



# Washington Pulse

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## DOL Releases Final PTE on Investment Advice

The Department of Labor (DOL) has released [Prohibited Transaction Exemption \(PTE\) 2020-02](#), which addresses how a financial organization or financial professional can receive certain compensation that would otherwise violate the prohibited transaction rules. This DOL class exemption and interpretation—entitled *Improving Investment Advice for Workers & Retirees*, is important for those who provide investment services to retirement plan participants, IRA owners, retirement plan and IRA beneficiaries, and plan fiduciaries. The PTE becomes effective on February 16, 2021, and outlines the factors that determine whether financial professionals are considered fiduciaries—while giving clear guidance about how fiduciaries must comply with their responsibilities.

In July 2020, the DOL released the proposed investment advice PTE. At that time, Ascensus published a [Washington Pulse](#), which detailed the provisions of the proposed guidance. Because the final PTE is similar to the proposed PTE, this article will focus on the final PTE's modified guidance and its practical implications.

### Background

Guidance on investment advice creating fiduciary duties has evolved throughout the years.

- **Giving investment advice may create a fiduciary duty.** Fiduciary duty—a legal concept with important implications for retirement plans—requires certain people to act with the utmost care when they serve in a particular role. While this duty may apply in numerous situations, it is especially relevant in retirement plans when one person owes this special duty of care to another. For example, this includes an employee benefit plan administrator, who must, among other things, administer the plan in the participants' sole interest. The Employee Retirement Income Security Act of 1974 (ERISA) addresses some specific roles that give rise to this fiduciary duty. ERISA Section 3(21)(A)(ii) specifically lists someone who “renders investment advice for a fee” regarding plan assets as a fiduciary. (Internal Revenue Code Section 4975(e)(3)(B) contains a parallel definition of “fiduciary.”)
- **Guidance on investment advice has shifted.** Over the years, the DOL and other regulatory entities have issued guidance on what constitutes investment advice. They have tried to strike a balance between protecting participants' retirement assets while avoiding overly burdensome rules that could limit participants' access to meaningful investment counseling. We now have a complex array of rules that dictate when financial professionals are providing investment advice—and that govern when they are bound by a duty to act in the best interests of those they serve. Even as this “final” PTE is being implemented, the new administration has indicated that proposed regulations (and other pronouncements that have not yet gone into effect) may be suspended pending further review. Although we do not know whether (or to what extent) the DOL or other

departments may add to or modify investment advice guidance, understanding the latest guidance is still important.

## The DOL Makes Four Changes in the Final PTE

The DOL received more than 100 written comments in response to last summer's proposed PTE. Although the final PTE "retains the proposal's broad protective framework," it makes four important changes.

- **The disclosure requirements have been changed.** The final PTE now requires financial organizations to document the reason that a rollover recommendation is in the retirement investor's best interest—and *they must provide this documentation to the investor before the rollover transaction*. This differs from the approach in the proposed PTE. The proposed PTE did not require that financial organizations provide this rollover documentation to retirement investors before engaging in the rollover transaction. Rather, they were required to make this documentation available to a potentially broad range of parties.
- **Recordkeeping requirements have been narrowed.** The broad access allowed to a financial organization's compliance records generated concern. The proposed PTE permitted access by any
  - authorized employee of the DOL;
  - plan fiduciary that engaged in an investment transaction under the PTE;
  - contributing employer and any employee organization whose members were covered by a plan that engaged in such a transaction; or
  - participant or beneficiary of a plan, or IRA owner that engaged in such a transaction.

Several commenters objected that allowing such broad access to records would create a significant burden on financial organizations. This access might encourage information requests for use in litigation, which in turn might lead financial organizations to avoid addressing compliance concerns for fear of disclosure. Consequently, the final PTE limits access to a financial organization's records to the Departments of Labor and Treasury. (The Treasury Department's access was added as part of the final PTE.)

