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It's Past February 1, 2022: The DOL's PTE 2020-02 Is Now Enforceable

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I. INTRODUCTION

For the past decade, federal governmental regulators have been concerned over the significant growth in the Individual Retirement Accounts (and Annuities) (IRA) rollover market, as it is more loosely regulated as compared to the 401(k) plan market. By the end of the third quarter of 2021, there were $13.2 trillion of assets in IRAs, as compared to $7.3 trillion of assets in 401(k) plans.[1] The Employee Benefits Retirement Income Security Act (ERISA) is the federal law that regulates employer-provided retirement plans and IRAs. As a result of this growth, the following issues surfaced — both from a federal securities law and an ERISA law perspective — what are the applicable fiduciary standards and disclosure requirements that should accompany a financial adviser's recommendation to roll monies out of a 401(k) plan and into an IRA rollover, coined by practitioners as ''capturing the IRA rollover.''[2] Releases from the U.S. Government Accountability Office (GAO), the Financial Industry Regulatory Authority (FINRA), U.S. Department of Labor (DOL), and Securities and Exchange Commission (SEC) have indicated that both the DOL and the SEC have concerns about the IRA rollover market.[3] Early on, the DOL attempted to subject broker-dealers to a higher fiduciary standard under ERISA, than under federal securities law. The DOL attempted to do so through the issuance of fiduciary regulations and related prohibited transaction exemptions (PTEs) under ERISA. Those regulations and related exemptions were struck down by the Fifth Circuit Court of Appeals in 2018 on the grounds that the DOL had exceeded its regulatory powers.[4] By 2019, the SEC issued its Regulation Best Interest (Reg BI), designed to set forth a new standard of care for broker-dealers who were providing investment advice, including rollover recommendations.[5] That regulation set forth a best interest standard of care, as well mandating certain disclosures of fees and conflicts of interest. After the SEC's issuance of Reg. BI, the DOL publicly stated that any new rulemaking from it would dovetail with the SEC's advice.[6] The DOL hopes that it has succeeded with the release of its new interpretation of an investment advice fiduciary and with the issuance of a new PTE, known as PTE 2020-02.[7] This paper provides a historical background to the DOL's attempt to regulate broker-dealers; it analyzes the conditions of PTE 2020-02 and the DOL's new interpretation of its 1975 regulation defining who is an investment advice fiduciary under ERISA; and it outlines some of the most common problems that will arise in complying with PTE 2020-02.

Part II of the article provides some background regarding ERISA's Title I and II statutory rules on investment advice fiduciaries and the related prohibited transactions, for those unfamiliar with ERISA. It describes the DOL's initial regulations, set forth in 1975, as to who is an investment advice fiduciary. Part III explains why various government regulators began to be concerned, during the 1990s, over the exponential growth of the IRA rollover market and applicable standards of care and disclosure rules that advisers should be subject to when recommending a rollover to a plan participant or beneficiary. It also discusses the DOL's investment advice fiduciary rules and its new PTEs that it set forth during 2010 and 2016. In 2018, the Fifth Circuit vacated the 2016 fiduciary rules, sending the DOL back to the drawing board. Part IV focuses on the DOL's current 2020 fiduciary rules, including the new PTE 2020-02, effective February 1, 2022. The terms and conditions of that exemption are discussed in-depth, including common pitfalls that can occur when attempting to comply with the exemption. Part V ends the article with the author's conclusion as to how investment advisers should proceed in light of the current guidance.

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[1] *See* Ted Godbout, *United States Retirement Assets Held Steady in Third Quarter*, NAPA (Dec. 29, 2021).

[2] *See* Fred Reish, Bruce Ashton, Joan Neri, and Joshua Waldbeser, *Capturing Plan Rollovers,* Plan Consultant (Spring 2014).

[3] Broker-dealers that interact with the public generally must become members of FINRA.

[4] *Chamber of Commerce v. DOL*, 885 F.3d 360 (5th Cir. 2018).

[5] SEC, Final Rule, Release No. 34-86031, File No. S7-07-18, Regulation Best Interest: The Broker-Dealer Standard of Conduct, RIN 3235-AM35, 84 Fed. Reg. 33,318 (July 12, 2019). The intent of Reg BI was not to impose the SEC's interpretation of the fiduciary duties applicable to investment advisers covered under the Adviser's Act; instead, it was limited to the applicable fiduciary standard for broker-dealers.

[6] *See* News Release, U.S. Department of Labor Announces Exemption To Improve Investment Advice and Enhance Financial Choices For Workers And Retirees (Dec. 15, 2020).

[7] 85 Fed. Reg. 82,798 (Dec. 18, 2020).

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II. BACKGROUND ANALYSIS OF TITLE I'S AND II'S FIDUCIARY AND PROHIBITED TRANSACTION RULES

A. Limitations of Title I and II of ERISA

Congress enacted ERISA[8] to regulate employer-sponsored retirement plans. As such, it amended Title 29 of the U.S. Annotated Code as it relates to federal labor laws (as retirement benefits are a form of compensation for an employee's services), as well as Title 26 as it relates to the I.R.C. (as such plans extend favorable tax treatment to both employees and employers). The rules set forth in Title 29 are provided under Title I of ERISA, whereas the rules set forth in Title 26 are provided under Title II of ERISA. For someone unfamiliar with ERISA, it is a difficult statute as it uses different terminology for the same concepts, different definitions for the same terms, and covers different types of employee benefit retirement plans. Thus, the author wishes to provide, in this Part II, some background regarding Title I and Title II of ERISA for those unfamiliar with it.

This article focuses on the fiduciary and prohibited transaction rules applicable under Title I and II of ERISA. Under Title I of ERISA, such rules govern an ''employee pension benefit plan,'' defined as any plan, fund, or program maintained by an employer or by an employee organization (i.e., a union), or by both, to the extent it provides retirement income to its employees.[9] In contrast, the fiduciary and prohibited transaction rules of Title II of ERISA cover a wider scope of plans, including an employee pension benefit plan qualified under I.R.C. §401(a) (which would encompass those plans subject to Title I of ERISA); an individual retirement account under I.R.C. §408(a) or an individual retirement annuity under I.R.C. §408(b); an Archer Medical Spending Accounts (MSAs) under I.R.C. §220(d); a health savings account (HSA) under I.R.C. §223(d); a Cloverdell education savings account under I.R.C. §530; or a trust or plan determined by the Treasury Secretary to be described in one of the preceding provisions.[10] Thus, an employer-sponsored retirement plan that extends tax-preferred retirement benefits to employees is subject to *both* sets of rules in Title I and II of ERISA. Given that retirement benefits are voluntary on the part of an employer, Congress realized that there would be those employees whose employers would not sponsor such a plan. To encourage those employees to save for retirement on their own, Congress created IRAs under I.R.C. §408 (i.e., Title II of ERISA), such that employees could defer a portion of their compensation without incurring taxes on their original contributions and on subsequent interest/gains of such funds until the funds were later distributed. As IRAs are not established nor maintained by an employer, they are not covered under Title I of ERISA, but are covered under Title II of ERISA due to the tax-preferred status of such accounts.[11]

The IRA model was that of a defined contribution plan model, shifting investment risk and mortality risk to the individual, as benefits paid from the IRA are solely from the individual's account balance. Initially, the maximum limitations for employer-sponsored defined contribution plans were the lesser of $25,000 or 25% of compensation, considerably higher than the maximum limitations for an IRA, which were the lesser of $1,500 or 100% of compensation. As such, employees without an employer-sponsored plan could save for retirement, but certainly not at the level provided under an employer-sponsored plan. However, Congress did provide that an employee under an employer-sponsored retirement plan could roll those pension assets out of the employer's plan and into an IRA, typically occurring when a participant terminates employment or retires. Such rollover could provide more investment choices for the employee through the IRA, but the employee would then be subject to all administrative and investment costs associated with the IRA, as the employer may have been subsidizing such costs under the employer's

[8] Pub. L. No. 93-406, 88 Stat. 829. Title II's provisions were codified in title 26 of the United States Code. All section references to the Internal Revenue Code of 1986, as amended (''I.R.C.'' or the Code), or Treasury regulations promulgated thereunder, unless otherwise indicated. All sections to Title I of ERISA (the ''ERISA''), or Labor Department regulations thereunder are labeled as such.

[9] ERISA §3(2)(A)(i). Plans that are not covered under this definition include governmental plans, church plans that do not make an election to be covered under I.R.C. §410(d), and unfunded excess benefit plans maintained for executives. *See* ERISA §4(b).

[10] I.R.C. §4975(e)(1)(A)–§4975(e)(1)(G).

[11] IRAs are exempt from Title I of ERISA, including the reporting and disclosure rules of Part 1, ERISA §101(a); the participation, benefit accrual, and survivor annuity rules of Part 2, ERISA §201(6); the funding rules of Part 3, ERISA §301(a)(7); and the fiduciary standards of Part 4, ERISA §401(a). This act may be referred to as ERISA in the text. According to the DOL regulations, IRAs are generally not employee benefit plans for purposes of Title I of ERISA, unless they are sponsored by an employer who does more than facilitate the payroll deduction of contributions to an IRA. DOL Reg. §2510.3-2(d)(1). The term IRA rollover in this article refers to the distribution of assets, typically from an eligible retirement plan to a tax-exempt IRA (i.e., an IRA where the distributions are not taxed until actual distribution). In contrast, a Roth IRA is a type of nondeductible IRA, described in I.R.C. §408A, where an employee's contributions are not deductible when contributed. The advantage of a Roth IRA is that the later withdrawal of contributions *and related earnings/investments* escape taxation, provided the distribution rules applicable to Roth IRAs are met.

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plan. While it may be tempting to an employee to roll assets into an IRA, many retirement investors do not realize that the fiduciary rules under Title II for IRAs are not as protective as the fiduciary rules under Title I for employer-provided plans.[12] In addition, transferring pension assets to an IRA causes the employee to lose the lifetime income protections, the surviving spouse protections, and the anti-alienation protections under Title I, that do not exist under Title II.[13]

Given that some of the rules of *both* Title I and II of ERISA were identical, the Congressional Reorganization Plan of 1976 assigned jurisdiction to either the DOL or the Treasury (via the IRS) based on the topic at issue.[14] The DOL has been given jurisdiction in interpreting the fiduciary and prohibited transactions rules. Both Titles of ERISA define who is a plan fiduciary with respect to plan assets,[15] as well as prohibiting certain transactions between plan fiduciaries and plan assets that could result in a conflict of interest (known as the prohibited transaction rules).[16] However, the fiduciary rules under Title I and II of ERISA are not identical, further complicating how the DOL interprets each of them. Under Title I, a fiduciary is also subject to certain standards of care, including the requirement to act *solely* in the interests of the plan participants and beneficiaries and for the exclusive purposes of providing benefits to such participants and beneficiaries (i.e., the duty of loyalty), as well as to act with the care, skill, prudence, and diligence that a prudent man would act in similar circumstances (i.e., the duty of prudence).[17] If the fiduciary fails to discharge his duties, he/she is subject to a federal cause of action for breach of fiduciary duty, rendering him/her personally liable to make good any losses to the plan and to restore to the plan any profits made through the use of such assets.[18] These fiduciary standards of care and federal cause of actions are not set forth under the Title II's fiduciary rules. Thus, in the context of an IRA, a fiduciary is not subject to explicit standards of care of loyalty and prudence, nor is he/she subject to an ERISA cause of action for breaches of such standards of care.

Likewise, Title I's and Title II's prohibited transaction rules are similar but not identical. The goal of the prohibited transaction rules is to set forth the presumption that a fiduciary is to have no other motive in its activities involving the plan or IRA other than serving it. Thus, they prohibit certain transactions between the plan and a ''party-in-interest'' (or ''disqualified person'' which is the term used in the Code), so as to avoid or minimize any conflicts of interest.[19] ERISA's prohibited transaction rules impose strict liability if applicable and require an exemption (statutorily or administratively through the DOL) for the fiduciary to act. This is in stark contrast with federal securities rules where fiduciary duties may be waived. This may be of concern to investment advisers who thought themselves subject only to federal securities law, and not the mandates of ERISA which are much different. In addition, if an IRA fiduciary triggers a prohibited transaction, it ceases to be an IRA exempt from taxation, and does so retroactively as of the first day of the tax year in which the prohibited transaction occurred.[20] Thus, the consequences for engaging in a prohibited transaction are severe for an IRA as it loses its tax qualified status. Under Title II of ERISA, the tax provisions which establish prohibited transaction rules are also enforced through an excise tax on disqualified persons, which includes fiduciaries.[21]

B. Who Is a Fiduciary With Respect to Rendering Investment Advice for a Fee?

Both Title I and II of ERISA have almost identical definitions as to who is a fiduciary with respect to a covered plan. To the extent a person or investment advisory firm exercises *discretionary* investment advice to an ERISA covered retirement plan or an IRA (e.g., he/she determines what investments should be chosen

[12] IRAs are exempt from the fiduciary standards of Part 4 of ERISA, ERISA §401(a), but are subject to the Internal Revenue Code's prohibited transaction rules, set forth in I.R.C. §4975.

