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WHITE PAPER

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# The DOL's Final "Fiduciary" Rule—Countdown to Implementation Begins in Earnest

Perhaps bringing some finality to a process initiated in 2010, the U.S. Department of Labor has issued final regulations (the "Final Rule") defining who is a fiduciary as a result of providing "investment advice" to employee benefit plans covered by established regulations. The Final Rule retains the basic structure of the earlier Proposed Rule but includes clarifications and adjustments in response to public comments. Still, the Final Rule, which becomes applicable on April 10, 2017, will have significant impact on how investment services and products are provided and marketed to retirement plan investors.

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On April 6, 2016, the Department of Labor ("DOL") issued final regulations ("Final Rule") defining who is a fiduciary as a result of giving "investment advice" to an employee benefit plan subject to the Employee Retirement Income Security Act ("ERISA") or an individual retirement account ("IRA"). The DOL also issued a revised Best Interest Contract Exemption ("BIC Exemption") and other related prohibited transaction exemptions that are designed—at least in the DOL's view—to make the Final Rule workable in practice. The rules were originally proposed in 2010, withdrawn in 2011, and then re-proposed in 2015 ("Proposed Rule").

The DOL received more than 3,000 comment letters and held four days of hearings regarding the Proposed Rule. Although many commentators asked the DOL to re-propose the rules and provide another opportunity for comments, the DOL chose to forge ahead and publish the rules in final form. The Final Rule becomes applicable on April 10, 2017, although the implementation of certain compliance matters is delayed until January 2018.

The Final Rule retains the basic structure of the Proposed Rule but includes many clarifications and adjustments to address public comments. To the extent certain comments and objections have been favorably addressed, the Final Rule is an improvement when compared to the Proposed Rule. Nevertheless, the Final Rule will have a dramatic impact on how investment services and products are provided and marketed to retirement plan investors.

## STRUCTURE OF THE FINAL RULE

The general approach of the Final Rule is similar to the Proposed Rule—to apply a very broad definition of "fiduciary advice," tempered by limited exceptions and other examples of conduct that is not "fiduciary" in nature. The Final Rule replaces the 1975 "five-part test." One of the avowed objectives of the Final Rule is to significantly expand the universe of investment professionals, advisers, and other service providers who can be held liable under the fiduciary standards of ERISA, especially in the retail market for IRAs and smaller ERISA plans. By making more advisers "fiduciaries," the DOL's proposal will subject more advisers to conflict of interest restrictions and, in many cases, impose ERISA-like duties on IRA advisers to whom the statutory rules of ERISA do not apply.

The Final Rule provides that a person becomes an investment fiduciary if the person provides to a plan, plan fiduciary, plan participant or beneficiary, IRA, or IRA owner any of the following types of advice for a fee or other compensation, direct or indirect:

- A recommendation as to the advisability of acquiring, holding, disposing of, or exchanging securities or other investment property, or a recommendation as to how securities or other investment property should be invested after the securities or other investment property are rolled over, transferred, or distributed from a plan, including a recommendation to take a distribution from a plan or IRA, or with respect to investments related to a rollover; or
- A recommendation as to the management of securities or other investment property, including, among other things, recommendations on investment policies or strategies, portfolio composition, selection of other persons to provide investment advice or investment management services, or selection of investment account arrangements (e.g., brokerage versus advisory); or recommendations with respect to rollovers, transfers, or distributions from a plan or IRA, including whether, in what amount, in what form, and to what destination such rollover, transfer, or distribution should be made.

In addition, the recommendation must have been made either directly or indirectly (e.g., through or together with any affiliate) by a person who:

- Represents or acknowledges that it is acting as a fiduciary;
- Renders the advice pursuant to a written or verbal agreement, arrangement, or understanding that the advice is based on the particular investment needs of the advice recipient; or
- Directs the advice to a specific advice recipient or recipients regarding the advisability of a particular investment or management decision with respect to securities or other investment property of the plan or IRA.

