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Exemptive Relief May Soften Impact of Fiduciary Advice Regulations

Highlights

- ✔ Best Interest Contract Exemption
- ✔ Principal Transaction Exemption
- ✔ Amendment of PTE 84-24
- ✔ Transition relief
- ✔ Grandfather provision

Inside

The Department of Labor has issued sweeping regulations, generally applicable April 10, 2017, that will require parties that provide investment advice for a fee to plans, plan sponsors, fiduciaries, plan participants, beneficiaries and IRAs and IRA owners to make prudent investment recommendations, without regard to their own interests (see *Special Briefing:* "DOL Expands Range of Investment Advisors Subject to ERISA in Attempt to Control Conflicts of Interest," April 2016)). Although many retirement advisors will be newly subject to the fiduciary standards, including the restriction on "non-level" compensation, the DOL, as part of a broad regulatory construct, has authorized a "Best Interest Contract" PT Exemption, which will allow brokers and other investment firms to continue to retain current forms of variable and incentive based compensation, including commissions, revenue sharing, and 12b-1 fees, as long as they comply with enforceable impartial fiduciary conduct standards, mitigate the inherent risk of conflicts of interest, and disclose such conflicts. The DOL has also approved a "Principal Transaction" Exemption that will allow investment advice fiduciaries to recommend the sale and purchase of fixed-income securities to investors directly from the adviser's own inventory and to or from plans and IRAs.

The Best Interest Contract Exemption and the Principal Transaction Exemption provide opportunities to parties that may find business and compensation practices restricted under the final regulations. The Exemptions are also being phased in, allowing advisers and financial institutions until January 1, 2018, to engage in authorized transactions under more relaxed conditions. Full compliance with the terms of the exemptions would not be required until January 1, 2018. However, even during the transition period, financial institutions and advisers must provide investment advice that is in the best interest of the investor and make specified disclosures.

While the primary focus has been on BICE and the Principal Transaction Exemption, DOL has also adopted amendments to existing PTE 84-24, which, applicable to transactions occurring on or after April 10, 2017, will allow fiduciaries and other service providers to receive reasonable compensation (e.g., insurance commissions, other than revenue sharing) when plans and IRAs purchase insurance contracts, fixed annuity contracts, securities of registered investment companies, or engage in certain related transactions. The terms of PTE 84-24 are more relaxed than those applicable under BICE. However, insurance agents, brokers and other parties receiving compensation under PTE 84-24 will need to comply with impartial conduct standards and disclosure requirements.

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Best Interest Contract Exemption

In order to allay concerns about the possible elimination of brokerage commissions and other forms of non-level compensation under the final regulations, the DOL has authorized a Prohibited Transaction Exemption that will allow individual advice fiduciaries (e.g., registered investment advisers, broker-dealers, insurance companies, and their agents and representatives) providing investment advice to "retail" retirement investors (plan participants and beneficiaries, IRA owners, and retail plan fiduciaries and plan sponsors) to continue to receive variable compensation and third party payments (commissions, 12b-1 fees, and revenue sharing) that may create conflicts of interest. However, in order to avoid the generally applicable 15% excise tax imposed under Code Sec. 4975 and potential fiduciary liability under ERISA, financial institutions would need to comply with specific conditions designed to mitigate conflicts of interest and ensure that investment advice is provided in the "best interests" of retirement investors.

Generally, a financial institution must acknowledge fiduciary status for itself and its advisers. The financial institution and advisers must further adhere to basic standards of impartial conduct, including: giving prudent advice that is in the customer's best interest; avoiding making misleading statements; and receiving no more than reasonable compensation. Finally, the financial institution must adopt and implement policies and procedures to mitigate harmful impacts of conflicts of interest and disclose basic information about its conflicts of interest and the cost of advice recommendations.

Note: The "best interests" standard essentially consolidates the prudent person and loyalty requirements applicable to ERISA plans, thereby providing retail investors greater protection than the previously applicable "suitability" standard. However, the scope of the protection may be a function of applicable circumstances and may need to be more explicitly defined by the courts.

Retirement investors. BICE covers investment advice provided to "retirement investors" (BICE Sec. I (a)). Retirement investors include: (1) a participant or beneficiary of an ERISA plan with authority to direct the investment of assets in his or her plan account or to take a distribution; (2) a beneficial owner of an IRA acting on behalf of the IRA; or (3) a retail fiduciary with respect to the plan or IRA (BICE Sec. VIII(o)).

Retail fiduciary. A retail fiduciary is defined as a fiduciary of a plan or IRA that is not described in ERISA Reg. 2510.3-21(c)(1)(i) (i.e., an independent fiduciary with financial experience) (BICE Sec. VIII(n)). Thus, retail fiduciaries will generally be limited to persons who hold or manage less than $50 million in assets and will not include banks, insurance carriers, retirement investment advisers, or broker-dealers.

Note: The extension of the Exemption to plans with less than $50 million in assets will effectively allow for the continued provision of investment advice to smaller plans.

Exclusions from coverage. The exemption will not apply if: (1) the plan is covered by ERISA Title I *and* (a) the adviser, financial institution, or any affiliate is the employer of employees covered by the plan (i.e., in-house plans) or (b) the adviser or financial institution is a named fiduciary or plan administrator with respect to the plan, or an affiliate thereof, that was selected to provide advice to the plan by a fiduciary who is not independent (BICE Sec. I(c)(1)). In addition, the compensation received may not result from: (a) a Principal Transaction (i.e., purchase or sale of an investment product to a plan participant or beneficiary account or IRA on behalf of the financial institution's own account (see below)) or (b) investment advice generated solely by an interactive website in which computer software-based models or applications provide investment advice based on the personal information supplied by an investor through the website (BICE Sec. I(c)(2)-(3)).

Note: The exclusion does not apply if the robo-advice provider is a "Level Fee Fiduciary" (see below).

Exercise of discretionary authority precludes Exemption. It is imperative to note that the BICE will not apply if the adviser has or exercises any discretionary authority or discretionary control with respect to the recommended transaction (BICE Sec. I(c)(4)).

Best interest contract. The enforceable standards for fiduciary conduct and fair dealing with respect to investors in IRAs and non-ERISA plans must be set forth in a written "best interest" contract (BICE Sec. II). The contract is essentially a written promise that the financial institution *and* its advisers will comply with the impartial conduct standards and the other conditions of the exemption.

Note: BICE, for the first time, empowers IRA owners and non-ERISA plan participants with an individual enforcement mechanism (breach of contract action) for ensuring compliance with the prohibited transaction rules.

ERISA plans. Financial institutions are not required to enter into a best interests contract with ERISA plans (BICE Sec. II(g)).

Note: The elimination of the written contract requirement does not relieve firms dealing with ERISA plans from the obligation to acknowledge in writing that they and their advisers are acting as fiduciaries when providing investment advice to plan participants or beneficiaries or from complying with the impartial conduct standards. ERISA plan participants also retain the right to enforce fiduciary standards under ERISA Sec. 502.

