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**4510-29-P**

**DEPARTMENT OF LABOR**

**Employee Benefits Security Administration**

**29 CFR Part 2550**

**[Application No. D-12011]**

**ZRIN 1210-ZA29**

**Prohibited Transaction Exemption 2020-02, Improving Investment Advice for  
Workers & Retirees**

**AGENCY:** Employee Benefits Security Administration, U.S. Department of Labor.

**ACTION:** Adoption of Class Exemption and Interpretation.

**SUMMARY:** This document contains a class exemption from certain prohibited transaction restrictions of the Employee Retirement Income Security Act of 1974, as amended (the Act). Title I of the Act codified a prohibited transaction provision in title 29 of the U.S. Code (referred to in this document as Title I). Title II of the Act codified a parallel provision now found in the Internal Revenue Code of 1986, as amended (the Code). These prohibited transaction provisions of Title I and the Code generally prohibit fiduciaries with respect to “plans,” including workplace retirement plans (Plans) and individual retirement accounts and annuities (IRAs), from engaging in self-dealing and receiving compensation from third parties in connection with transactions involving the Plans and IRAs. The provisions also prohibit purchasing and selling investments with the Plans and IRAs when the fiduciaries are acting on behalf of their own accounts (principal

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transactions). This exemption allows investment advice fiduciaries to plans under both Title I 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 principal transactions, that would otherwise violate the prohibited transaction provisions of Title I and the Code. The exemption applies to Securities and Exchange Commission - and state-registered investment advisers, broker-dealers, banks, insurance companies, and their employees, agents, and representatives that are investment advice fiduciaries. The exemption includes protective conditions designed to safeguard the interests of Plans, participants and beneficiaries, and IRA owners. The class exemption affects participants and beneficiaries of Plans, IRA owners, and fiduciaries with respect to such Plans and IRAs. This notice also sets forth the Department's final interpretation of when advice to roll over Plan assets to an IRA will be considered fiduciary investment advice under Title I and the Code.

**DATES:** The exemption is effective as of: [INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER].

**FOR FURTHER INFORMATION CONTACT:** Susan Wilker, telephone (202) 693-8557, or Erin Hesse, telephone (202) 693-8546, Office of Exemption Determinations, Employee Benefits Security Administration, U.S. Department of Labor (these are not toll-free numbers).

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## SUPPLEMENTARY INFORMATION

### BACKGROUND

The Employee Retirement Income Security Act of 1974 (the Act) provides, in relevant part, that a person is a fiduciary with respect to a “plan” to the extent he or she renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so. Title I of the Act (referred to herein as Title I), which generally applies to employer-sponsored Plans (Title I Plans), includes this provision in section 3(21)(A)(ii).<sup>1</sup> The Act’s Title II (referred to herein as the Code), includes a parallel provision in section 4975(e)(3)(B), which defines a fiduciary of a tax-qualified plan, including IRAs.<sup>2</sup>

In 1975, the Department issued a regulation establishing a five-part test for fiduciary status under this provision of Title I.<sup>3</sup> The 1975 regulation also applies to the definition of fiduciary in the Code, which is identical in its wording.<sup>4</sup> Under the 1975 regulation, for advice to constitute “investment advice,” a financial institution or investment professional who is not a fiduciary under another provision of the statute must—(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

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<sup>1</sup> Section 3(21)(A)(ii) of the Act is codified at 29 U.S.C. 1002(3)(21)(A)(ii). As noted above, Title I of the Act was codified in Title 29 of the U.S. Code. As a matter of practice, this preamble refers to the codified provisions in Title I by reference to the sections of ERISA, as amended, and not by its numbering in the U.S. Code.

<sup>2</sup> As noted above, Title II of the Act was codified in the Internal Revenue Code.

<sup>3</sup> 29 CFR 2510.3-21(c)(1), 40 FR 50842 (October 31, 1975).

<sup>4</sup> 26 CFR 54.4975-9(c), 40 FR 50840 (October 31, 1975).

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other property (2) on a regular basis (3) pursuant to a mutual agreement, arrangement, or understanding with the Plan, Plan fiduciary or IRA owner, that (4) the advice will serve as a primary basis for investment decisions with respect to Plan or IRA assets, and that (5) the advice will be individualized based on the particular needs of the Plan or IRA. A financial institution or investment professional that meets this five-part test, and receives a fee or other compensation, direct or indirect, is an investment advice fiduciary under Title I and under the Code.

Investment advice fiduciaries, like other fiduciaries to Plans and IRAs, are subject to duties and liabilities established in Title I and the Code. Fiduciaries to Title I Plans must act prudently and with undivided loyalty to the plans and their participants and beneficiaries. Although these statutory fiduciary duties are not in the Code, both Title I and the Code contain provisions forbidding fiduciaries from engaging in certain specified “prohibited transactions,” involving Plans and IRAs, including conflict of interest transactions.<sup>5</sup> Under these prohibited transaction provisions, a fiduciary may not deal with the income or assets of a Plan or an IRA in his or her own interest or for his or her own account, and a fiduciary may not receive payments from any party dealing with the

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<sup>5</sup> ERISA section 406 and Code section 4975. *Cf.* Code section 4975(f)(5), which defines “correction” with respect to prohibited transactions as placing a Plan or an IRA in a financial position not worse than it would have been in if the person had acted “under the highest fiduciary standards.”

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Plan or IRA in connection with a transaction involving assets of the Plan or IRA. The Department has authority in ERISA section 408(a) and Code section 4975(c)(2) to grant administrative exemptions from the prohibited transaction provisions in Title I and the Code.<sup>6</sup>

In 2016, the Department finalized a new regulation that would have replaced the 1975 regulation, and granted new associated prohibited transaction exemptions.<sup>7</sup> After the U.S. Court of Appeals for the Fifth Circuit vacated that rulemaking, including the new exemptions, in *Chamber of Commerce of the United States v. U.S. Department of Labor* in 2018 (the *Chamber* opinion),<sup>8</sup> the Department issued Field Assistance Bulletin (FAB) 2018-02, a temporary enforcement policy providing prohibited transaction relief to investment advice fiduciaries.<sup>9</sup> In the FAB, the Department stated it would not pursue prohibited transaction claims against investment advice fiduciaries who worked diligently and in good faith to comply with “Impartial Conduct Standards” for transactions that

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<sup>6</sup> Reorganization Plan No. 4 of 1978 (5 U.S.C. App. 1 (2018)) generally transferred the authority of the Secretary of the Treasury to grant administrative exemptions under Code section 4975 to the Secretary of Labor.

<sup>7</sup> See Definition of the Term “Fiduciary”; Conflict of Interest Rule – Retirement Investment Advice, 81 FR 20945 (Apr. 8, 2016).

<sup>8</sup> 885 F.3d 360 (5th Cir. 2018).

<sup>9</sup> Available at [www.dol.gov/agencies/ebsa/employers-and-advisers/guidance/field-assistance-bulletins/2018-02](http://www.dol.gov/agencies/ebsa/employers-and-advisers/guidance/field-assistance-bulletins/2018-02). The Impartial Conduct Standards incorporated in the FAB were conditions of the new exemptions granted in 2016. See Best Interest Contract Exemption, 81 FR 21002 (Apr. 8, 2016), as corrected at 81 FR 44773 (July 11, 2016).

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would have been exempted in the new exemptions, or treat the fiduciaries as violating the applicable prohibited transaction rules. The Impartial Conduct Standards have three components: a best interest standard; a reasonable compensation standard; and a requirement to make no misleading statements about investment transactions and other relevant matters.

On July 7, 2020, the Department proposed this class exemption, which took into consideration the public correspondence and comments received by the Department since February 2017 and responded to informal industry feedback seeking an administrative class exemption based on FAB 2018-02.<sup>10</sup> On the same day, the Department issued a technical amendment to 29 CFR 2510-3.21, instructing the Office of the Federal Register to remove language that was added in 2016 and reinsert the text of the 1975 regulation.<sup>11</sup> This ministerial action reflected the Fifth Circuit's vacatur of the 2016 fiduciary rule.<sup>12</sup> The technical amendment also reinserted into the CFR Interpretive Bulletin 96-1 relating to participant investment education, which had been removed and largely incorporated into the text of the 2016 fiduciary rule.<sup>13</sup> The Department received 106 written comments on the proposed exemption, and on September 3, 2020, held a public hearing at which the commenters were permitted to give additional testimony.<sup>14</sup>

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<sup>10</sup> 85 FR 40834 (July 7, 2020).

<sup>11</sup> 85 FR 40589 (July 7, 2020).

<sup>12</sup> The amendment also corrected a typographical error in the original text of the 1975 regulation, at 29 CFR 2510-3.21(e)(1)(ii).

<sup>13</sup> 29 CFR 2509.96-1.

<sup>14</sup> Hearing on Improving Investment Advice for Workers & Retirees, 85 FR 52292 (August 25, 2020).

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After careful consideration of the comments and testimony on the proposed exemption, the Department is granting the exemption. While the final exemption makes a number of significant changes in response to comments, it retains the proposal's broad protective framework, including the Impartial Conduct Standards; disclosures, including a written acknowledgment of fiduciary status; policies and procedures prudently designed to ensure compliance with the Impartial Conduct Standards and that mitigate conflicts of interest; and a retrospective compliance review. The exemption, like the proposal, also specifies the circumstances in which Financial Institutions and Investment Professionals are ineligible to rely upon its terms.

In response to commenters, the Department made a number of important changes. First, the final exemption's recordkeeping requirements have been narrowed to allow only the Department and the Department of the Treasury to obtain access to a Financial Institution's records as opposed to plan fiduciaries and other Retirement Investors. Second, the final exemption's disclosure requirements have been revised to include written disclosure to Retirement Investors of the reasons that a rollover recommendation was in their best interest. Third, the final exemption's retrospective review provision has been revised to provide that certification can be made by any Senior Executive Officer, as defined in the exemption, rather than requiring certification by the chief executive officer (or equivalent officer) as proposed. Fourth, a self-correction provision has also been added to the final exemption.

This document also sets forth the Department's final interpretation of the five-part test of investment advice fiduciary status for purposes of this exemption, and provides the

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Department's views on when advice to roll over Title I Plan assets to an IRA will be considered fiduciary investment advice under Title I and the Code.<sup>15</sup> Comments on the interpretation, which was proposed in the notice of proposed exemption, are discussed below.

The Department has also provided explanation in the preamble to respond to issues raised during the comment period. Additionally, to the extent public comments were based on concerns about compliance and interpretive issues with the final exemption or the Act, the Department intends to support Financial Institutions, Investment Professionals, plan sponsors and fiduciaries, and other affected parties, with compliance assistance following publication of the final exemption.

The Department further announces that FAB 2018-02 will remain in effect until [INSERT DATE THAT IS 365 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER]. This will provide a transition period for parties to develop mechanisms to comply with the provisions in the new exemption.

The Department grants this exemption, which was proposed on its own motion, pursuant to its authority under ERISA section 408(a) and Code section 4975(c)(2) and in accordance with procedures set forth in 29 CFR part 2570, Subpart B (76 FR 66637 (October 27, 2011)). The Department finds that the exemption is administratively

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<sup>15</sup> For purposes of any rollover of assets from a Title I Plan to an IRA described in this preamble, the term "Plan" only includes an employee pension benefit plan described in ERISA section 3(2) or a plan described in Code section 4975(e)(1)(A), and the term "IRA" only includes an account or annuity described in Code section 4975(e)(1)(B) or (C).



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feasible, in the interests of Plans and their participants and beneficiaries and of IRA owners, and protective of the rights of participants and beneficiaries of Plans and IRA owners. The Department has determined that the exemption is an Executive Order (E.O.) 13771 deregulatory action because it provides broader and more flexible exemptions that allow investment advice fiduciaries with respect to Plans and IRAs to receive compensation and engage in certain principal transactions that would otherwise be prohibited under Title I and the Code.

## **OVERVIEW OF THE FINAL EXEMPTION AND DISCUSSION OF COMMENTS RECEIVED**

This exemption is available to registered investment advisers, broker-dealers, banks, and insurance companies (Financial Institutions) and their individual employees, agents, and representatives (Investment Professionals) that provide fiduciary investment advice to Retirement Investors.<sup>16</sup> The exemption defines Retirement Investors as Plan participants and beneficiaries, IRA owners, and Plan and IRA fiduciaries.<sup>17</sup> Under the exemption, Financial Institutions and Investment Professionals can receive 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

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<sup>16</sup> References in the preamble to registered investment advisers include both SEC- and state-registered investment advisers.

<sup>17</sup> As defined in Section V(i) of the exemption, the term “Plan” means any employee benefit plan described in ERISA section 3(3) and any plan described in Code section 4975(e)(1)(A). In Section V(g), the term “Individual Retirement Account” or “IRA” is defined as any account or annuity described in Code section 4975(e)(1)(B) through (F), including an Archer medical savings account, a health savings account, and a Coverdell education savings account.

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mark-downs, and revenue sharing payments from investment providers or third parties.

The exemption's relief extends to prohibited transactions arising as a result of investment advice to roll over assets from a Plan to an IRA, as detailed later in this exemption. The exemption also allows Financial Institutions to engage in principal transactions with Plans and IRAs in which the Financial Institution purchases or sells certain investments from its own account.

As noted above, Title I and the Code include broad prohibitions on self-dealing. Absent an exemption, a fiduciary may not deal with the income or assets of a Plan or an IRA in his or her own interest or for his or her own account, and a fiduciary may not receive payments from any party dealing with the Plan or IRA in connection with a transaction involving assets of the Plan or IRA. As a result, fiduciaries who use their authority to cause themselves or their affiliates<sup>18</sup> or related entities<sup>19</sup> to receive additional compensation violate the prohibited transaction provisions unless an exemption applies.<sup>20</sup>

This exemption conditions relief on the Investment Professional and Financial

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<sup>18</sup> As defined in Section V(a) of the exemption, an "affiliate" includes: (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. (For this purpose, "control" means the power to exercise a controlling influence over the management or policies of a person other than an individual); (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.

<sup>19</sup> As defined in Section V(j) of the exemption, a "related entity" is an entity that is not an affiliate, but in which the Investment Professional or Financial Institution has an interest that may affect the exercise of its best judgment as a fiduciary.

<sup>20</sup> As articulated in the Department's regulations, "a fiduciary may not use the authority, control, or responsibility which makes such a person a fiduciary to cause a plan to pay an additional fee to such fiduciary (or to a person in which such fiduciary has an interest which may affect the exercise of such fiduciary's best judgment as a fiduciary) to provide a service." 29 CFR 2550.408b-2(e)(1).

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Institution investment advice fiduciaries providing advice in accordance with the Impartial Conduct Standards. In addition, the exemption requires Financial Institutions to acknowledge in writing their and their Investment Professionals' fiduciary status under Title I and the Code, as applicable, when providing investment advice to the Retirement Investor, and to describe in writing the services to be provided and the Financial Institutions' and Investment Professionals' material conflicts of interest. Financial Institutions must document the reasons that a rollover recommendation is in the best interest of the Retirement Investor and provide that documentation to the Retirement Investor. Financial Institutions are required to adopt policies and procedures prudently designed to ensure compliance with the Impartial Conduct Standards and conduct a retrospective review of compliance. The exemption also provides, subject to additional safeguards, relief for Financial Institutions to enter into principal transactions with Retirement Investors, in which they purchase or sell certain investments from their own accounts.

In order to ensure that Financial Institutions provide reasonable oversight of Investment Professionals and adopt a culture of compliance, the exemption provides that Financial Institutions and Investment Professionals will be ineligible to rely on the exemption if, within the previous 10 years, they were convicted of certain crimes arising out of their provision of investment advice to Retirement Investors. They will also be ineligible if they engaged in systematic or intentional violation of the exemption's conditions or provided materially misleading information to the Department in relation to their conduct under the exemption. Ineligible parties are permitted to rely on an

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otherwise available statutory exemption or administrative class exemption, or they can apply for an individual prohibited transaction exemption from the Department. This targeted approach of allowing the Department to give special attention to parties with certain criminal convictions or with a history of egregious conduct with respect to compliance with the exemption will provide meaningful protections for Retirement Investors.

While the exemption's eligibility provision provides an incentive to maintain an appropriate focus on compliance with legal requirements and with the exemption, it does not represent the only available enforcement mechanism. The Department has investigative and enforcement authority with respect to transactions involving Plans under Title I of ERISA, and it has interpretive authority as to whether exemption conditions have been satisfied. Further, ERISA section 3003(c) provides that the Department will transmit information to the Secretary of the Treasury regarding a party's violation of the prohibited transaction provisions of ERISA section 406. In addition, participants, beneficiaries, and fiduciaries with respect to Plans covered under Title I have a statutory cause of action under ERISA section 502(a) for fiduciary breaches and prohibited transactions under Title I. The exemption, however, does not expand Retirement Investors' ability to enforce their rights in court or create any new legal claims above and beyond those expressly authorized in Title I or the Code, such as by requiring contracts and/or warranty provisions.

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### ***Exemption Approach and Alignment with Other Regulators' Conduct Standards***

This exemption provides relief that is broader and more flexible than the other prohibited transaction exemptions currently available for investment advice fiduciaries. Those exemptions generally provide relief to specific types of financial services providers, for discrete, specifically identified transactions, and often do not extend to compensation arrangements that developed after the Department first granted the exemptions.<sup>21</sup> In comparison, this new exemption provides relief for multiple categories of Financial Institutions and Investment Professionals, and extends broadly to their receipt of reasonable compensation as a result of the provision of fiduciary investment advice. The conditions are principles-based rather than prescriptive, so as to apply across different financial services sectors and business models. The exemption provides additional certainty regarding covered compensation arrangements and avoids the complexity associated with requiring a Financial Institution to rely upon a patchwork of different exemptions when providing investment advice.

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<sup>21</sup> See e.g., PTE 86-128, Class Exemption for Securities Transactions involving Employee Benefit Plans and Broker-Dealers, 51 FR 41686 (Nov. 18, 1986), as amended, 67 FR 64137 (Oct. 17, 2002) (providing relief for a fiduciary's use of its authority to cause a Plan or an IRA to pay a fee for effecting or executing securities transactions to the fiduciary, as agent for the Plan or IRA, and for a fiduciary to act as an agent in an agency cross transaction for a Plan or an IRA and another party to the transaction and receive reasonable compensation for effecting or executing the transaction from the other party to the transaction); PTE 84-24, Class Exemption for Certain Transactions Involving Insurance Agents and Brokers, Pension Consultants, Insurance Companies, Investment Companies and Investment Company Principal Underwriters, 49 FR 13208 (Apr. 3, 1984), as corrected, 49 FR 24819 (June 15, 1984), as amended, 71 FR 5887 (Feb. 3, 2006) (providing relief for the receipt of a sales commission by an insurance agent or broker from an insurance company in connection with the purchase, with plan assets, of an insurance or annuity contract).

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The exemption’s principles-based approach is rooted in the Impartial Conduct Standards for fiduciaries providing investment advice. The Impartial Conduct Standards include a best interest standard, a reasonable compensation standard, and a requirement to make no misleading statements about investment transactions and other relevant matters. In the proposed exemption, the Department noted that the best interest standard was based on concepts of law and equity “developed in significant part to deal with the issues that arise when agents and persons in a position of trust have conflicting interests,” and accordingly, the standard is well-suited to the problems posed by conflicted investment advice.<sup>22</sup> The Department believes that conditioning the exemption on satisfaction of the Impartial Conduct Standards protects the interests of Retirement Investors in connection with this broader grant of exemptive relief.

The best interest standard in the exemption is broadly aligned with recent rulemaking by the Securities and Exchange Commission (SEC), in particular. On June 5, 2019, the SEC finalized a regulatory package relating to conduct standards for broker-dealers and investment advisers. The package included Regulation Best Interest which establishes a best interest standard applicable to broker-dealers when making a recommendation of any securities transaction or investment strategy involving securities

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<sup>22</sup> 85 FR at 40842.

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to retail customers.<sup>23</sup> The SEC also issued an interpretation of the fiduciary conduct standards applicable to investment advisers under the Investment Advisers Act of 1940 (SEC Fiduciary Interpretation).<sup>24</sup> In addition, as part of the package, the SEC adopted new Form CRS, which requires broker-dealers and SEC-registered investment advisers to provide retail investors with a short relationship summary with specified information (SEC Form CRS).<sup>25</sup>

The exemption's best interest standard is also aligned with the standard included in the National Association of Insurance Commissioners (NAIC)'s Suitability in Annuity Transactions Model Regulation (NAIC Model Regulation) which was updated in Spring 2020.<sup>26</sup> The model regulation provides that all recommendations by agents and insurers must be in the best interest of the consumer and that agents and carriers may not place

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<sup>23</sup> Regulation Best Interest: The Broker-Dealer Standard of Conduct, 84 FR 33318 (July 12, 2019) (Regulation Best Interest Release).

<sup>24</sup> Commission Interpretation Regarding Standard of Conduct for Investment Advisers, 84 FR 33669 (July 12, 2019).

<sup>25</sup> Form CRS Relationship Summary; Amendments to Form ADV, 84 FR 33492 (July 12, 2019) (Form CRS Relationship Summary Release). In addition to the SEC's rulemaking, the Massachusetts Securities Division amended its regulations for broker-dealers to apply a fiduciary conduct standard, under which broker-dealers and their agents must "[m]ake recommendations and provide investment advice without regard to the financial or any other interest of any party other than the customer." 950 Mass. Code Regs. 12.204 & 12.207 as amended effective March 6, 2020.

<sup>26</sup> NAIC Suitability in Annuity Transactions Model Regulation, Spring 2020, *available at* [www.naic.org/store/free/MDL-275.pdf](http://www.naic.org/store/free/MDL-275.pdf) (NAIC Model Regulation).

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their financial interest ahead of the consumer’s interest. Both Iowa and Arizona have adopted updated rules following the update of the NAIC Model Regulation.<sup>27</sup>

Some commenters expressed general support for the approach taken in the proposed exemption, although they opposed certain specific conditions as discussed in greater detail below. Commenters cited the flexible, principles-based approach rather than a prescriptive approach to exemptive relief, and they also praised the proposed exemptive relief for a broad range of otherwise prohibited compensation types which they said did not favor certain market segments or arrangements. Many of these commenters supported what they viewed as the proposed exemption’s alignment with regulatory conduct standards under the securities laws, particularly Regulation Best Interest. The commenters said this approach would reduce compliance costs and burdens, which will ultimately benefit Retirement Investors through reduced fees. Commenters also stated that they believed the exemption’s approach would facilitate providing investment advice to Retirement Investors through a wide variety of methods.

Some commenters urged the Department to more closely mirror Regulation Best Interest or offer an explicit safe harbor for compliance with Regulation Best Interest, or with any “primary financial regulator” of the Financial Institution, rather than including

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<sup>27</sup> Iowa Code § 507B.48 (2020), available at [https://iid.iowa.gov/sites/default/files/bi\\_af.pdf](https://iid.iowa.gov/sites/default/files/bi_af.pdf); Arizona Senate Bill 1557 (2020), available at [www.azleg.gov/legtext/54Leg/2R/laws/0090.pdf](http://www.azleg.gov/legtext/54Leg/2R/laws/0090.pdf). The New York State Department of Financial Services also amended its insurance regulations to establish a best interest standard in connection with life insurance and annuity transactions. New York State Department of Financial Services Insurance Regulation 187, 11 NYCRR 224, First Amendment, effective August 1, 2019 for annuity transactions.



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additional conditions in the exemption. They argued that otherwise Financial Institutions would have to comply with two differing yet mostly redundant regimes, with their attendant additional costs and liability exposure, and that the Department had failed to show that Retirement Investors would be insufficiently protected by other regulators' standards. Some commenters focused on conduct standards, disclosures, and policies and procedures as areas for increased alignment, which they said would further reduce compliance burdens. These comments, as they pertain to these particular aspects of the exemption, are discussed in greater detail below in their respective parts of the preamble.

Commenters made similar points with respect to alignment with the NAIC Model Regulation. Some commenters asked the Department to go further in aligning the exemption's terms to the NAIC Model Regulation, or even offer a safe harbor based on compliance with it. Commenters asserted that increased alignment is particularly important to allow for distribution of insurance products by independent insurance agents. Specifically, commenters expressed the view that the exemption establishes a structure of Financial Institution oversight for Investment Professionals that is incompatible with the independent agent distribution model, because independent insurance agents sell the products of more than one insurance company. They suggested that the NAIC Model Regulation better accommodated that business model.

In contrast, many commenters opposed the approach taken in the proposed exemption as insufficiently protective of Retirement Investors, and urged the Department to withdraw the proposal. Some of these commenters expressed the view that the exemption would not satisfy the statutory criteria under ERISA section 408(a) for the

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granting of an exemption or, more generally, that the conditions would not protect Plans and IRAs and their participants and beneficiaries from the dangers of conflicts of interest and self-dealing.

These commenters focused much of their opposition on the exemption's alignment with Regulation Best Interest and the NAIC Model Regulation, which the commenters said do not encompass a "true" fiduciary standard. Commenters stated that the provisions of Regulation Best Interest and the NAIC Model Regulation restricting conflicts of interest do not sufficiently protect investors from conflicted investment advice. Furthermore, commenters stated that the Act was enacted to provide *additional* protections to individuals saving for retirement, above and beyond existing laws. Some commenters noted that at the time the Act was enacted, Congress was aware of other federal and state regulatory schemes and that there was no suggestion of congressional purpose to base compliance on federal securities laws or other regulatory schemes.

Some commenters took the position that the alignment with the conduct standards in Regulation Best Interest rendered many of the exemption's other conditions, which are designed to support investment advice that meets the standards, too lax. Some commenters also opposed the breadth of the exemption. These commenters suggested that the exemption should not allow receipt of payments from third parties. Some commenters also opposed the exemption's application to recommendations of proprietary products. Further, commenters also stated that the failure to provide a mechanism for IRA owners to enforce the Impartial Conduct Standards was a significant flaw in the

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exemption's approach. Some of these commenters noted that the Department also lacks the authority to enforce the exemption with respect to these investors.

The Department has carefully considered these comments on the exemption's approach, its alignment with other regulators' conduct standards, as well as the comments on specific provisions of the exemption discussed below. The Department has proceeded with granting the final exemption based on the view that the exemption will provide important protections to Retirement Investors in the context of a principles-based exemption that permits a broad range of otherwise prohibited compensation, including compensation from third parties and from proprietary products.

In this regard, the Impartial Conduct Standards are strong fiduciary standards based on longstanding concepts in the Act and the common law of trusts. The exemption includes additional supporting conditions including a written acknowledgment of fiduciary status to ensure that the nature of the relationship is clear to Financial Institutions, Investment Professionals, and Retirement Investors; policies and procedures that require mitigation of conflicts of interest to the extent that a reasonable person reviewing the policies and procedures and incentive practices as a whole would conclude that they do not create an incentive for a Financial Institution or Investment Professional to place their interests ahead of the interest of the Retirement Investor; and documentation and disclosure to Retirement Investors of the reasons that a rollover recommendation is in the Retirement Investor's best interest.

The exemption does not include a provision permitting IRA owners to enforce the Impartial Conduct Standards. In developing the exemption, the Department was mindful

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of the Fifth Circuit’s *Chamber* opinion holding that the Department did not have authority to include certain contract requirements in the new exemptions enforceable by IRA owners as granted by the 2016 fiduciary rulemaking. In addition, the Department intends to avoid any potential for disruption in the market for investment advice that may occur related to a contract requirement. Instead, the exemption includes many protective measures and targeted opportunities for the Department to review compliance within its existing oversight and enforcement authority under the Act. For example, Financial Institutions’ reports regarding their retrospective review are required to be certified by a Senior Executive Officer<sup>28</sup> of the Financial Institution and provided to the Department within 10 business days of request. The exemption also includes eligibility provisions, discussed below, which the Department believes will encourage Financial Institutions and Investment Professionals to maintain an appropriate focus on compliance with legal requirements and with the exemption.

The Department believes that general alignment with the other regulators’ conduct standards is beneficial in allowing for the development of compliance structures that lack complexity and unnecessary burden. The Department has not, however, offered a safe harbor based solely on compliance with regulatory conduct standards under federal or state securities laws. The Department disagrees with commenters’ arguments that the

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<sup>28</sup> Senior Executive Officer is defined in Section V(l) as any of the following: the chief compliance officer, the chief executive officer, president, chief financial officer, or one of the three most senior officers of the Financial Institution.

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failure to do so will create a redundant, cost-ineffective regime, or one that could create unexpected liabilities at the edges. This exemption is offered as a deregulatory option for interested parties; it does not unilaterally impose any obligations. The additional conditions of the exemption provide important protections to Retirement Investors, who are investing through tax advantaged accounts and are the subject of unique protections under Title I and the Code.<sup>29</sup> The approach in the final exemption exemplifies the Department's important role in protecting Retirement Investors through promulgating only those exemptions that meet the requirements of ERISA section 408(a) and Code section 4975(c)(2).

For the same reasons, the Department likewise declines to provide a safe harbor based on the NAIC Model Regulation. A uniform approach to safeguards for Retirement Investors receiving fiduciary investment advice in the insurance marketplace is particularly important given the potential for variation across state insurance laws. Moreover, although commenters expressed concern about the scope of an insurance company's supervisory oversight responsibilities as a Financial Institution, the Department believes that the exemption is workable for the insurance industry, as discussed in greater detail below.

Some commenters raised questions as to whether the Department intends to defer to the SEC or other regulators on enforcement and how the Department will treat

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<sup>29</sup> See ERISA section 2(a).

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violations under other regulatory regimes. The Department has worked with other regulatory agencies, including the SEC, in numerous cases that implicate violations under different laws. The interaction of findings or settlements in parallel suits or investigations is decidedly a case-by-case determination. The Department confirms that it will coordinate with other regulators, including the SEC, on enforcement strategies and will harmonize regimes to the extent possible, but will not defer to other regulators on enforcement under the Act. Retirement Investors who have concerns about whether they have received investment advice that is not in accordance with the Impartial Conduct Standards or other conditions of the exemption are encouraged to contact the Department.<sup>30</sup>

***Interpretation of Fiduciary Investment Advice in Connection with Rollover Recommendations***

As stated in the proposed exemption, amounts accrued in a Title I Plan can represent a lifetime of savings, and often comprise the largest sum of money a worker has at retirement. Therefore, the decision to roll over assets from a Title I Plan to an IRA is potentially a very consequential financial decision for a Retirement Investor.<sup>31</sup> A sound

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<sup>30</sup> Contact information for regional offices of the Department's Employee Benefits Security Administration is available at [www.dol.gov/agencies/ebsa/about-ebsa/about-us/regional-offices](http://www.dol.gov/agencies/ebsa/about-ebsa/about-us/regional-offices).

<sup>31</sup> For simplicity, this preamble interpretation uses the term *Retirement Investor*, which is a defined term in the exemption. This is not intended to suggest that the interpretation is limited to Retirement Investors

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decision on the rollover will typically turn on numerous factors, including the relative costs associated with the new investment options, the range of available investment options under the plan and the IRA, and the individual circumstances of the particular investor.

Rollovers from Title I Plans to IRAs are expected to approach \$2.4 trillion cumulatively from 2016 through 2020.<sup>32</sup> These large sums of money eligible for rollover represent a significant revenue source for investment advice providers. A firm that recommends a rollover to a Retirement Investor can generally expect to earn transaction-based compensation such as commissions, or an ongoing advisory fee, from the IRA, but may or may not earn compensation if the assets remain in the Title I Plan.

In light of potential conflicts of interest related to rollovers from Title I Plans to IRAs, Title I and the Code prohibit an investment advice fiduciary from receiving fees resulting from investment advice to Title I Plan participants to roll over assets from the plan to an IRA, unless an exemption applies. The exemption provides relief, as needed, for this prohibited transaction, if the Financial Institution and Investment Professional provide investment advice that satisfies the Impartial Conduct Standards and comply with

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impacted by the class exemption. In this preamble interpretation, the term *Retirement Investor* is intended to refer more generally to Plan participants and beneficiaries and IRA owners.

<sup>32</sup> Cerulli Associates, “U.S. Retirement Markets 2019.”

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the other applicable conditions discussed below.<sup>33</sup> In particular, the Financial Institution is required to document the reasons that the advice to roll over was in the Retirement Investor’s best interest, and provide the documentation to the Retirement Investor.

The preamble to the proposed exemption provided the Department’s proposed views on when advice to roll over Plan assets to an IRA should be considered fiduciary investment advice under the Department’s regulation defining fiduciary investment advice,<sup>34</sup> and requested comment on all aspects of the interpretation. The proposed interpretation addressed both Advisory Opinion 2005-23A (the Deseret Letter) as well as the facts and circumstances analysis of rollover recommendations under the five-part test. The discussion also touched on the statutory definitional prerequisite that advice be provided “for a fee or other compensation, direct or indirect.” Comments on the proposed interpretation are discussed below. The Department has carefully considered these comments and has adopted the final interpretation, as follows.

### ***Deseret Letter***

The proposed exemption announced that, in determining the fiduciary status of an investment advice provider in the context of advice to roll over Title I Plan assets to an

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<sup>33</sup> The exemption would also provide relief for investment advice fiduciaries under either Title I or the Code to receive compensation for advice to roll Plan assets to another Plan, to roll IRA assets to another IRA or to a Plan, and to transfer assets from one type of account to another, all limited to the extent such rollovers are permitted under applicable law. The analysis set forth in this section will apply as relevant to those transactions as well. For purposes of any rollover of assets between a Title I Plan and an IRA described in this preamble, the term “IRA” includes only an account or annuity described in Code section 4975(e)(1)(B) or (C).

<sup>34</sup> 29 CFR 2510-3.21.



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IRA, the Department does not intend to apply the analysis in the Deseret Letter stating that advice to roll assets out of a Title I Plan, even when combined with a recommendation as to how the distribution should be invested, did not constitute investment advice with respect to the Title I Plan. The Department believes that the analysis in the Deseret Letter was incorrect when it stated that advice to take a distribution of assets from a Title I Plan is not advice to sell, withdraw, or transfer investment assets currently held in the plan. A recommendation to roll assets out of a Title I Plan is necessarily a recommendation to liquidate or transfer the plan's property interest in the affected assets and the participant's associated property interest in plan investments.<sup>35</sup> Typically the assets, fees, asset management structure, investment options, and investment service options all change with the decision to roll money out of a Title I Plan. Moreover, a distribution recommendation commonly involves either advice to change specific investments in the Title I Plan or to change fees and services directly affecting the return on those investments. Accordingly, the better view is that a recommendation to roll assets out of a Title I Plan is advice with respect to moneys or other property of the plan. An investment advice fiduciary making a rollover recommendation would be required to avoid prohibited transactions under Title I and the Code unless an exemption, including this one, applies.

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<sup>35</sup> Similarly, the SEC and FINRA have each recognized that recommendations to roll over Plan assets to an IRA will almost always involve a securities transaction. *See* Regulation Best Interest Release, 84 FR at 33339; FINRA Regulatory Notice 13-45 Rollovers to Individual Retirement Accounts (December 2013), available at [www.finra.org/sites/default/files/NoticeDocument/p418695.pdf](http://www.finra.org/sites/default/files/NoticeDocument/p418695.pdf).

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Some commenters supported the Department’s announcement that it would not apply the reasoning of the Deseret Letter but would rather approach the analysis of rollovers based on all the facts and circumstances under the five-part test. These commenters generally supported the possibility that rollover recommendations could be considered fiduciary investment advice if the five-part test is satisfied, particularly given the consequence of the decision to roll over large sums typically accumulated in a Retirement Investor’s workplace Plan.

Some commenters stated the Department’s proposed interpretation did not go far enough in protecting Retirement Investors, and that all rollover recommendations should be deemed fiduciary investment advice regardless of whether the five-part test is satisfied. Commenters noted that financial professionals have adopted titles such as financial consultant, financial planner, and wealth manager. These commenters stated that reinsertion of the five-part test makes it all too easy for financial services providers to hold themselves out as acting in positions of trust and confidence, even as they effectively avoided fiduciary status by relying on the “regular basis,” “mutual agreement, arrangement, or understanding” and “primary basis” prongs of the test.<sup>36</sup> One commenter argued that a rollover recommendation should be viewed as always satisfying the “regular basis” prong because, in its view, there are two distinct steps—the decision to do a rollover, and the decision to invest its proceeds.

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<sup>36</sup> Comments on the reinsertion of the five-part test are discussed in greater detail below in the section “Reinsertion of the Five-Part Test.”

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Other commenters asserted that the facts-and-circumstances analysis would lead to uncertainty as to fiduciary status and that a consequence of that uncertainty is a potential reduction in access to advice. One commenter argued that would lead to more leakage, missing participants, and abandoned accounts. Commenters disagreed with the conclusion that rollover recommendations typically include investment recommendations. Many commenters expressed concern that the Department intended to apply the facts and circumstances analysis to transactions occurring in the past. They said the Department's statement that it would no longer apply the reasoning in the Deseret Letter would expose financial services providers to liability for transactions entered into in the past. Some commenters asked for additional guidance on other types of interactions, including recommendations to increase contributions to a Plan.

After careful consideration of these comments, the Department has determined that, consistent with the position taken in the proposal, the facts and circumstances analysis required by the five-part test applies to rollover recommendations. A recommendation to roll assets out of a Title I Plan *is* advice with respect to moneys or other property of the plan and, if provided by a person who satisfies all of the requirements of the five-part test, constitutes fiduciary investment advice. This outcome is more aligned with both the facts and circumstances approach taken by Congress in drafting the Act's statutory functional fiduciary test, and with an approach centered on

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whether the parties have entered into a relationship of trust and confidence.<sup>37</sup> This outcome is also consistent with the Act’s goal of protecting the interests of Retirement Investors given the central importance to investors’ retirement security consequences of a decision to roll over Title I Plan assets.

The Department agrees that not all rollover recommendations can be considered fiduciary investment advice under the five-part test set forth in the Department’s regulation. Parties can and do, for example, enter into one-time sales transactions in which there is no ongoing investment advice relationship, or expectation of such a relationship. If, for example, a participant purchases an annuity based upon a recommendation from an insurance agent without receiving subsequent, ongoing advice, the advice does not meet the “regular basis” prong as specifically required by the regulation.<sup>38</sup> Nor is the Department persuaded by the commenter who suggested that a rollover transaction should always satisfy the regular basis prong on the grounds that it can be viewed as involving two separate steps—the rollover and a subsequent investment decision. These two steps do not, in and of themselves, establish a regular basis.

The Department does not believe that its interpretation will lead to loss of access to investment advice due to uncertainty of financial services providers as to their

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<sup>37</sup> For example, ERISA section 3(21) discusses a fiduciary relationship surrounding the “disposition of [plan] assets.”

<sup>38</sup> Where a broker-dealer or investment adviser makes a recommendation or provides advice that does not meet the five-part test, the recommendation or advice could still be subject to Regulation Best Interest or the investment adviser’s fiduciary duty under securities laws, as applicable.

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fiduciary status. Taken together, the five-part test as interpreted here and Interpretive Bulletin 96-1, regarding participant investment education, provide Financial Institutions and Investment Professionals a clear roadmap for when they are, and are not, Title I and Code fiduciaries. Since the exemption provides prohibited transaction relief for rollover recommendations that do constitute fiduciary investment advice, Financial Institutions and Investment Professionals would be free to provide fiduciary investment advice and comply with the exemption to avoid a prohibited transaction. In this regard, some commenters specifically supported the proposed exemption as facilitating investment advice and options for consumers. Alternatively, financial services providers can choose not to provide fiduciary investment advice and have no need of this exemption. And, of course, the Department acknowledges some commenters' observations that Retirement Investors may choose on their own to withdraw assets from a Title I Plan and roll over funds to an IRA; however, this exemption focuses on the interests of those Retirement Investors who do receive fiduciary investment advice. The Department further addresses concerns regarding purported uncertainty over whether certain relationships meet the prongs of the five-part test, including the "regular basis" and "mutual agreement" prongs, later in this preamble.

Some commenters stated that the Department should have engaged in notice and comment prior to announcing that it would no longer apply the analysis in the Deseret Letter. Commenters said that the position in the Deseret Letter contributed to a longstanding understanding of the five-part test which should be reversed only through the regulatory process. A commenter noted that, in 2016, the Department characterized

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the 2016 fiduciary rule as “superseding” the Deseret Letter, and asserted that characterization as evidence that the Department’s procedure in this exemption proceeding is inadequate.

The Department does not believe these comments have merit. Advisory opinions, such as the Deseret Letter, are interpretive statements that were not subject to the notice and comment process. As such, the Department need not go through notice and comment to offer a new interpretation of the regulation based on a better reading of governing statutory and regulatory authority, as here.<sup>39</sup> Moreover, in this instance, the statements made in the preamble to the now-vacated 2016 fiduciary rule are also unpersuasive as to the effect of the Deseret Letter for the same reasons. Rather than take the 2016 fiduciary rule’s approach of removing the five-part test through an amendment to the Code of Federal Regulations and, thus, “superseding” the Deseret Letter, the Department now is only changing its view on the Deseret Letter (and specifically, one aspect of it). The five-part test still applies without the Deseret Letter, as it did for decades before the letter. The 2016 fiduciary rule is not in effect, and statements made in the preamble to the vacated rule bear no weight. And, in this instance, the Department solicited and has had the benefit of public comment on its interpretation through the notice and comment process for the exemption. Comments regarding the Department’s compliance with Executive Order 13891 are addressed later in this preamble.

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<sup>39</sup> See *Perez v. Mortgage Bankers Assoc.*, 575 U.S. 92, 100–01 (2015).

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Nevertheless, in response to commenters expressing concern about the possibility of being held liable for past transactions that would not have been treated as fiduciary under the Deseret analysis, the Department 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 the period between 2005, when the Deseret Letter was issued, and [INSERT DATE THAT IS 60 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER], based on a rollover recommendation that would have been considered non-fiduciary conduct under the reasoning in the Deseret Letter. The Department recognizes that advisory opinions issued under ERISA Procedure 76-1, while directly applicable only to their requester, *see* ERISA Procedure 76-1 § 10, can also constitute “a body of experience and informed judgment to which the courts and litigants may properly resort for guidance.” *Raymond B. Yates, M.D., P.C. Profit Sharing Plan v. Hendon*, 541 U.S. 1, 18 (2004) (quoting *Skidmore v. Swift & Co.*, 323 U.S. 134, 140 (1944)). For this reason, and because the Department does not wish to disturb the reliance interests of those who looked to the Deseret Letter for guidance, the Department also does not expect or intend a private right of action to be viable for a transaction conducted in reliance on the Deseret Letter prior to that date. Further, the extension of the temporary enforcement policy in FAB 2018-02 until its expiration on [INSERT DATE THAT IS 365 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER] will allow parties a transition period during which the Department will not pursue prohibited transaction claims against investment advice fiduciaries who work diligently and in good faith to comply with the Impartial Conduct Standards for rollover

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recommendations or treat such fiduciaries as violating the applicable prohibited transaction rules.<sup>40</sup> Additionally, although the Department declines to set broad guidelines in this preamble for what is necessarily a facts-and-circumstances determination about particular business practices, to the extent public comments were based on concerns about compliance and interpretive issues with the final exemption or the Act, the Department intends to support Financial Institutions, Investment Professionals, plan sponsors and fiduciaries, and other affected parties with compliance assistance following publication of the final exemption.

#### ***Facts and Circumstances Analysis***

All the elements of the five-part test must be satisfied for the investment advice provider to be a fiduciary within the meaning of the regulatory definition, including the “regular basis” prong as well as requirements that the advice be provided pursuant to a “mutual” agreement, arrangement, or understanding that the advice will serve as “a primary basis” for investment decisions. In addition to satisfying the five-part test, a person must also receive a fee or other compensation to be an investment advice fiduciary under the provisions of Title I and the Code.

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<sup>40</sup> On March 28, 2017, the Treasury Department and the IRS issued IRS Announcement 2017-4 stating that the IRS will not apply § 4975 (which provides excise taxes relating to prohibited transactions) and related reporting obligations with respect to any transaction or agreement to which the Labor Department’s temporary enforcement policy described in FAB 2017-01, or other subsequent related enforcement guidance, would apply. The Treasury Department and the IRS have confirmed that, for purposes of applying IRS Announcement 2017-4, this preamble discussion and FAB 2018-02 constitute “other subsequent related enforcement guidance.”



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If, under this facts and circumstances analysis, advice to roll Title I Plan assets over to an IRA is fiduciary investment advice under Title I, the fiduciary duties of prudence and loyalty under ERISA section 404 would apply to the initial instance of advice to take the distribution and to roll over the assets. Fiduciary investment advice concerning investment of the rollover assets and ongoing management of the assets, once distributed from the Title I Plan into the IRA, would be subject to obligations in the Code. For example, a broker-dealer who satisfies the five-part test with respect to a Retirement Investor in advising on assets in a Title I Plan, advises the Retirement Investor to move his or her assets from the plan to an IRA, and receives any fees or compensation incident to distributing those assets, will be a fiduciary subject to Title I, including section 404, with respect to the advice regarding the rollover. Following the rollover, the broker-dealer will be a fiduciary under the Code subject to the prohibited transaction provisions in Code section 4975.

#### Final Interpretation

The Department 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. Likewise, sporadic interactions between a financial services professional and a Retirement Investor do not meet the regular basis prong. For example, if a Retirement Investor who is assisted with a rollover expresses the intent to direct his or her own investments in a brokerage account, without any expectation of entering into an ongoing advisory relationship and without receiving repeated investment recommendations from the investment professional, the Department would not view the

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regular basis prong as being satisfied merely because the investor subsequently sought the professional's advice in connection with another transaction long after receiving the rollover assistance.

However, advice to roll over plan assets can also occur as part of an ongoing relationship or an intended ongoing relationship that an individual enjoys with his or her investment advice provider. In circumstances in which the investment advice provider has been giving advice to the individual about investing in, purchasing, or selling securities or other financial instruments through tax-advantaged retirement vehicles subject to Title I or the Code, the advice to roll assets out of a Title I Plan is part of an ongoing advice relationship that satisfies the regular basis prong. Similarly, advice to roll assets out of a Title I Plan into an IRA where the investment advice provider has not previously provided advice but will be regularly giving advice regarding the IRA in the course of a more lengthy financial relationship would be the start of an advice relationship that satisfies the regular basis prong. It is clear under Title I and the Code that advice to a Title I Plan includes advice to participants and beneficiaries in participant-directed individual account pension plans, so in these scenarios, there is

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advice to the Title I Plan—meaning the Plan participant or beneficiary—on a regular basis.<sup>41</sup>

This interpretation is consistent with the approach of other regulators and protects Plan participants and beneficiaries under today’s market practices, including the increasing prevalence of 401(k) Plans and self-directed accounts. Numerous sources acknowledge that an outcome of advice given to a Retirement Investor to roll over Title I Plan assets is the compensation an advice provider receives from the investments made in an IRA. For example, in a 2013 notice reminding firms of their responsibilities regarding IRA rollovers, FINRA stated that “a financial adviser has an economic incentive to encourage an investor to roll plan assets into an IRA that he will represent as either a broker-dealer or an investment adviser representative.”<sup>42</sup> Similarly, in 2011, the U.S. Government Accountability Office (GAO) discussed the practice of cross-selling, in which 401(k) service providers sell Plan participants products and services outside of their Title I Plans, including IRA rollovers. GAO reported that industry professionals said “cross-selling IRA rollovers to participants, in particular, is an important source of

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<sup>41</sup> See ERISA section 408(b)(14) (providing a statutory exemption for transactions in connection with the provision of investment advice described in ERISA section 3(21)(A)(ii) to a participant or beneficiary of an individual account plan that permits such participant or beneficiary to direct the investment of assets in their individual account); Code section 4975(d)(17) (same); see also Interpretive Bulletin 96-1, 29 CFR 2509.96-1.

<sup>42</sup> FINRA Regulatory Notice 13-45.

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income for service providers.”<sup>43</sup> These types of transactions can initiate a future, ongoing relationship.<sup>44</sup>

In applying the regular basis prong of the five-part test, however, the Department intends to preserve the ability of financial services professionals to engage in one-time sales transactions without becoming fiduciaries under the Act, including by assisting with a rollover.<sup>45</sup> For example, such parties 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. In the event that assistance with a rollover does in fact mark the beginning of an ongoing relationship, however, the functional fiduciary test under Title I and the Code appropriately covers the entire fiduciary relationship, including the first instance of advice.

With respect to determining whether there is “a mutual agreement, arrangement, or understanding” that the investment advice will serve as “a primary basis for investment decisions,” the Department intends to consider the *reasonable* understanding of each of the parties, if no mutual agreement or arrangement is demonstrated. Written statements disclaiming a mutual understanding or forbidding reliance on the advice as a primary basis for investment decisions will not be determinative, although such

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<sup>43</sup> U.S. General Accountability Office, 401(k) Plans: Improved Regulation Could Better Protect Participants from Conflicts of Interest, GAO 11-119 (Washington D.C. 2011), *available at* [www.gao.gov/assets/320/315363.pdf](http://www.gao.gov/assets/320/315363.pdf).