Under the Final Rule, fiduciary investment advice cannot exist without a recommendation. For purposes of the Final Rule, the term "recommendation" means a communication that, based on its content, context, and presentation, would *reasonably be viewed as* a suggestion that the advice recipient engage in or refrain from taking a particular course of action. Unlike the Proposed Rule, the Final Rule includes a nonexhaustive list of examples of types of communications that are not "recommendations," and therefore are not subject to fiduciary standards. The DOL emphasized that even if a particular communication does not fall within any of the examples, that does not mean it is necessarily a fiduciary communication. A particular communication will be treated as fiduciary investment advice only if it is a "recommendation" and otherwise is captured by the Final Rule.

In a key clarification, the Final Rule provides that the determination of whether a "recommendation" has been made is an objective rather than subjective inquiry. The more individually tailored the communication is to a specific advice recipient, the more likely the communication will be viewed as a recommendation. Furthermore, a series of actions that may not constitute recommendations when viewed individually may amount to a recommendation when considered in the aggregate.

The Final Rule also includes an improved set of transactions and investment advice activity that are not considered investment advice, even if they meet the definition of a "recommendation" (previously called "carve-outs" in the Proposed Rule, but the DOL dropped the carve-out terminology in the Final Rule). For example, the "seller's exception" for investment advice provided to sophisticated plan investors was modified, so that the impact of the Final Rule should largely be limited to retail retirement investors. However, the DOL declined to adopt the suggestion that all transactions be exempted if they were with "accredited investors" or some other definition designed to identify wealthy customers.

## KEY CHANGES IN FINAL RULE

To accompany the Final Rule, the DOL published a summary of changes and a chart describing some of the ways the DOL addressed comments to the Proposed Rule. Among other things, the Final Rule:

- Attempts to clarify the standard for determining whether a person has made a "recommendation" covered by the Final Rule;
- Attempts to clarify that marketing oneself or one's services without making an investment recommendation is not fiduciary investment advice;
- Removes appraisals, valuation reports, and other statements of value from the rule—thus providing that valuation statements and reports cannot be investment advice without a recommendation;
- Allows asset allocation models and interactive materials to identify specific investment products or alternatives for ERISA plans (but not IRAs) without being considered fiduciary investment advice, subject to conditions; and
- Provides an expanded seller's exception for recommendations to independent fiduciaries of plans and IRAs with financial expertise and plan fiduciaries with at least $50 million in assets under management, subject to conditions.

As summarized by the DOL, some of the other key changes (from the DOL's point of view) include:

| Issue | Criticism of Proposal | What Changed in Final Rule |
|---|---|---|
| Education | The DOL should establish a clear line between education and investment advice and avoid a result in which service providers refrain from providing essential information and education to participants and investors due to concerns about triggering fiduciary status. In addition, when using asset allocation models to educate participants and investors, service providers should be able to identify specific investment options. | The Final Rule clearly describes the types of information and activities that constitute nonfiduciary investment education—including plan information and general financial, investment, and retirement information.<br><br>The DOL also revised the Final Rule to allow asset allocation models and interactive investment materials to identify specific investment alternatives under ERISA-covered and other plans if certain conditions are met.<br><br>However, in the IRA context, there is no independent plan fiduciary to review and select investment options so references to specific investment alternatives are not treated as education under the education provision in the Final Rule. |
| Coverage of health and welfare arrangements | The proposal could be read to apply to group health, dental, and disability insurance policies. The DOL should explicitly exclude these policies, which do not raise the concerns the DOL appears to be addressing with respect to advice regarding investment property. | The DOL clarified that advice regarding "investment property" does not include health, disability, and term life insurance policies and other assets that do not contain an investment component. |
| Appraisals | All appraisals and valuations, not just for ESOPs, should be excluded from the rule and addressed separately. | The DOL has reserved all appraisal issues, not just those involving ESOPs, for separate future rulemaking. |
| "Hire me" | An adviser should be able to recommend that the customer hire the adviser for a reasonable fee without that recommendation to "hire me" being treated as a fiduciary recommendation. | The DOL has made clear in the Final Rule that a person or firm can recommend that the customer hire the adviser (or its affiliate) for advisory or asset management services without the recommendation counting as a fiduciary recommendation.<br><br>However, the adviser's investment recommendations, such as the recommendation to roll money out of a plan or invest in a particular investment, are fiduciary recommendations. |
| Inappropriate bias toward low fee products | The proposal favors low-fee and low-cost products over all else, ignoring returns, quality, and other factors that may be important to consumers. | The DOL did not adopt the low-fee streamlined option considered in the proposal and clarified in the preamble that the adviser is not required to recommend the lowest fee option if another product is better for the client. |