Financial institutions. Financial institutions required to issue the best interest contract include registered investment advisers, banks, insurance companies, and registered broker-dealers (BICE Sec. VIII(e)).

Note: The Exemption does not specifically define a financial institution as including insurance brokers. This possible oversight may prove to be an issue with respect to fixed index annuities and other insurance products.

Advisers. The financial institution, in the contract, will essentially assume fiduciary responsibility for the actions of its advisers. For purposes of the Exemption, advisers include employees, independent contractors, agents, or representatives of a financial institution (BICE Sec. VIII(a)(2)). Thus, in an abrupt alteration of current practice, financial institutions will now be subject to fiduciary liability for the actions of independent agents or contractors.

Contract execution. The contract must be entered into prior to *or* at the same time as the execution of the recommended transaction.

Note: While the contract need not be executed before a recommendation is made, it is important to note the contract must still cover any advice provided prior to the contract date (BICE Sec. II).

Terms may be incorporated into master contract. In order to minimize compliance burdens, the terms of the contact may be incorporated into an investment advisory agreement, investment program agreement, account opening agreement, insurance or annuity contract or application, or other similar agreements commonly used with new customers (BICE Sec. II(a)(i)).

Note: The contract need not be signed by each individual adviser, but may be executed by the financial institution.

Negative consent to amendment to existing contract With respect to existing contracts (executed prior to January 1, 2018) financial institutions are authorized to use a "negative consent" process, under which a retirement investor would be deemed to assent to a contract amended to comply with the Exemption by not terminating the contract within 30 days (BICE Sec. II(a)(1)(ii)).

Note: No new contractual obligations, restrictions, or liabilities may be imposed on the retirement investor by negative consent.

Failure to enter into contract. The DOL has also provided advisers with a means of receiving compensation in the event a retirement investor does not enter into a contract with the adviser, but acts on the advice through other channels (BICE Sec. II(a)(1)(iii)). However, the adviser making the recommendation may not receive compensation (directly or indirectly) that is reasonably attributable to the retirement investor's purchase, holding, exchange or sale of the investment (BICE Sec. II(a)(1)(iii)(A)). In addition, the adviser and financial institution must comply with impartial conduct standards and other applicable conditions (BICE Sec. II(a)(1)(iii)(C)).

[I]n an abrupt alteration of current practice, financial institutions will now be subject to fiduciary liability for the actions of independent agents or contractors

Note: The financial institution must have established policies and procedures that prevent the institution and its affiliates and related entities from providing payments (e.g., bonuses, prizes, or other incentives) to their advisers in lieu of the prohibited compensation. Financial institutions are expressly required to "reasonably" monitor such policies and procedures (BICE Sec. II(a)(1)(iii)(B)).

Acknowledgement of fiduciary status. A central feature of the Best Interest Contract Exemption is the requirement that the financial institution state in writing that it and its advisers are acting as fiduciaries under ERISA or the Internal Revenue Code, with respect to any investment advice being provided (BICE Sec. II(b)). As noted, while advisers to ERISA plans are not required to execute a best interest contract, they must acknowledge fiduciary status with respect to any investment recommendation regarding the plan or participant or beneficiary account.

Note: The requirement to acknowledge fiduciary status reflects the DOL interest, expressed throughout the entire regulatory construct, in preventing service providers from structuring their relationship with plans so as to avoid being treated as a fiduciary. Under the amended fiduciary regulation (ERISA Reg. §2510.3-21) and BICE, a service provider that offers investment recommendations may no longer include boilerplate provisions in a contract that claim the investment recommendations are not intended to be the primary basis for plan investment decisions, even if the services have been marketed as providing individualized and tailored advice. Service providers, further, may no longer present investment fund options to a plan at the time the plan is established, but maintain that they are not fiduciaries because the plan sponsor is responsible for selecting the funds that are actually included in the plan, even if the funds have paid the provider (through 12b-1 fees and or sale loads) to be included in the options offered to the plan.

Impartial conduct standards. Financial institutions must affirmatively state the commitment of the firm and its advisers to specified "impartial conduct standards" (BICE Sec. II(c)). Generally, financial institutions must avoid making misleading statements and may not receive compensation (directly or indirectly) from a recommended transaction that exceeds what is reasonable (BICE Sec. II(c)(2) and (3)).

"Best interest" of retirement investor. The central component of the impartial conduct standard is the requirement that the adviser provide investment advice that is, at the time of the recommendation in the "best interest" of the retirement investor (BICE Sec. II(c)(1)). The best interest standard requires the adviser to: (1) act with the care, skill, prudence, and diligence under then prevailing circumstances that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims, based on the investment objectives, risk tolerance, financial circumstances, and needs of the investor, and (2) without regard to the financial or other interest of the adviser, financial institution, or any affiliate, related entity, or other party (BICE Sec. VIII(d)).

Note: Implicit in the duty of prudence is the obligation to monitor an investment recommendation in order to ensure that it continues to be in the best interest of plan participants. Thus, fiduciaries may not make a recommendation without monitoring its continuing merit. In a pointed note, perhaps directed at advisers with new fiduciary responsibilities to IRA owners, the DOL cautions against making recommendations for complex products without establishing a mechanism for monitoring the investment as being in the continued best interest of the investor (Preamble to BICE).

Warranties. The financial institution must affirmatively warrant that it has adopted and will comply with the written policies and procedures reasonably and prudently designed to ensure adherence to the impartial conduct standards (BICE Sec. II(d)). In formulating policies and procedures, the financial institution must specifically: (1) identify and document material conflicts of interest and (2) adopt measures reasonably and prudently designed to prevent material conflicts of interest from causing violations of the impartial conduct standards.

Note: Financial institutions are cautioned not to discount the importance of establishing policies and procedures to mitigate conflicts of interest. Absent such policies and procedures (and documented compliance) the DOL can deny or revoke the Exemption, jeopardizing otherwise exempt compensation arrangements.

"BICE monitor." The financial institution must also designate a person responsible for addressing material conflicts of interest and monitoring the adherence of its advisers to the impartial conduct standard (BICE Sec. II(d)(2)).

Material conflict of interest. A "material conflict of interest" arises when a financial institution has a financial interest that a reasonable person would conclude could affect the exercise of its best judgment as a fiduciary (BICE Sec. VIII(i)).

Use of quotas and performance bonuses. A feature of the impartial conduct standard that has drawn much interest is the requirement that the financial institution warrant that it will not "use or rely upon quotas, appraisals, performance or personnel actions, bonuses, contests, special awards, differential compensation or other actions or incentives that are intended or would reasonably be expected to cause advisers to make recommendations that are not in the Best Interest of the Retirement Investor" (BICE Sec. II(d)(3)).

Note: In the Preamble to BICE, the DOL clarified the broad scope of the restriction on incentive payments, cautioning that financial institutions "should not compensate *branch managers and other supervisors* [ital. added], or award bonuses or trips to such entities based on the sale of certain investments, if such awards could not be made directly to Advisers under the standards set forth in this exemption."