<sup>44</sup> It is by no means uncommon to interpret regulatory or statutory terms phrased in the present to incorporate the future tense. *See, e.g.*, 1 U.S.C. 1.

<sup>45</sup> Merely executing a sales transaction at the customer’s request also does not confer fiduciary status.

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statements will be appropriately considered in determining whether a mutual understanding exists. Similarly, after consideration of the comments, the Department also intends to consider marketing materials in which Financial Institutions and Investment Professionals hold themselves out as trusted advisers, in evaluating the parties' reasonable understandings with respect to the relationship.

The Department believes that Financial Institutions and Investment Professionals who meet the five-part test and are investment advice fiduciaries relying on this exemption should clearly disclose their fiduciary status to their Retirement Investor customers. By making this disclosure, they provide important clarity to the Retirement Investor and put themselves in the best possible position to meet their fiduciary obligations and comply with the exemption. By setting clear expectations and acting accordingly, the mutual understanding prong of the five-part test should seldom be an issue for parties relying on the exemption. Similarly, if a Financial Institution or Investment Professional does not want to assume a fiduciary relationship or create misimpressions about the nature of its undertaking, it can clearly disclose that fact to its customers up-front, clearly disclaim any fiduciary relationship, and avoid holding itself out to its Retirement Investor customer as acting in a position of trust and confidence.

The Department does not intend to apply the five-part test to determine whether the advice serves as "the" primary basis of investment decisions, as advocated by some commenters, but whether it serves as "a" primary basis, as the regulatory text provides.

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### Comments on the Regular Basis Analysis

Some commenters on the Department's proposed interpretation of the regular basis prong asserted that the regular basis prong would always be satisfied under the interpretation, and, therefore, the prong was effectively being eliminated from the five-part test. In this regard, one commenter stated that every financial professional wants to develop an ongoing relationship with her customers. Commenters opposed the statement that a rollover recommendation could be the first step in an ongoing advice relationship that would satisfy the regular basis prong. Some commenters characterized this statement as allowing for the "retroactive" imposition of fiduciary status on financial services providers in the event an ongoing relationship develops. Some commenters additionally opined that to be "regular," the interactions would have to be more than discrete or episodic. Some commenters stated that the advice to a Retirement Investor in a Title I Plan should be viewed as distinct from the advice to the same Retirement Investor whose assets have been transferred to an IRA, for purposes of the analysis of the regular basis prong. Commenters also cautioned that the preamble statement about rollover advice following a pre-existing advice relationship appeared to be overbroad with respect to the types of pre-existing advice relationships to which it would apply.

Commenters in the insurance industry asked the Department to confirm that insurance transactions generally would not be considered fiduciary investment advice, because commenters said they occur infrequently and that ongoing interactions may occur but they are related to servicing the insurance or annuity contract. Some commenters objected to the Department's statement in the preamble that agents who

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receive trailing commissions on annuity transactions may continue to provide ongoing recommendations or service with respect to the annuity. Commenters asserted that this method of compensation is paid for a variety of reasons and does not indicate an ongoing advice relationship.<sup>46</sup>

The Department has carefully considered these comments in clarifying its interpretation of the “regular basis” prong of the five-part test. The Department does not believe that the regular basis prong has effectively been eliminated by stating that this prong may be satisfied, in some cases, with the occurrence of first-time advice on rollovers that is intended to be the beginning of a long-term relationship. The regulation still requires, in all cases, that advice will be provided on a regular basis. The Department’s interpretation merely recognizes that the rollover recommendation can be the beginning of an ongoing advice relationship. It is important that fiduciary status extend to the entire advisory relationship.

In this regard, when the parties reasonably expect an ongoing advice relationship at the time of the rollover recommendation, the regular basis prong is satisfied. This expectation can be shown by various kinds of objective evidence, of which some examples are discussed below, such as the parties agreeing to check-in periodically on the

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<sup>46</sup> A few commenters in the insurance industry and the brokerage industry cited statements in the Fifth Circuit’s *Chamber* opinion for the proposition that brokers-dealers and insurance agents would ordinarily not develop a relationship of trust and confidence with prospective customers so as to properly be considered fiduciaries under Title I and the Code. These comments related to the Fifth Circuit’s *Chamber* opinion are discussed later in this preamble.

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performance of the customer’s post-rollover financial products. In such cases, the parties’ expectation at the time of the rollover recommendation appropriately demonstrates that the regular basis prong has been satisfied, and, if the other prongs of the test are satisfied, the financial service providers making the recommendation are appropriately treated as investment advice fiduciaries under Title I and the Code. Likewise, to the extent that financial service providers hold themselves out to the customer as providing such ongoing services, and meet the other elements of the five-part test, they are fiduciaries.

In the Department’s view, the updated conduct standards adopted by the SEC and the NAIC reflect an acknowledgment of the fact that broker-dealers and insurance agents commonly provide investment and annuity recommendations to their customers.<sup>47</sup> To the extent these professionals engage in an ongoing advice relationship, they will likely satisfy the regular basis prong. Moreover, the Department does not intend to interpret “regular basis” to be limited to relationships in which advice is provided at fixed intervals, as suggested by a commenter, but, instead, believes the term “regular basis” broadly describes a relationship where advice is recurring, non-sporadic, and expected to

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<sup>47</sup> See *Regulation Best Interest*, 17 CFR 240.15l-1(a) (“A broker, dealer, or a natural person who is an associated person of a broker or dealer, when making a recommendation of any securities transaction or investment strategy involving securities (including account recommendations) to a retail customer, shall act in the best interest of the retail customer at the time the recommendation is made, without placing the financial or other interest of the broker, dealer, or natural person who is an associated person of a broker or dealer making the recommendation ahead of the interest of the retail customer.”) and NAIC Model Regulation Section 6.A. (“A producer, when making a recommendation of an annuity, shall act in the best interest of the consumer under the circumstances known at the time the recommendation is made, without placing the producer’s or the insurer’s financial interest ahead of the consumer’s interest.”).



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continue. When insurance agents or broker-dealers frequently or periodically make recommendations to their clients on annuity or investment products or features, or on the investment of additional assets in existing products, they may meet the “regular basis” prong of the five-part test, and are appropriately treated as fiduciaries, assuming that they meet the remaining elements of the fiduciary definition.

The Department’s interpretation of the regular basis prong does not result in retroactive imposition of fiduciary status, as suggested by some commenters. As noted above, fiduciary status is 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. Every relationship has a beginning, and the five-part test does not provide that the first instance of advice in an ongoing relationship is automatically free from fiduciary obligations. The fact that the relationship of trust and confidence starts with a recommendation to roll the investor’s retirement savings out of a Title I Plan is not an argument for treating the recommendation as non-fiduciary. Rather, fiduciary status extends 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. A financial services provider that recommends that Retirement Investors roll potential life savings out of a Title I Plan with the expectation of offering ongoing advice to the same Retirement Investor whose retirement assets will now be held in an IRA should reasonably understand that the provider will be held to fiduciary standards.

This does not mean that fiduciary status applies to a prior isolated interaction, if the facts and circumstances surrounding the interaction do not reflect that the interaction

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marked the beginning of an ongoing fiduciary advice relationship. The Department recognizes that relationships, and the parties' understandings of their relationships, can change over time. The Department emphasizes that parties who do not wish to enter into an ongoing relationship can make that fact consistently clear in their communications and act accordingly.

The Department disagrees with commenters who suggested that the "regular basis" requirement must first be met with respect to the Title I Plan, and then again with respect to the IRA. Under the logic of this position, even if the investment advice provider specifically recommended the rollover to the IRA as part of a planned ongoing investment advice relationship, the "regular basis" requirement would not be satisfied with respect to the rollover advice because there was only one instance of advice under the Title I Plan, notwithstanding the expectation of a continued advisory relationship with the same customer with respect to the same assets that were rolled out of the plan. Similarly, the argument asserts that even if the investment advice provider regularly advised the Plan participant on how to invest plan assets, recommended the rollover to an IRA, and then continued to give advice on the IRA account, the first instance of advice post-rollover did not count because the "regular basis" requirement had only been satisfied with respect to the Title I Plan, but not the IRA.

In response, the Department notes that under Title I and the Code, advice to a Title I Plan includes advice to participants and beneficiaries in participant-directed

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individual account pension plans.<sup>48</sup> Given that the identical five-part test definition appears in the regulatory definition under both Title I and the Code, the advice is rendered to the exact same Retirement Investor (first as a Plan participant and then as IRA owner), and the IRA assets are derived, in the first place, from that Retirement Investor's Title I Plan account, it is appropriate to conclude that an ongoing advisory relationship spanning both the Title I Plan and the IRA satisfies the regular basis prong. It is enough, in the scenarios outlined above, 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. A different outcome could all too easily defeat legitimate investor expectations of trust and confidence by arbitrarily dividing an ongoing relationship of ongoing advice and uniquely carving out rollover advice from fiduciary protection.

Further, the Department believes an approach that coordinates the five-part test under Title I with the identical test under the Code is consistent with the transfer of authority to the Department under Reorganization Plan No. 4 of 1978.<sup>49</sup> Pursuant to the Reorganization Plan, the Secretary of Labor has authority to issue regulations, rulings, opinions, and exemptions under Code section 4975, with some limited exceptions not

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<sup>48</sup> See *supra*, n. 41.

<sup>49</sup> 5 U.S.C. App. (2018).

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relevant here. The message of the President that accompanied the Reorganization Plan indicated an intent to streamline administration of the Act, and to entrust the Department of Labor with responsibility to oversee fiduciary conduct.<sup>50</sup>

For similar reasons, the Department's interpretation of the regular basis prong does not artificially distinguish between advice to a Retirement Investor in a Title I Plan and advice to the same Retirement Investor in an IRA, when evaluating a rollover recommendation made in the context of a pre-existing advice relationship. Likewise, the Department does not arbitrarily subdivide advice rendered to a plan sponsor on multiple Title I Plans. It is enough, in that case, that the parties have an ongoing advisory relationship with respect to Title I Plans. If, on the other hand, the investment professional only made recommendations to the investor on non-"plan" assets held outside a Plan or an IRA, he or she would not meet the "regular basis" test based solely on additional one-time advice with respect to the Plan or IRA. To meet the regular basis prong in that circumstance, there must be ongoing advice to a "plan" (including Plans and IRAs).

As indicated by the discussion above, whether insurance transactions will fall within or outside the scope of the fiduciary definition in Title I and the Code depends on the related facts and circumstances. Like other transactions involving Retirement

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<sup>50</sup> Presidential Statement of October 14, 1978 on Congressional Action on Reorganization Plan No. 4, 1978, Weekly Compilation of Presidential Documents, Vol. 14, No. 42 (Aug. 10, 1978) (accompanying the Reorganization Plan No. 4 of 1978, 5 U.S.C.A. App. 1, 43 FR 47713-16 (Oct. 17, 1978)).

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Investors, insurance and annuity transactions must be evaluated based on application of the five-part test to the particular scenario. Some commenters raised concerns that trailing annuity commissions could be seen as indicating ongoing service that the Department would view as fiduciary investment advice. Other commenters asserted that the Department's view on this point fails to recognize that insurance agents may receive trailing commissions for reasons wholly unrelated to their relationship with a Retirement Investor, and that how an agent is compensated does not impact whether the regular basis prong of the five-part test is satisfied. The Department clarifies that payment of a trailing commission will not, in and of itself, result in the Department taking the position that the regular basis prong of the five-part test is satisfied with respect to a transaction. On the other hand, if the trailing commission is intended to compensate a financial professional for providing advice to the Retirement Investor on an ongoing basis, the conclusion could be different, depending on the full facts and circumstances of the advice arrangement.

Mutual agreement, arrangement, or understanding that the investment advice will serve as a primary basis for investment decisions

Similar to the comments discussed above, some commenters also asserted that the Department's interpretation of the "mutual agreement, arrangement, or understanding" and the "primary basis" requirements is so broad as to render them meaningless. Some of these commenters objected to the statement that recommendations by financial professionals, particularly pursuant to a best interest standard or another requirement to provide advice based on the individualized needs of the Retirement Investor, will typically involve a reasonable understanding by both parties that the advice will serve as

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at least a primary basis for the decision. The commenters asserted that the statement is inconsistent with the fact that the broker-dealer and insurance regulatory regimes do not incorporate a fiduciary standard. A few commenters sought confirmation that compliance with Regulation Best Interest would not automatically result in satisfaction of the primary basis prong of the five-part test. Some commenters stated that investors may consult multiple financial professionals and, therefore, the response by any one professional should not be considered a primary basis for the investment decision.

Some commenters opposed the Department's interpretive statement that written disclaimers of fiduciary status or elements of the five-part test will not be determinative. They stated that this interpretation ignores the requirement of "mutuality." Some commenters also criticized the statement that the five-part test focuses on "a" primary basis, not "the" primary basis, although some acknowledged that "a" is, in fact, the word used in the regulation. Commenters said the interpretation is at odds with the common understanding of the word "primary" and will result in an unwarranted expansion of the five-part test. Commenters also asserted that the statement in the Department's interpretation conflated the primary basis requirement with a separate requirement for individualized advice. On the other hand, another commenter advocated that a Retirement Investor's position as to whether there is an understanding for the advice to provide a primary basis for the investment decision should be provided a presumption of correctness, which can only be overcome with significant evidence.

The Department is not persuaded by these comments to revise its interpretation. As stated above, the Department's interpretation has not rendered these requirements of

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the five-part test meaningless. Rather, the Department is appropriately applying the five-part test to current marketplace conduct and realities. The fact that a financial services professional is not considered a fiduciary under other laws, such as securities law or insurance law, is not a determinative factor under the five-part test. The focus is on the facts and circumstances surrounding the recommendation and the relationship, including whether those facts and circumstances give rise to a mutual agreement, arrangement, or understanding that the advice will serve as a primary basis for an investment decision. While satisfying the other laws may implicate parts of the test, fiduciary status applies only if all five prongs are satisfied.

The Department does not interpret the “primary basis” requirement as requiring proof that the advice was the single most important determinative factor in the Retirement Investor’s investment decision. This is consistent with the regulation’s reference to the advice as “a” primary basis rather than “the” primary basis. Similarly, the fact that a Retirement Investor may consult multiple financial professionals about a particular investment does not indicate that the Department’s analysis is incorrect. If, 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, that is enough to satisfy the “primary basis” requirement. Even so, all elements of the five-part test must be satisfied for a particular recommendation to be considered fiduciary investment advice, and if a Retirement Investor does not act on a recommendation made by a financial professional, the financial professional would not have any liability for that recommendation.

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The Department also recognizes that the requirement for “individualized” advice is separate from the “primary basis” requirement, but this does not mean that the individualized nature of a particular advice recommendation is irrelevant to whether the parties understood that the advice could serve as a “primary basis” for investment decisions.

The Department also is not persuaded by commenters to change its position on the role of written disclaimers of fiduciary status or of elements of the five-part test. In the context of the rendering of investment advice by a financial services professional, written statements disclaiming a mutual understanding or forbidding reliance on the advice as a primary basis for investment decisions will not be determinative, although such statements can be appropriately considered in determining whether a mutual understanding exists. This interpretation will not deprive parties of the ability to define the nature of their relationship, but recognizes that there needs to be consistency in that respect. 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. While financial services professionals may contractually disclaim engaging in activities that trigger elements of the five-part test, such as rendering advice that can be relied upon as a primary basis for the Retirement Investor’s investment decisions, they must do so clearly and act accordingly to demonstrate that there is in fact no mutual agreement, arrangement, or understanding to the contrary.



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One commenter similarly requested that the Department confirm that broker-dealers can disclaim a mutual agreement, arrangement or understanding in cases in which they provide investment recommendations that comply with Regulation Best Interest. The Department declines to do so expressly. As discussed above, the Department has not provided a safe harbor in this exemption for compliance with other regulators' conduct standards. The Department also declines in this exemption to set forth evidentiary burdens applied to establish a mutual understanding, including any presumptions as one commenter suggested. That question is better left to development by the courts or, if necessary, future guidance or rulemaking. The Department reiterates, however, that all prongs of the five-part test, including the regular basis prong, must be satisfied for a person or entity to be a fiduciary. Further, as noted above, a broker-dealer who does not wish to establish a fiduciary relationship in connection with a rollover may make clear in its communications that it does not intend to enter into an ongoing relationship to provide investment advice and act in conformity with that communication.

#### “Hire Me” Communications

Some commenters asked the Department to confirm that so-called “hire me” communications, in which financial services professionals engage in introductory conversations to promote their advisory services to Retirement Investors, will not be treated as fiduciary communications under Title I and the Code. Commenters indicated that these types of communications are an important part of the process for a Retirement Investor to select an investment advice provider. A commenter pointed to statements in the Department's 2016 fiduciary rulemaking about the ability of a person or firm to “tout

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the quality of his, her, or its own advisory or investment management services” without being considered an investment advice fiduciary.<sup>51</sup> The commenter also pointed to an FAQ issued by the SEC staff in the context of Regulation Best Interest, which confirmed that, absent other factors, the SEC staff would not view this type of communication as a recommendation:

I have been working with our mutual friend, Bob, for fifteen years, helping him to invest for his kids’ college tuition and for retirement. I would love to talk with you about the types of services my firm offers, and how I could help you meet your goals. Here is my business card. Please give me a call on Monday so that we can discuss.<sup>52</sup>

In the context of the present exemption proceeding, the Department does not believe that there should be significant concerns about introductory “hire me” conversations. This is because all prongs of the five-part test must be satisfied for a financial services provider to be considered a fiduciary. Nevertheless, the Department confirms that the interpretive statements in this preamble are not intended to suggest that marketing activity of the type described above would be treated as investment advice covered under the five-part test. To the extent, however, that the marketing of advisory services is accompanied by an investment recommendation, such as a recommendation to

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<sup>51</sup> Definition of the Term “Fiduciary”; Conflict of Interest Rule – Retirement Investment Advice, 81 FR 20946, 20968 (April 8, 2016).

<sup>52</sup> See Frequently Asked Questions on Regulation Best Interest, *available at* [www.sec.gov/tm/faq-regulation-best-interest](http://www.sec.gov/tm/faq-regulation-best-interest).

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invest in a particular fund or security, the investment recommendation would be covered if all five parts of the test were satisfied.

***For a fee or other compensation, direct or indirect***

The Department’s preamble interpretation in the proposal noted that in addition to satisfying the five-part test, a person must receive a “fee or other compensation, direct or indirect” to be an investment advice fiduciary.<sup>53</sup> The Department has long interpreted this requirement broadly to cover “all fees or other compensation incident to the transaction in which the investment advice to the plan has been rendered or will be rendered.”<sup>54</sup> The Department previously noted that “this may include, for example, brokerage commissions, mutual fund sales commissions, and insurance sales commissions.”<sup>55</sup> In the rollover context, fees and compensation received from transactions involving rollover assets would be incident to the advice to take a distribution from the Plan and to roll over the assets to an IRA.

While commenters acknowledged this discussion is consistent with the Department’s longstanding interpretive position, they asserted that it is inconsistent with views expressed by the Fifth Circuit in the *Chamber* opinion and with the definition of a fiduciary in Title I and the Code. Responses to arguments about the fee requirement and the *Chamber* opinion follow in the next section.

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<sup>53</sup> ERISA section 3(21)(A)(ii); Code section 4975(e)(3)(B).

<sup>54</sup> Preamble to the Department's 1975 Regulation, 40 FR 50842 (October 31, 1975).

<sup>55</sup> *Id.*

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### ***Procedural and Legal Arguments***

Many commenters asserted that the Department failed to comply with the Administrative Procedure Act because the interpretation of the five-part test set forth in the proposal, in their view, effectively amended the five-part test without appropriate procedures. As discussed above, the commenters expressed the view that the Department’s preamble interpretation effectively eliminated the “regular basis” and “mutual agreement, arrangement or understanding” prongs of the five-part test. A few commenters additionally suggested that providing the interpretation in the preamble of a proposed class exemption did not provide sufficient notice and opportunity for comment.

The Department’s interpretation does not amend the five-part test, but only provides interpretive guidance, in the context of the relief provided in the new exemption, as to how that test applies to current practices in providing investment advice. The regulatory five-part test has long been understood to provide a functional fiduciary test, and the Department’s interpretation is based on this understanding. The Department’s interpretation does not effectively eliminate any of the elements of the five-part test, but rather applies them to current marketplace conduct and harmonizes with the current regulatory environment.<sup>56</sup>

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<sup>56</sup> One commenter asserted that the Department’s interpretation was in substance a “legislative rule” which required notice and comment rulemaking, citing *Am. Min. Cong. v. Mine Safety & Health Admin.*, 995 F.2d

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Some commenters opined that the Department's proposed interpretation of the five-part test would result in parties being considered fiduciaries under Title I and the Code under circumstances that would be inconsistent with pronouncements and holdings by the Fifth Circuit in the *Chamber* opinion. In particular, commenters invoked statements by the court that fiduciary status is based on the existence of a relationship of trust and confidence. Commenters stated that at the time of the first instance of advice in an ongoing relationship, a financial services professional may not have developed a relationship of trust and confidence with its customer.

In response, the Department notes that the Fifth Circuit's *Chamber* opinion discussed approvingly the Department's 1975 regulation, which established the five-part test. The court did not indicate that, in an ongoing relationship, there should be any initial instances of advice free of fiduciary status until some later period in which a relationship of trust and confidence has been demonstrated repeatedly. To the contrary, the court expressed agreement that investment advisers registered under the Investment Advisers Act may appropriately be considered fiduciaries without indicating that

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1106, 1112 (D.C. Cir. 1993), and *Chao v. Rothermel*, 327 F.3d 223, 227 (3d Cir. 2003). The Department disagrees that the factors cited in these cases are satisfied. In this regard, there would be an adequate legislative basis for enforcement in the absence of the interpretation; the preamble interpretation will not be published in the CFR; the Department has not invoked its general legislative authority; and for the reasons stated above, the interpretation does not effectively amend the five-part test. The Department further notes that the interpretation was subject to notice and comment as part of the proposal.

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fiduciary status would only apply after a period of time. Of particular importance, in the Department’s view, is the court’s approving discussion that the SEC has “repeatedly held” that “[t]he very function of furnishing [investment advice for compensation]—learning the personal and intimate details of the financial affairs of clients and making recommendations as to purchases and sales of securities—cultivates a confidential and intimate relationship.”<sup>57</sup>

The proposed exemption preamble included a discussion of some Financial Institutions paying unrelated parties to solicit clients for them in accordance with Rule 206(4)-3 under the Investment Advisers Act.<sup>58</sup> The Department noted that advice by a paid solicitor to take a distribution from a Title I Plan and to roll over assets to an IRA could be part of ongoing advice to a Retirement Investor, if the Financial Institution that pays the solicitor provides ongoing fiduciary advice to the IRA owner. A commenter asserted that the interpretation appeared to confer fiduciary status on the solicitor in the absence of a relationship of trust or confidence, which would be impermissible under the Fifth Circuit’s opinion. The commenter further asked the Department to clarify whether the mere fact of an affiliation, such as between a broker-dealer and a registered investment adviser, would result in a recommendation by a broker-dealer being

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<sup>57</sup> 885 F.3d 360, 374 (5th Cir. 2018) (citing *Hughes*, Exchange Act Release No. 4048, 1948 WL 29537, at \*4, \*7 (Feb. 18, 1948), *aff’d sub nom.*, *Hughes v. SEC*, 174 F.2d 969 (D.C. Cir. 1949) and *Mason, Moran & Co.*, Exchange Act Release No. 4832, 1953 WL 44092, at \*4 (Apr. 23, 1953)).

<sup>58</sup> 85 FR 40840 at n.40.

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considered fiduciary investment advice if an ongoing relationship later developed with an affiliated registered investment adviser.

The Department's statement regarding paid solicitors was intended to ensure that Financial Institutions do not take the position that the actions of a party paid to solicit business for them would be considered distinct from any ongoing relationship that resulted. Although the Fifth Circuit's *Chamber* opinion expressed agreement that investment advisers registered under the Investment Advisers Act may appropriately be considered fiduciaries under Title I and the Code, the opinion did not address the practice of paid solicitors. The Department confirms, however, that its statement about paid solicitors was not intended to suggest that a broker-dealer that makes an isolated recommendation would be considered a fiduciary if, entirely unrelated to the recommendation, an ongoing relationship developed with an affiliated investment adviser.

Commenters likewise pointed to statements made in the proposed exemption preamble regarding the statutory requirement that, for fiduciary status to attach, advice must be provided "for a fee or other compensation, direct or indirect." The preamble stated, "[i]n the rollover context, fees and compensation received from transactions involving rollover assets would be incident to the advice to take a distribution from the

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Plan and to roll over the assets to an IRA.”<sup>59</sup> This is consistent with the Department’s longstanding position that the statutory language covers “all fees or other compensation incident to the transaction in which the investment advice to the plan has been rendered or will be rendered.”<sup>60</sup>

Commenters stated that the preamble interpretation is inconsistent with the statute because, in their view, the fee would be for completed sales, rather than for advice. Some commenters asserted that their view was supported by the Fifth Circuit’s *Chamber* opinion. The Fifth Circuit’s *Chamber* opinion, however, did not criticize the Department’s longstanding interpretation of this statutory requirement. The Fifth Circuit, in fact, indicated the interpretation is appropriate as applied to a party that has met the elements of the five-part test.<sup>61</sup> The Department’s interpretation of the requirement of a “fee or compensation, direct or indirect” is consistent with the statutory language defining a fiduciary under Title I and the Code. Of course, this does not suggest that the Department intends to take the position that transactional compensation to an investment professional who does not meet the elements of the five-part test is a fee for advice. Rather, the Department recognizes that investment professionals may engage in non-

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<sup>59</sup> *Id.* at 40840.

<sup>60</sup> *Id.*

<sup>61</sup> 885 F.3d at 374 (discussing approvingly the Department’s Advisory Opinion 83-60 (Nov. 21 1983) which provided that, “if, under the particular facts and circumstances, the services provided by the broker-dealer include the provision of ‘investment advice’, as defined in regulation 2510 .3-21(c), it may be reasonably expected that, even in the absence of a distinct and identifiable fee for such advice, a portion of the commissions paid to the broker-dealer would represent compensation for the provision of such investment advice”).



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fiduciary sales activity in which, as in many sales activities, recommendations are made to a customer. The Department's interpretation respects the legitimate sales function of such a non-fiduciary investment professional.

A few commenters additionally asserted that the Department's preamble interpretation is inconsistent with Executive Orders 13891, Promoting the Rule of Law Through Improved Agency Guidance Documents, and 13892, Promoting the Rule of Law Through Transparency and Fairness in Civil Administrative Enforcement and Adjudication, which they described as requiring transparency and fairness, and as imposing notice and comment requirements, or new restrictions, on agencies when issuing guidance documents.<sup>62</sup> Even assuming the preamble interpretation is guidance regulated by the Executive Orders, the proposed preamble statement provided notice of the interpretation and solicited public comments on it.<sup>63</sup> Accordingly, the Department complied with the Executive Orders.

A few commenters contended that the Department's preamble interpretation is inconsistent with the characterization of the regulatory package as deregulatory. In the Department's view, the exemption as a whole is deregulatory because it provides a

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<sup>62</sup> Executive Order 13891, 84 FR 55235 (Oct. 15, 2019); Executive Order 13892, 84 FR 55238 (Oct. 15, 2019).

<sup>63</sup> See 85 FR at 40840 ("The Department requests comment on all aspects of this part of its proposal.").

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broader and more flexible means under which investment advice fiduciaries to Plans and IRAs may receive compensation and engage in certain principal transactions that would otherwise be prohibited under Title I and the Code. Some commenters stated that the exemption effectively reinstates the 2016 fiduciary rule, and one asserted that the Department did so without addressing the President’s related concerns in his Memorandum on Fiduciary Duty Rule.<sup>64</sup> As discussed above, the proposed exemption did not amend the 1975 regulation as the 2016 fiduciary rule sought to undertake. In addition, unlike the 2016 fiduciary rulemaking, this project did not amend other, previously granted, prohibited transaction exemptions.

## **Description of the Final Exemption**

### ***Scope of Relief – Section I***

#### ***Financial Institutions***

The exemption is available to entities that satisfy the exemption’s definition of a “Financial Institution.” The exemption limits the types of entities that qualify as a Financial Institution to SEC- and state-registered investment advisers, broker-dealers, insurance companies, and banks.<sup>65</sup> The definition is based on the entities identified in the

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<sup>64</sup> See *Presidential Memorandum on Fiduciary Duty Rule* (Feb. 3, 2017), [www.whitehouse.gov/presidential-actions/presidential-memorandum-fiduciary-duty-rule/](http://www.whitehouse.gov/presidential-actions/presidential-memorandum-fiduciary-duty-rule/).

<sup>65</sup> The exemption includes a “bank or similar financial institution supervised by the United States or a state, or a savings association (as defined in section 3(b)(1) of the Federal Deposit Insurance Act (12 U.S.C.

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statutory exemption for investment advice under ERISA section 408(b)(14) and Code section 4975(d)(17), which are subject to well-established regulatory conditions and oversight<sup>66</sup> and have been deemed able to prudently mitigate certain conflicts of interest in their investment advice through adherence to tailored principles under the statutory exemption. The Department takes a similar approach here, and, therefore, is including the same group of entities. To fit within the definition of *Financial Institution*, the firm must not have been disqualified or barred from making investment recommendations by any insurance, banking, or securities law or regulatory authority (including any self-regulatory organization).

The Department recognized in the proposed exemption that different types of Financial Institutions have different business models, and the exemption is drafted to apply flexibly to these institutions.<sup>67</sup> Following is a discussion of the different types of Financial Institutions and comments received in connection with the definition.

#### Broker-Dealers

Broker-dealers provide a range of services to Retirement Investors, ranging from executing one-time transactions to providing personalized investment recommendations, and they may be compensated on a transactional basis such as through commissions.<sup>68</sup> If

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1813(b)(1)).” The Department interprets this definition to extend to credit unions.

<sup>66</sup> ERISA section 408(g)(11)(A) and Code section 4975(f)(8)(J)(i).

<sup>67</sup> Some of the Department’s existing prohibited transaction exemptions would also apply to the transactions described in the next few paragraphs.

<sup>68</sup> Regulation Best Interest Release, 84 FR at 33319.

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broker-dealers that are investment advice fiduciaries with respect to Retirement Investors provide investment advice that affects the amount of their compensation, they must rely on an exemption.

One commenter argued that broker-dealers should not be able to rely on the exemption because they are not fiduciaries under the securities laws. The fiduciary definition in Title I and the Code does not turn, however, on whether parties are characterized as fiduciaries under the securities laws, but rather on whether the persons rendering advice meet the conditions of the functional test of fiduciary status as set forth in the Department’s regulation. Moreover, the best interest standard applicable to broker-dealers under Regulation Best Interest is rooted in fiduciary principles.<sup>69</sup>

As discussed by the SEC, under the securities laws, a key difference between broker-dealers and investment advisers is that investment advisers typically have a duty to monitor their customers’ investments, whereas broker-dealers may more readily limit the scope of their obligations to the specific transactions recommended.<sup>70</sup> Under Title I and the Code, investment advice fiduciaries are not necessarily obligated to assume a

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<sup>69</sup> The SEC explained “key elements of the standard of conduct that applies to broker-dealers, at the time a recommendation is made, under Regulation Best Interest will be substantially similar to key elements of the standard of conduct that applies to investment advisers pursuant to their fiduciary duty under the Advisers Act.” Regulation Best Interest Release, 84 FR at 33461.

<sup>70</sup> The SEC explained that “[t]here are also key differences between Regulation Best Interest and the Advisers Act fiduciary standard that reflect the distinction between the services and relationships typically offered under the two business models. For example, an investment adviser’s fiduciary duty generally includes a duty to provide ongoing advice and monitoring, while Regulation Best Interest imposes no such duty and, instead, requires that a broker-dealer act in the retail customer’s best interest *at the time* a recommendation is made.” Regulation Best Interest Release, 84 FR at 33321 (emphasis in the original).

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duty to monitor, absent an agreement, arrangement or understanding with their investor client to the contrary. The Department's exemption places the transaction-based advice model on an even playing field with the investment adviser model, and applies fiduciary standards in both contexts that are generally consistent with the standards imposed by the SEC. In this manner, the exemption avoids undue expense and generally aligns its requirements with SEC requirements. Moreover, Congress included broker-dealers and registered investment advisers in the statutory advice exemption in ERISA section 408(b)(14) and Code section 4975(d)(17), according to the same set of conditions.

#### Registered Investment Advisers

Registered investment advisers generally provide ongoing investment advice and services and are commonly paid either an assets under management fee or a fixed fee.<sup>71</sup> If a registered investment adviser is an investment advice fiduciary that charges only a level fee that does not vary on the basis of the investment advice provided, the registered investment adviser may not violate the prohibited transaction rules.<sup>72</sup> However, if the registered investment adviser provides investment advice that causes itself to receive the level fee, such as through advice to roll over Plan assets to an IRA, the fee (including an

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<sup>71</sup> 84 FR at 33319.

<sup>72</sup> As noted above, fiduciaries who use their authority to cause themselves or their affiliates or related entities to receive additional compensation violate the prohibited transaction provisions unless an exemption applies. 29 CFR 2550.408b-2(e)(1).

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ongoing management fee paid with respect to the IRA) is prohibited under Title I and the Code.<sup>73</sup> Additionally, if a registered investment adviser that is an investment advice fiduciary is dually-registered as a broker-dealer, the registered investment adviser may engage in a prohibited transaction if it recommends a transaction that increases the firm's compensation, such as for execution of securities transactions in its brokerage capacity. Of course, as discussed above, rollover recommendations or assistance with a rollover do not constitute fiduciary investment advice if the five-part test, including the regular basis prong, is not satisfied.

Commenters sought clarification of the exemption's coverage of certain transactions particularly relevant to registered investment advisers. The commenters inquired about reliance on the exemption solely for a rollover recommendation, under circumstances in which the advice arrangement after the rollover does not involve prohibited transactions (e.g., the compensation arrangement involves only a level fee that does not vary on the basis of the investment transactions) or is not eligible for relief because it is discretionary. The Department confirms that the exemption is available for fiduciary investment advice regarding rollover transactions, even in situations where the exemption is not available (or needed) either before or after the rollover transaction. The commenter also inquired as to whether a financial services provider that serves as a

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<sup>73</sup> As discussed above, the Department has long interpreted the requirement of a fee to cover "all fees or other compensation incident to the transaction in which the investment advice to the plan has been rendered or will be rendered." Preamble to the Department's 1975 Regulation, 40 FR 50842 (October 31, 1975).

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discretionary investment manager to a Plan pursuant to ERISA section 3(38), a transaction that is not covered by the exemption, can rely on the exemption to provide fiduciary investment advice to the Plan's participants and beneficiaries on distribution options. The Department confirms that the exemption is available in that circumstance as well.

#### Insurance Companies

Insurance companies commonly compensate insurance agents on a commission basis, which generally creates prohibited transactions when insurance agents are investment advice fiduciaries that provide investment advice to Retirement Investors in connection with the sales. The Department is aware that insurance companies often sell insurance products and fixed (including indexed) annuities through different distribution channels than broker-dealers and registered investment advisers. While some insurance agents are employees of an insurance company, other insurance agents are independent, and work with multiple insurance companies. The final exemption applies to all of these business models.

In the proposal, the Department suggested insurance companies would have several options for compliance. The proposal stated that insurance companies could comply with the new exemption by overseeing independent insurance agents; they could comply with the new exemption by creating oversight and compliance systems through contracts with insurance intermediaries such as independent marketing organizations (IMOs), field marketing organizations (FMOs) or brokerage general agencies (BGAs); or

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they could rely on the existing class exemption for insurance transactions, PTE 84-24,<sup>74</sup> as an alternative. Further, the Department sought comment on whether the exemption should include insurance intermediaries as Financial Institutions for the recommendation of fixed (including indexed) annuity contracts, and if so, how the insurance intermediaries should be defined and whether additional protective conditions might be necessary with respect to the intermediaries. Discussion of comments on these aspects of the proposal follow.

#### *Direct Oversight*

In the proposal, the Department stated that insurance companies could supervise independent insurance agent Investment Professionals who provide investment advice on their products. To comply with the exemption, the Department stated that an insurance company could adopt and implement supervisory and review mechanisms and avoid improper incentives that preferentially push the products, riders, and annuity features that might incentivize Investment Professionals to provide investment advice to Retirement Investors that does not meet the Impartial Conduct Standards. Insurance companies could implement procedures to review annuity sales to Retirement Investors to ensure

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<sup>74</sup> Class Exemption for Certain Transactions Involving Insurance Agents and Brokers, Pension Consultants, Insurance Companies, Investment Companies and Investment Company Principal Underwriters, 49 FR 13208 (Apr. 3, 1984), as corrected, 49 FR 24819 (June 15, 1984), as amended, 71 FR 5887 (Feb. 3, 2006).



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that they were made in satisfaction of the Impartial Conduct Standards, much as they may already be required to review annuity sales to ensure compliance with state-law suitability requirements.<sup>75</sup> The Department stated in the proposal that insurance company Financial Institutions would be responsible only for an Investment Professional’s recommendation and sale of products offered to Retirement Investors by the insurance company in conjunction with fiduciary investment advice, and not unrelated and unaffiliated insurers.<sup>76</sup>

A few commenters took the position in response to the proposal that insurance companies are not set up in such a manner as to be able to act as Financial Institutions

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<sup>75</sup> Cf. NAIC Model Regulation Section 6.C.(2)(d) (“The insurer shall establish and maintain procedures for the review of each recommendation prior to issuance of an annuity that are designed to ensure that there is a reasonable basis to determine that the recommended annuity would effectively address the particular consumer’s financial situation, insurance needs and financial objectives. Such review procedures may apply a screening system for the purpose of identifying selected transactions for additional review and may be accomplished electronically or through other means including, but not limited to, physical review. Such an electronic or other system may be designed to require additional review only of those transactions identified for additional review by the selection criteria”); and (e) (“The insurer shall establish and maintain reasonable procedures to detect recommendations that are not in compliance with subsections A, B, D and E. This may include, but is not limited to, confirmation of the consumer’s consumer profile information, systematic customer surveys, producer and consumer interviews, confirmation letters, producer statements or attestations and programs of internal monitoring. Nothing in this subparagraph prevents an insurer from complying with this subparagraph by applying sampling procedures, or by confirming the consumer profile information or other required information under this section after issuance or delivery of the annuity”). The prior version of the model regulation, which was adopted in some form by a number of states, also included similar provisions requiring systems to supervise recommendations. See Annuity Suitability (A) Working Group Exposure Draft, Adopted by the Committee Dec. 30, 2019, available at [www.naic.org/documents/committees\\_mo275.pdf](http://www.naic.org/documents/committees_mo275.pdf) (comparing 2020 version with prior version).

<sup>76</sup> Cf. *id.*, Section 6.C.(4) (“An insurer is not required to include in its system of supervision: (a) A producer’s recommendations to consumers of products other than the annuities offered by the insurer”).

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with respect to independent insurance agents, which they said would ultimately put insurance companies and insurance products at a competitive disadvantage. Commenters asserted that insurance companies do not have insight into or control over independent agents' business and/or behavior and do not consent to or authorize their activities.

While several commenters acknowledged that the proposal was consistent with the NAIC Model Regulation in providing that an insurance company Financial Institution would be responsible only for recommendations with respect to its own products, they argued that the proposed exemption deviated from the NAIC's approach in failing to also state that insurers do not have to include in their supervisory systems "consideration of or comparison to options available to the producer or compensation relating to those options other than annuities or other products offered by the insurer."<sup>77</sup>

In response, the Department notes that the NAIC Model Regulation contemplates that insurance companies will maintain a system of oversight with respect to insurance agents. Section I provides that the purpose of the Model Regulation is to "require producers, as defined in this regulation, to act in the best interest of the consumer when making a recommendation of an annuity and to require insurers to establish and maintain a system to supervise recommendations so that the insurance needs and financial

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<sup>77</sup> NAIC Model Regulation Section 6.C.(4)(B).

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objectives of consumers at the time of the transaction are effectively addressed.”<sup>78</sup>

Accordingly, the Department believes that a system of oversight by insurance companies over independent insurance agents is achievable.

In terms of the specific oversight requirements, the Department reiterates the statement in the proposal that the exemption requires insurance company Financial Institutions to be responsible only for an Investment Professional’s recommendation and sale of products offered to Retirement Investors by the insurance company in conjunction with fiduciary investment advice, and not an unrelated and unaffiliated insurer. The Department also clarifies, in response to commenters, that the exemption does not require consideration of or comparison to specific options available to an independent insurance agent or compensation relating to those options, other than annuities or other products offered by the insurer. The Department’s approach is consistent with the approach of the NAIC Model Regulation in this regard as well. However, the Department does not intend to suggest that insurance company Financial Institutions have no obligation to evaluate the financial inducements they offer to independent agents to ensure that the exemption’s

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<sup>78</sup> *Id.*, Section 1.A. The Department also notes that the prior version of the Model Regulation, which was adopted in some form by a number of states, contains a similar statement. (“The purpose of this regulation is to require insurers to establish a system to supervise recommendations and to set forth standards and procedures for recommendations to consumers that result in transactions involving annuity products so that the insurance needs and financial objectives of consumers at the time of the transaction are appropriately addressed.”)

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standards are satisfied. As discussed above, Financial Institutions can implement procedures to review annuity sales to Retirement Investors under fiduciary investment advice arrangements to ensure that they were made in satisfaction of the Impartial Conduct Standards, much as they may already be required to review annuity sales to ensure compliance with state-law suitability requirements.<sup>79</sup>

#### *Insurance Intermediaries*

In the proposal, the Department stated that insurance companies could create a system of oversight and compliance by contracting with an insurance intermediary or other entity to implement policies and procedures designed to ensure that all of the agents associated with the intermediary adhere to the conditions of this exemption. Thus, for example, as one possible approach, the preamble stated that an insurance intermediary could eliminate compensation incentives across all the insurance companies that work with the insurance intermediary, assisting each of the insurance companies with their independent obligations under the exemption. This might involve the insurance intermediary's review of documentation prepared by insurance agents to comply with the exemption, as may be required by the insurance company, or the use of third-party industry comparisons available in the marketplace to help independent insurance agents

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<sup>79</sup> See *supra* n. 75.

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recommend products that are prudent for the Retirement Investors they advise.

This type of arrangement is also contemplated by the NAIC Model Regulation, which provides that an insurer is not restricted from contracting for performance of supervisory review functions.<sup>80</sup> Also, insurance intermediaries can receive payment for these services; to the extent they are “affiliates” or “related entities” of the Financial Institution or Investment Professional, the exemption extends to their receipt of compensation so long as the conditions of the exemption are satisfied.

One commenter that is an IMO supported the suggestion in the preamble that insurance intermediaries could serve this function. The commenter stated that it currently works with insurance companies to ensure that their policies and procedures are carried out by independent agents. The commenter took the position that it is positioned to work directly with insurance companies to ensure that the proper oversight and compliance systems are in place to comply with the exemption.

*PTE 84-24*

To the extent that insurance companies determine that the supervisory requirements of this exemption are not well-suited to their business models, it is important to note that insurance and annuity products can also continue to be recommended and sold under the existing exemption for insurance transactions, PTE 84-24. Unlike in the Department’s 2016 fiduciary rulemaking, PTE 84-24 is not being

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<sup>80</sup> NAIC Model Regulation, Section 6.C.(3)(a).

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amended in connection with the current proposed exemption.

PTE 84-24 provides prohibited transaction relief for the “receipt, directly or indirectly, by an insurance agent or broker ... of a sales commission from an insurance company in connection with the purchase, with plan assets, of an insurance or annuity contract.” The agent or broker must generally disclose its sales commission and receive written approval of the transaction from an independent fiduciary.

A commenter expressed concern that the Department’s disavowal of the Deseret Letter would result in a requirement to provide the disclosures required by PTE 84-24 to a plan fiduciary, rather than the IRA owner, in the case of a rollover recommendation. The Department confirms that when a transaction under PTE 84-24 involves an IRA, the disclosure can be provided to the IRA owner. Further, to avoid uncertainty, the Department also confirms that an insurance intermediary can receive a part of the commission payment that is permitted under PTE 84-24, provided the conditions of the exemption are satisfied.

*Insurance Intermediaries as Financial Institutions*

The Department also sought comment in the proposal as to whether the exemption’s definition of Financial Institution should be expanded to include insurance intermediaries. Under that approach, the insurance intermediary would implement the conditions of the exemption applicable to Financial Institutions, and insurance companies would not have to do so.

Several commenters supported the addition of insurance intermediaries as Financial Institutions, in connection with their contention that insurance companies are

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not in a position to exert oversight over independent insurance agents because the independent agents sell products of other insurance companies as well. A few commenters stated that the insurance intermediaries are in a position to do so because of their proximity to and expertise working with independent insurance agents. The commenters stated that insurance intermediaries have greater insight into and control over the actions of independent insurance agents than insurance companies. Further, the commenters emphasized that insurance intermediaries are regulated by the states as insurance agencies, and they have sufficient resources and staff to act as Financial Institutions. These commenters also asserted insurance intermediaries' similarity to the registered investment adviser business model and stated that a failure to include insurance intermediaries as Financial Institutions would result in a competitive disadvantage for insurance intermediaries and potentially less choice for Retirement Investors.

Other commenters, however, indicated that insurance intermediaries are not in a position to oversee independent insurance agents because it is common for independent insurance agents to work with multiple intermediaries, raising issues as to whether multiple intermediaries would have to oversee the same independent agent. One commenter also indicated that independent agents have contracts or arrangements directly with the insurance company; by contrast, there is no contract or implied contract between insurance intermediaries and independent insurance agents, and insurance intermediaries do not direct the independent insurance agents' recommendations to Retirement Investors. A few commenters asserted that unlike the other entities included in the definition of a Financial Institution, insurance intermediaries do not have a regulator that

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sets standards regarding oversight and supervisory policies and procedures. One commenter asserted that the exemption would need to include conditions addressing the Department's oversight of insurance intermediaries if they were included in the definition of a Financial Institution. Another commenter urged the Department to work closely with insurance intermediaries before including them as Financial Institutions, so as to avoid imposing conditions that are impractical or burdensome.

Based on the record before it, the Department has concluded that it should not expand the scope of the definition of Financial Institution to insurance intermediaries, such as IMOs, FMOs, or BGAs. These entities do not have supervisory obligations over independent insurance agents under state or federal law that are comparable to those of the other entities, such as insurance companies, banks, and broker-dealers, or a history of exercising such supervision in practice. They are generally described as wholesaling and marketing and support organizations, but not tasked with ensuring compliance with regulatory standards. In addition, they are not subject to the sort of capital and solvency requirements imposed on state-regulated insurance companies and banks.

Commenters also did not provide specific suggestions for how to define the insurance intermediaries that could be Financial Institutions. One commenter suggested that Financial Institution status and its attendant compliance responsibilities should be placed on the intermediary that is closest to the Retirement Investor and the Investment Professional advising that investor. However, this suggestion does not alleviate the operational issues that would exist when an independent agent works with or through more than one intermediary. Commenters also did not offer suggestions as to substantive



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conditions that should be included to make up for the lack of regulatory oversight. The considerations above may not be insuperable obstacles to treating insurance intermediaries as Financial Institutions under the terms of a future exemption that is based on an appropriate record focused on such support organizations. The Department anticipates that any such exemption would specifically focus on the unique attributes, strengths, and weaknesses of these entities, and on any special conditions that would be necessary to ensure they are able to act in the necessary supervisory capacity as Financial Institutions.

The Department also has maintained the provision in this exemption under which the definition of a Financial Institution can expand based upon subsequently granting individual exemptions to additional entities that are investment advice fiduciaries that meet the five-part test and are seeking to be treated as covered Financial Institutions. Thus, additional types of entities, such as IMOs, FMOs, or BGAs may separately apply for prohibited transaction relief to receive compensation in connection with the provision of investment advice, according to the same conditions that apply to the Financial Institutions covered by this exemption. If the Department grants to such an entity an individual exemption under ERISA section 408(a) and Code section 4975(c)(2) after the date this exemption is granted, the expanded definition of Financial Institution in the individual exemption would be added to this class exemption so other entities that satisfy the definition could similarly use this class exemption.

