Advice About Advice: How Your Retirement Plan Will Be Impacted by the New Department of Labor Fiduciary Rule

August 25, 2016

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Agenda

- Fiduciary Rule Overview
- Exceptions and PTEs
- What Hasn't Changed?/What Has Changed?
- Investment Education & Participant Communications
- Distribution Counseling
- Selecting Service Providers and Investments
- Next Steps

Fiduciary Rule Overview—Importance of Fiduciary Status

- Fiduciaries:
  - Are subject to a "prudent expert" standard
  - Must perform their duties for the exclusive purpose of providing benefits to participants and beneficiaries
  - Must follow the terms of the plan
  - Must diversify
- Fiduciary breach may lead to personal liability
- Potential for co-fiduciary breach

Fiduciary Rule Overview—Prior Rule

- Five-part test:
  - Person renders advice about value or advisability of buying, selling, or investing;
  - On a regular basis;
  - Pursuant to a mutual agreement;
  - That the services will serve as a primary basis for investment decisions; and
  - The advice will be individualized to the plan

- Easy to avoid fiduciary status

Fiduciary Rule Overview—New Rule

- A person is a fiduciary if he provides advice for compensation about:
  - Buying, holding, selling or exchanging securities or other investment property; or
  - Managing securities, including rollover recommendations and selection of investment advisers
- And either:
  - Acknowledges fiduciary status;
  - Renders advice under agreement that advice is based on recipient’s particular needs; or
  - Provides individualized advice

Exceptions and PTEs

- Advisors selling investment products to financially sophisticated plans
- Certain plan sponsor employees offering advice in their capacity as employees
- Recordkeepers who merely present available investment options to plan sponsors

Exceptions and PTEs (cont.)

- Service providers who provide responses to replacement fund searches based on objective criteria

- Investment education

Exceptions and PTEs (cont.)

- PTEs allow fiduciaries to receive compensation from an otherwise prohibited transaction under ERISA
- DOL modified and revoked several existing PTEs
- Plan sponsors likely to see new disclosures/service agreements designed to fit modified PTEs

Exceptions and PTEs (cont.)

- Most important PTE is Best Interest Contract ("BIC") Exemption:
  - No contract required for ERISA plans
  - Fiduciary must comply with impartial conduct standards
  - Fiduciary cannot disclaim liability, limit class action rights, or impose certain requirements on arbitration
  - "Streamlined" BIC for level-fee fiduciaries

What Hasn’t Changed?

- Plan sponsor remains a fiduciary under ERISA
- Plan sponsor’s basic fiduciary obligations remain the same
- Plan sponsor remains bound by ERISA’s fiduciary obligations to select and monitor qualified service providers to the plan
  - Trustees
  - Recordkeepers
  - Investment advisors

What Hasn't Changed?—Sophisticated Fiduciaries

- Advice between service provider and sophisticated fiduciaries generally not investment advice. Generally, service provider must:
  - Know that plan fiduciary is sophisticated or holds at least $50 million and can evaluate risks independently
  - Inform plan fiduciary that advice is not impartial
  - Know or reasonably believe that plan fiduciary is an ERISA fiduciary; and
  - Not receive a fee or other compensation directly from the plan or fiduciary
- May be problematic for smaller plans

What Hasn’t Changed?—Platform Providers & Responses to Requests

- ► A service provider is generally not a fiduciary merely because it provides a platform
- ► Service providers do not become fiduciaries by responding to RFIs/RFPs
- ► Merely identifying investment alternatives based on objective criteria is not investment advice

What Has Changed?

- Rules about investment education/advice
- Rules about when distribution counseling is investment advice
- Some service providers who were not previously considered fiduciaries may now be fiduciaries
- Two responses:
  - Service providers will attempt to comply with the Fiduciary Rule
  - Service providers will attempt to recharacterize their relationship to avoid fiduciary status

Investment Education & Participant Communications

- General rule: investment education is not advice
- Four categories of investment education
  - Plan information
  - General financial, investment, and retirement information
  - Asset allocation models
  - Interactive investment materials
- Fiduciary Rule substantively similar to prior guidance, with some refinements and new conditions

Investment Education & Participant Communication (cont.)

- Plan sponsors should review any new participant communications and training programs prepared by service providers
- Plan sponsors likely to see:
  - Some references to specific investment alternatives removed
  - Less discussion of specific investment strategies
- Plan sponsors unlikely to be deemed fiduciaries because of internal educational materials

Investment Education & Participant Communication (cont.)

- Advice by employees in capacity as employees usually not investment advice. But:
  - No fee or other compensation beyond normal pay
  - If providing advice to employee in capacity as participant or beneficiary, must not require securities or insurance license

- No *de minimis* rule for compensation

Distribution Counseling

- Distribution counseling can be investment advice under Fiduciary Rule
- Some vendors may scale back communications about rollovers and distributions
- As a result, participants may have more questions for the plan sponsor about distribution options

Distribution Counseling (cont.)

