

DOL FIDUCIARY RULE IMPLEMENTATION DELAYED. WHAT DOES THE DOL DO NEXT?

HIGHLIGHTS:

- The Department of Labor (DOL) finalized regulations that change the longstanding fiduciary determination to broaden who classifies as a fiduciary under the Employee Retirement Income Security Act of 1974, as amended (ERISA).
- The DOL also amended several prohibited transaction exemptions with respect to investment advice, essentially creating a uniform standard for advice to plans and participants modeled after Prohibited Transaction Exemption 2020-2.
- The Final Rule was set to become effective on Sept. 23, 2024, and the changes to the prohibited transaction exemptions 2020-02 and 84-24 were to have a one-year phase-in from the effective date.
- On July 25, 2024, a Fifth Circuit federal judge in the Eastern District issued a stay that halted the implementation of the Fiduciary Rule until further notice. On July 26, 2024, the Northern District Circuit Court also issued a stay based on the case filed before it, also delaying the implementation of the new rule until further notice.
- The Courts noted that the plaintiffs were likely to succeed on the merits of their case and that the DOL did not appear to have narrowed their latest attempt in light of the Fifth Circuit's ruling to vacate the 2016 DOL Fiduciary Rule. The Eastern District Court also cited the recent Loper Bright case, (*Loper Bright Enterprises v. Raimondo*, 603 U.S. ____ (2024)) indicating that the Court no longer needs to show deference to administrative interpretations of laws and may decide for itself the intent behind unclear laws. For more information see "Legal Challenges" below.
- At this time, the original 1975 Rule should continue to be followed. Armstrong Teasdale will continue to monitor developments in the Fifth Circuit on the Fiduciary Rule and responses from the DOL.

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BACKGROUND

On April 23, 2024, the DOL finalized regulations titled the “Retirement Security Rule” (the Final Rule) that changed the longstanding meaning of what constitutes “investment advice” under the definition of a “fiduciary” under ERISA. This is the DOL’s latest attempt to alter the definition of “investment advice” which has remained unchanged since 1975. Based on the Preamble to the Final Rule, it is clear that the DOL, in their own way, attempted to produce a rule that could withstand a challenge in court by addressing concerns identified by the U.S. Court of Appeals for the Fifth Circuit (the Fifth Circuit) when that Court vacated the previous attempt to modify the investment advice definition.

In addition to amending the fiduciary definition, the DOL has amended certain existing prohibited transaction exemptions that investment advisors currently rely on by eliminating the advisor’s ability to receive relief when providing investment advice under such applicable exemption. Going forward fiduciaries will need to rely on a modified Prohibited Transaction Exemption 2020-02 and a modified Prohibited Transaction 84-24 to make investment advice relief conditions more standardized.

INVESTMENT ADVICE FIDUCIARY DEFINITION

The existing fiduciary rule contained five conditions that had to be met in order to be classified as an ERISA fiduciary: (i) render advice as to the value of securities or other property, or make recommendations as to the advisability of investing in, purchasing or selling securities or other property; (ii) provide advice on a regular basis (iii) pursuant to an express or implied mutual agreement, arrangement or understanding that such service will: (iv) serve as the primary basis for the plan’s investment decision; and (v) take into account the particular needs of the plan.

In the new Final Rules, the determination of who is a fiduciary is met upon meeting two conditions: if (i) the person makes a “**recommendation**” of any securities transaction or other investment transaction or any investment strategy to a “**retirement investor**” for a fee or other compensation (direct or indirect), *and* (ii) such recommendation is made either directly or indirectly (e.g., through or together with any affiliate) to investors on a regular basis as part of their business, and the recommendation is made under circumstances that would indicate to a reasonable investor in like circumstances that the recommendation (a) is based on review of the retirement investor’s particular needs or individual circumstances, (b) reflects the application of professional or expert judgment to the retirement investor’s particular needs or individual circumstances, and (c) may be relied on by the retirement investor as intended to advance the retirement investor’s best interest; or the person represents or acknowledges that they are acting as a fiduciary under ERISA with respect to

the recommendation.