Differential compensation based on neutral factors. Financial institutions may, however, provide advisers with differential compensation (including commissions) that is based on investment decisions by plans, participant or beneficiary accounts, or IRAs. Thus, differential compensation may be based on *neutral* factors tied to the services provided to the investor.

Note: The incentive practices adopted by the financial institution must be designed to avoid "misalignment" of the interests of the adviser and the interests of the retail investor. However, the allowance for differential compensation addresses the concern of providers that identical fees would need to be assessed for all services and recommendations, regardless of the investment product.

Also note that the requirement to act in an investor's best interest and without a material conflict of interest does not obligate an adviser to recommend the lowest fee or lowest cost investment product. The DOL has cited numerous academic studies indicating an inverse relationship between fees and costs and investment returns. However, an adviser may continue to recommend a higher cost product (e.g., actively traded fund) as long as the recommendation is documented as being in the best interest of the investor. However, be cautioned, a recommendation that is in the best interest of an investor, but that also results in additional compensation to the adviser, may suggest or invite suspicions of a breach of the duty of loyalty.

Disclosure requirements. Financial institutions must make written disclosures to retirement investors that state the best interest standard of care, describe material conflicts of interest, and address the treatment of proprietary products. (BICE Sec. II(e)).

The disclosures may be incorporated into the best interest contract or made in a single written disclosure provided to retirement investors with the contract. With respect to an ERISA plan, the financial institution may provide a single written disclosure to or at the same time as the recommended transaction. The disclosures must be clearly and prominently displayed (i.e., not buried in boilerplate).

Note: In addition, to the contractual disclosures, financial institutions are required to make web and transaction-based disclosures (see below).

Description of fees. In stating the best interest standard of care, financial institutions must inform the retirement investor of the services to be provided and how the investor will be required to pay for the services (e.g., directly or through third party payments). Financial institutions must, thus, clearly advise retirement investors whether payments will be made through commissions or other forms of transaction-based payments (BICE Sec. II(e)(1)).

Similarly, in describing material conflicts of interest, the financial institution must disclose any fees or charges imposed upon the retirement investor or the retirement investor's account. Specifically, the disclosure must state the types of compensation that the financial institution, its affiliates, and advisers expect to receive from third parties in connection with the investment recommended to the retirement investors (BICE Sec. II(e)(2)).

Recommendations limited to proprietary products. Financial institutions may continue to offer proprietary products to retirement investors and limit investment recommendations to such products (see below). However, the retirement investor must be fully apprised of whether the financial institution offers proprietary products or receives third party payments with respect to recommended investments. The disclosure must also indicate the extent to which recommendations are limited to proprietary products or investments that generate third party payments (BICE Sec. II(e)(5)).

Also note that the requirement to act in an investor's best interest and without a material conflict of interest does not obligate an adviser to recommend the lowest fee or lowest cost investment product.

Note: Merely advising retirement investors that investment recommendations "may" be limited to proprietary products would not be sufficiently specific disclosure.

Impermissible contract terms. In addition to terms that must be included in the best interest contract, the BICE prohibits financial institutions from incorporating within the contract, exculpatory provisions in which the institution or adviser disclaim or otherwise limit liability for violations of the contract's terms (BICE Sec. II(f)(1)).The contract may also not require the retirement investor to: waive the right to bring or participate in a class action suit; agree to an amount representing liquidated damages for breach of contract; or arbitrate claims in distant venues (BICE Sec. II(f)(2)-(3)).

Note: The restriction on impermissible contract terms also governs the investment recommendations of a financial institution with respect to ERISA plans (BICE Sec. II(g)(5)). Thus, while the written contract requirement does not apply to financial institutions dealing with ERISA plans, plan participants and beneficiaries are entitled to the other protections offered to retirement investors under BICE.

Level fee fiduciaries. Level fee fiduciaries that, along with their affiliates, receive only a level fee (rather than a commission or transaction-based fee) in connection with advice or investment management services, are not required to enter into a contract with retirement investors (BICE Sec. II(h)). Such level fee fiduciaries are also exempt from the requirements of BICE Sec. II(d)-(g), governing warranties, disclosures, and ineligible contract provisions.

Note: The accommodation for level fee fiduciaries reflects the DOL acknowledgement that level fee arrangements do not harbor the inherent conflicts of interest that generally obtain in the commission-based or non-level compensation context. However, level fee fiduciaries will need to comply with the best interest standards in making rollover recommendations (see below).

Level fee. A level fee (unlike a commission or transaction-based fee) is a fee or compensation provided on the basis of a fixed percentage of the value of the assets or a set fee that does not vary with the specific investment being recommended (BICE Sec. VIII(h)). Common examples include: assets under management percentage fees, annual retainers, subscription-based fees, and hourly fees.

Acknowledge fiduciary status and impartial conduct standards. In order to protect retirement investors, financial institutions and advisers that are level fee fiduciaries, must, prior to or at the same time as the execution of the recommended transaction, provide the retirement investor with written acknowledgment of the fiduciary status of the institution and its advisers (BICE Sec. II(h)(1)). The financial institution and the advisers must also comply with the impartial conduct standards (BICE Sec. II(h)(2)).

Document rollover recommendations. With respect to the recommendations of a rollover from an ERISA plan to an IRA, the financial institution must document the reasons supporting the recommendation as in the best interest of the investor (BICE Sec. II(h)(3)). The documentation must reflect consideration of the fees and expenses associated with the plan and the IRA (BICE Sec. II(h)(3)(i)).

Level fee recommendations. Recommendations to switch from a commission-based account to a level fee arrangement are permitted, if documented as being in the best interest of the investor. BICE, thus provides a major incentive for the transition from variable compensation structures to level fee arrangements, especially in the rollover context. However, in establishing that a level fee arrangement is in the best interest of an investor, services that will be provided for the level fee must be specifically documented (BICE Sec. II(h)(3)(ii)).

Note: The Best Interest Contract Exemption was significantly revised from its initial incarnation to facilitate implementation and compliance with the Exemption's terms. In addition to the streamlined level fee conditions, the revised exemption: permits reliance on a negative consent process for existing contract holders; simplifies pre-transaction disclosures to eliminate the proposed required projections of the total costs of the investment over time; eliminates the proposed annual disclosure and proposed data collection conditions; no longer restricts the covered asset classes; extends the Exemption to 401(k) plans with under $50 million in assets; and provides a means of correcting good faith violation of the Exemption's terms.

Web and transaction-based disclosures. In addition to pre-transaction disclosures made in the contract (discussed above), financial institutions are required to make transaction-based disclosures and maintain a website featuring additional information (BICE Sec. III).

Note: The disclosure requirements do not apply to level fee fiduciaries (BICE Sec. II(h)).

Transaction-based disclosures. Financial institutions must provide retirement investors, prior to or at the same time as the execution of the recommended investment, a single written document disclosing specified information (BICE Sec. III). Specifically, the document must state the best interest standard of care and describe any material conflicts of interest (BICE Sec. III(a)(1)).

