

## Comparison of Proposed DOL Investment Advice Exemption to SEC Regulation Best Interest

August 14, 2020

The table below compares the requirements of the SEC’s Regulation Best Interest and the conditions of the DOL’s proposed Improving Investment Advice for Workers and Retirees Class Exemption (the proposed class exemption), along with select observations. It is important to note that compliance with the proposed class exemption is not mandatory and other exemptions may be available for certain transactions, or an exemption may not be needed where a financial institution is not acting as a fiduciary or is not retaining variable compensation in connection with fiduciary investment advice. This comparison is intended to help firms assess the extent to which compliance with Reg. BI’s requirements can be leveraged to comply with the requirements of the proposed class exemption.

Requirement	Reg. BI	Proposed Class Exemption	Observations
<b>Covered Customers/ Clients</b>	“Retail customer”— a natural person, or legal representative of such natural person, who receives a recommendation of any securities transaction or investment strategy involving securities from a broker-dealer (or natural person who is an associated person) and <b>uses the recommendation primarily for personal, family, or household purposes.</b>	“Retirement Investor” — a <b>participant</b> or <b>beneficiary</b> of an ERISA-covered <b>plan</b> with authority to direct the investment of assets in his or her account or to take a distribution; the <b>beneficial owner of an IRA</b> (including HSAs, Archer MSAs, and Coverdell education savings accounts); or a <b>fiduciary</b> of a Plan or IRA.	<p>Reg. BI’s definition of retail customer focuses on natural persons and their legal representatives and is limited to persons who will use the advice for personal, family, or household purposes.</p> <p>Both Reg. BI and the proposed class exemption would apply to recommendations to plan participants and IRA owners, but Reg. BI generally does not apply to recommendations to plan sponsors/fiduciaries acting as such.</p> <p>Note that the DOL’s vacated Best Interest Contract Exemption would not have been available with respect to advice provided to large plan fiduciaries, for which there would instead have been a carve-out from fiduciary investment advice status. Given that the carve-out has been repealed, the proposed class exemption does not include this limitation.</p>

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<b>Covered financial institutions</b>	Registered broker-dealers	<p>Available to:</p> <ul style="list-style-type: none"> <li>• State and federally registered investment advisers</li> <li>• State and federally supervised banks and savings associations</li> <li>• State-qualified insurance companies</li> <li>• Registered broker-dealers</li> </ul> <p>To be able to use the exemption, financial institution (and investment professional) may not be disqualified or barred from making investment recommendations by any insurance, banking, or securities law or regulatory authority (including any self-regulatory organization).</p> <p>Other entities may apply to the DOL for individual prohibited transaction exemptions based on the same conditions as the proposed class exemption.</p>	While Reg. BI applies only to broker-dealers, the proposed class exemption would also be available to investment advisers, banks, and insurance companies.
<b>Covered transactions</b>	<p>Recommending:</p> <ul style="list-style-type: none"> <li>• securities transactions, or</li> <li>• investment strategies involving securities (including account-type and rollover recommendations)</li> </ul>	“Fiduciary” investment advice (i.e., nondiscretionary advice or recommendations with respect to securities or other property that would cause the financial institution or investment professional to be an ERISA or Code Section 4975 fiduciary under the five-part test) that results in:	<p>Reg. BI applies to all securities recommendations, while the proposed class exemption would be available for advice or recommendations regarding securities and “other property.”</p> <p>Both may apply to rollover and account-type recommendations.</p> <p>A key issue to consider in assessing the proposed</p>

