

CLIENT ALERT

U.S. Department of Labor Proposes New Definition of ERISA “Fiduciary” and Related Amendments to Prohibited Transaction Exemptions

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On October 31, 2023, the U.S. Department of Labor (the “DOL”) released a proposed regulation titled Retirement Security Rule: Definition of an Investment Advice Fiduciary (the “Proposed Rule”) that, if adopted as proposed, would change the definition of “fiduciary” for purposes of the Employee Retirement Income Security Act of 1974, as amended (“ERISA”), and parallel provisions of the Internal Revenue Code of 1986, as amended (the “Code”), when an investment adviser or other financial professional provides investment advice.¹ In addition to the Proposed Rule, the DOL also proposed amendments to Prohibited Transaction Exemption 2020-02 (the “Proposed PTE 2020-02 Amendment”),² Prohibited Transaction Exemption 84-24 (the “Proposed PTE 84-24 Amendment”) and several other existing Prohibited Transaction Exemptions (together with the Proposed PTE 2020-02 Amendment and the Proposed PTE 84-24 Amendment, the “Proposed PTE Amendments”). The Proposed PTE Amendments would modify certain Prohibited Transaction Exemptions that advisers and financial professionals rely on when providing investment recommendations.³

¹ Retirement Security Rule: Definition of an Investment Advice Fiduciary, 88 FR 75890 (Nov. 3, 2023), available [here](#).

² Proposed Amendment to Prohibited Transaction Exemption 2020-02, Department of Labor (Oct. 31, 2023), available [here](#).

³ Proposed Amendment to Prohibited Transaction Exemption 84-24, Department of Labor (Oct. 31, 2023), available [here](#).

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The Proposed Rule describes the circumstances in which an adviser or other financial professional would be considered a “fiduciary” under ERISA and/or the Code when such professional provides investment recommendations to “retirement investors” (including ERISA plans, individual retirement accounts and other plans subject to Section 4975 of the Code (collectively, “IRAs”), participants in such plans, IRA owners, and fiduciaries to these plans). The Proposed PTE Amendments explain the conditions such advisers must follow to protect retirement investors from certain conflicts in those circumstances. As further described below, under the Proposed Rule, investment advice provided by an adviser would be subject to a fiduciary standard under ERISA, the Code, or both if the advice satisfies each prong of a new, three-part test. Importantly, if adopted as proposed, the Proposed Rule would likely mean that more investment advisers and other financial professionals would be deemed “fiduciaries” under ERISA and the Code.

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.”⁴

In 1975, the DOL issued a regulation clarifying this definition of “fiduciary” under ERISA and the Code (the “1975 Regulation”). The 1975 Regulation provides a five-part test for determining when a person “renders investment advice” within the meaning of ERISA (and parallel provisions of the Code in the case of IRAs). Importantly, one prong of the test requires that such advice be given “on a regular basis to the plan.”⁵

There is a long saga between the DOL and the courts as to whether an investment adviser provides investment advice as a “fiduciary” under ERISA when the adviser provides an IRA rollover recommendation to an ERISA plan participant. An important event in this saga was the DOL’s promulgation of Prohibited Transaction Exemption 2020-02 (“PTE 2020-02”) in December 2020. Notably, in the preamble to PTE 2020-02, the DOL clarified 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 recent 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.

⁴ 29 U.S.C. § 1002(21)(A).

⁵ 40 Fed. Reg. 50842 (Oct. 31, 1975).

⁶ Class Exemption and Interpretation, PTE 2020-02, available [here](#).

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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 discussed 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] would be the start of an advice relationship and satisfies the regular basis requirement.”⁷ Shortly after the FAQ was issued, the American Securities Association, 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 *American Securities Association*, the U.S. District Court for the Middle District of Florida (“the Court”) 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. Notably, the Court found 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.”⁹ 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 therefore vacated the policy referenced in FAQ No. 7, remanding it back to the DOL for further proceedings consistent with its order.

The DOL filed a notice of appeal regarding the opinion and all other adverse rulings on April 14, 2023. However, the DOL abandoned the appeal, and a motion to voluntarily dismiss the appeal was granted on May 18, 2023. The DOL announced its intention to issue the Proposed Rule and Proposed PTE Amendments shortly thereafter.