[13] IRAs are exempt from the life annuity and joint and survivor annuity rules, and the anti-alienation rules of Part 2 of ERISA, §3(23), ERISA §205, ERISA §206(d).

[14] ERISA Reorganization Plan No. 4 of 1978, Executive Order No. 12, 108, 44 Fed. Reg. 47,713, 92 Stat. 3790 (Dec. 28, 1978), ''[T]he authority of the Secretary of the Treasury to issue interpretations regarding section 4975 of the Code, subject to certain exceptions . . . has been transferred to the Secretary of Labor and the Secretary of the Treasury is bound by such interpretations.'' The IRS has jurisdiction in determining whether IRAs and other covered plans are subject to the Code's prohibited transaction rules. The DOL has jurisdiction in its determination as to whether other plans are subject to ERISA's prohibited transaction rules and the issuance of exemptions to such rules. However, a DOL's determination that a prohibited transaction has not occurred does not prevent the IRS from finding liability under I.R.C. §4975. *See O'Malley v. Commissioner*, 972 F.2d 150, 154 (7th Cir. 1992); *Thoburn v. Commissioner*, 95 T.C. 132, 140 (1990).

[15] ERISA §3(21)(A)–§3(21)(B); I.R.C. §4975(e)(3)(A)–§4975(e)(3)(C).

[16] ERISA §406(a); I.R.C. §4975(c)(1).

[17] ERISA §404(a)(1)(A)–§404(a)(1)(D).

[18] ERISA §502(a)(2), ERISA §409.

[19] ERISA §408(a), §408(b); I.R.C. §4975(c)(1)(A)–§4975(c)(1)(F).

[20] I.R.C. §408(e)(2), §408(e)(3). Other parties to the prohibited transaction may be subject to a 15% excise tax on the amount involved, plus the potential 100% excise tax if the transaction is not timely corrected. I.R.C. §4975(a), §4975(b).

[21] I.R.C. §4975(a)–§4975(b).

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by the plan or IRA), he/she is definitely a fiduciary under Title I and II of ERISA and, thereby subject to the respective prohibited transaction rules.[22] However, what if an individual or firm does *not* have discretionary authority over the investment of plan assets, but nevertheless renders investment advice to the plan or the IRA in exchange for a fee, he/she may be a fiduciary subject to ERISA's fiduciary and prohibited transaction rules, as both ERISA §3(21) and I.R.C. §4975(e)(3) define a fiduciary to include someone who "renders investment advice for a fee or other compensation."[23] However, Title II of ERISA goes beyond Title I and states that an investment advice fiduciary is one who renders investment advice for a fee or other compensation, but who is also a registered investment adviser under the Investment Advisers Act of 1940; a bank or similar financial institution; an insurance company; a broker-dealer registered under the Securities Exchange Act of 1934; an affiliate of a person describe above; or an employee, agent, or registered representative of an entity described above.[24] Thus, even if the plan or IRA owner can ignore the investment advice of the person or firm, such investment adviser may nevertheless become a fiduciary under ERISA. Once an individual is found to be an ERISA fiduciary, he/she also becomes subject to its respective prohibited transaction rules.[25]

C. DOL's 1975 Regulations Regarding an Investment Advice Fiduciary

The DOL's original regulations, issued in 1975, set forth a five-part test as to who is a nondiscretionary investment adviser to the plan or IRA.[26] To the extent an individual or firm satisfies this five-part test *and* receives compensation in exchange for its investment advice, he/she may need a PTE in order to be able to receive various types of compensation. When ERISA was passed in 1974, the primary retirement model used by employers was the defined benefit pension plan, whereby an employee was promised a lifetime (or joint and survivor lifetime, if married) annuity of a specified amount beginning at a normal retirement age. Under this model, the employer undertook the investment and mortality risks, not the employee. Thus, most employers employed professional investment advisers to manage and invest plan assets. By the 1990s, defined contribution plans, particularly 401(k) plans, became the predominant retirement model used by employers.[27] Given that ERISA §404(c) absolves the plan fiduciary from liability for investment losses if the employer effectively shifts investment control over to the participant or beneficiary, most 401(k) plans took advantage of this and allowed plan participants and beneficiaries to select their investments under the employer's retirement plan.

Quoting from the 1975 regulations, DOL Reg. §2510.3-21(c)(1) states that:

A person shall be deemed to be rending 'investment advice' to an employee benefit plan . . . only if:

> (i) "Such person renders advice to the plan as to the value of securities or other property, or makes recommendations as to the advisability of investing in, purchasing, or selling securities or other property; and
>
> (ii) "Such person either directly or indirectly (e.g., through or together with any affiliate)
>
>> (A) Has discretionary authority or control . . . with respect to purchasing or selling securities or other property for the plan; or
>>
>> (B) Renders any advice described in paragraph (c)(1)(i) of this section (e.g., investment advice) on a regular basis to the plan pursuant to a mutual agreement, . . . written or otherwise, between such person and the plan or a fiduciary with respect to the plan, that such services will serve as a primary basis for investment decisions with respect to plan assets, and that such person will render individualized investment advice to the plan based on the particular needs of the plan regarding such matters as, among other things, investment policies or strategy, overall portfolio composition, or diversification of plan assets.

Thus, under the original regulations, a fiduciary investment adviser was deemed to be a fiduciary if:

- He/she rendered advice as to the value of the property or securities or made a *recommendation* as to the advisability of investing, purchasing, or selling such securities or other property;
- On a *regular* basis;
- Pursuant to a *mutual understanding* with the plan or the plan fiduciary;
- That served as *a primary basis* for the investment decision with respect to plan assets; and

[22] ERISA §3(21)(A); I.R.C. §4975(e)(3)(A).

[23] ERISA §3(21)(A)(ii); I.R.C. §4975(e)(3)(B).

[24] I.R.C. §4975(f)(8)(J)(i)(I)–§4975(f)(8)(J)(i)(VI).

[25] ERISA §406(a)–§406(b); I.R.C. §4975(c)(a)(A)–§4975(c)(a)(F).

[26] DOL Reg. §2510.3-21(c)(1), 40 Fed. Reg. 50,842 (Oct. 31, 1975) and Treas. Reg. §54.4975-9(c), 40 Fed. Reg. 50,840 (Oct. 31, 1975).

[27] *See* Samuel Estreicher and Laurence Gold, *The Shift from Defined Benefit Plans to Defined Contribution Plans,* 11 Lewis & Clark L. Rev. 331 (2007).

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- Where such advice was *individualized* based on the needs of the plan.

By applying this narrow interpretation of a nondiscretionary fiduciary investment adviser, the DOL limited the number of advisers that would be covered under the test, and thus restricting the number of advisers who would have to assess higher fees because of their fiduciary status. This five-part test excluded many financial advisers, including broker-dealers and their related financial institutions. To the extent an individual or investment firm satisfy all part of the five-part test *and* received compensation for such advice, he/she may need a PTE in order to be able to receive such compensation. A year later, the DOL further narrowed the fiduciary status definition, in the *Deseret* Letter, by stating that a recommendation from a financial adviser to take a distribution of employer-provided funds from a qualified plan and roll such funds into an IRA was *not* regarded as investment advice, even though such decision could result in alternative investment choices under the IRA.[28] Thus, an investment professional making such a recommendation did not become a fiduciary by virtue of rendering investment advice for a fee.

In the federal securities law context, a recommendation to roll monies from a 401(k) plan into an IRA was viewed as a securities recommendation, subjecting broker-dealers to the suitability standard of care that prompted certain disclosure requirements.[29] Securities laws permitted conflicts of interest between the adviser or broker dealer and the customer, provided there was adequate disclosure of such conflicts. In 2010, Congress directed the SEC to ascertain whether a uniform fiduciary standard should be utilized to broker-dealers and registered investment advisors s when offering personalized advice.[30] In contrast, Title I of ERISA's fiduciary standards require a fiduciary to act *solely* in the interest of the plan participants and beneficiaries.[31] As such, disclosure of any potential conflicts of interest is insufficient to absolve liability.

[28] DOL Adv. Op. 76-65A (June 7, 1976). The DOL later affirmed this position in DOL Adv. Op. 2005-23A (May 11, 2005), whereby a recommendation to a plan participant to take a distribution from the plan for purposes of completing a rollover is not ''investment advice'' nor a recommendation concerning a particular investment (i.e., purchasing or selling securities or other property) under the 1975 regulations. Any investment recommendation regarding how the proceeds should be invested would be advice with respect to funds that are no longer assets of the plan.

[29] See *In the Matters of Richard N. Cea, et al.*, Exchange Act Release No. 8662 at 18 (Aug. 6, 1969) (Release 8662); *In the Matter of Mac Robbins; & Co., Inc.*, Exchange Act Release No. 6846 (July 11, 1962).

[30] *See* Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, §913 of Title IX, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

[31] ERISA §404(a)(1)(A).

D. Prohibited Transaction Rules of Title I and II of ERISA

The prohibited transaction rules of Title I and II of ERISA are similar but not identical. Title I sets forth two sets of prohibited transactions in ERISA §406(a) and ERISA §406(b), whereas Title II's set of prohibited transaction rules are contained within a single set in I.R.C. §4975(c). ERISA §406(a) states, that except as otherwise provided in ERISA §408 (the statutory exemptions), a fiduciary may not cause the plan to engage in a direct or indirect transaction involving: a sale or exchange of property between the plan and a party-in-interest; the lending of money or extension of credit between the plan and a party-in-interest; furnishing of goods, services, or facilities between a plan and a party-in-interest; or the transfer to, or use by, a party-in-interest, of any assets or income of the plan. These are referred to as ''per se'' prohibited transactions. In contrast, ERISA §406(b) is *not* caveated with the phrase ''except as provided in section 408'' (indicating that the statutory exemption should not be applicable) and thus prohibit the fiduciary from dealing with plan assets for his own interest or for his own account (i.e., the self-dealing prohibition); from acting in a transaction involving the plan whose interest are adverse to the interest or the plan or its participants or beneficiary (i.e., the conflict of interest prohibition); and from receiving any consideration for the fiduciary's own personal account from any party dealing with the plan in connection with the transaction involving plan assets (i.e., the kickback prohibition).[32] These are referred to as the ''fiduciary prohibited transactions,'' as they benefit the fiduciary and do not necessarily involve a party-in-interest, unless he/she is also a fiduciary.

In contrast, I.R.C. §4975(c) sets forth a single set of prohibited transaction rules (which presumably are *all* exempt under the statutory exemptions of I.R.C. §4975(d)), which include the same four ''per se'' prohibited transactions set forth under Title I and the first and the third ''fiduciary prohibited transactions'' set forth under Title I. Title I's second fiduciary prohibited transaction involving conflicts of interest is not contained in Title II's prohibited transaction rules, as Title II does not impose a fiduciary standard of care to act in the best interest of the plan participants or beneficiaries (i.e., the duty of loyalty).[33] However, the IRS in its regulations has read the two fiduciary pro-

[32] ERISA §406(b)(1)–§406(b)(3).

[33] The legislative history indicates that the second fiduciary prohibited transaction rule was omitted under title due to the difficulty in determining the ''appropriate measure'' for an excise tax. *See* H.R. Rep. No. 93-1280, 4576 (1974) (Conf. Rep), *reprinted in* 1974 U.S.C.C.A.N. 5038 (stating ''[T]he labor provisions (but not the tax provisions) prohibit a fiduciary from acting

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hibited transactions in Title II to *include* a fiduciary's conflict of interest involving the income or assets of the plan.[34] In addition, where the statute under Title II appears to allow fiduciary prohibited transactions to be exempt under the statutory exemptions, the IRS takes the contrary position — namely, that the statutory exemptions of I.R.C. §4975(d) do not contain any exemptions for fiduciary prohibited transactions, as the latter involve separate transactions that are not described in any of the statutory exemptions.[35] Similar to Title I, Title II allows the DOL to establish administrative exemptions to the prohibited transaction rules.

The prohibited transaction rules of Title I and II of ERISA on their face would appear to deny the ability of a plan or IRA to engage in services that it would need in the course of its usual business. For example, they prohibit a fiduciary from rendering services between a plan and a party-in-interest (e.g., service-provider to the plan).[36] In order to render such services, the fiduciary and the party-in-interest would have to comply with one of the statutory exemptions or an administrative class exemption created by the DOL.[37] As expected, both Title I and II's statutory exemptions permit the fiduciary to contract with a party-in-interest (or a disqualified person in the context of the Code) for services necessary for the operation of the plan (including investment services), provided no more than reasonable compensation is paid therefor,[38] and for the party-in-interest to receive reasonable compensation for services rendered . . . in the performance of his duties with the plan.[39] Both the DOL and the IRS agree that the first of the two statutory exemptions permitting a fiduciary to contract with a party-in-interest (or disqualified person) for purposes of rendering services if no more than reasonable compensation is paid does *not* extend to permit self-dealing by the fiduciary.[40] Thus, self-dealing by a fiduciary would *require* a DOL class or individual administrative exemption.

