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PLAN DISTRIBUTION AND ROLLOVER GUIDANCE AFTER *CHAMBER OF COMMERCE V. US DEPARTMENT OF LABOR*

AN ANALYSIS OF THE DESERET LETTER

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This paper examines how a plan service provider (such as a trustee, record-keeper, broker-dealer, or investment adviser) can offer participant-level distribution and rollover guidance under the US Department of Labor's (DOL's) Advisory Opinion to Deseret Mutual Benefit Administrators (the Deseret Letter)[1] in compliance with the Employee Retirement Income Security Act (ERISA).

This paper was created by Morgan Lewis[2] and written by Lindsay B. Jackson, Daniel R. Kleinman, Michael B. Richman, and Ryan R. Montgomery who focus their practices on helping financial services firms and plan sponsors comply with the fiduciary duties and other laws and regulations that apply to retirement accounts under ERISA and the Internal Revenue Code (Code).

[1] DOL Advisory Opinion 2005-23A (Dec. 7, 2005).

[2] Fidelity Brokerage Services LLC (Fidelity) engaged Morgan, Lewis & Bockius to research and prepare this analysis, which is available for general distribution.

A Brief History of the Rules That Govern Plan Rollover Guidance

- ***December 2005***—DOL issues the Deseret Letter, which generally concludes that rollover guidance is not viewed as fiduciary "investment advice" under ERISA and DOL regulations, but muddies the waters for plan officers and other fiduciaries (as considered in this white paper)
- ***March 2013***—Government Accountability Office (GAO) issues a report recommending that regulators address concerns about rollovers, including that the process favors rollovers to IRAs over plan-to-plan rollovers.[3] In response, the DOL acknowledges that its regulations defining fiduciary investment advice allow advisors to guide rollover decisions without triggering fiduciary status, and states that the DOL would propose a "Fiduciary Rule" to address this concern[4]
- ***December 2013***—Financial Industry Regulatory Authority (FINRA) issues Regulatory Notice 13-45 to "remind" broker-dealers that a "recommendation" to roll over plan assets is subject to FINRA's suitability standard
- ***June 2017***—DOL's "Fiduciary Rule," under which any "recommendation" to roll over or take a distribution of plan assets is treated as fiduciary investment advice, becomes applicable.[5] This interpretation also clarifies that providing general information and education with respect to rollovers is not a fiduciary activity, so long as there is no "recommendation" to a plan participant, and broadly recognizes that soliciting and marketing one's services is not a fiduciary activity under the "hire me" doctrine
- ***April 2018***—US Securities and Exchange Commission (SEC) proposes standards of conduct applicable to "recommendations" to retail investors, including rollover recommendations that involve securities transactions
- ***June 2018***—The US Court of Appeals for the Fifth Circuit issues a mandate officially vacating the Fiduciary Rule in toto.[6] The revocation of the Fiduciary Rule means that the DOL's positions in the Deseret Letter are now again the primary guidance on how participant-level distribution and rollover assistance can be provided without running afoul of ERISA's fiduciary duty provisions.[7]

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3 GAO, "401(k) Plans: Labor and IRS Could Improve the Rollover Process for Participants" (March 2013).

4 Letter from P. Borzi, assistant secretary of Labor for Employee Benefits Security Administration, to C. Jeszeck, director, GAO Education, Workforce, and Income Security (Feb. 20, 2013).

5 In adopting the Fiduciary Rule, the DOL questioned its conclusions in the Deseret Letter, stating that "[t]he advisory opinion failed to consider that advice to take a distribution of assets from a plan is actually advice to sell, withdraw, or transfer investment assets currently held in a plan." 81 Fed. Reg. 20864 (Apr. 8, 2016). However, to conclude that every client solicitation or marketing effort involves an implied fiduciary recommendation to sell or otherwise transfer investments from a plan account would be an overly broad application of the concept of fiduciary advice and inconsistent with the DOL's recognition of the "hire me" doctrine, in which the DOL concluded that a service provider can recommend its services without triggering fiduciary status.

6 *Chamber of Commerce of the USA v. US Dep't of Labor*, No. 17-10238 (5th Cir. Mar. 15, 2018) (mandate issued June 21, 2018).

7 Recognizing that practitioners in this area have questioned whether the Fifth Circuit's decision to vacate the Fiduciary Rule reinstated the Deseret Letter, we note that members of the DOL staff have informally confirmed that the Deseret Letter is the DOL's current guidance on fiduciary status with respect to rollover advice. It should be noted that DOL guidance, such as an advisory opinion, is not binding on a court of law, but rather is entitled to respect only to the extent it has the power to persuade based on, among other factors, the validity of its reasoning. *See, e.g.*, *In re WorldCom Inc. ERISA Litig.*, 354 F. Supp. 2d 423, 34 Employee Ben. Cas. 1545, 1561 (SDNY 2005). Moreover, while DOL advisory opinions are commonly cited for the DOL's position on particular issues, as a technical matter only the parties that requested the advisory opinion may rely on it. *See* ERISA Procedure 76-1, § 10, 41 Fed. Reg. 36,281 (1976). We also note that the DOL's informal guidance is subject to change without notice and the DOL may issue further, perhaps contradictory, guidance on the fiduciary implications of rollover advice under ERISA or Section 4975 of the Internal Revenue Code.

