

THE
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The "Wholesaler" Exception: Interesting Angles on the DOL's Fiduciary Rule #72

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Advice to Advisors: The "Wholesaler" Exception

This is my 72nd article about interesting observations concerning the Department of Labor's (DOL) fiduciary rule and exemptions. These articles also cover the DOL's FAQs interpreting the regulation and exemptions and related developments in the securities laws.

In my [Angles post #70](#), I discussed three issues for recordkeepers related to the fiduciary rule and exemptions. [Angles #71](#) discussed the financial wellness programs developed by some recordkeepers. This article covers investment advice to advisors.

It is common knowledge that the recommendation of investments to a plan sponsor (that is, to a plan fiduciary such as a 401(k) committee) is fiduciary advice. However, it is less known that, under the new rules, investment recommendations made to fiduciary advisors is also considered fiduciary advice. And, since virtually every advisor to a plan, participant or IRA is now a fiduciary, that means that the presentation of sample investment line-ups to advisors can be fiduciary investment advice, resulting in a recordkeeper becoming a fiduciary. That is obviously problematic for the recordkeepers, but is also a problem for advisors and particularly for advisors who are not experienced in working with retirement plans.

Fortunately, though, there is at least a partial solution.

The fiduciary rules include an exception for fiduciary advice to "independent fiduciaries with financial expertise." Simply stated, an independent fiduciary with financial expertise (or IFFE) is a broker-dealer, RIA, bank or trust company, or insurance company that is willing to serve as a fiduciary and who will, in that capacity, oversee the advisor who is providing fiduciary advice to a plan. This is sometimes refer to as the "wholesaler's exception," and it covers recommendations made by both recordkeepers' wholesalers, and home office personnel.

Note that there is also an IFFE exception for advice to primary plan fiduciaries (e.g., plan committees) who oversee at least \$50,000,000 in assets. However, that is a subject of another article.

The wholesaler's exception permits recordkeepers to provide investment line-ups to fiduciary advisors, but not to plan sponsors. However, in a set of FAQs, the DOL noted that wholesaler recommendations could be made in the presence of a plan sponsor, so long as the fiduciary advisor was also at the meeting. So, the recordkeeper (and the wholesaler) can avoid fiduciary status by, for example, initially meeting with the advisor to discuss the investment line-up, and then making a presentation to the plan sponsor in the presence of the advisor (or, alternatively, having the advisor make the presentation, but with the wholesaler being able to provide comments and answer questions). It's important to know, though, that it must be clear that the recommendations are being vetted by the fiduciary advisor so that, in a sense, the recommendations are technically fiduciary advice by the advisor and not by the recordkeeper/wholesaler. As a result, advisors should make sure that they approve of the recommendations either before they are presented or at the meeting.

In my experience, broker-dealers, RIAs, and banks and trust companies will ordinarily serve as fiduciaries for the advice given by their representatives and employees. As a result, recordkeepers and wholesalers will be able to provide investment advice to these representatives without becoming fiduciaries. However, insurance companies

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are generally not willing to serve as co-fiduciaries with their insurance agents, and that is particularly true of independent insurance agents and brokers. However, if the insurance agents are also registered representatives of a broker-dealer, that does not present a problem, since the broker-dealer can, from a fiduciary perspective, oversee advice about insurance products; as a result, the agents will have a financial institution to qualify as the IFFE.

As described above, where an insurance agent is only licensed to sell insurance, there will not usually be a financial institution that will serve as the IFFE. That presents a significant problem for the distribution of insurance products to plans, participants, and IRAs through independent insurance agents and brokers. While group annuity contracts can be recommended under Prohibited Transaction Exemption 84-24, and the agent or broker can receive a commission, a wholesaler cannot provide the independent agent or broker with a recommended line-up — without the wholesaler and the recordkeeper becoming fiduciaries.

If properly done, a possible solution would be for the independent insurance agent or broker to not make any recommendations about investments, but instead for the plan sponsor to utilize the services of a fiduciary on the platform, for example, a 3(21) or 3(38) platform fiduciary.

The IFFE exception will likely be embraced by the recordkeeper community. As a result, the common approach will be to provide investment line-ups to fiduciary advisors who are supervised by IFFEs. That does present an issue, though, for recordkeepers who sell directly to plan sponsors without the use of an advisor. My next article will discuss the RFP/RFI approach that can be used for that purpose.

The views expressed in this article are the views of Fred Reish, and do not necessarily reflect the views of Drinker Biddle & Reath.