The Department acknowledges that some commenters felt this approach would put insurance intermediaries at a disadvantage as compared to other Financial

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Institutions. As discussed above, however, there is cause for concern about including insurance intermediaries in the final exemption on the same footing as the types of entities included in the Financial Institution definition. On the record before it, the Department has concluded that the better course of action is to invite any insurance intermediaries to apply for a separate exemption as part of a public notice and comment process that can specifically focus on their unique attributes, so that the Department can determine whether and how to grant exemptive relief, subject to appropriate definitional and protective conditions.

#### Banks

Banks and similar institutions are permitted to act as Financial Institutions under the exemption if they or their employees are investment advice fiduciaries with respect to Retirement Investors. The Department sought comment on whether banks and their employees provide investment advice to Retirement Investors, and if so, whether the proposal needed adjustment to address any unique aspects of their business models.

A trade association representing banks submitted a comment that described a wide variety of interactions with banking customers, including IRA investment programs and bank networking arrangements and referral programs. The commenter stated that banks that render investment advice are fully subject to applicable federal and state banking laws governing fiduciary status and activities.<sup>81</sup> The commenter expressed

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<sup>81</sup> Citing 12 CFR Part 9 (fiduciary activities of banks).

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support for the exemption, so long as certain suggested changes were adopted to conform to banks' distinct business model, particularly with respect to the retrospective review and the recordkeeping provision. The Department's responses to these comments on the exemption are discussed below in the sections on the retrospective review and recordkeeping provision.

#### Affiliates and Related Entities

One commenter stated that the exemption text should include a definition of "affiliate" and "related entity." The Department has added the definitions that previously appeared in the preamble of the proposed exemption, in Section V(a) and (j), respectively, of the final exemption text.

An affiliate is defined as (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 (for this purpose, "control" means the power to exercise a controlling influence over the management or policies of a person other than an individual); (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. A related entity is defined as an entity that is not an affiliate, but in which the Investment Professional or Financial Institution has an interest that may affect the exercise of its best judgment as a fiduciary.

Another commenter stated that the Department should add foreign affiliates of banks, broker-dealers, insurance companies, and registered investment advisers to the

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entities covered by the exemption, given the increasingly global nature of retirement services. The proposed exemption indicated that relief would be available to affiliates and related entities of a Financial Institution and Investment Professional, if the Financial Institution and Investment Professional satisfied the exemption's conditions. The Department did not exclude foreign affiliates in the proposal, and confirms that they are not excluded in the exemption, as finalized.

#### Other Entities – Recordkeepers and HSA providers

One commenter requested that recordkeepers be included as Financial Institutions. To the extent that an entity hired to act as a recordkeeper to a Plan or an IRA falls within the list of defined Financial Institutions, it may rely upon the exemption. However, the Department declines to add a general category for recordkeepers to the definition. The Department does not believe a recordkeeper that is not also a bank, broker-dealer, insurance company, or registered investment adviser would have the requisite regulatory oversight to necessarily act as a Financial Institution. However, such parties can seek an individual exemption from the Department, as provided in the definition of a Financial Institution in Section V(e).

One commenter addressed health savings accounts (HSAs), indicating that the exemption should apply to advice to individuals with HSAs. The commenter did not indicate whether the definition of Financial Institution needed to be expanded to facilitate advice regarding HSAs. The exemption, as proposed and finalized, defines an IRA as “any account or annuity described in Code section 4975(e)(1)(B) through (F)” which includes a “health savings account described in [Code] section 223(d).” Therefore,

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advice may be provided to individuals with HSAs, subject to the conditions of the exemption.

### ***Investment Professionals***

As defined in the proposal, an *Investment Professional* is an individual who is a fiduciary of a Plan or an IRA by reason of the provision of investment advice, who is an employee, independent contractor, agent, or representative of a Financial Institution, and who satisfies the federal and state regulatory and licensing requirements of insurance, banking, and securities laws (including self-regulatory organizations) with respect to the covered transaction, as applicable. Similar to the definition of *Financial Institution*, this definition also includes a requirement that the Investment Professional has not been disqualified from making investment recommendations by any insurance, banking, or securities law or regulatory authority (including any self-regulatory organization).

One commenter suggested that the exemption should require investment professionals to be certified by an accredited organization or state agency in financial planning issues. The Department has not adopted this suggestion because it does not have sufficient information in the record on this type of certification to incorporate it as a condition.

Another commenter asked the Department to confirm that insurance agents unaffiliated with a broker-dealer or registered investment adviser are investment advice fiduciaries when providing investment advice to Retirement Investors through the sale of insurance products and fixed (including indexed) annuities, and are subject to the requirements under the exemption. The Department confirms that an insurance agent that

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meets the elements of the five-part test and receives a fee or other compensation, direct or indirect, with respect to a particular transaction, is a fiduciary with respect to that transaction. Under those circumstances, the insurance agent must avoid prohibited transactions or comply with a prohibited transaction exemption.

### ***Retirement Investors and Plans***

The exemption provides relief for specified Covered Transactions when Financial Institutions and Investment Professionals provide investment advice to *Retirement Investors*. A Retirement Investor is defined as (1) a participant or beneficiary of a Plan with authority to direct the investment of assets in his or her account or to take a distribution, (2) the beneficial owner of an IRA acting on behalf of the IRA, or (3) a fiduciary of a Plan or an IRA. A *Plan* for purposes of the exemption is defined as any employee benefit plan described in ERISA section 3(3) and any plan described in Code section 4975(e)(1)(A). An *IRA* is defined as any plan that is an account or annuity described in the other parts of section 4975(e)(1): paragraphs 4975(e)(1)(B) through (F).

A few commenters questioned the meaning of Retirement Investor with respect to the definition's use of the word *Plan*. One commenter requested clarification that the use of the term *Plan* with respect to a Retirement Investor, in fact, included Title I welfare benefit plans despite the use of the word "retirement." Two other commenters requested that the definition of Plan specifically exclude Title I welfare benefit plans that do not include an investment component, such as health insurance plans, disability insurance plans, and term life insurance plans.

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While the exemption uses the term Retirement Investor throughout the exemption, the use of the term was not intended to exclude investment advice provided to Title I welfare benefit plans. In fact, the exemption's definition of Plan states that it is defined, in part, by reference to ERISA section 3(3), which explicitly includes Title I welfare benefit plans.

With respect to the request to exclude Plans that do not contain an investment component, the Department responds that the exemption is only necessary and available to fiduciaries who provide investment advice as described in the five-part test. If there is no fiduciary investment advice, the exemption would not be applicable or needed. In light of this limitation, the Department does not believe any further amendment to the definition of a Plan is necessary.

### ***Covered Transactions***

The exemption permits Financial Institutions and Investment Professionals, and their affiliates and related entities, to receive reasonable compensation as a result of providing fiduciary investment advice. The exemption specifically covers compensation received as a result of investment advice to roll over assets from a Plan to an IRA. The exemption also provides relief for a Financial Institution to engage in the purchase or sale of an asset in a riskless principal transaction or a Covered Principal Transaction, and receive a mark-up, mark-down, or other payment. The exemption provides relief from ERISA section 406(a)(1)(A) and (D) and 406(b) and Code section 4975(c)(1)(A), (D),

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(E), and (F).<sup>82</sup>

Section I(b)(1) of the exemption provides broad relief for Financial Institutions and Investment Professionals that are investment advice fiduciaries to receive all types of compensation as a result of their investment advice to Retirement Investors, so long as the compensation is reasonable. For example, it covers compensation received as a result of investment advice to acquire, hold, dispose of, or exchange securities and other investments. It also covers compensation received as a result of investment advice to take a distribution from a Plan or to roll over the assets to an IRA, or from investment advice regarding other similar transactions including (but not limited to) rollovers from one Plan to another Plan, one IRA to another IRA, or from one type of account to another account (e.g., from a commission-based account to a fee-based account), all limited to the extent such rollovers are permitted under applicable law.

Section I(b)(2) addresses the circumstance in which the Financial Institution may, in addition to providing investment advice, engage in a purchase or sale of an investment with a Retirement Investor and receive a mark-up or a mark-down or similar payment on the transaction. The exemption extends to both riskless principal transactions and Covered Principal Transactions. A riskless principal transaction is a transaction in which

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<sup>82</sup> The exemption does not include relief from ERISA section 406(a)(1)(C) and Code section 4975(c)(1)(C) for the furnishing of goods, services, or facilities between a Plan/IRA and a party in interest/disqualified person. The statutory exemptions in ERISA section 408(b)(2) and Code section 4975(d)(2) provide this necessary relief for Plan or IRA service providers, subject to the applicable conditions and accompanying regulations.



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a Financial Institution, after having received an order from a Retirement Investor to buy or sell an investment product, purchases or sells the same investment product for the Financial Institution's own account to offset the contemporaneous transaction with the Retirement Investor. Covered Principal Transactions are defined in the exemption as principal transactions involving certain specified types of investments, discussed in more detail below. Principal transactions that are not riskless and that do not fall within the definition of Covered Principal Transaction are not covered by the exemption.

#### General comments on the covered transactions

Several commenters expressed concern about the scope of the exemption extending to the receipt of payments from third parties, such as 12b-1 fees and revenue sharing. One commenter also objected to relief for sales loads. The commenter opined that the market itself is moving away from these types of fees and expenses and numerous court decisions indicate that a Plan's payment of such fees may be a violation of the duty of prudence. Another commenter likened this type of payment as akin to doctors taking kickbacks from pharmaceutical companies. Another commenter stated that the exemption should not provide relief for principal transactions and proprietary products.

The Department believes that the flexibility provided under the exemption ensures that the various business models used by different Financial Institutions are accommodated under the exemption to ensure Retirement Investors have full access to their preferred advice provider and method of paying for advice. The conditions of the exemption are designed to ensure that Financial Institutions assess all sources of fees and

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revenue to identify and mitigate conflicts of interest that they create, and ultimately receive no more than reasonable compensation in connection with investment advice transactions. These conditions are designed to ensure that Financial Institutions and Investment Professionals act in the best interest of Retirement Investors, even if some sources of compensation come from 12b-1 fees, revenue sharing, sales loads, principal transactions, or proprietary products. The Department continues to believe that this principles-based approach provides flexibility to Financial Institutions while ensuring all advice is in the best interest of Retirement Investors, compensation is limited to reasonable compensation, and Investment Professionals do not subordinate the Retirement Investors' interest to their own.

Another commenter asked the Department to expand the scope of relief in the exemption to ERISA section 406(a)(1)(B) and Code section 4975(c)(1)(B) for extensions of credit, in order to cover items such as overdraft protection, receipt of float, error corrections, settlement accommodations, short sales and other margin transactions, and paying fees in advance.

The Department has not expanded the exemption as requested by the commenter. The commenter did not provide information on these transactions and how the exemption conditions would protect the interests of Retirement Investors engaging in the transactions. An existing exemption, PTE 75-1, Part V, provides relief for an extension of credit by a broker-dealer in connection with the purchase or sale of securities; however, the exemption does not extend to the receipt of compensation for the extension of credit if the broker-dealer renders fiduciary investment advice with respect to the

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transaction. This does not foreclose the Department, however, from considering expanding the relief in PTE 75-1, Part V, based upon a separate request for exemptive relief.

### ***Principal Transactions***

Principal transactions involve the purchase from, or sale to, a Plan or an IRA, of an investment, on behalf of the Financial Institution's own account or the account of a person directly or indirectly, through one or more intermediaries, controlling, controlled by, or under common control with the Financial Institution. Because an investment advice fiduciary engaging in a principal transaction is on both sides of the transaction, the firm has a clear and direct conflict of interest. In addition, the securities typically traded in principal transactions often lack pre-trade price transparency and Retirement Investors may, therefore, have difficulty in prospectively evaluating the fairness of a particular principal transaction. These investments also can be associated with low liquidity, low transparency, and the possible incentive to sell unwanted investments held by the Financial Institution.

Consistent with the Department's historical approach to prohibited transaction exemptions for fiduciaries, this exemption includes relief for principal transactions that is limited in scope and subject to additional conditions, as set forth in the definition of Covered Principal Transaction, described below. Importantly, certain transactions are not considered principal transactions for purposes of the exemption, and so can occur under the more general conditions. This includes the sale of an insurance or annuity contract, or a mutual fund transaction.

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Principal transactions that are “riskless principal transactions” are covered under the exemption as well, subject to the general conditions. A riskless principal transaction is a transaction in which a Financial Institution, after having received an order from a Retirement Investor to buy or sell an investment product, purchases or sells the same investment product in a contemporaneous transaction for the Financial Institution’s own account to offset the transaction with the Retirement Investor.

Limited Definition of “Covered Principal Transaction”

The exemption uses the defined term *Covered Principal Transaction* to describe the types of non-riskless principal transactions that are covered under the exemption. For *purchases* from a Plan or an IRA, the term is broadly defined to include any security or other investment property. This is to reflect the possibility that a principal transaction will be needed to provide liquidity to a Retirement Investor. However, for *sales* to a Plan or an IRA, the exemption provides more limited relief. For sales, the definition of Covered Principal Transaction is limited to transactions involving: U.S. dollar denominated corporate debt securities offered pursuant to a registration statement under the Securities Act of 1933, U.S. Treasury securities, debt securities issued or guaranteed by a U.S. federal government agency other than the U.S. Department of Treasury, debt securities issued or guaranteed by a government-sponsored enterprise (GSE), municipal securities, certificates of deposit, and interests in Unit Investment Trusts. In response to one commenter’s specific question as to whether the term “certificates of deposit” includes brokered certificates of deposit, the Department clarifies that the use of the term “certificates of deposit” includes brokered certificates of deposit that are sold in principal

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transactions.

With respect to the definition of Covered Principal Transaction, some commenters wrote that there should not be a limit on the types of investments that can be sold by Financial Institutions to Retirement Investors, including one commenter who stated that the Department should eliminate or adjust exemption conditions that would limit Retirement Investors' access to full service brokerage accounts, including access to principal markets. They argued that some products would generally only be available through a principal transaction, and that the Department should not substitute its judgment for a fiduciary acting in accordance with the Act's standards. Further, they stated that the existing limit is inconsistent with Regulation Best Interest which does not include any limitations on principal transactions, and that there were sufficient existing protections under securities laws. Commenters identified a variety of potential investments that they would like to see incorporated as Covered Principal Transactions, including foreign debt, structured notes, corporate debt in the secondary market, equity securities (including initial public offerings and national market system securities), new issues, issuers other than corporations, foreign currency, foreign securities, and closed end funds.

The Department has considered these comments but has not expanded the exemption's definition of a Covered Principal Transaction, including its enumerated list of investments. The definition of Covered Principal Transaction is intentionally narrow, based on the potentially acute conflicts of interest created by principal transactions. While commenters argued that the Department is substituting its own judgment for that

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of Financial Institutions and Investment Professionals, the Department believes that the risks created by principal transactions' unique conflicts are great enough to only justify allowing otherwise prohibited transactions if those transactions are set within prescribed conditions specifically designed to address those conflicts of interest. Further, because the exemption is addressing transactions prohibited solely under Title I and the Code, whether the definition of a Covered Principal Transaction is consistent with Regulation Best Interest, or subject to other securities law protections, is not determinative. The Department is required to make findings as to whether the exemption is in the interests of, and protective of the rights of, Plan participants and beneficiaries and IRA owners.<sup>83</sup> The Department stresses its obligation to exercise great care in authorizing transactions that Congress prohibited based upon their potential for abuse and resulting injury to Plan participants and IRA owners. Given the unique starting point—that Congress statutorily prohibited these transactions in Title I and the Code—the Department does not agree that the approach suggested by the commenters is appropriate. To the extent parties have interpretive questions regarding the scope of the exemption in this regard, the Department intends to support Financial Institutions, Investment Professionals, plan sponsors and fiduciaries, and other affected parties, with compliance assistance following publication of the final exemption.

The Department believes the best way to address commenters' concerns regarding

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<sup>83</sup> See ERISA section 408(a) and Code section 4975(c)(2).

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additional investments is to include the provision allowing the definition of Covered Principal Transaction to expand upon the Department's grant of an individual exemption covering a particular type of principal transaction. An individual exemption request would provide the Department with the opportunity to gain the additional information it would need to determine whether an investment should be included in this exemption. Further, individual exemptions are required to be published in the Federal Register and allow for public comment before they are finalized. These procedural requirements are protective of Retirement Investors.

One commenter disagreed with the addition of investments through the individual prohibited transaction exemption process. The commenter argued that the addition of investments should be accomplished through a formal amendment to the exemption. The Department believes that the procedural requirements described in the preceding paragraph provide protections to Retirement Investors, and the ability to incorporate additional investments by adopting an individual exemption provides an appropriately streamlined approach to address discrete areas of scope within the class exemption.

#### Credit Quality and Liquidity

For sales of a debt security to a Plan or an IRA, the definition of Covered Principal Transaction requires the Financial Institution to adopt written policies and procedures related to credit quality and liquidity. Specifically, the policies and procedures must be reasonably designed to ensure that the debt security, at the time of the recommendation, has no greater than moderate credit risk and has sufficient liquidity that it could be sold at or near its carrying value within a reasonably short period of time.

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This standard is included to prevent the exemption from being available to Financial Institutions that recommend speculative or illiquid debt securities from their own accounts.

A few commenters opposed the proposed condition requiring adoption of policies and procedures related to credit quality and liquidity. The commenters argued that this condition substitutes the Department's judgment for that of the Retirement Investor. Further, they stated that the standards would be difficult to apply, requiring firms to look into the future to know whether a bond would be actively traded. One commenter stated specifically that a liquidity condition should not be included.

The Department has considered these comments, but has included the credit quality and liquidity policies and procedures condition in the final exemption. Principal transactions are inherently conflicted transactions. As a result, the Department believes that unique conditions, such as the credit and liquidity requirements, address the heightened conflicts of interest and are specifically tailored to address conflicts inherent with respect to debt securities. The Department is not substituting its judgment for that of Retirement Investors; it is only setting necessary safeguards to prevent abuses by Financial Institutions relying on the exemption. Additionally, the Department notes that the exemption is not necessary for self-directed retirement accounts or transactions that do not involve fiduciary investment advice. Therefore, such truly self-directed accounts and transactions may involve the purchase of any type of investment on a principal basis.

Further, the Department does not believe the standards are unworkable. Financial Institutions regularly evaluate the credit risk associated with their investments and assess



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their liquidity. And it is important to note that the policies and procedures must be reasonably designed to ensure that the standards are met *at the time of the transaction*; the exemption does not require them to be satisfied for the duration of the investment. Indeed, a commenter who raised concerns about the requirement went on to point out ways a Financial Institution could reasonably consider the liquidity at the time of the transaction. This commenter stated that it is the very nature of bond trading that liquidity generally tends to diminish as bonds mature. The Department expects that a Financial Institution would consider this and other reasonably available information at the time of the transaction in designing its policies and procedures. It is also important to note that Financial Institutions may consider credit ratings as a part of a Financial Institution's policies and procedures in this respect.

#### Municipal Bonds

The exemption covers principal transactions involving municipal bonds, including tax-exempt municipal bonds. The Department cautions, however, that Financial Institutions and Investment Professionals should pay special care when recommending that Retirement Investors invest in municipal bonds. Tax-exempt municipal bonds are typically a poor choice for investors in Title I Plans and IRAs because the Plans and IRAs are already tax-advantaged and, therefore, do not benefit from paying for the bond's tax-

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avored status.<sup>84</sup>

One commenter stated that no tax-exempt investment (including tax-exempt municipal bonds and certain annuities) should be included in the exemption, absent evidence that such investments are beneficial when purchased through a retirement account. The Department believes, however, that there are certain limited circumstances where these investments may benefit a Retirement Investor. For example, a particular municipal bond may have a higher tax-equivalent yield than a comparable taxable bond. Alternatively, a fiduciary adviser may conclude based upon careful analysis that a particular tax-exempt municipal bond carries less risk than a comparable corporate bond. Accordingly, the Department has not written the exemption to flatly exclude tax-exempt investments. However, given the increased risk of imprudence when making such recommendations, Financial Institutions and Investment Professionals may wish to document the reasons for any recommendation of a tax-exempt municipal bond or other tax-exempt investment and why the recommendation is in the Retirement Investor's best interest.

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<sup>84</sup> See e.g., Seven Questions to Ask When Investing in Municipal Bonds, *available at* [www.msrb.org/~media/pdfs/msrb1/pdfs/seven-questions-when-investing.ashx](http://www.msrb.org/~media/pdfs/msrb1/pdfs/seven-questions-when-investing.ashx). (“[T]ax-exempt bonds may not be an efficient investment for certain tax advantaged accounts, such as an IRA or 401k, as the tax-advantages of such accounts render the tax-exempt features of municipal bonds redundant. Furthermore, since withdrawals from most of those accounts are subject to tax, placing a tax exempt bond in such an account has the effect of converting tax-exempt income into taxable income. Finally, if an investor purchases bonds in the secondary market at a discount, part of the gain received upon sale may be subject to regular income tax rates rather than capital gains rates.”)

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### Separate Exemption

One commenter asserted that principal transaction relief should be provided through a separate exemption. The commenter argued that the exemption's conditions are not sufficiently protective with respect to the unique nature of principal transactions. Instead, the commenter advocated for a separate prohibited transaction class exemption modeled after the statutory exemption for cross-trading in ERISA section 408(b)(19) and Code section 4975(d)(22). Using the statutory exemption as a model, the commenter suggested that the exemption include conditions such as minimum size requirements and a requirement that the transaction occur at the "independent current market price."

The Department has considered this suggestion, but has not adopted it. Although the Department agrees that the conflicts of interest in cross-trades are significant, the transactions contemplated by the statutory exemptions for cross-trades are not, in the Department's view, necessarily so analogous to the principal transactions covered by this exemption that the conditions of the statutory exemption are easily applied in this context. The statutory exemption is aimed at discretionary investment managers that are managing large accounts, while this exemption is designed to include investment advice providers who may be providing advice in the retail market. It would be difficult, for example, for the Department to arrive at a minimum size that would be appropriate for engaging in principal transactions with retail investors. The Department also believes that combining relief for principal transactions within the exemption for other transactions arising out of the provision of fiduciary investment advice assists Financial Institutions and Investment Professionals in developing a comprehensive compliance

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approach.

### ***Exclusions***

Section I(c) provides that certain specific transactions are excluded from the exemption. The exemption retains the exclusions as proposed. Therefore, the exemption is not available for Title I Plans if the Investment Professional, Financial Institution, or an affiliate is (1) the employer of employees covered by the Plan; or (2) a named fiduciary or plan administrator, or an affiliate, who was selected to provide advice to the Plan by a fiduciary who is not independent. The exemption excludes investment advice generated solely by an interactive web site in which computer software-based models or applications provide investment advice based on personal information each investor supplies through the website, without any personal interaction or advice with an Investment Professional (i.e., robo-advice). The exemption is also specifically limited to investment advice fiduciaries within the meaning of the five-part test and does not include discretionary arrangements.

#### Employers, Named Fiduciaries, and Plan Administrators

Section I(c)(1) of the exemption provides that the exemption does not extend to transactions involving Title I Plans if the Investment Professional, Financial Institution, or an affiliate is either (1) the employer of employees covered by the Plan; or (2) 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.

The Department believes that employers generally should not be in a position to

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use their employees' retirement benefits as potential revenue or profit sources, without additional safeguards. Employers can always render advice and recover their direct expenses in transactions involving their employees without need of this exemption.<sup>85</sup>

Further, the Department does not intend for the exemption to be used by a Financial Institution or Investment Professional that is the named fiduciary or plan administrator of a Title I Plan or an affiliate thereof, unless the Financial Institution or Investment Professional is selected as an advice provider by a fiduciary (such as the employer sponsoring the Title I Plan) that is independent of them. Named fiduciaries and plan administrators have significant authority over plan operations and accordingly, the Department believes that any selection of these parties to also provide investment advice to the Title I Plan or its participants and beneficiaries should be made by an independent party who will also monitor the performance of the investment advice services.

For purposes of the exemption, the plan sponsor or other fiduciary is independent of the Financial Institution and Investment Professional if: (1) the fiduciary is not the Financial Institution, Investment Professional, or an affiliate; (2) the fiduciary does not have a relationship to or an interest in the Financial Institution, Investment Professional, or any affiliate that might affect the exercise of the fiduciary's best judgment in connection with transactions covered by the exemption; and (3) the fiduciary does not

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<sup>85</sup> A few existing prohibited transaction exemptions apply to employers. *See* ERISA section 408(b)(5), a statutory exemption that provides relief for the purchase of life insurance, health insurance, or annuities, from an employer with respect to a Plan or a wholly owned subsidiary of the employer.

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receive and is not projected to receive within the current federal income tax year, compensation or other consideration for his or her own account from the Financial Institution, Investment Professional, or an affiliate, in excess of 2% of the fiduciary's annual revenues based upon its prior income tax year.

Some commenters urged the Department to delete the exclusion of employers as fiduciary investment advice providers to Title I Plans covering their own employees. The commenters stated that the conditions of the exemption are protective for transactions involving employees of the Financial Institution, and there is no reason to prevent employees from choosing their own advice provider and benefiting from their employer's particular area of expertise. A different commenter raised the concern that employees would lose access to a valuable service their employer provides to others. In response, the Department notes that employers will continue to be able to provide such services to employees, just as they always have, if they recoup only their direct expenses. The Department has decided to maintain the exclusion as it was proposed, because of the Department's concerns that the danger of abuse is compounded when the advice recipient receives recommendations from the employer, upon whom he or she depends for a job, to make investments in which the employer has a financial interest.

Several commenters addressed the exclusion of named fiduciaries and plan administrators, unless selected by a fiduciary that is independent of them. One commenter sought clarification with respect to a particular factual scenario in which a plan sponsor appoints a bank as a directed trustee and named fiduciary. The commenter asked whether the exemption would require the bank to be selected to provide advice to

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the Title I Plan by the employer, and contended that this would result in disparate treatment as compared to other fiduciary service providers. For example, the commenter stated that the Title I Plan's investment adviser can solicit rollovers without selection by the employer.

The Department responds that the exemption would require a bank that is a named fiduciary to be selected by a fiduciary that is independent of the bank, as defined in the exemption. As noted above, this exclusion is based on the significant authority of named fiduciaries and plan administrators over Title I Plan operations.

Some commenters focused on the "independence" requirement under which the fiduciary selecting the advice provider cannot receive more than 2% of its income in the current tax year from the Financial Institution, Investment Professional, or an affiliate. The commenters urged the Department to increase the 2% limit to as high as 20%. One commenter stated this definition was far more restrictive than any definition ever used by the Department. The Department disagrees that the 2% limitation is unduly restrictive, and notes that the Department's exemption procedure regulation provides for a presumption that a 2% limitation will indicate that a fiduciary is independent.<sup>86</sup> The Department did not increase the 2% limit so as to avoid any concern that compensation may impact the fiduciary's selection of an advice provider for the Title I Plan.

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<sup>86</sup> 29 CFR 2570.31(j) (definition of "qualified independent fiduciary").

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### Pooled Employer Plans under the SECURE Act

In connection with the exemption's exclusion of named fiduciaries and plan administrators unless selected by a fiduciary that is independent, several commenters requested additional guidance and clarification regarding the exemption's application to Pooled Employer Plans (PEPs), which were authorized by the SECURE Act, passed in 2019.<sup>87</sup> The SECURE Act mandates that a PEP must be established by a Pooled Plan Provider (PPP) that is designated as a named fiduciary, plan administrator, and the person responsible for specified administrative duties. Commenters envisioned that some PPPs would want to make investment advice available through PEPs, by utilizing themselves or an affiliate as the advice provider. Commenters requested clarification that an employer that participates in a PEP could be considered "independent" so that this exclusion would not be applicable despite the fact that the PPP or an affiliate is providing advice.

The Department believes it is premature to address issues related to PEPs, given their recent origination, unique structure, and likelihood of significant variations in fact patterns and potential business models, as the PEPs' sponsors decide how to structure their operations. In particular, the Department believes it is premature to provide any

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<sup>87</sup> PEPs may not begin operating until January 1, 2021.



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views regarding the “independence” of participating employers. The Department recently published a request for information on prohibited transactions applicable to PEPs and is separately considering exemptions related to these types of Plans.<sup>88</sup>

### Robo-Advice

Section I(c)(2) of the exemption excludes from relief transactions that result from investment advice generated solely by an interactive website in which computer software-based models or applications provide investment advice that do not involve interaction with an Investment Professional (referred to herein as “pure robo-advice”). “Hybrid” robo-advice arrangements, which involve both computer software models and personal investment advice from an Investment Professional, are permitted under the exemption.

A detailed statutory exemption that specifically addresses computer model advice is set forth in ERISA section 408(b)(14), (g), and Code section 4975(d)(17) and 4975(f)(8), and the regulations thereunder.<sup>89</sup> The statutory exemption includes specific conditions governing the operation of the computer model, including a requirement that the model apply generally accepted investment theories and that it operate in an unbiased manner, and the exemption further requires that an expert certify that the computer model meets certain of the exemption’s requirements.

A number of commenters objected to the exclusion of pure robo-advice from the

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<sup>88</sup> 85 FR 36880 (June 18, 2020).

<sup>89</sup> 29 CFR 2550.408g-1.

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class exemption, arguing that there is no reason to treat it differently from other types of advice that are covered in the exemption. Commenters described robo-advice as providing a low-cost option that might become less available if it is not included in the exemption. Commenters indicated that covering pure robo-advice would allow Financial Institutions to adopt a single set of policies and procedures for all advice arrangements, and noted that the SEC does not treat robo-advice differently than other forms of advice. Some argued that the existence of a statutory exemption should not prevent the Department from issuing an administrative exemption, and that there are other examples in which multiple exemptions are available for a certain transaction. Some commenters argued that the statutory exemption is costly and cumbersome, and expressed concern about whether it extended to rollovers, even though the exemption does not, by its terms, exclude rollovers.

The final exemption maintains the exclusion of pure robo-advice. As noted above, the statutory exemption in ERISA section 408(b)(14), (g), and Code section 4975(d)(17) and 4975(f)(8), includes specific conditions that are tailored to computer-generated investment advice. This exemption, by contrast, is tailored to investment advice that is provided through a human Investment Professional who is supervised by a Financial Institution. The conditions of this exemption are not designed to address advice without an Investment Professional. Because of the different approaches, the Department does not believe that Financial Institutions would easily be able to develop a single set of conflict mitigation policies under this exemption that would govern both hybrid and pure robo-advice arrangements. The policies and procedures required by this exemption

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contemplate consideration of factors beyond those that may be considered in a pure robo-advice situation. A person may design a pure robo-advice model that incorporates other incentives than those addressed here. Further, without specificity as to how Financial Institutions' policies and procedures would address pure robo-advice in a way that improved upon the existing exemption, the Department is not persuaded that extending this exemption to cover pure robo-advice is in the interests of Retirement Investors and is protective of their rights, as it must find under ERISA section 408(a)(2) and (3) and Code section 4975(c)(2)(B) and (C) before issuing a new exemption. For these reasons, the Department has decided to retain the exclusion from the exemption, as proposed.

With regard to hybrid robo-advice arrangements that are covered by the exemption, one commenter suggested that the final exemption should require an Investment Professional who uses a computer model and deviates from its recommendation to provide the Retirement Investor with a written explanation of the reasons for the deviation. However, the Department has determined generally to avoid such a prescriptive approach to disclosure in the final exemption. Without additional information about the commenter's concerns related to Investment Professionals deviating from computer generated recommendations, the Department does not believe that a specific disclosure requirement is necessary in such circumstances.

#### Discretionary Arrangements

Under Section I(c)(3), the exemption does not extend to transactions in which the Investment Professional is acting in a fiduciary capacity other than as an investment advice fiduciary. For clarity, Section I(c)(3) specifically cites the Department's five-part

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test as the governing authority for status as an investment advice fiduciary.

Several commenters opposed this exclusion and stated that the conditions of the exemption are sufficiently protective in the context of discretionary arrangements. These commenters indicated that Retirement Investors who want discretionary management services should not be treated differently than those receiving non-discretionary advice services.

After consideration of the comments, the Department is adopting this exclusion as proposed. The protections that are included in the exemption were designed specifically for non-discretionary investment advice arrangements, consistent with standards from other regulators regarding similar arrangements. The Department does not believe this will unfairly prejudice discretionary arrangements because the same pool of exemptions for discretionary arrangements currently exists that existed before this exemption was proposed. Additionally, the Department understands there are a variety of ways to avoid prohibited transactions in discretionary arrangements, including utilizing fee structures that ensure compensation does not vary based on investment choice.

Moreover, the Department believes the differences between a discretionary and non-discretionary arrangement are not insignificant. For example, the potential for conflicts in a discretionary arrangement is heightened because most, if not all, of the investment transactions will occur without interaction with the Retirement Investor. The Department does not believe that the conditions of this exemption are appropriately tailored to address such conflicts. However, the Department remains open to requests for additional prohibited transaction relief for discretionary arrangements.

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### ***Exemption Conditions***

Section II of the exemption sets forth the general conditions of the exemption. Section III establishes the eligibility requirements. Section IV requires parties to maintain records to demonstrate compliance with the exemption. Section V includes the defined terms used in the exemption. These sections are discussed below. In order to obtain prohibited transaction relief under the exemption, the Financial Institution and Investment Professional must comply with all of the conditions of the exemption, and may not waive or disclaim compliance with any of the conditions. Similarly, a Retirement Investor may not agree to waive any of the conditions.

### ***Investment Advice Arrangement – Section II***

Section II sets forth conditions that govern the Financial Institution's and Investment Professional's investment advice arrangement. As discussed in greater detail below, Section II(a) requires Financial Institutions and Investment Professionals to comply with the Impartial Conduct Standards by providing advice that is in Retirement Investors' best interest, charging only reasonable compensation, and making no materially misleading statements about the investment transaction and other relevant matters. The Impartial Conduct Standards further require the Financial Institution and Investment Professional to seek to obtain the best execution of the investment transaction reasonably available under the circumstances, as required by the federal securities laws. Section II(b) requires Financial Institutions, prior to engaging in a transaction pursuant to the exemption, to provide a written disclosure to the Retirement Investor acknowledging that the Financial Institution and its Investment Professionals are fiduciaries under Title I

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and the Code, as applicable.<sup>90</sup> The disclosure must also include a written description, accurate in all material respects, regarding the services to be provided and the Financial Institution's and Investment Professional's material conflicts of interest. Financial Institutions and Investment Professionals would also be required to document and disclose the reasons that a recommendation to roll over assets is in the Retirement Investor's best interest. Under Section II(c), the Financial Institution is required to establish, maintain, and enforce written policies and procedures prudently designed to ensure that the Financial Institution and its Investment Professionals comply with the Impartial Conduct Standards. Section II(d) requires Financial Institutions to conduct an annual retrospective review.<sup>91</sup> Finally, Section II(e) provides a mechanism for Financial Institutions to correct certain violations of the exemption conditions and maintain relief under the exemption.

#### ***Impartial Conduct Standards – Section II(a)***

Financial Institutions and Investment Professionals must comply with the Impartial Conduct Standards by providing advice that is in Retirement Investors' best

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<sup>90</sup> As noted above, the Department does not intend the exemption to expand Retirement Investors' ability, such as by requiring contracts and/or warranty provisions, to enforce their rights in court or create any new legal claims above and beyond those expressly authorized in the Act, and the Department does not believe the exemption would create any such expansion.

<sup>91</sup> One commenter suggested that the exemption should be separated into different exemptions with different conditions to reflect diverse issues of Retirement Investors who are individuals, small plans, and large plans. The Department has not adopted that suggestion because of the concern that this would be overly complex for Financial Institutions to implement and could lead to concerns about technical violations of the exemptions.

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interest, charging only reasonable compensation, and making no materially misleading statements about the investment transaction and other relevant matters.

#### Best Interest Standard

Section II(a)(1) requires investment advice that is, at the time it is provided, in the best interest of the Retirement Investor. Section V(b) of the exemption defines “best interest” advice as advice that “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 interest 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.”

This standard is based on longstanding concepts in the Act and the high fiduciary standards developed under the common law of trusts, and is intended to comprise objective standards of care and undivided loyalty, consistent with the requirements of ERISA section 404. These longstanding concepts of law and equity were developed in significant part to deal with the issues that arise when agents and persons in a position of trust have conflicting interests, and accordingly are well-suited to the problems posed by conflicted investment advice.

The best interest standard is an objective standard that requires the Financial Institution and Investment Professional to investigate and evaluate investments, provide

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advice, and exercise sound judgment in the same way that knowledgeable and impartial professionals would. The standard of care is measured at the time the advice is provided, and not in hindsight.<sup>92</sup> The standard does not measure compliance by reference to how investments subsequently performed or turn Financial Institutions and Investment Professionals into guarantors of investment performance; rather, the appropriate measure is whether the Investment Professional gave advice that was prudent and in the best interest of the Retirement Investor at the time the advice is provided.

The standard also provides that Financial Institutions and Investment Professionals have a duty to “not place the financial or other interest 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 Department intends for the standard to be interpreted and applied consistently with the standard set forth in Regulation Best Interest<sup>93</sup> and the SEC’s interpretation regarding the conduct standard for investment advisers.<sup>94</sup>

This best interest standard allows Investment Professionals and Financial

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<sup>92</sup> See *Donovan v. Mazzola*, 716 F.2d 1226, 1232 (9th Cir. 1983).

<sup>93</sup> Regulation Best Interests’ best interest obligation provides that a “broker, dealer, or a natural person who is an associated person of a broker or dealer, when making a recommendation of any securities transaction or investment strategy involving securities (including account recommendations) to a retail customer, shall act in the best interest of the retail customer at the time the recommendation is made, without placing the financial or other interest of the broker, dealer, or natural person who is an associated person of a broker or dealer making the recommendation ahead of the interest of the retail customer.” 17 CFR 240.151-1(a)(1).

<sup>94</sup> See SEC Fiduciary Interpretation, 84 FR at 33671 (“An investment adviser’s fiduciary duty under the Advisers Act comprises a duty of care and a duty of loyalty. This fiduciary duty requires an adviser ‘to adopt the principal’s goals, objectives, or ends.’ This means the adviser must, at all times, serve the best interest of its client and not subordinate its client’s interest to its own. In other words, the investment adviser cannot place its own interests ahead of the interests of its client.”) (internal citations omitted).



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Institutions to provide investment advice despite having a financial or other interest in the transaction, so long as they do not place their own interests ahead of the interests of the Retirement Investor, or subordinate the Retirement Investor's interests to their own. For example, in choosing between two investments equally available to the investor, it is not permissible for the Investment Professional to advise investing in the one that is worse for the Retirement Investor because it is better for the Investment Professional's or the Financial Institution's bottom line. Because the standard does not forbid the Financial Institution or Investment Professional from having an interest in the transaction, this standard does not foreclose the Investment Professional and Financial Institution from being paid, nor does it foreclose investment advice on proprietary products or investments that generate third party payments. This best interest standard also does not impose an unattainable obligation on Investment Professionals and Financial Institutions to somehow identify the single "best" investment for the Retirement Investor out of all the investments in the national or international marketplace, assuming such advice were even possible at the time of the transaction.

Several commenters expressed support for the best interest standard and specifically for the phrasing aligned with Regulation Best Interest's conduct standard. Commenters articulated benefits to both Retirement Investors and to Financial Institutions that will come from clarity and consistency of alignment with the SEC. Some commenters requested that the Department specifically provide a safe harbor based on compliance with the SEC's requirements. According to these commenters, the

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Department should not merely rely on the phrasing in the securities regulations, but should also incorporate the securities laws enforcement through the SEC and FINRA.

Some commenters objected to the incorporation of the best interest standard and other Impartial Conduct Standards as conditions of the exemption. They stated that the conduct standards are duplicative for transactions involving Title I Plans because of the standards set forth in ERISA section 404. Some specifically opposed the Department's use of a prudence standard in the best interest standard. They noted that the specific word "prudence" is not included in the final Regulation Best Interest or in the NAIC Model Regulation, and, therefore, including it in the exemption standard would be an area of inconsistency. In addition, some commenters opined that the application of the best interest standard, including the prudence obligations, on IRAs is not permitted under the Fifth Circuit's *Chamber* opinion. In particular, these commenters opined that the Fifth Circuit determined that the Department was acting outside its authority by adding to the requirements of the Code provisions that Congress chose not to apply to such accounts.

Other commenters maintained that the Department's proposed best interest standard was not sufficiently protective of Retirement Investors. Commenters noted that the SEC described its standard as "separate and distinct from the fiduciary duty that has developed under the Advisers Act." These commenters argued that the Department should condition the exemption on what they referred to as a "true" fiduciary standard. They stated this is what Congress intended as part of the statutory framework for tax-advantaged treatment accorded to retirement investments. Some commenters specifically

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objected to the exemption’s loyalty formulation, including that it was not a true loyalty standard and needed alternative wording such as “without regard to” or “solely in the interest of.”

The Department has included the best interest standard in the final exemption as it was proposed. The Department believes that the standard, in combination with the other conditions of the exemption, will protect the interests of Retirement Investors affected by the exemption. Although the standards of ERISA section 404 already apply to transactions involving Title I Plans and their participants and beneficiaries, incorporating the Impartial Conduct Standards as conditions of the exemption requires Financial Institutions to demonstrate compliance with the standards and increases the consequence of non-compliance because of the excise tax. This creates an important incentive for Financial Institutions to ensure compliance with the standards. For that reason, the Department does not believe the standards are unnecessary or duplicative for those Retirement Investors who are Title I Plan participants or beneficiaries. The Department also is not persuaded that it should eliminate the reference to “prudence” from the best interest standard, given its importance in the Title I framework and longstanding application to the problems of agency that the exemption addresses.

The Department does not believe that including the Impartial Conduct Standards as conditions for transactions involving IRAs is impermissible in light of the Fifth Circuit’s *Chamber* opinion. The Fifth Circuit’s opinion addressed the 2016 fiduciary rule and related exemptions, particularly the perceived “over-inclusiveness” of the new definition of a fiduciary that the opinion indicated, in some circumstances, resulted in

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ordinary sales conduct activities causing a person to be classified as a fiduciary under Title I and the Code. Unlike the 2016 fiduciary rule and related exemptions, the present exemption provides relief to a more limited group of persons already deemed to be fiduciaries within the meaning of the five-part test and does not impose contract or warranty requirements on fiduciaries.<sup>95</sup> Further, the Fifth Circuit observed that the five-part test “captured the essence of a fiduciary relationship known to the common law as a special relationship of trust and confidence between the fiduciary and his client.” *Chamber*, 885 F.3d 360, 364 (2018) (citation omitted). The same five-part test exists under the Code’s regulations, based on an identical definition of *fiduciary* in the Code. This exemption merely recognizes that fiduciaries of IRAs, if they seek to use this exemption for relief from prohibited transactions, should adhere to a best interest standard consistent with their fiduciary status and a special relationship of trust and confidence.

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<sup>95</sup> In connection with the description of the best interest standard in the proposed exemption the Department included a footnote referencing Code section 4975(f)(5), which defines “correction” with respect to prohibited transactions as placing a Plan or an IRA in a financial position not worse than it would have been in if the person had acted “under the highest fiduciary standards.” The footnote stated that while the Code does not expressly impose a duty of loyalty on fiduciaries, the exemption’s best interest standard is intended to ensure adherence to the “highest fiduciary standards” when a fiduciary advises a Plan or an IRA owner under the Code. Commenters asked the Department to disavow this statement in the final exemption, asserting that the imposition of the Impartial Conduct Standards as an exemption condition for IRAs was rejected by the Fifth Circuit’s *Chamber* opinion. The Department disagrees with the commenters’ interpretation of the Fifth Circuit’s opinion, and its application to this exemption which applies only to plan fiduciaries who meet the five-part test and which does not impose contract or warranty requirements on these fiduciaries.

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The Department also disagrees with the suggestion that the best interest standard is not a “true” fiduciary standard. The Department acknowledges that the Best Interest Contract Exemption and other exemptions granted in association with the 2016 fiduciary rule used a loyalty formulation of “without regard to,” which was described as “a concise expression of Title I’s duty of loyalty, as expressed in section 404(a)(1)(A) of ERISA and applied in the context of advice.”<sup>96</sup> In connection with concerns expressed by commenters on those exemptions, however, the Department had to provide specific confirmation that the standard was not so exacting as to prevent a fiduciary from being paid.<sup>97</sup> The Department also provided a special definition of “best interest” in section IV of the exemption to accommodate concerns about proprietary products and limited menus of investment options that generate third party payments.<sup>98</sup> It is important to note that for decades the Department has also articulated the duty of loyalty in ERISA section 404 as prohibiting a fiduciary from “subordinating the interests of participants and beneficiaries in their retirement income to unrelated objectives.”<sup>99</sup>

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<sup>96</sup> See Best Interest Contract Exemption, 81 FR 21002, 21026 (April 8, 2016).

<sup>97</sup> *Id.* at 21029.

<sup>98</sup> *Id.* at 21080.

<sup>99</sup> See e.g., Advisory Opinion 2008-05A (June 27, 2008); Advisory Opinion No. 93-33A (Dec. 16, 1993); Advisory Opinion 85-36A (Oct. 23, 1985); Letter to James K. Tam (June 14, 1983); Letter to Harold G. Korbee (Apr. 22, 1981). The Department has also repeated this articulation of the loyalty standard in recent proposed and final regulations. See Financial Factors in Selecting Plan Investments final rule, 85 FR 72846, 72847 (Nov. 13, 2020) (In describing prior guidance on environmental, social, and corporate governance investing, noting that the Department “has construed the requirements that a fiduciary act

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As set forth above, however, the Department notes that the exemption’s best interest standard requires Financial Institutions and Investment Professionals to 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 duty not to subordinate the Retirement Investor's interests to their own is the standard applicable to investment advisers, who are fiduciaries under securities laws.<sup>100</sup> Although the SEC indicated in Regulation Best Interest that it was not subjecting broker-dealers to “a wholesale and complete application of the existing fiduciary standard under the Advisers Act,” it also said, “[a]t the time a recommendation is made, key elements of the Regulation Best Interest standard of conduct that applies to broker-dealers will be similar to key elements of the fiduciary standard for investment advisers.”<sup>101</sup>

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solely in the interest of, and for the exclusive purpose of providing benefits to, participants and beneficiaries as prohibiting a fiduciary from subordinating the interests of participants and beneficiaries in their retirement income to unrelated objectives.”). *See also* Fiduciary Duties Regarding Proxy Voting and Shareholder Rights proposed rule, 85 FR 55219, 52220-21 (September 4, 2020) (In discussing prior interpretations of proxy voting, noting that in 1994 “the Department also reiterated its view that ERISA does not permit fiduciaries, in voting proxies or exercising other shareholder rights, to subordinate the economic interests of participants and beneficiaries to unrelated objectives.”).

<sup>100</sup> SEC Fiduciary Interpretation, 84 FR at 33671.

<sup>101</sup> Regulation Best Interest Release, 84 FR at 33321-33322. The SEC stated that the phrasing in Regulation Best Interest (“without placing the financial or other interest . . . ahead of the interest of the retail customer”) aligns with an investment adviser’s fiduciary duty, noting the discussion in the SEC Fiduciary Interpretation (“This means the adviser must, at all times, serve the best interest of its client and not subordinate its client’s interest to its own. In other words, the investment adviser cannot place its own interests ahead of the interests of its client.”) 84 FR at 33671.

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Although the best interest standard is intended to be consistent with the securities law standards as discussed above, the Department declines to provide a safe harbor for compliance with the standards as interpreted by the SEC or FINRA. The Department confirms that it will coordinate with other regulators, including the SEC, on enforcement strategies and interpretive issues to the extent appropriate, but it cannot simply defer to other regulators on how best to discharge its own interpretive and enforcement responsibilities under Title I and the Code.<sup>102</sup> When Congress enacted the Act, it made a deliberate decision to entrust the protection of Retirement Investors to the Secretary of Labor, subject to an overarching regulatory structure that departs in significant ways from the securities laws (e.g., by creating a prohibited transaction structure that flatly prohibits many transactions, such as those at issue in this exemption, unless the Department first grants an exemption after making statutorily required participant-protective findings). While the Department has exercised its discretion in this exemption to incorporate a best interest standard that it believes is consistent with the securities law standard, it nevertheless retains full interpretive responsibility over, and must account for, the Title I and Code provisions at issue in this exemption, as well as the terms of the exemption, and for the protection of Retirement Investors.

#### Additional Guidance on the Best Interest Standard

A few commenters requested additional guidance on the best interest standard.

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<sup>102</sup> See, e.g., ERISA sections 502, 504, 505, and Reorganization Plan No. 4 of 1978.

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One commenter asked the Department to clarify how Title I's standards differed from the Impartial Conduct Standards. Another commenter asked the Department to make clear what an Investment Professional would be required to do to satisfy the standards, other than engaging in a prudent process. In this regard, the Department notes that the exemption is applicable solely to ERISA section 406 and Code section 4975; it does not provide an exemption from a Title I fiduciary's obligations under ERISA section 404.

