REGULATORY Update

QUARTERLY UPDATE, JULY 2017

DOL Conflict of Interest Rule Finally Takes Effect, Yet Uncertainty Remains

On June 9, 2017, the Department of Labor's (DOL) Conflict of Interest Rule became effective. This landmark date may seemingly signal a turning of the page on one of the most anticipated—and most debated—regulations to impact the qualified retirement plan industry in more than 40 years. Yet some of the rule's finer points, including its implementation, enforcement, and, ultimately, its fate, continue to be mired in uncertainty.

As a refresher, the Conflict of Interest Rule was originally proposed in 2010 and underwent numerous revisions before a final version was arrived at in April 2016. It broadens the definition of fiduciary advice on qualified retirement accounts, including workplace retirement plans covered under ERISA, and IRAs. It also requires fiduciaries to act in the best interests of retirement plan participants and retirement account holders when providing investment advice.

Where things stand today

As of June 9, anyone who receives compensation for providing investment advice to investors in an ERISA-covered retirement plan or IRA is considered a fiduciary. For example, financial advisors *must* provide impartial advice to retirement investors and cannot receive payments, such as commissions, that present a conflict of interest for providing that investment advice. But advisors may charge clients an advisory fee, which has no correlation to the advice provided, and still be in compliance with the rule.

The rule does allow financial advisors to receive non-fee-based compensation, such as commissions, provided that the advisor qualifies for an exemption, known as a Best Interest Contract (BIC) exemption. Under the BIC exemption, financial advisors must commit, via a written contract, to putting the client's best interests first and disclose any conflicts that may prevent them from doing so.

Since the DOL rule was finalized in April 2016, financial firms of all shapes and sizes have been dedicating time, resources, and capital to building operational infrastructures that would comply with the terms of the rule when it became effective.

A looming cloud of uncertainty

So, given that the DOL rule has already taken effect, what are the factors causing further uncertainty? Mainly, it boils down to politics, with leaders from both sides of the aisle continuing to forecast the positive and negative consequences of the rule.

When Donald Trump secured the White House and the Republicans swept Congress in November 2016, doubt was cast on the sustainability of the rule, which had been championed by the Obama administration. In February 2017, President Trump issued a memorandum instructing the DOL to conduct further examination of the rule, including its impact on the economy and on retirement investors in particular. In March 2017, the DOL filed a request with the Office of Management and Budget to impose a 60-day delay on implementation of the rule.

Subsequently, in May 2017, newly appointed Secretary of Labor Alexander Acosta declined to delay the rule's June 9 effective date. But he indicated that the DOL would continue to reassess the rule, which could lead to a restructuring of the regulation. In the interim, the DOL indicated that it would not enforce certain elements of the rule through January 1, 2018. On July 6, the DOL opened a new comment period, during which further public comments will be collected on certain provisions of the rule, most notably, the BIC exemption.

What do retirement plan sponsors need to know?

Unlike the roller-coaster ride leading up to the rule's implementation, sponsors of workplace retirement plans, like 401(k)s, should experience few bumps in the road in carrying out the day-to-day administrative duties for their plans. In some cases, sponsors may need to revise agreements or contracts in order to comply with the new rule (as it stands today).

But, as fiduciaries themselves, plan sponsors have a duty to monitor those who provide services to their retirement plans and employees. They should understand the crux of the DOL rule, particularly how service providers (including financial advisors, asset managers, third-party administrators, etc.) who perform services for their retirement plans are compensated.

New IRS Procedures for Preapproved Plan Opinion Letters

On June 30, 2017, the IRS announced new procedures, Rev. Proc. 2017-41, for issuing opinion letters on preapproved retirement plans. The procedures seek to "modify the IRS's historic approach to preapproved plans in order to expand the provider market and encourage employers that currently maintain individually designed plans to convert to the preapproved format."

The new procedures eliminate the distinction between master and prototype (M&P) and volume submitter (VS) plans, combining them into one opinion letter program. This reflects the intention on the part of the IRS to simplify the opinion letter program. And, by expanding the types of plans that qualify for preapproved status, the IRS is clearly looking to point more plans toward adopting a preapproved design, rather than maintaining an individually designed format.

Compliance Tip: Is a Midyear Nondiscrimination Test a Good Idea for Your Plan?

Retirement plan sponsors are likely familiar with the annual nondiscrimination tests required to satisfy IRS and DOL mandates. The data collection process and testing usually take place in February or early March (for calendar-year plans), but plan sponsors may also implement a midyear nondiscrimination test. Such a test can serve as a "dry run," enabling you to stay ahead of the curve on several important plan governance tasks. For example, a midyear test can help you:

- Project potential testing results for the following year and provide highly compensated employees (HCEs) with advanced notice that they could receive a corrective refund of some or all of their contributions
- Uncover operational errors, such as excess contributions, eligibility mistakes, and data inaccuracies
- Get a jump on contemplating a more suitable plan design (e.g., installing a safe harbor match for plans that consistently fail annual nondiscrimination testing)

Consult your third-party administrator, recordkeeper, or plan advisor to find out if conducting a midyear test is the right move for your plan.

We Can Help

Our firm is ready to provide you with the ideas, guidance, and foresight to position your firm for success. If you would like to review the DOL Conflict of Interest Rule, new IRS procedures, or any aspect of your retirement plan, we're here to assist you.

Commonwealth Financial Network® does not provide legal or tax advice. Please contact your legal or tax advisor for advice on your specific situation.

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