

**Group Legal Services Association  
Solo, Small Firm, and General Practice Section  
2016 Joint Spring Meeting  
May 11-14, 2016, Key West, Florida**

---

**Cost-Containment Strategies for Health &  
Welfare Plans:  
A Trustee Oversight Issue**

---

**Friday, May 13  
10:30 am – 11:30 am  
Salon A-2**

**Presenter: Stephen Mogila, Pitta & Giblin, LLP, New York, NY**

## Stephen Mogila



Stephen Mogila is Partner and Chair of Pitta & Giblin LLP's Employee Benefits Law Practice Group.

Mr. Mogila has practiced as an attorney in all aspects of employee benefits issues, including establishment, design, administration and termination of pension, profit-sharing, welfare and executive compensation plans. He advises employers, plan sponsors and administrators on the full spectrum of plan investment issues and transactions, mergers and terminations, government audits, participant communications, fiduciary responsibility matters, minimum funding issues, withdrawal liability, and prohibited transactions issues.

Mr. Mogila has worked extensively with both multiemployer and single employer pension, defined contribution and welfare funds, and serves as fund counsel to numerous multiemployer funds, providing advice to trustees and administrators in connection with statutory and regulatory issues. He has assisted clients with issues related to the tax qualification of ERISA-covered plans, including the avoidance and correction of plan qualification defects, as well as ensuring their continued compliance.

Prior to joining Pitta & Giblin LLP, Mr. Mogila served as a Deputy Attorney General in the Treasury Section of the Office of the New Jersey Attorney General; and practiced for several years at Proskauer Rose in its Employee Benefits Practice Center.

Mr. Mogila is a member of the bar in New Jersey and Maryland; and has passed the New York Bar (pending application).

Mr. Mogila has written extensively on the impacts of the Health Care Reform Law, co-authoring a law review article on the U.S. Supreme Court's decision upholding law; and contributing to one of the industry's leading guides to understanding and complying with this law.

Mr. Mogila was recently recognized by the New Jersey Bar Association in its 2012 New Leaders of the Bar as one of New Jersey's top 50 lawyers under the age of 40.

Mr. Mogila is a graduate of Seton Hall University; and earned a J.D. at the University of Baltimore School of Law; and an LLM in Taxation at New York University School of Law.

**PITTA & GIBLIN LLP**



# **REVIEW OF DOL'S FINAL FIDUCIARY RULE**

**1**

**What Employers and Plan Sponsors Need to Know Regarding  
Investment Advice/Education.**

**Stephen J. Mogila, Esq.**

**For May 12, 2016 Presentation**

# OVERVIEW OF DOL'S POLICY CONSIDERATIONS

- Since ERISA was enacted, dramatic shift in retirement marketplace with introduction of 401(k) Plans and Individual Retirement Accounts (IRAs).
- Increased importance of sound investment advice for participants/retirees.
- Many investment professionals have compensation structures that are misaligned with the participant's interests or create strong incentives to steer them into particular products.
- Need to protect tax-preferred retirement savings by imposing a stricter fiduciary standard that puts the clients' best interests first.



# **Background – Road to the Final Fiduciary Rule.**

# SUMMARY OF REGULATORY PATH

## ○ Beginning in 2009

- DOL undertook a multi-year project to address conflict of interest issues with regard to investment advice – recognizing need to protect retirement savings while minimizing disruptions to good practices within the investment industry.
- DOL sought input from interested stakeholders and published two (2) proposals for comment – in 2010 and 2015.
- DOL held multi-day public hearings and reviewed thousands of comments from proponents and opponents to the proposed rules.
- DOL's proposal was published on April 20, 2015
- The Fiduciary Rule was finalized on April 8, 2016

# SUMMARY OF NEW REQUIREMENTS

## **New Fiduciary Definition under ERISA:**

- Expands definition of who is (and is not) a “fiduciary” investment adviser.

## **Introduction of two (2) new Prohibited Transaction Class Exemptions (“Exemption” or PTE”) designed to:**

- Permit certain broker-dealers, insurance agents, and others to act as investment advice fiduciaries and receive a variety of common forms of compensation based on adherence to certain requirements aimed at ensuring that their advice is impartial and in the best interest of their customers (plan sponsors and participants).