As set forth above, the Department does not believe there is a distinction between ERISA's section 404 standards of prudence and loyalty and the Impartial Conduct Standards, given that the best interest standard includes a prudence obligation and the Department has in the past described the duty of loyalty as prohibiting fiduciaries from subordinating the interests of participants and beneficiaries in their retirement income to unrelated objectives

Financial Institutions wishing to be certain that they complied with the ERISA section 404 standard and the Impartial Conduct Standards would adopt rigorous policies and procedures to align the interests of Investment Professionals with their Retirement Investor customers, refrain from creating incentives for Investment Professionals to violate the Impartial Conduct Standards, and prudently oversee the implementation and enforcement of the policies and procedures. Investment Professionals would comply with the Financial Institution's policies and procedures, engage in a prudent process in recommending investment products, and ensure that their advice does not put the interests of the Investment Professional, Financial Institution, or other party ahead of the



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interests of the Retirement Investor.<sup>103</sup>

One commenter asked the Department to clarify the remedies available to a participant under Title I who receives fiduciary investment advice to roll over assets from a Title I Plan to an IRA. Specifically, the commenter sought confirmation that whenever a participant is the recipient of advice, the participant retains all of the rights and remedies under Title I even if the investment advice provider is selected by the participant's employer. The Department responds that individual participants and beneficiaries in a Title I Plan have a cause of action under ERISA section 502(a) for prohibited transactions, even if the investment advice provider is selected by the employer. As noted earlier, the Act does not permit exemptions to release fiduciaries from their Title I obligations under ERISA section 404 to a Plan, and its remedies remain available.

### *Monitoring*

In connection with the best interest standard, several commenters raised concerns that the conditions of the exemption could require Financial Institutions to provide ongoing monitoring services of certain investment property. The Department stated in the preamble to the proposed exemption that:

Financial Institutions should carefully consider whether certain investments can be prudently recommended to the individual Retirement

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<sup>103</sup> One commenter asked the Department to explain the difference between the exemption's best interest standard and a suitability standard. Given the recent developments in conduct standards applicable to broker-dealers and insurance agents, the Department does not believe it is appropriate or necessary for it to address these differences.

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Investor in the first place without ongoing monitoring of the investment. Investments that possess unusual complexity and risk, for example, may require ongoing monitoring to protect the investor's interests.

Some commenters interpreted this statement to require Financial Institutions and Investment Professionals to monitor certain investments. According to the commenters, any obligation for broker-dealers to monitor investments would be inconsistent with the securities laws. Another commenter stated that the monitoring requirement is inconsistent with the prudence standards because the Department's regulation at 29 CFR 2550.404a-1 regarding a fiduciary's duty of prudence in connection with investment decisions does not require account monitoring. Commenters asked the Department to confirm that the exemption does not require Financial Institutions or Investment Professionals to provide monitoring, particularly where the Financial Institution clearly discloses it will not do so. Commenters also stated the Department should not impose ongoing monitoring requirements based on a vague standard of "unusual complexity and risk."

Other commenters asked for more guidance on when monitoring would be required. They requested more specificity on which investments are considered complex and risky as described in the preamble of the proposed exemption. Some commenters sought the Department's assurance that annuities would not require ongoing monitoring. However, one commenter asserted that the Department's statement on monitoring did not go far enough; an ongoing fiduciary relationship should require ongoing monitoring. At the very least, this commenter noted, the Department should adopt the position that the SEC takes with regard to investment advisers' monitoring obligations, that for advice that

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is provided on a regular basis, there should be some duty to monitor consistent with the nature of that relationship.

As was stated in the proposal, the Department confirms that nothing in the final exemption requires Financial Institutions or Investment Professionals to provide ongoing monitoring services. Of course, the exemption's general prohibition against misleading statements applies, and Financial Institutions and Investment Professionals should be clear and candid with Retirement Investors about the existence, scope, and duration of any monitoring services. Accordingly, the Department does not believe it is requiring broker-dealers to engage in any activity that is not permitted under securities laws or that it is barring broker-dealers from recommending certain classes of investments. The Department did not require all Financial Institutions and Investment Professionals to offer monitoring because the exemption takes the approach of preserving the availability of a wide variety of investment advice arrangements and products. However, as part of making a best interest recommendation, the Department expects that Financial Institutions and Investment Professionals will consider whether the investment can be prudently recommended without some mechanism or plan for ongoing monitoring. To the extent that prudence requires ongoing monitoring, the final exemption does not require that such monitoring be done by the Financial Institution or Investment Professional; such monitoring could be performed by a third party, but the advice fiduciary should clearly explain the need for monitoring to the investor when making the recommendation.

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In response to requests for guidance identifying specific products that will require monitoring, or what constitutes a product of unusual complexity and risk, the Department notes that Financial Institutions and Investment Professionals will need to make these decisions on a case-by-case basis. The Department expects that Financial Institutions and Investment Professionals have the expertise necessary to evaluate the need for monitoring based on all the facts and circumstances.

#### Reasonable Compensation

Section II(a)(2) of the exemption includes a reasonable compensation standard. The exemption provides that compensation received, directly or indirectly, by the Financial Institution, Investment Professional, and their affiliates and related entities for their services is not permitted to exceed reasonable compensation within the meaning of ERISA section 408(b)(2) and Code section 4975(d)(2).

The obligation to pay no more than reasonable compensation to service providers has been long recognized under Title I and the Code. The statutory exemptions in ERISA section 408(b)(2) and Code section 4975(d)(2) expressly require all types of services arrangements involving Plans and IRAs to result in no more than reasonable compensation to the service provider. Investment Professionals and Financial Institutions—when acting as service providers to Plans or IRAs—have long been subject to this requirement, regardless of their fiduciary status.

The reasonable compensation standard requires that compensation not be excessive, as measured by the market value of the particular services, rights, and benefits the Investment Professional and Financial Institution are delivering to the Retirement

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Investor. Given the conflicts of interest associated with the commissions and other payments that would be covered by the exemption, and the potential for self-dealing, it is particularly important that Investment Professionals and Financial Institutions adhere to these statutory standards, which are rooted in common law principles.

The reasonable compensation standard applies to all transactions under the exemption, including investment products that bundle services and investment guarantees or other benefits, such as with annuities. In assessing the reasonableness of compensation in connection with these products, it is appropriate to consider the value of the guarantees and benefits as well as the value of the services. When assessing the reasonableness of a charge, one generally needs to consider the value of all the services and benefits provided for the charge, not just some. If parties need additional guidance in this respect, they should refer to the Department's interpretations under ERISA section 408(b)(2) and Code section 4975(d)(2).

One commenter expressed support for the proposed exemption's reasonable compensation requirement. However, several other commenters maintained that the requirement is not specific enough and too lenient. The commenters objected to the exemption not requiring recommendation of investments with the lowest fees. One commenter stated that, by focusing on the "market value," the standard may incorporate existing practices that involve conflicts of interest and inflated prices. The same commenter stated that applying a fact-specific test to the reasonableness of fees encourages investment advice providers to contrive reasons why compensation is reasonable.

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As the Department indicated in the preamble to the proposed exemption, and reiterates here, the reasonableness of fees will depend on all the facts and circumstances at the time of the recommendation. The Department outlines several of those factors below which are intended to ensure the objective reasonableness of the fee. Several factors inform whether compensation is reasonable, including the nature of the service(s) provided, the market price of the service(s) and/or the underlying asset(s), the scope of monitoring, and the complexity of the product. No single factor is dispositive in determining whether compensation is reasonable; the essential question is whether the charges are reasonable in relation to what the investor receives.

The Department did not intend to suggest that reasonableness will be assessed solely against the existing market practices. The reasonable compensation standard will not be met if the fees bear little relationship to the value of the services actually rendered. And separately, the exemption will not be satisfied if the Financial Institution does not establish, maintain, and enforce written policies and procedures prudently designed to ensure that the Financial Institution and its Investment Professionals comply with the reasonable compensation standard in connection with covered fiduciary advice and transactions.

One commenter stated that the reasonable compensation requirement is unnecessary because it is already applicable to Title I fiduciaries under ERISA section

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408(b)(2).<sup>104</sup> Another commenter asserted that the reference to ERISA section 408(b)(2) indicated the exemption would adopt not only the substance but the established process for reasonable compensation determinations (i.e., a determination made by an independent Plan or IRA fiduciary who engages the service provider).

Incorporating the reasonable compensation standard as a condition of relief in this exemption increases the consequence of non-compliance and improves the protections of the exemption. It is also a critical protection in the context of an exemption which provides relief not only for prohibited transaction violations under section 406(a) of ERISA, but for self-dealing violations under section 406(b).<sup>105</sup> In the context of this exemption, the standard serves the important function of preventing investment advice fiduciaries from overcharging their Retirement Investor customers, despite the conflicts of interest associated with their compensation.

In this regard, one commenter suggested that Investment Professionals should be required to disclose, in writing, the reasons that the Investment Professional is not recommending an investment with lower fees and the reasons the recommendation is more beneficial to the Retirement Investor. Thus, the Financial Institution would be required to demonstrate, in writing, that the compensation arising from an investment is reasonable and in the Retirement Investor's best interest.

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<sup>104</sup> See also Code section 4975(d)(2).

<sup>105</sup> See also Code section 4975(c).

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Although the exemption places the burden on the Financial Institution and Investment Professional not to charge fees in excess of reasonable compensation, the Department declines to require documentation as suggested by the commenter. Under the exemption, the Financial Institution and Investment Professional are not required to recommend the transaction that is the lowest cost or that generates the lowest fees without regard to other relevant factors. In fact, the Department agrees with commenters that recommendations of the “lowest cost” security or investment strategy, without consideration of other factors, could in some cases even violate the exemption. In addition, given the wide variety of investment products and fee structures available to investors, the commenter that asked for documentation did not provide a useful model to define lower fee investments that would serve as benchmarks for these purposes.

One commenter suggested that the exemption text should specifically provide that the cost of an investment product is a factor, although it need not be the determinative factor, in applying the best interest standard. While the Department agrees that the cost of an investment product will be a factor in every recommendation, the best interest standard envisions that all of the characteristics of an investment product—not just its cost—will be evaluated based on Retirement Investors’ investment objectives, risk tolerance, financial circumstances, and needs. Therefore, the Department has not added a reference to cost to the best interest standard or elsewhere in the Impartial Conduct Standards.

#### Best Execution

Section II(a)(2)(B) of the exemption requires, in accordance with the federal



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securities laws, that the Financial Institution and Investment Professional seek to obtain the best execution of the investment transaction reasonably available under the circumstances. Financial Institutions and Investment Professionals subject to federal securities laws such as the Securities Act of 1933, the Securities Exchange Act of 1934, and the Investment Advisers Act of 1940, and rules adopted by FINRA and the Municipal Securities Rulemaking Board (MSRB), are obligated to adhere to a longstanding duty of best execution. As described recently by the SEC, “[a] broker-dealer’s duty of best execution requires a broker-dealer to seek to execute customers’ trades at the most favorable terms reasonably available under the circumstances.”<sup>106</sup> This condition complements the reasonable compensation standard set forth in the exemption.

The Department applies the best execution requirement consistent with the federal securities laws. Financial Institutions that are FINRA members satisfy this subsection if they comply with the best execution standards under federal securities laws and FINRA rules 2121 (Fair Prices and Commissions) and 5310 (Best Execution and Interpositioning), or any successor rules in effect at the time of the transaction, as interpreted by FINRA. Financial Institutions engaging in a purchase or sale of a municipal bond satisfy this subsection if they comply with the standards in MSRB rules

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<sup>106</sup> Regulation Best Interest Release, 84 FR at 33373, note 565.

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G-30 (Prices and Commissions) and G-18 (Best Execution), or any successor rules in effect at the time of the transaction, as interpreted by MSRB. Financial Institutions that are subject to and comply with the fiduciary duty under section 206 of the Investment Advisers Act—which, as described by the SEC, encompasses a duty to seek best execution—will also satisfy this subsection.<sup>107</sup>

One commenter expressed general support but also stated that the exemption should clarify that the “best execution” standard for executing portfolio transactions includes not only the price of the transaction itself but, if applicable, fees and expenses including commissions that provide the most favorable total cost or proceeds reasonably obtainable under the circumstances. In response, the Department notes that the exemption’s requirement that the Financial Institution and Investment Professional seek to obtain best execution is the second part of an overarching “reasonable compensation” condition which is not limited to best execution. As outlined above, the best execution requirement is consistent with federal securities law, and compliance by the Financial Institution and Investment Professional with the applicable statutory and regulatory provisions is sufficient to comply with the requirement. The condition builds upon Section II(a)(2)(A), which requires that compensation not exceed reasonable compensation. To the extent that the applicable securities law provisions do not address certain fees and expenses, those amounts are still captured in the overall requirement that

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<sup>107</sup> SEC Fiduciary Interpretation, 84 FR at 33674-75 (Section II.B.2 “Duty to Seek Best Execution”).

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the compensation not exceed reasonable compensation.

A number of commenters broadly objected to the inclusion of a best execution condition. The general critique was that the condition duplicates existing securities laws and is, therefore, unnecessary. In conjunction with this critique, multiple commenters argued that the best execution condition could result in the Department creating divergent and inconsistent interpretations of the best execution rule as compared to interpretations by FINRA, the SEC, and the MSRB. One commenter viewed the best execution requirement as an existing fiduciary obligation under ERISA section 404, stating that Title I fiduciaries are already obligated to seek to obtain the most favorable terms in a transaction, but should not lose the exemption for failure to do so.

The Department has considered these comments, but determined to retain the best execution condition. With respect to the exemption's application to Covered Principal Transactions, the condition will provide protection to Retirement Investors that may not be provided by the more general reasonable compensation requirement. The Department believes that the best execution requirement is a meaningful way to do so. The Department exercises its interpretive authority here to take the position that Financial Institutions and Investment Professionals that comply with applicable securities laws and their successors will satisfy this condition of the exemption, because of this requirement's origination in securities law. As a result, the Department does not believe the condition will result in divergent or inconsistent interpretations of securities laws.

Two additional commenters raised questions regarding the expansiveness of the condition. One commenter objected to the best execution condition on the grounds that

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Financial Institutions might rely on third parties, such as trustees or custodians, to execute particular transactions with respect to which they provided investment advice. A second commenter requested that the Department clarify that the best execution requirement is limited to circumstances similar to those covered by FINRA rules 2121 and 5310. With respect to both of these comments, the Department notes that the best execution condition is applicable as it would otherwise be applicable under the federal securities laws.

### *Misleading Statements*

Section II(a)(3) requires that statements by the Financial Institution and its Investment Professionals to the Retirement Investor about the recommended transaction and other relevant matters are not materially misleading at the time they are made. Other relevant matters include fees and compensation, material conflicts of interest, and any other fact that could reasonably be expected to affect the Retirement Investor's investment decisions. For example, the Department would consider it materially misleading for the Financial Institution or Investment Professional to include any exculpatory clauses or indemnification provisions in an arrangement with a Retirement Investor that are prohibited by applicable law.<sup>108</sup>

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<sup>108</sup> See, e.g., ERISA section 410 and see also ERISA Interpretive Bulletin 75-4—Indemnification of fiduciaries. (“The Department of Labor interprets section 410(a) as rendering void any arrangement for indemnification of a fiduciary of an employee benefit plan by the plan. Such an arrangement would have the same result as an exculpatory clause, in that it would, in effect, relieve the fiduciary of responsibility and liability to the plan by abrogating the plan's right to recovery from the fiduciary for breaches of fiduciary obligations.”)

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The Department received a few comments on this requirement in the proposal. One commenter stated this standard is unnecessary because misleading statements are already addressed by the proposal's disclosure requirement. Another commenter asked the Department to clarify what is considered a "misleading statement." Other commenters suggested that the Department expand the standard to specifically include material omissions because material omissions may be equally damaging to a Retirement Investor's understanding.

The Department has not changed the specific language in Section II(a)(3) from the proposal. Misleading statements are not necessarily addressed by the exemption's disclosure requirement, which is limited to certain specific topics. Further, the Department notes that the requirement is to avoid "*materially* misleading" statements, so as to provide a standard for the condition and avoid uncertainty.

The Department agrees with commenters that materially misleading statements are properly interpreted to include statements that omit a material fact necessary in order to make the statements, in light of the circumstances under which they were made, not misleading. Retirement Investors are clearly best served by statements and representations that are free from material misstatements and omissions. Financial Institutions and Investment Professionals best promote the interests of Retirement Investors by ensuring that accurate communications are a consistent standard in all their interactions with their customers.

In connection with the prohibition against misleading statements in Section II(a)(3), one commenter reacted to the Department's preamble statement about

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exculpatory statements. The commenter objected on several grounds, including the view that this statement effectively incorporates state and local laws that may vary and, thus, undermines the Act's aim to provide a uniform national standard in the retirement space. The commenter opined that this statement creates an uncertain and unworkable standard and even Financial Institutions that attempt to comply in good faith may lose the exemption if they inadvertently fail to comply with a law.

The Department does not believe that the inclusion of an exculpatory statement that is prohibited by applicable law is fairly characterized as an inadvertent failure to comply with the law. Financial Institutions that provide fiduciary investment advice to Retirement Investors should be well aware of the laws in the jurisdictions within which they operate. If a Financial Institution fails to apprise itself of its legal responsibilities, it should not be permitted to rely upon an exemption that includes a best interest standard for advice that incorporates the principles of 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. Permitting false and misleading statements that have the effect of dissuading a Retirement Investor from seeking lawfully available remedies is not consistent with the requirement, under Title I and the Code, that the Department find that an exemption is protective of the rights of participants and beneficiaries of Plans and IRA owners. Furthermore, the Department notes that all Title I fiduciaries remain subject to the uniform fiduciary responsibility provisions in ERISA section 404 with respect to Title I Plan assets. Finally, the Department has included provisions in the exemption, which

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enable fiduciaries to cure violations of the exemption conditions, under certain circumstances, and thereby avoid loss of the exemption.

***Disclosure – Section II(b)***

Section II(b) of the exemption requires the Financial Institution to provide certain written disclosures to the Retirement Investor prior to engaging in any transactions pursuant to the exemption. The Financial Institution must acknowledge, in writing, that the Financial Institution and its Investment Professionals are fiduciaries under Title I and the Code, as applicable, with respect to any fiduciary investment advice provided by the Financial Institution or Investment Professional to the Retirement Investor. The Financial Institution must also provide a written description of the services to be provided and material conflicts of interest arising out of the services and any recommended investment transaction. The description must be accurate in all material respects. The Financial Institution also must provide documentation of the specific reasons that any recommendation to roll over assets from one Plan or IRA to another Plan or IRA, or from one type of account to another, is in the Retirement Investor's best interest.

The disclosure obligations are designed to protect Retirement Investors by enhancing the quality of information they receive in connection with fiduciary investment advice. The disclosures should be in plain English, taking into consideration Retirement Investors' level of financial experience. The requirement can be satisfied through any disclosure, or combination of disclosures, required to be provided by other regulators so long as the disclosure required by Section II(b) is included. Once disclosure has been

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provided, the Financial Institution is not obligated to provide it again, except at the Retirement Investor's request or if the information has materially changed.

#### Written Fiduciary Acknowledgment

Section II(b)(1) of the final exemption includes the requirement to provide Retirement Investors with a written fiduciary acknowledgment as proposed. This disclosure is designed to ensure that the fiduciary nature of the relationship is clear to the Financial Institution and Investment Professional, as well as the Retirement Investor, at the time of the investment transaction.

This exemption gives broad relief for a wide range of activities that fiduciaries otherwise would be prohibited from engaging in. Given this wide field of action, the Department has concluded that clear disclosure is one of the necessary protections for Retirement Investors. A Financial Institution and Investment Professional that seek to provide investment advice to a Retirement Investor and otherwise engage in a relationship that satisfies the five-part test should, at a minimum (if they wish to avail themselves of this particular exemption), make a conscious up-front determination of whether they are acting as fiduciaries; tell their Retirement Investor customers that they are rendering advice as fiduciaries; and, based on their conscious decision to act as fiduciaries, implement and follow the exemption's conditions. The requirement also supports Retirement Investors' ability to choose a provider of advice that is a fiduciary within the meaning of Title I and the Code.

The written fiduciary acknowledgment supports the exemption's objectives of preserving the availability of a wide variety of business models and expanding investor



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choice. Retirement Investors benefit from knowing if they are receiving advice from a fiduciary. Further, this disclosure increases the likelihood that Financial Institutions and Investment Professionals will take their compliance obligations seriously. This exemption contemplates that the Financial Institution and Investment Professional will put down a marker as fiduciaries when they indeed are acting as such. Financial Institutions and Investment Professionals may not rely on the exemption merely as a back-up protection for engaging in possible prohibited transactions when their ultimate intention is to deny the fiduciary nature of their investment advice.

#### Model Language

To assist Financial Institutions and Investment Professionals in complying with this condition of the exemption, the Department provides the following model fiduciary acknowledgment language as an example of language that will satisfy the disclosure requirement in Section II(b)(1):

When we provide investment advice to you regarding your retirement plan account or individual retirement account, we are fiduciaries within the meaning of Title I of the Employee Retirement Income Security Act and/or the Internal Revenue Code, as applicable, which are laws governing retirement accounts. The way we make money creates some conflicts with your interests, so we operate under a special rule that requires us to act in your best interest and not put our interest ahead of yours.

In addition, although the exemption does not require it, Financial Institutions and Investment Professionals could more fully explain the exemption's terms with the following model disclosure:

Under this special rule's provisions, we must:

- Meet a professional standard of care when making investment recommendations (give prudent advice);

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- Never put our financial interests ahead of yours when making recommendations (give loyal advice);
- Avoid misleading statements about conflicts of interest, fees, and investments;
- Follow policies and procedures designed to ensure that we give advice that is in **your** best interest;
- Charge no more than is reasonable for our services; and
- Give you basic information about conflicts of interest.

#### Discussion of Comments

A few commenters expressed support for the written fiduciary acknowledgment.

A number of other commenters objected to the acknowledgment condition in the proposal. Some commenters stated that it would require them to say they were fiduciaries at the outset of a relationship, at a time when the ongoing nature of the relationship may be uncertain, which some commenters said would be unworkable. Some asserted that the written fiduciary acknowledgment requirement would deter some financial services providers from relying on the exemption because of fear of increased liability, thus causing Retirement Investors to lose access to the full range of investment advice arrangements. Several commenters argued that Financial Institutions will not be fiduciaries for all purposes, including under securities laws, and that the acknowledgement could confuse investors and also potentially undermine the purpose of the SEC's Form CRS as a comprehensive source of investor information. Some of these commenters said that they already disclose their duties under the best interest standard

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under Regulation Best Interest and believed that a similar disclosure would more accurately characterize their duties to Retirement Investors under the exemption. Some of these commenters also said that the proposal was inconsistent with other exemptions such as PTE 84-24, which have traditionally covered such inadvertent fiduciaries.

Some commenters said the disclosure was inconsistent with the Fifth Circuit’s *Chamber* opinion because the statement would determine fiduciary status, rather than the five-part test. Other commenters argued that the fiduciary acknowledgment could create a unilateral contract between the Financial Institution and the Retirement Investor, which they said was also impermissible in light of the Fifth Circuit’s *Chamber* opinion. Some expressed concern about interaction with other laws, including the possibility that the acknowledgment could be considered to create a “contractual fiduciary duty” under Massachusetts securities law which could impose additional requirements on broker-dealers.

Other commenters described the standard as not providing enough protection for Retirement Investors. According to these commenters, the exemption’s best interest standard is not a “true” fiduciary standard. Some commenters also indicated the lack of a “true” fiduciary standard makes it misleading for Financial Institutions to disclose that they are fiduciaries and thereby causes Retirement Investors to expect protections that they will not in fact receive. These commenters pointed to the Act’s legislative purpose to provide tax-advantaged accounts with *more* protection for participants than other, existing standards. Some commenters noted that the Regulation Best Interest standard is new, and the Department cannot determine that it offers the necessary protections until it

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has been fully tested in the market. One commenter stated that the fiduciary acknowledgement would allow investment advice providers to “pose” as fiduciaries and give non-fiduciary advice to Retirement Investors, who are depending on them for important decisions.

Some commenters suggested alternatives to the fiduciary acknowledgement, such as requiring an acknowledgment of the applicability of the best interest standard. Commenters said this would avoid unnecessary complexity and preserve Retirement Investors’ access to low-cost, high quality advice. One commenter suggested that the Department work on an expanded version of the SEC Form CRS which would explain the standards applicable to Title I and Code fiduciaries, broker-dealers, and investment advisers. However, other commenters opposed the idea of a disclosure of the best interest standard, expressing concern that any expansion of required disclosure would cause even more Retirement Investor confusion. According to these commenters, any problems associated with a fiduciary acknowledgment—including increased liability—could also apply to acknowledgment of the best interest standard.

The Department has carefully considered comments on the requirement to provide written acknowledgment of fiduciary status. The Department believes the acknowledgment ensures clarity as to the nature of the relationship between the parties, supports Retirement Investors’ ability to choose a provider of advice that is a fiduciary within the meaning of Title I and the Code, and promotes compliance with the conditions of the exemption. To increase that clarity, the voluntary model disclosure includes disclosure of the best interest standard. Financial Institutions that do not want to act as

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fiduciaries can also make that clear and act accordingly. The five-part test, as interpreted above, and Interpretive Bulletin 96-1 regarding participant investment education, provide Financial Institutions and Investment Professionals a clear roadmap for determining when they are, and are not, Title I and Code fiduciaries.

The Department disagrees with commenters who stated that the disclosure could be misleading to Retirement Investors because the exemption's best interest standard is not, in their assessment, a "true" fiduciary standard. The exemption is only applicable to "fiduciaries" within the meaning of Title I and the Code. Accordingly, the acknowledgment does not mislead investors as to the nature of the advice relationship, but rather accurately recites the Financial Institution's and Investment Professional's fiduciary status under Title I and the Code. Moreover, as discussed above, although the best interest standard does not include a "without regard to" formulation of the loyalty standard, the standard is consistent with interpretive statements by the Department as to Title I's duty of loyalty in other contexts.

With respect to the commenters who stated they should not have to acknowledge fiduciary status if they are uncertain as to whether they satisfy the five-part test, the Department believes, in light of the broad scope of relief in the exemption, that it is critical for Financial Institutions and Investment Professionals who choose to rely on the exemption to determine up-front if they intend to act as fiduciaries, and structure their relationship with the Retirement Investor accordingly. Financial Institutions are unlikely to comply fully with the exemption if they are simply relying on the exemption as a fallback position in the event that a primary argument of non-fiduciary status fails.

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Financial services providers that are not fiduciaries have no need of this exemption. Financial services providers that are fiduciaries, however, have a statutory obligation to adhere to the prohibited transaction rules or meet the terms of the exemption. Compliance with the law turns on financial services providers knowing whether or not they are acting as fiduciaries and acting in accordance with that understanding.

This exemption is not designed as a backup method of compliance for Financial Institutions that intend to deny the fiduciary nature of their investment advice despite their actions to the contrary. Instead, it is intended to provide broad relief for parties who are indeed fiduciaries under the five-part test, as manifested by their purposes and actions, and who implement fiduciary structures to govern their relationship with their customers. In response to comments asserting inconsistency of this exemption with PTE 84-24, which does not require written fiduciary acknowledgment, the Department responds that it is the responsibility of the Department to craft exemptions to ensure they are protective of and in the interests of plans and plan participants. The conditions in the Department's exemptions are designed to address the scope of the relief in the exemption and the attendant conflicts of interest. The Department has determined that the written fiduciary acknowledgment serves as an important safeguard in connection with the very broad grant of relief in this exemption from the self-dealing prohibitions of Title I and the Code. Other pre-existing prohibited transaction exemptions that do not have a fiduciary acknowledgment as a requirement, including statutory exemptions, remain available as alternatives.

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As for the related argument that some financial service providers will withdraw their services rather than provide their Retirement Investor customers a written fiduciary acknowledgment, the Department does not believe that will have significant effects on Retirement Investors' choices. The exemption in fact offers new exemptive relief for Financial Institutions and Investment Professionals that provide fiduciary investment advice to Retirement Investors. Pre-existing exemptions, with different conditions, remain in place as alternatives. And, for Financial Institutions and Investment Professionals that are not fiduciaries, this exemption is unneeded.

The Department also does not believe that the possibility of investor confusion or lack of understanding of the term "fiduciary," or concerns about the interaction with SEC Form CRS, present sound bases for eliminating the requirement. The acknowledgment does not contradict SEC Form CRS, and it is limited to fiduciary investment advice as defined in Title I and the Code. The Department believes that the model acknowledgment and additional voluntary model disclosure set forth above meets the objectives of the exemption by communicating the fiduciary status of the Financial Institution and Investment Professional as well as the requirement that they are operating under the exemption's best interest standard.

The Department does not intend that the fiduciary acknowledgment or any of the disclosure obligations create a private right of action as between a Financial Institution or Investment Professional and a Retirement Investor, and it does not intend that any of the exemption's terms, including the acknowledgement, give rise to any causes of action

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beyond those expressly authorized by statute.<sup>109</sup> Similarly, the fiduciary acknowledgement does not create a contractual fiduciary duty. ERISA section 502(a) provides a cause of action for fiduciary breaches and prohibited transactions with respect to Title I Plans (but not IRAs). Code section 4975 imposes a tax on disqualified persons participating in a prohibited transaction involving Plans and IRAs (other than a fiduciary acting only as such). These are the sole remedies for engaging in non-exempt prohibited transactions. The exemption does not create any new causes of action, nor does it require firms to make enforceable contractual commitments or give enforceable warranties to Retirement Investors, as was true of the 2016 fiduciary rulemaking which the Fifth Circuit set aside in its *Chamber* opinion.

#### Description of services and material conflicts of interest

Under Section II(b)(2) of the exemption, the Financial Institution must also provide a written description of the services to be provided and material conflicts of interest arising out of the services and any recommended investment transaction. The description must be accurate in all material respects. The Department believes disclosure of these items is necessary to ensure Retirement Investors receive information to assess the services that will be provided and related conflicts of interest. The disclosure

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<sup>109</sup> The SEC similarly stated with respect to its Form CRS, which describes the conduct standard applicable to broker-dealers and investment advisers, that it is not intended to create a private right of action. Form CRS Relationship Summary Release, 84 FR at 33530. *See also* Regulation Best Interest Release 84 FR at 33327 (“Furthermore, we do not believe Regulation Best Interest creates any new private right of action or right of rescission, nor do we intend such a result.”).



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requirement is principles-based and intended to allow flexibility to apply to a wide variety of business models and practices.

While one commenter agreed with the Department that a principles-based approach to disclosure provides the flexibility necessary to apply to a wide variety of business models with respect to the services and conflict disclosure requirements, some commenters contended the required disclosures would be insufficiently protective of Retirement Investors. Some commenters focused on the Department's position in the 2016 rulemaking that disclosure alone is ineffective in mitigating the impact of conflicts of interest.

Some commenters opposed the ability to satisfy the disclosure requirement through disclosures required to be provided by other regulators, particularly in cases where such disclosures may not be in plain English. Commenters argued that other disclosure regimes, such as Forms CRS and ADV, are not sufficient and are not designed to comply with the Act. The same commenters also stated that the Department should ensure that Retirement Investors receive accurate, not misleading, information that does not omit any material conditions or information including information that the Financial Institution or Investment Professional knows or should know that the Retirement Investors needs to determine whether to maintain the advice relationship and/or investment(s). Some commenters supported allowing disclosure requirements to be satisfied by using disclosures such as Forms ADV and CRS.

A commenter suggested specific additional items, perhaps in a model form, that should be included in the disclosure, including an estimate of the retirement savings

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needs of each participant and that the Department should develop a model disclosure and/or test proposed disclosures for their effectiveness. Another commenter suggested that the Department should develop a highly prescriptive, one-page model form that would allow consumers to compare service providers. Other commenters requested full safe harbors based on disclosure requirements under securities laws or insurance laws.

After consideration of the comments, the Department has determined to adopt the disclosure provisions as they were proposed. The Department believes the exemption's disclosure of the provided services and associated conflicts is appropriate and important, and it is by no means the sole protection in the exemption. The disclosure requirement works in concert with the other protections, such as the Impartial Conduct Standards and policies and procedures, and reinforces the exemption's important focus on conflict mitigation. The Department additionally stresses that conflict mitigation is not the sole purpose of disclosure, as some comments appeared to assume. In the Department's view, disclosure also promotes consumer choice and permits Retirement Investors to enter into a professional relationship and make investments with a clear understanding of the nature of that relationship and of the investments' salient features. These are important values, independent of their impact in mitigating conflicts.

The Department's approach in the proposal allowed for the disclosure to be satisfied through disclosures provided pursuant to other regulators' requirements. Since the Department's 2016 rulemaking, other regulators have developed additional conflict of interest disclosure requirements and oversight that provide a greater measure of accountability and investor protection in the marketplace. Permitting use of other

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regulators' disclosures was intended to minimize the potential for duplicative and voluminous disclosures which could contribute to reduced effectiveness. For this reason, the Department has declined to offer a model disclosure with respect to this aspect of the disclosure or add additional specific items to the required disclosure. Although the Department supports participants receiving information about retirement savings needs, for example, that type of a required disclosure is beyond the scope of this exemption proceeding.

In response to commenters who expressed concern that the exemption's approach would not ensure accurate and complete disclosures, the Department responds that the exemption text requires the disclosure of services to be provided and material conflicts of interest to be "accurate and not misleading in all material respects." Inaccurate disclosures will not satisfy the exemption conditions, nor will disclosures with material omissions. However, the Department declines to specify that the disclosure must provide information that the Financial Institution or Investment Professional knows or should know the Retirement Investor needs to determine whether to maintain the advice relationship and/or the investments, out of concern that this sets up a standard for disclosure that may be difficult to satisfy.

A commenter urged the Department to delete the written fiduciary acknowledgment and, instead, consistent with Regulation Best Interest, require disclosure instead of all material facts relating to the scope and terms of the relationship and all material facts relating to conflicts of interest that are associated with the recommendation. As discussed above, the Department has retained the written fiduciary

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acknowledgment in the final exemption as well as the requirement to disclose in writing the services to be provided and the material conflicts of interest. The Department did not adopt the approach taken in Regulation Best Interest, despite the belief that the exemption's disclosure requirements involve similar information, because the exemption is available to Financial Institutions that are not subject to Regulation Best Interest and Department believes that a specific disclosure of fiduciary status is important to the goals of this exemption.

However, the Department confirms that, like the Regulation Best Interest requirements, the standard for materiality for purposes of this obligation is consistent with the one the Supreme Court articulated in *Basic v. Levinson*,<sup>110</sup> and, in the context of this exemption, the standard of materiality is centered on those facts that a reasonable Retirement Investor, as defined in the exemption, would consider important. Material conflicts of interest that would be required to be disclosed under the exemption would include, for example, conflicts associated with proprietary products, payments from third parties, and compensation arrangements.

Commenters also requested additional guidance regarding satisfaction of the exemption's disclosure obligations through (1) the use of disclosures required by other regulators or other Title I and Code requirements, or (2) safe harbors when such disclosures are used. Commenters argued this would avoid duplication and Retirement

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<sup>110</sup> *Basic, Inc. v. Levinson*, 485 U.S. 224 (1988).

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Investor confusion. In doing so, most commenters emphasized a desire to ensure harmonization between the exemption condition and other disclosure regimes.

While the exemption does not include specific safe harbors, the Department confirms that Financial Institutions may rely, in whole or in part, on other regulatory disclosures to satisfy certain aspects of this disclosure requirement, for example, the disclosures required under Regulation Best Interest and Form CRS, applicable to broker-dealers; Form ADV and Form CRS, applicable to registered investment advisers; and disclosures required under insurance and banking laws when such disclosures cover services to be provided and the Financial Institution's and Investment Professional's material Conflicts of Interest. Avoiding duplication of disclosures is important and the Department reiterates that the disclosure standard under this exemption may be satisfied in whole, or in part, by using other required disclosures to the extent those disclosures include information required to be disclosed by the exemption. Allowing the use of other disclosures to meet the disclosure standard under this exemption should serve to harmonize this exemption's conditions with those of other disclosure regimes.

The Department also confirms that the disclosure required by the exemption may be included with or accompanied by the disclosure provided to responsible Plan fiduciaries under 29 CFR 2550.408b-2, as applicable, and that such disclosures may satisfy, in whole or in part, the disclosure obligations under this exemption when the fiduciary of the Plan is the Retirement Investor receiving advice, as defined in Section V(k)(3). However, if advice is provided to individual Plan participants, disclosure to the Plan fiduciary will not satisfy the disclosure obligation under the exemption. In such

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cases, the Retirement Investor is the individual participant receiving the investment advice, as defined in Section V(k)(1), and the disclosure obligation applies to that particular individual.

The Department cautions Financial Institutions that the requirements under this exemption are not merely a “check-the-box” activity. Rather, it is imperative that Financial Institutions engage in a careful analysis to identify their material conflicts so that they and their Investment Professionals are able to provide accurate disclosures and make recommendations that satisfy the best interest standard. The Department notes that although disclosures are required under the statutory exemption in ERISA section 408(b)(2) and the accompanying regulation at 29 CFR 2550.408b-2, the 408(b)(2) disclosures do not require an accompanying focus on conflict mitigation. Relatedly, the 408(b)(2) statutory exemption does not provide prohibited transaction relief from the self-dealing prohibited transactions in ERISA section 406(b).

#### Documentation of Rollover Recommendation

Section II(b)(3) of the final exemption requires Financial Institutions to provide Retirement Investors, prior to engaging in a rollover recommended pursuant to the exemption, with documentation of the specific reasons that the recommendation to roll over assets is in the best interest of the Retirement Investor. This requirement extends to recommended rollovers from a Plan to another Plan or IRA as defined in Code section 4975(e)(1)(B) or (C), from an IRA as defined in Code section 4975(e)(1)(B) or (C) 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). The requirement to document the

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specific reasons for these recommendations is part of the required policies and procedures, in Section II(c)(3).

Rollover recommendations are a primary concern of the Department, as Financial Institutions and Investment Professionals may have a strong economic incentive to recommend that investors roll over assets into one of their institution's IRAs, whether from a Plan or from an IRA account at another Financial Institution, or even between different account types. The decision to roll over assets from a Title I Plan to an IRA, in particular, may be one of the most important financial decisions that Retirement Investors make, as it may have a long-term impact on their legal rights and remedies and their retirement security.

The requirement to document the reasons that a rollover is in the best interest of the Retirement Investor is included in the exemption's policies and procedures provision to ensure that Financial Institutions and Investment Professionals take the time to form a prudent recommendation, and that a record is available for later review. The written record serves an important role in protecting Retirement Investors during this significant decision. The final exemption also includes the additional new provision in Section II(b)(3) requiring this documentation be provided to the Retirement Investor. Because of the special importance of rollover recommendations, the Department has concluded that Retirement Investors should be provided with the rollover documentation.

Some commenters on the proposal expressed support for the requirement to document the reasons for rollover recommendations, although some suggested it be expanded to provide additional protections. One suggestion was for the requirement to

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apply to all recommendations or at least to an expanded list of consequential recommendations beyond rollovers. One commenter suggested that the written documentation of all recommendations should demonstrate how the recommendations comply with the Financial Institution's written policies and procedures. Commenters also suggested additional factors to consider and document, including a clear examination of the long-term impact of any increased costs and why the added benefits justify those added costs, as well as consideration of economically significant features—such as surrender schedules and index annuity cap and participation rate—that the commenter indicated providers use in lieu of direct fees. One commenter provided an example of how the documentation could look, including scoring alternative investments. Another commenter indicated that the documentation requirement is not fully protective unless the documentation is provided to the Retirement Investor.

Other commenters urged the Department not to include this condition in the final exemption. They wrote that the documentation requirement was overly burdensome on Financial Institutions, generally is not required in other exemptions, and would not provide meaningful protections to Retirement Investors. Commenters stated it may be difficult to obtain the required information and noted that the SEC chose specifically not



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to include this requirement in Regulation Best Interest, even though the SEC did encourage it as a good practice.<sup>111</sup>

Some commenters felt that the specific considerations identified in the preamble were too prescriptive, and the exemption should instead rely on a more principles-based approach, such as the Financial Institutions' reasonable oversight of Investment Professionals. A few commenters requested clarification that the factors included in the preamble are merely factors that Financial Institutions "may include" in their documentation but that Financial Institutions are ultimately permitted to use their judgment to determine the appropriate factors to be considered, depending on the facts and circumstances of particular Retirement Investors. On the other hand, a commenter supported the factors and suggested that the Department should include them in the exemption text.

Certain commenters expressed further concern that the preamble discussion of the requirement did not appropriately weigh the benefits of a rollover (including the loss of the professional expertise and advice if the Retirement Investor chooses to stay in a workplace Plan) or other factors that are important to a Retirement Investor (such as access to distribution options, asset consolidation, and access to discretionary asset management). A commenter also asserted that the documentation should not extend to

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<sup>111</sup> Regulation Best Interest Release, 84 FR at 33360 ("Similarly, we encourage broker-dealers to record the basis for their recommendations, especially for more complex, risky or expensive products and significant investment decisions, such as rollovers and choice of accounts, as a potential way a broker-dealer could demonstrate compliance with the Care Obligation.").

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recommendations related to IRA transfers and transfers between brokerage and advisory accounts, asserting that these transfers are not irrevocable.

Some commenters were concerned about potential enforcement related to this provision of the exemption. One asked the Department to state that Financial Institutions are not required to review and approve each recommendation on a case by case basis. Another requested a non-enforcement policy so that a Financial Institution would not lose the exemption if an Investment Professional failed to document the reasons for any specific transaction, as long as the Financial Institution worked diligently and in good faith to implement technology and systems to efficiently document and supervise rollover recommendations. One commenter requested a safe harbor from the requirement to document rollover recommendations as long as Regulation Best Interest is satisfied.

Upon consideration of the comments, the Department has determined to include the documentation requirement in the exemption, as proposed. Given the importance of these decisions, the Department does not find it unnecessarily burdensome to require Financial Institutions and Investment Professionals to document their reasons for the recommendation. The documentation can provide an important opportunity for evaluation and oversight of these recommendations by Financial Institutions, Retirement Investors, and the Department, and is appropriate in the context of this broad exemption. Requiring specific documentation for rollover transactions provides appropriate protection of Retirement Investors while minimizing the burden on Financial Institutions that would be attached to documentation of all recommendations. By additionally requiring that the rollover documentation be provided to the Retirement Investor, the

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Department believes that the Retirement Investor will be better positioned to understand the significance of a rollover decision and how acting upon a rollover recommendation will satisfy the best interest standard under this exemption. The Department has retained the scope of the documentation requirement to include IRA transfers and transfers between brokerage and advisory accounts, even though those decisions may not be irrevocable, because they may involve significant cost, particularly over the long term.

With respect to recommendations to roll assets out of an Title I Plan and into an IRA, the factors that a Financial Institution and Investment Professional should consider and document include the following: 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. For rollovers from another IRA or changes from a commission-based account to a fee-based arrangement, a prudent recommendation would include consideration and documentation of the services that would be provided under the new arrangement. The Department agrees with commenters that the long-term impact of any increased costs and the reason(s) why the added benefits justify those added costs, as well as the impact of features such as surrender schedules and index annuity cap and participation rates, should be considered as part of any rollover recommendation, as relevant.

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In response to commenters who asked whether these factors cited in the proposal's preamble are required to be documented in all cases, or whether they are suggested considerations, it is the Department's view that these factors are relevant to a prudent fiduciary's analysis of a rollover. It would be difficult to justify a rollover recommendation that did not consider these factors. Of course, the discussion of factors identified above is not intended to suggest that Financial Institutions and Investment Professionals may not consider other factors, including those that are important to a particular Retirement Investor, as part of their rollover recommendation.<sup>112</sup> For that reason, the Department has not added the specific factors identified in the preamble to the exemption text, as a commenter suggested.<sup>113</sup>

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<sup>112</sup> For example, in the Regulation Best Interest Release, the SEC identified a number of factors that should be considered by broker-dealers in determining whether a particular account would be in a particular retail customer's best interest, including (1) the services and products provided in the account (ancillary services provided in conjunction with an account type, account monitoring services, etc.); (2) the projected cost to the retail customer of the account; (3) alternative account types available; (4) the services requested by the retail customer; and (5) the retail customer's investment profile. The SEC also cited factors that should be considered by broker-dealers in making a recommendation to roll over Title I Plan assets to an IRA, including: fees and expenses; level of service available; available investment options; ability to take penalty-free withdrawals; application of required minimum distributions; protection from creditors and legal judgments; holdings of employer stock; and any special features of the existing account. 84 FR at 33382-83.

<sup>113</sup> A commenter suggested a number of other factors that should be documented as part of the rollover recommendation, including: any incentives and/or fees the Financial Institution and/or the Investment Professional receives if they keep the account when employees leave their employer (i.e., maintaining the rollover account) or if they obtain additional fees for investments of the participants outside of the Plan; and fees and historic rates of return comparing the rollover recommendation and its proposed investment with the alternative(s), including leaving the assets in the current Plan, in a chart, over a 1, 5, and 10-year period. While the Department has chosen to take a less prescriptive and burdensome approach to the documentation and disclosure requirements than the commenter suggested, the Department stresses that

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To satisfy this condition for Title I Plan to IRA rollovers, the Department expects that Investment Professionals and Financial Institutions evaluating this type of potential rollover will make diligent and prudent efforts to obtain information about the existing Title I Plan and the participant's interests in it. In general, such information should be readily available as a result of DOL regulations mandating disclosure of Plan-related information to the Plan's participants (*see* 29 CFR 2550.404a-5). If the Retirement Investor is unwilling to provide the information, even after a full explanation of its significance, and the information is not otherwise readily available, the Financial Institution and Investment Professional should make a reasonable estimation of expenses, asset values, risk, and returns based on publicly available information. The Financial Institution and Investment Professional should document and explain the assumptions used and their limitations. In such cases, the Investment Professional could rely on alternative data sources, such as the most recent Form 5500 or reliable benchmarks on typical fees and expenses for the type and size of Plan at issue.

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Retirement Investors' interests should be protected by the overarching obligations to adhere to the Impartial Conduct Standards and to implement policies and procedures that require mitigation of conflicts of interest to the extent that a reasonable person reviewing the Financial Institution's policies and procedures and incentive practices would conclude that they do not create an incentive for a Financial Institution or Investment Professional to place their interests ahead of the interest of the Retirement Investor. The Department also agrees that a prudent fiduciary would consider the impact of fees and returns under alternative investments over time-horizons consistent with the Plan participant's financial interests and needs. Such analyses, however, should turn on the fiduciary's assessment of the unique facts and circumstances applicable to the Plan participant, as opposed to a single standardized analysis mandated by the Department for all cases.

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A few commenters suggested that Financial Institutions and Investment Professionals should not have to go beyond any information provided by Retirement Investors. One commenter suggested that Investment Professionals should not be compelled to make an estimate and should be permitted to include in the documentation: any reasons why, in the absence of certain information, other information supports a recommendation; the fact that the Retirement Investor was unwilling to provide the relevant information; and/or that the Investment Professional after best efforts, was unable to obtain the relevant information. The Department concurs that the documentation can include these statements, but notes that the statements would not be sufficient as an alternative to the estimates described in the previous paragraph.

Several commenters reacted to the proposed exemption's preamble statement that the documentation should address 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. A commenter queried whether Investment Professionals would be required to reallocate plan investments into an ideal asset allocation. Some insurance industry commenters expressed concern that the requirement would cause them to evaluate non-insurance options which they asserted was not permitted under insurance laws. The preamble statement was not intended, however, to suggest that Investment Professionals need to make advice recommendations as to investment products they are not qualified or legally permitted to recommend. Instead, the Department was merely indicating that a rollover recommendation should not be based solely on the Retirement Investor's existing allocation without any consideration of

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other investment options in the Plan.<sup>114</sup> A prudent fiduciary would carefully consider the options available to the investor in the Plan, including options other than the Retirement Investor's existing plan investments, before recommending that the participant roll assets out of the Plan.

Likewise, the Department notes that nothing in the exemption or the Impartial Conduct Standards prohibits investment advice by "insurance-only" agents or requires such insurance specialists to render advice with respect to other categories of assets outside their specialty or expertise. An Investment Professional should disclose any limitation on the types of products he or she recommends, and refrain from recommending an annuity if it is not in the best interest of the Retirement Investor. If, for example, it would not be in the investor's best interest for the investor to purchase an annuity in light of the investor's liquidity needs, existing assets, lack of diversification, financial resources, or other considerations, the Investment Professional should not recommend the annuity purchase, even if that means the agent cannot make a sale.

