



The Best Interest Contract Exemption

THE ISSUE: The proposed new definition of investment advice fiduciary offered by the Department of Labor (DOL) contains the “best interest contract” (BIC) prohibited transaction exemption (PTE), which will allow otherwise so-called “conflicted compensation” to be paid if the terms of the BIC exemption are met. The BIC exemption, while intended as a way to allow continuation of the broker-dealer/registered representative model for providing investment advice, imposes such burdensome terms that it is unworkable in the real world of middle and lower income retirement investors.

EXPLANATION: The BIC exemption requires an extensive contract between the retirement investor and the advisor and between the retirement investor and the financial institutions that offer the investment choices that the advisor and the investor are discussing. The contract must contain many specific terms, including:

- Acknowledgement of the advisor’s and the financial institution’s fiduciary duty to the investor
- Disclosure of compensation and other fee information
- A warranty that neither the advisor nor the financial institution will make any misleading statements about information pertinent to a transaction (including on such issues as fees, assets and conflicts of interest)
- A list of the steps the advisor/financial institution will take to mitigate potential conflicts of interest

Further, to qualify under the BIC exemption and thus allow compensation—commissions, trailing commissions, 12b-1 fees, etc.—that would otherwise be considered “conflicted” and therefore prohibited under ERISA, the financial institution must provide quarterly and annual updates—to investors and on a public website—showing annual, five-year and 10-year performance projections, fees, expenses, and other relevant information on every product the advisor can offer to the investor through that financial institution.

The contract must be signed by the retirement investor, the financial advisor, and each financial institution whose products the investor and advisor are discussing prior to any mention of any specific product. Thus, the contract must be executed even before the investor has decided whether to work with the advisor, or before any particular product recommendation is made.

THE PROBLEM: The requirements of the BIC are burdensome, expensive and well beyond what is necessary to make clear that an advisor puts the best interest of the retirement investor above his/her own interests. The BIC PTE’s cost in time and money will make it difficult, and often impossible, for advisors—who themselves are most often hard-working middle class professionals—to work those with modest amounts of retirement funds to invest. This is exactly the opposite result intended by the proposed rule.

THE SOLUTION: The BIC PTE, while meant to give middle and lower income savers access to affordable professional investment advice, is unworkable due to its burdensome, expensive requirements. It must be substantially simplified so that professional advisors can afford to work with retirement investors who have only modest amounts of retirement savings to invest.

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