Note: Advisers are not merely required to disclose material conflicts of interest, but must acknowledge their obligation to provide a best interest standard of care.

Investors entitled to detailed disclosure of fees. The document must also inform retirement investors of their right to the specific disclosure of costs, fees, and other compensation, including third party payments, regarding recommended transactions (BICE Sec. III(a)(2)). Costs, fees, and other compensation must be disclosed in sufficient detail to allow the investor to make an informed judgment about the cost of the transaction and the significance and severity of the material conflicts of interest.

Financial institution must provide information on website. The financial institution must further maintain a website providing specified information that is freely accessible to the public and updated no less frequently than quarterly (BICE Sec. III(b)). Among the information that must be included on the website is: discussion of the material conflicts of interest associated with the financial institution's business model; a schedule of typical contract fees and service charges; a model contract or other model notice of contractual terms (renewed quarterly and updated within 30 days if necessary); description of policies and procedures for conflict mitigation and incentive practices; a description of arrangements that provide third party payments to either the adviser or the financial institution with respect to specific investment products or classes of investments; and disclosure of the financial institution's compensation and incentive arrangements with advisers (including incentives) (BICE Sec. III(b)(1)).

Note: The website must disclose compensation and incentive arrangements with advisers, including cash and non-cash awards, in sufficient detail to permit visitors to the website to make an informed judgment about the significance of the firm's compensation practices to an investment decision. However, the Exemption, as revised does not require individualized information regarding a particular adviser's compensation to be posted on the website.

Group disclosures. The financial institution may group required disclosures based on reasonably-defined categories of investment products or classes, product manufacturers, advisers and arrangements. A financial institution may also disclose reasonable ranges of values, rather than specific values, as appropriate (BICE Sec. III(b)(1)(vii)). However, the financial institution must retain the data and documentation supporting the group disclosure for six years as well as make the information available to the DOL within 90 days of a request (BICE Sec. III(b)(5)).

Investment recommendations may be limited to proprietary products. The conditions under BICE, as initially proposed, restricting variable compensation and requiring investment recommendations to be in a client's best interest, had raised the concern that advisers would be forced to recommend another company's products instead of their own. The revised BICE makes clear that financial institutions may restrict investment recommendations by advisers, in whole or in part, to proprietary products or to investments that generate third party payments (BICE Sec. IV(a)).

Third party payments. Third party payments, subject to the Exemption, include: sales charges that are not paid directly by the plan, participant or beneficiary account, or IRA; gross dealer concessions; revenue sharing; 12b-1 fees; distribution, solicitation, or referral fees; volume-based fees; fees for seminars and educational programs; and any other compensation, consideration or financial benefit provided to the financial institution or an affiliate or related entity by a third party as a result of the transaction (BICE Sec. VIII(q)).

Compliance with best interest standard. The primary condition for limiting recommendations to proprietary products or investments that generate third party payments is compliance with the best interest standard (BICE Sec. IV(b)). Compliance with the best interest standard requires the financial institution to: clearly and prominently inform the retirement investor in writing of the specific extent to which investment recommendations are in fact limited to proprietary products or to investments that generate third party payments; disclose material conflicts of interest with respect to the recommended transaction; document in writing limitations on the universe of recommended investments and material conflicts of interest associated with any contract or arrangement providing for the receipt of third party payments or associated with the sale or promotion of proprietary products; and document services that it will provide to investors in exchange for third party payments, as well as services or consideration it will furnish to any other party in exchange for the payments (BICE Sec. IV(b)(1)-(3)).

[F]inancial institutions may restrict investment recommendations by advisers, in whole or in part, to proprietary products or to investments that generate third party payments.

Restrictions on differential compensation. Significantly, the proprietary interest exemption specifically requires the financial institution (including affiliates and related entities) to not use or rely upon, quotas, appraisals, performance or personnel actions, bonuses, contests, special awards, differential compensation or other actions or incentives that are intended or would reasonably be expected to cause an adviser to make imprudent investment recommendations or to make recommendations based on the consideration of factors or interests other than the investment objectives, risk tolerance, financial circumstances, and needs of the retirement adviser (BICE Sec. IV(b)(4)).

Advance notice to DOL of reliance on BICE. Prior to receiving compensation, the financial institution must notify the DOL of its intention to rely on the Exemption (BICE Sec. V(a)). The notice will remain in effect until revoked in writing by the financial institution.

Note: The financial institution is merely required to notify the DOL of the intention to use BICE. The financial institution is not required to secure DOL approval of the use of BICE. Of course, DOL would be empowered to revoke continued use of the Exemption in the event of noncompliance with the specified terms.

Advance notice to plans and IRAs not required. The financial institution is not required to provide such advance notice to any plan or IRA.

Recordkeeping requirements. The financial institution (subject to penalty under ERISA Sec. 502(i) or Code Sec. 4975(a) and (b)) must maintain, for a period of six years, records necessary to enable a determination of whether the conditions of the Exemption have been satisfied (BICE Sec. V(b)).

Note: The recordkeeping requirements of the 2015 proposed Exemption have been relaxed. However, policies and procedures governing recordkeeping will need to be documented in order to establish compliance with the terms of the Exemption.

Records must be accessible. The records must be reasonably available for examination during normal business hours by: representatives of the DOL and IRS, plan fiduciaries, contributing employers and any employee organization, plan participants and beneficiaries, and IRA owners (BICE Sec. V(c)(1)).

Note: The recordkeeping requirements do not apply to level fee fiduciaries (BICE Sec. II(h)).

Protection of trade secrets. No party otherwise authorized to examine records regarding a recommended transaction may have access to records regarding privileged trade secrets or privileged commercial or financial information of the financial institution (BICE Sec. V(c) (2)). Similarly, such parties may not have access to records with respect to a transaction involving another retirement investor or to information identifying other individuals.

Note: The failure to satisfy the recordkeeping requirements will result in the loss of the Exemption, but only for the transaction or transactions for which the records are missing or have not been maintained (BICE Sec. V(c)(4)). Transactions for which proper records have been maintained my still qualify for the Exemption.

Purchase and sale of insurance and annuity contracts. The Exemption authorizes a plan, participant or beneficiary account, or IRA to engage in a purchase or sale of an investment product (including an insurance or annuity product from an insurance company) with a financial institution that is a service provider or other party in interest or disqualified person to the plan or IRA (BICE Sec. VI(a)-(b)).

The transaction must be effected by the financial institution in the ordinary course of its business and payments for services performed by the financial institution may not exceed reasonable compensation. In addition, the terms of the transaction must be at least as favorable to the plan, participant or beneficiary account, or IRA as the terms generally available in an arm's length transaction with an unrelated party (BICE Sec. VI(c)).