The exemption also does not mandate that a Financial Institution review documentation of each and every rollover recommendation. However, depending on the Financial Institution's business model and the other methods available to mitigate

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<sup>114</sup> FINRA has recognized that broker-dealers making a rollover recommendation should consider investment options among other factors. "The importance of this factor will depend in part on how satisfied the investor is with the options available under the plan under consideration. For example, an investor who is satisfied by the low-cost institutional funds available in some plans may not regard an IRA's broader array of investments as an important factor." See Regulatory Notice 13-45, *supra* note 42.

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conflicts of interest, regular review of some or all rollover recommendations may be an effective approach to compliance with the exemption. Because of the importance of this condition, the Department declines to provide a non-enforcement policy related to an Investment Professional's failure to document the recommendation or a safe harbor for general compliance with Regulation Best Interest. However, an isolated failure will only expose the Financial Institution to liability for that recommended transaction.

#### Timing of the disclosure

Some commenters urged the Department to modify the timing requirements of the disclosure. A few requested that, consistent with Regulation Best Interest, the Department allow the disclosure to be provided "prior to or at the time of the recommendation." Another commenter was concerned that Retirement Investors would not have sufficient time to review the information, and suggested that the disclosures should be provided 14 days before the close of the recommended transaction.

The Department has included the disclosure timing requirements in the final exemption as proposed. Because the exemption requires the disclosure to be provided prior to the transaction, parties wishing to provide disclosure at the time of the recommendation would be permitted to do so. The Department has not adopted the suggestion that the exemption require disclosure at least 14 days before the close of a recommended transaction due to concerns that this requirement could create an artificial timeframe that may, depending on the circumstances, prevent a Retirement Investor from entering into a beneficial transaction in a timely fashion.

#### ***Policies and Procedures – Section II(c)***



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Section II(c)(1) of the exemption establishes an overarching requirement that Financial Institutions establish, maintain, and enforce written policies and procedures prudently designed to ensure that the Financial Institution and its Investment Professionals comply with the Impartial Conduct Standards. Under Section II(c)(2), Financial Institutions' policies and procedures are required to mitigate conflicts of interest to the extent that a reasonable person reviewing the policies and procedures and incentive practices as a whole would conclude that they do not create an incentive for a Financial Institution or Investment Professional to place their interests ahead of the interest of the Retirement Investor.<sup>115</sup>

As defined in section V(c), 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.” Conflict mitigation is a critical condition of the exemption, and is important to the required findings under ERISA section 408(a) and Code section 4975(c)(2), that the exemption is in the interests of, and protective of, Retirement Investors.

To comply with Section II(c)(2) of the exemption, Financial Institutions would need to identify and carefully focus on the conflicts of interest in their particular business models that may create incentives to place their interests ahead of the interest of Retirement Investors. Under the exemption condition, Financial Institutions' policies and

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<sup>115</sup> Section II(c)(3) of the exemption, regarding documentation of the reasons for a rollover recommendation, is discussed above in the section on the disclosure of the documentation.

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procedures must be prudently designed to, among other things, protect Retirement Investors from recommendations to make excessive trades, or to buy investment products, annuities, or riders that are not in the investor's best interest or that allocate excessive amounts to illiquid or risky investments. Examples of policies and procedures and conflict mitigation strategies are provided later in this preamble.

Some commenters on the proposal expressed the view that the policies and procedures requirement was not sufficiently protective because it is based on the exemption's best interest standard, which the commenters believed was not a "true" fiduciary standard. Further, the commenters indicated that the exemption should include substantive provisions regarding the policies and procedures, beyond the statement that they must be prudent. One commenter suggested a number of specific provisions, including a description of the criteria that will be applied in determining that the recommendation did not place the interests of the Financial Institution or Investment Professional ahead of the interests of the Retirement Investor; a description of how the Financial Institution and Investment Professional will mitigate conflicts of interest; a requirement that the Financial Institution and investment professionals maintain written records showing the basis for each recommendation and how it complies with the written policies and procedures; the engagement of an independent compliance officer; identification, in the annual report, of the compliance officer and his or her qualifications; a statement describing the scope of the review conducted by the compliance officer; to the extent the self-review uncovers any violations of the policies and procedures, an unwinding of the transaction(s); and distribution of the self-review to all Retirement

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Investors receiving conflicted fiduciary investment advice. Another commenter expressed concern that the stated intention of the policies and procedures requirement did not align with what the proposal indicated would actually be accepted as demonstrating compliance.

In the proposal, Section II(c)(2) provided that a Financial Institution's policies and procedures would be required to mitigate conflicts of interest to the extent that the policies and procedures, and the Financial Institution's incentive practices, when viewed as a whole, are prudently designed to avoid misalignment of the interests of the Financial Institution and Investment Professionals and the interests of Retirement Investors. Some commenters criticized the proposal's approach to conflict mitigation, asserting that the proposal's terms were vague and lacked sufficient specifics. For instance, one commenter noted disapprovingly that the proposal required that policies and procedures be designed to "mitigate" conflicts of interest rather than "eliminate" them. Another commenter took issue with the proposal's suggestion that financial institutions should simply "consider minimizing" incentives that operate at the firm level. The commenter opined that the exemption's language does not address how to minimize the conflicts associated with receipt of revenue sharing payments, for instance.

Commenters also objected to the alignment of the best interest standard with the SEC's regulatory standards, which they asserted were intentionally designed to avoid disruption of broker dealers' highly conflicted business model. These commenters described the SEC standards as allowing that the vast majority of conflicted practices to continue unabated, and they said the same would be the case in the exemption. At the

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September 3, 2020, public hearing, several commenters warned the Department that the Regulation Best Interest standards were untested, and it was premature for the Department to rely on the SEC. Some commenters urged the Department to go further and describe specific lines of prohibited conduct.

Commenters also criticized the proposal for suggesting that significant conflicts of interest can be addressed through more rigorous supervision, stating that firms often have no incentive to constrain the conduct that their practices encourage. One commenter pointed specifically to the preamble's statement that a firm with "significant variation in compensation across different investment products would need to implement more stringent supervisory oversight," and noted that, in practice, when firms' bottom lines also benefit from recommending the higher compensating investment products, they will likely turn a blind eye when their financial professionals improperly push those products.

On the other hand, a few commenters urged the Department to increase alignment of the policies and procedures with securities laws, including Regulation Best Interest. A commenter requested the Department to clarify that, consistent with their understanding of Regulation Best Interest, firm-level conflicts must be disclosed or eliminated and any conflicts for the Investment Professional must be disclosed and mitigated. Other commenters asked that the wording of the policies and procedures be aligned to a greater degree with Regulation Best Interest and that the Department make clear that the satisfaction of other existing regulatory standards will satisfy the relevant conditions of the exemption for investment advice providers in order to eliminate confusion. Several

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commenters also asked the Department to acknowledge that “prudently” developed policies and procedures are the same as “reasonably” developed policies and procedures, or to simply revise the exemption requirement to use the term “reasonably designed” in accord with the text of Regulation Best Interest. These commenters opined that the difference between “prudence” and “reasonableness” was either unclear or nonexistent. One commenter urged the Department to adopt a definition of commission-based incentives limited to ones where incentives are tied to the sale of specific financial or insurance products within a limited period of time.

After consideration of all comments, the Department has adopted Section II(c)(1) as proposed. As discussed above, the Department believes that the best interest standard in the exemption is consistent with Title I’s fiduciary standard and that it is sufficiently protective of Retirement Investors’ interests. As the Department intends to retain interpretive authority with respect to satisfaction of the standards, it does not agree with commenters that it is necessary to defer action until further evaluation of the impact of Regulation Best Interest.

However, the Department has revised Section II(c)(2) to provide that Financial Institutions’ policies and procedures must mitigate conflicts of interest “to the extent that a reasonable person reviewing the policies and procedures and incentive practices as a whole would conclude that they do not create an incentive for a Financial Institution or Investment Professional to place their interests ahead of the interest of the Retirement Investor.” The Department believes this revised phrasing provides a standard that more clearly communicates the intent that incentives must be mitigated, and provides a

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standard of mitigation based on the view of a “reasonable person.” The preamble to the proposed exemption communicated this type of “reasonable person” standard in discussing the meaning of the proposal’s standard to avoid misalignment of interests.<sup>116</sup>

The standard retains the requirement that the policies and procedures and incentive practices must be viewed as a whole, so that Financial Institutions have flexibility in adopting practices that both mitigate compensation incentives and use supervisory oversight to prudently ensure that the standard is satisfied. The exemption’s policies and procedures requirement is deliberately principles-based, enabling multiple types of Financial Institutions and Investment Professionals to rely upon the exemption in connection with providing investment advice to Retirement Investors. The Department agrees, however, with the commenter that suggested that the Financial Institution’s written policies and procedures would necessarily express the criteria for determining that the exemption’s standards will be met and describe the Financial Institution’s conflict mitigation methods.<sup>117</sup>

Although some commenters requested the elimination of certain practices or asserted that the exemption should include more specific provisions regarding conflict mitigation, the Department has maintained the approach from the proposal. The Department disagrees with the commenters who stated that the vast majority of conflicted

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<sup>116</sup> 85 FR at 40845.

<sup>117</sup> The commenter’s other specific suggestions related to documentation of recommendations and to the retrospective review are discussed in the sections of the preamble on those requirements of the exemption.

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practices can continue unabated under the exemption. This claim is expressly contrary to the proposal's requirement that the policies and procedures be prudently designed to avoid misalignment of the interests of the Financial Institution and Investment Professional with the Retirement Investors they serve, which was clarified in this final exemption as discussed above.

As stated in the preamble to the proposal, Financial Institutions that continue to offer transaction-based compensation would focus on both financial incentives to Investment Professionals and supervisory oversight of investment advice to meet the standards. The exemption lacks additional specific mandates regarding conflict mitigation in order to accommodate the wide variety of business models used throughout the financial services industry. The type and degree of conflicts is susceptible to change over time. The Department believes that prescriptive conflict mitigation provisions would decrease the utility of the exemption, now and in the future.

Although a commenter criticized the suggestion that supervisory oversight can be protective, the Department believes that it is an important component of a Financial Institution's policies and procedures. Given that the exemption permits Investment Professionals to be compensated on a transactional basis, it is not possible to fully mitigate compensation incentives and accordingly Financial Institutions will always be required to oversee recommendations. In this regard, the Department declines to adopt the position suggested by a commenter that, for purposes of the exemption, commission-based incentives are limited to ones where incentives are tied to the sale of specific financial or insurance products within a limited period of time. Among other things, this

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approach would be inconsistent with the broad definition of a conflict of interest in the exemption, as 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.

As described above, one commenter identified a number of sales practices the commenter believed would still be permitted under the exemption, and stated that the exemption should more clearly limit incentive practices that a reasonable person would view as creating incentives to recommend investments that are not in Retirement Investors' best interest. The Department notes that the preamble to the proposal described the exemption as requiring this level of conflict mitigation, and the final exemption was revised to use that standard so that the meaning would be clearer.<sup>118</sup> Therefore, for example, the final exemption would not permit Financial Institutions to pay Investment Professionals significantly more to recommend one investment product over another, without putting in place stringent oversight mechanisms to ensure that the compensation structure does not incentivize recommendations that do not adhere to the exemption's standards.

The Department notes that regulators in the securities and insurance industry have

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<sup>118</sup> See 85 FR at 40845.



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adopted provisions requiring policies and procedures to eliminate sales contests and similar incentives such as sales quotas, bonuses, and non-cash compensation that are based on sales of certain investments within a limited period of time.<sup>119</sup> The Department intends to apply a principles-based approach to sales contests and similar incentives. To satisfy the exemption's standard of mitigation, Financial Institutions would be required to carefully consider all performance and personnel actions and practices that could encourage violation of the Impartial Conduct Standards.<sup>120</sup>

The Department further notes that the exemption's obligation to mitigate conflicts is not limited to conflicts of Investment Professionals. The conflict mitigation requirement in the policies and procedures obligation extends to the Financial Institution's own interests, including interests in proprietary products and limited menus of investment options that generate third party payments. The Department believes this exemption's standard of mitigation ensures that Financial Institutions will take a broad-based approach to addressing their conflicts of interest, which will provide a strong threshold foundation for the formulation of best interest investment recommendations.

In response to commenters seeking guidance on the differences, if any, between the prudence standard under this part of the exemption and the reasonableness standards

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<sup>119</sup> Regulation Best Interest Release, 84 FR at 33394-97; NAIC Model Regulation, Section 6.C.(2)(h).

<sup>120</sup> None of the conditions of the exemption are intended to categorically bar the provision of employee benefits to insurance company statutory employees, despite the practice of basing eligibility for such benefits on sales of proprietary products of the insurance company. *See* Code section 3121.

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under the federal securities laws, the Department states that it does not have interpretive authority over the federal securities laws, and declines to provide interpretations as to how these standards may differ. The prudence requirement indicates a level of care, skill, and diligence that a 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.

The Department offers the following examples of business models and practices that may present conflicts of interest that a Financial Institution would address through its policies and procedures:

*Example 1:* A Financial Institution anticipates that prohibited conflicts of interest related to compensation in its business model will only arise in connection with advice to roll over Plan or IRA assets, because after the rollover, the Financial Institution and Investment Professional will provide ongoing investment advice and be compensated on a level-fee basis. The Financial Institutions decides to seek prohibited transaction relief in connection with rollover conflicts by relying upon the exemption.<sup>121</sup> The Financial Institution's policies and procedures would focus on rollover recommendations.<sup>122</sup>

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<sup>121</sup> In general, after the rollover, the ongoing receipt of compensation based on a fixed percentage of the value of assets under management may not require a prohibited transaction exemption. However, the Department cautions that certain practices such as "reverse churning" (i.e. recommending a fee-based account to an investor with low trading activity and no need for ongoing advice or monitoring) or recommending holding an asset solely to generate more fees may be prohibited transactions. This exemption would not be available for such practices because they would not satisfy the Impartial Conduct Standards.

<sup>122</sup> As explained earlier, it is the Department's view that a recommendation to roll assets out of a Plan is advice with respect to moneys or other property of the Plan. Advice to take a distribution of assets from a Title I Plan is advice to sell, withdraw, or transfer investment assets currently held in the Plan. A distribution recommendation commonly involves either advice to change specific investments in the Plan or to change fees and services directly affecting the return on those investments.

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Additionally, the policies and procedures should appropriately address how to document rollover recommendations, consistent with the requirement in Section II(c)(3) to document the reason for a rollover recommendation and why such recommendation is in the best interest of the Retirement Investor.

*Example 2:* A Financial Institution intends to receive transaction-based compensation, and generate compensation for the Financial Institution and its Investment Professionals based on transactions that occur in a Retirement Investor's accounts, such as through commissions. The Financial Institution's policies and procedures would address the incentives created by these compensation arrangements.

*Example 3:* Insurance company Financial Institutions can comply with the new exemption by supervising independent insurance agents, or by creating oversight and compliance systems through contracts with insurance intermediaries. The Financial Institution and/or intermediary would address incentives created with respect to independent agents' recommendations of the Financial Institution's insurance or annuity products.

In connection with these examples, following is a discussion of various possible components of effective policies and procedures. While the Department is not adjusting the policies and procedures to provide a safe harbor for compliance with securities or other law, many of the conflict mitigation approaches identified below were identified by

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the SEC in Regulation Best Interest.<sup>123</sup>

### Commission-based Compensation Arrangements

Financial Institutions that compensate Investment Professionals through transaction-based payments and incentives would be required to minimize the impact of these compensation incentives on fiduciary investment advice to Retirement Investors, so that the Financial Institution would be able to meet the exemption's standard of conflict mitigation set forth in Section II(c)(2). As noted above, this standard would require mitigation of conflicts to the extent that a reasonable person reviewing the policies and procedures and incentive practices as a whole would conclude that they do not create an incentive for a Financial Institution or Investment Professional to place their interests ahead of the interest of the Retirement Investor.

For commission-based compensation arrangements, Financial Institutions would be encouraged to focus on financial incentives to Investment Professionals and supervisory oversight of investment advice. These two aspects of the Financial Institution's policies and procedures would complement each other, and Financial Institutions could retain the flexibility, based on the characteristics of their businesses, to adjust the stringency of each component provided that the exemption's overall standards

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<sup>123</sup> As one commenter noted, the scope of Regulation Best Interest and the Department's exemption do not overlap precisely. Therefore, the commenter asked the Department to acknowledge that Financial Institutions developing policies and procedures will need to address interactions with Retirement Investors that are not addressed in Regulation Best Interest. This is another reason that the Department intends to maintain interpretive authority with respect to the exemption.

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would be satisfied. Financial Institutions that significantly mitigate commission-based compensation incentives would have less need to rigorously oversee individual Investment Professionals and individual recommendations. Conversely, Financial Institutions that have significant variation in compensation across different investment products would need to implement the policies and procedures by using more stringent supervisory oversight.<sup>124</sup>

In developing compliance structures, the Department expects that Financial Institutions will also look to conflict mitigation strategies identified by the Financial Institutions' other regulators. For illustrative purposes only, the following are non-exhaustive examples of practices identified as options by the SEC that could be implemented by Financial Institutions in compensating Investment Professionals: (1) avoiding compensation thresholds that disproportionately increase compensation through incremental increases in sales; (2) 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; (3) eliminating compensation incentives within comparable product lines by, for example,

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<sup>124</sup> This is not to suggest that a Financial Institution that analyzes the conflicts associated with commission-based compensation incentives does not need to engage in a separate mitigation analysis with respect to the conflicts specifically associated with rollover recommendations as opposed to non-rollover recommendations. Nor does it suggest that every financial incentive can be effectively mitigated through oversight, no matter how severe the conflict of interest. As reflected in the SEC's ban on time-limited sales contests, some incentive structures are too prone to abuse to permit as part of firm policies and procedures.

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capping the credit that an associated person may receive across mutual funds or other comparable products across providers; (4) implementing supervisory procedures to monitor recommendations that are: near compensation thresholds; 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 (such as recommendations to roll over or transfer assets in a Title I Plan account to an IRA) or from one product class to another; (5) adjusting compensation for associated persons who fail to adequately manage conflicts of interest; and (6) limiting the types of retail customer to whom a product, transaction or strategy may be recommended.<sup>125</sup>

Financial Institutions also must review and mitigate incentives at the Financial Institution level. Firms should establish or enhance the review process for investment products that may be recommended to Retirement Investors. This process should include procedures for identifying and mitigating conflicts of interest associated with the product or declining to recommend a product if the Financial Institution cannot effectively mitigate associated conflicts of interest.<sup>126</sup>

#### Insurance Companies

To comply with the exemption, insurance company Financial Institutions could

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<sup>125</sup> Regulation Best Interest Release, 84 FR at 33392.

<sup>126</sup> For additional discussion of Financial Institution conflicts, see the preamble discussion below, “Proprietary Products and Limited Menus of Investment Products.”

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adopt and implement supervisory and review mechanisms and avoid improper incentives that preferentially push the products, riders, and annuity features that might incentivize Investment Professionals to provide investment advice to Retirement Investors that does not meet the Impartial Conduct Standards. Insurance companies could implement procedures to review annuity sales to Retirement Investors under fiduciary investment advice arrangements to ensure that they were made in satisfaction of the Impartial Conduct Standards, much as they may already be required to review annuity sales to ensure compliance with state-law suitability requirements.<sup>127</sup>

In this regard, as discussed above, insurance company Financial Institutions would be responsible only for an Investment Professional's recommendation and sale of

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<sup>127</sup> Cf. NAIC Model Regulation, Section 6.C.(2)(d) ("The insurer shall establish and maintain procedures for the review of each recommendation prior to issuance of an annuity that are designed to ensure that there is a reasonable basis to determine that the recommended annuity would effectively address the particular consumer's financial situation, insurance needs and financial objectives. Such review procedures may apply a screening system for the purpose of identifying selected transactions for additional review and may be accomplished electronically or through other means including, but not limited to, physical review. Such an electronic or other system may be designed to require additional review only of those transactions identified for additional review by the selection criteria"); and (e) ("The insurer shall establish and maintain reasonable procedures to detect recommendations that are not in compliance with subsections A, B, D and E. This may include, but is not limited to, confirmation of the consumer's consumer profile information, systematic customer surveys, producer and consumer interviews, confirmation letters, producer statements or attestations and programs of internal monitoring. Nothing in this subparagraph prevents an insurer from complying with this subparagraph by applying sampling procedures, or by confirming the consumer profile information or other required information under this section after issuance or delivery of the annuity"). The prior version of the model regulation, which was adopted in some form by a number of states, also included similar provisions requiring systems to supervise recommendations. See Annuity Suitability (A) Working Group Exposure Draft, Adopted by the Committee Dec. 30, 2019, *available at* [www.naic.org/documents/committees\\_mo275.pdf](http://www.naic.org/documents/committees_mo275.pdf). (comparing 2020 version with prior version).

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products offered to Retirement Investors by the insurance company in conjunction with fiduciary investment advice, and not to product sales of unrelated and unaffiliated insurers.<sup>128</sup>

Insurance companies could also create a system of oversight and compliance by contracting with an insurance intermediary or other entity to implement policies and procedures designed to ensure that all of the agents associated with the intermediary adhere to the conditions of this exemption. The intermediary could, for example, take action directly aimed at mitigating or eliminating compensation incentives. The intermediary could also review documentation prepared by insurance agents to comply with the exemption, as may be required by the insurance company, or use third-party industry comparisons available in the marketplace to help independent insurance agents recommend products that are prudent for the Retirement Investors they advise.

#### Periodic Review of Policies and Procedures

The Department notes that Financial Institutions complying with the exemption would need to review their policies and procedures periodically and reasonably revise them as necessary to ensure that the policies and procedures continue to satisfy the conditions of this exemption. In particular, the exemption requires ongoing vigilance as to the impact of conflicts of interest on the provision of fiduciary investment advice to Retirement Investors. As a matter of prudence, Financial Institutions should regularly

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<sup>128</sup> *Cf. id.*, Section 6.C.(4) (“An insurer is not required to include in its system of supervision: (a) A producer’s recommendations to consumers of products other than the annuities offered by the insurer”).



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review their policies and procedures to ensure that they are achieving their intended goal of ensuring compliance with the exemption and the provision of advice that satisfies the Impartial Conduct Standards. For example, to the extent new products, lines of business, or compensation structures are introduced, Financial Institutions should consider whether their policies and procedures continue to be appropriate and effective. To the extent that the policies are failing to achieve their goal of ensuring compliance, the deficiencies should be corrected.

### ***Proprietary Products and Limited Menus of Investment Products***

The best interest standard can be satisfied by Financial Institutions and Investment Professionals that provide investment advice on proprietary products or on a limited menu of investment options, including limitations to proprietary products<sup>129</sup> and products that generate third party payments.<sup>130</sup> Product limitations can serve a beneficial purpose by allowing Financial Institutions and Investment Professionals to develop increased familiarity with the products they recommend. At the same time, limited menus, particularly if they focus on proprietary products and products that generate third party payments, can result in heightened conflicts of interest. Financial Institutions and their affiliates and related entities may receive more compensation than they would for

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<sup>129</sup> Proprietary products include products that are managed, issued, or sponsored by the Financial Institution or any of its affiliates.

<sup>130</sup> Third party payments include sales charges when not paid directly by the Plan or IRA; gross dealer concessions; revenue sharing payments; 12b-1 fees; distribution, solicitation or referral fees; volume-based fees; fees for seminars and educational programs; and any other compensation, consideration or financial benefit provided to the Financial Institution or an affiliate or related entity by a third party as a result of a transaction involving a Plan or an IRA.

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recommending other products, and, as a result, Investment Professionals and Financial Institutions may have an incentive to place their interests ahead of the interest of the Retirement Investor.

As the Department explained in the proposal, Financial Institutions and Investment Professionals providing investment advice on proprietary products or on a limited menu can satisfy the conditions of the exemption. They can do so by providing complete and accurate disclosure of their material conflicts of interest in connection with such products or limitations and adopting policies and procedures that mitigate conflicts to the extent that a reasonable person reviewing the policies and procedures and incentive practices as a whole would conclude that they do not create an incentive for a Financial Institution or Investment Professional to place their interests ahead of the interest of the Retirement Investor.

The Department envisions that Financial Institutions complying with the Impartial Conduct Standards and policies and procedures would carefully consider their product offerings and form a reasonable conclusion about whether the menu of investment options would permit Investment Professionals to provide fiduciary investment advice to Retirement Investors in accordance with the Impartial Conduct Standards. The exemption would be available if the Financial Institution prudently concludes that its offering of proprietary products, or its limitations on investment product offerings, in conjunction with the policies and procedures, would not create an incentive for Financial Institutions or Investment Professionals to place their interests ahead of the interest of the Retirement Investor.

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Several commenters expressed general support for the Department’s approach to proprietary products and limited menus. One commenter noted that practical considerations call for limiting the investment menu when thousands of mutual funds and securities exist on a Financial Institution’s platform. Another commenter agreed that Financial Institutions would form a reasonable conclusion about whether the limited menu supports recommendations that satisfy the Impartial Conduct Standards.

Some commenters expressed concern about the exemption’s coverage of recommendations involving proprietary products or limited menus because it would allow recommendations of poorly performing, high commission products. One commenter stated the exemption should not extend to such recommendations, as they create the largest potential for conflicts that cannot be fully eliminated, and suggested that the Department require that such recommendations be handled through the individual prohibited transaction exemption process. Another commenter indicated that the proposal did not address some “non-financial structures” used in connection with rollovers, such as requirements imposed by service providers for investors to fill out lengthy forms in order to roll plan assets over to third-party entities, while simultaneously providing simple and easy mechanisms for rollovers from the Plan into proprietary products maintained by the provider. Another commenter thought the exemption should specifically require Financial Institutions to document their conclusions as to why their offering of proprietary products or limited menus, in conjunction with the policies and procedures, would not cause a misalignment of their interests with Retirement Investors.

In response to comments, the Department has not restricted the exemption to

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exclude recommendations of proprietary products and products from a limited menu, or required them to be addressed solely through individual exemptions. The Department believes that the conditions of the class exemption, including the best interest standard, appropriately address concerns about proprietary products. The Department has not added a specific requirement that Financial Institutions document their conclusions as to why their offering of proprietary products or limited menus, in conjunction with the policies and procedures, would not create an incentive for the Financial Institutions or Investment Professionals to place their interests ahead of the interest of the Retirement Investor. However, the Department notes that this is a best practice and may serve the interests of Financial Institutions since they are required under Section IV to keep records demonstrating compliance with the exemption. Even though there is no specific documentation requirement, the Department expects a Financial Institution would be able to explain clearly the process it used in making this determination. The Department also cautions Financial Institutions and Investment Professionals about practices that selectively promote Retirement Investors' purchase of products that are not in their best interest in the manner suggested by the commenter above (e.g., by making it much more burdensome for the Retirement Investor to rollover assets to one investment rather than another). Even if the practices do not directly involve the provision of fiduciary advice, they potentially undermine the required policies and procedures to mitigate conflicts of interest and may facilitate violations of fiduciary standards. Such practices should also be a matter of concern for the fiduciaries responsible for hiring the Financial Institutions and Investment Professionals to provide plan services.

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A few commenters sought clarification of the Department's preamble statement that a Financial Institution's policies and procedures should extend to circumstances in which the Financial Institution or Investment Professional determines that its proprietary products or limited menu do not offer Retirement Investors an investment option in their best interest when compared with other investment alternatives available in the marketplace. They sought confirmation that the Department did not intend to require Financial Institutions to compare their product offerings to all available investment alternatives, a confirmation they stated is consistent with guidance provided by the SEC on Regulation Best Interest. These commenters asserted that imposing such a requirement would serve to limit investor access to prudent investment advice, and could potentially require Investment Professionals that are insurance-only agents to compare annuities against securities, which they are not be licensed to sell, and which would potentially cause compliance issues under state securities laws.

The Department confirms that the exemption does not require Financial Institutions to compare proprietary products with all other investment alternatives available in the marketplace. There is no obligation to perform an evaluation of every possible alternative, including those the Financial Institution or Investment Professional are not licensed to recommend, and the exemption does not contemplate that there is a single investment that is in a Retirement Investor's best interest. The exemption merely provides that Financial Institutions and Investment Professionals cannot use a limited menu to justify making a recommendation that does not meet the Impartial Conduct Standards.

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### ***Retrospective Review – Section II(d)***

Section II(d) of the exemption requires Financial Institutions to conduct a retrospective review, at least annually, that is reasonably designed to assist the Financial Institution in detecting and preventing violations of, and achieving compliance with, the Impartial Conduct Standards and the policies and procedures governing compliance with the exemption. While mitigation of Financial Institutions' and Investment Professionals' conflicts of interest is critical, Financial Institutions must also monitor Investment Professionals' conduct to detect advice that does not adhere to the Impartial Conduct Standards or the Financial Institution's policies and procedures.

The methodology and results of the retrospective review must be reduced to a written report that is provided to one of the Financial Institution's Senior Executive Officers.

That officer is required to certify annually that:

- (A) The officer has reviewed the report of the retrospective review;
- (B) The Financial Institution has in place policies and procedures prudently designed to achieve compliance with the conditions of this exemption; and
- (C) 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 this exemption.

This retrospective review, report and certification must be completed no later than

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six months following the end of the period covered by the review. The Financial Institution is required to retain the report, certification, and supporting data for a period of six years. If the Department requests the written report, certification, and supporting data within those six years, the Financial Institution would make the requested documents available within 10 business days of the request, to the extent permitted by law including 12 U.S.C. § 484. The Department believes that the requirement to provide the written report within 10 business days will ensure that Financial Institutions diligently prepare their reports each year, resulting in meaningful protection of Retirement Investors.

Financial Institutions can use the results of the review to find more effective ways to ensure that Investment Professionals are providing investment advice in accordance with the Impartial Conduct Standards and to correct any deficiencies in existing policies and procedures. Requiring a Senior Executive Officer to certify review of the report is a means of creating accountability for the review. This would serve the purpose of ensuring that more than one person determines whether the Financial Institution is complying with the conditions of the exemption and avoiding non-exempt prohibited transactions. If the officer does not have the experience or expertise to determine whether to make the certification, he or she would be expected to consult with a knowledgeable compliance professional to be able to do so.

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The retrospective review is based on FINRA rules governing how broker-dealers supervise associated persons,<sup>131</sup> adapted to focus on the conditions of the exemption.

The Department is aware that other Financial Institutions are subject to regulatory requirements to review their policies and procedures;<sup>132</sup> however, for the reasons stated above, the Department believes that the specific certification requirement in the exemption will serve to protect Retirement Investors in the context of conflicted investment advice transactions.

Several commenters expressed support for a retrospective review but indicated the provision needs strengthening. One commenter stated that the requirement would be strengthened if the best interest standard is strengthened.<sup>133</sup> One commenter suggested several methods of strengthening the exemption's retrospective review requirements, including requiring an independent audit, requiring appointment of a compliance officer and identification of the compliance officer and his or her qualifications in the report, and requiring the report of the retrospective review to be provided to Retirement Investors. One commenter provided an example of how the report could look and criticized the Department's statement that sampling would be permitted, asserting that the concentration of noncompliance is more likely to occur in large transactions. A few commenters stated the exemption should specify consequences of violations of the

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<sup>131</sup> See FINRA rules 3110, 3120, and 3130.

<sup>132</sup> See, e.g., Rule 206(4)-7(b) under the Investment Advisers Act of 1940.

<sup>133</sup> The best interest standard and the comments received on it are discussed above in "Impartial Conduct Standards."



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policies and procedures when such violations do not rise to the level of egregious patterns of misconduct.

A number of commenters opposed the requirement, stating it is burdensome, costly and unnecessary. As support for this assertion, some commenters stated that other exemptions do not include this condition and it also is not a requirement of Regulation Best Interest. Some commenters urged the Department to avoid what they viewed as a separate “prescriptive” requirement in terms of ensuring that Financial Institutions satisfy the conditions of the exemption, in favor of a review incorporated into a firm’s policies and procedures. Some asserted that the other exemption conditions will provide a sufficient compliance structure and the consequences of failing to comply with the exemption will provide sufficient incentive for Financial Institutions to oversee their own compliance. One commenter said wording of the condition was too vague and could expose Financial Institutions to liability for not meeting the standard. A few commenters suggested eliminating subsections (B) and (C) of the certification requirement, and, instead, merely referencing Section II(c)’s policies and procedures requirement.<sup>134</sup> Another commenter asked the Department to provide a safe harbor based on compliance with FINRA’s similar review requirement.

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<sup>134</sup> Subsection (B) requires certification that “[t]he Financial Institution has in place policies and procedures prudently designed to achieve compliance with the conditions of this exemption;” and subsection (C) requires certification that “[t]he 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 this exemption.”

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As further described below, the Department has adopted the retrospective review requirement largely as proposed based on the view that compliance review is a critical component of a Financial Institution's policies and procedures. Without this specific requirement, some Financial Institutions may take the position that adoption of policies and procedures is sufficient, without paying attention to whether the policies and procedures are prudently designed and whether Investment Professionals are complying with the policies and procedures and the Impartial Conduct Standards. The Department does not agree with those commenters who claimed such a review was unnecessary or overly burdensome.

While some commenters expressed concern that the retrospective review needed strengthening, the Department notes the review must be signed and certified. The Department believes that requiring the results to be reduced to a written document certified by a Senior Executive Officer increases the likelihood that isolated compliance failures will be corrected before they become systemic. Although some commenters expressed the general view that the exemption relies upon self-policing, the requirement that Financial Institutions make their report available to the Department within 10 business days upon request ensures that the Department retains an appropriate level of oversight over exemption compliance.

To maintain this principles-based approach, the Department did not mandate specific detailed components of the retrospective review. Financial Institutions will be free to design the review process in the context of their own business models and the particular conflicts of interest they face. Although the exemption does not specify that a

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compliance officer must be appointed, the Department envisions that Financial Institutions will, as a practical matter, assign a compliance role to an appropriate officer.

The Department did not narrow subsections (B) and (C) of the certification requirements merely to reference the requirements of Section II(c) as suggested by a few commenters. The broader certification properly focuses the Financial Institution's assessment of the ongoing effectiveness of the policies and procedures, the periodic testing of those policies and procedures, and the need to make modifications to the extent they are not working. A strong process to review the effectiveness of the Financial Institution's policies and procedures and to make course corrections as necessary is critical to the protection of Retirement Investors affected by the exemption.

In the proposal, the Department indicated that it envisioned that the review would involve testing a sample of transactions to determine compliance. In response to a comment that indicated sampling may not be appropriate since non-compliance may occur more frequently with respect to large transactions, the Department clarifies that an appropriate retrospective review would be aimed at detecting non-compliance across a wide range of transactions types and sizes, large and small, identifying deficiencies in the policies and procedures, and rectifying those deficiencies. For large Financial Institutions that conduct large numbers of transactions each year, sampling may not be the sole means of testing compliance, but it is an important and necessary component of any prudent review process, and should be performed in a manner designed to identify potential violations, problems, and deficiencies that need to be addressed.

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The Department considered the alternative of requiring a Financial Institution to engage an independent party to provide an external audit, as suggested by a commenter. Because of the potential costs of such audits, and the exemption's reliance on the retrospective review process, the Department elected not to impose this additional requirement. The Department is not convinced that an independent, external audit would yield sufficient benefits in addition to the results of the retrospective review to justify the increased cost, especially in the case of smaller Financial Institutions without any past practice of actions that may render it ineligible to rely on this class exemption. The Department also has not included a requirement that the report of the retrospective review be provided to all Retirement Investors. As discussed below in the section on recordkeeping, the Department believes that Financial Institutions' internal compliance documents should be available to regulators but not Retirement Investors, so as to promote full identification and remediation of compliance issues without undue concern about the widespread disclosure of the issues.

The Department does not believe the requirement is too vague for Financial Institutions to know how to comply. The requirement that the review be "reasonably designed" is consistent with reasonableness as a term commonly used in a variety of legal settings, and especially under the Act. Further, as noted above, the Department provided this approach to allow Financial Institutions flexibility in designing their compliance reviews.

Although a retrospective review is not a requirement of Regulation Best Interest, as one commenter pointed out, the Department notes that an analogous requirement is

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already applicable to broker-dealers under FINRA rules. The Department declines to provide a safe harbor based on compliance with the FINRA rule because that rule is aimed at reviewing compliance with FINRA rules, not the Financial Institution's separate compliance with the terms of this exemption.

Some commenters said that a retrospective review was an unusual requirement for a class exemption, and that the Department had not pointed to any noncompliance to warrant such a condition. The Department, however, has routinely made independent audits a condition in individual exemptions. It is important that entities comply with the terms of the exemption and that the Department can readily verify such compliance. Here, the Department continues to believe that a retrospective review, which is less costly than an audit, strikes the appropriate balance for this class exemption. Additionally, the Department notes that it frequently imposes a recordkeeping requirement documenting compliance as a condition of exemption. In drafting a principles-based exemption that works with different business models, the Department has determined that this retrospective review is a crucial way to determine compliance with the exemption, and to ensure covered entities review, enforce, and update their policies and procedures as needed.

In response to commenters who asked the Department to specify the consequences of a violation discovered in the retrospective review, and other commenters who asked for the ability to correct compliance issues uncovered during the review, the Department has included a self-correction feature in the final exemption, as described below. If self-correction is not available or a Financial Institution decides not to self-

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correct, then the Financial Institution remains liable for a prohibited transaction associated with the transaction for which there was a failure.

One commenter stated that the Department should not require Financial Institutions to provide the report within 10 business days of request by the Department because Financial Institutions may have legitimate difficulties meeting this requirement. However, this aspect of the exemption provides an important mechanism for the Department to ensure that Financial Institutions are taking their roles under the exemption seriously. The Department does not intend for Financial Institutions to prepare a retrospective review only after it has been requested by the Department. The exemption provides a separate deadline for the completion of each annual review, so the obligation to provide the accompanying report within 10 business days of request will only apply to completed reports. For this reason, the Department has not extended the 10 business-day period.<sup>135</sup>

Another commenter requested a transition period for the retrospective review through 2022, for the creation and testing of the report that is required in connection with the retrospective review. The commenter suggested that so long as the Financial Institution is working towards creating and testing the process, it should be able to use the exemption. As there is not a specified form of the report, the Department does not

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<sup>135</sup> Another commenter stated that the retrospective review should be required only once every three years. The Department has not adopted this suggestion. A review that is conducted as infrequently as once every three years would be unlikely to identify compliance concerns within a reasonable amount of time so as to prevent more systemic violations.

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believe an additional transition period is warranted. Because the report is annual and retrospective, preparation of the first report would not need to begin until at least one year after the exemption's effective date, and the report does not need to be completed for an additional six months after that. The Department believes this will give the Financial Institution sufficient time to create and test its reporting methods. Furthermore, Financial Institutions that are subject to the FINRA regulation should already be conducting a similar type of review. The Department believes it would be inconsistent with the principles and protective nature of the exemption to further delay implementation of the retrospective review.

One commenter addressed the interaction of banking law with the requirement in Section II(d)(5) to provide the report of the retrospective review, the certification and supporting data available to the Department. The commenter stated that a provision of the National Bank Act, 12 U.S.C. § 484, prohibits any person from exercising visitorial powers over national banks and federal savings associations except as authorized by federal law. The commenter requested that Section II(d)(5) be revised with the addition, at the end of the sentence, of, "except as prohibited under 12 U.S.C. § 484." Without conceding that the Department's authority is limited by this provision, the Department has made the requested edit.

One commenter indicated that the Department does not have jurisdiction to enforce the prohibited transaction rules for transactions involving IRAs, so the Department's interest in and access to the report of the retrospective review should be limited to Title I Plan transactions. As the agency with authority to grant prohibited

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transaction exemptions under the Code, the Department retains the ability to determine whether the conditions of an exemption are being met by reviewing records for the purpose of determining parties' compliance for IRAs.<sup>136</sup>

#### Senior Executive Officer Certification

While the proposal stated that the Financial Institution's chief executive officer (or equivalent) must certify the retrospective review, the final exemption provides, instead, that the retrospective review may be certified by any of the Financial Institution's Senior Executive Officers. The exemption defines a "Senior Executive Officer" as any of the following: the chief compliance officer, the chief executive officer, president, chief financial officer, or one of the three most senior officers of the Financial Institution. In making this change, the Department accepts the views of a number of commenters that stated that the CEO should not be the only person who can provide a certification regarding the retrospective review. The Department does not believe that permitting the Financial Institution to choose whichever Senior Executive Officer it believes is most appropriate to perform the certification alters the protective nature of this condition. As commenters pointed out, other officers than the CEO, such as the chief compliance officer, may have more information, specific training, and be better able to understand the retrospective review. Further, no matter which Senior Executive Officer is selected to provide the certification, the definition of a Senior Executive Officer ensures that an

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<sup>136</sup> See Reorganization Plan No. 4 of 1978 and discussion *supra*.



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officer of sufficient authority within the Financial Institution will be held accountable for oversight of exemption compliance. In this way, the Department believes that requiring certification will help reinforce a culture of compliance within the Financial Institution.

One commenter raised concerns regarding the applicability of the CEO certification requirement in the banking regulatory environment, stating that this type of certification is unusual for bank CEOs. Another commenter worried more broadly that a CEO certification might interfere with other financial certifications required of the CEO or unduly burden corporate governance. The Department believes that allowing the certification to be performed by any Senior Executive Officer addresses these concerns while still preserving the protective nature of the condition.

Some commenters objected to the certification requirement as a whole. They argued that the certification is burdensome and increases liability exposure without necessarily improving compliance. Others asserted certification is not required under Regulation Best Interest or the NAIC Model Regulation. On the other hand, some commenters acknowledged the similar existing requirements under FINRA but argued the requirement would be duplicative or should be harmonized.

The certification provides an important protection of Retirement Investors by creating accountability for the retrospective review and report at an executive level within the Financial Institution. Without a requirement that a Senior Executive Officer be held accountable by certifying the review, there is no assurance that any person in the leadership of a Financial Institution will review or be aware of its contents. The Department is required to find that the exemption is protective of, and in the interests of,

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Plans and their participants and beneficiaries, and IRA owners. This condition is important to the Department's ability to make these required findings.

One commenter indicated that an exemption with the certification requirement would not be considered "deregulatory" as was stated in the proposal. The Department responds that the exemption as a whole is deregulatory because it provides a broader and more flexible means for investment advice fiduciaries to Plans and IRAs to engage in certain transactions that would otherwise be prohibited under Title I and the Code. Financial Institutions remain free to structure their business in a manner that complies with the statutes and their prohibitions, or to request an individual exemption tailored to their specific business.

Finally, one commenter requested that the Department state that signing the certification does not implicate personal liability for the signing officer under the Act. The Department responds that signing the certification would not, in and of itself, impact the officer's personal liability under the Act; any such liability would be based on the officer's status as a fiduciary, the Act's statutory framework, and other relevant facts and circumstances.

***Self-Correction – Section II(e)***

The Department has added a new Section II(e) to the exemption, under which Financial Institutions will be able to correct certain violations of the exemption. Under the new Section II(e), the Department will not consider a non-exempt prohibited transaction to have occurred due to a violation of the exemption's conditions, provided: (1) either the violation did not result in investment losses to the Retirement Investor or

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the Financial Institution made the Retirement Investor whole for any resulting losses; (2) the Financial Institution corrects the violation and notifies the Department via email to [IIAWR@dol.gov](mailto:IIAWR@dol.gov) within 30 days of correction; (3) the correction occurs no later than 90 days after the Financial Institution learned of the violation or reasonably should have learned of the violation; and (4) the Financial Institution notifies the persons responsible for conducting the retrospective review during the applicable review cycle, and the violation and correction is specifically set forth in the written report of the retrospective review.

While this section was not a part of the proposal, several commenters raised the issue of instituting a self-correction procedure as it related to the Department's proposal requiring a retrospective review. Commenters requested that the Department provide a means for Financial Institutions, acting in good faith, to avoid loss of the exemption for violations of the conditions. Some commenters focused on minor or technical violations, others on violations in connection with specific conditions, such as allowing a correction for failure to provide disclosures. Some pointed to existing methods of correction allowed by the Department and other regulators, including the Department's regulation under ERISA section 408(b)(2).<sup>137</sup> One commenter specified that there should be a correction process in connection with the retrospective review, because failure to include this could put Financial Institutions in a difficult position of having discovered technical

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<sup>137</sup> 29 C.F.R. § 2550.408b-2(c)(1)(vii).

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violations but not being able to cure them without being subject to an excise tax for the prohibited transaction.

Upon consideration of the comments, the Department determined to provide this self-correction procedure. Although many commenters cited minor or technical violations, the Department does not view violations of any condition of the exemption as necessarily minor or technical. Accordingly, the section allows for correction even if a Retirement Investor has suffered investment losses, provided that the Retirement Investor is made whole. The Department believes that the self-correction provision will provide Financial Institutions with an additional incentive to take the retrospective review process seriously, timely identify and correct violations, and use the process to correct deficiencies in their policies and procedures, so as to avoid potential future penalties and lawsuits.

### ***Eligibility – Section III***

Section III of the exemption identifies circumstances under which an Investment Professional or Financial Institution will become ineligible to rely on the exemption for a period of 10 years. The grounds for ineligibility involve certain criminal convictions or certain egregious conduct with respect to compliance with the exemption. Ineligible parties may rely on an otherwise available statutory exemption or administrative class exemption, or the parties can apply for an individual prohibited transaction exemption from the Department. This will allow the Department to give special attention to parties with certain criminal convictions or with a history of egregious conduct regarding compliance with the exemption.

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Many commenters expressed concern that the conditions of the proposed exemption were not sufficiently enforceable to provide meaningful protections. Commenters noted that, unlike the Best Interest Contract Exemption granted in connection with the 2016 fiduciary rule, this exemption did not include a contract or other means of making the Impartial Conduct Standards enforceable. Therefore, IRA owners would not have a mechanism to enforce the requirements of the exemption, and the Department lacks direct enforcement authority over Plans not covered by Title I. Even with respect to Retirement Investors in ERISA-covered Plans, some commenters described the structure of the exemption as effectively allowing the financial services industry to self-regulate; they said the exemption would permit the “fox to guard the henhouse.” One commenter specifically criticized the proposed exemption’s eligibility provision as too weak to prevent or punish violations of the exemption. Other commenters were concerned that the eligibility provision did not provide any incentive for Financial Institutions to comply with the requirements of the exemption.

Other commenters objected to the exemption including any eligibility provision, arguing that the Department’s investigative authority and existing consequences for prohibited transactions are sufficient. Some raised concerns that the exemption’s eligibility provision has no basis in the statute and may be unconstitutional. Some acknowledged that the Department’s QPAM class exemption has a similar provision

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related to criminal convictions, but one commenter argued this too, is impermissible.<sup>138</sup>

Some commenters cited the Fifth Circuit’s *Chamber* opinion as support for the position that the eligibility provision impermissibly expands the Department’s enforcement authority over IRAs. One commenter indicated that the eligibility provision would only serve to increase compliance complexity, costs, and burdens, along with compliance uncertainty, under the exemption.

The Department has considered comments on the eligibility provision in Section III and has adopted it generally as proposed, but with non-substantive revisions.<sup>139</sup> The Department disagrees with commenters that expressed the view that the exemption is essentially self-regulatory and that the Department should not proceed with the exemption because it lacks an express enforcement mechanism for IRA owners. The Department believes that the eligibility provision will encourage Financial Institutions and Investment Professionals to maintain an appropriate focus on compliance with legal requirements and with the exemption, and, therefore, it has not eliminated them as overly burdensome, as suggested by a commenter. The Department intends to use its investigative, enforcement, and referral authority to enforce compliance with the exemption, and it will impose ineligibility on Financial Institutions or Investment

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<sup>138</sup> See PTE 84-14, Class Exemption for Plan Asset Transactions Determined by Independent Qualified Professional Asset Managers, 49 FR 9494 (Mar. 13, 1984) as corrected at 50 FR 41430 (Oct. 10, 1985), as amended at 67 FR 9483 (Mar. 1, 2002), 70 FR 49305 (Aug. 23, 2005), and 75 FR 38837 (July 6, 2010).

<sup>139</sup> As described in more detail below, all references to the “Office of Exemption Determinations” have been replaced with references to the “Department.”

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Professionals that demonstrate the type of compliance issues described in the exemption.

The Department notes that, in developing the exemption, it was mindful of the Fifth Circuit's *Chamber* opinion holding that the Department did not have authority to include certain contract requirements in the new exemptions enforceable by IRA owners granted as part of the 2016 fiduciary rulemaking. The Department's approach was designed to avoid any potential for disruption in the market for investment advice that may occur related to a contract requirement.