- Plan sponsors traditionally not involved in distribution counseling
- In light of the Fiduciary Rule, plan sponsors:
  - Will want to oversee any distribution counseling provided to plan participants
  - May find that participants elect to leave assets in the plan following termination
- This trend may increase plan headcount, resulting in:
  - Increased plan costs
  - Additional leverage for sponsors to negotiate for lower fees on plan investments because of greater plan assets

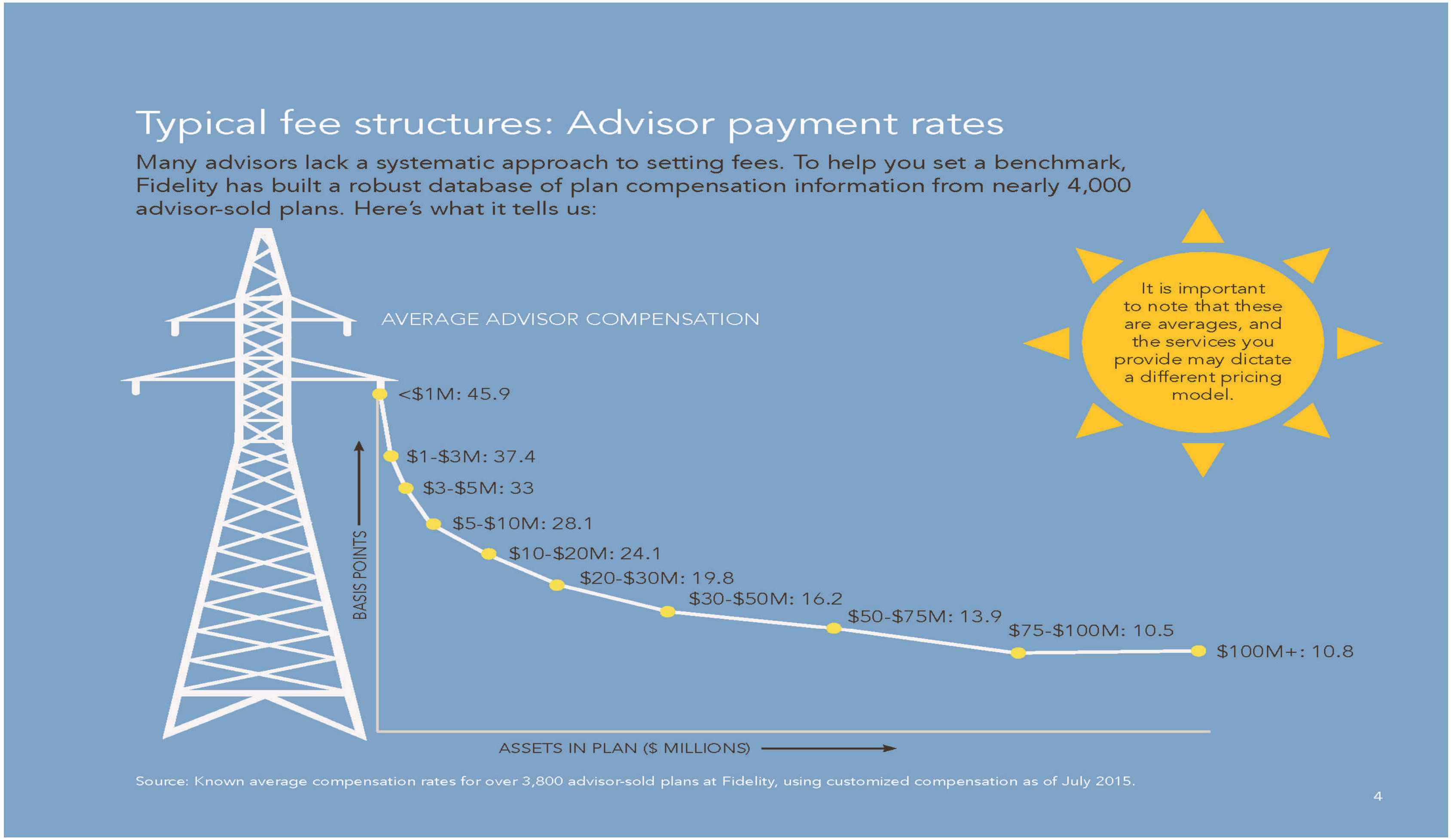
Selecting Service Providers and Investments—What Hasn't Changed?

- Plan fiduciaries should engage in an objective process designed to elicit information necessary to assess all relevant factors, including:
  - The qualifications of the provider
  - The quality of services offered
  - The reasonableness of the fees charged in light of the services provided

Selecting Service Providers and Investments—What Hasn't Changed? (cont.)

- Fiduciaries should consider:
  - Needs of the plan and the particular services to be provided
  - Experience and/or past performance of similarly situated plans handled by the service provider
  - Identity, experience and qualifications of staff that will be handling the plan's account or assets
  - Direct and indirect fees charged for the services
  - Existence of any conflicts of interest
  - Service provider's ability to provide information necessary for reporting purposes

Selecting Service Providers and Investments—What Hasn't Changed? (cont.)



Selecting Service Providers and Investments (cont.)

- Plan sponsors should work with service providers to determine:
  - Desired fiduciary status
  - Whether agreements need to be changed
- If there is a change to fiduciary status/terms of agreement, plan sponsors should evaluate fees
- Plan sponsors may need to consider RFPs if scope of services changes (e.g. service provider no longer offers distribution advice)

Selecting Service Providers and Investments (cont.)

- The Fiduciary Rule does not preclude:
  - A plan fiduciary from selecting investments managed by the plan recordkeeper's affiliates
  - Bundling of investment management and recordkeeping services
- Plan sponsors should ensure that they engage in a prudent investments selection process
- Plan sponsors should properly document process

Next Steps

- Review
  - Existing service provider relationships
    - Fee benchmarking
  - Investment education materials
  - Distribution counseling practices
  - Employee investment advice practices

Next Steps (cont.)

- Determine whether existing relationships/in-house practices need to be modified
  - Fiduciary governance review
- Consider educating participants about Fiduciary Rule
- Determine timetable for required changes

Questions?

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