DOL Proposes a Broad Definition of Fiduciary for ERISA and IRA Purposes

The U.S. Department of Labor ("DOL") recently proposed regulations under ERISA that, when they are issued in final form, will significantly broaden who will be considered to be a "fiduciary" as a result of providing investment advice to a retirement or welfare benefit plan or an IRA.

Background

ERISA defines "fiduciary" as a person who renders "investment advice for a fee or other compensation, direct or indirect, with respect to money or property of a plan or who has any authority or responsibility to do so." In 1975, the DOL issued regulations defining an ERISA "fiduciary" as any person who provides investment advice to the plan for a fee—

- on a *regular* basis;
- as to the value of securities or other property or the advisability of purchasing or selling securities or other property;
- pursuant to a *mutual agreement or understanding* with the fiduciary, written or otherwise;
- with the understanding the advice will serve as the *primary basis* for the plan's investment decisions; AND
- that is *individualized investment advice* based on the plan's particular needs.

A person must satisfy all five parts of this test in order to be an ERISA "fiduciary."

DOL concerns

The preamble to the proposed DOL fiduciary regulations states that "the current regulations' narrow approach to fiduciary status sharply limits its ability to protect plans and beneficiaries from conflicts of interest that may arise from diverse and complex fee practices existing in today's retirement plan services market and to devise effective remedies for misconduct when it occurs."

The preamble also refers to a 2009 Government Accountability Office study and a 2005 Securities and Exchange Commission study that each described harmful effects of conflicts of interest in the retirement plan marketplace where 90% of defined contribution plans are 401(k) plans, and 95% of the participants are in participant-directed investment plans.

The proposed fiduciary definition

The proposed ERISA definition of a fiduciary, as it applies to a person who provides investment advice to a plan for a fee, includes any person who:

- Provides advice, appraisals or fairness opinions as to the value of securities or other property or makes recommendations as to the purchasing, selling or holding of securities or other property, or provides advice regarding the *management* of securities or other property;
- Acknowledges its fiduciary status under ERISA, relating to discretionary authority or control relating to the investment or administration of a plan;
- Is an investment advisor under the Investment Advisors Act of 1940; or
- Provides advice pursuant to an agreement or understanding with a plan, a plan participant or a fiduciary that *may be considered* in connection with making investment or management decisions with respect to plan assets and will be individualized to the needs of a plan or a participant.

Exceptions

The proposed fiduciary definition includes the following exceptions for any person who:

- Demonstrates that such person's investment advisory services are as a purchaser, seller or appraiser whose interests are adverse to the interests of the plan or its participants and that the person is not undertaking to provide impartial investment advice;
- Provides educational information and assistance (under current DOL guidance);
- Markets a platform (or menu) of investment alternatives that a plan sponsor may choose from, provides assistance in selecting and monitoring those investments, and discloses, in writing, that it is not providing impartial investment advice; OR
- Prepares reports required to comply with ERISA, the Internal Revenue Code or regulations or forms issued thereunder.

The proposed DOL regulations would also apply to prohibited transactions under the Code relating to investment advice for a fee that is related to an IRA.

Investment advice related to a plan distribution

The DOL has also requested comments with respect to whether final regulations should include defining a person as an ERISA "fiduciary" if the person provides investment advice for a fee related to a plan distribution.

DOL hearing/outlook

The DOL held hearings earlier this week and has received numerous comments. A theme of many of the comments is that the proposed definition of an ERISA fiduciary is too broad and may shrink the pool of vendors who are willing to provide necessary plan services.

At the present time, the DOL intends to issue final regulations sometime in 2011.

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