## **Going forward, under the new Fiduciary Rule, plan investment professionals must either**

- Avoid payments that create conflicts of interest or comply with the protective terms of an Exemption



# **What is (and is not) Covered Investment Advice Under the New Fiduciary Rule?**

6



# ERISA'S EXISTING FIDUCIARY DEFINITION FOR INVESTMENT ADVISORS

- Fiduciary Status
  - Covers person who provides “investment advice” relating to plan assets for compensation
  - Not a fiduciary if no investment advice is given
- 5-Prong Definition for “Investment Advice”
  - Making investment recommendations
  - On regular basis
  - Mutual understanding
  - Primary basis for plan’s decisions
  - Individualized to plan’s needs

# NEW FIDUCIARY DEFINITION FOR INVESTMENT ADVISORS

- **Required Context for Investment Advice**
  - Advisor acknowledges it is acting as a fiduciary under ERISA or Internal Revenue Code, or
  - Written or verbal understanding that advice is based on particular investment needs of client, or
  - Advice is directed to specific person(s) regarding advisability of a particular investment decision
  
- **Required Nature of Investment Advice**
  - Advisor makes a “recommendation” for a fee or other direct or indirect compensation

# WHAT CONSTITUTES A “RECOMMENDATION” UNDER THE NEW RULE?

## Covered Recommendations to Plan/IRA

- On advisability of investing in property, or
- Relating to management of property including:
  - IPS, strategies, portfolio composition
  - Selection of other persons to provide advice
  - Selection of account (brokerage vs. advisory)
  - Transfers or rollovers from Plan/IRA

## “Recommendation”

- Reasonably viewed as suggestion to engage in particular course of action (i.e., call to action)

# MATERIAL CHANGES BETWEEN THE OLD AND NEW RULE

- Changes to “Investment Advice”
  - Includes one-time advice (without “regular basis” condition)
  - No need for “mutual understanding” of parties
  - Advice may address particular investment needs or a particular investment decision (and does not necessarily need to be individualized)
  - Client only needs to receive advice (which does not need to be “primary basis” for decisions)
  - Expressly revises definition to cover investment management recommendations

# WHAT IS NOT COVERED INVESTMENT ADVICE UNDER THE NEW RULE?

- Exclusions from “Recommendations”
  - Platform Providers
  - Investment Education
  - General Communications
  
- Exclusions from “Fiduciary” Definition
  - Sellers to Institutional Fiduciaries
  - Swap Counterparties
  - Plan Sponsor’s Employees

***NOTE:** Exclusion does not apply if the advisor acknowledges its fiduciary status*

# FIRST EXCLUSION – PLATFORM PROVIDERS

## Requirements for “Platform Provider” Exclusion

- Defined Contribution Plan record-keepers may market investment options available through their platforms (without regard to individualized needs)
- Must disclose that platform does not provide impartial fiduciary advice
- Can identify options that meet objective criteria (where financial interests are disclosed)
- Can identify sample list of options based on plan size or current options in response to request for proposal (where financial interests are disclosed)
- Can provide objective financial data and benchmark comparisons

## SECOND EXCLUSION – INVESTMENT EDUCATION

- **Similar to Current Safe Harbor (IB 96-1)**
  - Plan Information
  - General Financial/Retirement Information
  - Asset Allocation Models
  - Interactive Investment Materials
- **Observations**
  - Exclusion applies to both Plans and IRAs
  - Asset allocation models and interactive materials cannot reference specific options unless:
    - They are subject to oversight of plan sponsor
    - Options with similar risk/return are identified
    - Statement on how more info may be obtained

# THIRD EXCLUSION – GENERAL COMMUNICATIONS

- Definition of “General Communications”
  - Reasonable person must not view as investment recommendation
- Examples
  - Newsletters, talk shows
  - Speeches and conferences
  - Research or news reports
  - Market data
  - Performance reports
  - Prospectuses



# FOURTH EXCLUSION – SELLERS TO INSTITUTIONAL FIDUCIARIES

- Scope of Exclusion
  - Covers advice provided by seller of investment product to Institutional Fiduciary of a Plan/IRA
  - Institutional Fiduciary has over \$50 million in assets under management (AUM) or is a Bank, Insurer, Registered Investment Adviser (RIA) or Broker Dealer
- Requirements for Exclusion
  - Seller informs that it is not providing impartial fiduciary advice
  - Seller does not receive any direct compensation
  - Seller reasonably believes that Institutional Fiduciary is capable, independent, licensed and regulated provider of financial services
  - Conditions are designed to ensure that exclusion is limited to a true arm's length transaction between an adviser and investment professional or large asset manager who do not have an expectation that this relationship will create an impartial advice between them.