Restriction on application of exemption to ERISA plans. The Exemption for the purchase and sale of annuity contracts will not apply to plans covered by ERISA Title I if: (a) the adviser, financial institution, or any affiliate is the employer of employees covered by the plan or (b) the adviser and financial institution is a named fiduciary or plan administrator (BICE Sec. VI(d)(1)). Similarly, the adviser may not have or exercise any discretionary authority or discretionary control with respect to the recommended transaction (BICE Sec. VI(d)(4)).

Compensation based on "robo-advice." The compensation received as a result of the investment advice may not have been generated solely by an interactive website in which computer software-based models or applications provide investment advice based on personal information supplied by the investor through the website without any advice from an individual adviser (BICE Sec. VI(d)). However an exception is authorized if the robo-advice provider is a level fee fiduciary that complies with the conditions discussed above.

Private rights of action authorized. Under current rules, consumers have limited recourse under ERISA and the Internal Revenue Code to redress conflicts of interest. As noted above, the BICE ensures that retirement advisors can now be held accountable to their clients if they provide advice that is not in their clients' best interest.

A financial institution, when providing advice to an IRA owner, must commit to the best interest standard and the other prescribed protective conditions as part of an enforceable contract. ERISA plan investors will be able to rely on an adviser's fiduciary acknowledgement to assert their rights under ERISA. If advisers and financial institutions do not adhere to the standards established in the exemption, retirement investors will be able to hold them accountable either through a breach of contract claim (for IRAs and other non-ERISA plans) or ERISA's enforcement provisions.

Note: The DOL cautions that investors will not be able to use the enforcement mechanism solely to challenge investment results. Under long-existing ERISA jurisprudence, advisers can prove they have acted in their clients' best interest by documenting the use of a reasonable process and adherence to professional standards in deciding to make the recommendation and determining that it was in the customer's best interest. Advisers should, however, be certain to document compliance with the financial institution's policies and procedures required by the BICE.

Arbitration retained. Investment firms will still be able to require that individual disputes be handled through arbitration, absent unreasonable venue restrictions.

Note: The governing contract must allow clients the right to bring class action lawsuits in court if a group of people are harmed. This provision suggests the potential of settlements that could prove very expensive to brokerage firms and other investment fiduciaries that may be otherwise be willing to absorb compensatory damages for breaching the terms of the Exemption as the cost of doing business.

Phased implementation of BICE. The Best Interest Contract Exemption will generally become available on the April 10, 2017 applicability date. However, DOL has authorized a transition period from April 10, 2017 to January 1, 2018, during which advisers, financial institutions, and their affiliates and related entities may, subject to specified conditions, continue to receive compensation or investment advice that would otherwise be prohibited, absent compliance with BICE (BICE Sec. IX).

Restrictions on application of transition period. The transition period will not apply to plans covered by ERISA Title I if: (a) the adviser, financial institution, or any affiliate is the employer of employees covered by the plan, or (b) the adviser or financial institution is a named fiduciary or plan administrator with respect to a plan (or an affiliate thereof) that was selected to provide investment advice to the plan by fiduciary who is not independent (BICE Sec. IX (c)). In addition, the transition period will not apply if: the compensation is received as a result of a Principal Transaction (see below); the compensation is generated by robo-advice; or the adviser has or exercises any discretionary authority or discretionary control with respect to the recommended transaction (BICE Sec. IX(c)(2)-(4)).

Compliance conditions during transition period. During the transition period, financial institutions and advisers must provide investment advice that is in the best interest of the retirement investor (BICE Sec. IX(d)). Generally, the investment advice must be prudent and 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, financial institution, or any affiliate, related entity or other party (BICE Sec. IX(d)(1)(i)). In addition, the recommended transaction may not result in direct or indirect payments to the financial institution, adviser, or their affiliates or related entities that is in excess of reasonable compensation (BICE Sec. IX (d)(ii)).

During the transition period, financial institutions and advisers must provide investment advice that is in the best interest of the retirement investor.

Required disclosures. During the transition period, the financial institution must provide the retirement investor, prior to or at the same time as the execution of the recommended transaction, a single written disclosure (which may cover multiple or all transactions occurring within the transition period) that clearly and affirmatively states that the institution and its advisers are acting as fiduciaries with respect to the recommendation (BICE Sec. IX(d)(2)(i)). The financial institution and adviser, further, must: set forth the best interest standards and state that investment recommendations are made in compliance with the standards; describe material conflicts of interest; and disclose whether proprietary products are offered or third party payments are received with respect to any investment recommendations (BICE Sec. IX(d)(2)(ii-(iv)).

Person designated to monitor compliance. The financial institution must designate a person responsible for addressing material conflicts of interest and monitoring the adherence of advisers to the impartial conduct standards (BICE Sec. IX(d)(3)).

Recordkeeping requirements. The recordkeeping requirements discussed above also apply during the transition period (BICE Sec. IX(d)(4)).

Grandfather exception for pre-existing transactions. The BICE includes a grandfather provision that will allow advisers, financial institutions, and their affiliates and related entities to continue to receive reasonable compensation (e.g., 12b-1fees) for investment advice provided in connection with a plan's, participant or beneficiary account's, or IRA's purchase, sale, exchange, or holding of securities or other investment properties that were: (1) acquired prior to the April 10, 2017 applicability date of the Exemption, or (2) acquired pursuant to a recommendation to continue to adhere to a systematic purchase program that was established before the applicability date (BICE Sec. VII(a)-(b)). The compensation must be received pursuant to an agreement, arrangement, or understanding that was entered into before the applicability date and that has not expired or come up for renewal after the applicability date (BICE Sec. VII(b)).

Note: Implicit in the grandfather exemption is the condition that the transaction not have been a prohibited transaction when first executed.

Restriction on compensation from "additional" investments. Compensation may not be received in connection with the investment by a plan, participant or beneficiary account, or IRA of "additional amounts" in the previously acquired investment vehicle (BICE Sec. VII(b)(3)). However, the grandfather rule will apply to compensation received incident to a recommendation to exchange investments within a mutual fund family or variable annuity contract pursuant to an exchange privilege or rebalancing program that was established before the Exemption's applicability date (BICE Sec. VII(b)(3)). In order for the compensation to be grandfathered, the recommendation may not result in the adviser or financial institution (or affiliates and related entities) receiving more compensation (either as a fixed dollar amount or as a percentage of assets) than they were entitled to receive prior to the applicability date.

Note: Investment recommendations made after the applicability date by the financial institution or adviser with respect to the grandfathered securities or other investment property must comply with the best interest and impartial conduct fiduciary standards (BICE Sec. VII(b)(5)). Thus, the recommendations may not be tainted by conflicts of interest or generate unreasonable compensation.

Principal Transaction Exemption

The DOL has approved an additional "Principal Transaction" Exemption (PT) that will allow investment advice fiduciaries to recommend the sale and purchase of fixed-income securities to investors directly from the adviser's own inventory and to or from plans and IRAs (PT Sec. I). Advisers would need to acknowledge fiduciary status, comply with stipulated impartial conduct standards that mirror those under the Best Interest Contact Exemption, and obtain the consent of the plan or IRA .

