CLIENT ALERT

Federal Court Invalidates Department of Labor ERISA Fiduciary Rollover Guidance

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A recent decision by the U.S. District Court for the Middle District of Florida (the "Court") has, for the moment, settled the long-debated issue of when advice to roll over assets from an Employee Retirement Income Security Act ("ERISA") plan to an individual retirement account ("IRA") may be considered "fiduciary" investment advice under ERISA.[1] Specifically, the Court ruled that the Department of Labor (the "DOL") was "arbitrary and capricious" in promulgating guidance that rollover advice provided to an ERISA plan participant as the beginning of an intended future ongoing relationship between the plan participant and investment advice provider constitutes "fiduciary" investment advice under ERISA. Accordingly, the Court's ruling has significantly narrowed the circumstances in which investment advisers who provide rollover recommendations to ERISA plan participants may be subject to fiduciary obligations under ERISA.

Below is a short history of the DOL's application of ERISA to plan participant rollover advice, followed by an overview of the Court's ruling and its potential implications for investment advisers.

Background

Under ERISA, "a person is a fiduciary with respect to a plan to the extent . . . he 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."[2] In 1975, the DOL issued a regulation clarifying this definition of "fiduciary" under ERISA (the "1975

[1] *American Securities Association v. Department of Labor*, No. 8:22-cv-330, 2023 U.S. Dist. LEXIS 24076 (M.D. Fl. Feb. 13, 2023).

[2] 29 U.S.C. § 1002(21)(A).

Regulation"). The 1975 Regulation provides a five-part test for determining when a person "renders investment advice" within the meaning of ERISA. Importantly, one prong of the test requires that such advice be given "on a regular basis to the plan."[3] In 2005, the DOL issued an advisory letter interpreting this "fiduciary" definition in the 1975 Regulation, stating that one-time advice regarding a rollover from an ERISA plan would generally *not* be considered fiduciary investment advice for purposes of ERISA.[4]

In 2016, the DOL amended the 1975 Regulation substantially. One important consequence of such amendment was that any recommendation to roll over or distribute assets from an ERISA plan would constitute "fiduciary" investment advice, but general investment information and education would not, absent an investment recommendation to an ERISA plan participant. In 2018, the U.S. Court of Appeals for the Fifth Circuit vacated this 2016 rulemaking, reasoning that the DOL's "interpretation of 'investment advice fiduciary' fatally conflicts with the [ERISA] statutory text and contemporary understandings."[5]

Following the 2018 Fifth Circuit ruling, the DOL promulgated Prohibited Transaction Exemption 2020-02 ("PTE 2020-02") in December 2020. PTE 2020-02 is a prohibited transaction exemption under ERISA that allows investment advice fiduciaries to receive various forms of otherwise prohibited compensation in consideration for providing investment advice to ERISA plans and IRAs, including rollover recommendations. Notably, in the preamble to PTE 2020-02, the DOL altered its interpretation of the five-part test in the 1975 Regulation, stating that the "regular basis" prong of the test is satisfied in the rollover context when an adviser "expects to regularly make investment recommendations regarding the IRA as part of its ongoing relationship," notwithstanding that such adviser may not have had a *prior* fiduciary relationship with the ERISA plan or plan participant.[6] Simply put, under this DOL interpretation, a one-time rollover recommendation to an ERISA plan participant could trigger ERISA fiduciary obligations on the part of the investment adviser even if the advisory relationship would be developed only in the future.

In April 2021, the DOL issued a set of frequently asked questions with respect to PTE 2020-02 (the "FAQ"). Importantly, and consistent with the DOL's revised interpretation of the "regular basis" prong articulated in the PTE 2020-02 preamble, FAQ No. 7 states that "when the investment advice provider has not previously provided advice but expects to regularly make investment recommendations . . . as part of an ongoing relationship, the advice to roll assets out of [an ERISA plan]

[3] 40 Fed. Reg. 50842 (Oct. 31, 1975).

[4] Advisory Opinion, 2005 – 23A (Dec. 7, 2005), available at https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/advisory-opinions/2005-23a.

[5] *Chamber of Commerce of the United States v. U.S. Department of Labor*, 885 F.3d 360 (5th Cir. 2018).