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| Grandfather relief | The DOL should treat existing arrangements and investments differently than new transactions. | The DOL included a grandfathering provision that allows for additional compensation based on investments that were made prior to the April 10, 2017, applicability date.<br><br>It includes compensation from recommendations to hold, as well as systematic purchase agreements, but requires that after the April 10, 2017, applicability date, additional advice must satisfy basic best interest and reasonable compensation requirements. |
| Implementation concerns | Eight months is far too short a time period to implement such an expansive overhaul. The DOL should consider phased implementation and/or an implementation safe harbor. | The DOL extended the first phase of implementation to one year after publication of the Final Rule. In addition, the DOL adopted a "phased" implementation approach for the BIC Exemption and the Principal Transaction exemption so that firms will have more time to come into full compliance. In particular, the full disclosure provisions, the policies and procedures requirements, and the contract requirement do not go into full effect until January 1, 2018. Finally, the DOL made it clear that it intends to provide compliance assistance to firms that have implementation questions to the greatest extent possible. |

## BEST INTEREST CONTRACT EXEMPTION ("BIC EXEMPTION")

ERISA and the Internal Revenue Code generally prohibit fiduciary advisers to plans and IRAs from receiving compensation that varies based on their investment advice. Similarly, fiduciary advisers are prohibited from receiving compensation from third parties in connection with their advice. Because many brokers and other advisers who previously were not fiduciaries would become so under the Final Rule, many common types of compensation—such as commissions, trailing commissions, revenue sharing, and 12b-1 fees—would become prohibited without some form of relief. Accordingly, in connection with the Final Rule, the DOL published a revised BIC Exemption in an effort to accommodate a wide range of current types of compensation practices (e.g., commissions) that would otherwise become prohibited as a result of the Final Rule's expansion of the fiduciary universe.

The BIC Exemption is a critical component of the Final Rule framework. For brokers and other advisers in the IRA market who choose to continue a compensation model including commissions and other transaction-based or variable compensation, the practical need to use the BIC Exemption will, in effect, make such brokers and advisers subject to ERISA's fiduciary requirements, despite the fact that Congress chose not to do so in the language of ERISA itself.

At the heart of the BIC Exemption is the obligation of the adviser to comply with an "Impartial Conduct Standard," including the obligation to provide advice that is in the "Best Interest" of the retirement investor. The Best Interest standard blends the duties of prudence and loyalty under ERISA and requires recommendations to be based on the investment objectives, risk tolerance, financial circumstances, and needs of the retirement investor, without regard to the financial or other interests of the adviser or any other party.

The Impartial Conduct and Best Interest standards must be included in a contract with the investor (other than ERISA plans), and financial institutions must adopt prudent and reasonable policies and procedures designed to prevent violations of those standards. The adviser must acknowledge that it is acting as a fiduciary for the retirement investor, but the adviser's acknowledgment can be limited to the recommendations subject to the BIC Exemption contract. In other words, a blanket acknowledgment is not required—the contractual acknowledgment can be limited "to the extent" of the particular recommendations covered by the arrangement.