The Principal Transaction Exemption is applicable to transactions occurring on or after April 10, 2017. However, the DOL has authorized a transition period for compliance that extends to January 1, 2018.

Principal transactions and riskless principal transactions. The Exemption authorizes advisers or financial institutions to engage in the purchase or sale of "Principal Traded Assets in a Principal Transaction or Riskless Principal Transaction" with a plan, participant or beneficiary account, or IRA (PT Sec. I(b)). Advisers or financial institutions may receive a "mark-up, mark-down, or other similar payment as applicable" for the transaction for themselves or any affiliate, resulting from advice offered with respect to the transaction.

Principal traded asset. A principal traded asset, for purposes of a *purchase* by a plan, participant or beneficiary account, or IRA, is a: debt security (as defined under Rule 10b-10(d)(4) of the Exchange Act (see below)); certificate of deposit; an interest in a Unit Investment Trust (UIT); or an investment that is permitted to be purchased under a subsequently issued individual exemption (PT Sec. VI(j)(1)).

With respect to a *sale* by a plan, participant or beneficiary account, or IRA, a principal traded asset is defined as securities or other investment property (PT Sec. VI(j)(2).

Principal transaction. A principal transaction refers to a purchase or sale of a principal traded asset in which an adviser or financial institution is purchasing from or selling to a plan, participant or beneficiary account, or IRA, on behalf of the financial institution's own account or the account of a person directly or indirectly, through one or more intermediaries, controlling, controlled by, or under common control with the financial institution (PT Sec. VI(k)).

Riskless principal transaction. Distinct from a principal transaction, in a "riskless principal transaction," the financial institution, after having received an order from a retirement investor to buy or sell a principal traded asset, purchases or sells the asset for the financial institution's own account to offset the contemporaneous transaction with the retirement investor (PT Sec. VI(m)).

Conditions for purchase of debt security. The purchase of a debt security by a plan, participant or beneficiary account, or IRA is subject to conditions (PT Sec. III(a)). Specifically, the debt security may not have been issued by the financial institution or any affiliate. In addition, the debt security may not have been purchased by the plan, participant or beneficiary, or IRA in an underwriting or underwriting syndicate in which the financial institution or any affiliate is an underwriter or member. Finally, the adviser must determine that the debt security: (a) possesses no greater than a moderate credit risk and (b) is sufficiently liquid to enable sale at or near its carrying value within a reasonably short period of time.

Cash purchase. The purchase or sale of the principal traded asset must be for cash (PT Sec. III(c)).

Limited scope of Exemption. The Exemption will not apply if the adviser: (1) has or exercises any discretionary authority or discretionary control with respect to the management or disposition of the assets of the plan, participant or beneficiary account, or IRA involved in the transaction, or (2) has any discretionary authority or discretionary responsibility in the administration of the plan, participant or beneficiary account, or IRA (PT Sec. I (c)(1)). In addition, the Exemption will not apply if the plan is covered by ERISA Title I and: (1) the financial institution (or any affiliate) is the employer of employees covered by the plan or (2) the adviser or financial institution is a named fiduciary or plan administrator with respect to the plan (or an affiliate thereof) that was selected to provide investment advice for the plan by a fiduciary who is not independent (PT Sec. I(c)(2)).

Written contract, fiduciary status, and impartial conduct requirements. As with the BICE, the Principal Transaction Exemption requires a financial institution to execute a written contract, acknowledge fiduciary status, comply with impartial conduct requirements, and make specified transaction disclosures (PT Sec. II).

Written contract. With respect to IRAs and non-ERISA plans, financial institutions must agree, in an enforceable written contract, that they and their advisers will adhere to the Exemption standards (PT Sec. II(a)). The requirements applicable to the execution of the written contract under BICE, including authorization for negative consent, apply under the Principal Transaction Exemption (PT Sec. II(a)(1)).

Note: The contract need not be executed before the advice regarding the principal transaction is provided to a retirement investor. However, the DOL cautions, the contract must cover any advice given prior to the contract in order for the Exemption to apply to the advice (PT Sec. II).

The contract may not contain exculpatory provisions disclaiming or otherwise limiting the liability of the adviser or the financial institution

*Ineligible contractual terms***.** The contract may not contain exculpatory provisions disclaiming or otherwise limiting the liability of the adviser or the financial institution (PT Sec. II(f)). The contract may also not limit the right of the plan, IRA, or retirement investor to participate in class action litigation.

Arbitration provisions. Arbitration provisions in a contract are valid. However, the contract may not require the retirement investor to arbitrate claims in venues that are distant or that otherwise unreasonably limit the ability of the investor to assert claims (PT Sec. II(f)(3)).

Written contract not required for recommendations to ERISA plans. The written contract requirement does not apply to recommendations made to retirement investors with respect to ERISA plans. However, prior to or at the same time as the execution of the transaction, the financial institution must provide the retirement investor with a written statement of the financial institution's and the adviser's fiduciary status and comply with the specified impartial conduct standards (PT Sec. II(g)).

Acknowledge fiduciary status. The financial institution must affirmatively state in writing that it is acting as fiduciary with respect to any investment advice regarding the principal transaction or riskless principal transaction subject to contract or with respect to the plan or participant or beneficiary account (PT Sec. II(b)).

Note: Fiduciary status must be conveyed incident to advice provided to IRA owners and non-ERISA plans pursuant to a contract and to ERISA plans and participant or beneficiary accounts.

Impartial conduct standards. In order to ensure the protection of retirement investors, a financial institution and its advisers must comply with impartial conduct standards (PT Sec. II(c)). Generally, the recommendation must be in the best interest of the retirement investor and made without regard to the financial or other interests of the adviser or financial institution (PT Sec. II(c)(1)).

Best execution standard. The adviser and the financial institution must also seek to obtain the "best execution" reasonably available under the circumstances with respect to the transaction (PT Sec. II(c)(2)).Financial institutions may comply with this standard by adhering to specified FINRA rules.

Materially misleading statements. Financial institutions and advisers must not make any statements to retirement investors with respect to the transaction, fees and compensation related to the transaction, material conflicts of interest, or any other matters relevant to the investor's decision to engage in the transaction that are materially misleading at the time they are made (PT Sec. II(c)(3)).

Transaction disclosures. The financial institution, in the contract, or in a separate single written disclosure provided to the retirement investor prior to or at the same time as the execution of the principal transaction or riskless principal transaction, must set forth in writing a description of the type of compensation that may be received in the connection with transaction, including any compensation that may be received from third parties (PT Sec. II (e)(1)). The financial institution must also identify and disclose material conflicts of interest associated with the transactions.

Investor consent. With the exception of existing contracts, the financial institution must document the retirement investor's affirmative written consent, on a prospective basis, to the transaction (PT Sec. II (e)(2)). The financial institution must also inform the retirement investor that the consent is terminable at will without penalty to the plan or IRA (PT Sec. II (e)(3)).

