Fiduciary Rule: Enforcement by No Enforcement

If you thought the Fiduciary Rule was mind boggling, the latest DoL policy directive takes contradictions to new levels.

First, the facts.

The DoL has confirmed that the Fiduciary Rule will take effect on June 9th, 2017 ("Transition Period"). But the enforcement of the Rule (See FAB 2017-02) and several of the exemptions will not be applicable until after a review ordered by President Trump. This final portion of the rule is scheduled for January 1st, 2018 and is likely to be changed from what is on the books today.

The promise of no enforcement does come with strings attached and offers only limited protection until the final portion of the Rule becomes applicable.

The first "string" is that new business must comply with three of the provisions of the BIC exemptions. All new business must meet the standard of being in the client's best interest, compensation must not be above a reasonable level and there can be no material misleading statements. While it is not necessary to prove compliance, **doing nothing is an enormous risk**.

The second "string" is that compensation from existing accounts must not be above a reasonable level. It is necessary to test if the compensation from existing accounts is reasonable.

The third "string" is that advisors and firms must be able to show that they are *working diligently and in good faith to comply* with the new Rule. **It becomes essential to show progress or readiness during the Transition Period**.

The protections offered by the DoL no-enforcement policy extends to the IRS but *does not address the rights or obligations of other parties*. Other parties include other regulators and clients who have the right to sue if they should lose money and find non-compliance!

Now, what it means.

Starting on June 9th, firms and advisors will be at risk for doing nothing. Action is required to move in the direction of compliance with the new Rule.

It is also far from certain what the new rule will be. Compliance must be based on the current version of the Rule and adaptations made if the Rule changes. While it is unlikely that the June 9th regulations will change materially, it is very likely that the delayed portions will be revised.

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The January 1st date is also subject to change, so the Transition Period could go on for an extended period, increasing the odds of a market crash or other events that lead to lawsuits.

And finally, how to avoid trouble.

The looming question is what actions make the most sense for firms to take leading up to June 9th and immediately thereafter. The following list of actions are prudent because they demonstrate working diligently, are low cost and least likely to be changed as well as offer the best protection from threats outside the DoL and IRS:

- Get trained on fiduciary practices that apply to the business that are designated as “fiduciary” by the June 9th applicability. A certification will show that that work was done and the threat of litigation is minimized by learning what prudent fiduciary practices are.
- Develop new templates that permit advisors to accurately discover what client’s best interests are.
- Write procedures that adapt the business to fiduciary practices.
- Begin the process of changing practices to meet the fiduciary standard.
- Test the reasonableness of compensation for existing clients and make the necessary changes that justify the compensation.
- Notify clients of changes that affect them.
- Consider using an exemption other than those outlined in the Fiduciary Rule. Alternatives include using a certified computer model (“408(g)”), a fee leveling arrangement (“408(g)”) under the Pension Protection Act or a non-conflicted business model.

These actions should be examined and those that are feasible should be adopted as soon as possible.

Test your knowledge of the June 9th rules… take the free test here!

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