Why Are Plan Sponsors and Service Providers Concerned About ERISA's Rollover Rules?

When a person provides "investment advice for a fee" under ERISA (and applicable DOL regulations) to a plan or plan participant, that person is acting as a "fiduciary" under ERISA. Questions have been raised as to whether advising a plan participant on distributions and rollovers of plan investments could be viewed as a fiduciary activity.

Fiduciaries are subject to

- ***fiduciary duties*** that require them to act with prudence and solely in the interest of the plan and its participants; and
- ***prohibited transaction rules*** that prohibit them from receiving and retaining additional compensation in connection with fiduciary investment advice, unless a prohibited transaction exemption applies.

Thus, if a person is a fiduciary with respect to a participant's decision to rollover his or her plan account from a plan to an IRA (presumably generating additional fees for the fiduciary or its affiliate, such as IRA custody fees or brokerage commissions), the rollover advice provided could be viewed as subject to ERISA's fiduciary duties and could result in a prohibited transaction.[8]

What Did the DOL Conclude About Rollover Guidance in the Deseret Letter?

1. Rollover guidance is not fiduciary "investment advice."

In the Deseret Letter, the DOL concludes that merely advising a plan participant to take an otherwise permissible plan distribution, even when combined with a "recommendation" as to how that distribution should be invested, is not fiduciary "investment advice" to a plan under ERISA.[9] This is because, according to the DOL

- a recommendation to take a distribution is not advice concerning a particular plan investment; and
- any investment recommendation as to the distributed proceeds would be advice with respect to funds that are no longer assets of the particular ERISA plan.[10]

Thus, the DOL's currently articulated position is that a person can provide rollover guidance, including a rollover recommendation, to a plan participant without that guidance constituting "investment advice" under ERISA, and the person providing such guidance or recommendation does not become a fiduciary to the plan merely by reason of providing such guidance.[11]

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8 There are currently no prohibited transaction exemptions that explicitly cover rollover advice.

9 The Deseret Letter left open whether such a recommendation is a fiduciary action under Section 4975 of the Internal Revenue Code, as amended, with respect to the newly funded or rollover IRA.

10 Without citing the Deseret Letter, a federal court reached the same conclusion in *Beeson v. Fireman's Fund Ins. Co.*, 48 Employee Ben. Cas. 1412 (ND Cal. 2009).

11 While the DOL's Fiduciary Rule reflected a contrary position, defining fiduciary investment advice as advice with respect to plan distributions and rollovers, the Fifth Circuit rejected this view in vacating the Fiduciary Rule. *Chamber of Commerce of the USA v. US Dep't of Labor,* No. 17-10238, p. 38 (describing the DOL's overreach of regulatory authority and noting that "[w]hen Congress has acted with a scalpel, it is not for the agency to wield a cudgel.").

2. Rollover guidance from a plan fiduciary could raise additional issues.

After concluding that rollover guidance is not fiduciary investment advice, the DOL then went on to muddy the waters for plan officers and other fiduciaries who discuss distribution options with plan participants. Specifically, the DOL stated:

> Where, however, a plan officer or someone who is already a plan fiduciary responds to participant questions concerning the advisability of taking a distribution … that fiduciary is exercising discretionary authority respecting management of the plan and must act prudently and solely in the interest of the participant. Moreover, if, for example, a fiduciary exercises control over plan assets to cause the participant to take a distribution and then to invest the proceeds in an IRA account managed by the fiduciary, the fiduciary may be using plan assets in his or her own interest, in violation of [ERISA's prohibited transaction rules].

In this language, the DOL appears to have been concerned that the plan officer or fiduciary could be using its official or fiduciary role and status to influence the participant's decision to roll over his or her account to an IRA that generates additional fees for the fiduciary. This reading is supported by the DOL's citation in this paragraph to the US Supreme Court's decision in *Varity Corp. v. Howe*.[12] In that case, a plan sponsor was found to have been acting as an ERISA fiduciary when it made misleading statements regarding what employees' benefits would be following a corporate change, and was found to have violated its fiduciary duty of loyalty because it had an interest in the participants' decisions.

