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DOL Issues Guidance on 2020 Investment Advice Exemption



Just yesterday, the U.S. Department of Labor (DOL) released a set of [Frequently Asked Questions](#) (FAQs) designed to clarify certain aspects of Prohibited Transaction Exemption 2020-02, *Improving Investment Advice for Workers & Retirees* (PTE 2020-02). The exemption enables investment advice fiduciaries to ERISA plans and IRAs to receive a wide range of compensation (e.g., commissions, 12b-1 fees, revenue sharing, etc.) as a result of the advice without running afoul of the applicable prohibited transaction rules. As described by the DOL, “[t]he exemption offers a compliance option to investment advisers, broker-dealers, banks, and insurance companies (financial institutions) and their employees, agents, and representatives (investment professionals) that is broader and more flexible than pre-existing prohibited transaction exemptions.” We summarize some of the key takeaways from the FAQs below:

- PTE 2020-02 is in effect (Feb. 16, 2021). There was some confusion over this due to a memorandum from Ronald Klain, Chief of Staff to the President, regarding a regulatory freeze. The (new) DOL, however, was pleased enough with PTE 2020-02, a Trump-era rulemaking, that it waved it through. The transition period for parties to devise mechanisms to comply with the provisions in the exemption remains in place until Dec. 20, 2021.

- The DOL hinted at further sub-regulatory guidance and/or returning to the fiduciary investment advice regulation. No promises were made, or timetables offered.
- The DOL reiterated that a “single, discrete instance of advice to roll over assets from an employee benefit plan to an IRA” would generally not give rise to investment advice under ERISA. But, such communication could constitute investment advice if it were part of an ongoing relationship or the beginning of an intended future ongoing relationship that an individual has with the investment advice provider.
- The DOL reminded the industry that boilerplate, fine print disclaimers that say investment advice is not being provided generally won’t cut it. This echoes sentiment the DOL expressed in 2020. However, “[w]ritten statements disclaiming a “mutual” understanding or forbidding reliance on the advice as “a primary basis for investment decisions” may be considered in determining whether a mutual understanding exists, but such statements will not be determinative.” Ultimately, whether there is a “mutual” understanding that investment advice is being provided is based on the totality of the facts and circumstances.
- The DOL reiterated that PTE 2020-02 provides relief for rollover recommendations that result in a prohibited transaction, so long as the exemption’s conditions are satisfied.
- Investment professionals and financial institutions can provide investment advice, despite having a financial interest in the transaction, as long as the advice meets the best interest standard. Under this standard, the advice must be based on the interests of the customer rather than the competing financial interest of the investment professional or financial institution. Investment professionals may receive payments for their advice within this framework.
- Prior to engaging in a transaction under the exemption, a financial institution must give the retirement investor a written description of its material conflicts of interest arising out of the services and any investment recommendation. The disclosure should allow a reasonable person to assess the scope and severity of the financial institution’s and investment professional’s conflicts of interest. The DOL cautioned that the disclosure should be more than simply having the retirement investor “check the box” to confirm that they know of the conflicts.

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- Financial institutions and their investment professionals need to consider and document their analysis of why a rollover recommendation is in a retirement investor's best interest. For recommendations to roll over assets from an employee benefit plan to an IRA, the DOL listed the following "relevant" non-exhaustive factors to consider: (1) the alternatives to a rollover, including leaving the money in the investor's employer's plan, if permitted; (2) the fees and expenses associated with both the plan and the IRA; (3) whether the employer pays for some or all of the plan's administrative expenses; and (4) the different levels of services and investments available under the plan and the IRA. The DOL also elaborated on what other factors would be part of a prudent analysis.
- The DOL reminded financial institutions that they "must take special care in developing and monitoring compensation systems to ensure that their investment professionals satisfy the fundamental obligation to provide advice that is in the retirement investor's best interest." With carefully considered compensation structures, financial institutions can avoid structures that a reasonable person would view as creating incentives for investment professionals to place their interests ahead of the interest of the retirement investor. Thus, quotas, bonuses, prizes and performance standards are likely out. On the flip side, a financial institution could provide level compensation for recommendations to invest in assets that fall within reasonably defined investment categories (e.g., mutual funds) and provide heightened supervision as between investment categories (e.g., between mutual funds and fixed annuities), to the extent that it is not possible for the institution to eliminate conflicts of interest between these categories. The DOL also reminded financial institutions that the exemption requires they address and mitigate firm-wide conflicts.
- Unlike the 2016 rulemaking, PTE 2020-02 does not impose contract or warranty requirements on the financial institutions or investment professionals responsible for compliance. Nor does the exemption expand an investors' ability to enforce their rights in court or create any new legal claims beyond those in Title I of ERISA and the Code.

Financial institutions seeking additional information about their obligations under PTE 2020-02 may consider our initial [analysis](#) on PTE 2020-02 and its related rulemaking.