NORTHERN TRUST

PLAN SPONSOR UPDATE

Current outlook – November 30, 2017

Tax Reform update

On November 28, 2017, the Senate Tax Reform proposal was approved by the Senate Budget Committee on a party line vote. On November 29, 2017, the full Senate approved a procedural motion allowing for consideration, debate and amendment of the bill. Passage, at this point, faces the challenges of approval by the full Senate and either (1) approval of the Senate bill by the House or (2) a conference on the House and Senate bills.

Thus far, it appears that with respect to retirement policy and retirement savings tax incentives, there is no change from the proposal approved by the Senate Finance Committee on November 16, 2017.

DOL delays full application of Best Interest Contract Exemption to July 1, 2019

On November 27, 2017, the Department of Labor released a final rule extending for 18 months, to July 1, 2019, the special transition period delaying full application of certain provisions of the Best Interest Contract Exemption and other Prohibited Transaction Exemptions that were part of its original 2016 Fiduciary Rule package.

Background

On April 7, 2017, DOL finalized a regulation delaying the applicability date of its 2016 Fiduciary Rule for 60 days, until June 9, 2017. At the same time, it delayed the “full application” of the requirements of the exemptions that were part of its regulation package (including, e.g., the Best Interest Contract exemption (BIC)) until January 1, 2018. Until that date, “fiduciaries relying on these exemptions for covered transactions [are required to] adhere only to the Impartial Conduct Standards (including the “best interest” standard), as conditions of the exemptions.”

Critically, the regulation delayed until January 1, 2018, the application of the BIC requirements of a written contract, (robust) fee and conflicts disclosure and adoption of conflict-mitigation pay policies.

November 2017

SUMMARY
In this Current outlook we briefly review the status of the Republicans’ Tax Reform proposal and then discuss the DOL’s finalization of an 18-month extension of its fiduciary rule transition relief.

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In August, 2017, DOL proposed extending this transition relief 18 months, until July 1, 2019.

Final rule

The final rule released November 27, 2017 adopts DOL's August, 2017, proposal without amendment. Thus, until July 1, 2019, fiduciaries will have to comply with the Impartial Conduct Standards under the BIC. These generally require "that Financial Institutions and Advisers must give prudent advice that is in retirement investors' best interest, charge no more than reasonable compensation, and avoid misleading statements." But, e.g., they will not have to comply with the more rigorous contract, disclosure and pay policy requirements of the BIC.

In addition, DOL is extending its "temporary enforcement relief" to July 1, 2019. During this period DOL "will not pursue claims against fiduciaries who are working diligently and in good faith to comply with the Fiduciary Rule and applicable provisions of the PTEs [Prohibited Transaction Exemptions], or treat those fiduciaries as being in violation of the Fiduciary Rule and PTEs."

While this DOL enforcement policy may provide some relief to fiduciaries, DOL noted that two enforcement mechanisms remain in place: "the imposition of excise taxes, and a statutorily-provided cause of action for advice to ERISA plan assets, including advice concerning rollovers of these assets."

DOL's discussion of its reasons for the delay

DOL gave three reasons for its further delay of full applicability of the BIC and other exemptions: (1) its ongoing review of the original rule ordered by President Trump and responses to its July 6, 2017, Request for Information; (2) its expectation that it will propose ("in the near future") a "new streamlined class exemption," presumably with respect to clean shares; and (3) the need to accommodate DOL's "desire to coordinate with the Securities and Exchange Commission and other regulators."

Significance of the interim standard for plan sponsors

One of the major sponsor-fiduciary burdens under the new fiduciary rule (and the related BIC) will be the duty to monitor the provider-fiduciary's compliance with the rule and the BIC. The more complicated those compliance requirements are, the more difficult the sponsor-fiduciary's burden.

While DOL's special transition period rules relax those compliance standards, in some respects the relaxation is with respect to the easiest things to monitor – objective contract and disclosure requirements. By contrast, the Impartial Conduct Standards that do apply during the transition period are somewhat vague. Sponsor-fiduciaries will want to consider, with their counsel, e.g., what sort of representations from provider-fiduciaries with respect to compliance with the Impartial Conduct Standards may be appropriate and whether any further review of compliance may be necessary.

We will continue to follow these issues.

Outlook

It appears that we will be seeing a new clean shares exemption proposal "in the near future" but that DOL's determination of the ultimate fate of the rule and related exemptions is going to take a while. In the interim, the Fifth Circuit is considering a legal (and Constitutional) challenge to the rule. There has not been, thus far, any attempt to include something about the rule in the current Republican Tax Reform proposal.