# FIFTH EXCLUSION – SWAP COUNTERPARTY

- Requirements for this Exclusion:
  - Counterparty is swap dealer (or security-based swap dealer) or major swap participant
  - Not acting as “advisor” to plan under Commodity Exchange Act or Securities Exchange Act
  - Does not receive any direct compensation
  - Written representation from plan fiduciary that it understands:
    - Advice is not impartial fiduciary advice
    - It is exercising independent judgment

This exemption is coordinated with both the Commodities Futures Trading Commission and the Securities and Exchange Commission

# SIXTH EXEMPTION – PLAN SPONSOR EMPLOYEES

- **Advice from Employee to Plan Sponsor**
  - Exclusion applies if employee does not receive compensation beyond employee's normal pay
  - Carve-out is designed to protect employees from potential fiduciary liability
  
- **Advice from Human Resource (HR) Employee to Co-Worker**
  - HR employee's duties do not include providing advice
  - HR employee is not licensed (or required to be licensed) under securities or insurance law
  - No compensation beyond normal pay

# KEY DIFFERENCES/COMPARISONS TO THE DOL'S PROPOSED RULE

- Generally speaking, the DOL's Final Rule follows the structure of its proposed rule.
- Clarifications in Final Fiduciary Definition
- Fiduciary advice may be limited to one-time advice (subject to Best Interest standards)
- Asset allocation "Investment Education" for IRAs must not refer to specific investments
- Marketing/Advertising ("Hire Me") recommendation is not fiduciary advice
- Appraisals are not fiduciary advice and will be addressed in future (including ESOP appraisals)
- See Handout of DOL Chart identifying all differences between the Proposed and New Fiduciary Rule.



# **Discussion of New Prohibited Transaction Exemptions**

19

## NEW PROHIBITED TRANSACTION EXEMPTIONS RELATED TO THE NEW FIDUCIARY RULE

- Need for “ERISA 406(b)” Exemptive Relief
  - New “investment advice” definition confers fiduciary status on all types of advisors
  - Prohibited transaction rules ban advisors from earning variable compensation (commissions)
  - Exemption required for brokers and insurance agents, including advisors to IRAs
  - DOL has created Best Interest Class Exemption

# THE BEST INTEREST CONTRACT (BIC): STRONGER PROTECTIONS FOR RETIREMENT SAVINGS

- General Prohibition – Under ERISA and Code, fiduciary investment advisers to plan sponsors, participants, and IRA owners can NOT receive payments creating conflicts of interest without a prohibited transaction exemption (“PTE”)
- BIC Exemption – Advisers may continue to use current compensation/fee practices
  - BUT, must meet specific conditions to mitigate conflicts of interest; and
  - Provide investment advice in the best interests of their customers.
- Observations
  - No relief for variable compensation arising from discretionary advice

# POLICY CONSIDERATIONS FOR BIC EXEMPTION

To align advisers' interests with customers:

- Financial institution must acknowledge fiduciary status for itself and its advisers.
- Financial institution and advisers must adhere to basic standards of impartial conduct,
  - Giving prudent advice that is in the customer's best interest,
  - Avoiding making misleading statements, and
  - Receiving no more than reasonable compensation.

Financial institution must

- have policies and procedures to mitigate harm from conflicts of interest
- disclose basic information about their conflicts of interest and the cost of their advice.



## DISCLOSURE REQUIREMENTS FOR BIC EXEMPTION

- Investment Advisers must provide:
  - Descriptions of material conflicts of interest, fees, or charges paid by investor; and
  - Statement of types of compensation the firm expects to receive from third parties in connection with recommended investments.
- Investment Advisers must provide upon request:
  - Specific disclosure of costs, fees, and other compensation

## ADDITIONAL DISCLOSURE REQUIREMENTS

- Investment Adviser must maintain and regularly update website for:
  - financial institution's business model
  - and associated material conflicts of interest
  - a written description of the financial institution's policies and procedures that mitigate conflicts of interest; and
  - disclosure of compensation and incentive arrangements with advisers, among other information.
- Individualized information about a particular adviser's compensation is not required to be included on the website.

# PRINCIPAL TRANSACTIONS EXEMPTION

- Fiduciary investment advisers may sell/purchase certain recommended debt securities and other investments out of their own inventories to or from plans and IRAs
- MUST adhere to certain impartial conduct standards:
  - Act in the customer's best interest;
  - Avoid misleading statements; and
  - Seek out best execution reasonably available under the circumstances.

# ERISA COMPLIANCE PLANNING

- Plan Sponsors should consider:
  - Reviewing all existing investment adviser contracts to identify fiduciary relationships and ensure that the appropriate contractual representations are reflected in the related service agreements.
  - Reviewing plan policies and procedures for providing investment information to make sure that they have not crossed the line into providing investment advice for a fee.

# EFFECTIVE DATE AND TRANSITION

- Phase-in of New Requirements
- New Fiduciary Rule becomes effective on April 10, 2017
- Certain PTE conditions are phased in on this date, and other conditions go into effect on January 1, 2018