## CHANGES TO BIC EXEMPTION

The DOL made significant changes to the BIC Exemption in response to the torrent of comments, and in significant ways, it made the exemption more workable. Whether the changes are enough to induce financial institutions to adopt the BIC Exemption is yet to be seen. Among the changes made to the BIC Exemption, the DOL:

- Eliminated the "asset list" entirely; thus, the BIC Exemption can apply to any investment product if the other conditions of the exemption are satisfied;
- Expanded the coverage of the BIC Exemption to include advice provided to sponsors of small 401(k) plans;
- Eliminated the formal contract requirement for ERISA plans and participants (because the remedies available under ERISA are already similar to the remedies created under the BIC Exemption);
- Improved the timing rules for the BIC Exemption contract—it no longer requires contract execution prior to advisers' recommendations;
- Allowed the required contract terms to be incorporated in account-opening documents;
- Authorized a "negative consent" process for existing clients to avoid having to get new signatures from those clients;
- Simplified execution of the contract by requiring the financial institution to execute the contract rather than also requiring each individual adviser to sign;
- Clarified how a financial institution that limits its offerings to proprietary products can satisfy the BIC Exemption;
- Provided more streamlined compliance for advisers that recommend a rollover from a plan to an IRA, or who recommend moving from a commission-based account to a fee based account, if the adviser will receive only level fees (but the DOL clarified that such recommendations are fiduciary in nature and likely require an exemption);
- Eliminated or streamlined the data collection and disclosure requirements (although they are still substantial);
- Permitted a financial institution to provide the most detailed disclosures envisioned by the BIC Exemption only upon request; and
- Provided a mechanism to correct good faith violations of the disclosure conditions without losing the benefit of the exemption (but the financial institution will have to act quickly to correct even good faith violations).

As summarized by the DOL, some of the key changes to the BIC Exemption (again, from the DOL's point of view) include:

| Issue | Criticism of Proposal | What Changed in Final Rule |
|---|---|---|
| Small Businesses | By excluding small plans from the proposed “seller’s carve-out,” the DOL will deprive small businesses of essential advice, because the BIC Exemption did not provide relief to sponsors of participant-directed plans. | The DOL has made the BIC Exemption available to small plans of all types.<br><br>Further, the proposed “seller’s carve-out” has been substantially revised and is now available to any plan that is represented by an independent fiduciary with financial expertise that satisfies specified criteria or has $50M in assets. |
| Asset list in BIC Exemption | By listing only certain asset classes to be covered by the BIC Exemption, the proposal limits investor choice. | The DOL has eliminated the list so that advice to invest in all asset classes is covered by the BIC Exemption. |
| Timing of the contract | The contract requirement is unwieldy, calls for the signatures of too many parties, and must be executed too early in the process—before the customer even knows he or she will make an investment | The contract requirement was eliminated for ERISA plans; it applies only to IRAs and other non-ERISA plans.<br><br>The DOL also adjusted the contract requirement to make it clear that it can be incorporated into other account opening documents and can be entered into before or at the same time the recommended transaction is executed. Any advice given before the contract was signed must be covered by the contract.<br><br>The exemption provides a special “negative consent” procedure for existing clients to obtain the new protections. In other words, the firm can send out a notification to its clients informing them of proposed contract amendments. If the client does not terminate the amended contract within 30 days, the amended contract is effective.<br><br>There is also a provision for advisers who provide advice in accordance with the conditions of the exemption, but due to circumstances beyond their control, the contract was not executed. |
| Call centers and required contract parties | There is a lot of uncertainty about the role and ability of call centers to interact with customers under the new regime. In particular, since the contract requirement requires signatures of the firm, the adviser, and the client, will a new contract need to be signed every time the client speaks to another employee of the same firm (such as a different call center representative)? | The DOL modified the contract requirement so that the contract is between the firm and the client, and a new contract will not be required for each interaction with a different employee of the same firm. |
| Disclosure | The disclosure requirements of the BIC Exemption are overly cumbersome. In particular, the one-, five-, and 10-year projections are nearly impossible to execute. | The DOL significantly streamlined the disclosure requirements in the final BIC Exemption. In particular, requirements to include projections, as well as the annual disclosure requirement, have been entirely eliminated. |
| Web Disclosure | The web disclosure requirements are too burdensome for firms and could be read to require disclosure of individual adviser compensation and salaries. | The DOL has streamlined this provision and clarified that individualized information about advisers is not required. |
| Data Retention | The data retention requirements that called for the retention of detailed information on inflows and outflows are too burdensome. | The DOL has removed those requirements. Just as they would in other situations, firms have to retain only the records that show they complied with the law (in this case, the BIC Exemption or other exemption). |

