if certain conditions are satisfied. Further, the exemption permits a fiduciary to engage in riskless principal transactions and certain other principal transactions as described below. Unlike other existing statutory and administrative exemptions that only apply to particular transactions or investment products, the Final Exemption might be viewed as a "one stop shop" for providers of many types of fiduciary investment advice. The Final Exemption also reflects the DOL's desire to harmonize its approach with that of the Securities and Exchange Commission (the "SEC") in Regulation Best Interest ("Reg BI") and the National Association of Insurance Commissioners (the "NAIC") Suitability in Annuity Transactions Model Regulation (the "NAIC Model Regulation").

A. Rationale for Exemption

The Final Exemption is intended to provide prohibited transaction relief to financial institutions that have fiduciary investment advice programs. Many institutions created or expanded their advice programs as a consequence of the DOL's 2016 investment advice regulation, and they relied on the Best Interest Contract Exemption to receive compensation. After the Fifth Circuit Court of Appeals vacated the 2016 regulation and the Best Interest Contract Exemption in 2018, the DOL issued a temporary non-enforcement policy to allow the advice programs to continue. The Final Exemption provides permanent relief, provided it takes effect. The Final Exemption is particularly important given the DOL's new, more expansive interpretation of the five part test.

B. Summary of Significant Changes to the Proposed Exemption

The Final Exemption generally retains the structure of the DOL's proposed exemption, which was issued in June 2020. Overall, while some changes were made to the conditions for relief, there are no changes to the DOL's proposal with respect to the broad exemptive coverage available under the Final Exemption. Notable changes to the conditions for relief include:

- More flexibility in completing the annual retroactive review condition of the proposed exemption by allowing the review to be certified by a senior officer other than a financial institution's CEO,
- A new procedure by which financial institutions may self-correct violations of the exemption's conditions.
- A narrower group of entities that can request documentation from the financial institution concerning its compliance.
- A new disclosure that must be provided to Retirement Investors in connection with rollover recommendations.

C. Covered Transactions and Relief Provided

The Final Exemption provides relief from the restrictions of ERISA sections 406(a)(1)(A),(D), and 406(b) and Internal Revenue Code of 1986, as amended ("Code") sections 4975(c)(1)(A),(D), (E), and (F) for the receipt of prohibited compensation in connection with the provision of non-discretionary investment advice. The Final Exemption exempts prohibited transactions that arise from the payment of otherwise prohibited compensation in connection with the recommendation of any security or investment product, and fiduciary rollover recommendations, as well as recommendations of investment managers and investment advice providers. Moreover, the Final Exemption covers recommendations of a financial institution's proprietary investment products or investment products that generate payments from third parties. Finally, in addition to recommendations to engage in agency transactions, the Final Exemption covers recommendations to engage in riskless principal transactions and principal transactions involving certain types of covered securities, described below.

D. Covered Recipients of Advice

The Final Exemption applies to investment advice given to "Retirement Investors," which include (i) a participant or beneficiary of a plan subject to Title I of ERISA, or a plan described in section 4975(e)(1)(A) of the Code but not subject to Title I of ERISA[1] (in either case, a "Plan") with authority to direct the investment of assets in his or her Plan account or to take a distribution, (ii) the beneficial owner of an IRA acting on behalf of the IRA,[2] and (iii) a fiduciary with respect to an Plan or IRA (no matter the size of the Plan). Despite the use of the term "Retirement Investor," the DOL confirms in the Final Exemption's preamble that advice to fiduciaries, participants, and beneficiaries with respect to ERISA welfare plans with an investment component is covered.

E. Covered Providers of Advice

Investment advice fiduciaries – both individual "Investment Professionals" and the "Financial Institutions" that employ or otherwise contract with them – and their Affiliates[3] and Related Entities[4] are eligible for relief under the Final Exemption.

- An "Investment Professional" is an employee, independent contractor, agent, or registered representative of a "Financial Institution" who acts as a fiduciary of a Plan or IRA when providing covered investment advice under the Final Exemption and satisfies applicable law and licensing requirements with respect to receipt of compensation.
- A "Financial Institution" is a registered investment adviser, bank, insurance company, or registered broker-dealer that employs an Investment Professional or otherwise retains the Investment Professional as an independent contractor, agent, or registered representative. Notably, the DOL declined to include independent marketing organizations, field marketing organizations, or brokerage general agencies who may supervise independent insurance agents

[1] Plans described in section 4975(e)(1)(A) of the Code but not subject to ERISA may include plans for self-employed individuals and their spouses, such as Keogh plans or solo 401(k) plans. *See* 29 C.F.R. § 2510.3-3.