The DOL has interpreted the self-dealing fiduciary prohibited transaction rule to apply in situations where the plan fiduciary uses its authority or control to *increase* its own compensation in a transaction involving plan assets.[41] This would apply in the situation where the fiduciary recommends use of investment products (e.g., propriety products) offered by it or its affiliates which resulted in indirect fees (e.g., finder fees, commissions) back to the fiduciary. The *Frost Bank* Opinion by the DOL allowed the fiduciary to avoid committing a fiduciary prohibited transaction by *offsetting* fees that it would have otherwise received from the plan or the plan sponsor.[42] The opinion allowed the plan fiduciary to obtain 12b-1 fees and other administrative service fees (e.g., record-keeping fees) from the mutual funds that it was recommending as plan investments provided they offset any fees that the plan owed the plan fiduciary. Thus, such indirect compensation was not considered to be *additional* compensation to the fiduciary which would have resulted in self-dealing.

Compensation practices whereby a fiduciary adviser is paid a fixed percentage of assets (i.e., level fees) regardless of the investments actually selected do not need a class exemption from the prohibited transaction rules, as there is no self-dealing. However, when the fiduciary adviser wishes to receive *variable* fees (e.g., commissions, 12b-1 fees, and revenue sharing payments) that do vary depending on the investment products selected, such arrangements will need a class exemption due to the significant conflict of interest posed.

Other relevant prohibited transaction exemptions that the DOL has issued over the years include PTEs

in any transaction involved the plan on behalf of a person (or representing a party) whose interests are adverse to the interest of the plan or of its participants or beneficiaries. This prevents a fiduciary from being put in a position where he has duel loyalties, and, therefore, he cannot act exclusively for the benefit of a plan's participants and beneficiaries. (This prohibition is not included in the tax provisions, because of the difficulty in determining an appropriate measure for an excise tax.'')).

[34] Treas. Reg. §54.4975-6(a)(5)(i) (''The prohibitions of sections 4975(c)(1)(E) and (F) supplement the other provisions . . . by imposing on disqualified persons who are fiduciaries a duty of undivided loyalty to the plans for which they act. These prohibitions are imposed upon fiduciaries to deter them from exercising the authority, control, or responsibility which makes such persons fiduciaries when they have interests which may conflict with the interests of the plans for which they act'').

[35] Treas. Reg. §54.4975-6(a) (stating that the statutory exemption for office space or services does not contain an exemption for acts described in I.R.C. §4975(c)(1)(E) or I.R.C. §4975(c)(1)(F) as such acts are separate transactions not described in the statutory exemption).

[36] ERISA 406(a)(1)(C) and I.R.C. §4975(c)(1)(C), but the Code uses the term ''disqualified person'' to identify the person/entity who is providing services to the plan.

[37] ERISA §408(a)–§408(b).

[38] ERISA §408(b)(2); I.R.C. §4975(d)(2).

[39] ERISA §408(c)(2); I.R.C. §4975(d)(10).

[40] DOL Reg.§2550.408b-2(a) (stating that ERISA §408(b)(2) ''exempts from the prohibitions of section 406(a) of the Act . . .'' but ''does not contain an exemption from acts described in section 406(b)(1) . . ., section 406(b)(2) or section 406(b)(3)'') and Treas. Reg. §54.4975-6(a) (stating that the statutory exemption for office space or services does not contain an exemption for acts described in I.R.C. §4975(c)(1)(E) or I.R.C. §4975(c)(1)(F) as such acts are separate transactions not described in the statutory exemption).

[41] DOL Adv. Op. 97-15A (May 22, 1997) and DOL Adv. Op. 2005-10A (May 11, 2005).

[42] DOL Adv. Op. 97-15A.

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75-1, 84-24, and 86-128. PTE 75-1 extends relief to non-fiduciary broker-dealers who execute buy-sell agreements with the plan as agents for securities transactions and receive a commission.[43] Since the broker-dealer would be a party-in-interest in providing services to the plan in exchange for fees, a class exemption was needed. It would later be replaced by PTE 86-128 which allowed a plan fiduciary to receive fees (e.g., 12b-1 fees, commissions) for effecting and executing securities transaction as an agent for a plan or IRA.[44] Bank trustees utilizing their in-house brokers relied on this exemption, but it did mandate that the additional compensation not be excessive and that specific disclosures were to be made. Broker-dealers and their affiliates generally did not make use of this exemption due to the disclosure requirements. PTE 84-24 granted a class exemption relief for agents and brokers who sold insurance products to plans and received fees in the form of commissions.[45]

III. BEGINNING IN 2010, REGULATORS RETHINK STANDARDS OF CONDUCT APPLICABLE TO INVESTMENT ADVISERS

A. Exponential Growth of the IRA Marketplace

The exponential growth of the IRA rollover market in the early 1990s caused a number of government and regulatory agencies — the DOL, the SEC, FINRA, the GAO, and the Consumer Financial Protection Bureau (CFPB) — to reexamine the applicable standard of care applicable when a financial adviser, particularly broker-dealers and registered investment advisors, recommend that 401(k) plan assets be rolled into an IRA.[46] The phrase ''capture the rollover'' refers to the ability to have some or all of monies held in a 401(k) employer-provided plan to be rolled over into an IRA.[47]

Due to the expansion of the IRA marketplace, the DOL noticed that brokerage firms were now offering comprehensive guidance services, as opposed to mere transactional support, and that their sources of compensation — such as brokerage commissions, revenue share by mutual funds and funds' assets managers, and mark-ups on bonds sold from their own inventory — produced acute conflicts of interest. For the DOL to control the types of compensation that an investment adviser to an employee benefit plan or IRA could receive, the DOL first had to find such adviser to be an investment advice fiduciary under Title I and II of ERISA, such that it could then subject such adviser to the fiduciary PTEs. Thus, it needed to rethink its 1975 regulations as to who is an investment advice fiduciary and then to craft PTEs such that the fiduciary could receive variable forms of compensation. By 2010, the DOL became vocal that it was troubled with three parts of its five-part definition of who is an investment advice fiduciary receiving a fee — namely, the requirement that the advice be provided on a *regular* basis; through a *mutual understanding* between the parties; that serviced as *a primary basis* for the investment decision. It was also alarmed that such investment advisers ''may operate with conflicts of interests that they need not disclose to plan fiduciaries . . . . [a]nd have limited liability under ERISA for the advice they provide.''[48] Without any advance public groundwork, the DOL issued proposed regulations (referred to by practitioners as Proposal 1.0), altering who could be a fiduciary investment adviser and applying such definition to the PTE rules applicable to employee benefit plans and IRAs.[49] The proposal would have rendered a financial adviser to be a fiduciary if he/she (1) rendered ''covered advice'' (covering three categories of advice) (2) involving one of four different ''covered relationships'' and (3) received a fee for such advice (defining the term fee expansively).[50] The proposal made investment advisers registered under the Investment Advisers Act of 1940, as amended, automatic plan fiduciaries, as well as broker-dealers if their investment advice ''may be considered'' for plan investment purposes and was in-

[43] Securities Transactions Involving Broker-Dealers, Reporting Dealers, and Banks, PTE 75-1, 40 Fed. Reg. 50,845 (Oct. 31, 1975).

[44] Class Exemption for Securities Transactions Involving Employee Benefit Plans and Broker-Dealers, 81 Fed. Reg. 21,181 (Apr. 8, 2016).

[45] Class Exemption for Certain Transactions Involving Insurance Agents and Brokers, Pension Consultant, Insurance Companies, Investment Companies, and Investment Company Principal Underwriters, 49 Fed. Reg. 13,208 (Apr. 3, 1984), amended at 71 Fed. Reg. 5887 (Feb. 3, 2006).

[46] *See* GAO-13-30, 401(k) plans: Labor and IRS Could Improve the Rollover Process for Participants (Mar. 2013). By 2012, IRA assets totaled $5.1 trillion, accounting for 28% of U.S. retirement assets, according to the Investment Company Institute (ICI), The U.S. Retirement Market, Second Quarter 2012 (Sept. 2012). This GAO report followed a 2011 report entitled GAO-11-119 (Jan. 2011). Responding to the 2013 GAO report, Assistant Secretary of Labor Phyllis Borzi stated, ''[w]e believe our work regarding the definition of fiduciary is key to addressing conflicted investment advice and related problems your report identifies.''

[47] *See* Fred Reish, Bruce Ashton, Joan Neri, and Joshua Waldbeser, *Capturing Plan Rollovers,* Plan Consultant (Spring 2014).

[48] Preamble to DOL Prop. Reg. §2510.3-21(c), 75 Fed. Reg. 65,263, 65,265 (Oct. 22, 2010).

[49] DOL Prop. Reg. §2510.3-21(c), 75 Fed. Reg. 65,263.

[50] DOL Prop. Reg. §2510.3-21(c)(1)(i)(A).

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dividualized for the plan or the participant.[51] That proposal generated much debate within the investment community, particularly recommending that the DOL wait for SEC regulatory guidance. As a result, the DOL withdrew the proposal in 2011, in hopes of reproposing it in 2012.

A 2013 GAO report was quite critical as it investigated the number of 401(k) participants deciding to take IRA rollovers in lieu of other distribution options offered under the employer's plan.[52] In December of 2013, FINRA issued a regulatory notice, reminding broker-dealers that they were subject to a suitability standard when recommending a rollover from an employer retirement plan to an IRA and directing them to critique their marketing communications in promoting such IRA rollovers.[53] By 2014, the SEC had placed on its examination priority list the sales practices of investment advisers promoting 401(k) participants to roll distributions into an IRA, as well as the marketing and advertising promotions used by broker-dealers and investment advisers to solicit such IRA rollovers.[54] Such activity demonstrated that a number of regulators were becoming concerned with the IRA rollover market.

B. DOL's 2015 Proposal and 2016 Final Fiduciary Rules

By early spring of 2015, President Obama announced in a speech to AARP that he would direct the DOL to repropose the definition of an investment adviser fiduciary.[55] Under the 2015 proposal, the DOL defined an investment adviser fiduciary as an individual who (1) provided ''covered advice'' (covering four categories of advice) (2) for a fee (direct or indirect) to a plan, a plan fiduciary, a participant/ beneficiary, an IRA or an IRA holder in (3) two circumstances, *either* (a) it acknowledges to be a fiduciary or (b) it provides advice under an agreement (not necessarily mutual) where the advice is *individual to* or specifically directed to the recipient for *consideration* (even if it is not the primary basis) in making investment or management decisions with respect to securities or other property (referred to by practitioners as Proposal 2.0).[56] The proposed expansive definition of a fiduciary targeted individuals giving occasional or transactional investment advice, unlike the 1975 regulations, as well as those making recommendations as to whether to take a distribution and invest the monies outside of the plan. Hence, the DOL proposed revoking the *Deseret* Letter.

With the proposed regulations, the DOL issued two new prohibited transaction class exemptions, including the Best Interest Contract (BIC) Exemption,[57] as well as amending existing prohibited transaction class exemptions.[58] In order for financial advisers to continue to receive fees under their current compensation schemes (e.g., brokerage and insurance commissions, 12b-1 fees, and revenue sharing), the BIC Exemption required the adviser to acknowledge its fiduciary status; to adhere to standards of impartial conduct; to warrant that there existed policies and procedures reasonably designed to mitigate any conflicts of interest; and to disclose its conflicts and the cost of advice.[59] Thus, the DOL attempted to impose ERISA's Title I duties of prudence and loyalty on an investment adviser to an IRA, as well as creating a private cause of action enforceable under state court, which was unavailable to IRAs as they are not subject to Title I of ERISA.[60] These elements of the proposal were the most controversial aspects of the exemption, according to the financial community.

In response to the DOL's proposal, the Security Industry and Financial Markets Association (SIFMA) issued in early June of 2015 a proposed standard for financial broker-dealers that set forth a uniform best interest customer standard to be used when providing personalized advice about securities to retain investors.[61] It criticized the DOL's proposal as being ''ex-

[51] DOL Prop. Reg. §2510.3-21(c)(1)(ii)(D).

[52] See Note 45, above.

[53] FINRA Regulatory Notice 13-45, Rollovers to Individual Retirement Accounts (Dec. 2013).

[54] *See* Examination Priorities for 2014, SEC Office Of Compliance Inspection and Examination (Jan. 9, 2014).

[55] *See* Mark Schoeff Jr., Obama directs Labor Department to move ahead on fiduciary rule, Investment News (Mar. 4, 2015).

