

# THE NATIONAL LAW REVIEW

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## The Fiduciary Rule: Mistaken Beliefs (#2): Interesting Angles on the DOL's Fiduciary Rule #77

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This is 77<sup>th</sup> 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.

The DOL's fiduciary regulation and the transition Best Interest Contract Exemption (BICE) first applied on June 9, 2017. In other words, the recommendations made by broker-dealers and RIAs, and their representatives, have been governed by those rules for more than six months. While the requirements of the fiduciary standard of care and transition BICE are fairly straightforward—at least for advisors who understand the fiduciary concept, I am hearing about misunderstandings of those requirements. [Angles #76](#) was my first post about mistaken beliefs; this article continues that theme by examining whether the best interest standard mandates the selection of the “best investment.”

To focus on BICE, when an advisor gives conflicted advice to IRAs, plans or participants, the advisor must adhere to the Impartial Conduct Standards. In that case the advisor must:

- Adhere to the best interest standard of care.
- Receive no more than reasonable compensation.
- Make no materially misleading statements.

The best interest standard of care is, in its essence, a combination of ERISA's prudent man rule and duty of loyalty. More literally, BICE defines the best interest standard as:

*Investment advice is in the “Best Interest” of the Retirement Investor when the Adviser and Financial Institution providing the advice act **with the care, skill, prudence, and diligence** under the circumstances then prevailing **that a prudent** person acting in a like capacity and **familiar with such matters would use** in the conduct of an enterprise of a like character and with like aims, based on the investment objectives, risk tolerance, financial circumstances, and needs of the Retirement Investor, without regard to the financial or other interests of the Adviser, Financial Institution or any Affiliate, Related Entity, or other party. (Emphasis added by me.)*

While the full meaning of that language may not be obvious on its face, there is a substantial amount of guidance, through court cases and DOL opinions, about its meaning. It means, first and foremost, that an advisor must engage in a prudent process to develop a recommendation. And, the process must be done carefully and skillfully at the level of a person who is knowledgeable about the particular issues (for example, asset allocation, selection of investments, insurance products, etc.).

However, some people are saying that the best interest standard means that an advisor must recommend the best possible investment. That is incorrect. In fact, the DOL has specifically stated that, even if it were possible to select the best possible investment, that is not the requirement.

Instead, the requirement is that advisors act prudently when selecting investments . . . and prudence is defined by the quality of the process used by the advisor. So, for example, where an advisor uses reputable software to evaluate the investments and to develop an appropriate asset allocation, the use of that software would be part



Article By [Drinker Biddle & Reath LLP](#)  
[Fred ReishFredReish.com](#)

[Financial Institutions & Banking](#)  
[Labor & Employment](#)  
[All Federal](#)

of a prudent process and would document that the advisor was complying with the rules.

Perhaps people are confusing the best interest standard with “best practice.” But, those are different things.

Having said that, there is certainly nothing wrong with an advisor doing more than is legally needed in an effort to prudently select investments.

The best interest standard—while more demanding than the suitability standard—is not as burdensome or difficult as some people believe. Instead, it requires a thoughtful and diligent process implemented by a knowledgeable advisor. Since these rules are designed to protect retirement money, that doesn’t seem like an unreasonable standard.

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

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