Disclosure of policies and procedures. In addition to specified pre-transaction and annual disclosures that must be provided to retirement investors (see PTE Sec. IV(a)-(d)), the financial institution must prepare a written description of its policies and procedures (PT Sec. IV(e)). The policies and procedures must be made available on the financial institution's website and to retirement investors without charge.

Summaries of procedures. The disclosure may summarize key components of the policies and procedures relating to conflict mitigation and incentive practices. However, complete policies and procedures must be provided to DOL upon request.

Note: The disclosures must be made in a manner that will allow retirement investors to make an informed judgment about the stringency of the financial institution's protections against conflicts of interest. Thus, the financial institution would not be able to disguise conflicts of interest or impermissible compensation practices through the use of arcane language or misleadingly simplistic jargon.

Recordkeeping requirements. Among the record retention conditions with which a financial institution must comply under the Exemption is the requirement to maintain, for a period of six years from the date of each principal transaction or riskless principal transaction, the records necessary to enable government representatives, fiduciary parties to the transaction, the employer of participants and beneficiaries and any employee organization whose members are covered by the plan, and any participant or beneficiary of the plan or beneficial owner of an IRA to determine whether the conditions of the Exemption have been met (PT Sec. V(a)-(b)). As with the Best Interest Contract Exemption, persons allowed to examine records regarding the principal transaction are not further authorized to examine: records regarding a prohibited transaction with another retirement investor, trade secrets of the financial institution, or commercial or financial information that is privileged or confidential (PT Sec. V(b)(2)).

Failure to maintain records. The failure to comply with the record maintenance requirements will result in the loss of the Exemption. However, the penalty is limited to the transaction for which the records have not been maintained and will not affect the application of the relief to other transactions (PT Sec. V(b)(4)).

Transition period. As with the Best Interest Contract Exemption, DOL has provided a transition period for the Principal Transaction Exemption during which advisers and financial institutions may, from April 10, 2017 to January 1, 2018, engage in principal transactions and riskless principal transactions under more relaxed conditions (PT Sec. VII(a)).

Discretionary authority of adviser will negate transition period. The transition period will not apply if the adviser has or exercises discretionary authority or discretionary control with respect to the management of the plan or IRA involved in the transaction or exercises any discretionary authority or control respecting management or disposition of the assets (PT Sec. VII(c)(1)). Nor will the transition period apply if the adviser has any discretionary authority or discretionary responsibility in the administration of the plan or IRA.

Application to ERISA plans. The transition period will not apply to ERISA plans if: (1) the adviser, financial institution, or any affiliate is the employer of the employees covered by the plan, or (2) the adviser or financial institution is a named fiduciary or administrator of the plan that was selected to provide advice by a fiduciary who is not independent (PT Sec. VII(c)(2)).

Conditions applicable during transition period. During the transition period, financial institutions and advisers must provide investment advice that is in the best interest of the retirement investor (PT Sec. VII(d)(1)). Thus, the advice must reflect care, skill, prudence, and diligence, and 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, financial institution, or any affiliate.

In addition, the financial institution must make a signed written disclosure furnishing specified information to the retirement investor, prior to or at the same time as the execution of the transaction (PT Sec. VII(d)(2)). In the written disclosure, which may cover multiple transactions, the financial institution must affirmatively state that it and its advisers are fiduciaries and have adhered to the best interest standards (PT Sec. VII(d)(1)). The statement must also disclose material conflicts of interest.

Finally, as with BICE, the financial institution must designate a person responsible for addressing material conflicts of interest and monitoring advisers' adherence to the impartial conduct standards (PT Sec. VII(d)(3)).

PTE 84-24 amended to facilitate access to "simple" lifetime income products

The DOL has also amended existing PTE 84-24, which allows insurance agents and brokers, and insurance companies, to receive compensation for recommending specified insurance and annuity contracts ("fixed rate annuity" contracts) and investment company securities (e.g., mutual fund shares) to plans and IRAs. As amended, PTE 84-24 will allow fiduciaries and other service providers to receive reasonable compensation (e.g., insurance commissions, other than revenue sharing) when plans and IRAs purchase insurance contracts, fixed annuity contracts, securities of registered investment companies, or engage in certain related transactions.

PTE 84-24 does not require a written contract or a documented compliance policy and, thus, its terms are more relaxed than those applicable under BICE. However, PTE 84-24 now contains impartial conduct standards and disclosure requirements, applicable to transactions occurring on or after April 10, 2017, that are designed for the protection of retirement investors (PTE 84-24 Sec. I-III).

The amendments are applicable to transactions occurring on or after April 10, 2017.

PTE 84-24 does not require a written contract or a documented compliance policy and, thus, its terms are more relaxed than those applicable under BICE.

Fixed rate annuity contract. The Exemption allows for the receipt, directly or indirectly, by an insurance agent or broker or a pension consultant of an insurance commission and related employee benefits from an insurance company in connection with the purchase, with assets of a plan or IRA (including through a rollover or distribution) of an insurance contract or a fixed rate annuity contract (PTE 84-24 Secs. I(b)(1) and VI(f)).

A "fixed rate annuity contract" is defined as a fixed annuity contract issued by an insurance company that is either an immediate annuity contract or a deferred annuity that: (1) satisfies applicable state standard nonforfeiture laws at the time of issue, or (2) in the case of a group fixed annuity, guarantees return of principal net of reasonable compensation and provides a guaranteed declared minimum interest rate in accordance with the rates specified in the state nonforfeiture law that are applicable to individual annuities (PTE 84-24 Secs. I(b)((1) and VI(k)). Under either arrangement, the benefits may not vary, in whole or in part, based on the investment experience of a separate account or accounts maintained by the insurer or the investment experience of an index or investment model.

Note: A fixed rate annuity contract, under the amended Exemption, will not include a variable annuity or an indexed annuity or similar annuity (PTE 84-24 Sec. I(c)).

Thus, the purchase by a plan or IRA of such products is not covered by PTE 84-24. The Best Interest Contract Exemption, however, is designed to address transactions involving annuity contracts that are not fixed rate annuity contracts, such as variable and index annuities (see above).

Insurance commissions. An insurance commission is a sales commission paid by the insurance company to the insurance agent or broker or pension consultant for effecting the purchase of the fixed annuity contract or insurance contract (PTE 84-24 Sec. VI(f)). Authorized commission payments include renewal fees and trailers, but expressly do not include revenue sharing, administrative fees, or marketing payments.

Investment company securities. The Exemption allows investment advice fiduciaries and other service providers to receive compensation as a result of recommendations to plans to purchase investment company securities. Insurance agents, insurance brokers, pension consultants, and investment company principal underwriters that are parties in interest or fiduciaries with respect to plans or IRA may also effect the purchase and collect the resultant commissions (PTE 84-24 Sec. I(b)(3)).

Note: An independent fiduciary must approve the transaction on behalf of the plan.

Purchase of investment company securities by IRAs. The amended Exemption revokes authorization for compensation received in connection with the purchase of investment company securities by IRAs (PTE 84-24 Sec. I(c)).