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		<ul style="list-style-type: none"> <li>• The receipt of reasonable compensation;</li> <li>• The purchase or sale of an asset in a riskless principal transaction or a Covered Principal Transaction, and the receipt of a markup, markdown, or other payment.</li> </ul> <p>For sales to (but not purchases by) plans and IRAs, "Covered Principal Transaction" is limited to transactions involving:</p> <ul style="list-style-type: none"> <li>• US corporate debt securities</li> <li>• US Treasury and other federal agency securities</li> <li>• Debt securities of a government-sponsored enterprise</li> <li>• Municipal securities</li> <li>• Certificates of deposit</li> <li>• Interests in UITs</li> </ul> <p>The DOL would consider individual class exemptions for other investments subject to the same conditions as the class exemption.</p> <p>Purchases from plans and IRAs are not similarly limited to types of security.</p>	<p>class exemption is the limitation on securities that can be sold to a plan in a principal transaction. Notably, the proposed class exemption would not be available for principal transactions involving sales to plans of equity securities (including IPOs) and closed-end funds.</p> <p>Note also that not all Reg. BI recommendations are necessarily fiduciary investment advice under the five-part test and this should be carefully analyzed. The preamble to the proposed class exemption indicates the DOL's view that a retirement investor would understand a Reg. BI recommendation to be a "primary basis" for an investment decision, so that it would likely meet this one part of the test, but to constitute fiduciary investment advice, it must meet the four other parts as well. Thus, additional factors would need to be analyzed.</p>
<b>Exclusions, ineligibility, and disqualifications</b>	None	Proposed class exemption would not be available to financial institutions and investment professionals who:	Consider potential issues where advice is provided to participants by a financial institution that is a named fiduciary to the plan (e.g.,

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		<ul style="list-style-type: none"> <li>• Sponsor the plan involved in the transaction</li> <li>• Are the named fiduciary or plan administrator of the plan involved in the transaction, unless selected to provide advice by an independent plan fiduciary</li> </ul> <p>The proposed class exemption would also be unavailable to robo-advisors (without personal interaction with an investment professional) and where the investment professional is acting in a fiduciary capacity other than as an investment advice fiduciary (<i>e.g.</i>, investment manager for the assets of the plan).</p> <p>Financial institutions and investment professionals would be ineligible to rely on the proposed class exemption if convicted of a crime in ERISA Section 411 as a result of their or a control group member providing investment advice to a retirement investor, or where the DOL provides notice of ineligibility for intentionally, or engaging in a “systematic pattern or practice” of, violating the exemption or providing materially misleading information to the DOL in connection with the exemption. The proposed class exemption includes procedures for hearings and a one-year wind-down</p>	<p>in OCIO arrangements or potentially in a “pooled employer plan” arrangement), as well as with respect to the investment professional’s own IRA (unless provided without compensation).</p> <p>The ineligibility provisions are different from those under the QPAM exemption—narrower in the sense that they include only crimes involving advice to retirement investors, but broader in that the DOL has fairly broad discretion to determine that a firm or investment professional is ineligible to rely on the proposed class exemption. This condition poses some risks to firms who choose to rely on it, as a DOL finding which could be subjective, may effectively prohibit a firm from providing recommendations and advice with respect to retirement investors where no other exemption or compensation structure is available.</p>

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		period, among other procedures.	
<b>Standard of conduct</b>	"best interest"	"best interest"/"fiduciary"	The proposed class exemption defines the applicable standard as "best interest," but required firms to acknowledge fiduciary status under ERISA and the Code. This contrasts with the SEC's express decision to differentiate broker-dealers and investment advisers by not calling the broker-dealer standard a "fiduciary" standard. While ERISA/Code and the securities laws are under different statutory regimes, consider the potential for investor confusion here, as well as potential issues under state fiduciary laws.
<b>Conflict of interest</b>	"Conflict of interest" — an interest that might incline a broker, dealer, or a natural person who is an associated person of a broker or dealer—consciously or unconsciously—to make a recommendation that is not disinterested.	"Conflict of Interest" — an interest that might incline a Financial Institution or Investment Professional — consciously or unconsciously — to make a recommendation that is not in the Best Interest of the Retirement Investor.	Both define conflict of interest similarly.
<b>Loyalty/Conflicts</b>	Act <b><i>without placing the financial or other interest</i></b> of the broker, dealer, or natural person who is an associated person from making the recommendation <b><i>ahead of</i></b> the interest of the retail customer. Must establish, maintain, and enforce written policies and procedures <b><i>reasonably</i></b> designed to: <ul style="list-style-type: none"> <li>• Identify and at a minimum <b><i>disclose,</i></b></li> </ul>	Advice <b><i>does not place the financial or other interests</i></b> of the Investment Professional, Financial Institution, or any affiliate, related entity, or other party <b><i>ahead of the interests</i></b> of the Retirement Investor, <b><i>or subordinate the Retirement Investor's interests</i></b> to their own. <p>Policies and procedures mitigate Conflicts of Interest "to the extent that the policies and</p>	Both raise questions as to the extent to which disclosure can address a conflict of interest, and, if not, what additional steps to mitigate the conflict are required. <p>Unlike Reg. BI, the proposed class exemption does not expressly limit the requirement to mitigate conflicts to financial incentives for investment professionals.</p>