Proposed Rule

Perhaps partly in response to the ruling in *American Securities Association*, the Proposed Rule notably replaces the five-part test under the 1975 Regulation with a three-part test that, among other things, significantly expands the “regular basis” element of the test. Under this new test, an adviser would be a fiduciary if:

- the provider renders investment advice or makes an investment recommendation to a retirement investor,
- the advice or recommendation is provided for a fee or other compensation, direct or indirect, and

⁷ New Fiduciary Advice Exemption: PTE 2020-02, *Improving Investment Advice for Workers & Retirees*, Frequently Asked Questions (April 2021), available [here](#).

⁸ *American Securities Association v. Department of Labor*, No. 8:22-cv-330, 2023 U.S. Dist. LEXIS 24076 (M.D. Fl. Feb. 13, 2023). For a discussion of the *American Securities Association* ruling, please see the Willkie Farr & Gallagher LLP Client Alert, available [here](#).

⁹ *American Securities Association*, 2023 U.S. Dist. LEXIS 24076, at 46 (M.D. Fl. Feb. 13, 2023).

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- the adviser makes the recommendation in the context of a professional relationship in which the retirement investor would reasonably expect to receive sound investment recommendations that are in the retirement investor’s best interest, in one of the following circumstances:
 - the provider has discretion over investment decisions for the retirement investor;
 - the provider makes investment recommendations to investors on a regular basis as part of its business, and the recommendation is provided under circumstances indicating that the recommendation is based on the particular needs or individual circumstances of the retirement investor and may be relied upon by the retirement investor as a basis for investment decisions that are in the retirement investor’s best interest; or
 - the provider states that they are acting as a fiduciary when making investment recommendations.

This new test reframes the meaning of “regular basis” to include one-time rollover advice by shifting the focus from the regularity of interactions between an adviser and a particular retirement investor to the regularity of investment recommendations made by the adviser as part of its overall business. Previously, one-time rollover advice arguably was not captured under the 1975 Regulation’s five-part test, as articulated in the *American Securities Association* ruling. Unlike the 1975 Regulation, under the Proposed Rule an adviser providing advice on a one-time basis, such as a one-time IRA rollover recommendation, would likely be required under ERISA to make recommendations that are in the retirement investor’s best interest and to avoid engaging in transactions prohibited by ERISA and parallel provisions of the Code.

Proposed PTE Amendments

In addition to the Proposed Rule, the DOL released Proposed PTE Amendments that apply to investment advice fiduciaries. Currently, the Prohibited Transaction Exemptions allow advisers to receive compensation for advice that would otherwise be prohibited by ERISA and the Code, as long as the advisers comply with the exemptions’ conditions.

The Proposed PTE 2020-02 Amendment maintains all of PTE 2020-02’s core provisions but makes clarifying changes that build on existing conditions that are intended by the DOL to provide additional protections for retirement investors and more certainty for fiduciary investment advisers. It requires, among other things, that additional disclosures be made to retirement investors and stricter policies and procedures on the part of advisers and other financial professionals.

The Proposed PTE 84-24 Amendment would limit coverage for advice to independent insurance agents. It also provides relief for insurance agents receiving compensation in connection with the sale of insurance products to retirement investors that would otherwise be prohibited for investment advice transactions, subject to conditions similar to those in PTE 2020-02.

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Implications

Under the Proposed Rule, various advice, including recommendations on plan distributions, including rollovers, recommendations regarding the purchase of insurance products, and recommendations to entrust plan assets to a particular financial professional, would fall within the scope of “fiduciary” investment advice. The Proposed Rule and Proposed PTE Amendments, if adopted as proposed, would affect the manner in which broker-dealers, investment advisers, and insurance companies and agents, among others, provide investment advice to retirement investors. It would likely result in more of these entities and individuals being investment advice fiduciaries under ERISA and the Code and require corresponding compliance with Prohibited Transaction Exemptions, as amended by the Proposed PTE Amendments.

We continue to monitor developments in this area.

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