

Axing Commissions 'No Panacea' DOL FAQs Show

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Adopting fee-based account models will not necessarily ensure advisors' compliance with the Labor Department's fiduciary rule, and collecting even minimal 12b-1 fees will count as commissions, according to the regulator's newly issued responses to frequently asked questions about the new retirement advice standard.

The long-awaited [guidance document](#), released Thursday, contains no bombshells, says Joshua Waldbeser, an associate at Drinker Biddle.

"At a high level, there are no real surprises in the FAQs at all," Waldbeser says. "Certainly, there are no 'reversals' as to the exemptions' fundamental requirements."

But several of the FAQ clarify how the DOL expects advisors and broker-dealers to meet certain requirements, and emphasizes that the agency will be looking to ensure the spirit of the rule—protecting retirement savers and ensuring clearer disclosures around compensation—is being followed.

For instance, the DOL specifies that firms and advisors may need to invoke the rule's best interest contract, or BIC, exemption, even if they are compensated solely through level-fee arrangements.

"There is a clear and substantial conflict of interest when an advisor recommends that a participant roll retirement savings out of a plan into a fee-based account that will generate ongoing fees for the advisor that he would not otherwise receive, even if the fees going-forward do not vary with the assets recommended or invested," the FAQs read.

"Similarly ... investment advice to switch from a commission-based account to an account that charges a fixed percentage of assets under management on an ongoing basis could be a prohibited transaction."

The regulator noted that it recognizes that in some cases, investors could be at risk of so-called "reverse churning," or paying ongoing fees for advice on an account that is rarely rebalanced such that those fees add up to more than the sum of the commissions a client like that would otherwise be charged.

Another example would be first recommending a mutual fund with a front-end sales load but then soon thereafter recommending that the customer move the shares into an advisory account subject to asset-based fees, the regulator notes.

"The DOL made it very, very clear that changing to a level-fee platform is not a panacea because there could be some other issues that arise" says Marcia Wagner, head of the [Wagner Law Group](#).

Robo-advisors operating as "level-fee fiduciaries" and engaging in such rollover business could consequently qualify for relief under the BIC exemption, even though the full BIC exemption does not cover robo advice, the FAQs also say.

But robots that are fully computer-driven and offer no human advisor component are not fully covered under the Best Interest Contract Exemption. That decision is based on the DOL's view that "that the marketplace for robo-advice is still evolving in ways that appear to avoid conflicts of interest that would violate the prohibited transactions provisions and that minimize cost."

The FAQs also specify that collecting 12b-1 fees or revenue-sharing payments will count as commissions and therefore can be claimed only by invoking the BIC exemption.

"If the advisor or financial institution is going to recommend products that generate third-party payments [12b-1s or revenue-sharing compensation], they need to comply with the more stringent provisions of the full BIC exemption to safeguard the investor from biased advice," the DOL says.

"Basically, they're saying that if you even get 20 bps through a 12b-1 fee or other revenue-sharing payment, they consider that [a] transaction-based [fee] and therefore not level, and you have to rely on the provisions of the full BIC exemption," Wagner says.

The guidance does, however, note that distributors that offer breakpoint discounts on wrap fees to clients of a certain size can continue that practice, provided the initial fee schedule is "reasonably and prudently designed."

"If the financial institution has established a price or pricing schedule for services that satisfies the reasonable compensation standard, it is permissible for advisers to discount such prices for individual clients under the full BIC Exemption. Assuming that the discounts are not used in a manner that re-introduces conflicts of interest, neither the Rule nor the exemption prohibits such practices," the guidance reads.

The DOL plans to issue more FAQs "in the coming months," and in the meantime is encouraging firms and advisors to approach it with any queries.

"If you have questions about it, come and talk to us," said Phyllis C. Borzi, assistant secretary of labor for the Employee Benefits Security Administration, in a [blog post](#) announcing the new FAQs. "It's always better to get an answer straight from the source than to drive ahead with processes or practices that may run afoul of the law."