[2] IRAs are defined to include Health Savings Accounts, Archer Medical Savings Accounts, and Coverdell Education Savings Accounts.

[3] The term "Affiliate" refers to (1) any person directly or indirectly through one or more intermediaries, controlling, controlled by, or under common control with the Investment Professional or Financial Institution, (2) any officer, director, partner, employee, or relative (as defined in ERISA section 3(15)), of the Investment Professional or Financial Institution, and (3) any corporation or partnership of which the Investment Professional or Financial Institution is an officer, director, or partner.

[4] The term "Related Entity" refers to entities that are not affiliates, but in which the Investment Professional or Financial Institution has an interest that may affect the exercise of its best judgment as a fiduciary.

within the definition of Financial Institutions covered under the Final Exemption. Moreover, the DOL declined to cover Plan recordkeepers that do not otherwise meet the definition of a "Financial Institution." However, the DOL stated that such organizations could apply to the DOL for individual prohibited transaction exemptions and, in the case of insurance intermediaries, thereby expand the Final Exemption to gain coverage as Financial Institutions.

F. Exclusions

The Final Exemption is not available where:

- The Investment Professional, Financial Institution, or Affiliate is the employer of employees covered by the ERISA-covered Plan.
- The Investment Professional or Financial Institution is a named fiduciary or plan administrator (or an affiliate thereof) of an ERISA-covered Plan, unless the Investment Professional or Financial Institution was selected to provide advice by an independent fiduciary. Commenters noted that the application of this provision is unclear in connection with pooled employer plans under section 3(43) of ERISA, where the plan administrator of such plan would be a "Pooled Plan Provider." In particular, commenters asked the DOL to clarify that an affiliate of the Pooled Plan Provider would be permitted to provide advice to participants and beneficiaries in reliance upon the Final Exemption. However, the DOL declined to address pooled employer plans in the Final Exemption.
- The Investment Professional exercises discretion with respect to the transaction.
- The transaction involves only "robo-advice" (*i.e.*, investment advice generated solely by an interactive web site in which computer software-based models or applications provide investment advice based on personal information supplied by investors through the website, without personal interaction with or advice from an Investment Professional). However the Final Exemption covers "hybrid" robo-advice arrangements where an Investment Professional is personally involved.

Investment Professionals and Financial Institutions are ineligible to rely on the Final Exemption in certain circumstances, in each case for a period of ten years:

- The Investment Professional, Financial Institution, or a member of the Financial Institution's Controlled Group[5] is convicted of a crime described in section 411 of ERISA[6] arising out of investment advice to a Retirement Investor. The Investment Professional would immediately become ineligible to rely on the Final Exemption, but the Financial Institution would be permitted to petition the DOL for permission to continue to rely on the exemption.

[5] The term "Controlled Group" is defined by reference to the terms "controlled group of corporations" or "under common control" under Code section 414(b) and (c), and their accompanying regulations.

[6] Section 411 of ERISA restricts individuals convicted of certain crimes from serving in certain positions with respect to an ERISA plan, including as a fiduciary.

- The DOL issues a finding that the Investment Professional, Financial Institution, or a member of the Financial Institution's Controlled Group has (a) engaged in a systematic pattern or practice of violating the conditions of the Final Exemption in connection with otherwise non-exempt prohibited transactions; (b) intentionally violated the conditions of the Final Exemption in connection with otherwise non-exempt prohibited transactions; or (c) provided materially misleading information to the DOL in connection with the Financial Institution's conduct under the exemption. Prior to making such a finding, the DOL would provide a warning and a six-month opportunity to cure the violation. If the DOL believes the behavior has not been cured, it would provide the Investment Professional or Financial Institution an opportunity to be heard.