| Issue | Criticism of Proposal | What Changed in Final Rule |
|---|---|---|
| Proprietary Products | The requirement to recommend the product that is in the client's best interest will force advisers to recommend another company's products instead of their own (because their financial interest in their own products means they could never say it was solely in the client's best interest). | The DOL has included language in the BIC Exemption to make clear that advisers may continue to sell proprietary products and has provided specific guidance on how proprietary product providers can satisfy the best interest standard. |
| Lifetime income products | The focus on fee transparency in the proposal disadvantages lifetime income options and other insurance products, whose value—particularly the guaranteed lifetime income—may not be as easily understandable by consumers. | The DOL has included language in the BIC Exemption to make clear that advisers may recommend insurance products and revised the disclosure provisions to better reflect how insurance products are sold.<br><br>In addition, the final amendment to PTE 84-24 provides a streamlined exemption for recommendations of "fixed rate annuity contracts," which are less complex lifetime income products |
| Recommendations to move into a level fee arrangement | Advisers would be discouraged from making recommendations to plan participants to move into an investment advisory arrangement with a level fee, i.e., rollover recommendations. Plan advisers who receive level compensation from a retirement plan, and would receive level compensation for advice provided to an IRA rollover from a retirement plan, would be discouraged from working with plan participants on rollovers. The DOL should address this so that advisers are treated the same regardless of whether they have a relationship to the plan and regardless of the fee structure they use. | The DOL added a special provision for level fee fiduciaries in the final BIC Exemption. Essentially, it requires that documentation is kept to show why a recommendation to roll over from a plan or IRA to a level fee arrangement or to switch from a commission to a level fee arrangement was in the customer's best interest. |
| Conversions to fee-based accounts | The proposal will effectively prohibit commissions. | The DOL clarified this issue by, among other changes, providing examples of policies and procedures that are compatible with commission-based models. In addition, the DOL notes that if moving a customer into a fee-based model is not in that customer's best interest, the firm/adviser would have engaged in a nonexempt prohibited transaction. |

## EFFECTIVE DATE, APPLICABILITY DATE, AND TRANSITION PERIOD

The Final Rule becomes effective 60 days after publication in the Federal Register. However, the Final Rule does not become applicable until one year after publication—April 10, 2017.

In addition, the DOL adopted a "phased" implementation approach for the BIC Exemption and certain other exemptions, which gives financial institutions more time to come into full compliance. In particular, the BIC Exemption contract requirement, the policies and procedures requirements, and certain disclosure requirements will not become effective until January 1, 2018.

## PREEXISTING TRANSACTIONS

To ease the transition for financial institutions and advisers that are now more clearly recognized as fiduciaries under the Final Rule, the DOL expanded the "grandfathering" relief in the BIC Exemption for compensation in connection with investments acquired before April 10, 2017 (as long as the advice arrangement did not expire or come up for renewal after April 10, 2017). The exemption permits continued receipt of compensation based on investment transactions that occurred before April 10, 2017, as well as receipt of compensation for recommendations to continue to follow a systematic purchase program established before April 10, 2017.

The exemption also explicitly covers compensation received as a result of a recommendation to hold an investment that was acquired before April 10, 2017 (which was not clear under the Proposed Rule). However, to be grandfathered, the compensation cannot be received in connection with the plan or IRA's investment of additional amounts in the previously acquired investment. Presumably, this "investment of additional amounts" limitation should be interpreted in a way that does not nullify the exemption for additional investments made pursuant to a "pre-existing recommendation to continue to follow a systematic purchase program."

Any advice given after April 10, 2017, however, even with respect to a preexisting account, must comply with the best interest standard of the BIC Exemption. Note, also, that even in the case of a grandfathered preexisting arrangement, the compensation paid (directly or indirectly) in connection with the grandfathered transaction must not be in excess of reasonable compensation (which effectively applies some aspect of the BIC Exemption even to grandfathered arrangements). In addition, some comments had requested broader grandfather relief that would have exempted all current IRA and retirement plan accounts and investors, and the DOL declined to provide such broad relief.