[56] DOL Prop. Reg. §2510.3-21, 80 Fed. Reg. 21,928 (Apr. 30, 2015). For a more in-depth discussion of the DOL proposals, see Kathryn J. Kennedy, *The DOL Proposed Fiduciary Regulations and Related Prohibited Transaction Exemptions,* NYU Rev. of Employee Benefits and Executive Compensation, CH 3 (2015).

[57] Proposed Best Interest Contract Exemption, 80 Fed. Reg. 21,960 (Apr. 20, 2015), and Proposed Class Exemption for Principal Transactions in Debt Securities, 80 Fed. Reg. 21,989 (Apr. 20, 2015).

[58] Proposed Amendment to Prohibited Transaction Exemption (PTE) 75-1, Part V., etc., 80 Fed. Reg. 22,004 (Apr. 20, 2015); Proposed amendment to and Proposed Partial Revocation of Prohibited Transaction Exemption (PTE) 84-24, 80 Fed. Reg. 22,010 (Apr. 20, 2015); Proposed Amendment and Proposed Revocation of Prohibited Transaction Exemption (PTE) 86-128, 80 Fed. Reg. 22,012 (Apr. 20, 2015); and Proposed Amendments to Class Exemption 7-1, 77-4, 80-83, and 83-1, 80 Fed. Reg. 22,035 (Apr. 20, 2015).

[59] See Note 57, above at Section II.

[60] *Id.*

[61] Proposed Best Interest of the Customer Standard for Broker-Dealers, SIFMA (June 3, 2015).

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tremely burdensome and perhaps ultimately in practice inconsistent with the best interest of the client.''[62]

By 2016, the DOL finalized its 2015 proposals by issuing (1) final regulations under ERISA §3(21) and I.R.C. §4975(e)(3) as to who was an investment advice fiduciary,[63] as well as two prohibited transaction class exemptions, including the BIC Exemption and the Class Exemption for Principal Transactions in Certain Assets Between Investment Advice Fiduciaries and Employee Benefit plans,[64] and (2) amendments to existing prohibited transaction class exemptions.[65] The final regulations (referred to as 2016 Fiduciary Rule) replaced the five-part test with a much broader test such that an individual who (1) provided ''covered advice'' (which included a recommendation to take a distribution of benefits from a plan and roll such amounts into an IRA) for a fee to a plan, participant or beneficiary, an IRA, or an IRA owner and (2) *either* acknowledged himself/herself to be a fiduciary or provided advice pursuant to an agreement based on the particular investment needs of the recipient or directed advice to the recipient regarding the advisability of a particular investment or management decisions regarding securities.[66]

The DOL finalized the BIC Exemption for use by broker-dealers and insurance agents rendering nondiscretionary investment advice to retirement investors in exchange for fees that varied depending on the investment options selected.[67] That exemption required: (1) that there be a written contract between the adviser and the investor; (2) that the adviser give written acknowledgment that he/she was a fiduciary for purposes of its investment recommendations (3) that the adviser was required to adhere to ''Impartial Conduct Standards'' when rendering investment advice, incorporating ERISA's loyalty and prudence standards of care; limiting the adviser to a reasonable amount of compensation; and requiring the adviser to refrain from making misleading statements about possible investments; (4) that the adviser would adopt and adhere to policies and procedures, designed to ensure compliance with the impartial conduct standard; that the adviser would disclose its material conflicts of interest and adopt measures to avoid or mitigate conflicts of interest that could lead to a breach of the Impartial Conduct Standards; the contract named the person/title responsible for addressing material conflicts of interest or for monitoring compliance of the adviser to the Impartial Conduct Standards; and the contract prohibited the use of quotas, bonuses, etc. that would lead to recommendations not otherwise in the best interest of the investor.[68] The BIC Exemption created a cause of action for IRA owners if the exemption was violated.

The DOL's final regulations and related PTEs, published on April 8, 2016, were to be effective 60 days after the date of their publication in the Federal Register. President Trump, by Memorandum to the Secretary of Labor dated February 3, 2017, directed the DOL to examine whether the fiduciary rule would adversely affect the ability of Americans to gain access to retirement information and financial advice, and to prepare an updated economic and legal analysis regarding the impact of the fiduciary rule as part of that examination. On April 7, 2017, the DOL extended the effective date of the fiduciary rules until April 10, 2017. In the case of the BIC Exemption, the DOL further delayed its effective date until January 1, 2018, but required fiduciaries relying on the exemption to adhere to the Impartial Conduct Standards during the transition period from June 9, 2017 until January 1, 2018. On November 29, 2017, the DOL further extended the effective date for the 2016 final regulations and related PTEs by 18 months, such that the new transition period would end on July 1, 2019, rather than on January 1, 2018.[69]

C. Fifth Circuit's Vacatur of the 2016 Final Fiduciary Rules

Three business groups (U.S. Chamber of Commerce, the American Council of Life Insurers, and the

[62] *See* SIFMA President and CEO Kenneth E. Bentsen, Jr. Remarks as Prepared for the SIFMA DOL Fiduciary Seminar: Assessing the Intended and Unintended Consequences (June 3, 2015).

[63] DOL Reg. §2510.3-21, 81 Fed. Reg. 20,946 (Apr. 8, 2016). For a more in-depth discussion of the DOL proposals, *see* Kathryn J. Kennedy, *The DOL Fiduciary Regulations and Related Prohibited Transaction Exemptions,* NYU Rev. of Employee Benefits and Executive Compensation, CH. 3 (2016).

[64] Best Interest Contract Exemption, 81 Fed. Reg. 21,002 (Apr. 8, 2016); Class Exemption for Principal Transaction in Certain Assets Between Investment Advice Fiduciaries and Employee Benefit Plans, 81 Fed. Reg. 21,089 (Apr. 8, 2016).

[65] Amendment to Prohibited Transaction Exemption (PTE) 75-1, Part V, etc., 81 Fed Reg. 21,139 (Apr. 8, 2016); Amendment to and Partial Revocation of Prohibited Transaction Exemption (PTE) 84-24, 81 Fed. Reg. 21,147 (Apr. 8, 2016); Amendment and Revocation of Prohibited Transaction Exemption (PTE) 86-128, 81 Fed. Reg. 21,181 (Apr. 8, 2016); and amendments to Class Exemption 75-1, 77-4, 80-83, and 83-1, 81 Fed. Reg. 21,208 (Apr. 8, 2016). The financial community estimated that the stricter fiduciary standards in Proposal 2.0 would cost an estimated $2.4 billion and $5.7 billion over 10 years by eliminating conflicts of interest like front-end load commissions and mutual fund 12b-1 fees. *See* Katelyn Peters, Everything You Need to Know About the DOL Fiduciary Rule July 14, 2021).

[66] DOL Reg. §2510.3-21(a)(2).

[67] See Note 65, above.

[68] *Id.,* Section II(d)(1)–(3).

[69] 82 Fed. Reg. 56,545, 56,548, 56,550, 56,552 (Nov. 29, 2017).

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Indexed Annuity Leadership Council) filed separate lawsuits in 2016, challenging the DOL's 2016 Fiduciary Rule (which included its regulations as to who was an investment advice fiduciary and its related PTEs). Such lawsuits alleged that the 2016 Fiduciary Rule was inconsistent with the governing statutes; that the DOL overreached its authority to regulate services and providers; that the DOL had imposed legally unauthorized contract terms to enforce its new guidance; that there were various First Amendment violations; that the treatment of variable and fixed indexed annuities under the 2016 Fiduciary Rule was arbitrary and capricious. The three lawsuits were later consolidated, and the district court in the Northern District of Texas rejected all of the challenges.[70] Upon appeal to the Fifth Circuit, the court reversed the district court's judgment on March 15, 2018, and vacated the DOL's 2016 Fiduciary Rule.[71] As a result, the 2016 Fiduciary Rule was removed, as well as the BIC Exemption. On May 7, 2018, the DOL issued Field Assistance Bulletin 2018-02, providing temporary nonenforcement of prohibited transaction claims against investment advice fiduciaries who worked ''diligently and in good faith'' to comply with the Impartial Conduct Standards for transactions that would have been exempt under the BIC Exemption.[72]

D. SEC's 2019 Regulation Best Interest

Under the Investment Advisers Act of 1940, investment advisers have a fiduciary duty of care in advising clients that requires putting their clients' best interests before their own; such duty encompasses both the duty of care and the duty of loyalty.[73] In contrast, the Securities Exchange Act of 1934 imposes a standard of conduct for a broker-dealer when making a recommendation of any securities transaction or investment strategy involving securities such that the recommendation be ''suitable,'' when considering the client' financial needs, objectives, and circumstances; such standard does not require that such recommendations be in the client's best interest.[74] The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 directed the SEC (1) to provide a standard of conduct for broker-dealers and investment advisers when providing personal investment advice about securities to retail consumers, and (2) to study the effectiveness of its existing standards of care for broker-dealers and investment advisers when offering personalized advice.[75]

In response to this congressional request, the SEC proposed Reg BI in 2018, designed to set forth the standard of care for broker-dealers who were providing investment advice.[76] Such standard obligated the broker-dealer to act in the best interest of the retail customer at the time of the recommendation, without placing the financial or other interest of the broker-dealer (or another entity associated with the broker-dealer) *ahead of* the interest of the retail customer. By 2019, the SEC adopted a new set of rules ''designed to enhance the quality and transparency of retail investors' relationship with investment advisers and broker-dealers,'' which included:

- Finalization of Reg BI, with its new standard of care for broker-dealers when making recommendations to retail customers, including retirement plan rollover recommendations. The standard was not an explicit loyalty standard (as found in ERISA), but required the broker-dealer to act in the ''best interest'' of the retail customer, without placing the financial or other interest of the broker-dealer ahead of the inter-

[70] *Chamber of Commerce v. Hugler*, 231 F. Supp. 3d 152 (N.D. Tex. 2017).

[71] *Chamber of Commerce v. DOL*, 885 F.3d 360 (5th Cir. 2018).

[72] DOL Field Assistance Bulletin 2018-02 (May 7, 2018).

[73] 15 U.S.C. §80b-1–§80b-21. The Investment Advisers Act also requires investment advisers to act in good faith and to disclose all relevant facts relating to the investment to clients; to obtain the best possible price in buying and selling of securities (best execution); to avoid conflicts of interest and to disclose any potential conflicts of interests to clients; and to establish, maintain, and enforce written policies and procedures reasonably designed to avoid the misuse of material, nonpublic information by the investment adviser. *See SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 194 (1963) (*SEC v. Capital Gains*); see also footnotes 34–44 in *Capital Gains Research Bureau, Inc.*,375 U.S. 180, 207 and accompanying text; Investment Adviser Codes of Ethics, Investment Advisers Act (Advisers Act) Release No. 2256 (July 2, 2004); Compliance Programs of Investment Companies and Investment Advisers, Investment Advisers Act Release No. 2204 (Dec. 17, 2003); Electronic Filing by Investment Advisers; Proposed Amendments to Form ADV, Investment Advisers Act Release No. 1862 (Apr. 5, 2000). Investment advisers also have antifraud liability with respect to prospective clients under section 206 of the Advisers Act.

[74] Securities Exchange Act of 1934, §15(b), 15A, Pub. L. 73-291, 15 U.S.C. §78a *et seq. See In the Matters of Richard N. Cea*, Exchange Act Release No. 8662 at 18 (Aug. 6, 1969), and *In the Matter of Mac Robbins & Co., Inc.*, Exchange Act Release No. 6846 (July 11, 1962). See also FINRA Rule 2111.01 (Suitability) (''Implicit in all member and associated person relationships with customers and others is the fundamental responsibility for fair dealing. Sales Efforts must therefore be undertaken only on a basis that can be judged as being within the ethical standards of [FINRA's] Rules, with particular emphasis on the requirement to deal fairly with the public. The suitability rule is fundamental to fair dealing and is intended to promote ethical sales practices and high standards of professional conduct.'').

[75] *See* Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, §913 of Title IX, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

[76] See Note 5, above.

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est of the retail customer. It required the broker-dealer, prior to or at the time of the recommendation, to disclose the scope and terms of the relationship, including the materials fees and costs; to note any material limitations on the securities or strategies that may be recommended (e.g., that the broker-dealer may be recommending propriety products); and to state all material facts relating to conflicts of interest associated with the recommendation.[77]

- A new Form CRS Relationship Summary (Form CRS) was issued to help the retail investor with his/her initial selection and ongoing decision to maintain an existing relationship with the adviser. Such form would aid the investor in selecting and maintaining a relationship with a financial professional or firm, by described the services offered; the fees, costs, conflicts of interest, and standards of conduct associated with the services; whether the firm or its financial professionals have engaged in legal or disciplinary actions; and how to obtain more information about the firm. The Form CRS would be filed with the SEC and furnished to the client.[78]

Then SEC Chairman Jay Clayton stated that his agency collaborated with the DOL in setting its investment advice standards in Reg BI.[79] The DOL's 2016 fiduciary standard provided a much higher level of accountability for broker-dealers than the best interest standard, as it would require the adviser to adhere to Title I's prudence and loyalty standards.

