

# RIA Compliance Consultants

RIA Compliance Connection Conference  
August 24 & 25, 2022  
Omaha, NE

IRA Rollover – PTE 2020-02  
Conducting Required Retrospective Review

# 2022 RIA Compliance Connection

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## Agenda

- *Regulatory Resources*
- *Background - PTE 2020-02 Conditions*
- *Retrospective Annual Review*
- *Corrective Action*
- *RCC Resources*

## Regulatory Resources Related to U.S. Department of Labor's New Interpretation of Fiduciary (IRA Rollovers) under ERISA/IRC

- ***PTE 2020-02:***

<https://www.federalregister.gov/documents/2020/12/18/2020-27825/prohibited-transaction-exemption-2020-02-improving-investment-advice-for-workers-and-retirees>

- ***FAQs on New Fiduciary Advice Exemption:***

<https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/faqs/new-fiduciary-advice-exemption>

- ***Field Assistance Bulletin 2021-02:***

<https://www.dol.gov/agencies/ebsa/employers-and-advisers/guidance/field-assistance-bulletins/2021-02>

## No Conflicted Advice without PTE

Under ERISA and the Internal Revenue Code, parties providing fiduciary investment advice to plan sponsors, plan participants, and IRA owners may not receive payments creating conflicts of interest, unless they comply with protective conditions in a prohibited transaction exemption.

## Recommending IRA Rollover = Conflict of Interest

To the Extent an Investment Adviser Would Not Receive Compensation Unless a Client Decides to Transfer His Retirement Funds from Retirement Plan to IRA, the Investment Adviser Has a Conflict of Interest When Making a Recommendation on Whether Client Should Make an IRA Rollover & Needs to Meet a Prohibited Transaction Exemption (PTE) Issued by U.S. Department of Labor



## Includes Converting IRA from Commission to Fee Account

Similar to a Recommendation to Rollover from a Retirement Plan to IRA, a Recommendation by an Investment Adviser to Convert an IRA from a Commission Account to a Fee Account Would be Treated as Conflicted and Requiring a Prohibited Transaction Exemption

## Prohibited Transaction Exemption (PTE) 2020-02 - Conditions

- *Investment Adviser and Rep Acknowledge their fiduciary status under ERISA in writing,*
- *Exemption is only available for non-discretionary advice (e.g., only client can make decision to rollover, switch from commission to fee account or invest in a proprietary fund)*
- *Disclose their services and material conflicts of interest,*
- *Adhere to Impartial Conduct Standards requiring that they*
  - ✓ *Investigate and evaluate investments, provide advice, and exercise sound judgment in the same way that knowledgeable and impartial professionals would (i.e., their recommendations must be “prudent”),*
  - ✓ *Act with undivided loyalty to retirement investors when making recommendations (in other words, they must never place their own interests ahead of the interests of the retirement investor, or subordinate the retirement investor’s interests to their own),*
  - ✓ *Charge no more than reasonable compensation and comply with federal securities laws regarding “best execution,” and*
  - ✓ *Avoid making misleading statements about investment transactions and other relevant matters,*
- *Adopt policies and procedures prudently designed to ensure compliance with the Impartial Conduct Standards and to mitigate conflicts of interest that could otherwise cause violations of those standards;*
- *Document and disclose the specific reasons that any rollover recommendations are in the retirement investor’s best interest; and*
- *Conduct an annual retrospective compliance review*

## All or Nothing under PTE 2020-02

- Must Meet All the Conditions from the Previous Slide In Order to Receive the Exemption
- If Only Meet Some (But Not All) Conditions, Then the Rollover Recommendation Is a Prohibited Transaction
- In Other Words, If Forget the Annual Retrospective Review, Then There's No Protection from the Exemption

## PTE 2020-02 Annual Retrospective Review

- Reasonably Designed to Assist in Detecting and Preventing Violations of, and Achieving Compliance with, the Impartial Conduct Standards and P&P
- Methodology and Results of the Annual Retrospective Review Must Be in a Written Report to Investment Adviser's Senior Executive Officers
  - Recommend as Best Practice that Reviewer/Preparer of Annual Retrospective Review Is Different/Separate from Senior Executive Who Will Be Certifying
- Investment Adviser's Senior Executive Must Certify Review of Report

## Annual Retrospective Review (Continued)

- Report Must Be Used to Find More Effective Ways to Ensure IARs Are Providing Investment Advice in Accordance with Impartial Conduct Standards and To Correct Any Deficiencies with Existing P&P
- Senior Executive Officer Should Carefully Review the Report Before Making the Certification
  - Making Certification Without Senior Executive Officers Carefully Reviewing the Report Would Constitute a Violation of the Exemption
  - If Senior Executive Officer Does Not Have Experience and or Expertise, Then Should Consider Consulting with Compliance Consultant or Legal Counsel
- Must Maintain the Written Report of the Annual Retrospective Review, the Certification and Supporting Data for 6 Years
- Provide Those Documents to DoL within 10 Business Days of a Request