Part 1- [Interesting Angles on DOL's Fiduciary Rule #1](#)

Part 2 - [Best Interest Standard of Care: Interesting Angles on the DOL's Fiduciary Rule #2](#)

Part 3 - [Hidden Preamble Observations: Interesting Angles on the DOL's Fiduciary Rule #3](#)

Part 4 - [TV Stock Tips and Fiduciary Advice: Interesting Angles on DOL's Fiduciary #4](#)

Part 5 - [Level Fee Fiduciary Exemption: Interesting Angles on DOL's Fiduciary Rule #5](#)

Part 6 - [Fiduciary Regulation And The Exemptions: Interesting Angles on the DOL's Fiduciary Rule #6](#)

Part 7 - [Fiduciary Regulations And The Exemptions : Interesting Angles on the DOL's Fiduciary Rule #7](#)

Part 8 - [Designated Investment Alternatives: Interesting Angles on the DOL's Fiduciary Rule #8](#)

Part 9 - [Best Interest Standard and the Prudent Man Rule: Interesting Angles on the DOL's Fiduciary Rule #9](#)

Part 10 - [FINRA Regulatory Notice: Interesting Angles on the DOL's Fiduciary Rule #10](#)

Part 11- [ERISA and the Internal Revenue Code: Interesting Angles on the DOL's Fiduciary Rule #11](#)

Part 12- [Potential Prohibited Transactions: Interesting Angles on the DOL's Fiduciary Rule #12](#)

Part 13- [Investment Policies: Interesting Angles on the DOL's Fiduciary Rule #13](#)

Part 14- [Investment Suggestions: Interesting Angles on the DOL's Fiduciary Rule #14](#)

Part 15- [Best Interest Contract Exemption: Interesting Angles on the DOL's Fiduciary Rule #15](#)

Part 16 - [Adviser Recommendations: Interesting Angles on DOL's Fiduciary Rule #16](#)

Part 17 - [Level Fee Fiduciary: Interesting Angles on DOL's Fiduciary Rule #17](#)

Part 18- [Best Interest Contract Exemption and IRA Advisor Compensation: Interesting Angles on the DOL's Fiduciary Rule #18](#)

Part 19- [Interesting Angles on the DOL's Fiduciary Rule #19: Advisors' Use of "Hire Me" Practices.](#)

Part 20- [Three Parts of "Best Interest Standard of Care": Interesting Angles on the DOL's Fiduciary Rule #20](#)

Part 21- [Retirement Plan Documentation and Prudent Recommendation: Interesting Angles on the DOL's Fiduciary Rule #21](#)

Part 22-[Banks and Prohibited Transactions: Interesting Angles on the DOL's Fiduciary Rule #22](#)

Part 23-[Prohibited Transactions: IRA and RIA Qualified Money: Interesting Angles on the DOL's Fiduciary Rule #23](#)

Part 24 - [Differential Compensation Based on Neutral Factors: Interesting Angles on DOL's Fiduciary Rule #24](#)

Part 25-[Reasonable Compensation Versus Neutral Factors: Interesting Angles on the DOL's Fiduciary Rule #25](#)

Part 26- [Interesting Angles on the DOL's Fiduciary Rule #26- Reasonable Compensation for IRAs: When and How Long?](#)

Part 27 - [Definition of Compensation: Interesting Angles on DOL's Fiduciary Rule #27](#)

Part 28 - [What About Rollovers that Aren't Recommended?: Interesting Angles on the DOL's Fiduciary Rule #28](#)

Part 29- [Capturing Rollovers: What Information is Needed?: Interesting Angles on the DOL's Fiduciary Rule #29](#)

Part 30- [Three Kinds of Level Fee Fiduciaries . . . and What's A "Level Fee?": Interesting Angles on the DOL's Fiduciary Rule #30](#)

Part 31 - ["Un-levelizing" Level Fee Fiduciaries: Interesting Angles on the DOL's Fiduciary Rule #31](#)

Part 32 - [What "Level Fee Fiduciary" Means for Rollover Advice: Interesting Angles on the DOL's Fiduciary Rule #32](#)

Part 33- [Discretionary Management, Rollovers and BICE: Interesting Angles on the DOL's Fiduciary Rule #33](#)

Part 34- [Seminar Can Be Fiduciary Act: Interesting Angles on DOL's Fiduciary Rule #34](#)

Part 35- [Presidential Memorandum on Fiduciary Rule: Interesting Angles on the DOL's Fiduciary Rule #35](#)

Part 36 -[Retirement Advice and the SEC: Interesting Angles on the DOL's Fiduciary Rule #36](#)

Part 37 - [SEC Retirement-Targeted Examinations: Interesting Angles on the DOL's Fiduciary Rule #37](#)