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	<p><i>or eliminate, all conflicts of interest</i> that are associated with such recommendations.</p> <ul style="list-style-type: none"> <li>• Identify and <i>mitigate any</i> conflicts that create an incentive for a natural person who is an associated person of a broker-dealer to place the broker-dealer's or associated person's interests ahead of the retail customer's interests.</li> <li>• Identify and <i>disclose any material limitations</i> placed on recommendations of securities or investment strategies and <i>any conflicts of interest associated</i> with such limitations. <b>Prevent such limitations and associated conflicts of interest</b> from causing the broker, dealer, or natural person who is an associated person to make recommendations that place their interest ahead of the retail customer.</li> <li>• Identify and <i>eliminate</i> any sales contests, sales quotas, bonuses, and noncash compensation that are based on the sales of <i>specific securities or specific types</i> of securities <i>within a</i></li> </ul>	<p>procedures, and the Financial Institution's incentive practices, when viewed as a whole, are prudently designed to <b>avoid misalignment of the interests</b> of the Financial Institution and Investment Professionals and the interests of Retirement Investors in connection with covered fiduciary advice and transactions.</p>	<p>The preamble to the proposed class exemption indicates the DOL's view that supervisory oversight and mitigation of financial incentives complement each other and provide flexibility to adjust the stringency of each component based on the business model—as an example, where there is significant variation in compensation, the firm could implement more stringent supervisory oversight.</p> <p>Page 40,846 of the preamble to the proposed exemption includes additional examples of mitigation as potential strategies that could satisfy the proposed class exemption. These examples are generally consistent with approaches to mitigation under Reg. BI.</p> <p>The DOL indicates that sales contests with respect to certain products would not be permitted under the proposed class exemption and would require firms to "carefully consider performance and personnel actions and practices that could encourage violations of the Impartial Conduct Standards."</p> <p>The DOL notes in the preamble, that Financial Institutions Investment Professionals can have limited menus, focus on proprietary products or products that pay third-party compensation, but such limitations and</p>