- **Retrospective review certification rules have been relaxed.** Financial organizations must still conduct an annual review that is designed to assist the organization "in detecting and preventing violations of, and achieving compliance with, the Impartial Conduct Standards and the policies and procedures governing compliance with the exemption." But while the proposed PTE required that the financial organization's Chief Executive Officer (or equivalent) certify the details of the report, the final PTE now allows a "senior executive officer"—which includes the chief compliance officer, the president, the chief financial officer, or one of the financial organization's three most senior officers—to certify compliance.
- **A self-correction provision has been added.** Based on comments, the DOL added a new provision to the final PTE: a self-correction feature. Under this provision, the DOL will not consider a prohibited transaction to have occurred because of a failure to meet the PTE's conditions if the
  - violation did not create a loss to the investor or if the financial organization made the investor whole for the loss;
  - financial organization corrects the violation and notifies the DOL within 30 days of the correction;
  - correction occurs no later than 90 days after the financial organization learned (or should have learned) of the violation; and
  - financial organization notifies those responsible for conducting the retrospective review, and the violation and correction are specifically set forth in the written report of the review.

## The "Five-Part Test" Still Determines Fiduciary Status

In 1975, the DOL established a five-part test to determine fiduciary status, paralleled under the definition of "fiduciary" in Treas. Reg. 54.4975-9(c)(ii)(B). In 2016, the DOL finalized a new regulation meant to expand the definition of "investment advice." In 2018, this final regulation was vacated by the U.S. Court of Appeals for the Fifth Circuit. Consequently, the 1975 regulatory text was restored. Under the 1975 regulation, an investment professional or a financial organization that receives a fee or other compensation is considered a fiduciary if it meets *all* of the following prongs of the test.

- The investment professional or financial organization gives advice on investing in, purchasing, or selling securities, or other property.
- The investment professional or financial organization gives investment advice to the retirement investor on a regular basis.
- Investment advice is given pursuant to a mutual agreement or understanding with a retirement plan, plan fiduciary, or IRA owner.
- The retirement investor uses the advice as a primary basis for investment decisions.
- The investment professional or financial organization provides individualized advice, taking into account the IRA's or plan's demographics, needs, goals, etc.

This five-part test relies on all the facts and circumstances that surround each scenario. But the DOL points out that not *all* recommendations, including recommendations to roll over plan assets to an IRA, would qualify as providing investment advice “on a regular basis.” Some such advice may truly be an isolated, one-time event. But other similar recommendations could be part of an ongoing relationship—or the *start* of an ongoing relationship—that could trigger fiduciary responsibilities. This is one reason that the DOL advises financial organizations and investment professionals to carefully consider their roles—even if they don't think that their advice is provided on a regular basis.

### The Final PTE Retains Four Main Requirements

Although the final PTE contains four provisions absent from the proposed PTE, the fundamental requirements remain. Briefly, here are those four elements.

- **Impartial Conduct Standards.** The Impartial Conduct Standards impose three conditions.
  - The investment advice must be in the retirement investor's best interest.
  - The compensation for the advice must be reasonable (and the best execution of the investment transaction must be sought, as required by federal securities laws).
  - The advice, when made, must not be materially misleading.
- **Disclosure.** Before engaging in a transaction under the PTE, the financial organization must provide
  - a written acknowledgement that the financial organization and its investment professionals are fiduciaries under ERISA and the Internal Revenue Code (whichever applies);
  - a written description of the services to be provided and a conflicts-of-interest statement that is accurate and not misleading in all material respects; and
  - documentation that lists specific reasons for a rollover recommendation—*before* engaging in a rollover recommended under the PTE.
- **Policy and Procedures.** Three requirements pertain to this element.
  - Financial organizations must establish, maintain, and enforce written policies and procedures prudently designed to ensure compliance with the Impartial Conduct Standards.
  - The policies and procedures must mitigate conflicts of interest to the extent that a reasonable person reviewing them as a whole would conclude that they do not create an incentive for the financial organization or investment professional to place their interests ahead of the retirement investor.
  - The financial organization must document the specific reasons that any recommendation to roll over assets from a plan to another plan or an IRA, from an IRA to a plan, from an IRA to another IRA, or from one type of account to another (such as from a commission-based account to a fee-based account) is in the retirement investor's best interest.

- **Retrospective Review.** Three requirements also apply to this provision.
  - The financial organization must conduct reviews (at least annually) that are designed to help achieve compliance with the Impartial Conduct Standards and with the policies and procedures governing compliance with the PTE.
  - A senior executive officer must receive a written report that addresses the methodology and results of the retrospective review.
  - A senior executive officer must certify each year that the retrospective review meets the detailed requirements in the PTE.

