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Fiduciary Rule and Attendant New Exemptions Become Law on June 9, 2017

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On April 4, 2017, the U.S. Department of Labor (DOL) officially extended the applicability date of the Fiduciary Conflict of Interest Rule for Retirement Investment Advice (Fiduciary Rule) and the Best Interest Contract (BIC) and the Principal Transaction class exemptions from April 10, 2017, to June 9, 2017. The applicability date of the Impartial Conduct Standards was also extended for the same 60-day period. This extension results from President Trump's February 3, 2017 memorandum instructing the DOL to review the Fiduciary Rule and determine whether modifications or rescissions are needed if it affirmatively finds that the Fiduciary Rule would: (1) limit investment advice to the investor community; (2) cause disruption in the financial industry; or (3) lead to an increase in litigation.

Effect of Extending the Applicability Date

The DOL's April 4 rule creates some degree of certainty, at least for the foreseeable future, that the Fiduciary Rule and the BIC and Principal Transaction class exemptions are here to stay, albeit with some modifications. At the same time, the DOL's decision to allow use of the BIC and Principal Transaction exemptions through January 1, 2018, by adhering only to the Impartial Conduct Standards creates hope, among some, that the more burdensome requirements of these exemptions may be eased prior to the current final phase-in date of January 1, 2018.

In the preamble to the April 4 rule, the DOL explained that it decided delaying full implementation of the Fiduciary Rule beyond a 60-day period would be inappropriate, after reviewing about 193,000 comments and letters in response to the proposal to delay the April 10, 2017 applicability date. The DOL noted that of the 193,000 comments, 15,000 supported a delay and 178,000 opposed any delay. The DOL also reasoned that the rigorous public debate on the Fiduciary Rule prior to issuance of the final rule on April 8, 2016, also militated against a longer extension during the period it considers the questions posed in President Trump's February 3 memorandum.

The original Fiduciary Rule implementation timeline included a transition period from April 10, 2017 through January 1, 2018, during which the requirements of the BIC and Principal Transaction exemptions would be phased in. Under the April 4 rule, the BIC and Principal Transaction class exemptions will be available to provide relief for covered transactions, but these exemptions will only require fiduciaries to adhere to the Impartial Conduct Standards during the revised transition period that begins June 9, 2017, and ends January 1, 2018. The Impartial Conduct Standards require that advisers make recommendations that: (1) are in the customer's best interest, commonly interpreted as consistent with ERISA's duties of prudence and loyalty standards; and (2) avoid misleading statements. The Impartial Standards Conduct also require that advisers charge no more than reasonable compensation. At the end of the transition period, the remaining conditions of the exemptions will become effective, unless they are revised or withdrawn based on the DOL's reconsideration.

The BIC and Principal Transaction exemptions imposed numerous requirement on advisers, well beyond adherence to the Impartial Conduct Standards, including implementing policies and procedures to ensure that material conflicts were mitigated, revisions of compensation structures to reduce conflicts of interests, and a written agreement with specific warranties and disclosures. The April 4 rule gives advisers relief from these other requirements through the transition period. The DOL will continue to collect comments from the public to determine what, if any, changes should be made to the other requirements of the BIC and Principal Transaction class exemptions while the DOL engages in the review instructed by President Trump's February 3 memorandum. The April 4 rule also delays full implementation of the amendments to Prohibited Class Transaction Exemptions 75-1, 77-3, 80-83, 83-1, 84-24, and 86-128. The Impartial Standards Conducts amendments to these exemptions, however, will be enforced during the transition period.

Impact

Financial institutions and other advisers now have certainty that the basic tenets of the Fiduciary Rule, which broadly expanded the definition of an investment advice fiduciary, will replace the DOL's 1975 regulations more narrowly defining investment advice fiduciary. While this change is significant, advisers have been readying for this change since at least April 8, 2016, when the Fiduciary Rule was released in final form in the Federal Register. The DOL hopes that the April 4 rule strikes a fair balance between the uncertainty that Trump's February 3 memorandum injected into the implementation process of the Fiduciary Rule by providing certainty on a June 9, 2017 applicability date for the Fiduciary Rule, the BIC and Principal Transaction exemptions, and the Impartial Standards Conduct. The April 4 rule, as noted, provides relief through the transition period of the many other more burdensome requirements of the exemptions while the DOL takes more time to undertake the review Trump requested in the February 3 memorandum. Whether some of the more burdensome provisions of the BIC and Principal Transaction exemptions survive this next round of review will remain to be seen.

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