## PRELIMINARY OBSERVATIONS

The Final Rule, BIC Exemption, and associated other exemptions weigh in at just over 1,000 pages. As you might expect, it will take some time to digest the full impact of the Final Rule and related exemptions on financial professionals, plan sponsors, plan fiduciaries, investment fund sponsors, third-party service providers, and others. With that caveat in mind, the following are some of our preliminary observations:

- The Final Rule is an improvement over the proposal, but that is only a generalization. For particular clients, the Final Rule and related exemptions could still require significant changes in policies, procedures, and compensation models, especially in the retail market for IRAs and smaller ERISA plans. Whether the BIC Exemption will be workable still remains to be seen, despite the clarifications and improvements.
- Furnishing or making available general communications that a reasonable person would not view as an investment recommendation is not subject to the Final Rule. The delivery of a prospectus is expressly included as this type of general communication, and thus not treated as a recommendation subject to the Final Rule. In general, the structure of the Final Rule gives fund sponsors more basis for contending that their sales activities should not be treated as a "recommendation," since in many cases it will be clear that neither side assumes that the counterparty to the plan is acting as an impartial or trusted adviser. The Preamble indicated that the DOL did not intend to depart from a "plain and natural reading" of the term "investment advice" in the statutory text of ERISA.
- The DOL also stated (in the Preamble only) that a communication must involve a "call to action" in order to rise to the level of a recommendation. The DOL looked to similar conclusions under existing FINRA interpretations but stopped short of a wholesale incorporation of FINRA interpretations of "recommendation"—in large part to avoid the DOL losing control of its rule to another agency. The DOL also made it clear that the "suitability" standard of FINRA and securities law is not as high as the "best interest" standard under the BIC Exemption, although a recommendation that is not suitable will clearly fall short of the best interest standard (i.e., suitability is a necessary, but not sufficient, condition of a best interest recommendation).
- Sponsors of pooled investment funds will likely start to modify subscription agreements and offering documents to anticipate the "seller's carve-out" for transactions with institutional ERISA investors.
- In the retail environment, the Final Rule continues to reflect the DOL's rejection of any distinction between mere "sales" activity and "advice" when communications are directed to the investor. In that context, the DOL is much more likely to conclude that all facts and circumstances, taken together, support a conclusion that a "recommendation" is being made unless the contrary evidence is clear (e.g., the mere execution of orders).

- By removing the "asset list" in the BIC Exemption, the scope of the exemption expands significantly, and comes closer to becoming the "principles-based" approach intended by the DOL.

- The BIC Exemption does not prohibit all conflicted compensation, nor does it prohibit conflicts of interest. Instead, it requires advisers to *manage* the conflicts so as to demonstrate that their investment advice was in the best interest of the investor notwithstanding the potential for conflict (e.g., in a simple setting, by concluding that a commission-based account is more appropriate for a buy-and-hold investor). This is potentially a far-reaching shift from the traditional approach of the DOL (and many ERISA professionals) to regard similar conflicts as *per se* violations of ERISA.

- Failure to adhere to the BIC Exemption will result in *both* a violation of the BIC Exemption contract and a prohibited transaction subject to excise tax. In the public hearings on the Proposed Rule, officials of the DOL took the position that violation of the contract terms would result only in contractual liability but would not invalidate the exemption itself (implying that people reading the Proposed Rule more broadly were needlessly concerned). Now, the double exposure is clearly stated.

- The Final Rule makes it clear that recommendations to move from a commission-based account to an advisory fee-based account is fiduciary investment advice and would have to be made in the customer's best interest. In that regard, the DOL explicitly noted FINRA's guidance regarding so-called "reverse churning."

- The DOL made clear in the Final Rule that a person or firm can recommend that the customer hire the adviser (or its affiliate) for advisory or asset management services without the recommendation counting as a fiduciary recommendation. It is not as clear whether this "hire me" clarification also applies to sponsors of alternative investment funds when they are marketing their own funds and do not receive any fee directly for the sales activity.