IV. DOL'S 2020 PROPOSED AND FINAL REINTERPRETATION OF AN INVESTMENT ADVICE FIDUCIARY AND ITS RELATED PROHIBITED TRANSACTION EXEMPTION (PTE) (PTE 2020-02)

A. DOL's 2020 Proposal

In response to the Fifth Circuit's vacatur, the DOL on July 7, 2020, did the following:

- It reinstated the 1975 regulation (affirming the original five-part test as to who is an investment advice fiduciary) and its Interpretive Bulletin 96-1 regarding participant investment education;
- It proposed a new prohibited transaction class exemption available to investment advice fiduciaries entitled "Improving Investment Advice for Workers and Retirees;" and
- It updated its website to remove the prior BIC Exemption (PTE 2016-01) and the Class Exemption for Principal Transactions in Certain Assets Between Investment Advice Fiduciaries and Employee Benefit plans and IRA (PTE 2016-02) and to return the amended PTEs (PTEs 75-1, 77-4, 80-83, 83-1, 84-24, and 86-128) to their pre-amendment form.[80]

The DOL did not revoke FAB 2018-02, which provided a temporary nonenforcement policy against prohibited transaction claims against investment advice fiduciaries who were diligently and in good faith complying with the Impartial Conduct Standards set forth in the 2016 BIC Exemption.

B. Preamble Which Reinterprets the 1975 Regulations and the Proposed Exemption

In the Preamble of its proposal, the DOL clarified elements of the five-part test: (1) it stated that the analysis in the *Deseret* Letter was incorrect and thus, advice regarding a distribution from a plan and rolling it to an IRA or another plan can be considered to be on "a regular basis," if the rollover advice is part of an on-ongoing investment advice or if the rollover advice is the start of an ongoing relationship;[81] (2) when a financial service professional gives advice in compliance with the SEC's Reg BI or another requirement to provide individualized advice, the parties should reasonably understand that the advice will serve as a primary basis for the investment decision;[82] and (3) any disclaimer of fiduciary would not be conclusive.[83] Under the proposed PTE, broad relief was provided for the receipt of compensation by the investment professional and its financial institution (e.g., commissions, 12b-1 fees, training commissions, sales loads, mark-ups and mark-downs, and revenue sharing payments) from investment providers or third parties, in connection with investment advice, as well as allowing financial institutions to engage in princi-

[77] *Id.*

[78] SEC Rule Release No. 34-86032, SEC Form CRS Relationship Summary; Amendments to Form ADV (final rule), 84 Fed. Reg. 33,492 (July 19, 2019).

[79] Mark Schoeff Jr., *DOL proposes new standard to replace vacated fiduciary rule*, Investment News (June 29, 2020).

[80] Improving Investment Advice for Workers & Retirees, 85 Fed. Reg. 40,834 (July 7, 2020).

[81] *Id.,* 85 Fed. Reg. 40,834, 40,839–40,840.

[82] *Id.,* 85 Fed. Reg. 40,834, 40,840.

[83] *Id.,* 85 Fed. Reg. 40,834, 40,844.

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pal transactions with plans and IRAs in which the financial institution purchases and sells certain investments from its own account.[84] The term financial institution included a registered investment adviser, bank, insurance company, or registered broker-dealer that employs an investment professional, or retains the investment professional as an independent contractor, agent, or registered representative.[85]

Adherence to the proposed PTE required: (1) Investment advice is to be provided under the *Impartial Conduct Standards* which incorporated the ERISA prudence standard and the requirement that the investment professional or its financial institution or any affiliate not place its financial or other interests ahead of the retirement investors, as well as the requirements that the compensation be reasonable; that the financial institution and the investment professional must seek to obtain the best execution of the investment transaction; and that no materially misleading statements were made regarding the recommendation transaction and other relevant matters;[86] (2) Written disclosure be made prior to the recommended transaction that the financial institution and its investment professionals are fiduciaries with respect to any fiduciary investment advice, and written disclosure of their material conflicts of interest;[87] (3) Policies and procedures must be established and maintained to enforce the Impartial Conduct Standards; they must mitigate conflicts of interest; and the financial institution must document the rationale for the rollover and account transfer recommendations;[88] (4) The financial institution must engage in an annual review ''reasonably designed'' to avoid violations of the Impartial Conduct Standards, that is written and certified by the Chief Executive Officer or equivalent officer of the financial institution.[89]

The proposal did **not** enlarge the retirement investor's ability to enforce his/her rights in court, **nor** did it create any new legal claims over and above those authorized by ERISA, which had been principal objections from the financial community.[90] By toning down the requirements of the new exemption as compared to the BIC Exemption, the DOL avoid a confrontation with the financial community.

C. 2020 Final Fiduciary Rule: PTE 2020-02

On December 18, 2020, the DOL finalized its new exemption and coined it PTE 2020-02, ''Improving Investment Advice for Workers & Retirees,'' which set forth the new Best Interest Prohibited Transaction Exemption.[91] PTE 2020-02 permits investment advice fiduciaries to receive variable compensation (e.g., commissions, 12b-1 fees, revenue sharing, and markups and mark-downs in certain principal transactions), otherwise prohibited under Title I and II of ERISA, provided the conditions of the exemption are satisfied.

While the new rules were to be effective February 16, 2021, the Preamble to PTE 2020-02 stated that the DOL would not be pursuing enforcement claims for breaches of fiduciary duty or prohibited transactions for the period between 2005 (when the Deseret Letter was issued) and February 16, 2021.[92] On October 25, 2021, the DOL issued FAB 2021-02 which extended the nonenforcement policy from December 21, 2021 through January 31, 2022, for investment advice fiduciaries who were working diligently, and in good faith, to comply with the Impartial Conduct Standards.[93] Hence, Investment Professionals and their Financial Institutions are wrestling with the new rules beginning February 1, 2022, as they become subject to full enforcement. The DOL also extended the nonenforcement policy with respect to the specific docu-

[84] *Id.,* 85 Fed. Reg. 40,834, 40,836.

[85] See Note 80, above, Section V(d).

[86] *Id.,* Section II(a).

[87] *Id.,* Section II(b).

[88] *Id.,* Section II(c).

[89] *Id.,* Section II(d).

[90] *Id.,* 85 Fed. Reg. 40,834, 40,837.

[91] Improving Investment Advice for Workers & Retirees, 85 Fed. Reg. 82,798 (Dec. 18, 2020). The DOL considered whether to delay the effective date of the exemption, pursuant to the memorandum from Ronald A. Klain, Assistant to the President and Chief of Staff, entitled *Regulatory Freeze Pending Review*, but decided that the PTE 2020-02 should go into effect as scheduled. Throughout the discussion of Part IV.C. of this article (2020 Final Fiduciary Rule: PTE 2020-02), defined terms such as Financial Institution, Investment Professional, Affiliate, Retirement Investor, and Impartial Conduct Standards will be capitalized, referring to the specific definition used in Section V to define such persons or entities.

[92] 85 Fed. Reg. 82,798, 82,804. The DOL also allowed FAB 2018-02 to remain in effect until December 20, 2021. 85 Fed. Reg. 82,798, 82,799. *See also* DOL, New Fiduciary Advice Exemption: PTE 2020-02 Improving Investment Advice for Workers & Retirees, Frequently Asked Questions (Apr. 2021).

[93] *See* DOL, News Release, U.S. Department of Labor Announces Temporary Enforcement Policy on Prohibited Transaction Rules Applicable to Investment Advice Fiduciaries, The DOL stated that the new transition relief was provided due to the ''practical difficulties for financial institutions that are in the process of complying with the exemption conditions.'' In footnote four of FAB 2021-02, the DOL states that the Treasury and the IRS, on March 28, 2017, issued IRS Announcement 2017-4, which provides that the IRS will not apply the excise tax provisions of I.R.C. §4975 and the related reporting requirements with respect to any transaction to which the DOL's temporary enforcement policy described in FAS 2017-02, or other subsequent related enforcement guidance, would apply. The Treasury and the IRS confirmed that for purposes of IRS Announcement 2017-4, FAS 2021-02 constitutes ''other subsequent related enforcement guidance.''

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mentation and disclosure requirements for rollovers in PTE 2020-02 through June 30, 2022.[94]

In the Preamble to the new exemption, the DOL gave its thoughts as to how it would be reinterpreting the five-part test as to who is an investment advice fiduciary. The DOL recently put on its regulatory guidance plan its intent to amend the regulatory definition of the term fiduciary set forth in the regulations.[95] It is questionable whether the courts will give deference to the DOL's new interpretation as to who is an investment adviser fiduciary, as its prior interpretation was in existence for the past 46 years.[96]

The remainder of this article is to provide an analysis of the new rules and a guide as to common mistakes that may be made in compliance with the new rules.

1. Preamble Which Reinterprets the 1975 Regulations

In the Preamble to the 2020 Final Fiduciary Rule, the DOL provided its opinion as to how it now interprets the five-part test under the 1975 regulations. It focused particularly on what is a *recommendation* in the context of investment advice; how is it provided on *a regular basis*; and what constitutes a *mutual agreement* between the parties.

As to what it regards as a *recommendation* as to the advisability of investing in, purchasing, or selling securities in the context of a rollover recommendation, the DOL notes that advice to roll over plan assets into an IRA will be considered to be fiduciary investment advice under the five-part definition, even if there is no recommendation as to how to invest the assets in the IRA.[97] The rationale is that a recommendation to roll assets out of one plan and into another results in changes in fees, asset management structures, investment options, and investment service options. Thus, the *Deseret* Letter is revoked prospectively.[98] The DOL's interpretation is prefaced by stating the advice to roll over plan assets must be part of the ongoing advice relationship that satisfies the *regular* basis prong of the five-part test.[99] The DOL rejected that ''regular basis'' is limited to relationships in which the advice is provided at fixed intervals; instead, it describes such relationship as one that is ''recurring, non-sporadic, and expected to continue.''[100] Thus, a single instance of advice to take a distribution or a one-time sales transaction in which there is no ongoing investment advice relationship (nor is there an expectation of such an ongoing relationship) will not be regarded as ''regular.''[101] Likewise, ''sporadic interactions'' between the adviser and the investor do not rise to the level required of ''a regular basis.''[102] The DOL intends to view marketing materials used by advisers in making this determination. The advisers can make it clear in their communications that there is no intent to enter into an ongoing relationship to provide investment advice.[103]

But any *first-time* advice to roll assets over to an IRA that is intended to be the beginning of a long-term relationship (determined at the time of the rollover recommendation) will be deemed to have satisfied ''a regular basis'' requirement.[104] The issue will then be whether the parties reasonably expected an ongoing investment advice relationship at the time the rollover recommendation was made. The DOL confirmed that it does not regard this as a retroactive imposition of fiduciary status. Similarly, where the person making the recommendation to roll assets over expects to make investment recommendations regarding the IRA as part of an ongoing relationship, such recommendation will be regarded as being provided on a regular basis. Here, the DOL does not distinguish between advice given to the retirement investor in a Title I plan, and advice given to the same individual in an IRA, when determining whether there is an ongoing relationship.

Because the term ''rollover'' is defined broadly under the exemption, it covers the following transfer of assets:

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[94] See Note 93, above.

[95] DOL, Definition of the Term ''Fiduciary,'' RIN 1210-AC02 (Fall 2021).

[96] *See National Muffler Dealers Assn., Inc. v. United States*, 440 U.S. 472 (1979), where the Supreme Court questioned an agency's interpretation of a statute with skepticism when it had not been consistent over time.

[97] 85 Fed. Reg. 82,798, 82,803. The DOL states that rollovers from Title I Plans to IRAs are expected to approach $2.4 trillion cumulatively from 2016 through 2020, *quoting* Cerulli Associates, *U.S. Retirement Markets 2019*.

[98] 85 Fed. Reg. 82,798, 82,803–82,804. Thus, the *Deseret* Letter is rescinded prospectively, and the DOL states that it will not pursue claims for rollover advice that would have been covered by such letter. 85 Fed. Reg. 82,806. The DOL mentions that advisory opinions, such as the *Deseret* Letter, are interpretive statements from the agency and thus were not subject to the notice and comment process. 85 Fed. Reg. 82,804.

[99] 85 Fed. Reg. 82,798, 82,805. ''In circumstances in which the investment advice provider has been giving advice to the individual about investing in, purchasing, or selling securities or other financial instruments through tax-advantaged retirement vehicles, . . . the advice to roll assets out of a Title I Plan is part of an ongoing advice relationship. Similarly, advice to roll assets out of a Title I Plan into an IRA where the investment advice provider has not previously provided advice but will be regularly giving advice regarding the IRA in the course of a lengthier financial relationship would be the start of an advice relationship that satisfies the regular basis prong.''

[100] 85 Fed. Reg. 82,798, 82,806.

[101] 85 Fed. Reg. 82,798, 82,805.

[102] *Id.*

[103] *Id.*

[104] 85 Fed. Reg. 82,798, 82,805.