[6] Class Exemption and Interpretation, PTE 2020-02, available at https://www.federalregister.gov/documents/2020/12/18/2020-27825/prohibited-transaction-exemption-2020-02-improving-investment-advice-for-workers-and-retirees.

would be the start of an advice relationship that satisfies the regular basis requirement."[7] FAQ No. 7 was the subject of the Court's ruling, as discussed below.

American Securities Ruling

In 2022, the American Securities Association ("ASA"), a trade association of regional financial services firms, challenged the DOL's authority to promulgate PTE 2020-02 and filed a motion for summary judgment that sought to invalidate FAQ No. 7.[8] In its ruling, the Court first determined that ASA had standing to bring suit against the DOL, as at least one ASA member suffered a concrete injury-in-fact. Specifically, the Court reasoned that when the plaintiff is "an object of the action (or foregone action) at issue . . . there is ordinarily little question that the action or inaction has caused him injury, and that a judgment preventing or requiring the action will redress it."[9] One ASA member alleged that it no longer provides advice pertaining to rollover recommendations as a consequence of FAQ No. 7, and the Court found this effect on the member's operational and business decisions to be sufficient to establish an injury-in-fact to give the ASA standing to bring suit against the DOL.

The Court next determined that the policy referenced in FAQ No. 7 is not a reasonable interpretation of either the text of ERISA or the 1975 Regulation and is therefore not entitled to deference under the Administrative Procedures Act (the "APA"). The APA governs the procedures for federal regulatory agencies to develop and issue regulations and empowers courts to set aside agency actions, findings, or conclusions that are "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law[.]"[10] Notably, the Court stated that the policy referenced in FAQ No. 7 "impermissibly unmoors the focus of the inquiry into whether an individual is a fiduciary away from a specific ERISA plan, rendering it inconsistent with the statute and previous guidance."[11] The Court explained:

> Before a rollover occurs, a professional who gives rollover advice does so with respect to an ERISA-governed plan. However, after the rollover, any future advice will be with respect to a new non-ERISA plan, such as an IRA that contains new assets from the rollover. The professional's one-time rollover advice is thus the last advice that he or she makes to the specific plan. So, while an offer to provide future advice may, as the Department suggests, be the beginning of a relationship, that relationship is inherently divorced from the ERISA-

7 New Fiduciary Advice Exemption: PTE 2020-02, *Improving Investment Advice for Workers & Retirees*, Frequently Asked Questions (April 2021), available at https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/faqs/new-fiduciary-advice-exemption.

8 *American Securities Association*, 2023 U.S. Dist. LEXIS 24076 (M.D. Fl. Feb. 13, 2023).

9 *Id.* at 23 (quoting *Lujan v. Defs. of Wildlife*, 504 U.S. 555, 561–62 (1992)).

10 5 U.S.C. § 706(2)(A).

11 *American Securities Association*, 2023 U.S. Dist. LEXIS 24076, at 46 (M.D. Fl. Feb. 13, 2023).

> governed plan. Because any provision of future advice occurs at a time when the assets are no longer plan assets, it is not captured by the “regular basis” analysis.[12]

Accordingly, the Court held that because the policy referenced in FAQ No. 7 conflicts with the text of ERISA and the 1975 Regulation, it is an arbitrary and capricious interpretation of the 1975 Regulation. The Court vacated the policy referenced in FAQ No. 7, remanding it back to the DOL for further proceedings consistent with its order.

Implications

The Court’s ruling is somewhat unusual, in that it vacates a specific piece of DOL subregulatory guidance as opposed to a regulation promulgated by the DOL. The ruling is significant because it limits ERISA fiduciary status in the rollover advice context to investment advisers that have an *existing* relationship with an ERISA plan or ERISA plan participant. Such investment professionals who provide rollover advice with respect to an ERISA plan or plan participant will likely still need to rely on PTE 2020-02 in order to be paid for their advice. However, by virtue of the Court’s ruling, it appears that investment advisers who do not *already* have an existing fiduciary relationship with an ERISA plan client may now provide a one-time rollover recommendation without triggering ERISA fiduciary status.

It remains to be determined whether the DOL will appeal the Court’s order and, if it does, how the circuit court will decide the matter. Moreover, even if the decision stands, the DOL may seek to amend the 1975 Regulation through notice and comment rulemaking, to codify its current views regarding fiduciary status as it relates to rollovers. Thus, while the Court’s ruling is notable and important, it is unlikely to be the last word on this topic.

[12] Id. at 51.

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