The Department disagrees that this eligibility provision is problematic simply because only one other class exemption includes this condition. It is the responsibility of the Department to craft exemptions to ensure they are protective of and in the interests of plans and plan participants. The conditions in the Department's exemptions are designed to address the conflicts of interest raised by the transactions covered by the exemption. The Department has determined that limiting eligibility in this manner serves as an important safeguard in connection with this very broad grant of relief from the self-dealing prohibitions of ERISA and the Code in this exemption.

The specific provision governing eligibility and the comments received on the provision are discussed in the next sections.

### ***Criminal Convictions***

An Investment Professional or Financial Institution will become ineligible upon the conviction of any crime described in ERISA section 411 arising out of provision of advice to Retirement Investors, except as described below. Crimes described in ERISA section 411 are likely to directly contravene the Investment Professional's or Financial

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Institution's ability to maintain a high standard of integrity and will cast doubt on their ability to act in accordance with the Impartial Conduct Standards. The Department intends that the phrase "arising out of the provision of advice to Retirement Investors" be interpreted broadly to include, for example, a Financial Institution or Investment Professional embezzling money from the account of a Retirement Investor to whom they provide or provided investment advice.

An Investment Professional will automatically become ineligible after a criminal conviction in ERISA section 411 arising out of provision of advice to Retirement Investors. However, a Financial Institutions with such a criminal conviction may submit a petition to the Department and seek a determination that continued reliance on the exemption would not be contrary to the purposes of the exemption. Petitions must be submitted within 10 business days of the conviction to the Department by e-mail at [IIAWR@dol.gov](mailto:IIAWR@dol.gov).

Following submission of the petition, the Financial Institution has the opportunity to be heard, in person or in writing or both. Because of the 10-business day timeframe for submitting a petition, the Department does not expect the Financial Institution to set forth its entire position or argument in its initial petition. The opportunity to be heard in person will allow the Financial Institution to address the facts and circumstances more fully. The opportunity to be heard will be limited to one in-person conference unless the Department determines in its sole discretion to allow additional conferences.

The Department's determination as to whether to grant a Financial Institution's petition to continue relying on the exemption following a criminal conviction will be



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based solely on its discretion. In determining whether to grant the petition, the Department will consider the gravity of the offense; the relationship between the conduct underlying the conviction and the Financial Institution's system and practices in its retirement investment business as a whole; the degree to which the underlying conduct concerned individual misconduct, corporate managers, and/or policy; how recently the underlying conduct occurred and any related lawsuit; remedial measures taken by the Financial Institution upon learning of the underlying conduct; and such other factors as the Department determines in its discretion are reasonable in light of the nature and purposes of the exemption. The Department will consider whether any extenuating circumstances indicate that the Financial Institution should be able to continue to rely on the exemption despite the conviction. In sum, the Department will focus on the Financial Institution's ability to fulfill its obligations under the exemption for the protection of Retirement Investors.

Upon making a determination as to a Financial Institution's petition, the Department will provide a written determination to the Financial Institution that states the basis for the determination. Denial of a Financial Institution's petition will not necessarily indicate that the Department will not entertain a separate individual exemption request submitted by the same Financial Institution; however, any individual exemption is likely to be subject to additional protective conditions. The final exemption provides that Financial Institution will have 21 days after denial of the petition before becoming ineligible. This will allow Financial Institutions, and other Financial Institutions in the same Controlled Group, to assess their legal and operational options.

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Some commenters on the proposal expressed general agreement that a Financial Institution that is convicted of a crime should be ineligible for the exemption. One commenter believed there are due process concerns if ineligibility occurs at the time of conviction rather than allowing for an appeal. Other commenters stated that the Department can take action under ERISA section 411 to seek to disqualify an entity from acting as a fiduciary so a provision in the exemption is unnecessary.

The Department believes that the criminal basis for ineligibility is appropriately applied in the context of both Title I Plans and IRAs. Despite the availability of action under ERISA section 411, it is appropriate to condition further reliance on the broad relief in the exemption more directly on the lack of such convictions, without the Department having to take further action. The Department does not agree that the application of the crimes listed in ERISA section 411 would not be permitted by the Fifth Circuit's *Chamber* opinion. The 2016 fiduciary rule and related exemptions did not contain a comparable provision, and the Fifth Circuit did not address the issue. As part of its authority to craft exemptions and make findings under ERISA section 408(a) and Code section 4975(c)(2), the Department is permitted to impose reasonable protective conditions, including those related to the conduct of those entrusted with investors' funds. The Department does not view ERISA section 411 or the statutory penalties for exemption noncompliance as creating a negative inference that prohibits a criminal prohibition as part of this exemption, whether in the Title I or Code context, especially when both provisions share the same essential purpose. Further, the only consequence

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flowing from a violation of the criminal conviction provision of this exemption is the loss of eligibility to use the exemption; no further penalties attach.

The Department also does not believe that the eligibility provision raises due process issues. The exemption specifically entitles the Financial Institution to submit a petition informing the Department of the conviction and seeking a determination that the Financial Institution's continued reliance on the exemption would not be contrary to the purposes of the exemption. This process constitutes notice and an opportunity to be heard, and parties aggrieved by the denial of an exemption can appeal that final agency action under the Administrative Procedure Act. The Department also does not believe it is appropriate to defer ineligibility until the conclusion of an appeal because of the significant delay that an appeal may entail, during which time Retirement Investors' interests may be at risk.

The Department has also clarified, in response to another comment, that ineligible parties under this exemption may alternatively rely on a statutory exemption or an administrative class exemption, if one is available. Ineligible Financial Institutions may also request an individual exemption, subject to additional protective conditions as warranted, and with the same appeal rights.

### ***Conduct With Respect to Compliance with the Exemption***

Investment Professionals and Financial Institutions will also become ineligible if they are issued a written ineligibility notice from the Department stating that they (i) engaged in a systematic pattern or practice of violating the conditions of the exemption, (ii) intentionally violated the conditions of the exemption, or (iii) provided materially

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misleading information to the Department in connection with the Investment Professional's or Financial Institution's conduct under the exemption. These categories of noncompliance militate against the Investment Professional or Financial Institution continuing to rely on the broad prohibited transaction relief in the class exemption. Provided that a Financial Institution has established, maintained and enforced prudent policies and procedures as required by this exemption, a minor number of isolated violations of the conditions of the exemption does not constitute a systematic pattern or practice.

The exemption sets forth a process governing the issuance of the written ineligibility notice, as follows. Prior to issuing a written ineligibility notice, the Department will issue a written warning to the Investment Professional or Financial Institution, as applicable, identifying specific conduct that could lead to ineligibility, and providing a six-month opportunity to cure. At the end of the six-month period, if the Department determines that the conduct has persisted, it will provide the Investment Professional or Financial Institution with the opportunity to be heard, in person or in writing, before the Department issues the written ineligibility notice. If a written ineligibility notice is issued, it will state the basis for the determination that the Investment Professional or Financial Institution engaged in conduct warranting ineligibility. The final exemption provides that Financial Institution will have 21 days after the date of the written ineligibility notice before becoming ineligible. This will allow Financial Institutions, and other Financial Institutions in the same Controlled Group, to assess their legal and operational options.

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A number of commenters expressed opposition to this basis of ineligibility in the proposed exemption. Most of the opposition centered on the proposal's specific references to the Office of Exemption Determinations (OED) in determining ineligibility. Commenters stated that the standards in the exemption are not objective or detailed and asserted this could result in a violation of due process, inconsistency, and unfairness. Further, because of these concerns, one commenter requested an appeals process beyond OED and another requested the use of administrative law judges. Some commenters raised concerns about the QPAM exemption and a few commenters cited a GAO report regarding OED procedures as evidence that OED should not be permitted to oversee this process.<sup>140</sup> Some commenters cited a recent Supreme Court case, *Lucia v. SEC*, which they said struck down a similar structure.<sup>141</sup> Other commenters stated that this eligibility provision overstepped the Department's authority.

In response to commenters, the eligibility provision has been non-substantively revised to state that the Department will determine eligibility. This will ensure that the Department, acting under the direction of the Secretary of Labor, maintains full responsibility for eligibility determinations under the exemption. As laid out in the Reorganization Plan No. 4 of 1978, the Secretary of Labor has the authority to issue exemptions, oversee fiduciary conduct and prohibited transactions. Accordingly, the

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<sup>140</sup> Individual Retirement Accounts, Formalizing Labor's and IRS's Collaborative Efforts Could Strengthen Oversight of Prohibited Transactions, GAO-19-495 (June 2019), available at [www.gao.gov/assets/700/699575.pdf](http://www.gao.gov/assets/700/699575.pdf).

<sup>141</sup> 585 U.S. \_\_\_, 138 S.Ct. 2044 (2018).

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Department disagrees with those commenters who claim the Department lacks the appropriate authority, or is overstepping its role. On the contrary, the Department is acting squarely within the authority granted to it to issue regulations, rulings, opinions, and exemptions under Code section 4975. The Department believes that the eligibility provision does not need additional adjustments given that the exemption specifies an extensive process before a written ineligibility notice will be issued. The Department has clarified, in response to a comment, that ineligible parties under this exemption may alternatively rely on a statutory exemption or an administrative class exemption, if one is available.

The Department also disagrees with those commenters who claim that the ineligibility provision is too vague as to be meaningful. The exemption clearly states that an entity will be provided with a statement of the specific conduct at issue, and will be provided with a six-month period to cure the conduct. Commenters expressed concern that the Department did not provide a specific number of violations a Financial Entity may commit before such violations become egregious (and, therefore, disqualifying). The Department has crafted a principles-based exemption, and does not consider it appropriate to set forth all of the possible ways in which an entity may engage in egregious conduct. The Department continues to believe that providing entities with specific notice and an opportunity to cure better balances the issues at stake.

The Department also notes that, in connection with its earlier response to a commenter, clarifying that the scope of relief in this exemption extends to foreign

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affiliates of Financial Institutions,<sup>142</sup> so too does the application of the eligibility provision regarding egregious conduct with respect to compliance with the exemption. As that commenter indicated, including relief for foreign affiliates is important, given the increasingly global nature of retirement services. The Department agrees, and, therefore, impresses upon Financial Institutions the importance of ensuring proper oversight of foreign affiliates with respect to compliance with the conditions of the exemption. If a foreign affiliate performs services in connection with a transaction covered by this exemption, but does so in a manner that is in violation of the conditions of this exemption, this will subject the Financial Institution to possible ineligibility under Section III(a)(2).

### ***Scope of Ineligibility***

A Financial Institution's ineligibility would be triggered by its own conviction or receipt of a written ineligibility notice, or by the conviction or receipt of such a notice by another Financial Institution in the same Controlled Group. A Financial Institution is in the same Controlled Group with another Financial Institution if it would be considered in the same "controlled group of corporations" or "under common control" with the Financial Institution, as those terms are defined in Code section 414(b) and (c), in each case including the accompanying regulations. The Department is including in the eligibility provision other Financial Institutions in the same Controlled Group to ensure

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<sup>142</sup> See discussion on Scope of Relief - Section I, Affiliates and Related Entities.

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that a Financial Institution facing ineligibility for its actions affecting Retirement Investors cannot simply transfer its fiduciary investment advice business to another Financial Institution that is closely related and that also provides fiduciary investment advice to Retirement Investors, thus avoiding ineligibility entirely. The definition of Controlled Group is narrowly tailored to cover only other investment advice fiduciaries that share significant ownership. This definition ensures that a Financial Institution would not become ineligible based on the actions of an entity engaged in unrelated services that happens to share a small amount of common ownership.

The proposed exemption provided that a Financial Institution is in a Control Group with another Financial Institution if, directly or indirectly, the Financial Institution owns at least 80 percent of, is at least 80 percent owned by, or shares an 80 percent or more owner with, the other Financial Institution. If the Financial Institutions are not corporations, the proposal provided that ownership would be defined to include interests in the Financial Institution such as profits interest or capital interests in which, directly or indirectly, the Financial Institution owns at least 80 percent of, is at least 80 percent owned by, or shares an 80 percent or more owner with, the other Financial Institution. For purposes of this provision, the proposal provided if the Financial Institutions are not corporations, ownership would be defined to include interests in the Financial Institution such as profits interest or capital interests.

The Department stated in the proposal that the 80 percent threshold is consistent with the Code's rules for determining when employees of multiple corporations should be treated as employed by the same employer, citing Code section 414(b). The Department



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also sought comment on this approach. In response, one commenter asserted that different forms of ownership would make it difficult to determine how to apply the 80% threshold suggested. Accordingly, the Department revised the definition to directly incorporate both definitions in both Code section 414(b) and 414(c) which address these arrangements. The Department believes these provisions will provide a well-known frame of reference for Financial Institutions and avoid uncertainty as to how the definition will be applied.

A few other commenters opposed including Control Group members within the eligibility provision, as proposed. These commenters asserted that a common parent is not an indicator of any other connection between corporate entities; rather, these commenters stated that affiliates typically maintain different policies and procedures. One commenter asserted that conduct by the Financial Institution's affiliates may not relate to investment advice or conduct involving Title I Plans or IRAs. This commenter stated that affiliates typically maintain different compliance policies and procedures and a Financial Institution and its affiliates are managed by different officers and compliance staff. Another commenter asserted that a Financial Institution may not know of the conviction of another Financial Institution in the same Controlled Group within 10 business days. Another commenter stated that independent firms may have common ownership but different business models or professional culture.

The Department has not revised its approach in response to these comments. The eligibility provision and the definition of Controlled Group are narrowly drafted so that they identify conduct involving services to Retirement Investors, and also are limited to

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Financial Institutions, within the meaning of the exemption, that are Controlled Group members with a high level of common ownership. The Department continues to believe that the tailored definition of Controlled Group and provision that a Financial Institution becomes ineligible on the 10th business day after conviction ensures that there is a culture of compliance across the Controlled Group for entities engaging in this otherwise prohibited transaction. The Department notes that given the high level of ownership, it is not unreasonable for the Financial Institution be aware of the conviction of another Financial Institution in the same Controlled Group and it should not be difficult for Financial Institutions to keep track of such convictions. Accordingly, the Department has not adjusted the 10 business-day deadline.

### ***Period of Ineligibility***

The period of ineligibility under Section III is 10 years; however, the eligibility provision would apply differently to Investment Professionals and Financial Institutions. An Investment Professional that is convicted of a crime would become ineligible immediately upon the date the Investment Professional is convicted by a trial court, regardless of whether that judgment remains under appeal, or upon the date of the written ineligibility notice from the Department, as applicable.

Financial Institutions, on the other hand, would have a one-year winding down period after becoming ineligible, during which they may continue to rely on the exemption, as long as they comply with the exemption's other conditions during that year. The winding down period begins 10 business days after the date of the trial court's judgment, regardless of whether that judgment remains under appeal. Financial

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Institutions that timely submit a petition regarding the conviction would become ineligible 21 days after the date of a written notice of denial from the Department.

Financial Institutions that become ineligible due to conduct with respect to exemption compliance would become ineligible 21 days after the date of the written ineligibility notice from the Department and begin their winding down period at that point.

Financial Institutions or Investment Professionals that become ineligible to rely on this exemption may rely on a statutory or administrative class prohibited transaction exemption if one is available or may seek an individual prohibited transaction exemption from the Department. The Department encourages any Financial Institution or Investment Professional facing allegations that could result in ineligibility, or that otherwise determines it may need individual prohibited transaction relief, to begin the application process as soon as possible. An applicant is not guaranteed an individual exemption, even if one is proposed. If an exemption is proposed, the Department is required to provide notice and a period of public comment and to consider those comments before granting an exemption. If an individual exemption applicant becomes ineligible and the Department has not granted a final individual exemption, the Department will consider additional retroactive relief, consistent with its policy as set forth in 29 CFR 2570.35(d). Retroactive relief may require inclusion of additional exemption conditions.

#### ***Recordkeeping – Section IV***

Under Section IV of the exemption, Financial Institutions must maintain records for six years demonstrating compliance with the exemption. The Department generally

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includes a recordkeeping requirement in its administrative exemptions to ensure that parties relying on an exemption can demonstrate, and the Department can verify, compliance with the conditions of the exemption. Section IV requires that the records be made available, to the extent permitted by law, to any authorized employee of the Department or the Department of the Treasury.

To demonstrate compliance with the exemption, Financial Institutions are required to maintain, among other things, documentation of rollover recommendations; their written policies and procedures adopted pursuant to Section II(c); and the report of the retrospective review, certification, and supporting data. Except with respect to rollovers, the Department does not expect Financial Institutions to document the reason for every investment recommendation made pursuant to the exemption. However, documentation may be especially important for recommendations of particularly complex products or recommendations that might, on their face, appear inconsistent with the best interest standard.

One commenter supported the recordkeeping requirement as proposed but recommended extending the recordkeeping requirement to 10 years. The Department declines to extend the time period. The six-year time period is consistent with standard recordkeeping requirements imposed in many existing exemptions, and it is consistent with the statute of limitation set forth in ERISA section 413.

Other commenters opposed the scope of access to records in the proposed exemption. The proposal provided that records should be available for review by the following parties in addition to the Department: any fiduciary of a Plan that engaged in

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an investment transaction pursuant to this exemption; any contributing employer and any employee organization whose members are covered by a Plan that engaged in an investment transaction pursuant to this exemption; or any participant or beneficiary of a Plan, or IRA owner that engaged in an investment transaction pursuant to this exemption.

Several commenters stated that allowing parties other than the Department to review records would increase the burden placed on Financial Institutions. In particular, they expressed the view that parties might overwhelm Financial Institutions with requests for information in order to generate claims for use in litigation. Fear of potential litigation could, in turn, they argued, lead to a “culture of quiet” in which employees of Financial Institutions elect not to address compliance issues because of the fear of this disclosure.

In response to these comments, the Department has revised the final exemption’s recordkeeping provisions so that access is limited to the Department and the Department of the Treasury, although, in connection with this change, the Department has revised Section II(b) of the exemption, as described above, to provide Retirement Investors with documentation of the reasons that a rollover recommendation made to them was in their best interest. The Department accepts that Financial Institutions may have concerns about internal compliance records, particularly the record of their retrospective reviews, becoming widely accessible. However, the Department believes that it is important for the exemption to be conditioned on Retirement Investors receiving documentation of the reasons for rollover recommendations made to them, to allow them to carefully evaluate those important recommendations. The Department also notes that even if the exemption

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does not require disclosure of certain records, Financial Institutions would not be precluded from providing them voluntarily as a matter of customer relations.

One commenter raised concerns that the proposal's recordkeeping requirements were inconsistent with certain "visitorial powers" under banking law, discussed above. The Department notes that the exemption, as well as the proposal, contains the limiting language "to the extent permitted by law including 12 U.S.C. § 484," which the Department believes substantially addresses these concerns.

A few commenters also asserted that the Department should not be permitted to request records regarding IRA transactions because the Department does not have enforcement jurisdiction over IRAs, and under the Fifth Circuit's *Chamber* opinion, the records provision would be an impermissible attempt to usurp enforcement jurisdiction. In conjunction with this, one commenter suggested the Internal Revenue Service should be able to obtain records regarding IRAs. While the Department may lack certain enforcement jurisdiction with respect to IRAs, it does not lack the ability to issue exemptions to the prohibited transaction provisions under Code section 4975.<sup>143</sup> The Department has authority to grant prohibited transaction exemptions, as well as the associated authority to determine whether the conditions of its exemption are being met by reviewing records for the purpose of determining that compliance. The Department does not, based on those same grounds, agree that a recordkeeping requirement that

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<sup>143</sup> See supra note 6.

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impacts IRAs is inconsistent with the Fifth Circuit’s *Chamber* opinion, which did not specifically address the issue. However, the Department has added the Department of the Treasury, which includes the Internal Revenue Service, as an additional regulator that can obtain a Financial Institution’s records under the exemption.

Lastly, one commenter was concerned about the application of a 30-day requirement to notify the Department of a decision to withhold documents from parties other than the Department. Because the exemption has been modified to only provide for the Department’s and the Department of the Treasury’s review, the commenter’s concern has been addressed.

### ***Effective Date***

The exemption is effective 60 days after its publication in the Federal Register. This responds to several commenters who urged the Department to make the exemption available promptly. Some commenters requested that the exemption be effective immediately upon publication in the Federal Register, rather than after 60 days. Another commenter, however, suggested that the exemption should be effective no earlier than July 1, 2021, 180 days after the publication of the exemption, or 90 days after the end of the current public health emergency, because of market turmoil and COVID-19.

The Department has retained the 60 day effective date timeframe to permit transmittal of the exemption to Congress and the Comptroller General for review in accordance with the Congressional Review Act provisions of the Small Business Regulatory Enforcement Fairness Act of 1996 (5 U.S.C. 801 et seq.). As stated above, parties can continue to rely on FAB 2018-02 for one year following publication of the

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final exemption, so there will be a transition period for Financial Institutions to develop compliance structures. The Department has not delayed the effective date as suggested by one commenter. The Department believes that the exemption's conditions provide protections of Retirement Investors even in the event of market turmoil, and, therefore, a delay in the effective date is not in the interests of Retirement Investors.

### ***Procedural Issues***

Following the proposal, the Department received comments about the process it has followed in this exemption proceeding. Some commenters requested that the Department extend the proposed exemption's 30-day comment period. Many commenters also requested the Department hold a public hearing, which it did on September 3, 2020, although a few other commenters asserted that the procedure establishing the hearing was improper. Commenters in particular pointed to the more extensive comment period provided in the Department's 2016 fiduciary rulemaking.

The Department believes that its procedure with respect to the proposal was appropriate under applicable requirements, including the Administrative Procedure Act. The Department received and carefully reviewed 106 comments on the proposal. Further, the Department accommodated all requests by commenters to testify at the hearing, and this resulted in 21 organizations testifying. This hearing was broadcast publicly, and all interested parties were invited to watch the hearings. The hearings gave the Department time to hear oral testimony from these 21 different organizations, and question them on aspects of the comments and their testimony. Moreover, the general issues and concerns raised by the proposal have been subject to significant amounts of



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commentary and discussion between the Department and the public since October 2010.

In light of the narrower issues raised in the present exemption project as opposed to the 2016 fiduciary rulemaking, as well as the public record developed on the proposal, the Department does not believe that the shorter comment period indicates an insufficient opportunity for public comment.

### ***Reinsertion of the Five-Part Test for Investment Advice Fiduciary Status***

On the same day as the Department published the proposed exemption, the Department issued a technical amendment to 29 CFR 2510-3.21 instructing the Office of the Federal Register to remove language that was added in 2016 and reinsert the text of the 1975 regulation. The 1975 regulation established the five-part test for investment advice fiduciary status.

Many commenters on the Department's proposed exemption addressed the Department's technical amendment reinserting the five-part test. Some commenters supported the technical amendment, stating that it provides welcome certainty to the regulated community as to the current legal definition of an investment advice fiduciary. Some commenters indicated that the five-part test properly defines an investment advice fiduciary. Some expressed the view that reinsertion of the five-part test was the appropriate response to the Fifth Circuit's *Chamber* opinion.

Many commenters expressed significant opposition to the reinsertion of the five-part test via the technical amendment, and the five-part test in general. They stated that the five-part test was established before the prevalence of 401(k) plans and IRAs, and is now outdated and ill-suited to address the complex investment products offered in

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today's marketplace. They also said the five-part test is narrower than the statutory definition in Title I and the Code, which defines a fiduciary as anyone who "renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so."<sup>144</sup>

These commenters said despite the Department's preamble interpretation regarding rollovers, many rollovers would occur without the protections of a fiduciary standard.

Commenters criticized several of the individual elements of the five-part test. The "regular basis" prong in particular, they said, creates loopholes for financial professionals to avoid fiduciary status while holding themselves out as trusted advisers. Some commenters particularly pointed to transactions involving non-securities which they said can involve significant conflicts of interest and may often be considered one-time transactions. Commenters also stated that the regular basis prong will mean that advice to a plan sponsor regarding investment options in a Title I Plan will rarely be fiduciary advice, which will adversely affect Plan participants' investment options. The commenters also stated that disclaimers of a 'mutual agreement' or that the advice will serve as 'a primary basis' for investment decisions will be used to avoid application of the fiduciary standard. As a result of all these factors, the commenters said Retirement Investors would be harmed by unchecked conflicts of interest.

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<sup>144</sup> ERISA section 3(21)(A)(ii); Code section 4975(e)(3)(B).

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Some of the commenters raised legal arguments in connection with the technical amendment reinserting the five-part test. The commenters stated the Department had discretion as to whether to reinstate the five-part test, and, therefore, should have provided notice, economic analysis, and an opportunity for public comment before it took action.

While this exemption proceeding interprets aspects of the five-part test, including by providing a new interpretation as to how it applies to rollovers, this exemption has not put at issue the five-part test itself as codified at 26 CFR 54.4975-9 and 29 C.F.R. 2510.3-21. Thus, these comments are outside the scope of this exemption proceeding.

Additionally, as stated in its technical amendment, the five-part test was reinstated by the Fifth Circuit's decision in *Chamber*, not by any discretionary action of the Department. As a result of that decision, the 2016 fiduciary regulation and associated exemptions were vacated *in toto*. The Department merely directed the Office of the Federal Register to update the Code of Federal Regulations to correctly reflect current law.

Finally, as explained below regarding the need for this rulemaking, this exemption appropriately takes into account the reasoning in the Fifth Circuit's *Chamber* opinion and changes in the regulatory landscape that have occurred since the 2016 fiduciary rulemaking.

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## **Regulatory Impact Analysis**

### ***Executive Orders 12866 and 13563 Statement***

Executive Orders 12866<sup>145</sup> and 13563<sup>146</sup> direct agencies to assess all costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits (including potential economic, environmental, public health, and safety effects; distributive impacts; and equity). Executive Order 13563 emphasizes the importance of quantifying costs and benefits, reducing costs, harmonizing rules, and promoting flexibility.

Under Executive Order 12866, “significant” regulatory actions are subject to review by the Office of Management and Budget (OMB). Section 3(f) of the Executive Order defines a “significant regulatory action” as any regulatory action that is likely to result in a rule that may:

- (1) Have an annual effect on the economy of \$100 million or more or adversely and materially affect a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or State, local, or tribal governments or communities (also referred to as “economically significant”);
- (2) Create a serious inconsistency or otherwise interfere with an action taken or planned by another agency;

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<sup>145</sup> Regulatory Planning and Review, 58 FR 51735 (Oct. 4, 1993).

<sup>146</sup> Improving Regulation and Regulatory Review, 76 FR 3821 (Jan. 21, 2011).

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- (3) Materially alter the budgetary impacts of entitlement grants, user fees, or loan programs or the rights and obligations of recipients thereof; or
- (4) Raise novel legal or policy issues arising out of legal mandates, the President's priorities, or the principles set forth in the Executive Order.

The Department anticipates that this exemption is economically significant within the meaning of section 3(f)(1) of Executive Order 12866. Therefore, the Department provides the following assessment of the potential benefits and costs associated with this exemption. In accordance with Executive Order 12866, this exemption was reviewed by OMB.

The final exemption will be transmitted to Congress and the Comptroller General for review in accordance with the Congressional Review Act provisions of the Small Business Regulatory Enforcement Fairness Act of 1996 (5 U.S.C. 801 et seq.). Pursuant to the Congressional Review Act, OMB has designated this final exemption as a “major rule,” as defined by 5 U.S.C. 804(2), because it would be likely to result in an annual effect on the economy of \$100 million or more.

### ***Need for Regulatory Action***

Participants in individual participant-directed defined contribution Plans (DC Plans) and IRA investors are responsible for investing their retirement savings, and they often seek high quality, impartial advice from financial service professionals to make prudent investment decisions. This is especially true as the share of total plan participation attributable to Defined Contribution (DC) Plans continues to grow. In 2017, 83 percent of DC Plan participation was attributable to 401(k) Plans, and 98 percent of

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401(k) Plan participants were responsible for directing some or all of their account investments.<sup>147</sup>

Following the Fifth Circuit’s *Chamber* opinion, the Department issued a temporary enforcement policy under FAB 2018-02 and announced its intent to provide additional guidance in the future. Since then, as discussed earlier in this preamble, the regulatory landscape has changed as other regulators, including the SEC, have adopted enhanced conduct standards for financial services professionals.<sup>148</sup>

Some commenters claimed that the Department changed its previous position from its 2016 fiduciary rulemaking without providing detailed justification. In response to these comments, the Department more clearly specifies some of the factors that compelled it to take this action. First, the Department’s current action follows and is guided by the Fifth Circuit’s *Chamber* opinion decision that vacated the Department’s 2016 fiduciary rule and associated exemptions, *in toto*. The Department carefully studied the court’s decision and developed this exemption consistent with it. Second, the regulatory landscape has changed since the Department issued the 2016 fiduciary rule

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<sup>147</sup> *Private Pension Plan Bulletin Historic Tables and Graphs 1975–2017*, Employee Benefits Security Administration (Sep. 2018), [www.dol.gov/sites/dolgov/files/ebsa/researchers/statistics/retirement-bulletins/private-pension-plan-bulletin-historical-tables-and-graphs.pdf](http://www.dol.gov/sites/dolgov/files/ebsa/researchers/statistics/retirement-bulletins/private-pension-plan-bulletin-historical-tables-and-graphs.pdf).

<sup>148</sup> The SEC’s Regulation Best Interest went into effect June 30, 2020. Although not a regulatory agency, the NAIC approved revisions to Model Regulation 275 in February 2020 and recommended adoption by state insurance regulators. According to a commenter in the insurance industry, the updated NAIC’s Model Regulation 275 has been finalized in two states (Arizona and Iowa), and four others (Idaho, Kentucky, Ohio, and Rhode Island) have publicly stated their intention to pursue adoption in late 2020 or early 2021. Other commenters expect the updated NAIC Model Regulation to be adopted in a majority of states within the next two to three years. These commenters also stated that the Dodd-Frank Act requires adoption of the NAIC Model Regulation amendments within five years to maintain exclusive state regulation of fixed annuity and insurance products.

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and exemptions. At that time, no other regulators had adopted enhanced conduct standards of financial service professionals. Currently, other regulators such as the SEC and state insurance commissioners have adopted or are currently in the process of enhancing the conduct standards of financial service professionals. These developments encourage the Department to take these regulatory changes into account when taking this action.

For instance, at the Department's September 3, 2020, public hearing on the proposed exemption, a witness testified that financial services firms made fundamental changes in their business models for several years after the Department issued its 2016 fiduciary rule and the SEC issued Regulation Best Interest. Those changes include new commission and fee schedules, the elimination of certain products and services, and third-party revenue sources, modified compensation and incentive programs, and caps on mutual fund and annuity upfront fees and trailing commissions. Additionally, according to data in studies cited by some commenters, the Department's 2016 fiduciary rulemaking also correlated with financial service professionals transitioning to lower-fee products, which has remained the case even after the rulemaking was vacated by the Fifth Circuit, but when FAB 2018-02 was in effect.

In sum, the Department considered the changes in regulatory landscape, business practices, and product offerings as it developed this exemption. To the extent Financial Institutions have already implemented measures to mitigate conflicts of interest and reduce related investor harms, the benefits of this exemption will be reduced. Similarly, to the extent Financial Institutions have already incurred costs to comply with other

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regulators' actions and the Department's 2016 fiduciary rulemaking, the costs of this exemption also will be reduced. Accordingly, these changes are reflected in the baseline that the Department applies when it evaluates the benefits and costs associated with this exemption that are discussed below.

Given this background, the Department believes that it is appropriate to replace the relief provided in FAB 2018-02 with a permanent exemption. The exemption will provide Financial Institutions and Investment Professionals with broader, more flexible prohibited transaction relief than is currently available, while safeguarding the interests of Retirement Investors. Offering a permanent exemption based on FAB 2018-02 will provide certainty to Financial Institutions and Investment Professionals that currently may be relying on the temporary enforcement policy.

### ***Benefits***

This exemption will generate several benefits. It will provide Financial Institutions and Investment Professionals with flexibility to choose between this new exemption or existing exemptions, depending on their needs and business models. In this regard, the exemption will help preserve different business models, compensation arrangements, and products that meet different needs in the market. This can, in turn, help preserve the existing wide availability of investment advice arrangements and products for Retirement Investors. Furthermore, the exemption will provide certainty for Financial Institutions and Investment Professionals that opted to comply with the enforcement policy the Department announced in FAB 2018-02 to continue with, and build upon, that compliance approach. Further, the exemption will ensure that



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investment advice satisfying the Impartial Conduct Standards is widely available to Retirement Investors without interruption.

As described above, in FAB 2018-02, the Department announced a temporary enforcement policy that would apply until the issuance of further guidance. Its designation as “temporary” communicated its status as a transitional measure following the vacatur of the Department’s 2016 fiduciary rulemaking. FAB 2018-02 was not intended to represent a permanent approach for prohibited transaction relief. This is due in part to the fact that FAB 2018-02 allows Financial Institutions to avoid enforcement action by the Department, but it does not (and cannot) provide relief from private litigation related to prohibited transactions.

In addition to the more permanent relief it will provide, this exemption will have more specific conditions than FAB 2018-02, which requires only good faith compliance with the Impartial Conduct Standards. The conditions in the exemption are designed to support the provision of investment advice that meets the Impartial Conduct Standards. For example, the required policies and procedures and retrospective review work in concert with the Impartial Conduct Standards to help Financial Institutions comply with the standards that will protect Retirement Investors.

Some Financial Institutions may consider whether to rely on the Department’s existing exemptions rather than adopt the specific conditions in this new exemption. The existing exemptions generally condition relief on disclosure and cover narrowly tailored transactions and types of compensation arrangements as well as the parties that may rely on the exemption. For example, the existing exemptions were never amended to clearly

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cover third-party compensation arrangements, such as revenue sharing, that developed over time. Investment advice fiduciaries relying on some of the existing exemptions will be limited to the types of compensation that tend to be more transparent to Retirement Investors, such as commission payments.

For a number of reasons, Financial Institutions may decide to rely on this new exemption, instead of the Department's existing exemptions. First, this exemption is broadly available for a wide variety of investment advice transactions and compensation arrangements, which gives Financial Institutions greater flexibility and simplifies compliance. Additionally, Financial Institutions may determine that there is a marketing advantage to acknowledging their fiduciary status with respect to Retirement Investors, as required by the new exemption.

Some commenters questioned the effectiveness of this disclosure because investors may decline to read or not fully understand such disclosures. In response to these concerns, the Department strongly encourages Financial Institutions to design disclosures that are easy to understand and written in plain English. The Department has provided model language that Financial Institutions may use for this purpose. The Department believes this required disclosure will further help Retirement Investors to make informed investment decisions.

In addition, one study suggests that disclosure requirements sometimes directly affect disclosers' actions. It showed that disclosers sometimes made changes to their practices before sending disclosures to consumers, especially when corporate reputation is particularly important. For example, corporate managers concerned with protecting

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market share or reputation often introduced lines of healthy products or tightened corporate governance before the public responded.<sup>149</sup> This suggests that disclosures can be effective even when investors may not read or not fully understand them.

As the exemption will apply to multiple types of investment advice transactions, it will potentially allow Financial Institutions to rely on one exemption for investment advice transactions under a single set of conditions. This approach may allow Financial Institutions to streamline compliance, as compared to relying on multiple exemptions with multiple sets of conditions, resulting in a lower overall compliance burden for some Financial Institutions.

This exemption's alignment with other regulatory conduct standards can result in a reduction in overall regulatory burden as well. As discussed earlier in this preamble, the exemption was developed in consideration of other regulatory conduct standards. The Department envisions that Financial Institutions and Investment Professionals that have already developed, or are in the process of developing, compliance structures for

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<sup>149</sup> Mary Graham, *Democracy by Disclosure: The Rise of Technopopulism* (2002). When Congress required manufacturers to disclose how many pounds of toxic chemicals they released into the air, water, and land and required chief executives to sign off on these reports, some chief executives became aware of total toxic pollutions for the first time and publicly announced the future reductions at the same time or before they issued their reports. In response to the Nutrition Labeling and Education Act (NLEA), which mandated the uniform nutrition label, some food companies added healthier options. Furthermore, some food companies added healthier products before the NLEA was implemented but after enacted. (See Christine Moorman, *Market-Level Effects of Information: Competitive Responses and Consumer Dynamics*, *Journal of Marketing Research*, Vol. 35, No. 1 (Feb., 1998). Another experimental study shows that when advisors have a choice to accept or reject conflicts of interest, advisors who would have to disclose their conflict would more likely to reject conflicts of interest, so that they have nothing to disclose except the absence of conflicts. (See Sah, Sunita, and George Loewenstein. "Nothing to declare: Mandatory and voluntary disclosure leads advisors to avoid conflicts of interest." *Psychological science* 25.2 (2014): 575-584.).

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other regulators' standards will be able to rely on the new exemption while incurring less costs than they otherwise would if other regulators' compliance structures did not exist.

As discussed above, the Department believes that the exemption will provide significant protections for Retirement Investors. The exemption relies in large measure on Financial Institutions' reasonable oversight of Investment Professionals and their adoption of a culture of compliance. Accordingly, in addition to the Impartial Conduct Standards, the exemption includes conditions designed to support investment advice that meets those standards, such as the provisions requiring written policies and procedures, documentation of rollover recommendations, and retrospective review. However, the exemption will not expand Retirement Investors' ability to enforce their rights in court or create any new legal claims above and beyond those expressly authorized in Title I or the Code, such as through required contracts and warranty provisions.

Finally, this exemption provides that Financial Institutions and Investment Professionals with certain criminal convictions or that engage in egregious conduct with respect to compliance with the exemption would become ineligible to rely on the exemption, for a period of 10 years. Engaging in these types of conduct would suggest that the Financial Institution or Investment Professional is not able or willing to maintain a high standard of integrity and will cast doubt on their ability to act in accordance with the Impartial Conduct Standards. This will allow the Department to give special attention to parties with certain criminal convictions or with a history of egregious conduct regarding compliance with the exemption which should provide significant protections

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for Retirement Investors while preserving wide availability of investment advice arrangements and products.

Although the Department expects this exemption to generate significant benefits, it does not have sufficient data to quantify such benefits. However, the Department expects the benefits to justify the compliance costs associated with this exemption because it creates an additional pathway for Financial Institutions to comply with the prohibited transaction provisions in Title I and the Code. This new pathway is broader than existing exemptions, and, thus, applies to a wider range of transactions and compensation arrangements and products than the relief that is currently available. The Department anticipates that entities will generally take advantage of this exemptive relief only if it is less costly than other alternatives currently available, including avoiding prohibited transactions or complying with an existing exemption. The Department requested comments in the proposal about the specific benefits that may flow from the exemption and invited commenters to submit quantifiable data that would support or contradict the Department's expectations about benefits. In response, the Department received no comments or data that could help it quantify the benefits associated with this exemption.

### ***Costs***

To estimate compliance costs associated with the exemption, the Department considers the changed regulatory baseline. For example, the Department assumes affected entities will likely incur only incremental costs if they are already subject to another regulator's similar rules or requirements. Because this exemption is intended to

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align significantly with other regulators' rules and standards of conduct, the Department expects that satisfying the exemption conditions will not be unduly burdensome. The Department estimates that the exemption would impose costs of more than \$87.8 million in the first year and \$78.9 million in each subsequent year.<sup>150</sup> Over 10 years, the costs associated with the exemption would total approximately \$562 million, annualized to \$80.1 million per year (using a seven percent discount rate).<sup>151</sup> Using a perpetual time horizon (to allow the comparisons required under E.O. 13771), the annualized costs in 2016 dollars are \$57 million at a seven percent discount rate. These costs are broken down and explained below. More details are provided in the Paperwork Reduction Act section as well. The Department solicited any quantifiable data that would support or contradict any aspect of its analysis and received none.

The Department also requested comments on this overall estimate and the cost burdens across different entities. In response, the Department received several comments concerning its proposed cost burden analysis. After careful reviews of those comments,

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<sup>150</sup> These estimates rely on the Employee Benefits Security Administration's 2018 labor rate estimates. See *Labor Cost Inputs Used in the Employee Benefits Security Administration, Office of Policy and Research's Regulatory Impact Analyses and Paperwork Reduction Act Burden Calculation*, Employee Benefits Security Administration (June 2019), [www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/technical-appendices/labor-cost-inputs-used-in-ebsa-opr-ria-and-pra-burden-calculations-june-2019.pdf](http://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/technical-appendices/labor-cost-inputs-used-in-ebsa-opr-ria-and-pra-burden-calculations-june-2019.pdf).

<sup>151</sup> The costs would be \$682 million over 10-year period, annualized to \$79.9 million per year, if a three percent discount rate were applied.

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the Department revised its cost estimate upward from the proposed cost estimate. For example, in the proposal, the Department applied an hourly rate for compliance attorneys based on the U.S. Bureau of Labor Statistics' average attorney hourly rate.<sup>152</sup> Because this rate is significantly lower than the average senior compliance officer's hourly wage, one commenter noted that the wage suggested the Department believed such compliance activities would be handled by junior attorneys, rather than more senior compliance counsel. In response, the Department's new cost burden analysis relies on a higher hourly wage rate that reflects the hourly wage of senior compliance attorneys in the financial services sector.<sup>153</sup> Details of the comments and the Department's revised cost estimates are discussed below.

### ***Affected Entities***

As a first step in its analysis, the Department examines the entities likely to be affected by the exemption. The exemption will potentially impact SEC- and state-registered investment advisers (IAs), broker-dealers (BDs), banks, and insurance companies, as well as their employees, agents, and representatives. The Department

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<sup>152</sup> In the proposal, the Department used \$138.41 as an attorney's hourly rate. For more details about the Department's methodologies, see *Labor Cost Inputs Used in the Employee Benefits Security Administration, Office of Policy and Research's Regulatory Impact Analyses and Paperwork Reduction Act Burden Calculation*, Employee Benefits Security Administration (June 2019), [www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/technical-appendices/labor-cost-inputs-used-in-ebsa-opr-ria-and-pra-burden-calculations-june-2019.pdf](http://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/technical-appendices/labor-cost-inputs-used-in-ebsa-opr-ria-and-pra-burden-calculations-june-2019.pdf).

<sup>153</sup> In the final exemption, the Department used \$365.39 as an attorney's hourly rate. This is an hourly rate estimate for an in-house compliance counsel, obtained from the SEC's Regulation Best Interest Release, 84 FR at 33455, footnote 1304: hour for in-house compliance counsel. *Available at* [www.govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12164.pdf](http://www.govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12164.pdf).

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acknowledges that not all these entities will serve as investment advice fiduciaries to Plans and IRAs within the meaning of Title I and the Code. Additionally, because other exemptions are also currently available to these entities, it is unclear how widely Financial Institutions will rely upon this exemption and which firms are most likely to choose to rely on it. To err on the side of caution, the Department includes all entities eligible for this relief in its cost estimate. The Department solicited comments about which, and how many, entities would likely use this exemption. Although no commenters provided precise counts of entities that would use this exemption, many commenters expressed their support for an exemption that is broad and flexible enough to cover a wide range of transactions and circumstances. They further expressed their interest in consolidating multiple exemptions into one exemption to streamline compliance. As discussed earlier in this preamble, the Department clarified points raised by commenters and considered all comments in finalizing this exemption. Thus, the Department expects that this exemption will be widely used across different entities.

***Broker-Dealers (BDs)***

As of December 2018, there were 3,764 registered BDs. Of those, 2,766, or approximately 73.5 percent, reported retail customer activities, while 998 were estimated



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to have no retail customers.<sup>154</sup> The Department does not have information about how many BDs provide investment advice to Retirement Investors, which, as defined in the exemption include Plan fiduciaries, Plan participants and beneficiaries, and IRA owners. However, according to one compliance survey, about 52 percent of IAs provide services to retirement plans.<sup>155</sup> Assuming the same percentage of BDs provide advice to retirement plans, nearly 2,000 BDs will be affected by the exemption.<sup>156</sup> This exemption may also impact BDs that provide investment advice to Retirement Investors that are Plan participants or beneficiaries, or IRA owners, but the Department does not have a basis to estimate the number of these BDs. The Department assumes that such BDs would be considered as providing recommendations to retail customers under the SEC's Regulation Best Interest.

To continue providing investment advice to retirement plans with respect to transactions that otherwise would be prohibited under Title I and the Code, this group of BDs will be able to rely on the exemption.<sup>157</sup> Because BDs with retail customers are

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<sup>154</sup> Regulation Best Interest Release, 84 FR at 33407.

<sup>155</sup> *2019 Investment Management Compliance Testing Survey*, Investment Adviser Association (Jun. 18, 2019), [https://higherlogicdownload.s3.amazonaws.com/INVESTMENTADVISER/aa03843e-7981-46b2-aa49-c572f2ddb7e8/UploadedImages/about/190618\\_IMCTS\\_slides\\_after\\_webcast\\_edits.pdf](https://higherlogicdownload.s3.amazonaws.com/INVESTMENTADVISER/aa03843e-7981-46b2-aa49-c572f2ddb7e8/UploadedImages/about/190618_IMCTS_slides_after_webcast_edits.pdf).

<sup>156</sup> If this assumption is relaxed to include all BDs, the costs would increase by \$2.8 million for the first year.

<sup>157</sup> The Department's estimate of compliance costs does not include any state-registered BDs because the exception from SEC registration for BDs is very narrow. See *Guide to Broker-Dealer Registration*, Securities and Exchange Commission (Apr. 2008), [www.sec.gov/reportspubs/investor-](http://www.sec.gov/reportspubs/investor-)

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subject to the SEC’s Regulation Best Interest, they already comply with standards substantially similar to those set forth in the exemption.

### ***SEC-Registered Investment Advisers (IAs)***

As of December 2018, there were approximately 13,299 SEC-registered IAs.<sup>158</sup>

Generally, an IA must register with the appropriate regulatory authorities—the SEC or state securities authorities.<sup>159</sup> IAs registered with the SEC are generally larger than state-registered IAs, both in staff and in regulatory assets under management (RAUM).<sup>160</sup>

SEC-registered IAs that provide investment advice to retirement plans and other Retirement Investors would be directly affected by the exemption.

Some IAs are dual-registered as BDs. To avoid double counting when estimating compliance costs, the Department counted dually-registered entities as BDs and excluded

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publications/divisionsmarketregbdguidehtm.html.

<sup>158</sup> Form CRS Relationship Summary Release, 84 FR at 33564.

<sup>159</sup> Generally, a person that meets the definition of “investment adviser” under the Advisers Act (and is not eligible to rely on an enumerated exclusion) must register with the SEC, unless it: (i) is prohibited from registering under Section 203A of the Advisers Act, or (ii) qualifies for an exemption from the Act’s registration requirement. An adviser precluded from registering with the SEC may be required to register with one or more state securities authorities.

<sup>160</sup> After the Dodd-Frank Wall Street Reform and Consumer Protection Act, an IA with \$100 million or more in regulatory assets under management generally registers with the SEC, while an IA with less than \$100 million registers with the state in which it has its principle office, subject to certain exceptions. For more details about the registration of IAs, see *General Information on the Regulation of Investment Advisers*, Securities and Exchange Commission (Mar. 11, 2011), [www.sec.gov/divisions/investment/iaregulation/memoia.htm](http://www.sec.gov/divisions/investment/iaregulation/memoia.htm); see also *A Brief Overview: The Investment Adviser Industry*, North American Securities Administrators Association (2019), [www.nasaa.org/industry-resources/investment-advisers/investment-adviser-guide/](http://www.nasaa.org/industry-resources/investment-advisers/investment-adviser-guide/).

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them from the burden estimates of IAs.<sup>161</sup> Therefore, the Department estimates there to be 12,940 SEC-registered IAs, a figure produced by subtracting the 359 dually-registered IAs from the 13,299 SEC-registered IAs.

Similar to BDs, the Department assumes that about 52 percent of SEC-registered IAs provide investment advice to retirement plans.<sup>162</sup> Applying this assumption, the Department estimates that approximately 6,729 SEC-registered IAs currently provide investment advice to retirement plans. An inestimable number of IAs may provide advice only to Retirement Investors that are Plan participants or beneficiaries or IRA owners, rather than the workplace retirement plans themselves. These IAs are fiduciaries, and they already operate under standards substantially similar to those required by the exemption.<sup>163</sup> Accordingly, the exemption will pose no more than a nominal burden for these entities.

### ***State-Registered Investment Advisers***

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<sup>161</sup> The Department applied this exclusion rule across all types of IAs, regardless of registration (SEC registered versus state only) and retail status (retail versus nonretail).

<sup>162</sup> 2019 Investment Management Compliance Testing Survey, *supra* note 155.

<sup>163</sup> *SEC Standards of Conduct Rulemaking: What It Means for RIAs*, Investment Adviser Association (July 2019), <https://higherlogicdownload.s3.amazonaws.com/INVESTMENTADVISER/aa03843e-7981-46b2-aa49-c572f2ddb7e8/UploadedImages/resources/IAA-Staff-Analysis-Standards-of-Conduct-Rulemaking2.pdf>.