- The DOL confirmed that the BIC Exemption contract may provide for binding arbitration of individual claims (but not class actions) and may waive contractual rights to punitive damages or rescission.

- It is the DOL's intent that the best interest standard, including the "without regard to" phrase, be given the same meaning as the language in Section 404 of ERISA that requires a fiduciary to act "solely in the interest" of participants and beneficiaries, as the ERISA standard has been interpreted by the DOL and courts. We think it is naive to expect that the differences in language between ERISA and the best interest standard will not lead to different meanings in the hands of courts and litigants over time.

## OBSERVATIONS FOR PLAN SPONSORS

- The effect of the Final Rule on plans, plan sponsors, and associated fiduciaries is perhaps more subtle but still very significant. For this purpose, we are using "associated fiduciaries" to mean those plan fiduciaries that are established by the plan sponsor, such as plan administration committees and investment committees made up of plan sponsor employees. At root, the Final Rule requires the plan, plan sponsor, and associated fiduciaries to more clearly understand when a fiduciary decision is being made and by whom. This is important for managing risk allocation—that is to say, you will want to know if you are responsible for task "y" or if the service provider you hired is responsible. In turn, the nature of the responsibility and the party having the obligation should be memorialized in writing.

- Because of the scope of the Final Rule, plan sponsors and associated fiduciaries may become frustrated by future third-party service provider engagements because many such service providers may seek to limit services and disclaim responsibilities (even more than they do now) to avoid the very duties you want to engage them to do. For example, many investment advisers currently contract to avoid fiduciary liability for their services, or alternatively, they may acknowledge their fiduciary status but limit it to "advice only," thereby seeking to avoid responsibility for actual investment decisions. Under the Final Rule, the so-called "seller's exception" permits investment advisers to "sophisticated investors" to avoid fiduciary status but only when clear notice is given to the associated fiduciary and such associated fiduciary acknowledges the investment adviser's nonfiduciary status. You can also expect that the institutional trustees to your tax-qualified plans will react in a similar fashion. Such trustees are usually " fully directed," meaning they are a fiduciaries in name only. A potential effect of the Final Rule is that these institutional trustees become fiduciaries even though directed. Therefore, they will also seek to limit the potential liability being foisted upon them under the Final Rule and request to renegotiate their trust agreement terms.

- Where a service provider is now made a fiduciary under the Final Rule, associated fiduciaries have a duty under ERISA to make a prudent selection and monitor such service provider as a co-fiduciary. The failure to do this is a breach of fiduciary duty and can lead to co-fiduciary liability under ERISA. An associated fiduciary may stumble over this duty in unexpected ways. The Preambles to the Final Rule address the situation where plan sponsors engage a third party administrator to provide recordkeeping services for a 401(k) plan. Under the Final Rule, it is the DOL's position that such a third-party administrator can, in the selling of its services, go too far by "recommending" investment funds that will be offered in the plan investment lineup. This might be particularly likely where the third-party administrator offers a family of proprietary funds. When this occurs, the associated fiduciary is engaging a co-fiduciary, not just a record keeper, bringing with it the higher standard of care that ERISA requires. The services agreement with such a co-fiduciary should contemplate this change in status to fully protect the associated fiduciary from unwarranted liability.

- Third-party service providers that sell products and services to plan participants eligible to roll over account balances to IRAs are clearly fiduciaries under the Final Rule. As fiduciaries, the service provider and its products and services must be prudently vetted and monitored on an ongoing basis. If associated fiduciaries fail to do this, it is a breach of fiduciary duty under ERISA, and such associated fiduciaries can be held responsible if the service provider's actions or products cause harm to plan participants.

- Plan sponsors that are not publicly traded and offer company stock in their defined contribution plans should stay tuned. In the Preamble, the DOL addressed the unique and thorny issues raised by valuation appraisals in general and with respect to company stock in particular. The DOL clearly suggested that there are fiduciary issues that may arise in this context concerning the appraiser's work product. Rather than tackle those issues in the Final Rule, the DOL indicated that rules specifically addressing valuation appraisals will be issued separately in the future.

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