Fiduciary Commentary: The DOL Fiduciary Rule… Here we go again…

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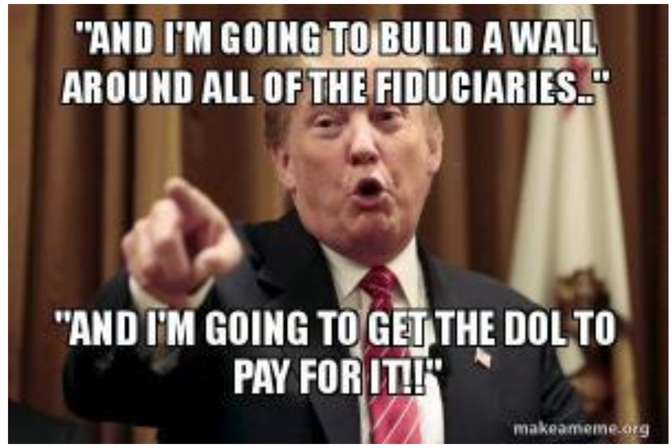

Like the UK's Brexit vote in 2016, Trump's stunning election upset demonstrates the political volatility and policy uncertainty of our day. Many laws and regulations put forward during Obama's presidency now hang in jeopardy awaiting the new administration's actions.

Post-election, the fate of many regulations governing the financial sector are now in question and Trump's victory has given new momentum to the opponents of these laws. The DOL's update to the 40-year old fiduciary rule is among the highest profile regulations whose outcome is now uncertain. This law was designed to elevate the standards of care in handling retirement accounts and eliminate conflict of interest by those providing advice to retirement savers. The far-reaching rule is one of the most transformative financial regulations in decades and would dramatically alter the investment practices of Wall Street and the management of the nation's $3 trillion of retirement assets.

The DOL's controversial advice regulation has provoked intense debate by those threatened by a law that seeks to require the interests of investors to come first, before their own. Affected parties face significant risks to their profitability if the law moves forward as planned. Despite resistance to the DOL's efforts for expanded fiduciary standards, financial firms have been preparing for its implementation with sizable investments in compliance, technology, and revised business practices.

The New Administration's Alternatives

So now what? The industry is assessing the effect of Trump's win on the future of fiduciary rule set to take effect on April 10, 2017, with a phase-in period that ends December 31. 2017. The Trump camp has voiced its discontent with the Obama administration's strict regulation of the nation's financial institutions repeatedly on the campaign trail. Trump's advisor Anthony Scaramucci went so far as promised to repeal the DOL fiduciary rule stating, "We've got to get rid of this".

The new administration and the GOP's Congressional majority has caused many to speculate on the new rule's future. Supporting an effort to dismantle the fiduciary regulation is that the Republicans maintained control of Congress. With Republicans having stated its intent to repeal the DOL's investor protection regulation, they could presumably draft legislation to kill the rule and President Trump could sign it.

However, even if the new administration wants to kill or radically change the final rule, it would prove particularly difficult given the law has been on the books for over eight months and its effective date is just a few short months away. To eliminate the law, the legislation would have to be proposed through the statutory process, which includes the lengthy comment period before it could be finalized. Furthermore, it is not likely that there will be any new legislation until a new DOL secretary is installed and possibly a new assistant secretary of the DOL's EBSA (Employee Benefits Security Administration) is appointed, which is not anticipated until February.

A more likely scenario is that Trump will delay the DOL law through its executive authority. A stay for the advice rule's compliance deadlines would provide the administration time to evaluate its next moves which might include nullifying, amending the rule or using it as a political bargaining chip to further Trump's agenda.

FAQs

In October, the DOL issued its first of three FAQs to help guide firms in their compliance efforts with the new law. The first FAQ addressed the law's exemptions, such as BICE (best interest contract exemptions, and the principal transaction exemptions. A particular focus of the fall's FAQs was how brokers would be able to continue selling investment products while receiving variable compensation and 12(b)(1) fees without running afoul of the new law.

The second round of FAQs was released mid-January to provide additional guidance to the upcoming rule. However, given that the election results and new political realities of a Republican-controlled government that has maintained a hostile stance towards the incoming fiduciary rule, some might understandably wonder why the DOL even bothered to issue further support on the rule. Despite this looming threat of the law being dismantled, the DOL has said, "We are moving forward with implementation as planned."

The second round of FAQs on the DOL fiduciary rule cleared confusion on a common compensation practice for 401(k) advisers. The DOL gave a thumbs-up to a long-standing and commonplace compensation method used by retirement plan advisers. The practice, explicitly approved by the DOL in an Advisory Opinion 97-15A (frequently referred to as the "Frost letter"), clarified that an adviser charging clients a level asset-based fee for providing advice to a retirement plan may use revenue-sharing payments to offset part or all of that level fee. This now common, almost obligatory mid and large market compensation arrangement was clarified by the DOL in its answer to question 7 of the FAQs stating, "Nothing in the Rule or the Exemption alters the analysis of Advisory Opinion 97-15A."

The DOL also covered non-fiduciary forms of communication in its FAQs. The concern that non-fiduciary communications can often be just a brief step away from fiduciary investment advice was highlighted citing how communication can progress into investment advice.

The discussion on the slippery-slope of how communications can evolve into advice seemed to support the use of technology-enhanced communication alternatives. Communication technology, of the fiduciary or non-fiduciary sort, will not deviate from its programmed objective, thus eliminating the risk of "off-script" exchanges that may meander into the fiduciary lane. To those organizations concerned about piercing the fiduciary veil, programmable technology producing the analysis of investment alternatives to be communicated to investors and rollover considerations would be considerably more reliable than depending on members of a sales force staying on script. The marketplace is already begun to adopt these tech-heavy alternatives and the DOL seems likely to support it.

Conclusion

It's difficult to argue the merit of protecting workers and retirees from conflicted advice. Numerous studies have shown the cost of non-fiduciary advice in the billions of dollars each year. Thus, the DOL's Fiduciary Rule is the logical advancement of advisory services that supports the interests of plan sponsors and retirement success of savers.

Despite the uncertain outcome of the DOL's new rule in the Trump-era, the DOL is proceeding with the rule's implementation with the April 2017 effective date of the law. Though nearly everyone anticipates the rule will not survive in its current form or maintain its schedule to the effective date, most financial firms are moving forward to comply with the rule – and for good reason. Financial firms have already invested millions of dollars in retooling their operations to meet the requirements of the law and publicly embraced (appear more investor-friendly I suspect) an elevated standard of fiduciary care to their clients. To backtrack from that position would appear hypocritical. With higher consumer awareness of the benefits of an elevated fiduciary standard since the rule's passing, these firms may march forward with implementation after all.

The full impact of a Trump administration on the DOL's transformative advice rule will be revealed over time. After two prior failed attempts to put forward an expanded fiduciary rule, the DOL's contentious rule is now law. Let's hope it sticks this time.