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- From a Title I plan to an IRA;
- From a Title I plan to another Title I plan;
- From an IRA to a Title I plan;
- From an IRA to another IRA; and
- From one type of account to another.[105]

As to whether there is a *mutual agreement* that the investment advice will serve as *a primary basis* for investment decisions, the DOL asserts that it will look to the facts and circumstances surrounding the recommendation and the relationship to ascertain whether those facts gave rise to a mutual agreement that the advice would serve as a primary basis for an investment decision.[106] The DOL states that written disclaimers made by advisers that there is no mutual agreement will not be conclusive, nor will be statements that the adviser is not a fiduciary. Note that if the adviser is relying on the PTE 2020-02 exemption in order to receive certain types of compensation for its investment advice, he/she *must* in fact disclose his/her fiduciary status, which will satisfy the mutual understanding prong of the test.

Likewise, the *primary basis* requirement does not demand proof that the advice was the *sole* and *most important* determinative factor in the investor's decision.[107] The question is whether the advice served as ''a'' primary basis. Hence, the use of the phrase *a primary basis* goes to the materiality of the advice.[108] Similarly, the fact that the investor consulted multiple advisers could lead one to conclude that each outcome was important and enough to satisfy *a primary basis* requirement.[109] But all the elements of the five-part test must be met and if the investor does not act on the recommendation made by the adviser, the adviser will not have liability for such recommendation.

The DOL stated that ''Hire Me'' communications whereby advisers attempt to engage in introductory conversations to advocate for their services will not be treated as fiduciary communications.[110] These types of communications may be relevant when the retirement investor has already made the decision to do a rollover of assets and is now requesting assistance with respect to the investment of those assets. This may be useful for smaller registered investment adviser firms that can supervise and train investment professionals. They may choose to design educational brochures that investment professionals can hand to investors regarding investment choices.

2. Applicable Terms and Conditions of PTE 2020-02

The final prohibited transaction, PTE 2020-02, followed closely its proposal. It retains the proposal's wide protective framework, including the Impartial Conduct Standards; disclosures, including a written acknowledgment of fiduciary status; policies and procedures prudently designed to ensure compliance with the Impartial Conduct Standards and that mitigate conflicts of interest; and a retrospective compliance review.[111] The conditions of the exemption were designed to ensure that financial institutions will assess all sources of fees and revenue to identify and mitigate conflicts of interest and to receive no more than reasonable compensation in connection with investment advice transaction.[112] The exemption allows prohibited transactions that otherwise would arise due to the payment of prohibited compensation in connection with the recommendation of a security or investment product or a rollover recommendation.

PTE 2020-02 is divided into **five** Sections:

- Section I sets forth what *transactions* permit Investment Professionals and Financial Institutions who provide fiduciary investment advice to Retirement Investors to receive otherwise prohibited compensation. It also notes that the exemption excludes certain plans and transactions.

- Section II sets forth the terms that govern those transactions: the new Impartial Conduct Standards; new disclosure requirements; new policies and procedures to ensure that the Impartial Conduct Standards are met; a retrospective review by the Financial Institution to detect and prevent violations of the Impartial Conduct Standards; and a self-correction mechanism to be utilized to avoid a violation of the conditions of the exemption.

- Section III is labeled ''Eligibility,'' but describes those Investment Professionals and Financial Institutions who may be ineligible to rely on the exemption due to a criminal conviction under ERISA or due to the DOL's determination.

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[105] 85 Fed. Reg. 82,798, 82,803, n.33, and 82,830. The DOL does not specify what is meant by a transfer of assets from one type of account to another but provides an example whereby assets are transferred from a commission-based account to a fee-based account.

[106] 85 Fed. Reg. 82,798, 82,805.

[107] 85 Fed. Reg. 82,798, 82,808.

[108] *Id.*

[109] *Id.*

[110] 85 Fed. Reg. 82,798, 82,809.

[111] 85 Fed. Reg. 82,798, 82,799.

[112] 85 Fed. Reg. 82,798, 82,816. Thus, Financial Institutions and Investment Professionals may receive various sources of compensation such as 12b-1 fees, revenue sharing, sales loads, principal transactions, or propriety products.

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- Section IV requires certain records be maintained for a period of six years.
- Section V sets forth the definitions of specific terms utilized throughout the exemption.

a. Who Are the Covered Parties Subject to the Exemption?

In its definitional section of PTE 2020-02, *Financial Institutions* includes SEC and state registered investment advisers, broker-dealers, insurance companies, and banks, who employ Investment Professionals.[113] However, a record-keeper to a plan or IRA that is not also a bank, broker-dealer, insurance company, or registered investment adviser would not be covered.[114] *Investment Professionals* are defined to include an individual who is a fiduciary to the plan or IRA by reason of providing investment advice; who is an employee, independent contractor, agent, or representative of a Financial Institution; and who satisfies federal and state regulatory requirements of insurance, banking, and securities laws with respect to the covered transaction.[115] By capturing employees, independent contractors, agents, or representatives of a Financial Institutions, the DOL has taken a very broad approach as to who must rely on the PTE. An *Affiliate* of a Financial Institution or an Investment Professional is defined as a person or entity within the control (i.e., power to exercise a controlling influence over the management or policies) of the Financial Institution or the Investment Professional; any officer, director, partner, employee or relative of the Financial Institution or the Investment Professional; or any corporation or partnership of which the Financial Institution or Investment Professional is an officer, director, or partner.[116]

Retirement Investors are defined to include (1) a participant or beneficiary of a plan with authority to direct the investments of his account assets or to take a distribution (2) the beneficial owners of an IRA acting on behalf of the IRA or (3) a fiduciary of a plan or an IRA.[117] Unlike prior proposals, the definition of a plan is not based on the size of the plan assets.

The exemption explicitly *excludes*: (1) Title I plans where the Investment Professional, Financial Institution, or an Affiliate is the employer of the employees covered under the plan; (2) transactions involving investment advice generated solely by an interactive website in which computer software-based models or applications provide investment advice based on the personal information supplied by the Retirement Investor; (3) transactions involving the Investment Professional acting in its fiduciary activity other than as an investment advice fiduciary (e.g., the transaction relates to discretionary management transactions or arrangements).[118]

b. What Are the "Covered Transactions"?

To better understand what transactions are covered by the exemption, the author has provided some background information for those less knowledgeable about securities laws. When an investor wishes to purchase stock, he/she can work through a Financial Institution and purchase the stock in either a principal transaction or an agency transaction. A principal transaction is one in which the Financial Institution buys and sells the requested securities out of *its own inventory* in order to fulfill the investor's request. In contrast, an agency transaction is one in which the Financial Institution acts as an agent for the investor. A broker-dealer generally acts as a "dealer" in a principal transaction and as a "broker" in an agency transaction. For example, the investor asks the broker to purchase a share of stock and the dealer acts as the counterparty and sells the stock to the investor out of its own inventory. In contrast, in an agency transaction, the broker would purchase the stock in the marketplace for his/her account (taking on the role of principal), in order to offset the transaction with the investor.

When a broker-dealer acts in a principal transaction, he/she is compensated for executing the transaction by assessing a "markup" or "markdown" on the market price of the stock being purchased or sold. In the case of a sale, a markup is the difference between the price of the stock that the broker paid in the market and the price the dealer receives from the investor. In the case of a purchasing, the market price of the stock is increased by an amount that the dealer assessed for the transaction. Due to the adviser's ability to receive price spreads from principal transactions, the DOL is troubled that such transaction could bias the adviser's recommendation.

Under PTE 2020-02, the DOL makes a distinction between a *riskless principal transaction* and a principal transaction that is not riskless (referred to as a *nonriskless principal transaction*). A *nonriskless principal transaction* is one in which the Investment Professional or Financial Institution is purchase from or

[113] 85 Fed. Reg. 82,798, Section V — Definitions (e). This definition is based on the entities set forth in the statutory exemption for investment advice under ERISA §408(b)(14) and I.R.C. §4975(d)(17).

[114] 85 Fed. Reg. 82,798, 82,814.

[115] 85 Fed. Reg. 82,798, Section V — Definitions (h).

[116] 85 Fed. Reg. 82,798, Section V — Definitions (a). In the Preamble, the DOL notes that foreign affiliates were not excluded from the definition of an affiliate. 85 Fed. Reg. 82,798, 82,814.

[117] 85 Fed. Reg. 82,798, Section V — Definitions (k).

[118] 85 Fed. Reg. 82,798, Section I — (c).

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selling to the plan, the participant or beneficiary account, or IRA a security or other investment from the account of the Financial Institution or its affiliate. Because the Investment Professional or Financial Institution is on both sides of the transaction, there is a clear and direct conflict of interest. Not only does the adviser earn the commission on the sale, it may also earn extra income on the bid-ask spread. In addition, such transactions typically lack pre-trade price transparency and as such, the investor may not be able to evaluate the fairness of the transaction.

In contrast, a *riskless principal transaction* is one in which the Financial Institution, after receiving an order from the plan or IRA investor to purchase or sell an asset, executes an identical order in the marketplace, taking on the role of principal to fill the order. A riskless principal transaction is more akin to an agency transaction and thus, poses less of an inherent conflict of interest. FINRA requires such trades be executed at the same price, exclusive of a markup/markdown, commission, or other fees. For example, a broker who, upon getting investor A's order to buy 1,000 shares of ABC at the current price of $10/share, must buy 1,000 shares of ABC at $10 from another broker. As both trades were executed at $10/share (excluding commissions), it is a riskless principal transaction.[119]

Principal transactions that are *riskless principal transactions* are covered under the exemption and thus, permitted if the other conditions are met. However, principal transactions that are *non-riskless principal transactions* are subject to additional limitations under the exemption:

- For *purchases from* a plan or an IRA, the transaction can involve any security or other investment property.[120]
- For *sales to* a plan or an IRA, the transaction is limited to transactions involving: U.S. dollar denominated corporate debt securities; U.S. Treasury securities; debt securities issued or guaranteed by a U.S. federal government agency other than the U.S. Department of Treasury; debt securities issued or guaranteed by a government-sponsored enterprise (GSE); municipal securities; certificates of deposit; and interests in Unit Investment Trusts.[121]

c. Conditions of the Exemption

For Financial Institutions, Investment Professionals, and their Affiliates to engage in covered transactions as a result of providing investment advice, the following conditions of the exemption must be met in order to receive variable compensation:

i. The **first** condition is adherence to the *Impartial Conduct Standards*. This condition envisions three parts: **First**, the investment advice must be in the ''best interest'' of the retirement investor (i.e., a prudence standard) and may not place the financial interest or other interests of the Financial Institution, Investment Professional, or its Affiliate *ahead* of the interest of the Retirement Investor (i.e., a loyalty standard).[122] The loyalty standard was intended to be on par with the standard set forth in the SEC's Reg BI and the SEC's interpretation regarding the conduct standard for investment advisers. The new standard deleted the prior BIC Exemption requirement that the fiduciary to act ''without regard'' to his/her own interest, which would have been more consistent with ERISA Title I's duty of loyalty (i.e., to act for the exclusive benefit of the plan participants and beneficiaries). **Second**, the exemption sets forth a reasonable compensation standard, such that the Financial Institution, Investment Professional, or their Affiliates or related entities are not to receive compensation in excess of what is ''reasonable compensation,'' within the meaning of ERISA §408(b)(2) and I.R.C. §4975(d)(2). The factors the DOL will consider in determining reasonableness of the compensation include: the nature of the services provided; the market price of the services and/or the underlying assets; the scope of monitoring; and the complexity of the product.[123] For example, when faced with two investments equally available to the investor, the adviser is not permitted to advise one over the other based on the Investment Professional's or the Financial Institution's bottom line.[124] This part also invokes a best execution standard such that, consistent with federal securities law, the Financial Institution and the Investment Profes-

[119] 85 Fed. Reg. 82,798, 82,816.

[120] 85 Fed. Reg. 82,798, Section V — Definitions, (d)(2).

[121] 85 Fed. Reg. 82,798, Section V — Definitions, (d)(1).

[122] 85 Fed. Reg. 82,798, Section II — Investment Advice Arrangement (a)(1). This prudence standard requires the investment advice to ''reflect the care, skill, prudence, and diligence under the circumstance 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.''

[123] 85 Fed. Reg. 82,798, 82,824. What is reasonable is a facts and circumstances determination. For example, when faced with two investments equally available to the investor, the adviser is not permitted to advise one over the other based on the adviser's or the financial institution's bottom line.

[124] *See* New Fiduciary Advice Exemption: PTE 2020-02, Improving Investment Advice for Workers & Retirees, Frequently Asked Questions, Q&A 12 (Apr. 2021).