G. Final Exemption Conditions

Investment Professionals and Financial Institutions must comply with all of the following conditions to obtain relief under the Final Exemption:

1. Impartial Conduct Standards

The Investment Professional and Financial Institution must satisfy certain Impartial Conduct Standards:

- **Best Interest Standard**. Investment advice must meet a "Best Interest" standard, meaning it "reflects the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims, based on the investment objectives, risk tolerance, financial circumstances, and needs of the Retirement Investor, and does not place the financial or other interests of the Investment Professional, Financial Institution or any affiliate, related entity, or other party ahead of the interests of the Retirement Investor, or subordinate the Retirement Investor's interests to their own." The DOL notes that the language prohibiting placing the interests of the investment advice fiduciaries "ahead" of the advice recipient and prohibiting "subordinat[ion]" of the advice recipient's interest was intended to harmonize the Final Exemption's Best Interest standard with the Best Interest standard in the SEC's Reg BI and the standard in the NAIC Model Regulation. The DOL also notes that the standard is consistent with the fiduciary duties of prudence and loyalty under ERISA.
- **Reasonable Compensation Standard**. An investment recommendation may not cause a Financial Institution, an Investment Professional, or their affiliates or related entities to receive, directly or indirectly, compensation for their services that exceeds "reasonable compensation" within the meaning of ERISA section 408(b)(2) and Code section 4975(d)(2). Notably, an Investment Professional and Financial Institution do not have to recommend a transaction that involves the lowest cost or that generates the lowest fees. In this regard, the DOL notes that focusing solely on cost may in fact violate the Best Interest standard.
- **Best Execution Standard**. The Financial Institution and Investment Professional must seek to obtain best execution of the investment transaction reasonably available under the

circumstances. The DOL intends for the best execution condition to encompass best execution requirements already applicable to certain Financial Institutions under securities laws, including FINRA, the Municipal Securities Rulemaking Board, and the Investment Advisers Act rules (*i.e.*, compliance with such requirements would satisfy the best execution standard).

- **No Materially Misleading Statements Standard**. The Financial Institution and Investment Professional must not make statements about the recommended transaction and other relevant matters that are materially misleading. For example, the DOL says a Financial Institution's inclusion of exculpatory language in a contract that is not compliant with applicable law (including state law) would be misleading because it may discourage a Retirement Investor from asserting rights that it would otherwise have.

2. Disclosure

A Financial Institution must provide the following written disclosures to the Retirement Investor prior to a covered investment recommendation:

- A written acknowledgment that the Financial Institution and its Investment Professionals are fiduciaries under ERISA and the Code, as applicable, with respect to fiduciary investment advice provided to the Retirement Investor. The DOL considered removing or replacing the acknowledgment with a disclosure of the Best Interest standard, but it decided to require a fiduciary acknowledgement to prevent Investment Professionals and Financial Institutions who rely on the exemption from later claiming that they did not act as investment advice fiduciaries. The preamble to the Final Exemption includes some sample language in this regard that may be included in a Financial Institution's disclosures.
- A written description of the Financial Institution's and Investment Professional's services and material conflicts of interest that is accurate and not misleading in all material respects. A conflict of interest is "an interest that might incline a Financial Institution or Investment Professional - consciously or unconsciously - to make a recommendation that is not in the Best Interest of the Retirement Investor."
- With respect to rollover recommendations only, documentation of the specific reasons why the rollover recommendation is in the Best Interest of the Retirement Investor. For this purpose, a rollover includes rollovers from a Plan to an IRA, from an IRA to an IRA, and from an IRA to a Plan. Moreover, a transfer from one type of account to another (*e.g.*, fee-based to commission-based accounts) is covered for this purpose.
    - The documentation of a rollover from an ERISA-covered Plan to an IRA should include (1) 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; (2) the fees and expenses associated with both the plan and the IRA; (3) whether the employer pays for some or all of the Plan's administrative expenses; (4) and the different levels of services and investments available under the plan and the IRA. In this regard, an Investment Professional should make a "diligent and prudent effort" to obtain information regarding the Retirement Investor's existing plan and describe the

significance of the information, or otherwise make assumptions of expenses, asset values, risk, and returns based on publicly available information (e.g., the most recent Form 5500 or reliable benchmarks on typical fees and expenses for the type and size of Plan at issue), and explain the limitations of the assumptions.
  - For rollovers from another IRA or changes from a commission-based account to a fee-based arrangement, the DOL stated that documentation should describe the services that would be provided under the new arrangement.

The DOL confirmed that the above disclosure requirements may be satisfied if the relevant information is included in disclosures already mandated by the DOL or other regulators, including disclosures mandated by Regulation Best Interest and Form CRS and, in appropriate circumstances, disclosures under Section 408(b)(2) of ERISA.