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	<p><i>limited period of time.</i></p>		<p>conflicts would need to be disclosed to the Retirement Investor, and the firm would need to adopt policies and procedures to prevent conflicts from causing misalignment of interests—including where the proprietary products on the limited menu do not offer a best interest option when compared with other available investment alternatives in the marketplace.</p>
<p><b>Care</b></p>	<p>Must act in the retail customer’s best interest and exercise reasonable diligence, care, and skill to:</p> <ul style="list-style-type: none"> <li>• <b>Understand</b> the potential <b>risks, rewards, and costs</b> associated with the recommendation and have a reasonable basis to believe the recommendation could be in the best interest of at least some retail customers;</li> <li>• Have a <b>reasonable basis</b> to believe that the recommendation is in the <b>best interest of a particular retail customer based on</b> that retail customer’s <b>investment profile</b> and the potential <b>risks, rewards, and costs</b> associated with the recommendation and does not place financial or other interests ahead of</li> </ul>	<p>Advice must reflect the care, skill, <b>prudence</b>, and diligence under the circumstances that a prudent person acting in a like capacity and familiar with such matters would use, based on the investment objectives, risk tolerance, financial circumstances, and needs of the Retirement Investor.</p> <p>Financial institution must <b>document</b> “the specific reasons” that <b>any rollover recommendation</b> (plan-to-IRA, plan-to-plan, IRA-to-IRA, or from one account type to another account type) is in the Best Interest if the Retirement Investor.</p> <p>If the transaction is a <b>sale</b> to a plan or IRA in a <b>principal transaction</b>, and the recommended investment is a <b>debt security</b>, must have written policies and procedures that are reasonably designed to ensure that the security, at the time of the recommendation, has no</p>	<p>The SEC expressly declined to use “prudence” in the Reg. BI Care Obligation</p> <p>However, the preamble to the proposed class exemption states that the DOL intends this standard to be interpreted and applied consistently with Reg. BI.</p> <p>Reg. BI does not require documentation of the basis of any recommendation, but the SEC indicated that documentation may be viewed as a best practice.</p> <p>Reg. BI does not impose express limits on credit risks and liquidity.</p>



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	<p>retail customer's interests; and</p> <ul style="list-style-type: none"> <li>Have a <b>reasonable basis</b> to believe that a <b>series of recommended transactions</b>, even if in the retail customer's best interest when viewed in isolation, <b>is not excessive</b> and is in the retail customer's <b>best interest when taken together</b> in light of the retail customer's investment profile and does not place financial or other interests ahead of retail customer's interests.</li> </ul>	<p>greater than moderate credit risk and sufficient liquidity that it could be sold at or near carrying value within a reasonably short period of time.</p>	
<b>Reasonable compensation</b>	<p>No specific requirement; SEC noted in proposed Regulation Best Interest that broker-dealers already required to receive only fair and reasonable compensation.</p>	<p>Compensation received, directly or indirectly, does not exceed reasonable compensation within the meaning of ERISA Section 408(b)(2) and Code Section 4975(d)(2).</p>	<p>Neither requires that the lowest cost option be recommended.</p> <p>Preamble to the proposed class exemption notes that reasonable compensation can be based on the totality of the services.</p>
<b>Best execution</b>	<p>No specific requirement under Regulation Best Interest; broker-dealers already subject to best execution obligations, but encompassed in other SEC and FINRA rules.</p>	<p>Must seek to obtain the best execution of the investment transaction reasonably available under the circumstances.</p>	<p>What if the investment advice fiduciary under the class exemption is not involved in executing the transaction? Under the predecessor exemptions, "best execution" had applied only to principal transactions.</p>
<b>Ongoing/episodic</b>	<p>Obligation applies <b>prior to or at the time recommendation is made</b>.</p>	<p>Obligation applies <b>at the time investment advice is provided</b>.</p>	<p>Obligations for both are generally limited to the time a recommendation/ investment advice is provided, and do not impose ongoing obligations.</p>
<b>Compliance</b>	<p>Establish, maintain, and enforce written policies</p>	<p>Establish, maintain, and enforce written policies and</p>	<p>Not clear whether "reasonably" versus</p>



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	and procedures <b>reasonably</b> designed to achieve compliance with Regulation Best Interest.	procedures <b>prudently</b> designed to ensure compliance with the Impartial Conduct Standards in connection with covered fiduciary advice and transactions.	“prudently” would suggest a meaningfully different standard in this context.
<b>Retrospective review</b>	None, but the DOL indicated that the proposed class exemption’s retrospective review requirement is based on FINRA Rule 3130.	<p>Financial Institution must conduct a retrospective review, at least <b>annually</b>, reasonably designed to assist in detecting and preventing violations of, and achieving compliance with, the Impartial Conduct Standards and the policies and procedures governing compliance with the proposed class exemption.</p> <p>The methodology and results of the retrospective review must be reduced to a written report that is provided to the Financial Institution’s chief executive officer (or equivalent officer) and chief compliance officer (or equivalent officer).</p> <p>The Financial Institution’s chief executive officer (or equivalent officer) must certify, annually, that:</p> <ul style="list-style-type: none"> <li>• The officer has reviewed the report of the retrospective review;</li> <li>• The Financial Institution has in place policies and procedures prudently designed to achieve compliance with the conditions of this exemption; and</li> </ul>	<p>As this condition is based on a FINRA rule, registered broker-dealers should presumably already have a process in place to conduct such reviews.</p> <p>However, it is less clear that registered investment advisers, banks, and insurance companies currently have, or would readily be able to implement, this type of process.</p> <p>It is unclear to what extent this obligation can be delegated to another senior officer or executive.</p>