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sional must seek to obtain the best execution of the investment transaction reasonably available under the circumstances.[125] **Third,** the standard requires that the statements made by the Financial Institutions and its Investment Professionals made to the Retirement Investor about the recommended transaction and other relevant matters not be materially misleading at the time they are made.[126]

ii. The **second** condition involves disclosures. Prior to engaging in any transaction pursuant to the exemption, the Financial Institution is required to disclose in writing:

- Its acknowledgment that the Financial Institution and its Investment Professional are fiduciaries under Title I and/or the Code, as applicable, with respect to the investment advice being provided to the investor;[127] and
- A description of the services to be provided, and the material conflicts of interest arising out of the services and any recommended investment transaction.[128]
- Examples provided of material conflicts of interest required to be disclosed include conflicts inherent in recommending proprietary products, payments from third parties, and certain compensation arrangements.[129] In the context of a recommendation to roll monies over to an IRA managed or advised by the adviser, the conflict of interest resulting in the payment of *additional* compensation should also be disclosed. The description must be accurate in all material aspects. The purpose of the disclosure requirements is to reinforce the exemption's focus on conflict mitigation and to promote consumer choice, such that the investor has a clear understanding of the nature of the relationship between him/her and the adviser.[130]
- In the context of a rollover recommendation, there must be a documentation, given *prior* to engaging in the rollover, as to the specific reasons that such rollover is in the best interest of the investor.[131] Because the decision to roll assets over from a Title I plan to an IRA may be one of the most important financial decision a Retirement Investor makes due to the impact it has on his/her legal rights and remedies, the DOL wants the rationale for such decision to be documented and to serve as a record for later review.[132] This will undoubtedly be the most difficult part of the exemption to comply with, as it depends on so many variables. Such documentation will also be the most critical document for plaintiff attorneys and the DOL regulators, when reviewing whether the terms of the exemption were satisfied. Thus, there will be five steps needed for compliance in the typical rollover from an employer's plan to an IRA: (1) information about the participant's existing plan investments (e.g., portfolio of investments offered, costs and expenses); (2) information about the plan; in this regard the DOL believes that the disclosure statement required under ERISA §404(a)[133] would be a good starting point; (3) information about the IRA to which the

[125] 85 Fed. Reg. 82,798, Section II — Investment Advice Arrangement (a)(2)(A). Such federal securities law include the Securities Act of 1933, the Securities Exchange Act of 1934, and the Investment Advisers Act of 1940, as well as rules adopted by FINRA and the Municipal Securities Rulemaking Board (MSRB).

[126] 85 Fed. Reg. 82,798, Section II — Investment Advice Arrangement (a)(3). In this regard, the DOL provides an example in which a financial institution's inclusion of exculpatory language (clearly prohibited under state law) would be misleading as it would dissuade a retirement investor from asserting legal rights otherwise available to him/her. *See* Preamble, 85 Fed. Reg. 82,826.

[127] 85 Fed. Reg. 82,798, Section II — Investment Advice Arrangement (b)(1). In this regard, the DOL provides model fiduciary acknowledgment language in the preamble: "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 interest, so we operate under a special rule that requires us to act in your best interest and not put our interest ahead of yours." The DOL also acknowledges in the preamble that such fiduciary acknowledgment is not intended to create a private right of action between a financial institution or investment professional and the retirement investor. *See* Preamble, 85 Fed. 82,826–82,828. Also, note that while some fiduciaries have acknowledged their status as a fiduciary under Title I of ERISA, they have not done so in the context of being a fiduciary under Title II of ERISA.

[128] 85 Fed. Reg. 82,798, Section II — Investment Advice Arrangement (b)(2).

[129] 85 Fed. Reg. 82,798, 82,829.

[130] 85 Fed. Reg. 82,798, 82,829.

[131] 85 Fed. Reg. 82,798, Section II — Investment Advice Arrangement (b)(3).

[132] 85 Fed. Reg. 82,798, 82,830.

[133] The DOL Reg. §2550.404a-5 set for the plan fiduciary's disclosure requirements for the allocation of investment responsibilities to participants or beneficiaries: their rights and responsibilities with respect to the investment assets held within their account; fees and expenses assessed against their accounts; and designated investment alternatives, including fees and expenses, available for the participant or beneficiary.

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funds will be rolling into, particularly if the IRA involves increased costs, and why the added benefits justify such costs; (4) in light of the participant's needs and circumstances (e.g., is he/she retiring and entering into a decumulation stage, as opposed to accumulation stage), the reasons why the IRA rollover is in the best interest of the participant; and (5) written documentation of the specific reasons for recommending a rollover.[134]

Factors that the Financial Institution and Investment Professional may wish to highlight with a rollover recommendation include:

- Alternatives to a rollover available to the Retirement Investor, including leaving money in his/her current employer plan, rolling assets into an IRA, or transferring monies into a new employer plan, if available;
- The fees, services, and investment options available under each option, and whether the employer currently pays for some or all of the plan's administrative expenses;
- The longer-term impact of an increase in costs due to the compounding of interest;
- The effect of significant features such as surrender schedules and participation rates; and
- For rollovers from another IRA or changes from a commission-based account to a fee-based arrangement, consideration and documentation of services to be provided under the new arrangement.[135]

The new disclosure requirements are to be written in plain English and must take into account the Retirement Investor's level of financial experience. They may be satisfied through a single disclosure or combination of disclosures, some of which may be required by other regulators.[136] The disclosures are to be provided prior to the transaction, but the DOL notes that the parties wishing to provide the disclosure at the time of the recommendation would be permitted to do so.[137]

iii. The **third** condition of the exemption involves policies and procedures. This part of the exemption requires Financial Institutions to establish, maintain, and enforce written policies and procedures prudently designed to ensure compliance with the Impartial Conduct Standards.[138] Such policies and procedures "are required to mitigate conflicts of interest to the extent that a reasonable person reviewing the policies and procedures and incentive practices as a whole would conclude that they do not create an incentive for a Financial Institution or Investment Professional to place their interests ahead of the interest of the Retirement Investor."[139] Such standard requires that incentives must be mitigated to make Financial Institutions identify and focus on any conflicts of interest in their business models that could create incentives to place their interests ahead of the interest of the investor.[140] The DOL's intent with this condition is to force Financial Institutions to identify and to focus on any conflicts of interest in their business models that could create incentives to place their interests ahead of the interests of the investor.[141] This requirement will pose practical problems for Financial Institutions who have relied upon sales incentives to increase business.

The DOL acknowledges that regulators in the securities and insurance industries have similar requirements as to having policies and procedures in place for registered investment advisers to eliminate sales contests and similar incentive programs.[142] In the securities space, the challenge has been to avoid making policies and procedures too detailed such that they can't be flexible when circumstances changes; to test and enforce their compliance based on current resources; and to identify who is responsible for supervising those subject to the policies and procedures.

Inherent in this third condition is to have the Financial Institutions to periodically review the policies and procedures to ensure they are ac-

[134] 85 Fed. Reg. 82,798, 82,830–82,832.

[135] 85 Fed. Reg. 82,798, 82,831.

[136] 85 Fed. Reg. 82,798, 82,829. Examples of other regulatory disclosures that may be used to satisfy this condition include the SEC's Form ADV or Form CRS, applicable to registered investment advisers; disclosures required under insurance and banking laws when such disclosures cover services to be provided and the Financial Institution's and Investment Professional's material conflicts of interest.

[137] 85 Fed. Reg. 82,798, 82,832.

[138] 85 Fed. Reg. 82,798, Section II — Investment Advice Arrangement (c)(1).

[139] 85 Fed. Reg. 82,798, 82,832.

[140] *Id.*

[141] 85 Fed. Reg. 82,798, 82,834.

[142] *Id.*

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complishing their intended purpose.[143] Hence, to the extent new products, lines of business, or compensation packages are newly established, the Financial Institution should consider how to adjust their policies and procedures accordingly.

iv. The **fourth** condition mandates a retrospective review by the Financial Institution. This condition requires the Financial Institution to conduct an annual retrospective review to detect and prevent violations of the exemption, and to achieve compliance with the Impartial Conduct Standards and the policies and procedures.[144] As such, the Financial Institution will be required to monitor the conduct of their Investment Professionals to assure compliance with the exemption. The methodology and results of the retrospective review must appear in a written report provided to one of the financial institution's senior executive officers (e.g., chief executive officers, chief financial officers, president, or any one of the three most senior officers).[145] Such report must be certified by a Senior Executive Officer of the Financial Institution as follows:

- He/she has reviewed the report;
- The Financial Institution has in place policies and procedures prudently designed to assure compliance with the exemption;
- The Financial Institution has in place a prudent process to modify its policies and procedures as changes and events dictate, and to evaluate the effectiveness of its policies and procedures on a regular basis to ensure compliance; and
- The report has been completed no later than six months following the end of the period covered by the review, and the report, its certification, and its supporting data must be maintained for a period of 6 years.[146]

This annual certification may be too daunting for small investment firms, forcing them to take the educational route in advising Retirement Investors.

v. The **fifth** condition of the exemption involves self-correction. The DOL has provided a method of self-correction under the exemption such that a non-exempt prohibited transaction will not be deemed to have occurred if:

- Either the violation resulted in no investment losses to the Retirement Investor, or the Financial Institution made the Retirement Investor whole for any resulting losses;
- The Financial Institution corrects the violation and notifies the DOL via email within 30 days of correction;
- The correction occurs no later than 90 days after the Financial Institution learned of the violation or reasonably should have learned of the violation; and
- The Financial Institution notifies the persons responsible for conducting the retrospective review during the applicable cycle, and the violation and correction are duly noted in the written report of the retrospective review.[147]

vi. The **sixth** condition of the exemption focuses on who is eligible to utilize it. While the section of the exemption is labeled ''Eligibility,'' it sets forth those Financial Institutions and Investment Professionals who are ineligible to invoke the exemption because they, within the previous 10 years, were convicted of certain crimes arising out of their provision of investment advice to Retirement Investors.[148] They may also be ineligible if the DOL notifies them that they have engaged in systematic or intentional violations of the exemption's provisions or provided materially misleading information to the DOL in relation to their conduct pursuant to the exemption.[149]

3. Effective Dates

The DOL announced that FAB 2018-02 would remain in effect until December 20, 2021.[150] The effective date of PTE 2020-02 was originally February 16, 2021.[151] Due to the difficulties for Financial Institutions to implement the disclosures conditions of the exemption, the DOL gave two extensions to the effective date in PTE 2020-02:

- January 31, 2022, whereby the DOL and the IRS would not enforce the conditions of the exemption for Financial Institutions and Invest-

[143] 85 Fed. Reg. 82,798, 82,836.

[144] 85 Fed. Reg. 82,798, Section II — Investment Advice Arrangement (d)(1).

[145] 85 Fed. Reg. 82,798, Section II — Investment Advice Arrangement (d)(2). The retrospective review is based on FINRA rules applicable to broker-dealers. *See* 85 Fed. Reg. 82,798, n.131, 82,838.

[146] 85 Fed. Reg. 82,798, Section II — Investment Advice Arrangement (d)(3)(A)–(C), (d)(4), and (d)(5).

[147] 85 Fed. Reg. 82,798, Section II — Investment Advice Arrangement (e)(1)–(4).

[148] 85 Fed. Reg. 82,798, Section III — Eligibility (a)(1).

[149] 85 Fed. Reg. 82,798, Section III — Eligibility (a)(2).

[150] 85 Fed. Reg. 82,798, 82,799.

[151] 85 Fed. Reg. 82,798, 82,799.

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ment Professionals "who are working diligently and in good faith to comply with the Impartial Conduct Standards for transactions that are exempted in PTE 2020-02;"[152] and

- June 30, 2022, whereby the nonenforcement approach would extend to the specific documentation and disclosure requirements set forth for rollovers in the exemption.[153] All other parts of the exemption become subject to full enforcement beginning on February 1, 2022.

One may ask if there are any alternatives to complying with PTE 2020-02. To avoid application of the new rules, the Investment Professional may argue that he/she has engaged in only "hire me" communications, so as to begin an introductory conversation with the investor. An adviser may also argue that all five elements of the DOL regulations have not been met, and thus he/she is not a fiduciary. However, the DOL has stated in the Preamble that disclaimers do not negate the adviser being held to be a fiduciary.[154] Finally, the Financial Professional may decide to rely on only information and education, consistent with Interpretive Bulletin 96-1,[155] as to investment options available to the Retirement Investor. Here, the Financial Professional must guard against making any explicit or implied investment recommendations.

4. Enforcement Efforts

For those Investment Professionals and Financial Institutions who fail to satisfy all the conditions of the exemption, various sources of liability include:

- Filing of the Form 5330 to the IRS and payment of I.R.C. §4975 imposes an excise tax of 15% on the amount involved for the plan or IRA (increased to 100% of the amount involved is the prohibited transaction is not timely corrected);
- ERISA Title I subjects an investment advice fiduciary to claims for breach of fiduciary duty under ERISA §502(a)(2) and equitable relief (e.g., removal of the fiduciary) under ERISA §502(a)(3) *initiated by the DOL* for claims related to plans (as well as possible penalties equal to 20% of any "amount recovered" by the DOL pursuant to litigation or a settlement agreement, under ERISA §502(1)); such liability would not be applicable for IRAs; and
- Breach of fiduciary duty and equitable relief under ERISA §502(a)(2) and ERISA §502(a)(3) *initiated by the plan or participants/beneficiaries* for losses incurred or disgorgement of wrongful profit or undue enrichment.