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As of December 2018, there were 16,939 state-registered IAs.<sup>164</sup> Of these state-registered IAs, 13,793 provide advice to retail investors, while 3,146 do not.<sup>165</sup> State-registered IAs tend to be smaller than SEC-registered IAs, both in RAUM and staff. For example, according to one survey of both SEC- and state-registered IAs, about 47 percent of respondent IAs reported 11 to 50 employees.<sup>166</sup> In contrast, an examination of state-registered IAs reveals about 80 percent reported only up to two employees.<sup>167</sup> According to one report, 64 percent of state-registered IAs manage assets under \$30 million.<sup>168</sup> A study by the North American Securities Administrators Association found that about 16 percent of state-registered IAs provide advice or services to retirement plans.<sup>169</sup> Based on this study, the Department assumes that 16 percent of state-registered IAs provide investment advice to retirement plans. Thus, the Department estimates that approximately 2,710 state-registered IAs provide advice to retirement plans and other Retirement Investors.

### ***Insurance Companies***

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<sup>164</sup> This excludes state-registered IAs that are also registered with the SEC or dual registered BDs.

<sup>165</sup> Form CRS Relationship Summary Release.

<sup>166</sup> 2019 Investment Management Compliance Testing Survey, *supra* note 155.

<sup>167</sup> *2019 Investment Adviser Section Annual Report*, North American Securities Administrators Association (May 2019), [www.nasaa.org/wp-content/uploads/2019/06/2019-IA-Section-Report.pdf](http://www.nasaa.org/wp-content/uploads/2019/06/2019-IA-Section-Report.pdf).

<sup>168</sup> *2018 Investment Adviser Section Annual Report*, North American Securities Administrators Association (May 2018), [www.nasaa.org/wp-content/uploads/2018/05/2018-NASAA-IA-Report-Online.pdf](http://www.nasaa.org/wp-content/uploads/2018/05/2018-NASAA-IA-Report-Online.pdf).

<sup>169</sup> 2019 Investment Adviser Section Annual Report, *supra* note 167.

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The exemption will affect insurance companies, which primarily are regulated by states. No single regulator records a national-level count of insurance companies. Although state regulators track insurance companies, the total number of insurance companies cannot be calculated by aggregating individual state totals because individual insurance companies often operate in multiple states. However, the NAIC estimates there were approximately 386 insurance companies directly writing annuities in 2018. Some of these insurance companies may not sell any annuity contracts in the IRA or Title I retirement plan markets.<sup>170</sup> Furthermore, insurance companies can rely on other existing exemptions instead of this exemption. Some insurance industry commenters questioned whether the Department's existing exemptions offer realistic alternatives. In response to these concerns, the Department clarified earlier in this preamble that insurance companies can rely on other existing exemptions if such exemptions better fit their current business models. In the proposal, the Department invited comments about how many insurance companies would use this exemption. No commenters provided data that could help the Department more precisely quantify the number of insurance companies that will rely on this exemption or the associated compliance costs. Due to lack of data, the Department

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<sup>170</sup> One comment letter from the insurance industry stated that about half of annuity products sold by insurance agents were IRA or tax-qualified products. This suggests that fewer than 386 of the insurers included in this analysis will be affected by this exemption. However, the comment did not provide data quantifying the number of insurers likely to be affected by or likely to use this exemption.

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includes all 386 insurance companies in its cost estimate, although this likely presents an upper bound.

### ***Banks***

There are 5,066 federally insured depository institutions in the United States.<sup>171</sup>

Banks will be permitted to act as Financial Institutions under the exemption if they or their employees are investment advice fiduciaries with respect to Retirement Investors.

The Department nevertheless believes that most banks will not be affected by the exemption for the reasons discussed below.

The Department understands that banks most commonly use “networking arrangements” to sell retail non-deposit investment products (RNDIPs), including, among other products, equities, fixed-income securities, exchange-traded funds, and variable annuities.<sup>172</sup> Under such arrangements, bank employees are limited to performing only clerical or ministerial functions in connection with brokerage transactions. However, bank employees may forward customer funds or securities and may describe, in general

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<sup>171</sup> The FDIC reports there are 4,430 Commercial banks and 636 Savings Institutions (thrifts) for 5,066 FDIC- Insured Institutions as of June 30, 2020. For more details, see *Statistics at a Glance*, Federal Deposit Insurance Corporation (Jun 30, 2020), [www.fdic.gov/bank/statistical/stats/2020jun/industry.pdf](http://www.fdic.gov/bank/statistical/stats/2020jun/industry.pdf).

<sup>172</sup> For more details about “networking arrangements,” see *Conflict of Interest Final Rule, Regulatory Impact Analysis for Final Rule and Exemptions*, U.S. Department of Labor (Apr. 2016), [www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/completed-rulemaking/1210-AB32-2/ria.pdf](http://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/completed-rulemaking/1210-AB32-2/ria.pdf). Financial Institutions that are broker-dealers, investment advisers, or insurance companies that participate in networking arrangements and provide fiduciary investment advice would be included in the counts in their respective sections.

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terms, the types of investment vehicles available from the bank and BD under the arrangement. Similar restrictions exist with respect to bank employees' referrals of insurance products and IAs. Because of these limitations, the Department believes that in most cases such referrals will not constitute fiduciary investment advice within the meaning of the exemption. Due to the prevalence of banks using networking arrangements for transactions related to RNDIPs, the Department believes that most banks will not be affected with respect to such transactions.<sup>173</sup>

The Department does not have sufficient data to estimate the costs to banks of any other investment advice services, because it does not know how frequently banks use their own employees to perform activities that would be otherwise prohibited. The Department invited comments on the magnitude of such costs and solicited data that would facilitate their quantification in the proposal. No comments expressly discussed costs to banks nor provided data for the Department to quantify the compliance burden, if any, imposed on banks.

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<sup>173</sup> A comment letter from the banking industry described various interactions with customers, including those related to RNDIP and IRA investment programs. According to this commenter, there are generally two types of bank IRA investment programs available for retirement customers: (i) customer-directed bank IRA-CD and other bank deposit programs, and (ii) bank discretionary IRA programs. This commenter stated that they believe neither program would be required to rely on the exemption, which implies that most banks will not be affected by this exemption.

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### *Costs Associated with Disclosures*

The Department estimates the compliance costs associated with the exemption's disclosure requirement will be approximately \$2 million in the first year and \$0.2 million per year in each subsequent year.<sup>174</sup>

Section II(b) of the exemption requires Financial Institutions to acknowledge, in writing, their status as fiduciaries under Title I and the Code, as applicable. In addition, Financial Institutions must furnish a written description of the services they provide and any material conflicts of interest. For many entities, including IAs, this condition will impose only modest additional costs, if any at all. Most IAs already disclose their status as a fiduciary and describe the types of services they offer in Form ADV. As of June 30, 2020, BDs with retail investors are also required to provide disclosures about services provided and conflicts of interest on Form CRS and pursuant to the disclosure obligation in Regulation Best Interest. Even among entities that currently do not provide such disclosures, such as insurance companies and some BDs, the Department believes that developing disclosures required in this exemption will not substantially increase costs because the required disclosures are clearly specified and limited in scope.

Not all entities will decide to use the exemption. Some may instead rely on other existing exemptions that better align with their business models. However, for this cost

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<sup>174</sup> Except where specifically noted, all cost estimates are expressed in 2019 dollars throughout this document.



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estimation, the Department assumes that all eligible entities will use the exemption and incur, on average, modest costs.

The Department estimates that developing disclosures that acknowledge fiduciary status and describe the services offered and any material conflicts of interest will cost regulated parties approximately \$1.9 million in the first year.<sup>175</sup>

The Department estimates that it will cost Financial Institutions about \$0.2 million to print and mail required disclosures to Retirement Investors, but it assumes most required disclosures will be electronically delivered to Retirement Investors.<sup>176</sup> The

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<sup>175</sup> A written acknowledgment of fiduciary status would cost approximately \$0.6 million, while a written description of the services offered and any material conflicts of interest would cost another \$1.3 million. The Department assumes that 11,782 Financial Institutions, comprising 1,957 BDs, 6,729 SEC-registered IAs, 2,710 state-registered IAs, and 386 insurers, are likely to engage in transactions covered under this exemption. For a detailed description of how the number of entities is estimated, see the Paperwork Reduction Act section, below. The \$0.6 million cost associated with a written acknowledgment of fiduciary status is calculated as follows. The Department assumes that it will take each retail BD firm 15 minutes, each nonretail BD or insurance firm 30 minutes, and each registered IA five minutes to prepare a disclosure conveying fiduciary status at an hourly labor rate of \$365.39, resulting in cost burden of \$584,130. Accordingly, the estimated per-entity cost ranges from \$30.45 for IAs to \$182.7 for non-retail BDs and insurers. The \$1.3 million costs associated with a written description of the services offered and any material conflicts of interest are calculated as follows. The Department assumes that it will take each retail BD or IA firm five minutes, each small nonretail BD or small insurer 60 minutes, and each large nonretail BDs or larger insurer five hours to prepare a disclosure conveying services provided and any conflicts of interest at an hourly labor rate of \$365.39, resulting in cost burden of \$1,348,628. Accordingly, the estimated per-entity cost ranges from \$30.45 for retail broker-dealers and IAs to \$182.7 for large non-retail BDs and insurers.

<sup>176</sup> The Department estimates that approximately 1.8 million Retirement Investors are likely to engage in transactions covered under this PTE, of which 8.1 percent are estimated to receive paper disclosures. Distributing paper disclosures is estimated to take a clerical professional one minute per disclosure, at an hourly labor rate of \$64.11, resulting in a cost burden of \$151,341. Assuming the disclosures will require two sheets of paper at a cost \$0.05 each, the estimated material cost for the paper disclosures is \$14,164. Postage for each paper disclosure is expected to cost \$0.55, resulting in a printing and mailing cost of \$92,063.

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Department assumes that approximately 92 percent of participants who roll over their plan assets to IRAs will receive required disclosures electronically.<sup>177</sup> According to one study, approximately 3.6 million accounts in defined contribution plans were rolled over to IRAs in 2019.<sup>178</sup> Of those, slightly less than half, 1.8 million, were rolled over by financial services professionals.<sup>179</sup> Therefore, prior to transactions necessitated by rollovers, participants are likely to receive required disclosures from their Investment Professionals. In some cases, Financial Institutions and Investment Professionals may send required disclosures to participants, particularly those with participant-directed defined contribution accounts, before providing investment advice.

The Financial Institution now must provide documentation of the specific reasons that any rollover recommendation is in the Retirement Investor's best interest to the Retirement Investor. The Department estimates and presents costs associated with documenting rollover recommendations in the section below. Beyond the cost associated with producing the documentation, Financial Institutions may incur additional costs to

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<sup>177</sup> The Department estimates approximately 56.4 percent of participants receive disclosures electronically based on data from various data sources including the National Telecommunications and Information Agency (NTIA). In light of the 2020 Electronic Disclosure Regulation, the Department estimates that additional 35.5 percent of participants receive their disclosures electronically. In total, 91.9 percent of participants are expected to receive disclosures electronically.

<sup>178</sup> *U.S. Retirement-End Investor 2020: Helping Participants Navigating Uncertainty*, The Cerulli Report (2020).

<sup>179</sup> *Id.*

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provide such documentation to Retirement Investors. The Department expects that once the Financial Institutions document rollover recommendations, any additional costs for providing the documentation, such as printing and mailing costs, will be somewhat modest.<sup>180</sup>

The Department sought further comments in the proposed RIA on the costs associated with the required disclosures. In response, a commenter argued that the associated hourly wage of a legal professional used in the Department's cost estimate did not correspond to that of a compliance counselor. The Department acknowledges the importance of taking into account the level of experience and specialization of legal professionals in charge of compliance testing. Accordingly, the Department updated its legal professional's hourly labor rate to reflect the typical compensation of those who provide such services to Financial Institutions.<sup>181</sup>

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<sup>180</sup> The costs associated with documenting rollover recommendations are estimated and discussed in more details below in the section entitled "Costs associated with rollover documentation." To avoid double-counting, this section only includes associated distribution costs of such documentation. As discussed above, the Department estimates that approximately 92 percent of Retirement Investors will receive disclosures electronically, eliminating printing and mailing costs. Thus, providing rollover documentation will increase costs by approximately \$240,000.

<sup>181</sup> The hourly wage estimate for an in-house compliance counsel was obtained from Regulation Best Interest Release, 84 FR at 33455, note 1304, [www.govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12164.pdf](http://www.govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12164.pdf).

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### ***Costs Associated with Written Policies and Procedures***

The Department estimates that developing policies and procedures prudently designed to ensure compliance with the Impartial Conduct Standards will cost approximately \$4.4 million in the first year.<sup>182</sup>

The estimated compliance costs reflect the different regulatory baselines under which various entities are currently operating. For example, IAs already operate under a fiduciary standard substantially similar to that required under the exemption,<sup>183</sup> and report how they address conflicts of interests in Form ADV.<sup>184</sup> Similarly, BDs subject to the SEC's Regulation Best Interest also operate under a standard that is substantially similar to the exemption. To comply fully with the exemption, however, these entities

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<sup>182</sup> The Department assumes that 11,782 Financial Institutions, comprising 1,957 BDs, 6,729 SEC-registered IAs, 2,710 state-registered IAs, and 386 insurers, are likely to engage in transactions covered under this exemption. For a detailed description of how the number of entities is estimated, see the Paperwork Reduction Act section, below. The Department assumes that it will take a legal professional, at an hourly labor rate of \$365.39, 22.5 minutes at each small retail BD, 45 minutes at each large retail BD, five hours at each small nonretail BD, 10 hours at each large nonretail BD, 15 minutes at each small IA, 30 minutes at each large IA, five hours at each small insurer, and 10 hours at each large insurer to meet the requirement. This results in a cost burden estimate of \$4,393,011. Accordingly, the estimated per-entity cost ranges from \$91.35 for small IAs to \$3,653.90 for large non-retail BDs and insurers. These compliance cost estimates are not discounted.

<sup>183</sup> See SEC Fiduciary Interpretation, 84 FR 33669.

<sup>184</sup> See *Form ADV*, 17 C.F.R. § 279.1 (1979). (Part 2A of Form ADV requires IAs to prepare narrative brochures that contain information such as the types of advisory services offered, fee schedules, disciplinary information, and conflicts of interest. For example, item 10.C of part 2A asks IAs to identify if certain relationships or arrangements create a material conflict of interest, and to describe the nature of the conflict and how to address it. If an IA recommends or selects other IAs for its clients, and receives compensation directly or indirectly from those advisers that creates a material conflict of interest, or has other business relationships with those advisers that create a material conflict of interest, an adviser must describe these practices, discuss the material conflicts of interest these practices create, and how the adviser addresses them. See Item 10.D of Part 2A of Form ADV.)

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may need to review and amend their existing policies and procedures. These additional steps will impose additional, but not substantial, costs at the Financial Institution level.

Insurers and non-retail BDs currently operating under a suitability standard in most states and largely relying on transaction-based forms of compensation, such as commissions, will be required to establish written policies and procedures that comply with the Impartial Conduct Standards if they choose to use this exemption. These activities will likely involve higher cost increases than those experienced by IAs and retail BDs. To a large extent, however, the entities facing potentially higher costs will likely elect to continue to rely on other existing exemptions. In this regard, the burden estimates on these entities are likely overestimated to the extent that many of them would not use this exemption.

Smaller entities may have less complex business practices and arrangements than their larger counterparts, it may cost less for these entities to comply with the exemption. This is reflected in the compliance cost estimates presented in this economic analysis.

#### ***Costs Associated with Annual Report of Retrospective Review***

Section II(d) of the exemption requires Financial Institutions to conduct an annual retrospective review reasonably designed to ensure that the Financial Institution is in compliance with the Impartial Conduct Standards and its own policies and procedures. Section II(d) further requires the institution to produce a written report on the review that is certified by a Senior Executive Officer of the institution. In the proposal, the Department required certification by the chief executive officer of the Financial Institution, however several comments stated that this requirement is overly burdensome

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and unnecessary. After careful deliberation, the Department changed the requirement to allow certification from a Senior Executive Officer, which is defined to include any of the following: the chief compliance officer, chief executive officer, president, chief financial officer, or one of the three most senior officers of the Financial Institution, to reduce any unnecessary burden. Furthermore, by having a Senior Executive Officer certify the report, any inadequacies or irregularities may be detected during the review process and addressed appropriately before becoming systematic failures.

Some commenters suggested that this requirement could create the perverse incentive for a Financial Institution to carefully craft the language in the report to avoid any suggestion that any violation has occurred or even that its compliance could be improved. These commenters were particularly concerned because the penalty of noncompliance is severe—loss of exemption and exposure to litigation. In response to these comments, the Department amended the rule to allow Financial Institutions to self-correct certain violations of the exemption by following the procedures specified in Section II(e). Furthermore, Section IV now requires Financial Institution to make records available, to the extent permitted by law, to any authorized employee of the Department and the Department of the Treasury, not to others.<sup>185</sup> The Department believes that these

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<sup>185</sup> In the proposal, Section IV required that the records be made available to (1) any authorized employee of the Department, (2) any fiduciary of a Plan that engaged in an investment transaction pursuant to this exemption, (3) any contributing employer and any employee organization whose members are covered by a Plan that engaged in an investment transaction pursuant to this exemption, or (4) any participant or beneficiary of a Plan or an IRA owner that engaged in an investment transaction pursuant to this exemption.

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changes will minimize any perverse incentives and encourage Financial Institutions to use the retrospective review process for its intended purposes—to (1) detect any business models creating conflicts of interests, (2) test the adequacies of the policies and procedures, (3) identify any compliance areas for improvements, and (4) update and modify its compliance system based on the review results. As a result, protection for Retirement Investors will be strengthened without imposing any unnecessary burden on Financial Institutions.

The Department estimates that this requirement will impose \$15.9 million in costs in the first year.<sup>186</sup> FINRA requires BDs to establish and maintain a supervisory system reasonably designed to facilitate compliance with applicable securities laws and

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<sup>186</sup> The Department assumes that 794 Financial Institutions, comprising 20 BDs, 538 SEC-registered IAs, 217 state-registered IAs, and 20 insurers, would be likely to incur costs associated with producing a retrospective review report. The Department estimates it will take a legal professional, at an hourly labor rate of \$365.39, five hours for small firms and ten hours for large firms to produce a retrospective review report, resulting in an estimated cost burden of \$2,569,337. The per-entity cost estimate ranges from \$1,826.95 for small entities to \$3,653.9 for large entities. In addition, the Department assumes that 11,782 Financial Institutions, comprising 1,957 BDs, 6,729 SEC-registered IAs, 2,710 state-registered IAs, and 386 insurers, would be likely to incur costs associated with adding and modifying this report. The Department estimates it will take a legal professional one hour for small firms and two hours for large firms to add and modify the report, resulting in an estimated cost burden of \$7,573,614. The estimated per-entity cost ranges from \$365.39 for small entities to \$730.78 for large entities. Lastly, the Department also assumes that 9,845 Financial Institutions, comprising 20 BDs, 6,729 SEC-registered IAs, 2,710 state-registered IAs, and 386 insurers, would be likely to incur costs associated with reviewing and certifying the report. The Department estimates it will take a certifying officer two hours for small firms and four hours for large firms to review the report and certify the exemption, resulting in an estimated cost burden of \$5,750,451. The estimated per-entity cost ranges from \$331.26 for small entities to \$584.12 for large entities. For a detailed description of how the number of entities for each cost burden is estimated, see the Paperwork Reduction Act section.

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regulations,<sup>187</sup> to test the supervisory system, and to amend the system based on the testing.<sup>188</sup> Furthermore, the BD's chief executive officer (or equivalent officer) must annually certify that it has processes in place to establish, maintain, test, and modify written compliance policies and written supervisory procedures reasonably designed to achieve compliance with FINRA rules.<sup>189</sup>

Many insurance companies are already subject to similar standards.<sup>190</sup> For instance, the NAIC's Model Regulation contemplates that insurance companies establish a supervision system that is reasonably designed to comply with the Model Regulation and annually provide senior management with a written report that details findings and recommendations on the effectiveness of the supervision system.<sup>191</sup> States that have adopted the Model Regulation also require insurance companies to conduct annual audits and obtain certifications from senior managers. Based on these regulatory baselines, the Department believes the compliance costs attributable to this requirement will be modest.

SEC-registered IAs are already subject to Rule 206(4)-7, which requires them to adopt and implement written policies and procedures reasonably designed to ensure

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<sup>187</sup> *Rule 3110. Supervision*, FINRA Manual, [www.finra.org/rules-guidance/rulebooks/finra-rules/3110](http://www.finra.org/rules-guidance/rulebooks/finra-rules/3110).

<sup>188</sup> *Rule 3120. Supervisory Control System*, FINRA Manual, [www.finra.org/rules-guidance/rulebooks/finra-rules/3120](http://www.finra.org/rules-guidance/rulebooks/finra-rules/3120).

<sup>189</sup> *Rule 3130. Annual Certification of Compliance and Supervisory Processes*, FINRA Manual, [www.finra.org/rules-guidance/rulebooks/finra-rules/3130](http://www.finra.org/rules-guidance/rulebooks/finra-rules/3130).

<sup>190</sup> The previous NAIC Suitability in Annuity Transactions Model Regulation (2010) was adopted by many states before the newer NAIC Model Regulation was approved in 2020. Both previous and updated Model Regulations contain standards similar to that of the written report of retrospective review required under the proposed exemption.

<sup>191</sup> *Suitability in Annuity Transactions Model Regulation*, NAIC Regulation, Section 6.C.(2)(i). (The same requirement is found in the previous NAIC Suitability in Annuity Transactions Model Regulation (2010), Section 6.F.(1)(f).)



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compliance with the Advisers Act, and rules adopted thereunder, and review them annually for adequacy and the effectiveness of their implementation. Under the same rule, SEC-registered IAs must designate a chief compliance officer to administer the policies and procedures. However, they are not required to produce a report detailing findings from its audit. Nonetheless, many seem to voluntarily produce reports after conducting internal reviews. One compliance testing survey reveals that about 92 percent of SEC-registered IAs voluntarily provide an annual compliance program review report to senior management.<sup>192</sup> Relying on this information, the Department estimates that only eight percent of SEC-registered IAs advising retirement plans will start to produce a retrospective review report for this exemption.<sup>193</sup> The rest will incur some incremental costs to revise their existing review reports to fully satisfy the conditions related to this requirement.

Due to lack of data, the Department based the cost estimates associated with state-registered IAs on the assumption that eight percent of state-registered IAs advising retirement plans currently do not produce compliance review reports, and, thus, will incur costs associated with the oversight conditions in the exemption. As discussed above,

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<sup>192</sup> *2019 Investment Management Compliance Testing Survey*, Investment Adviser Association (Jun. 18, 2019), <https://www.acacompliancegroup.com/blog/2019-investment-management-compliance-testing-survey-results>.

<sup>193</sup> One commenter questioned the Department's assumption that only the eight percent of SEC- and state-registered IAs that do not currently produce reports will incur costs to produce them. According to this commenter, to fully comply with this exemption, most of the IAs that currently produce reports will need to somewhat modify their current reports. The Department incorporated this comment in this analysis and now assumed that all entities will likely see somewhat modest increases in their costs to make any additional entries in their reports. For more details, see the discussion later in this section.

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compared with SEC-registered IAs, state-registered IAs tend to be smaller in terms of RAUM and staffing, and, thus, may not have formal procedures in place to conduct retrospective reviews to ensure regulatory compliance. If that were often the case, the Department's assumption would likely underestimate costs. However, because state-registered IAs tend to be smaller than their SEC-registered counterparts, they tend to handle fewer transactions, limit the range of transactions they handle, and have fewer employees to supervise.<sup>194</sup> Therefore, the costs associated with establishing procedures to conduct internal retrospective reviews and produce compliance reports will likely be low.

One commenter mentioned that the Financial Institutions would likely revise their retrospective review reports to fully comply with the exemption even if they already produce the reports to comply with other regulators or to voluntarily improve their compliance system. The Department accepted this comment and incorporated in its compliance cost estimates potential burden increases on all entities relying on this exemption regardless of whether they already produce reports. However, the Department believes that this burden increase will be incremental, because the Department takes a principles-based approach in the exemption and provides Financial Institutions with flexibility to design and perform this review in a way that works best with their business model. Therefore, the Department expects Financial Institutions to develop and

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<sup>194</sup> An examination of state-registered IAs reveals about 80 percent reported only up to two employees. *See supra* note 167.

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implement procedures that are least burdensome and work with their current system to meet the standard set forth in the exemption.

According to another commenter, the Department did not estimate sufficient time for a certifying official to review and certify the retrospective review report. No commenters provided data the Department could use to more accurately estimate the burden associated with this requirement. Despite this lack of data, in response to these comments, the Department substantially increased its estimated burden associated with certification to dispel any misconception that this requirement is a mere formality.<sup>195</sup> The Department expects the certification process will facilitate on-going communications about compliance issues among senior executives and compliance staffers.

In sum, the Department estimates that the costs associated with the retrospective review requirement of the exemption will be approximately \$15.9 million in the first year.

#### ***Costs Associated with Rollover Documentation***

In 2019, slightly more than 3.6 million defined contribution plan accounts rolled over to an IRA, while 0.5 million accounts rolled over to other defined contribution

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<sup>195</sup> The Department assumes that it will take the certifying officer two hours (small firms) or four hours (large firms). If we assume that an average person reads 250 words per minute, this individual can read 30,000 words for two hours or 60,000 words for four hours. This implies a retrospective review report would be approximately 125 pages to 250 pages if this report is written in double space with 12 font size.

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plans.<sup>196</sup> Not all rollovers were managed by financial services professionals. As discussed above, slightly less than half of all rollovers from plans to IRAs were handled by financial services professionals, while the rest were self-directed.<sup>197</sup> Based on this information, the Department estimates slightly less than 1.8 million participants obtained advice from financial services professionals.<sup>198</sup> These rollovers tended to be larger than the self-directed rollovers. For example, in 2019, the average account balance of rollovers by financial services professionals was \$169,000, whereas the average account balance of self-directed rollovers was \$109,000.<sup>199</sup> Some of these rollovers likely involved financial services professionals who were not fiduciaries under the Department's five-part investment advice fiduciary test; thus, the actual number of rollovers affected by this exemption is likely lower than 1.8 million.

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<sup>196</sup> U.S. Retirement-End Investor 2020, *supra* note 178. (To estimate costs associated with documenting rollovers, the Department did not include rollovers from plans to plans because plan-to-plan rollovers are unlikely to be mediated by Investment Professionals. Also plan-to-plan rollovers occur far less frequently than plan-to-IRA rollovers. Thus, even if plan-to-plan rollovers were included in the cost estimation, the impact would likely be small.)

<sup>197</sup> *Id.*

<sup>198</sup> Another report suggested that a higher share, 75 percent, of households owning IRAs held their IRAs through Investment Professionals. The same report indicated that about half of traditional IRA-owning households with rollovers primarily relied on professional financial advisers for their rollover decisions. Note that this is household level data based on an IRA owners' survey, which was not particularly focused on rollovers. (See Sarah Holden & Daniel Schrass, *The Role of IRAs in US Households' Saving for Retirement, 2019, ICI Research Perspective*, vol. 25, no. 10 (Dec. 2019).)

<sup>199</sup> U.S. Retirement-End Investor 2020, *supra* note 178.

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Many commenters discussed various issues concerning rollovers in the five-part test context. In discussing rollovers, they sometimes distinguished new relationships between financial services professionals and investors from existing relationships. A close inspection of rollover data suggests that most rollovers do not occur in a vacuum. Specifically, 87 percent of rollovers handled by financial services professionals were executed by professionals with whom investors had an existing relationship, while only 13 percent were handled by new financial services professionals.<sup>200</sup> Furthermore, rollovers handled by existing financial service professionals were, on average, larger (\$174,000) than rollovers handled by new financial service professionals (\$132,000).<sup>201</sup>

The exemption requires Financial Institutions to document why a recommended rollover is in the best interest of Retirement Investors and provide that documentation to the Retirement Investor. As a best practice, the SEC already encourages firms to record the basis for significant investment decisions, such as rollovers, although doing so is not required under Regulation Best Interest.<sup>202</sup> In addition, some firms may voluntarily document significant investment decisions to demonstrate compliance with applicable law, even if not required.<sup>203</sup> Therefore, in the proposal, the Department stated that it expects many Financial Institutions already document significant decisions like rollovers.

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<sup>200</sup> *Id.*

<sup>201</sup> *Id.*

<sup>202</sup> Regulation Best Interest Release, 84 FR at 33360.

<sup>203</sup> According to a comment letter about the proposed Regulation Best Interest, BDs have a strong financial incentive to retain records necessary to document that they have acted in the best interest of clients, even if it is not required. Another comment letter about the proposed Regulation Best Interest suggests that BDs generally maintain documentation for suitability purposes.

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One commenter disagreed with the Department, stating that the Department's expectation was not realistic. However, a report commissioned by this commenter found that slightly more than half (52 percent) of asset management firms implementing Regulation Best Interest require their financial service professionals to document rollover recommendations. About half require documentation on all recommendations, while 56 percent require documentation for specific product recommendations, such as mutual funds and variable annuities.<sup>204</sup> Since Regulation Best Interest is now in effect, the Department expects that these Financial Institutions already are implementing these policies and procedures. Therefore, the Department assumes that 52 percent of Financial Institutions already require documentation for rollover recommendations, and, thus, will face no more than an incremental burden increase.<sup>205</sup> The remaining 48 percent will face a larger burden increase to implement new documentation procedures for rollover recommendations

In estimating costs associated with rollover documentations, the Department faces uncertainty in determining the number of rollovers affected by the exemption. The

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<sup>204</sup> *Regulation Best Interest: How Wealth Management Firms are Implementing the Rule Package*, Deloitte (Mar. 6, 2020). (This report is based on a survey given to 48 SIFMA member firms providing financial advice and related services to retail customers. The survey ended on December 2, 2019. Ninety percent of survey participant firms were dual registrants.)

<sup>205</sup> Therefore, the Department estimates that 52 percent of rollovers are done by financial professionals whose institutions already require such documentations.

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Department assumes that 67.4 percent of rollovers involving financial services professionals will be affected by the exemption.<sup>206</sup> Using this assumption, the estimated costs will be \$65 million per year.<sup>207</sup> The Department acknowledges that uncertainty still remain, because the lack of available data makes it difficult to estimate how many financial services professionals may act in a fiduciary capacity when making certain rollover recommendations that meet all elements of the five-part test, and, thus, will be affected by the exemption. The Department invited comments and data that could help it more precisely estimate the number of rollovers affected by the exemption and did not receive any comments countering its 67.4 percent assumption. Therefore, the Department maintained that assumption in its cost estimate.

In addition, the Department invited comments about financial services professionals' practices related to documenting rollover recommendations, particularly whether financial services professionals often use a form with a list of common reasons

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<sup>206</sup> In 2019, a survey was conducted on financial services professionals who hold more than 50 percent of their practice's assets under management in employer-sponsored retirement plans. These financial services professionals include both BDs and IAs. Forty-five percent of those surveyed indicated that they make a proactive effort to pursue IRA rollovers from their DC plan clients, and approximately 32.6 percent reported that they function in a non-fiduciary capacity. Therefore, the Department assumes that approximately 67.4 percent of financial service professionals serve their Plan clients as fiduciaries. (*See U.S. Defined Contribution 2019: Opportunities for Differentiation in a Competitive Landscape*, The Cerulli Report (2019).) The Department assumes that 67.4 percent of 1.8 million rollovers involving financial service professionals will likely be affected by this exemption.

<sup>207</sup> The Department assumes that financial advisors whose firms do not currently document rollover justifications will take, on average, 30 minutes per rollover to comply with this exemption. In contrast, financial advisors whose firms already require such documentation will take, on average, an additional five minutes per rollover to fully satisfy the requirement. The Department estimates over 335,000 burden hours in aggregate and slightly more than \$65 million assuming \$194.77 hourly rate for a personal financial advisor.

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for rollovers and how long, on average, it would take for a financial services professional to document a rollover recommendation. One commenter stated that the Department's proposed estimate was ambitious but reasonable, particularly for firms using compliance software to automate this process. This commenter, however, pointed out that the Department did not take into account the cost associated with purchasing compliance software. According to this commenter, the Department's low estimate for time spent documenting rollovers suggests that hasty and superficial analysis would satisfy this requirement. The Department fervently disagrees with this claim. As explained in the proposal, the Department did not expect this requirement to create an undue burden for the following reasons: (1) financial services professionals generally seek and gather information on investor profiles in accordance with other regulators' rules; and (2) as a best practice, financial professionals often discuss the basis for their recommendations and associated risks with their clients.<sup>208</sup> Because financial professionals already collect relevant information and discuss the basis for certain recommendations with clients, the Department believes that it would be relatively easy for them to document such information with respect to rollover recommendations.

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<sup>208</sup> FINRA, Reg BI and Form CRS Firm Checklist. Also Regulation Best Interest Release 4 FR 33360 (July 12, 2019).



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In addition, as discussed above, a report indicates that the majority of wealth management firms already require their financial service professionals to document rollover recommendations in response to Regulation Best Interest.<sup>209</sup> According to the same report, almost eight in ten firms that require such documentation use a predetermined list for this purpose.<sup>210</sup> Furthermore, approximately three out of four firms surveyed indicated that they would change their technology in response to Regulation Best Interest before it became effective.<sup>211</sup> Some Financial Institutions might have elected not to enhance their technologies in the wake of Regulation Best Interest because they recently updated their technology capabilities or decided to rely more on manual processes. This implies that most Financial Institutions are not likely to incur large technological costs, such as purchasing compliance software to comply with this exemption. Therefore, the Department assumes Financial Institutions that have not enhanced technology capabilities for other regulator's rule will take a mixed approach, combining current technology solutions with manual processes.

In sum, the Department estimates that Financial Institutions already requiring rollover documentation will face no more than a nominal burden increase, and only to the extent that their current compliance systems do not meet the requirements of this

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<sup>209</sup> *Regulation Best Interest: How Wealth Management Firms are Implementing the Rule Package*, Deloitte (Mar. 6, 2020). The participating firms in this study included dual-registrants, BDs and RIAs that were owned by or affiliated with banks, holding companies, insurance companies, and trust companies, as well as independent dually-registered BDs and RIAs. 90% of participating firms were dual registrants.

<sup>210</sup> *Id.*

<sup>211</sup> *Id.*

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exemption. Those firms currently not documenting rollover recommendations will likely face a larger, but still somewhat limited, burden increase due to the reasons discussed above.

### ***Costs Associated with Recordkeeping***

Section IV of the exemption requires Financial Institutions to maintain records demonstrating compliance with the exemption for six years. The Financial Institutions are required to make records available to the Department and the Department of the Treasury. Recordkeeping requirements in Section IV are generally consistent with requirements made by the SEC and FINRA.<sup>212</sup> In addition, the recordkeeping requirements correspond to the six-year period in section 413 of ERISA. The Department understands that many firms already maintain records, as required in Section IV, as part of their regular business practices. Therefore, the Department expects that the recordkeeping requirement in Section IV would impose a negligible burden.<sup>213</sup> The

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<sup>212</sup> The SEC's Regulation Best Interest amended Rule 17a-4(e)(5) requires that BDs retain all records of the information collected from or provided to each retail customer pursuant to Regulation Best Interest for at least six years after the date the account was closed or the date on which the information was last replaced or updated, whichever comes first. FINRA Rule 4511 also requires its members to preserve for a period of at least six years those FINRA books and records for which there is no specified period under the FINRA rules or applicable Exchange Act rules.

<sup>213</sup> The Department notes that the insurers most likely to use the exemption are generally not subject to the SEC's Regulation Best Interest and FINRA rules. The Department understands, however, that some states' insurance regulations require insurers to retain similar records for less than six years. For example, some states require insurers to maintain records for five years after the insurance transaction is completed. Thus, the recordkeeping requirement of the proposed exemption will likely impose an additional burden on the insurers that rely on this exemption. However, the Department expects most insurers to maintain records

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Department solicited comments regarding the recordkeeping burden in the proposed regulatory impact analysis but did not receive any comments disagreeing with the Department’s approach. Therefore, the Department took the same approach in this final regulatory impact analysis.

Table 1 provides a summary of the associated costs discussed.

<b>Table 1. Associated Costs Summary (\$ millions)</b>		
<b>Requirement</b>	<b>First Year</b>	<b>Subsequent Years</b>
Disclosures	\$2.2	\$0.2
Policies and Procedures	\$4.4	-
Rollover Documentation	\$65.3	\$65.3
Annual Report of Retrospective Review	\$15.9	\$13.3
<b>Total</b>	<b>\$87.8</b>	<b>\$78.9</b>

Note: Totals in table may not sum precisely due to rounding.

### ***Regulatory Alternatives***

The Department considered various alternative approaches in developing this exemption that are discussed below.

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electronically. Electronic storage prices have decreased substantially as cloud services become more widely available. For example, cloud storage space costs, on average, \$0.018 to \$0.021 per GB per month. Some estimate that approximately 250,000 PDF files or other typical office documents can be stored on 100GB. Accordingly, the Department believes that maintaining records in electronic storage for an additional year or two will not impose a significant cost burden on the affected insurers. (For more detailed pricing information of three large cloud service providers, *see* <https://cloud.google.com/products/calculator>, <https://azure.microsoft.com/en-us/pricing/calculator>, or <https://calculator.s3.amazonaws.com/index.html>.)

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### ***No New Exemption***

The Department considered merely leaving in place the existing exemptions that provide prohibited transaction relief for investment advice transactions. However, the existing exemptions generally apply to more limited categories of transactions and investment products, and they include conditions that are tailored to the particular transactions or products covered under each exemption. Therefore, under the existing exemptions, Financial Institutions may find it inefficient to implement advice programs for all the different products and services they offer. By providing a single set of conditions for a wide variety of investment advice transactions, this exemption allows the use and availability of investment advice for a variety of types of transactions in a manner that aligns with the conduct standards of other regulators, such as the SEC.

### ***Keeping FAB 2018-02***

Similarly, the Department considered keeping FAB 2018-02 in effect without finalizing this exemption. However, the Department rejected this alternative, because FAB 2018-02 was intended to be a temporary policy. Furthermore, replacing the relief provided in FAB 2018-02 with a permanent exemption will provide certainty and stability to Financial Institutions and Investment Professionals that may currently be relying on the temporary enforcement policy. The final exemption includes conditions designed to support investment advice that meets the Impartial Conduct Standards.

To provide a transition period for Financial Institutions relying on FAB 2018-02 to comply with the final exemption, the Department has announced that FAB 2018-02 will remain in effect place for one year after the final exemption is published. This will

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allow some Financial Institutions to defer incurring compliance costs associated with this exemption for a limited period. The cost estimates discussed in this regulatory impact analysis are overstated to the extent such costs are deferred. On the other hand, the benefits discussed in this analysis will not be fully realized to the extent that some Financial Institutions rely on FAB 2018-02 during the transition period. However, the Department believes that most Financial Institutions will begin complying with all the conditions of the final exemption before the end of the transition period, because it provides protection from private litigation and Financial Institutions will be better positioned in an extremely competitive market.

***Including an Independent Audit Requirement in the Exemption***

This exemption will require Financial Institutions to conduct a retrospective review, at least annually, designed to detect and prevent violations of the Impartial Conduct Standards and to ensure compliance with the policies and procedures governing the exemption. The exemption does not require that the review be conducted by an independent party, allowing Financial Institutions to self-review.

As an alternative to this approach, the Department considered requiring independent audits to ensure compliance under the exemption. The Department decided against this approach, because it is not convinced that an independent, external audit would yield sufficient benefits in addition to the results of the retrospective review to justify the increased cost, especially in the case of smaller Financial Institutions. This exemption instead requires that Financial Institutions provide a written report documenting the retrospective review, and supporting information, to the Department and

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within 10 business days of a request. The Department believes this requirement compels Financial Institutions to take the review obligation seriously, regardless of whether they choose to hire an independent auditor to conduct the review.

While the proposal stated that the Financial Institution’s chief executive officer (or equivalent) must certify the retrospective review, the final exemption provides, instead, that the retrospective review may be certified by any of the Financial Institution’s Senior Executive Officers. The exemption defines a “Senior Executive Officer” as any of the following: the chief compliance officer, the chief executive officer, president, chief financial officer, or one of the three most senior officers of the Financial Institution. In making this change, the Department accepts the views of a number of commenters that stated that the CEO should not be the only person who can provide a certification regarding the retrospective review.

### ***Paperwork Reduction Act***

In accordance with the Paperwork Reduction Act of 1995 (PRA 95) (44 U.S.C. 3506(c)(2)(A)), the Department solicited comments concerning the information collection request (ICR) included in the proposed exemption entitled “Improving Investment Advice for Workers & Retirees” (85 FR 40834). At the same time, the Department also submitted an information collection request (ICR) to the Office of Management and Budget (OMB), in accordance with 44 U.S.C. 3507(d). OMB filed a comment on the proposed rule with the Department on September 21, 2020, requesting the Department to provide a summary of comments received on the ICR and identify changes to the ICR made in response to the comments. OMB did not approve the ICR

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and requested the Department to file future submissions of the ICR under OMB control number 1210-0163.

The Department received no comments that specifically addressed the paperwork burden analysis of the information collections. Additionally, comments were submitted which contained information relevant to the costs and administrative burdens attendant to the proposed exemption. The Department considered such public comments in connection with making changes to the final exemption, analyzing the economic impact of the proposal, and developing the revised paperwork burden analysis summarized below.

In connection with publication of this final exemption, the Department is submitting an ICR to OMB requesting approval of a new collection of information under OMB Control Number 1210-0163. The Department will notify the public when OMB approves the ICR.

A copy of the ICR may be obtained by contacting the PRA addressee shown below or at *www.RegInfo.gov*.

*PRA Addressee:* Address requests for copies of the ICR to G. Christopher Cosby, Office of Regulations and Interpretations, U.S. Department of Labor, Employee Benefits Security Administration, 200 Constitution Avenue NW, Room N-5718, Washington, D.C., 20210. Telephone (202) 693-8425; Fax: (202) 219-5333; ([cosby.chris@dol.gov](mailto:cosby.chris@dol.gov)). These are not toll-free numbers. ICRs submitted to OMB also are available at *www.RegInfo.gov*.

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As discussed in detail below, the exemption requires Financial Institutions and/or their Investment Professionals to (1) make certain disclosures to Retirement Investors, (2) adopt written policies and procedures, (3) document the basis for rollover recommendations, (4) prepare a written report of the retrospective review, and (5) maintain records showing that the conditions have been met to receive relief under the exemption. These requirements are ICRs subject to the Paperwork Reduction Act. The Department has made the following assumptions in order to establish a reasonable estimate of the paperwork burden associated with these ICRs:

- Disclosures distributed electronically will be distributed via means already used by respondents in the normal course of business, and the costs arising from electronic distribution will be negligible;
- Financial Institutions will use existing in-house resources to prepare the disclosures, policies and procedures, rollover documentations, and retrospective reviews, and to maintain the recordkeeping systems necessary to meet the requirements of the exemption;



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- A combination of personnel will perform the tasks associated with the ICRs at an hourly wage rate of \$194.77 for a personal financial advisor, \$64.11 for mailing clerical personnel, and \$365.39 for a legal professional;<sup>214</sup>
- Approximately 11,782 Financial Institutions will take advantage of the exemption and they will use the exemption in conjunction with transactions involving nearly all their clients that are defined benefit plans, defined contribution plans, and IRA holders.<sup>215</sup>

The exemption's impact on the hour and cost burden associated with the Department's information collections are discussed in more detail below.

### ***Disclosures, Documentation, Retrospective Review, and Recordkeeping***

Section II(b) of the exemption requires Financial Institutions to furnish Retirement Investors with a disclosure prior to engaging in a covered transaction.

Section II(b)(1) requires Financial Institutions to acknowledge in writing that the Financial Institution and its Investment Professionals are fiduciaries under Title I and the Code, as applicable, with respect to any investment advice provided to the Retirement

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<sup>214</sup> The Department's 2018 hourly wage rate estimates include wages, benefits, and overhead, and are calculated as follows: mean wage (from the 2018 National Occupational Employment Survey, May 2018, [www.bls.gov/news.release/archives/ocwage\\_03292019.pdf](http://www.bls.gov/news.release/archives/ocwage_03292019.pdf)), wages as a percent of total compensation (from the Employer Cost for Employee Compensation, December 2018, [www.bls.gov/news.release/archives/ecec\\_03192019.pdf](http://www.bls.gov/news.release/archives/ecec_03192019.pdf)), and overhead cost corresponding to each 2-digit NAICS code (from the Annual Survey of Manufacturers, December 2017, [www.census.gov/data/Tables/2016/econ/asm/2016-asm.html](http://www.census.gov/data/Tables/2016/econ/asm/2016-asm.html)) multiplied by the percent of each occupation within that NAICS industry code based on a matrix of detailed occupation employment for each NAICS industry (from the BLS Office of Employment projections, 2016, [www.bls.gov/emp/data/occupational-data.htm](http://www.bls.gov/emp/data/occupational-data.htm)).

<sup>215</sup> For this analysis, "IRA holders" include rollovers from Title I Plans.

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Investors. Section II(b)(2) requires Financial Institutions to provide a written description of the services they provide and any material conflicts of interest. The written description must be accurate in all material respects. Financial Institutions will generally be required to provide the disclosure to each Retirement Investor once, but Financial Institutions may need to provide updated disclosures to ensure accuracy. Section II(b)(3) requires Financial Institutions to provide the documentation of specific reasons for the rollover recommendation to the Retirement Investor.

Section II(c)(1) of the exemption requires Financial Institutions to establish, maintain, and enforce written policies and procedures prudently designed to ensure that they and their Investment Professionals comply with the Impartial Conduct Standards. Section II(c)(2) further requires that the Financial Institutions design the policies and procedures to mitigate conflicts of interest. Section II(c)(3) of the exemption requires Financial Institutions to document the specific reasons for any rollover recommendation and show that the rollover is in the best interest of the Retirement Investor.

Under Section II(d) of the exemption, Financial Institutions are required to conduct an annual retrospective review that is reasonably designed to prevent violations of the exemption's Impartial Conduct Standards and the institution's own policies and procedures. The methodology and results of the retrospective review are reduced to a written report that is certified by a Senior Executive Officer of the Financial Institution. The certifying officer will be required to verify that (1) the officer has reviewed the report of the retrospective review, (2) the Financial Institution has in place policies and procedures prudently designed to achieve compliance with the conditions of the

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exemption, and (3) the Financial Institution has a prudent process for modifying such policies and procedures. The process for modifying policies and procedures will need to be responsive to business, regulatory, and legislative changes and events, and the Financial Institution will be required to periodically test their effectiveness. The review, report, and certification must be completed no later than six months following the end of the period covered by the review. The Financial Institution will be required to retain the report, certification, and supporting data for at least six years, and to make these items available to the Department within 10 business days of the request.

Section IV sets forth the recordkeeping requirements in the exemption.

#### ***Production and Distribution of Required Disclosures***

The Department assumes that 11,782 Financial Institutions, comprising 1,957 BDs,<sup>216</sup> 6,729 SEC-registered IAs,<sup>217</sup> 2,710 state-registered IAs,<sup>218</sup> and 386 insurance

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<sup>216</sup> The SEC estimated that there were 3,764 BDs as of December 2018 (*see* Form CRS Relationship Summary Release). The IAA Compliance 2019 Survey estimates that 52 percent of IAs have a pension consulting business. The estimated number of BDs affected by this exemption is the product of the SEC's estimate of total BDs in 2018 and IAA's estimate of the percent of IAs with a pension consulting business.

<sup>217</sup> The SEC estimated that there were 12,940 SEC-registered IAs that were not dually registered as BDs as of December 2018 (*see* Form CRS Relationship Summary Release). The IAA Compliance 2019 Survey estimates that 52 percent of IAs have a pension consulting business. The estimated number of IAs affected by this exemption is the product of the SEC's estimate of SEC-registered IAs in 2018 and the IAA's estimate of the percent of IAs with a pension consulting business.

<sup>218</sup> The SEC estimated that there were 16,939 state-registered IAs that were not dually registered as BDs as of December 2018 (*see* Form CRS Relationship Summary Release). The NASAA 2019 estimates that 16 percent of state-registered IAs have a pension consulting business. The estimated number of state-registered IAs affected by this exemption is the product of the SEC's estimate of state-registered IAs in 2018 and NASAA's estimate of the percent of state-registered IAs with a pension consulting business.