3. Policies and Procedures

The Final Exemption requires Financial Institutions to establish, maintain, and enforce policies and procedures that (1) are prudently designed to ensure compliance with the Impartial Conduct Standards and (2) mitigate the Investment Professional's and Financial Institution's conflicts of interests to such an extent that a reasonable person would not view the Financial Institution's incentive practices to create an incentive for the Financial Institution and Investment Professional to place their interests ahead of those of Retirement Investors. Additionally, as noted above, Financial Institutions would need to document and disclose specific information in support of rollover recommendations. Financial Institutions would be required to periodically review and revise their policies and procedures as circumstances dictate.

The preamble to the Final Exemption provides examples of policies and procedures the Financial Institution may adopt in response to certain conflicts of interest and other circumstances.

a. Commission-based Compensation Arrangements

If Investment Professionals are compensated through transaction-based payments and incentives, Financial Institutions' policies and procedures must focus on financial incentives and oversight of investment advice. The DOL notes that conflict mitigation measures identified by the SEC may be adopted by Financial Institutions:

- Avoiding compensation thresholds that disproportionately increase compensation through incremental increases in sales;
- Minimizing compensation incentives for employees to favor one type of account over another; or to favor one type of product over another; proprietary or preferred provider products, or comparable products sold on a principal basis, for example, by establishing differential compensation based on neutral factors;
- Eliminating compensation incentives within comparable product lines by, for example, capping the credit that an associated person may receive across mutual funds or other comparable products across providers;

- Implementing supervisory procedures to monitor recommendations that: are near compensation thresholds; are near thresholds for firm recognition; involve higher compensating products, proprietary products or transactions in a principal capacity; or, involve the rollover or transfer of assets from one type of account to another or from one product class to another;
- Adjusting compensation for associated persons who fail to adequately manage conflicts of interest; and
- Limiting the types of retail customer to whom a product, transaction, or strategy may be recommended.

In a slight shift from the DOL's proposed exemption, the DOL states that the policies and procedures condition is principles-based and therefore does not necessarily prohibit sales contests and similar incentives. The DOL notes, however, that the Financial Institution would be required to carefully consider all performance and personnel actions and practices.

b. Insurance Companies

The DOL states that insurance companies' policies and procedures could incorporate review of products, riders, and annuity features that might incentivize Investment Professionals to provide investment advice that does not comply with the Impartial Conduct Standards as well as review of annuity sales. Additionally, the DOL observes that distribution of insurance products is often conducted by independent agents, and that insurance companies could contract with an insurance intermediary to enforce policies and procedures and oversee agents. Indeed, such contracts may be necessary if these insurance intermediaries are not Financial Institutions. The DOL also notes that insurance companies are not responsible for insurance agents' sales of unaffiliated insurers' products.

c. Proprietary Products, Products that Generate Third Party Payments, and Limited Menus of Investment Products

The DOL confirms that Investment Professionals and Financial Institutions can satisfy the Best Interest standard when they provide investment advice on proprietary products or on a limited menu of investment options, including limitations to proprietary products and products that generate third party payments (*e.g.*, shareholder servicing and distribution fees). However, Investment Professionals and Financial Institutions should provide complete and accurate disclosure of their material conflicts of interest associated with such products.

Additionally, the DOL states that Financial Institutions that offer proprietary products or a limited menu of products should consider whether their offerings allow an Investment Professional to provide advice that meets the Impartial Conduct Standards and whether the offerings create incentives to place the interests of Investment Professionals and Financial Institutions above those of Retirement Investors. For this purpose, the DOL explains that Financial Institutions are not required to compare their offerings to every other available investment in the marketplace. Financial Institutions are not required to document these determinations, but they should be prepared to explain their process.

The DOL also suggests that practices that "selectively promote" certain products may violate the policies and procedures conditions even if the practices do not directly involve the provision of investment advice. For example, Financial Institutions should not make it much more burdensome for the Retirement Investor to rollover assets to one investment rather than another.

4. Annual Retrospective Compliance Review

The Final Exemption requires Financial Institutions to conduct an annual retrospective review reasonably designed to assist in detecting and preventing violations of the Impartial Conduct Standards and the Financial Institution's policies and procedures. The methodology and results of the review must be set forth in a written report submitted to the Senior Executive Officer of the Financial Institution (the CEO, Chief Compliance Officer, Chief Financial Officer, President, or one of the three most senior officers of the Financial Institution), who must certify, within six months of the end of the annual review period that:

- The officer reviewed the report;
- The Financial Institution has in place policies and procedures prudently designed to achieve compliance with the conditions of the Final Exemption; and
- The Financial Institution has in place a prudent process to modify such policies and procedures as business, regulatory and legislative changes and events dictate, and to test the effectiveness of such policies and procedures on a periodic basis, the timing and extent of which is reasonably designed to ensure continuing compliance with the conditions of the Final Exemption.

