Between the Lines
A Review of Q and A Releases on Rollovers

April 14, 2021

Introduction

On April 13, 2021, the Department of Labor ("DoL") released two Question and Answer documents ("QandA") to amplify the regulation on rollovers that took effect on February 16, 2021[1] ("February 16 Regulation") and will be enforced beginning December 20, 2021.

The QandAs are:

- Industry Guidance, entitled "*New Fiduciary Advice Exemption: PTE 2020-02 Improving Investment Advice for Workers & Retirees Frequently Asked Questions"*
- Investor Guidance, entitled "*Choosing the Right Person to Give You Investment Advice: Information for Investors in Retirement Plans and Individual Retirement Accounts*"

The QandAs reinforce the February 16 Regulations and closes a number of avenues of interpretation that exist in that regulation.

At the core of the February 16 Regulations is the ERISA compensation prohibition that "*parties providing fiduciary investment advice to plan sponsors, plan participants, and IRA owners may not receive payments creating conflicts of interest, unless they comply with protective conditions in a prohibited transaction exemption*". The February 16 Regulation includes a prohibited transaction exemption ("PTE 2020-02") that permits payments, including commissions, 12b-1 fees, revenue sharing, and mark-ups and mark-downs in certain principal transactions to be received under certain conditions.

> *The preamble to the new exemption [PTE 2020-02] makes clear that the 1975 fiduciary regulation can extend to advice to roll assets out of a plan to an IRA and the exemption provides relief for prohibited transactions resulting from such advice.*
>
> *An important aim of the exemption is to make sure that fiduciary advice providers adhere to stringent standards designed to ensure that their investment recommendations reflect the best interest of plan and IRA investors. In addition to other requirements, financial institutions and investment professionals relying on the exemption must:*
>
> - *acknowledge their fiduciary status in writing,*
> - *disclose their services and material conflicts of interest,*
> - *adhere to Impartial Conduct Standards…*
> - adopt policies and procedures prudently designed to ensure compliance with the Impartial Conduct Standards and to mitigate conflicts of interest that could otherwise cause violations of those standards,
> - document and disclose the specific reasons that any rollover recommendations are in the retirement investor's best interest; and

[1] Improving Investment Advice for Workers and Retirees Prohibited Transaction Exemption 2020

- conduct an annual retrospective compliance review.

Three Options Remain

The February 16 Regulation permitted three options for conducting rollover business which are unaffected by the QandAs. These options are:

- Educate but give no advice. This is a non-fiduciary choice but permits referring a client to a fiduciary for rollover advice. Advisor can be compensated for the education provided (97-1).
- Pure Robo Advice. Advice is derived exclusively from an eligible computer model, with no intervention from an individual (408(g)).
- Fiduciary Advisor. This arrangement relies on PTE 2020-02 and permits fiduciaries to be compensated.

No Guidance on How to Determine Best Interest

The QandAs make repeated references to an "investor's best interest", but is silent on how advice providers are expected to determine what the best interests are for a particular investor. Unless it is assumed that all investor's interests are identical (a ridiculous notion), a determination of best interest is required.

In the absence of specific guidance, it is left to the best efforts of the advice provider to make the critical determination of what constitutes the best interest of each investor.

Final Regulations

While regulators always have the power to introduce new or amend existing regulations, in this case the DoL has expressed the intent to do so. The QandAs explain:

> *The Department anticipates taking further regulatory and sub-regulatory actions, as appropriate, including amending the investment advice fiduciary regulation, amending PTE 2020-02, and amending or revoking some of the other existing class exemptions available to investment advice fiduciaries*.

Prohibition Applies Before, During and After Rollover

The QandAs emphasize that rollover advice is prohibited if there is compensation from a pre-existing relationship or is expected from a future relationship unless there is compliance with the exemption PTE 2020-02.

> *… advice to roll over plan assets can also occur as part of an ongoing relationship or as the beginning of an intended future ongoing relationship that an individual has with an investment advice provider*.

Disclosure Is No Protection

Unlike other regulations that offer relief when proper disclosures are made, PTE 2020-02 permits no such escape.

> *Written statements disclaiming a "mutual" understanding or forbidding reliance on the advice as "a primary basis for investment decisions" may be considered in determining whether a mutual understanding exists, but such statements will not be determinative. Boilerplate disclaimers are insufficient to defeat the test, when the parties have a mutual understanding that the adviser is making an individualized recommendation upon which the investor can be expected to rely in making the investment decision. When firms and investment professionals hold themselves out in their oral communications, marketing materials, or interactions with retirement investors as making individualized recommendations that the investor can rely upon to make an investment decision that is in the best interest of the investor, and the investor, accordingly, relies upon the recommendation to make an investment decision, the 1975 test's requirement for a "mutual agreement, arrangement, or understanding" is satisfied. In applying the 1975 test, the Department intends to consider the reasonable understandings of the parties based on the totality of the circumstances. Firms and investment professionals cannot use written disclaimers to undermine reasonable investor understandings. Similarly, written statements disclaiming other parts of the 1975 test will not be determinative of fiduciary status.*

Suggested Fiduciary Disclosure

The QandAs include a sample fiduciary disclosure that meets the requirement of clarity to the financial institution and investment professional, as well as the retirement investor, at the time of the recommended investment transaction.

> "*When we provide investment advice to you regarding your retirement plan account or individual retirement account, we are fiduciaries within the meaning of Title I of the Employee Retirement Income Security Act and/or the Internal Revenue Code, as applicable, which are laws governing retirement accounts. The way we make money creates some conflicts with your interests, so we operate under a special rule that requires us to act in your best interest and not put our interest ahead of yours.*
>
> *Under this special rule's provisions, we must:*
>
> - *Meet a professional standard of care when making investment recommendations (give prudent advice);*
> - *Never put our financial interests ahead of yours when making recommendations (give loyal advice);*
> - *Avoid misleading statements about conflicts of interest, fees, and investments;*
> - *Follow policies and procedures designed to ensure that we give advice that is in your best interest;*
> - *Charge no more than is reasonable for our services; and*
> - *Give you basic information about conflicts of interest."*

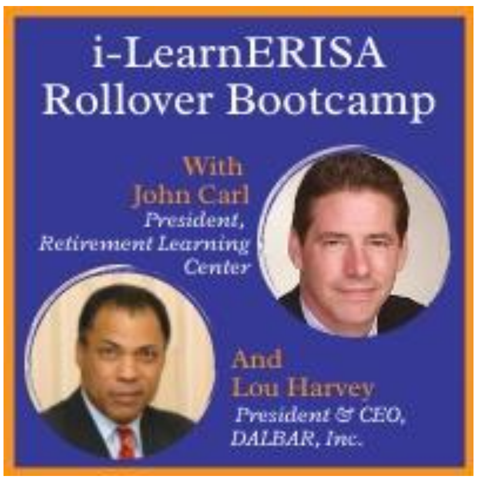
i-LearnERISA Rollover Bootcamp Complimentary Webinar

Thursday, May 6, 2021
1:00 PM – 2:00 PM EDT

Demystifying the DOLs Latest Q&A Release

John Carl and Lou Harvey will provide an overview of the Department of Labor's new regulation regarding rollover recommendations (PTE-2020-02). The session will focus on the DOL's recently published Q&A and provide answers to the questions your clients will soon be asking.

The session will answer vital question, such as:



- *When does discussing rollovers make me a fiduciary?*
- *What does a best interest rollover recommendation look like?*
- *What new compliance requirements can advisors expect?*
- *What options do financial professional have?*
- *What additional regulations concerning rollovers are on the horizon?*
- *How do I become a winner in this new rollover landscape?*

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