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Kirkland Alert

Update on DOL's Proposed Rule Regarding Definition of "Investment Advice" Fiduciary

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On November 3, 2023, the U.S. Department of Labor (the "**DOL**") published a proposed regulation (the "**Proposed Rule**") expanding the definition of "investment advice" for purposes of determining which parties are subject to fiduciary status under the Employee Retirement Income Security Act of 1974, as amended ("**ERISA**"). According to the DOL, the current regulation (originally adopted in 1975) must be updated to address changes in how Americans save for retirement, including the importance of IRAs for Americans' retirement savings and investments.

Existing Framework and Background

Section 3(21) of ERISA provides that any person who renders or has authority or responsibility to provide "investment advice" for a fee or other compensation with respect to an ERISA plan's assets is subject to ERISA's heightened fiduciary standards. Under the existing regulation (also known as the "five-part test"), a person is considered to have rendered investment advice if they render advice to an ERISA plan (1) as to the value of, or recommendations as to the advisability of investing in or disposing of, securities or other property, (2) on a regular basis, (3) pursuant to a mutual agreement, arrangement or understanding that, (4) the investment advice will serve as a primary basis for the plan's investment decisions, and that (5) the advice will be individualized based on the particular needs of the plan.

The DOL has made several attempts to amend this definition. The most recent effort was published in 2016 and became effective in 2017 (the "**Prior Rule**").¹ The Prior Rule was an expansive shift from the 1975 rule and was the subject of significant debate and criticism. After several legal challenges were filed, the Fifth Circuit vacated the Prior Rule, finding that the Prior Rule violated the Administrative Procedures Act and exceeded the DOL's authority.² In its release of the Proposed Rule, the DOL states that

it has taken a more narrowly tailored approach than prior iterations. Nonetheless, the Proposed Rule has received substantial industry pushback.

Proposed Rule

Under the Proposed Rule, a person renders “investment advice” for purposes of ERISA if, for a fee or other compensation, they recommend a transaction or strategy involving securities or other property to a retirement investor (i.e., an ERISA plan, an IRA, or their fiduciaries, participants, or beneficiaries) and:

1. the person (or any of its affiliates) has discretionary authority or control with respect to the purchasing or selling of securities or other investment property of the retirement investor;
2. the person represents or acknowledges they are acting as a fiduciary when making investment recommendations; **or**
3. the person (or any of its affiliates) makes investment recommendations to investors on a regular basis as part of its business, and the recommendation is provided under circumstances indicating that the recommendation (i) is based on the particular needs or circumstances of the retirement investor and (ii) may be relied on by the retirement investor as a basis for investment decisions that are in the retirement investor’s best interest.

Certain Proposed Changes

Regular Basis. Unlike the five-part test, which required that investment advice be provided to an investor on a regular basis before rising to the level of fiduciary advice, the Proposed Rule would cover discrete advice arrangements if the advisor (or its affiliates) provides investment advice as a regular part of its business. The DOL found the prior standard deficient in that it would not afford fiduciary status to advice arrangements that are limited in duration or scope, even where such advice would have a significant financial impact. Although the Proposed Rule extends beyond recommendations to roll retirement assets out of employee benefit plans, the Proposed Rule’s preamble and public comments by DOL officials indicate a particular desire for rollover advice to be considered fiduciary advice, given that such decisions often involve the bulk of an individual’s retirement savings.

Mutual Agreement or Understanding. The Proposed Rule eliminates the “mutual agreement or understanding” prong of the definition of investment advice and instead

focuses on the retirement investor's reasonable expectations and the circumstances surrounding the recommendation. The Proposed Rule explicitly states that disclaimers of fiduciary status will not be effective if other materials provided to, or interactions with, the retirement investor are indicative of a fiduciary relationship.

Primary Basis. The Proposed Rule would eliminate the existing requirement that the investment advice will serve as a "primary basis" for investment decisions. Instead, the Proposed Rule focuses on whether circumstances indicate that the investor may rely upon the advice as a basis for investment decisions in the investor's best interest.

Prohibited Transaction Exemption Amendments. In conjunction with its issuance of the Proposed Rule, the DOL amended PTE 2020-02 to require additional disclosures and narrowed the scope of various prohibited transaction class exemptions (PTEs 75-1, 77-4, 80-83, 83-1 and 86-128) relating to the receipt of otherwise prohibited compensation by investment advice fiduciaries. The DOL indicated that these changes are intended to encourage investment advice fiduciaries to solely utilize PTE 2020-02 for covered investment advice transactions, which requires adherence to "impartial conduct standards," including providing advice that is in the retirement investor's best interest.

Reactions to the Proposed Rule

As with prior attempts to modify the definition of fiduciary "investment advice," the Proposed Rule has already faced significant industry pushback, and its future is uncertain. The DOL received more than 19,000 comments and held a two-day hearing on the Proposed Rule prior to the expiration of the 60-day comment period on January 2, 2024. While some comments expressed support for the Proposed Rule's imposition of necessary protections for investors and the critical importance of retirement savings, many commenters opposed the rule. Several comments alleged that the Proposed Rule is overbroad, exceeds the DOL's authority and that stakeholders needed additional time to analyze the rule and provide feedback. Senators and House members from both parties have sent letters calling on the DOL to withdraw the proposal, and the House Financial Services Committee held a hearing regarding the necessity of the Proposed Rule on January 10, 2024. The rule faces the risk of being overturned under the Congressional Review Act, particularly if Republicans take control of both the House and the Senate in the next election and the rule is not finalized prior to the 60 legislative days preceding the seating of the next Congress. Finally, opponents of the Proposed Rule have signaled an intent to challenge the rule in court if necessary.

1. [81 FR 20946 \(Apr. 8, 2016\)](#) ↩

2. *Chamber of Commerce v. United States Department of Labor*, [885 F.3d 360 \(5th Cir. 2018\)](#) ↩

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