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companies,<sup>219</sup> are likely to engage in transactions covered under this exemption. Each will need to provide disclosures that (1) acknowledge its fiduciary status, and (2) identify the services it provides and any material conflicts of interest. The Department estimates that preparing a disclosure indicating fiduciary status would take a legal professional between five and 30 minutes, depending on the nature of the business,<sup>220</sup> resulting in an hour burden of 1,599<sup>221</sup> and a cost burden of \$584,130.<sup>222</sup> Preparing a disclosure identifying services provided and conflicts of interest would take a legal professional an estimated five minutes to five hours, depending on the nature of the business,<sup>223</sup> resulting in an hour burden of 3,691<sup>224</sup> and an equivalent cost burden of \$1,348,628.<sup>225</sup>

The Department estimates that approximately 1.8 million Retirement Investors<sup>226</sup> have relationships with Financial Institutions and are likely to engage in transactions

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<sup>219</sup> NAIC estimates that the number of insurers directly writing annuities as of 2018 is 386.

<sup>220</sup> The Department assumes that it will take each retail BD firm 15 minutes, each nonretail BD or insurance firm 30 minutes, and each registered IA five minutes to prepare a disclosure conveying fiduciary status.

<sup>221</sup> Burden hours are calculated by multiplying the estimated number of each firm type by the estimated time it will take each firm to prepare the disclosure.

<sup>222</sup> The hourly cost burden is calculated by multiplying the burden hour of each firm associated with preparation of the disclosure by the hourly wage of a legal professional.

<sup>223</sup> The Department assumes that it will take each retail BD or IA firm five minutes, each small nonretail BD or small insurer 60 minutes, and each large nonretail BDs or large insurer five hours to prepare a disclosure conveying services provided and conflicts of interest.

<sup>224</sup> Burden hours are calculated by multiplying the estimated number of each firm type by the estimated time it will take each firm to prepare the disclosure.

<sup>225</sup> The hourly cost burden is calculated by multiplying the burden hour of each firm associated with preparation of the disclosure by the hourly wage of a legal professional.

<sup>226</sup> The Department estimates the number of affected Plans and IRAs be approximately equal to 49 percent

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covered under this exemption. Of these 1.8 million Retirement Investors, it is assumed that 8.1 percent<sup>227</sup> or 141,636 Retirement Investors, will receive paper disclosures.

Distributing paper disclosures is estimated to take a clerical professional one minute per disclosure, resulting in an hourly burden of 2,361<sup>228</sup> and an equivalent cost burden of \$151,341.<sup>229</sup> Assuming the disclosures will require two sheets of paper at a cost \$0.05 each, the estimated material cost for the paper disclosures is \$14,164. Postage for each paper disclosure is expected to cost \$0.55, resulting in a printing and mailing cost of \$92,063.

### ***Written Policies and Procedures Requirement***

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of rollovers from defined contribution plans to IRAs. Cerulli has estimated the number of accounts in defined contribution plans rolled into IRAs to be 3,593,592 (see U.S. Retirement-End Investor 2020, *supra* note 178).

<sup>227</sup> According to data from the National Telecommunications and Information Agency (NTIA), 37.7 percent of individuals age 25 and over have access to the internet at work. According to a Greenwald & Associates survey, 84 percent of plan participants find it acceptable to make electronic delivery the default option, which is used as the proxy for the number of participants who will not opt-out of electronic disclosure if automatically enrolled (for a total of 31.7 percent receiving electronic disclosure at work). Additionally, the NTIA reports that 40.5 percent of individuals age 25 and over have access to the internet outside of work. According to a Pew Research Center survey, 61 percent of internet users use online banking, which is used as the proxy for the number of internet users who will affirmatively consent to receiving electronic disclosures (for a total of 24.7 percent receiving electronic disclosure outside of work). Combining the 31.7 percent who receive electronic disclosure at work with the 24.7 percent who receive electronic disclosure outside of work produces a total of 56.4 percent who will receive electronic disclosure overall. In light of the 2019 Electronic Disclosure Regulation, the Department estimates that 81.5 percent of the remaining 43.6 percent of individuals will receive the disclosures electronically. In total, 91.9 percent of participants are expected to receive disclosures electronically.

<sup>228</sup> Burden hours are calculated by multiplying the estimated number of plans receiving the disclosures non-electronically by the estimated time it will take to prepare the physical disclosure.

<sup>229</sup> The hourly cost burden is calculated as the burden hours associated with the physical preparation of each non-electronic disclosure by the hourly wage of a clerical professional.

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The Department assumes that 11,782 Financial Institutions, comprising 1,957 BDs,<sup>230</sup> 6,729 SEC-registered IAs,<sup>231</sup> 2,710 state registered IAs,<sup>232</sup> and 386 insurance companies,<sup>233</sup> are likely to engage in transactions covered under this exemption. The Department estimates that establishing, maintaining, and enforcing written policies and procedures prudently designed to ensure compliance with the Impartial Conduct Standards will take a legal professional between 15 minutes and 10 hours, depending on the nature of the business.<sup>234</sup> This results in an hour burden of 12,023<sup>235</sup> and an equivalent cost burden of \$4,393,011.<sup>236</sup>

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<sup>230</sup> The SEC estimated that there were 3,764 BDs as of December 2018 (*see* Form CRS Relationship Summary Release). The IAA Compliance 2019 Survey estimates that 52 percent of IAs have a pension consulting business. The estimated number of BDs affected by this exemption is the product of the SEC's estimate of total BDs in 2018 and IAA's estimate of the percent of IAs with a pension consulting business.

<sup>231</sup> The SEC estimated that there were 12,940 SEC-registered IAs, who were not dually registered as BDs, as of December 2018 (*see* Form CRS Relationship Summary Release). The IAA Compliance 2019 Survey estimates that 52 percent of IAs have a pension consulting business. The estimated number of IAs affected by this exemption is the product of the SEC's estimate of SEC-registered IAs in 2018 and IAA's estimate of the percent of IAs with a pension consulting business.

<sup>232</sup> The SEC estimated that there were 16,939 state-registered IAs who were not dually registered as BDs as of December 2018 (*see* Form CRS Relationship Summary Release). The NASAA 2019 estimates that 16 percent of state-registered IAs have a pension consulting business. The estimated number of state-registered IAs affected by this exemption is the product of the SEC's estimate of state-registered IAs in 2018 and NASAA's estimate of the percent of state-registered IAs with a pension consulting business.

<sup>233</sup> NAIC estimates that 386 insurers were directly writing annuities as of 2018.

<sup>234</sup> The Department assumes that it will take each small retail BD 22.5 minutes, each large retail BD 45 minutes, each small nonretail BD five hours, each large nonretail BD 10 hours, each small IA 15 minutes, each large IA 30 minutes, each small insurer five hours, and each large insurer 10 hours to meet the requirement.

<sup>235</sup> Burden hours are calculated by multiplying the estimated number of each firm type by the estimated time it will take each firm to establish, maintain, and enforce written policies and procedures.

<sup>236</sup> The hourly cost burden is calculated as the burden hour of each firm associated with meeting the written policies and procedures requirement multiplied by the hourly wage of a legal professional.

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### ***Rollover Documentation Requirement***

To meet the requirement of the rollover documentation, Financial Institutions must document the specific reasons that any recommendation to roll over assets is in the best interest of the Retirement Investor. The Department estimates that 1.8 million defined contribution plan accounts rolled into IRAs in accordance with advice from a financial services professional.<sup>237</sup> Facing uncertainty, the Department assumes that 67.4 percent of rollovers will be affected by the exemption.<sup>238</sup> Under this assumption, the Department estimates that the costs for documenting the basis for rollover decisions will come to \$65 million per year.<sup>239</sup> This was based on the assumption that most financial services professionals already incorporate documenting the basis for rollover recommendations in their regular business practices and another assumption that 67.4 percent of rollovers are handled by financial services professionals who act in a fiduciary capacity.<sup>240</sup> The Department estimates that documenting each rollover recommendation will require 30 minutes for a personal financial advisor whose firms currently do not require rollover documentations and five minutes for financial advisors whose firms

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<sup>237</sup> Cerulli has estimated the number of accounts in defined contribution plans rolled into IRAs to be 3,593,591 (see U.S. Retirement-End Investor 2020, *supra* note 178). The Department estimates that 49 percent of these rollovers will be handled by a financial professional.

<sup>238</sup> See *supra* note 206.

<sup>239</sup> See *supra* note 207.

<sup>240</sup> See *supra* note 206.

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already require them to do so,<sup>241</sup> resulting in 335,330<sup>242</sup> burden hours and an equivalent cost burden of \$65,313,770.<sup>243</sup>

### ***Annual Retrospective Review Requirement***

Under the internal retrospective review requirement, a Financial Institution is required to (1) conduct an annual retrospective review reasonably designed to assist the Financial Institution in detecting and preventing violations of, and achieving compliance with the Impartial Conduct Standards and their policies and procedures; and (2) produce a written report that is certified by a Senior Executive Officer of the Financial Institution.

The Department understands that, as per FINRA Rule 3110,<sup>244</sup> FINRA Rule 3120,<sup>245</sup> and FINRA Rule 3130,<sup>246</sup> broker-dealers are already held to a standard functionally identical to that of the retrospective review requirements of this exemption. Accordingly, in this analysis, the Department assumes that broker-dealers will incur minimal costs to meet this requirement. In 2018, the Investment Adviser Association

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<sup>241</sup> See *supra* note 207.

<sup>242</sup> Burden hours are calculated by multiplying the estimated number of rollovers affected by this proposed exemption by the estimated hours needed to document each recommendation.

<sup>243</sup> The hourly cost burden is calculated as the burden hour of each firm associated with meeting the rollover documentation requirement multiplied by the hourly wage of a personal financial advisor.

<sup>244</sup> *Rule 3110. Supervision*, FINRA Manual, [www.finra.org/rules-guidance/rulebooks/finra-rules/3110](http://www.finra.org/rules-guidance/rulebooks/finra-rules/3110).

<sup>245</sup> *Rule 3120. Supervisory Control System*, FINRA Manual, [www.finra.org/rules-guidance/rulebooks/finra-rules/3120](http://www.finra.org/rules-guidance/rulebooks/finra-rules/3120).

<sup>246</sup> *Rule 3130. Annual Certification of Compliance and Supervisory Processes*, FINRA Manual, [www.finra.org/rules-guidance/rulebooks/finra-rules/3130](http://www.finra.org/rules-guidance/rulebooks/finra-rules/3130).



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estimated that 92 percent of SEC-registered IAs voluntarily provide an annual compliance program review report to senior management.<sup>247</sup> The Department estimates that only eight percent, or 538,<sup>248</sup> of SEC-registered IAs advising retirement plans will incur costs associated with producing a retrospective review report. Due to lack of data, the Department assumes that state-registered IAs exhibit similar retrospective review patterns and estimates that eight percent, or 217,<sup>249</sup> of state-registered IAs will also incur costs associated with producing a retrospective review report.

As SEC-registered IAs are already subject to SEC Rule 206(4)-7, the Department assumes these IAs will incur minimal costs to satisfy the conditions related to this

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<sup>247</sup> 2018 Investment Management Compliance Testing Survey, Investment Adviser Association (Jun. 14, 2018), [https://higherlogicdownload.s3.amazonaws.com/INVESTMENTADVISER/aa03843e-7981-46b2-aa49-c572f2ddb7e8/UploadedImages/publications/2018-Investment-Management\\_Compliance-Testing-Survey-Results-Webcast\\_pptx.pdf](https://higherlogicdownload.s3.amazonaws.com/INVESTMENTADVISER/aa03843e-7981-46b2-aa49-c572f2ddb7e8/UploadedImages/publications/2018-Investment-Management_Compliance-Testing-Survey-Results-Webcast_pptx.pdf).

<sup>248</sup> The SEC estimated that there were 12,940 SEC-registered IAs that were not dually registered as BDs as of December 2018 (see Form CRS Relationship Summary Release). The IAA Compliance 2019 Survey estimates that 52 percent of IAs have a pension consulting business. The IAA Investment Management Compliance Testing Survey estimates that 92 percent of SEC-registered IAs provide an annual compliance program review report to senior management. The estimated number of IAs affected by this exemption who do not meet the retrospective review requirement is the product of the SEC's estimate of SEC-registered IAs in 2018, the IAA's estimate of the percent of IAs with a pension consulting business, and IAA's estimate of the percent of IA's who do not provide an annual compliance program review report.

<sup>249</sup> The SEC estimated that there were 16,939 state-registered IAs that were not dually registered as BDs as of December 2018 (see Form CRS Relationship Summary Release). The NASAA 2019 estimates that 16 percent of state-registered IAs have a pension consulting business. The IAA Investment Management Compliance Testing Survey estimates that 92 percent of SEC-registered IAs provide an annual compliance program review report to senior management. The Department assumes state-registered IAs exhibit similar retrospective review patterns as SEC-registered IAs. The estimated number of state-registered IAs affected by this exemption is the product of the SEC's estimate of state-registered IAs in 2018, NASAA's estimate of the percent of state-registered IAs with a pension consulting business, and IAA's estimate of the percent of IA's who do not provide an annual compliance program review report.

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requirement. Insurance companies in many states are already subject state insurance law based on the NAIC's Model Regulation.<sup>250</sup> Thus, the Department assumes that insurance companies will incur negligible costs associated with producing a retrospective review report. This is estimated to take a legal professional five hours for small firms and 10 hours for large firms, depending on the nature of the business. This results in an hour burden of 7,032<sup>251</sup> and an equivalent cost burden of \$2,569,337.<sup>252</sup>

Financial Institutions that already produce retrospective review reports voluntarily or in accordance with other regulators' rules likely will spend additional time to fully comply with this exemption condition such as revising their current retrospective review reports. This is estimated to take a financial professional one hour for small firms and two hours for large firms, depending on the nature of the business. This results in an hour burden of 20,727 hours and an equivalent cost burden of \$7,573,614.

In addition to conducting the audit and producing a report, Financial Institutions also will need to review the report and certify the exemption. The Department substantially increased the burden hours associated with this requirement in response to

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<sup>250</sup> NAIC Model Regulation, Section 6.C.(2)(i) (The same requirement is found in the NAIC Suitability in Annuity Transactions Model Regulation (2010), Section 6.F.(1)(f).)

<sup>251</sup> Burden hours are calculated by multiplying the estimated number of each firm type by the estimated time it will take each firm to review the report and certify the exemption.

<sup>252</sup> The hourly cost burden is calculated by multiplying the burden hours for reviewing the report and certifying the exemption requirement by the hourly wage of a legal professional.

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concerns raised by a commenter that this is a superficial process.<sup>253</sup> This is estimated to take the certifying officer two hours for small firms and four hours for large firms, depending on the nature of the business.<sup>254</sup> This results in an hour burden of 34,718<sup>255</sup> and an equivalent cost burden of \$5,750,451.<sup>256</sup>

### ***Overall Summary***

Overall, the Department estimates that in order to satisfy the exemption, 11,782 Financial Institutions will produce 1.8 million disclosures and notices annually. These disclosures and notices will result in 417,480 burden hours during the first year and 393,136 burden hours in subsequent years, at an equivalent cost of \$87.7 million and \$78.8 million respectively. The disclosures and notices in this exemption will also result in a total cost burden for materials and postage of \$92,063 annually.

These paperwork burden estimates are summarized as follows:

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<sup>253</sup> For more detailed discussion, see the corresponding Cost section of the Regulatory Impact Analysis above.

<sup>254</sup> Due to lack of data, the Department estimates the hourly labor cost of a certifying officer to be that of a Financial Manager, as outlined on the Employee Benefits Security Administration's 2018 labor rate estimates. See *Labor Cost Inputs Used in the Employee Benefits Security Administration, Office of Policy and Research's Regulatory Impact Analyses and Paperwork Reduction Act Burden Calculation*, Employee Benefits Security Administration (June 2019), [www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/technical-appendices/labor-cost-inputs-used-in-ebsa-opr-ria-and-pra-burden-calculations-june-2019.pdf](http://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/technical-appendices/labor-cost-inputs-used-in-ebsa-opr-ria-and-pra-burden-calculations-june-2019.pdf). The Department assumes that it will take the certifying officer two hours for small firms and four hours for large firms. If we assume that an average person reads 250 words per minute, the certifying officer can read 30,000 words in two hours or 60,000 words in four hours. This implies a retrospective review report would be approximately 125 pages to 250 pages if this report is double-spaced with a width 12 point font size.

<sup>255</sup> Burden hours are calculated by multiplying the estimated number of each firm type by the estimated time it will take each firm to review the report and certify the exemption.

<sup>256</sup> The hourly cost burden is calculated by multiplying the burden hours for reviewing the report and certifying the exemption requirement by the hourly wage of a financial professional.

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- *Type of Review:* New collection
- *Agency:* Employee Benefits Security Administration, Department of Labor.
- *Title:* Improving Investment Advice for Workers & Retirees.
- *OMB Control Number:* 1210–0163.
- *Affected Public:* Business or other for-profit institution.
- *Estimated Number of Respondents:* 11,782
- *Estimated Number of Annual Responses:* 1,755,959
- *Frequency of Response:* Initially, Annually, and when engaging in exempted transaction.
- *Estimated Total Annual Burden Hours:* 417,480 during the first year and 393,136 in subsequent years.
- *Estimated Total Annual Burden Cost:* \$92,063 during the first year and \$92,063 in subsequent years.

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### ***Regulatory Flexibility Act***

The Regulatory Flexibility Act (RFA)<sup>257</sup> imposes certain requirements on rules subject to the notice and comment requirements of section 553(b) of the Administrative Procedure Act or any other law.<sup>258</sup> Under section 604 of the RFA, agencies must submit a final regulatory flexibility analysis (FRFA) of a proposal that is likely to have a significant economic impact on a substantial number of small entities, such as small businesses, organizations, and governmental jurisdictions.

The Department has determined that this final class exemption will likely have a significant economic impact on a substantial number of small entities. Therefore, the Department has prepared the FRFA presented below.

### ***Need for and Objectives of the Rule***

As discussed earlier in this preamble, the final class exemption will allow investment advice fiduciaries to receive compensation and engage in transactions that would otherwise violate the prohibited transaction provisions of Title I and the Code. As such, the final exemption will provide Financial Institutions and Investment Professionals with flexibility to address different business models and would lessen their overall regulatory burden by coordinating potentially overlapping regulatory requirements. The exemption conditions, including the Impartial Conduct Standards and other conditions

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<sup>257</sup> 5 U.S.C. § 601 et seq.

<sup>258</sup> 5 U.S.C. §§ 601(2), 603(a); *see also* 5 U.S.C. § 551.

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supporting the standards, are expected to provide protections to Retirement Investors.

Therefore, the Department expects that the final exemption will benefit Retirement Investors that are small entities and provide efficiencies to small Financial Institutions.

### ***Significant Issues Raised by Public Comments***

In response to the Department's Initial Regulatory Flexibility Analysis (IRFA), no significant issue was raised by public comments. In the preamble to the proposed class exemption, the Department solicited comments regarding whether the proposed exemption would have a significant economic impact on a substantial number of small entities and received no comments in response. Moreover, the Department received no public comments from the Small Business Administration. As a result, the Department made no major changes to the IFRA.

### ***Affected Small Entities***

The Small Business Administration (SBA),<sup>259</sup> pursuant to the Small Business Act,<sup>260</sup> defines small businesses and issues size standards by industry. The SBA defines a small business in the Financial Investments and Related Activities Sector as a business with up to \$41.5 million in annual receipts. Due to a lack of data and shared jurisdiction, for purpose of performing Regulatory Flexibility Analyses pursuant to section 601(3) of

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<sup>259</sup> 13 C.F.R. § 121.201.

<sup>260</sup> 15 U.S.C. § 631 et seq.

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the Regulatory Flexibility Act, the Department, after consultation with SBA's Office of Advocacy, defines small entities included in this analysis differently from the SBA definitions.<sup>261</sup> For instance, in this analysis, the small-business definitions for BDs and SEC-registered IAs are consistent with the SEC's definitions, as these entities are subject to the SEC's rules as well as the Act.<sup>262</sup> As with SEC-registered IAs, the size of state-registered IAs is determined based on total value of the assets they manage.<sup>263</sup> The size of insurance companies is based on annual sales of annuities. The Department requested comments on the appropriateness of the size standard used to evaluate the impact of the proposed exemption on small entities and received no comments in response. In particular, the Department received no comments asserting that it is inappropriate for the Department to use size standards that are different from those promulgated by the SBA.

In December 2018, there were 985 small-business BDs and 528 SEC-registered, small-business IAs.<sup>264</sup> The Department estimates that approximately 52 percent of these small-businesses will be affected by the final class exemption.<sup>265</sup> In December 2018, the

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<sup>261</sup> The Department consulted with the Small Business Administration Office of Advocacy in making this determination as required by 5 U.S.C. §603(c).

<sup>262</sup> 17 C.F.R. Parts 230, 240, 270, and 275, [www.sec.gov/rules/final/33-7548.txt](http://www.sec.gov/rules/final/33-7548.txt).

<sup>263</sup> Due to lack of available data, the Department includes state-registered IAs managing assets less than \$30 million as small entities in this analysis.

<sup>264</sup> See *Form CRS Relationship Summary; Amendments to Form ADV*, 84 Fed. Reg. 33492 (Jul. 12, 2019).

<sup>265</sup> *2019 Investment Management Compliance Testing Survey*, Investment Adviser Association (Jun. 18, 2019), [https://higherlogicdownload.s3.amazonaws.com/INVESTMENTADVISER/aa03843e-7981-46b2-aa49-c572f2ddb7e8/UploadedImages/about/190618\\_IMCTS\\_slides\\_after\\_webcast\\_edits.pdf](https://higherlogicdownload.s3.amazonaws.com/INVESTMENTADVISER/aa03843e-7981-46b2-aa49-c572f2ddb7e8/UploadedImages/about/190618_IMCTS_slides_after_webcast_edits.pdf).

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Department estimates there were approximately 10,840 small state-registered IAs,<sup>266</sup> of which about 1,700 are estimated to be affected by the final exemption.<sup>267</sup> There were approximately 386 insurers directly writing annuities in 2018,<sup>268</sup> 316 of which the Department estimates are small entities.<sup>269</sup> Table 1 summarizes the distribution of affected entities by size.

Table 2. Distribution of affected entities by size.

	BDs		SEC-registered IAs		State-registered IAs		Insurers	
Small	985	26%	528	4%	10,840	64%	316	82%
Large	2,779	74%	12,412	96%	6,099	36%	70	18%
Total	3,764	100%	12,940	100%	16,939	100%	386	100%

### ***Projected Reporting, Recordkeeping, and Other Compliance Requirements***

As discussed above, the final exemption provides Financial Institutions and Investment Professionals with flexibility to choose between the new final exemption or the Department’s existing exemptions, depending on their individual needs and business

<sup>266</sup> The SEC estimates there were approximately 17,000 state-registered IAs (*see Form CRS Relationship Summary; Amendments to Form ADV*, 84 Fed. Reg. 33492 (Jul. 12, 2019)). The Department estimates that about 64 percent of state-registered IAs manage assets less than \$30 million, and it considers such entities small businesses. (*See 2018 Investment Adviser Section Annual Report*, North American Securities Administrators Association (May 2018), [www.nasaa.org/wp-content/uploads/2018/05/2018-NASAA-IA-Report-Online.pdf](http://www.nasaa.org/wp-content/uploads/2018/05/2018-NASAA-IA-Report-Online.pdf).) Therefore, the Department estimates there were about 10,840 small, state-registered IAs.

<sup>267</sup> Of the small, state-registered IAs, the Department estimates that 16 percent provide advice or services to retirement plans (*see 2019 Investment Adviser Section Annual Report*, North American Securities Administrators Association, (May 2019)).

<sup>268</sup> NAIC estimates that the number of insurers directly writing annuities as of 2018 is 386.

<sup>269</sup> LIMRA estimates in 2016, 70 insurers had more than \$38.5 million in sales. (*See U.S. Individual Annuity Yearbook: 2016 Data*, LIMRA Secure Retirement Institute (2017)).



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models. Furthermore, the final exemption provides Financial Institutions and Investment Professionals broader, more flexible prohibited transaction relief than is currently available, while safeguarding the interests of Retirement Investors. In this regard, this final exemption could present a less burdensome compliance alternative for some Financial Institutions because it would allow them to streamline compliance rather than rely on multiple exemptions with multiple sets of conditions.

This final exemption simply provides an additional alternative pathway for Financial Institutions and Investment Professionals to receive compensation and engage in certain transactions that would otherwise be prohibited under Title I and the Code. Financial Institutions would incur costs to comply with conditions set forth in the final exemption. However, the Department believes the costs associated with those conditions are modest because the final exemption was developed in consideration of other regulatory conduct standards. The Department believes that many Financial Institutions and Investment Professionals have already developed compliance structures for similar regulatory standards. Therefore, the Department does not expect that the final exemption will impose a significant compliance burden on small entities. For example, the Department estimates that a small entity would incur, on average, an additional \$3,034 in compliance costs to meet the conditions of this final exemption. These additional costs represent 0.6 percent of the net capital of BD with \$500,000. A BD with less than \$500,000 in net capital is generally considered small, according to the SEC.

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### ***Steps Taken to Minimize Impacts and Significant Alternatives Considered***

Section 604 of the RFA requires the Department to consider significant alternatives that would accomplish the stated objective, while minimizing any significant adverse impact on small entities. Title I and the Code rules governing advice on the investment of retirement assets overlap with SEC rules that govern the conduct of IAs and BDs who advise retail investors. The Department considered conduct standards set by other regulators, such as SEC, state insurance regulators, and FINRA, in developing the final exemption, with the goal of avoiding overlapping or duplicative requirements. To the extent the requirements overlap, compliance with the other disclosure or recordkeeping requirements can be used to satisfy the exemption, provided the conditions are satisfied. This will lead to overall regulatory efficiency.

The Department describes below additional steps it has taken to minimize the significant economic impact on small entities consistent with the stated objectives of applicable statutes, including a statement of the factual, policy, and legal reasons for selecting the alternatives adopted in the final exemption.

***Revisions to Annual Retrospective Review Requirement:*** Under section II(d) of the final exemption, Financial Institutions are required to conduct an annual retrospective review that is reasonably designed to detect and prevent violations of, and achieve compliance with, the Impartial Conduct Standards and the institution's own policies and procedures. The Department considered the alternative of requiring a Financial Institution to engage an independent party to provide an external audit. The Department

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elected not to require this condition to avoid the increased costs this approach would impose. Smaller Financial Institutions may have been disproportionately impacted by such costs, which would have been contrary to the Department's goals of promoting access to investment advice for Retirement Investors. Further, the Department is not convinced that an independent, external audit would yield useful information commensurate with the cost, particularly to small entities. Instead, the final exemption requires that Financial Institutions to document their retrospective review, and provide it, and supporting information, to the Department, within 10 business days of request, to the extent permitted by law.

***Addition of Self-Correction Provision:*** The Department has added a new Section II(e) to the exemption, under which Financial Institutions will be able to correct certain violations of the exemption. Under the new Section II(e), the Department will not consider a non-exempt prohibited transaction to have occurred due to a violation of the exemption's conditions, provided: (1) either the violation did not result in investment losses to the Retirement Investor or the Financial Institution made the Retirement Investor whole for any resulting losses; (2) the Financial Institution corrects the violation and notifies the Department via email to [IIAWR@dol.gov](mailto:IIAWR@dol.gov) within 30 days of correction; (3) the correction occurs no later than 90 days after the Financial Institution learned of the violation or reasonably should have learned of the violation; and (4) the Financial Institution notifies the persons responsible for conducting the retrospective review during the applicable review cycle, and the violation and correction is specifically set forth in the written report of the retrospective review.

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While this section was not a part of the proposal, several commenters requested that the Department provide a means for Financial Institutions, acting in good faith, to avoid loss of the exemption for violations of the conditions. One commenter specified that there should be a correction process in connection with the retrospective review, because failure to include this could put Financial Institutions in a difficult position of having discovered technical violations but not being able to cure them without being subject to an excise tax for the prohibited transaction.

Upon consideration of the comments, the Department determined to provide this self-correction procedure. Accordingly, the section allows for correction even if a Retirement Investor has suffered investment losses, provided that the Retirement Investor is made whole. The Department believes that the self-correction provision will provide Financial Institutions with an additional incentive to take the retrospective review process seriously, timely identify and correct violations, and use the process to correct deficiencies in their policies and procedures, so as to avoid potential future penalties and lawsuits.

***Revision to Recordkeeping Requirements:*** Under Section IV of the exemption, Financial Institutions must maintain records for six years demonstrating compliance with the exemption. The Department generally includes a recordkeeping requirement in its administrative exemptions to ensure that parties relying on an exemption can demonstrate, and the Department can verify, compliance with the conditions of the exemption. The proposal provided that records should be available for review by the following parties in addition to the Department: any fiduciary of a Plan that engaged in

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an investment transaction pursuant to this exemption; any contributing employer and any employee organization whose members are covered by a Plan that engaged in an investment transaction pursuant to this exemption; or any participant or beneficiary of a Plan, or IRA owner that engaged in an investment transaction pursuant to this exemption.

Several commenters stated that allowing parties other than the Department to review records would increase the burden placed on Financial Institutions. In particular, they expressed the view that parties might overwhelm Financial Institutions with requests for information in order to generate claims for use in litigation. Fear of potential litigation, could in turn, they argued, lead to a “culture of quiet” in which employees of Financial Institutions elect not to address compliance issues because of the fear of this disclosure. In response to these comments, the Department has revised the final exemption’s recordkeeping provisions so that access is limited to the Department and the Department of the Treasury.

### ***Unfunded Mandates Reform Act***

Title II of the Unfunded Mandates Reform Act of 1995<sup>270</sup> requires each federal agency to prepare a written statement assessing the effects of any federal mandate in a proposed or final rule that may result in an expenditure of \$100 million or more (adjusted annually for inflation with the base year 1995) in any one year by state, local, and tribal governments, in the aggregate, or by the private sector. For purposes of the Unfunded

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<sup>270</sup> Pub. L. 104-4, 109 Stat. 48 (1995).

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Mandates Reform Act, as well as Executive Order 12875, this exemption does not include any Federal mandate that will result in such expenditures.

### ***Federalism Statement***

Executive Order 13132 outlines fundamental principles of federalism. It also requires federal agencies to adhere to specific criteria in formulating and implementing policies that have “substantial direct effects” on the states, the relationship between the national government and states, or on the distribution of power and responsibilities among the various levels of government. Federal agencies promulgating regulations that have these federalism implications must consult with state and local officials and describe the extent of their consultation and the nature of the concerns of state and local officials in the preamble to the final regulation. The Department does not believe this class exemption has federalism implications because it has no substantial direct effect on the states, on the relationship between the national government and the states, or on the distribution of power and responsibilities among the various levels of government.

### ***General Information***

The attention of interested persons is directed to the following:

(1) The fact that a transaction is the subject of an exemption under ERISA section 408(a) and Code section 4975(c)(2) does not relieve a fiduciary, or other party in interest or disqualified person with respect to a Plan or an IRA, from certain other provisions of Title I and the Code, including any prohibited transaction provisions to which the exemption does not apply and the general fiduciary responsibility provisions of ERISA section 404 which require, among other things, that a fiduciary act prudently and

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discharge his or her duties respecting the Plan solely in the interests of the participants and beneficiaries of the Plan. Additionally, the fact that a transaction is the subject of an exemption does not affect the requirement of Code section 401(a) that the Plan must operate for the exclusive benefit of the employees of the employer maintaining the Plan and its beneficiaries;

(2) In accordance with section 408(a) of ERISA and section 4975(c)(2) of the Code, and based on the entire record, the Department finds that this exemption is administratively feasible, in the interests of Plans and their participants and beneficiaries and IRA owners, and protective of the rights of participants and beneficiaries of the Plan and IRA owners;

(3) The exemption is applicable to a particular transaction only if the transaction satisfies the conditions specified in the exemption; and

(4) The exemption is supplemental to, and not in derogation of, any other provisions of Title I and the Code, including statutory or administrative exemptions and transitional rules. Furthermore, the fact that a transaction is subject to an administrative or statutory exemption is not dispositive of whether the transaction is in fact a prohibited transaction.

## **IMPROVING INVESTMENT ADVICE FOR WORKERS & RETIREES**

### ***Section I—Transactions***

(a) *In general.* ERISA Title I (Title I) and the Internal Revenue Code (the Code) prohibit fiduciaries, as defined, that provide investment advice to Plans and individual

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retirement accounts (IRAs) from receiving compensation that varies based on their investment advice and compensation that is paid from third parties. Title I and the Code also prohibit fiduciaries from engaging in purchases and sales with Plans or IRAs on behalf of their own accounts (principal transactions). This exemption permits Financial Institutions and Investment Professionals who provide fiduciary investment advice to Retirement Investors to receive otherwise prohibited compensation and engage in riskless principal transactions and certain other principal transactions (Covered Principal Transactions) as described below. The exemption provides relief from the prohibitions of ERISA section 406(a)(1)(A), (D), and 406(b), and the sanctions imposed by Code section 4975(a) and (b), by reason of Code section 4975(c)(1)(A), (D), (E), and (F), if the Financial Institutions and Investment Professionals provide fiduciary investment advice in accordance with the conditions set forth in Section II and are eligible pursuant to Section III, subject to the definitional terms and recordkeeping requirements in Sections IV and V.

*(b) Covered transactions.* This exemption permits Financial Institutions and Investment Professionals, and their Affiliates and Related Entities, to engage in the following transactions, including as part of a rollover from a Plan to an IRA as defined in Code section 4975(e)(1)(B) or (C), as a result of the provision of investment advice within the meaning of ERISA section 3(21)(A)(ii) and Code section 4975(e)(3)(B):

- (1) The receipt of reasonable compensation; and
- (2) The purchase or sale of an asset in a riskless principal transaction or a Covered Principal Transaction, and the receipt of a mark-up, mark-down, or other payment.



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*(c) Exclusions.* This exemption does not apply if:

(1) The Plan is covered by Title I of ERISA and the Investment Professional, Financial Institution or any Affiliate is (A) the employer of employees covered by the Plan, or (B) a named fiduciary or plan administrator with respect to the Plan that was selected to provide advice to the Plan by a fiduciary who is not independent of the Financial Institution, Investment Professional, and their Affiliates;

(2) The transaction is a result of investment advice generated solely by an interactive web site in which computer software-based models or applications provide investment advice based on personal information each investor supplies through the website, without any personal interaction or advice with an Investment Professional (i.e., robo-advice); or

(3) The transaction involves the Investment Professional acting in a fiduciary capacity other than as an investment advice fiduciary within the meaning of the regulations at 29 CFR 2510.3-21(c)(1)(i) and (ii)(B) or 26 CFR 54.4975-9(c)(1)(i) and (ii)(B) setting forth the test for fiduciary investment advice.

### ***Section II—Investment Advice Arrangement***

Section II requires Investment Professionals and Financial Institutions to comply with Impartial Conduct Standards, including a best interest standard, when providing fiduciary investment advice to Retirement Investors. In addition, the exemption requires Financial Institutions to acknowledge fiduciary status under Title I and/or the Code, and describe in writing the services they will provide and their material Conflicts of Interest. Finally, Financial Institutions must adopt policies and procedures prudently designed to

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ensure compliance with the Impartial Conduct Standards when providing fiduciary investment advice to Retirement Investors and conduct a retrospective review of compliance.

(a) *Impartial Conduct Standards.* The Financial Institution and Investment Professional comply with the following “Impartial Conduct Standards”:

(1) Investment advice is, at the time it is provided, in the Best Interest of the Retirement Investor. As defined in Section V(b), such advice 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;

(2)(A) The compensation received, directly or indirectly, by the Financial Institution, Investment Professional, their Affiliates and Related Entities for their services does not exceed reasonable compensation within the meaning of ERISA section 408(b)(2) and Code section 4975(d)(2); and (B) as required by the federal securities laws, the Financial Institution and Investment Professional seek to obtain the best execution of the investment transaction reasonably available under the circumstances; and

(3) The Financial Institution’s and its Investment Professionals’ statements to the Retirement Investor about the recommended transaction and other relevant matters are

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not, at the time statements are made, materially misleading.

(b) *Disclosure.* Prior to engaging in a transaction pursuant to this exemption, the Financial Institution provides the disclosures set forth in (1) and (2) to the Retirement Investor:

(1) A written acknowledgment that the Financial Institution and its Investment Professionals are fiduciaries under Title I and the Code, as applicable, with respect to any fiduciary investment advice provided by the Financial Institution or Investment Professional to the Retirement Investor;

(2) A written description of the services to be provided and the Financial Institution's and Investment Professional's material Conflicts of Interest that is accurate and not misleading in all material respects; and

(3) Prior to engaging in a rollover recommended pursuant to the exemption, the Financial Institution provides the documentation of specific reasons for the rollover recommendation, required by Section II(c)(3), to the Retirement Investor.

(c) *Policies and Procedures.*

(1) The Financial Institution establishes, maintains, and enforces written policies and procedures prudently designed to ensure that the Financial Institution and its Investment Professionals comply with the Impartial Conduct Standards in connection with covered fiduciary advice and transactions.

(2) Financial Institutions' policies and procedures mitigate Conflicts of Interest to the extent that a reasonable person reviewing the policies and procedures and incentive practices as a whole would conclude that they do not create an incentive for a Financial

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Institution or Investment Professional to place their interests ahead of the interest of the Retirement Investor.

(3) The Financial Institution documents the specific reasons that any recommendation to roll over assets from a Plan to another Plan or an IRA as defined in Code section 4975(e)(1)(B) or (C), from an IRA as defined in Code section 4975(e)(1)(B) or (C) 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) is in the Best Interest of the Retirement Investor.

(d) *Retrospective Review.*

(1) The Financial Institution conducts a retrospective review, at least annually, that is reasonably designed to assist the Financial Institution in detecting and preventing violations of, and achieving compliance with, the Impartial Conduct Standards and the policies and procedures governing compliance with the exemption.

(2) The methodology and results of the retrospective review are reduced to a written report that is provided to a Senior Executive Officer.

(3) A Senior Executive Officer of the Financial Institution certifies, annually, that:

(A) The officer has reviewed the report of the retrospective review;

(B) The Financial Institution has in place policies and procedures prudently designed to achieve compliance with the conditions of this exemption; and

(C) 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,

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the timing and extent of which is reasonably designed to ensure continuing compliance with the conditions of this exemption.

(4) The review, report and certification are completed no later than six months following the end of the period covered by the review.

(5) The Financial Institution retains the report, certification, and supporting data for a period of six years and makes the report, certification, and supporting data available to the Department, within 10 business days of request, to the extent permitted by law including 12 U.S.C. § 484.

(e) *Self-Correction.* A non-exempt prohibited transaction will not occur due to a violation of the exemption's conditions with respect to a transaction, provided:

(1) Either the violation did not result in investment losses to the Retirement Investor or the Financial Institution made the Retirement Investor whole for any resulting losses;

(2) The Financial Institution corrects the violation and notifies the Department of Labor of the violation and the correction via email to [IIAWR@dol.gov](mailto:IIAWR@dol.gov) within 30 days of correction;

(3) The correction occurs no later than 90 days after the Financial Institution learned of the violation or reasonably should have learned of the violation; and

(4) The Financial Institution notifies the person(s) responsible for conducting the retrospective review during the applicable review cycle and the violation and correction is specifically set forth in the written report of the retrospective review required under subsection II(d)(2).

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### ***Section III—Eligibility***

(a) *General.* Subject to the timing and scope provisions set forth in subsection (b), an Investment Professional or Financial Institution will be ineligible to rely on the exemption for 10 years following:

(1) A conviction of any crime described in ERISA section 411 arising out of such person's provision of investment advice to Retirement Investors, unless, in the case of a Financial Institution, the Department grants a petition pursuant to subsection (c)(1) below that the Financial Institution's continued reliance on the exemption would not be contrary to the purposes of the exemption; or

(2) Receipt of a written ineligibility notice issued by the Department for (A) engaging in a systematic pattern or practice of violating the conditions of this exemption in connection with otherwise non-exempt prohibited transactions; (B) intentionally violating the conditions of this exemption in connection with otherwise non-exempt prohibited transactions; or (C) providing materially misleading information to the Department in connection with the Financial Institution's or Investment Professional's conduct under the exemption; in each case, as determined by the Department pursuant to the process described in subsection (c).

#### *(b) Timing and Scope of Ineligibility.*

(1) An Investment Professional shall become ineligible immediately upon (A) the date of the trial court's conviction of the Investment Professional of a crime described in subsection (a)(1), regardless of whether that judgment remains under appeal; or (B) the date of the written ineligibility notice described in subsection (a)(2), issued to the

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Investment Professional.

(2) A Financial Institution shall become ineligible following (A) the 10<sup>th</sup> business day after the conviction of the Financial Institution or another Financial Institution in the same Controlled Group of a crime described in subsection (a)(1) regardless of whether that judgment remains under appeal, or, if the Financial Institution timely submits a petition described in subsection (c)(1) during that period, 21 days after the date of the Department’s written denial of the petition; or (B) 21 days after the date of the written ineligibility notice, described in subsection (a)(2), issued to the Financial Institution or another Financial Institution in the same Controlled Group.

(3) Controlled Group. A Financial Institution is in the same Controlled Group with another Financial Institution if it would be considered in the same “controlled group of corporations” or “under common control” with the Financial Institution, as those terms are defined in Code section 414(b) and (c), in each case including the accompanying regulations.

(4) Winding Down Period. Any Financial Institution that is ineligible will have a one-year winding down period during which relief is available under the exemption subject to the conditions of the exemption other than eligibility. After the one-year period expires, the Financial Institution may not rely on the relief provided in this exemption for any additional transactions.

(c) *Opportunity to be heard.*

(1) Petitions under subsection (a)(1).

(A) A Financial Institution that has been convicted of a crime described under

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subsection (a)(1) or another Financial Institution in the same Controlled Group may submit a petition to the Department informing the Department of the conviction and seeking a determination that the Financial Institution's continued reliance on the exemption would not be contrary to the purposes of the exemption. Petitions must be submitted, within 10 business days after the date of the conviction, to the Department by e-mail at [IIAWR@dol.gov](mailto:IIAWR@dol.gov).

(B) Following receipt of the petition, the Department will provide the Financial Institution with the opportunity to be heard, in person or in writing or both. The opportunity to be heard in person will be limited to one in-person conference unless the Department determines in its sole discretion to allow additional conferences.

(C) The Department's determination as to whether to grant the petition will be based solely on its discretion. In determining whether to grant the petition, the Department will consider the gravity of the offense; the relationship between the conduct underlying the conviction and the Financial Institution's system and practices in its retirement investment business as a whole; the degree to which the underlying conduct concerned individual misconduct, or, alternately, corporate managers or policy; how recent was the underlying lawsuit; remedial measures taken by the Financial Institution upon learning of the underlying conduct; and such other factors as the Department determines in its discretion are reasonable in light of the nature and purposes of the exemption. The Department will provide a written determination to the Financial Institution that articulates the basis for the determination.

(2) Written ineligibility notice under subsection (a)(2). Prior to issuing a written



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ineligibility notice, the Department will issue a written warning to the Investment Professional or Financial Institution, as applicable, identifying specific conduct implicating subsection (a)(2), and providing a six-month opportunity to cure. At the end of the six-month period, if the Department determines that the conduct persists, it will provide the Investment Professional or Financial Institution with the opportunity to be heard, in person or in writing or both, before the Department issues the written ineligibility notice. The opportunity to be heard in person will be limited to one in-person conference unless the Department determines in its sole discretion to allow additional conferences. The written ineligibility notice will articulate the basis for the determination that the Investment Professional or Financial Institution engaged in conduct described in subsection (a)(2).

(d) A Financial Institution or Investment Professional that is ineligible to rely on this exemption may rely on a statutory or separate administrative prohibited transaction exemption if one is available or seek an individual prohibited transaction exemption from the Department. To the extent an applicant seeks retroactive relief in connection with an exemption application, the Department will consider the application in accordance with its retroactive exemption policy as set forth in 29 CFR 2570.35(d). The Department may require additional prospective compliance conditions as a condition of retroactive relief.

#### ***Section IV—Recordkeeping***

The Financial Institution maintains for a period of six years records demonstrating compliance with this exemption and makes such records available, to the extent permitted

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by law including 12 U.S.C. § 484, to any authorized employee of the Department or the Department of the Treasury.

***Section V—Definitions***

(a) “**Affiliate**” means:

(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. (For this purpose, “control” would mean the power to exercise a controlling influence over the management or policies of a person other than an individual);

(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.

(b) Advice is in a Retirement Investor’s “**Best Interest**” if such advice 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.

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(c) 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.

(d) A “**Covered Principal Transaction**” is a principal transaction that:

(1) For sales to a Plan or an IRA:

(A) Involves 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, an interest in a Unit Investment Trust, or any investment permitted to be sold by an investment advice fiduciary to a Retirement Investor under an individual exemption granted by the Department after the effective date of this exemption that includes the same conditions as this exemption; and

(B) If the recommended investment is a debt security, the security is recommended pursuant to written policies and procedures adopted by the Financial Institution that are 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; and

(2) For purchases from a Plan or an IRA, involves any securities or investment property.

(e) “**Financial Institution**” means an entity that is not disqualified or barred from

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making investment recommendations by any insurance, banking, or securities law or regulatory authority (including any self-regulatory organization), that employs the Investment Professional or otherwise retains such individual as an independent contractor, agent or registered representative, and that is:

(1) Registered as an investment adviser under the Investment Advisers Act of 1940 (15 U.S.C. 80b-1 et seq.) or under the laws of the state in which the adviser maintains its principal office and place of business;

(2) A bank or similar financial institution supervised by the United States or a state, or a savings association (as defined in section 3(b)(1) of the Federal Deposit Insurance Act (12 U.S.C. 1813(b)(1)));

(3) An insurance company qualified to do business under the laws of a state, that:  
(A) has obtained a Certificate of Authority from the insurance commissioner of its domiciliary state which has neither been revoked nor suspended; (B) has undergone and shall continue to undergo an examination by an independent certified public accountant for its last completed taxable year or has undergone a financial examination (within the meaning of the law of its domiciliary state) by the state's insurance commissioner within the preceding five years, and (C) is domiciled in a state whose law requires that an actuarial review of reserves be conducted annually and reported to the appropriate regulatory authority;

(4) A broker or dealer registered under the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.); or

(5) An entity that is described in the definition of Financial Institution in an

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individual exemption granted by the Department after the date of this exemption that provides relief for the receipt of compensation in connection with investment advice provided by an investment advice fiduciary under the same conditions as this class exemption.

(f) For purposes of subsection I(c)(1), a fiduciary is “**independent**” of the Financial Institution and Investment Professional if: (i) the fiduciary is not the Financial Institution, Investment Professional, or an Affiliate; (ii) the fiduciary does not have a relationship to or an interest in the Financial Institution, Investment Professional, or any Affiliate that might affect the exercise of the fiduciary’s best judgment in connection with transactions covered by the exemption; and (iii) the fiduciary does not receive and is not projected to receive within the current federal income tax year, compensation or other consideration for his or her own account from the Financial Institution, Investment Professional, or an Affiliate, in excess of 2% of the fiduciary’s annual revenues based upon its prior income tax year.

(g) “**Individual Retirement Account**” or “**IRA**” means any plan that is an account or annuity described in Code section 4975(e)(1)(B) through (F).

(h) “**Investment Professional**” means an individual who:

(1) Is a fiduciary of a Plan or an IRA by reason of the provision of investment advice described in ERISA section 3(21)(A)(ii) or Code section 4975(e)(3)(B), or both, and the applicable regulations, with respect to the assets of the Plan or IRA involved in the recommended transaction;

(2) Is an employee, independent contractor, agent, or representative of a Financial

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Institution; and

(3) Satisfies the federal and state regulatory and licensing requirements of insurance, banking, and securities laws (including self-regulatory organizations) with respect to the covered transaction, as applicable, and is not disqualified or barred from making investment recommendations by any insurance, banking, or securities law or regulatory authority (including any self-regulatory organization).

(i) “**Plan**” means any employee benefit plan described in ERISA section 3(3) and any plan described in Code section 4975(e)(1)(A).

(j) A “**Related Entity**” is any party that is not an Affiliate, but in which the Investment Professional or Financial Institution has an interest that may affect the exercise of its best judgment as a fiduciary.

(k) “**Retirement Investor**” means:

(1) A participant or beneficiary of a Plan with authority to direct the investment of assets in his or her account or to take a distribution;

(2) The beneficial owner of an IRA acting on behalf of the IRA; or

(3) A fiduciary of a Plan or an IRA.

(l) A “**Senior Executive Officer**” is any of the following: the chief compliance officer, the chief executive officer, president, chief financial officer, or one of the three most senior officers of the Financial Institution.

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