Note: The parties authorized to engage in the transactions authorized by PTE 84-24, Sec. I(b)(1)-(4) are subject to restriction (PTE 84-24 Sec. IV). Specifically, the insurance agent, broker, pension consultant, investment company or investment company principal underwriter, covered by the Exemption, may not be: (1) a trustee of the plan or IRA (other than a nondiscretionary trustee who does not render investment advice with respect to plan assets); (2) a plan administrator; (3) a fiduciary authorized in writing to manage, acquire, or dispose of assets of the plan or IRA on a discretionary basis; or (4) an employer with employees covered by the plan.

Impartial conduct standards. Insurance agents, brokers, pension consultants, insurance company or investment company principal underwriters who are fiduciaries with respect to assets involved in the transaction must comply with specified impartial conduct standards (PTE Sec. 84-24 Sec. II). As with the standards prescribed under BICE and the Principal Transaction Exemption, fiduciaries involved in transactions under PTE 84-24 must act in the best interests of the plan or IRA (PTE 84-24 Sec. II(a)). In addition, the fiduciaries may not make materially misleading statements regarding: recommended investments, fees, material conflicts of interest, and other matters relevant to a plan's or IRA owner's investment decisions (PTE 84-24 Sec. II(b)).

Note: The Exemption explicitly cautions that a fiduciary's failure to disclose a material conflict of interest with respect to a plan or IRA owner's investment decision is a misleading statement.

Disclosure requirements. With respect to a transaction involving the purchase with plan or IRA assets of a fixed rate, annuity contract, or the receipt of an insurance commission thereon, the insurance agent or broker or pension consultant, prior to the execution of the transaction, must disclose to an independent fiduciary for the plan or the IRA owner, information regarding conflicts of interest (e.g., an affiliate relationship with insurance company whose contract is being recommended), compensation, and fees (PTE 84-24 Sec. IV(b)(1)).

Annual disclosure of insurance commissions. The insurance commission received incident to the transaction must be expressed, to the extent feasible, as an absolute dollar figure, or, otherwise, as a percentage of gross annual premium payments, asset accumulation value, or contract value, *for the first year and for each of the succeeding renewal years*, that will be paid by the insurance company to the agent, broker, or consultant in connection with the purchase of the contract (PTE 84-24, Sec. IV(b)(1)(B)).

Note: The annual disclosure of ongoing deposits is a tightening of the proposed amendment, which had required disclosure every three years.

The disclosure must also include a separate indication of the amount of an insurance commission that will be paid to any other person as a gross dealer concession, override, or similar payment (PTE 84-24 Sec. IV(b)(1)(B)).

Fees, discounts, and penalties. The disclosure must include a statement of any charges, fees, discounts, penalties, or adjustments which may be assessed under the contract in connection with the transaction (PTE 84-24 Sec. IV(b)(1)(C)).

Written authorization of transaction. Following the receipt of the required disclosures and prior to the transaction, the fiduciary or IRA owner must acknowledge, in writing, receipt of the information and approve the transaction on behalf of the plan or IRA (PTE 84-24 Sec. IV(b)(2)).

Purchase of investment company securities. Similar disclosure requirements also apply to transactions involving the use of plan assets to purchase securities issued by an investment company or the receipt of a mutual fund commission thereon by an investment company principal underwriter (PTE 84-24, Sec. IV(c)). In addition to mutual fund commissions and fees, discounts, and penalties, the principal underwriter of the investment company whose securities are being recommended must disclose any limitations placed upon its ability to recommend investment company securities.

Recordkeeping requirements. Insurance agents , brokers, pension consultants, insurance company or investment company principal underwriters engaging in the covered transaction must maintain (or cause to be maintained) records necessary to verify that the conditions of the Exemption have been met (PTE 84-24 Sec. V). The records must be maintained for a period of six years. Safeguards to protect the privacy of individuals and trade secrets, comparable to those applicable under the BICE and Principal Transaction Exemption, also apply (PTE 84-24 Sec V(b)(2)).

April 10, 2017 applicability date. The amendments to PTE 84-24 are applicable to transactions occurring on or after April 10, 2017. The amendments may be relied on prior to the applicability date (Preamble to PTE 84-24). However, the revocation of the Exemption as it applies to plan and IRA purchases of annuity contracts that do not qualify as fixed rate annuity contracts and to IRA purchases of investment company securities will not apply prior to the applicability date (Preamble to PTE 84-24).

Grandfathering of pre-existing contracts not authorized. The amended Exemption does not contain a grandfathering provision for pre-existing annuity contracts. Nor does the Exemption allow for transactions that occur after the applicability date, but are based on advice furnished prior to the applicability date. (Preamble to PTE 84-24).

Note: DOL advises that the Best Interest Contract Exemption authorizes relief for pre-existing insurance and annuity contracts, under specified conditions (BICE Sec.VII). However, noting that the purpose of the exemption for pre-existing contracts in BICE is to preserve compensation for services already rendered, the DOL is not allowing for investment advice fiduciaries to recommend *additional* investments in existing insurance or annuity contracts, absent compliance with the expanded conditions of PTE 84-24.

Conclusion

The exemptive relief may temper some of the anxiety generated by the expanded scope of fiduciary responsibility under the final regulations. The relief will allow for a continuation of many of the compensation structures and practices currently in effect. However, while the impact of the regulatory construct may not be as disruptive as anticipated, there is no doubt that nearly all financial service and investment professionals will be affected directly or indirectly by the new rules.

Perhaps the biggest initial challenge will be the attitudinal adjustment required to acknowledge that mere disclosure of compensation and conflicts of interest will no longer be sufficient to constitute service in the best interest of clients. Financial institutions and advisers will also need to modify the variable compensation mindset and structure incentives around the best interest of investors.

Beyond the attitudinal adjustments, changes in the marketplace that can reasonably be anticipated include: a transition from commission or transaction- based variable compensation structures to a levelized fee system and the attendant promotion of level fee products; a reduction in revenue sharing arrangements as firms move to a flat dollar payment structure; a new focus on fee offset arrangements; and increased use of level fee robo-advice based on accepted computer models.

In addition, as financial institutions pay more stringent attention to documentation, anticipate the development of services in support of such demand (e.g., model compliance and disclosure forms). A common stress point of DOL throughout the fiduciary regulations and the exemptive relief is the necessity of documenting compliance with the specified terms and conditions. The allowance for variable compensation practices under the exemptive relief disappears without documentation and disclosure. Expect financial institutions that wish to continue variable compensation practices to allocate significant resources to documenting compliance with the terms of the relief.

Finally, although the DOL filled well over 1000 pages with regulatory text and exemptive relief, history would suggest that further guidance (e.g., FAQs) will be forthcoming. In addition to additional DOL guidance, courts will, no doubt, be active participants in flushing out the requirements of the new rules. Accordingly, the situation remains fluid. However, in the exemptive relief, DOL has extended a lifeline that will enable financial service professionals to stay afloat.