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		<ul style="list-style-type: none"> <li>The Financial Institution has in place a prudent process to modify such policies and procedures as business, regulatory and legislative changes and events dictate, and to test the effectiveness of such policies and procedures on a periodic basis, the timing and extent of which is reasonably designed to ensure continuing compliance with the conditions of this exemption.</li> </ul> <p>Retrospective review report, certification, and supporting data must be kept for a period of six years, and must be made available to the DOL upon request.</p>	
<p><b>Recordkeeping</b></p>	<p>Must keep records of all information collected from and provided to the retail customer and the identity of each representative responsible for the account.</p> <p>Records must be retained for at least <b>six years</b> after the earlier of the date the account was closed or the date on which the information was collected, provided, replaced, or updated.</p> <p>Must maintain a record of the fact that oral disclosure was provided</p>	<p>Records would need to be kept for <b>six years</b> demonstrating compliance with the proposed class exemption.</p> <p>Records would need to be made available upon request to the following persons:</p> <ul style="list-style-type: none"> <li>DOL;</li> <li>Fiduciary of a Plan that engaged in a transaction pursuant to the exemption;</li> </ul>	<p>Reg. BI would generally not require financial institutions to make records available to individual investors; as such the proposed class exemption goes beyond Reg. BI's requirements. This scope of availability may also raise issues under banking laws and state laws.</p>

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	to the retail customer, if applicable.	<ul style="list-style-type: none"> <li>Contributing employer or any employee organization whose members are covered by a plan that engaged in a transaction pursuant to the exemption; or</li> <li><b>Any participant or beneficiary of a plan, or IRA owner</b> that engaged in a transaction pursuant to the exemption.</li> </ul>	
<b>Disclosures</b>	<p>Must disclose <b>prior to or at the time</b> of the recommendation <b>all material facts</b> relating to the scope and terms of the relationship with the retail customer, including broker-dealer capacity, material fees and costs, type and scope of services (including any material limitations), and all material facts regarding conflicts of interest associated with the recommendation.</p> <p>Must provide disclosure in writing either prior to or at time of the recommendation.</p>	<p>Must disclose <b>prior to</b> engaging in the transaction:</p> <ul style="list-style-type: none"> <li>A written <b>acknowledgment of fiduciary status</b> under ERISA and the Code, as applicable, with respect to any fiduciary investment advice provided,</li> <li>A written description of the services to be provided, and</li> <li>A written description of all material Conflicts of Interest that is accurate and not misleading in all material respects.</li> </ul> <p>Statements to the Retirement Investor about the recommended transaction and other relevant matters may not</p>	<p>Other than with respect to the fiduciary acknowledgment (discussed above), the proposed class exemption does not seem to require disclosures that would be in addition to those Reg. BI requires. However, clarity on this point and any required timing would be helpful.</p>

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		be materially misleading when made.	
<b>Effective date</b>	June 30, 2020	60 days after publication of the final class exemption in the <i>Federal Register</i> .	The proposed class exemption effective date would also be expected to mean the termination of the DOL temporary non-enforcement relief that was announced following the repeal of the DOL Fiduciary Rule and related exemptions. While generally it would be preferable to have an earlier effective date to a class exemption, there may be requests to postpone the effective date or extend the non-enforcement relief to accommodate a transition to the new exemption.