Part 38- [SEC Examinations of RIAs and Broker-Dealers under the ReTIRE Initiative: Interesting Angles on the DOL's Fiduciary Rule #38](#)

Part 39- [FINRA Regulatory Notice 13-45: Guidance on Distributions and Rollovers: Interesting Angles on the DOL's Fiduciary Rule #39](#)

Part 40 - [New Rule, Old Rule - What Should Advisers Do Now?: Interesting Angles on the DOL's Fiduciary Rule #40](#)

Part 41 - [While We Wait: The Current Fiduciary Rule and Annuities: Interesting Angles on DOL's Fiduciary Rule #41](#)

Part 42 - [Rollovers under DOL's Final Rule: Interesting Angles on DOL's Fiduciary Rule #42](#)

Part 43 - [BICE Transition: More Than the Eye Can See - Interesting Angles on DOL's Fiduciary Rule #43](#)

Part 44 - [Basic Structure of Fiduciary Package \(June 9\): Interesting Angles on DOL's Fiduciary Rule #44](#)

Part 45 - [DOL Fiduciary "Package": Basics on the Prohibited Transaction Exemptions: Interesting Angles on the DOL's Fiduciary Rule #45](#)

Part 46 - [How Does an Adviser Know How to Satisfy the Best Interest Standard?: Interesting Angles on the DOL's Fiduciary Rule #46](#)

Part 47- ["Real" Requirements of Fiduciary Rule: Interesting Angles on DOL's Fiduciary Rule #47](#)

Part 48- [The Last Word: The Fiduciary Rule Applies on June 9- Interesting Angles on the DOL's Fiduciary Rule #48](#)

Part 49- [The Requirement to Disclose Fiduciary Status: Interesting Angles on the DOL's Fiduciary Rule #49](#)

Part 50- [Fourth Impartial Conduct Standard: Interesting Angles on DOL's Fiduciary Rule #50](#)

Part 51- [Recommendations to Transfer IRAs: Interesting Angles on the DOL's Fiduciary Rule #51](#)

Part 52 - [The Fiduciary Rule and Exemptions: How Long Will Our Transition Be?: Interesting Angles on the DOL's Fiduciary Rule #52](#)

- Part 53 - [Fiduciary Rule and Discretionary Investment Management: Interesting Angles on DOL's Fiduciary Rule #53](#)
- Part 54 - [The DOL's RFI and Possible changes to BICE: Interesting Angles on the DOL's Fiduciary Rule #54](#)
- Part 55- [DOL's RFI and Recommendation of Annuities- Interesting Angles on DOL's Fiduciary Rule #55](#)
- Part 56-[Recommendations of Contributions as Fiduciary Advice: Interesting Angles on the DOL's Fiduciary Rule #56](#)
- Part 57- [Relief from 408\(b\)\(2\) Requirement on Change Notice: Interesting Angles on the DOL's Fiduciary Rule #57](#)
- Part 58- [Recommendations to Contribute to a Plan or IRA- Interesting Angles on the DOL's Fiduciary Rule #58](#)
- Part 59- [What Plans and Arrangements Are Covered by the Fiduciary Rule: Interesting Angles on the DOL's Fiduciary Rule #59](#)
- Part 60- [What the Tibble Decision Means to Advisers: Interesting Angles on the DOL's Fiduciary Rule #60](#)
- Part 61- [The Fiduciary Rule, Distributions and Rollovers: Interesting Angles on the DOL's Fiduciary Rule #61](#)
- Part 62 - [Is It Possible To Be An Advisor Without Being A Fiduciary? - Interesting Angles on the DOL's Fiduciary Rule #62](#)
- Part 63-[Policies and Procedures: The Fourth BICE Requirement - Interesting Angles on the DOL's Fiduciary Rule #63](#)
- Part 64 -[What Does the Best Interest Standard of Care Require?-Interesting Angles on the DOL's Fiduciary Rule #64](#)
- Part 65- [Unexpected Consequences of Fiduciary Rule - Interesting Angles on the DOL's Fiduciary Rule #65](#)
- Part 66- [Concerns About 408\(b\)\(2\) Disclosures: Interesting Angles on the DOL's Fiduciary Rule #66](#)
- Part 67- [From the DOL to the SEC - Interesting Angles on the DOL's Fiduciary Rule #67](#)
- Part 68-[Recommendations of Distributions - Interesting Angles on the DOL's Fiduciary Rule #68](#)
- Part 69- [Compensation Risks for Broker-Dealers and RIAs: Interesting Angles on the DOL's Fiduciary Rule #69](#)
- Part 70-[The Fiduciary Rule and Recordkeeper Services: Interesting Angles on the DOL's Fiduciary Rule #70](#)
- Part 71- [Recordkeepers and Financial Wellness Programs: Interesting Angles on the DOL's Fiduciary Rule #71](#)
- Part 73- [Recordkeeper Investment Support for Plan Sponsors: Interesting Angles on the DOL's Fiduciary Rule #73](#)
- Part 74 -[One More Fiduciary Issue for Recordkeepers: Interesting Angles on the DOL's Fiduciary Rule #74](#)
- Part 75 - [The Fiduciary Rule: Mistaken Beliefs-Interesting Angles on the DOL's Fiduciary Rule #75](#)
- Part 76 - [Discretionary Management of IRAs: Prohibited Transaction Issues for RIAs- Interesting Angles on the DOL's Fiduciary Rule #76](#)
- Part 77 - [The Fiduciary Rule: Mistaken Beliefs \(#2\): Interesting Angles on the DOL's Fiduciary Rule #77](#)
- Part 78 - [The Fiduciary Rule: Mistaken Beliefs \(#3\): Interesting Angles on the DOL's Fiduciary Rule #78](#)
- Part 79 - [The Fiduciary Rule: Mistaken Beliefs \(#4\)- Interesting Angles on the DOL's Fiduciary Rule #79](#)
- Part 80 - [Enforceable During Transition?: Interesting Angles on the DOL's Fiduciary Rule #80](#)
- Part 81 - [The Fiduciary Rule Prohibits Commissions... or Not \(Myth #6\): Interesting Angles on the DOL's Fiduciary Rule #81](#)
- Part 82 - [Undisclosed \(and Disclosed\) 12b-1 Fees: The Different Views of the SEC and DOL - Interesting Angles on the DOL's Fiduciary Rule #82](#)
- Part 83 - [Part 2 of Undisclosed \(and Disclosed\) 12b-1 Fees: Interesting Angles on the DOL's Fiduciary Rule #83](#)

