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Client Alert

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Fiduciary Rule Delayed – But It's Not Entirely What Was Expected

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The DOL released the final regulation delaying applicability of the Fiduciary Rule and related exemptions by 60 days. This was expected, but the regulation includes some additional surprises – both as to specific terms and general policy. The three most important takeaways for most firms and advisers are:

- The expanded definition of "fiduciary" investment advice will become applicable on June 9, 2017, rather than April 10, 2017.
- PTE 84-24 will remain available for all annuity recommendations – fixed, fixed indexed and variable annuities – until January 1, 2018. The Impartial Conduct Standards will apply under PTE 84-24 on June 9, 2017, but the pre-Fiduciary Rule version of 84-24 will otherwise remain in place throughout 2017 (the three Impartial Conduct Standards are "Best Interest," no misleading statements, and reasonable compensation, but the pre-existing version of 84-24 already reflects a reasonable compensation limitation).
- During the transition period of the Best Interest Contract (BIC) Exemption, the only requirements that will apply are the Impartial Conduct Standards. This means, among other things, that no transition period disclosures will need to be provided. The transition period will now run from June 9, 2017, through December 31, 2017. Similar relief is provided under the "Principal Transactions" exemption.

Otherwise, the delay means the "old" rules will apply to the sale of investments (including insurance and annuities) and investment-related services to IRAs and ERISA-governed plans for another 60 days. This also means that – until June 9, 2017 – many firms and advisers will not be classified as fiduciaries and will not need to comply with a prohibited transaction exemption to do business.

The relief provided under PTE 84-24, although temporary, is also significant. Insurance intermediaries who would not qualify as "Financial Institutions" under the BIC Exemption will now be able to continue selling all types of annuities throughout 2017. This will give the DOL time to re-evaluate and finalize the proposed BIC Exemption for insurance intermediaries.

Those firms who do qualify as Financial Institutions under the "regular" BIC Exemption will be able to choose between 84-24 and transition BIC – when recommending all types of annuities - until December 31, 2017.

The delay regulation is effective April 10, but we expect it will be published in the Federal Register this week. This is the last step needed to make the delay official.

Further delays beyond June 9 may still be possible given the presidential order directing the DOL to review the Fiduciary Rule and decide whether it should be revised or withdrawn. However, the regulation indicates that the DOL does not intend to issue further delays, opting instead to provide broader prohibited transaction exemption relief through the end of the year. Even if further delays are issued, which now appears unlikely, they may not have the same level of significance as the delay regulation at hand.

At the same time, we do expect that there will be more changes made to the Rule and exemptions, following the DOL's review process. But at this point, we simply don't know what the changes will be, and we won't know for sure until later in 2017.

In issuing the regulation, the DOL noted that it had received about 193,000 comment letters, over 90 percent of which opposed any delay. In explaining its rationale for delaying the Rule despite widespread opposition, the DOL made two observations:

- A delay is necessary in order to "conduct a careful and thoughtful process pursuant to the Presidential Memorandum..."
- Because firms may have slowed down their compliance efforts in anticipation of a delay, "rigid adherence to the April 10 applicability date could result in an unduly chaotic transition to the new standards as firms rush to prepare required disclosure documents and finalize compliance structures that are not yet ready, resulting in investor confusion, excessive costs, and needlessly restricted or reduced advisory services."

However, the DOL clearly does not back down from the Fiduciary Rule and exemptions as a general matter. As the regulation's preamble explains, the DOL has

> "…concluded that it would be inappropriate to broadly delay application of the fiduciary definition and Impartial Conduct Standards for an extended period in disregard of its previous findings of ongoing injury to retirement investors."

In effect, the DOL is confirming that the new definition of fiduciary advice and the "Best Interest" standard of conduct (and other Impartial Conduct Standards) will apply on and after June 9, even as it completes its review of the Rule and decides how to proceed. Financial institutions and advisers providing investment recommendations related to IRAs and ERISA-governed plans will therefore be fiduciaries after June 9, but will be able to rely on expanded exemptive relief for "conflicted" compensation arrangements until January 1, 2018. This reflects a policy decision that is somewhat different than what many observers expected.

The DOL's rationale for its position is summarized as follows:

- There is widespread (though admittedly not universal) acceptance that the Impartial Conduct Standards are appropriate;
- Because firms and advisers will be acting under the relaxed transition rules, the risk of litigation, especially class action litigation, is at least reduced in the IRA context, which was a major concern expressed by those who oppose the Rule and exemptions;
- The approach selected is consistent with the DOL's "compliance-first posture toward implementation" – that is, the DOL's previously announced focus "on compliance assistance, both in the period before January 1, 2018, and for some time after";
- The approach provides more certainty for the financial services industry; and
- The DOL can always change things later on.

The impact of the delay regulation is somewhat of a mixed blessing. For firms that have spent a year or more on compliance, and substantial sums in the process, it is essentially a non-event — they have a 60-day delay to start implementing compliance. For others, the delay is a welcome relief because it gives them another 60 days to complete their compliance steps. Perhaps the biggest beneficiaries are firms involved in annuity sales, as they now have until the end of the year to figure out how to live with the new regulatory scheme.

The debate about the content of the Fiduciary Rule and the structure of the related exemptions is not over. Despite the DOL's statement about the possibility of major changes, we do not think the Rule will be scrapped altogether. Those who support a heightened fiduciary standard for financial service firms and their advisers will undoubtedly push for the Rule and exemptions to be retained without further changes. Those who oppose the Rule and exemptions, or certain aspects that they believe will harm retirement investors, will have a chance to advocate for modifications. Regardless of whose view the DOL follows, we think a compromise is likely. Only time will tell.

Employee Benefits and Executive Compensation Team

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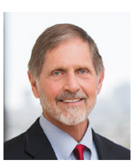

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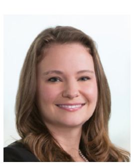

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