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“Am I a fiduciary?” Know how the DOL would answer that

This past weekend I did what parents often do with their children at the beginning of summer: I took my kids to the pool. As I prepared to enter the pool on that tepid 70 degree day, I anticipated the discomfort of the cold water and thought about ways of coping with the inescapable reality. I could leap headfirst. Or, I could work my way in, submerge myself, and swim around to warm up. Or, I could stay in the shallow end for as long as possible, hoping never to venture deeper.

This situation reminded me of the new **DOL Fiduciary Rule**. Yes, bear with me.

The first phase of the fiduciary rule went into effect this past Friday at midnight. And while the fiduciary rule is by no means a ‘day at the pool,' one can see behavioral parallels in terms of adapting to a chilly reality. Do you leap, wade-swim, or hug the shallow end? Before I address that, let me answer the question some of you may be wondering which is "Am I in the pool? **Am *I* a fiduciary?**"

If you are asking that question, then the answer is almost certainly **"Yes, you are a fiduciary."** The DOL rule has intentionally made it very easy for you to be considered a fiduciary. If you are in the business of advising clients who have IRAs, 401(k) or pension assets, then you are a probably a fiduciary. If you engage with those clients in a way that your actions expand beyond the very narrow parameters of investment education or sales and marketing, then your actions constitute recommendations and advice. And, if you or your firm gets paid somehow or someway by that client, then you are a fiduciary.

If you're thinking, "Yeah, but I thought ERISA also required that I provide advice on a regular basis to the client, and that my advice is tailored to the client, and that I have a written agreement with the client, and that my advice is the primary basis of the client's investment decisions," well, that too has changed. All it takes to become a fiduciary now is to give advice once, to an individual who holds ERISA qualified assets, even if that individual has no prior relationship with you, written or otherwise, and that person (whether relying on your advice or not) pays you or your firm for advice or uses one of your financial products. **Welcome to the pool! So, what now?**

Starting at 11:59pm on June 9, 2017, at a minimum every advisor is subject to the DOL's new "impartial conduct standards" which means you must:

1. Act with prudence, diligence, and care;
2. Act with loyalty (mitigate conflicts);
3. Do not say anything that is materially misleading (e.g., failing to fully disclose your conflicts); and
4. Ensure that your compensation is "reasonable."

The challenge facing all firms and advisors is not only to *act* consistently with these standards but also to *demonstrate* that you and your firm have acted consistently with these standards. Demonstrating means being able to explain your rationale for using a particular asset allocation or a particular product for your client; it means being able to show that a financial incentive (e.g., commission) did not skew the advice you gave to a client; it means being able to show that you told your client about relationships you have with affiliates or reasons why you believe proprietary products are in client's best interest; and it means being able to defend the "value" of your services relative to the client's achievement of their financial goals and relative to competitor's products in the market.

Proving the negative is hard and fraught with challenges. That's why some firms are moving to fee-based relationships and why other firms are adopting T-shares (to neutralize commission differences across products).

So, what now?

- We urge advisors to contact their home office for guidance, where applicable.
- We believe that advisors should wade deeper into the pool and not delay implementation of changes in their business that will help them create capacity and manage risk. The imperative to achieve these results is heightened now that the first part of the rule is applicable. And, our view is that whatever further changes the DOL, the SEC or others plan to make, the features of prudence, loyalty, fees, and disclosure will persist—and you will have to demonstrate that you met those standards.
- We believe that regardless of the fiduciary rule, advisors will be at a competitive advantage in the face of major industry-wide challenges like demographic change, technology development and margin compression if they adopt fiduciary business models that are prudent and in the clients' best interest.
- Russell Investments has been a partner in meeting the fiduciary challenge for over 40 years and has nearly 20 years of experience in helping advisors implement fiduciary solutions. Regardless of the fate of the DOL fiduciary rule, we are committed to assisting advisors in addressing not only the threat of regulatory risk, but also the opportunity for competitive differentiation.

The bottom line

The financial service industry is arguably facing one of the most disruptive periods in its history: new regulations, demographic shifts, technology integration and margin compression to name but a few. Taken together, the bar for being a top-performing advisor is being raised. These competitive pressures require potentially fundamental changes to your advisory business.

Helping advisors transform their business—whether for regulatory or competitive reasons—is not new to Russell Investments. It is our heritage. Whether you need a little education or a lot of re-engineering, we're committed to helping you brave the new post-DOL world with confidence.

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