On April 13, 2021, the DOL released FAQs on PTE 2020-02, which listed 21 questions and answers.[156] In question 21, the DOL addressed the question as to how it was going to enforce compliance with the exemption. In its answer, the DOL stated that it had both *investigative* and *interpretive* authority as to exemption compliance. For those plans covered by Title I of ERISA, the DOL plans on investigating for compliance with the exemption and enforcing the protections afforded under Title I (i.e., the statutory causes of action under ERISA §502).[157] For IRAs and other non-Title I plans, the DOL states that it has interpretive authority to determine whether the exemption conditions have been satisfied and that it will transmit information to the IRS regarding the enforcement of Title II's excise tax. It is not clear how the DOL through its investigatory processes would be in a position to know whether Title II's plans are in compliance with the exemption. A question exists as to whether the DOL's ability under ERISA §502 to request documents in connection to an investigation would be considered an "interpretation."[158]

D. Common Pitfalls for Investment Advisers to Watch for in Complying With PTE 2020-02

The following highlights common pitfalls that Financial Institutions and their Investment Professionals may make, running afoul of the DOL's final rules.[159] Under the federal securities law, a fiduciary can have its duty waived, whereas ERISA's PTE rules impose strict liability and require a fiduciary to satisfy the conditions of the exemption in order to act.

1. Implied Recommendations

Financial advisers may not realize that a recommendation that is implied may nevertheless be subject to the new exemption. For example, simply proposing an investment strategy for a rollover IRA to a retirement investor for a fee will fall within the parameters

[152] DOL Field Assistance Bulletin No. 2021-02 (Oct. 25, 2021).

[153] *Id.*

[154] 85 Fed. Reg. 82,798, 82,805.

[155] Interpretive Bulletin 96-1; Participant Investment Education, 61 Fed. Reg. 29,586 (June 11, 1996).

[156] *See also* New Fiduciary Advice Exemption: PTE 2020-02 Improving Investment Advice for Workers & Retirees Frequently Asked Questions, Frequently Asked Questions (Apr. 2021).

[157] *Id.* at Q&A 21.

[158] *See* Groom Law Group, DOL Releases FAQs on PTE 2020-02, Foreshadows Future Activity on Investment Advice/(Apr. 16, 2021).

[159] The author would like to thank attorneys Jeffrey Blumberg, Joan Neri, Fred Reish, and Joshua Waldbeser of Faegre Drinker for hosting a webinar which highlights these common mistakes in complying with DOL PTE 2020-02, entitled DOL PTE 2020-02 Disclosures and Policies — Common Mistakes.

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of the DOL's regulations, making the adviser an investment advice fiduciary. The DOL certainly believes statements from the investment adviser, such as ''If I were you, I'd invest in the following . . .'' involve an implied recommendation. Hence to avoid that result, advisers will have to draft their information in a more general or objective format — with no implied recommendations. In the rollover context, information should be more general and totally objective as to pros and cons of making a distribution from a Title I plan, as well as the legal consequences for rolling such assets into an IRA. While practitioners will be examining Interpretative Bulletin 96-1 to see what constitutes education and not advisement, that bulletin was designed for participants in a 40(k) plan, but not rollover decisions. But if the investment firms decide to go the educational route, in order to avoid fiduciary status, they will need to document their materials and supervise their advisers through ongoing training.[160]

2. Rollovers Include More Than Plan to IRA Transfers

Due to the expansive definition of a ''plan'' for Title II's fiduciary rules, financial advisers may think that only rollovers from Title I plans to IRAs are covered, not realizing that the following are also covered by the exemption: a rollover from a plan to another plan; a rollover from an IRA to a plan; a rollover from one IRA to another IRA; or a rollover from one type of account to another. As to the latter rollover, the DOL indicates that moving from a commission-based account to a fee-based account is also covered as rollovers, but it doesn't elaborate as to other types of accounts that could be covered. Hence, all five of these types of rollovers are subject to the conditions of the exemptions. It is unclear if an investor wishes to roll from a traditional IRA to a Roth IRA, whether that advice covered or is it regarded as tax, and not investment, advice.

3. Meaning of IRA More Expansive Than Realized

Advisers may not realize that the term ''IRA'' is defined more broadly than just Individual Retirement Accounts and Individual Retirement Annuities, but also include MSAs, HSAs, and Coverdell Education Savings Accounts. Under Title II's fiduciary rules, the term ''plan'' includes:

- A retirement plan qualified under I.R.C. §401(a) or plan described in I.R.C. §403(a);
- An IRA;
- An Archer MSA;
- An HSA;
- A Coverdell education savings account; and
- A plan determined by the DOL to be described in one of the plans noted above. This excludes governmental plans, church plans (unless they elect to be subject to the qualification rules of I.R.C. §401(a)), and I.R.C. §457 plans.

4. Not Knowing When a Prohibited Transaction Occurred

A prohibited transaction occurs when compensation (e.g., advisory fees) is paid to the adviser or its financial firm as a result of ''conflicted'' recommendations. Hence, financial advisers may not realize when a prohibited transaction has occurred when either they or an affiliate of theirs receives compensation, and therefore, is in need of a PTE. The following are examples of conflicted recommendations, which trigger the exemption:

- An adviser recommends to an IRA owner to transfer his/her funds into an IRA managed by the adviser (e.g., by using proprietary funds);
- An adviser makes a recommendation to a plan or IRA regarding certain investments, such that investing in those investment will result in a revenue sharing payment or marketing allowance from the provider to the adviser;
- An adviser recommends to the plan that the adviser or its financial institution could manage the participants' account; or
- An adviser recommends that the plan or IRA invest in a proprietary investment product that results in an investment management fee to an affiliate of the adviser or its financial institution.

5. Not Knowing That Conflicts of Interest Must Be Mitigated

The DOL's PTE 2020-02 requires both the adviser and his/her financial institution to mitigate any conflicts of interest. To achieve this, the financial institution must have a strict process in place for making the type of recommendation it is making, and then must supervise that process. This must be true, not only for the financial institution, but also for its investment professionals. For example, the adviser wishes to recommend to the IRA owner that he/she should roll such monies into a different IRA. As the adviser will draw upon more compensation if the rollover occurs, he/she must document the process used in making such the recommendation and the financial firms must supervise its agents to assure the process is being fol-

[160] See Note 53, above, whereby FINRA cautioned investment firms to supervise their advisers through training so that they do not make an implied recommendation.

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lowed. In this example, the following steps should be considered by the investment adviser in the context of a rollover from one IRA to another IRA:

- The adviser must collect sufficient information to understand where the investor is relative to retirement (e.g., is the investor still working and thus, in the accumulation phase; alternatively, if the investor has retired, and thus, in the deaccumulation phase, what other considerations should be examined on the part of the adviser?).
- The adviser needs to secure information about the original IRA, perhaps using the IRA owner's quarterly statements, in order to ascertain fees and services being charged to the IRA owner's account.
- Since the adviser is recommending a rollover to another IRA (with the adviser's firm), he/she must consider what new investments and services that it could provide to the IRA owner.
- The adviser must then analyze the original IRA's statements to see how the investor has directed the account in the past, so that he/she can determine what investments, services, and fees are available under the second IRA.
- With all the information combed above, the adviser must determine what is in the best interest of the investor. The reasons for recommending the rollover must be documented in writing, beginning July 1, 2022.

6. Deficient Fiduciary Acknowledgments

Most of the disclosures required by PTE 2020-02 must be made *before* the time in which the transaction occurs. One of these required disclosures is the fiduciary acknowledgment form, whereby the advisers and their financial institutions, acknowledge that they are fiduciaries for purposes of Title I of ERISA and/or fiduciaries for purposes of Title II of ERISA. The DOL provides model language that can be used, which looks similar to the disclosure made under the federal securities' Form ADV.[161] As the DOL permits advisers and their Financial Institutions to use information disclosed to other federal agencies (e.g., the SEC), Financial Institutions will be examining current disclosure forms to see if they can used for purposes of PTE 2020-02.

7. Assessing Reasonableness of Compensation Paid

PTE 2020-02 requires, through its Impartial Conduct Standards, that the compensation received by the adviser and his/her financial firm cannot exceed reasonable compensation. The DOL intends to use a market-based standard — one that compares the fees received by the adviser and his/her financial institution for the services rendered to those fees assessed in the marketplace.[162] To comply with this requirement, advisers and their financial firms will have to either compare their fees to other advisers providing comparable services, or rely on benchmarking services. Hence, financial institutions will need to devise policy and procedures regarding their fee schedules. Note, in this regard, the SEC's view on the reasonableness of compensation depart from the DOL's view, as the SEC simply requires the registered investment adviser to disclose that comparable service may be available from other advisers at lower costs.

8. Best Interest Process Requires More than the "Investor Prefers Me"

Relying on the rationale that the ''Investor Prefers Me'' is likely insufficient to meet the best interest standard as it requires the adviser to know the investor's risk tolerance, financial circumstances, and investment objectives in making a recommendation as to investments. In turn the Financial Institution's policies and procedures should reflect that the adviser has adhered to this best interest standard.

9. Best Interest Process Requires Consideration of All Costs

The adviser must understand that the best interest standard requires the evaluation of *all costs* of the recommended investments (e.g., expense ratios), as well as the cost of the adviser's services. In the context of a rollover recommendation, the adviser must analyze the services, fees, and investment of each option (e.g., staying put in the employer plan or rolling into an IRA) in ascertaining what is in the best interest of the investor relative to his/her risk tolerance, investment objectives, and financial circumstances.

10. Best Interest Process Requires Information Regarding the Plan

In satisfying the documentation required for a recommended rollover from a plan to an IRA, the DOL requires that the adviser and his/her related financial institution make diligent and prudent efforts regarding information about the investor's existing employee benefit plan. This would suggest that the adviser provide the investor with a full explanation as to why he/she needs such information. If such information is not

[161] Form ADV is the uniform form used by investment advisers to register with both the SEC and state securities authorities.

[162] Note the SEC's position on reasonableness of compensation is dramatically different. As long as a registered investment adviser discloses that services rendered are available through other firms at a lower cost, the adviser has conformed to his fiduciary duty for securities' law purposes.

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otherwise available, the DOL allows the investor to use alternative data sources, such as the plan's Form 5500, as well as reliable benchmarks on the customary fees assessed by type and size of the plan in question. If the adviser relied upon this outside information, he/she should document and explain why the information was utilized.

11. Best Interest Process Requires Certain Documentation

Advisers and their financial institutions will be required, as of July 1, 2022, to provide documentation as to why a rollover recommendation was made, and why it is in the best interest of the investor. Prior to the July date, financial institutions should be developing the best interest processes and documenting such processes

V. CONCLUSION

Due to the Fifth Circuit's vacatur of the 2016 Fiduciary Rules, the DOL was forced to reinstate the 1975 investment advice fiduciary regulations, but had to reinterpret such regulations as it wished to expand the universe of those who would be found to be investment advice fiduciaries. It made known its opinion in the Preamble of the most recent exemption (PTE 2020-02), that it has changed its determination of what is an investment *recommendation* (so as to include a rollover recommendation); expanded its notion of what is *a regular basis* needed to subject an adviser as to who is an investment advice fiduciary (allowing the rollover recommendation to be the starting point for such regular basis); and modified its notion of what constitutes a *mutual understanding* between the parties (prohibiting exculpatory clauses to disclaim such understanding). The DOL will set forth its new interpretation of an investment advice fiduciary in its regulations to be proposed, hopefully during 2022, which will be open for comment and discussion. It also will begin reinterpreting many of the outstanding PTEs that provided for certain compensation to be paid to investment advice fiduciaries.[163] As its new PTE 2020-02 better aligns with the SEC's Regulation Best Interest, it's likely not to prompt the kind of fury that the financial community exhibited to the 2016 Fiduciary Rules. However, much more disclosure and documentation is needed under PTE 2020-02 than under federal securities law. There is an outstanding lawsuit challenging the DOL's new rules, so it will be important to see how that lawsuit is resolved.[164] In the meantime, the financial community appears to be gearing up to comply with the new rules, which became effective as of February 1, 2022, except for the disclosure requirements applicable to rollover recommendations which have been further extended until June 30, 2022.

[163] 85 Fed. Reg. 40,834, 40,856.

[164] See *Federation of Americans for Consumer Choice v. U.S. Department of Labor*, No. 3:22-cv-00243-K (filed N.D. Tex. Feb. 2, 2022). The case seeks to vacate the DOL's interpretation of the five-part test articulated in the preamble to PTE 2020-02.

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