Part 84- [What Does the 5th Circuit Decision Mean for Rollover Recommendations?: Interesting Angles on the DOL's Fiduciary Rule #84](#)

Part 85 - [The Fiduciary Rule: What's Next \(Part 1\)? : Interesting Angles on the DOL's Fiduciary Rule #85](#)

Part 86- [The Fiduciary Rule: What's Next \(Part 2\)?: Interesting Angles on the DOL's Fiduciary Rule #86](#)

Part 87 - [The Fiduciary Rule: What's Next \(Part 3\)?: Interesting Angles on the DOL's Fiduciary Rule #87](#)

Part 88 - [The Fiduciary Rule: What's Next \(Part 4\)? : Interesting Angles on the DOL's Fiduciary Rule #88](#)

Part 89 - [The 5th Circuit Decision, Prohibited Transactions, and New Non-Enforcement Policies: Interesting Angles on the DOL's Fiduciary Rule #89](#)

Part 90 - [Parallels Between the SEC Regulation Best Interest and the DOL Best Interest Contract Exemption \(Part 1\): Interesting Angles on the DOL's Fiduciary Rule #90](#)

Part 91- [Parallels Between the SEC Regulation Best Interest and the DOL Best Interest Contract Exemption \(Part 2\): Interesting Angles on the DOL's Fiduciary Rule #91](#)

Part 92 - [SEC Proposed Reg BI and Recommendations of Rollovers \(Part 1\): Interesting Angles on the DOL's Fiduciary Rule #92](#)

Part 93 - [SEC Proposed Reg BI and Recommendations of Rollovers \(Part 2\): Interesting Angles on the DOL's Fiduciary Rule #93](#)

Part 94 - [SEC Proposed Reg BI and Recommendations of Rollovers \(Part 3\) : Interesting Angles on the DOL's Fiduciary Rule #94](#)

Part 95 - [Regulation Best Interest Recommendations by Broker-Dealers: Part 1- Interesting Angles on the DOL's Fiduciary Rule #95](#)

Part 96 - [Regulation Best Interest Recommendations by Broker-Dealers: Part 2- Interesting Angles on the DOL's Fiduciary Rule #96](#)

Part 97 - [Regulation Best Interest Recommendations by Broker-Dealers: Part 3 - Interesting Angles on the DOL's Fiduciary Rule #97](#)

Part 98 - [Regulation Best Interest: Consideration of Cost and Compensation- Interesting Angles on the DOL's Fiduciary Rule #98](#)

Part 99 - [Investment Advisers and the SEC's Interpretation of Their Duties: Interesting Angles on the DOL's Fiduciary Rule #99](#)

Part 100 - [Investment Advisers and the SEC's Interpretation of Their Duties: Part II- Interesting Angles on the DOL's Fiduciary Rule #100](#)

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