Under the Final Rule, a “*retirement investor*” is defined as a plan, plan fiduciary, plan participant or beneficiary, IRA, IRA owner or beneficiary, or IRA fiduciary. The term “*recommendation*” has been defined to mean:

1. the advisability of acquiring, holding, disposing of or exchanging securities or other investment property, investment strategy or how securities or other investment property should be invested following a rollover, transfer or distribution from a plan or IRA;
2. the management of securities or other investment property, including, among other things, recommendations on investment policies or strategies, portfolio composition, selection of other persons to provide investment advice or investment management services, selection of investment account arrangements, or voting of proxies appurtenant to securities; or
3. rollovers, transfers or distributions of assets from a plan or IRA, including recommendations as to whether to engage in the transaction, the amount, the form and the destination of such a rollover, transfer or distribution.

AMENDMENTS TO PROHIBITED TRANSACTION EXEMPTIONS

The DOL finalized amendments to Prohibited Transaction Exemptions 2020-2 (PTE 2020-02) and 84-24 (PTE 84-24). In doing this, the DOL has made it clear that they are seeking uniformity when exempting reasonable compensation for fiduciaries providing investment advice. The DOL has officially eliminated from Prohibited Transaction Exemptions:

- 75-1 “Securities Transactions Involving Broker-Dealers, Reporting Dealers and Banks”
- 77-4 “Purchase of Shares of Open-End Investment Companies”
- 80-83 “Use of Proceeds from Sale of Securities to Reduce or Retire Indebtedness”
- 83-1 “Mortgage Pool Investment Trusts”
- 86-128 “Executing Securities Transactions and Recapture of Commissions,” the portion of those exemptions that allowed fiduciaries to receive reasonable compensation

Going forward, investment advice fiduciaries who use those exemptions for other transactions will need to rely on either PTE 2020-2 or PTE 84-24 to exempt the reasonable compensation component of any such transaction.

LEGAL CHALLENGES

Shortly after the DOL issued their Final Rule, insurance industry trade groups

filed a lawsuit in the Fifth Circuit's Eastern District of Texas and another in the Fifth Circuit's Northern District of Texas asking each Court to stay the DOL's Final Rule. The lawsuit brought in the Eastern District essentially claimed that the Final Rule was no different than the 2016 Fiduciary Rule that was vacated by the Fifth Circuit.

On July 25, 2024, the U.S. District Court for the Eastern District of Texas issued a stay siding with the insurance industry plaintiffs and enjoining the DOL from enforcing the Final Rule on its effective date of Sept. 23. In his decision, the judge stated that "Plaintiffs are likely to succeed on the merits of their claim because the 2024 Fiduciary Rule conflicts with ERISA in several ways, including by treating as fiduciaries those who engage in onetime recommendations to roll over assets from an ERISA plan to an IRA."

In addition, the Court cited to the Supreme Court's recent decision in *Loper Bright*, which overturned the so-called Chevron Doctrine which generally allowed administrative agencies to receive deference when interpreting ambiguities in the law, stating that "[a] court should no longer defer to an agency's interpretation of a statute but should decide for itself whether the law means what the agency says." Based on the overall language and tone of the Court's decision, it would appear that the DOL will have its work cut out for it if it wants to save this version of the fiduciary rule change.

On July 26, 2024, the Northern District Court also issued a stay that incorporated the Eastern District's holding but went further and extended the stay to the prohibited transaction exemption changes made under the Final Rule. The Northern District, like the Eastern District, found that the DOL's Final Rule was likely going to lose on the merits of the plaintiffs' claims and the plaintiffs would suffer irreputable harm if the Final Rule were to be implemented.

Lastly, the House of Representatives has passed a rule and included it in the 2025 fiscal budget to defund the DOL's priorities including the Fiduciary Rule. This could certainly help the insurance industry's argument that the DOL has not interpreted the intent of Congress correctly, seeing how Congress is attempting to defund the DOL's attempt to change the existing rule rather than support its implementation.

CONCLUSION

It appears that the DOL's fourth attempt to expand the fiduciary definition under ERISA could very well suffer the same fate as the previous three attempts. The Fifth Circuit's reasoning in issuing the stays certainly gives the impression that the Court is skeptical that the DOL, regardless of what was said in the preamble to the Final Rule, has made any significant changes to their Final Rule from the previous version which was vacated by the Fifth Circuit.



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Unlike in 2016, however, this time there has been a pause granted so that companies do not have to expend millions of dollars in resources to comply with a rule that could very well be found unlawful. The District Courts in Texas have provided relief for now, and the business community may wait to see how these cases resolve before taking any steps to implement these Final Rules. In the meantime, the existing 1975 rules will remain in effect as will the original text of the prohibited transaction exemptions that the DOL attempted to change.

If you have any questions regarding the proposed rules, please contact your regular Armstrong Teasdale lawyer or one of the listed authors.