The Financial Institution must retain the report, certification, and supporting data for a period of six years. These materials must be made available to the DOL within 10 business days of DOL's request for them.

The DOL envisions the annual review process involving a sample of recommended transactions. A Financial Institution's Senior Executive Officer could consult with compliance professionals in making the required certifications. This condition is based upon FINRA rules requiring broker-dealers to engage in annual compliance reviews. However, the DOL declined to provide a safe harbor based on compliance with FINRA rules.

5. Self-Correction

Generally, if an Investment Professional or Financial Institution provides fiduciary investment advice and receives compensation resulting from that advice but fails to fully comply with any of the conditions of the Final Exemption, a non-exempt prohibited transaction will occur. However, in a departure from the DOL's proposed exemption, the Final Exemption permits Financial Institutions to self-correct violations of the Final Exemption. If a Financial Institution follows the self-correction procedure, a non-exempt prohibited transaction will not occur. In order to self-correct a violation of the Final Exemption, a Financial Institution must:

- Correct the violation within 90 days of the date the Financial Institution learns or should have learned of the violation;
- Make the Retirement Investor whole for investment losses, if any;
- Notify the DOL within 30 days of the correction; and
- Report the correction in the Financial Institution's annual retrospective compliance review.

6. Principal Transactions

The Final Exemption is available to exempt prohibited transactions that arise by reason of an Investment Professional or Financial Institution recommending that a Retirement Investor engage in the following principal transactions: (i) a riskless principal transaction; (ii) a principal transaction involving the purchase of a security from a Retirement Investor by the Financial Institution; and, (iii) a principal transaction involving the sale of only certain, specified securities by a Financial Institution to a Retirement Investor ("Covered Principal Transactions"). In the case of Covered Principal Transactions, the security involved in the transaction must be:

- a U.S. dollar denominated debt security issued by a U.S. corporation and offered pursuant to a registration statement under the Securities Act of 1933;
- a U.S. Treasury Security;
- a debt security issued or guaranteed by a U.S. federal government agency other than the U.S. Department of Treasury;
- a debt security issued or guaranteed by a government-sponsored enterprise;
- a municipal security;
- a certificate of deposit; or
- an interest in a Unit Investment Trust.

In addition, for recommendations of sales of debt securities, Financial Institutions are required to adopt policies and procedures reasonably designed to ensure that the security, at the time of the recommendation, has no greater than moderate credit risk and sufficient liquidity that it could be sold at or near carrying value within a reasonably short period of time. In the case of municipal bond investment recommendations to Retirement Investors, the DOL urges Financial Institutions to exercise caution and to consider documenting the reasons for such recommendations.

7. Recordkeeping

Financial Institutions that rely on the Final Exemption must maintain compliance records for a period of six years. Under the proposed exemption, the records would have been made available to certain employers, plan fiduciaries, participants and beneficiaries, and IRA owners upon their request. However, under the Final Exemption, only the DOL and Treasury Department may request these records. The DOL added this limitation on who may request such records in order to restrict Retirement Investors and their attorneys from requesting these records as a mechanism to bring breach of fiduciary duty and other lawsuits against Financial Institutions and Investment Professionals. In other words, the DOL believes that enforcement of compliance with the Final Exemption should primarily lie with the DOL and the Treasury Department rather than the plaintiffs' bar.

III. Temporary Non-Enforcement Policy

On May 7, 2018, the DOL issued transition relief pursuant to Field Assistance Bulletin 2018-02 ("FAB 2018-02") following the vacatur by the Fifth Circuit Court of Appeals of the DOL's 2016 fiduciary investment advice rulemaking. In FAB 2018-02, the DOL assured that it "will not pursue prohibited transaction claims against investment advice fiduciaries who are working diligently and in good faith to comply with the impartial conduct standards for transactions that would have been exempted in the 2016 Best Interest Contract Exemption and Principal Transactions Exemption, or treat such fiduciaries as violating the applicable prohibited transaction rules."

In the preamble to the Final Exemption, the DOL states that FAB 2018-02 will continue to be available for one year following the publication of the Final Exemption (the Final Exemption was published on December 18, 2020).