## The DOL Rejects Its Analysis in the Deseret Letter

Throughout the final PTE, the DOL focuses on the potential conflicts of interest that rollover recommendations can pose. The final PTE cites the cumulative \$2.4 trillion in ERISA Title I plans that was expected to be rolled over between 2016 and 2020. Given the enormous sums involved—and the general prohibition against an investment advice fiduciary receiving fees for recommending that a Title I plan participant roll over assets from a plan to an IRA—the DOL reaffirms an important assertion that it made in the proposed PTE.

In the final PTE, the DOL holds firm to its assertion in the proposed PTE that its analysis in Advisory Opinion 2005-23A (the “Deseret Letter”) was incorrect. The Deseret Letter stated that the advice to roll assets out of a Title I plan, even when combined with a recommendation as to how the distribution should be invested, did not constitute investment advice. The DOL now rejects this analysis. But the DOL has also indicated that it will not pursue claims for breach of fiduciary duty or prohibited transactions between the 2005 release of the Deseret Letter and February 16, 2021, “based on a rollover recommendation that would have been considered non-fiduciary conduct under the reasoning in the Deseret Letter.”

## Other Takeaways from the Final PTE

The final PTE remains largely the same as the proposed PTE. But some of the DOL’s responses to the many comments it received—and other details contained in the preamble—seem worth noting.

- Parties can clearly communicate that they do not intend to enter into an ongoing relationship to provide (or receive) investment advice. And a single sales transaction may not confer fiduciary status. So when reviewing the transaction, the DOL will consider the reasonable understanding of each of the parties. While statements forbidding reliance on advice are not determinative, they can be considered, as can marketing materials and other communications.
- Compliance with the standards of other governing entities (such as the Securities and Exchange Commission) does not constitute compliance with the DOL’s final PTE. Although the DOL’s standards are intended to be consistent with securities law standards, the DOL has not provided a compliance safe harbor.
- As mentioned above, before engaging in a transaction under the PTE, the financial organization (or investment professional) must provide the retirement investor with an acknowledgment of the organization’s fiduciary status in writing, a written description of the services to be provided (along with any material conflicts of interest), and—if recommending a rollover—documentation that lists specific reasons for the rollover recommendation. Although the PTE does not include model language that satisfies all aspects of the disclosure requirement, it *does* include model language that will satisfy an entity’s acknowledgment of fiduciary status. In addition, although the PTE does not require it, the DOL has included plain-language, model text that spells out a fiduciary’s obligations to the retirement investor.
- What if investment professionals or financial organizations are uncertain about their fiduciary status? Clearly, they wouldn’t want to sign a fiduciary acknowledgement if they don’t meet each prong of the five-part test. And yet the final DOL indicates that parties cannot rely on the PTE “merely as back-up protection for engaging in possible prohibited transactions” while they try to deny the fiduciary nature or their investment advice. In particular, the DOL believes that, “in light of the broad scope of relief in the PTE, it is critical for [those] who choose to rely on the PTE to determine up-front if they intend to act as fiduciaries, and structure their relationship with the Retirement Investor accordingly.” So if investment professionals or financial organizations intend to act as fiduciaries, they should disclose this clearly; if they do *not* intend to act as fiduciaries, they should also disclose this—clearly and unequivocally—so that they do not tempt retirement investors to place unwarranted trust in them.

- The DOL has extended the relief provided in [Field Assistance Bulletin \(FAB\) 2018-02](#) until December 20, 2021. This FAB provides a transition period for parties to develop ways to comply with the final PTE. Specifically, the DOL indicates that “it [will] not pursue prohibited transaction claims against investment advice fiduciaries who worked diligently and in good faith to comply with Impartial Conduct Standards for transactions that would have been exempted in the new exemptions . . . .”

## Looking Ahead

Over the past several years, we have experienced a whirlwind of investment advice guidance from different regulatory entities. This includes the DOL’s revising some of its own guidance. It is possible that, as a new administration evaluates priorities, it could revisit previously released guidance, including this final PTE. Ascensus will continue to analyze any new guidance as it is released. Visit [ascensus.com](http://ascensus.com) for the latest developments.