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Department of Labor Issues Proposed Rules on Who is a Fiduciary

JOHN WIRTSHAFTER | TAX AND BENEFITS CHALLENGES | APR 16, 2015

ERISA provides special rules applicable to fiduciaries. These rules are designed to ensure that the fiduciary acts prudently and solely in the interests of plan participants and beneficiaries. Thus, such fiduciaries must ensure that the advice they are providing is in the best interest of their customer rather than in their own financial interest.

While ERISA provides that an individual who provides investment advice to a plan for a fee or other compensation is a fiduciary, regulations issued by the Department of Labor (DOL) in 1975 limited the application of who is treated as fiduciary for these purposes. By falling within these exceptions, many advisers have been able to avoid being treated as fiduciaries under the rules. This is particularly true for financial advisers providing advice with respect to the purchase of annuities or with respect to distributions and rollovers from retirement plans and IRAs. This has allowed them to avoid the restrictions imposed on fiduciaries by ERISA.

As the retirement universe has evolved from a trustee-directed to a more participant-directed investment model, the role of investment guidance and assistance for participants has become more important. For many years, the DOL has been attempting to clarify and expand the rules for when an individual providing investment advice to ERISA plans and participants qualifies as a “fiduciary” under ERISA. The DOL issued proposed rules on this subject back in 2010. However, the rules were pulled back in 2011 after a number of practitioners voiced concerns over them. We have been waiting patiently for the DOL to revise and reissue their guidance. Our wait ended earlier this week when the DOL issued 120 pages of proposed regulations on the subject. In addition, the DOL published a 250-page regulatory impact analysis, FAQs, and a fact sheet relating to the proposed rules.

The proposed rules are intended to provide greater protection to employee benefit plans and their participants and beneficiaries. The protections come from expanding the definition of a “fiduciary” for these purposes to include a broader group of investment and financial professionals and advisers. The protection extends fiduciary protections to the plan participants and beneficiaries by imposing the obligation on the advisers to act with the care, skill, prudence, and diligence in which a prudent person would act in such circumstance, and to act in the best interests of the plan participants and beneficiaries. One of the main goals of the rules is to better ensure such advisers fully disclose their fees and their conflicts in interest to the plan fiduciaries and plan participants and beneficiaries. Thus, for example, if the investment adviser is rewarded for steering funds to a particular family of mutual funds over others, this would need to be disclosed.

The proposed regulations provide for a number of exemptions that will permit some investment advisers to continue to provide services and collect fees in a manner that is consistent with their prior practices. However, the rules will require a full disclosure of such fees and any conflicts in interest, and will require the advisers to ensure they are acting in the best interest of the plan participants and beneficiaries.

We don’t expect the new rules will have a significant impact on how our clients manage their retirement plans. However, the rules will have a significant impact on how investment professionals working with ERISA plans will need to conduct their business. In the end, this should be good for participants and beneficiaries.

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Having designed and handled employee benefits and executive compensation issues in hundreds of business transactions involving over $30 billion, I bring a broad wealth of legal knowledge, experience and creativity to solving and resolving complex legal issues and problems.

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