Some have broadly interpreted this excerpt to suggest that a person's preexisting status as a plan officer or fiduciary would cause any distribution or rollover guidance provided to participants to be fiduciary in nature and that such person can therefore never recommend a distribution from the plan or rollover into the fiduciary's own investment products. However, this expansive reading is at odds with both the longstanding principle that a person can step out of his or her fiduciary role to act in a nonfiduciary capacity and offer additional services to a plan and its participants for additional fees[13] and the DOL's more recent recognition of the "hire me" doctrine.

As such, a better and more consistent reading would be that the DOL was concerned that plan participants may not know that the plan fiduciary had stepped out of its fiduciary role, and could incorrectly believe that they are receiving rollover advice from a fiduciary acting as such, as opposed to guidance from a financial services firm marketing its services in its individual capacity. Thus, where the plan fiduciary makes clear that any distribution or rollover guidance it provides is not provided in its official plan capacity, the DOL's primary concern here should be adequately addressed.

Accordingly, the DOL's statements highlight the importance of making clear to plan participants that a person discussing plan distributions, or otherwise providing rollover guidance, is not acting in a fiduciary capacity when doing so. Importantly, regardless of whether the service provider (or its affiliate) has a

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12 516 US 489 (1996).

13 *See* 29 CFR § 2550.408b-2(f)(1) (fiduciary investment adviser was not acting as a fiduciary when it proposed to an independent plan fiduciary to perform additional services to the plan for additional fees). *See also Santomenno v. John Hancock Life Ins. Co. (USA),* 768 F.3d 284, 58 Employee Ben. Cas. 2845, 2853 (3d Cir. 2014) (plan service provider was not a fiduciary through its authority to change investment options where it was required to give the plan trustee "adequate notice and sufficient information" to decide whether to accept or reject any changes; notice period not specified); *McCaffree Fin'l Corp. v. Principal Life Ins. Co.*, 65 F. Supp. 3d 653 (SD Iowa 2014), aff'd, 811 F.3d 998 (8th Cir. 2016) (service providers do not act as ERISA fiduciaries in negotiating their own fees). This is implicit in ERISA's definition of the term "fiduciary," which makes clear that a person is considered a fiduciary only "to the extent" the person is performing any of the functions described in the definition. *See Pegram v. Herdrich,* 530 US 211 (2000) (the issue in a breach-of-fiduciary-duty case is whether the defendant was performing a fiduciary function when taking the action that was the subject of the complaint, not whether the person was a fiduciary in any capacity).

preexisting fiduciary relationship with the plan, we do not view the Deseret Letter as concluding that rollover guidance is *per se* fiduciary investment advice, or as prohibiting a service provider from ever offering rollover guidance and soliciting rollovers to the service provider's own IRA product offerings.

What Options Are There for Plan Service Providers to Offer Distribution and Rollover Guidance and Advice as a Nonfiduciary Under the Deseret Letter?

There are three primary options for providing distribution and rollover guidance as a nonfiduciary under the Deseret Letter:

1. Ensure all communications regarding distributions and rollovers are limited to general information and education about distribution options, and that no recommendations are provided.

Communications that are limited to general information and education, and do not include "recommendations" or advice, should not create fiduciary status or liability.[14] As such, we believe a service provider, even one with a preexisting fiduciary relationship, can offer guidance to plan participants in evaluating their plan distribution options in the form of general information and education without triggering fiduciary status and the prohibited transaction rules. Critical here is that the communications are fair and balanced in their approach to portraying the factors a participant should reasonably consider, and do not preference rollovers to the service provider's IRAs. These communications should also clearly indicate that they are not intended to create a fiduciary relationship.

2. Only provide distribution and rollover recommendations if the service provider has no preexisting fiduciary relationship.

Another approach that would be permissible under the Deseret Letter would be to limit recommendations to participants in plans with which there is no preexisting fiduciary relationship. Consistent with the Deseret Letter, such recommendations should not be viewed as fiduciary investment advice and would more readily avoid the concern that plan participants could be confused about the nature of the advice received from a plan fiduciary or official. In adopting this approach, service providers should make clear that they are not providing rollover guidance in a fiduciary capacity. We note that distribution and rollover recommendations may be subject to other applicable laws and regulators, such as the SEC and FINRA in the case of a registered broker-dealer.

3. Provide distribution and rollover recommendations and guidance where there is a preexisting fiduciary relationship, but take steps to make clear that the recommendations and guidance are not provided in a fiduciary capacity.

We believe a service provider can offer distribution and rollover recommendations and guidance to participants without violating its obligations to the plan where there is a preexisting fiduciary relationship, so long as it is clear to the participant that the guidance is not offered in the service provider's fiduciary capacity, or as part of its fiduciary services. Critical to this approach are clear communications establishing where (and when) the service provider is acting as a plan fiduciary and where (and when) it is not.

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[14] *See generally*, Interpretive Bulletin 96-1, 29 CFR § 2509.96-1 (1996).

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