## Scope of Review

- Whether to Sample or Review All Recommendations Will Depend Upon Whether P&P Included a Contemporaneous Review by a Supervisor?
- If No Contemporaneous Review by Supervisor, Then Will Need to Review All Transactions as Part of Annual Retrospective Review
  - The Lack of a Contemporaneous Review by a Supervisor Is Problematic (Except for One-Person RIA)

## Examples of Items to Review - Disclosures

- Fiduciary Status – Did both firm and rep make in writing (and in advance of any recommendation) a clear statement acknowledging fiduciary status?
  - Keep a copy of each written statement to an applicable client and proof that such statement was made in advance of any recommendation
- Conflict of Interest Disclosure – Did the firm provide in advance a written conflict of interest disclosure related to IRA rollover recommendations?
  - Did the Disclosure Admit Bias, Explain How Conflict Mitigated and Does Not Use “Potential”?
  - Does the Firm Have Proof of the Conflict of Interest Disclosure Was Received (e.g., Form ADV Part 2A, Client Agreement, Client Acknowledgement)

## Examples of Items to Review – Prudent Review & Analysis

Did Firm and IAR Conduct a Prudent Review & Analysis and Consider/Document Following?

- Alternatives to a Rollover Including Leaving Money in Plan if Permitted;
- Whether Employer Pays for Some or All of the Plan's Administrative Expenses;
- Different Levels of Services under Plan versus Rollover IRA;
- Adequacy of Investments Available under Plan versus Rollover IRA
- Fees & Expenses Associated with Plan and Rollover IRA and Long-Term Impact
  - Did the firm and IAR obtain the 404a-5 disclosure for the plan's expenses for analysis? If no, did the firm and IAR make a reasonable estimation and use Form 5500 and an applicable benchmark of similar size plan?
  - Was the long-term impact of the anticipated expenses disclosed to the client? If an estimate of the expenses is made, was this disclosed to the client?



## Examples of Items to Review

- Did the IAR review with client whether facing bankruptcy?
- Did the IAR review when client would desire distributions (mandatory RDMs and penalty-free withdrawal)?
- Did the IAR review whether the client had a concentrated position of the employer's stock within the plan?
- Did the IAR disclose in writing the pros and cons of the different options?
- If Actual Expenses of Plan Not Available or Used, Did IAR Explain Assumptions/Limitations of Benchmark Data?
- Did the IAR disclose the reasons for the recommendation provided to the client in writing?
- Did the client acknowledge (by signing) fiduciary status, conflicts of interest, pros/cons, expenses and reasons for recommendation?

## Items to Check – Impartial Conduct Standards

- Has the firm adopted Impartial Conduct Standards (“ICS”) which are in writing?
- Did the firm train its rep and supervisory staff on PTE 2020-02 ICS?
- Does the ICS Require Firm and IAR Act in Client’s Best Interest and Define What Is Best Interest?
- Does ICS Require the Firm Charge No More than Reasonable Compensation?
- Does ICS Require the Firm Comply with Federal Securities Laws Regarding Best Execution?
- Does the ICS Require No Misleading Statements About Investment Transactions and Other Relevant Matters

## Items to Review – P & P

- Does the firm have written supervisory procedures related to IRA rollovers and PTE 2020-02?
- Does the Firm Have a Supervisor Review Each IRA Rollover Recommendation?
- Are IRA Rollover Recommendations Systematically Tracked and All Documents Preserved in Document Management System?
- Does the Firm Have a Supervisor Review Any Conflicted Transaction in an IRA (e.g., Recommend Switch from Commission to Fees, Proprietary Product, Principal Trade, Higher Paying Advisory Service or 3<sup>rd</sup> Party Money Manager)?
- Did the Firm Have Procedures to Identify & Mitigate Conflicts of Interest?

## Examples of How to Mitigate Conflicts

- Do Not Permit Proprietary Products within IRAs
- Do Not Use a Grid for Rep Payout – Same Payout Rate Regardless of Assets under Management
- Asset Based Fee Same for All Asset Classes
- If Using Different 3<sup>rd</sup> Party Money Managers, Levelize Compensation to Rep
- Levelize Compensation Between Different Advisory Services or Use Neutral Factors
- Require Supervisor to Review Recommendations to Use Higher Paying Advisory Services
- Do Not Pass on Firm Conflicts to Reps and Executives

## Items to Check - Compensation

- Does Compensation of IAR Minimize Conflict of Interest?
  - Is the compensation level or does it vary by investment/product or services?
    - Does the investment advisory fee rate vary by type of assets or product?
    - Does the firm receive more from one third-party money manager than another?
  - Are compensation conflicts at firm level passed to the IAR?
    - Is Revenue Sharing Received by Firm Passed on to IAR?
    - If IAR Paid a Fixed % of Fees Generated by Firm, This Reward IAR for Recommending Service with Greatest Compensation to Firm
  - Is there a bonus, prize/trip or quota?
  - Does the firm use a payout grid with IAR?
    - Are the increases in compensation drastic?
    - Are the increases retroactive for past advisory services already provided?
    - If Using a Grid, Did the Firm Monitor IAR When Approaching Threshold on Grid for Recommendations Contrary to Client's Interest

## Corrective Action for Violation

*“Financial institutions can correct violations of the exemption within 90 days after the financial institution learns, or reasonably should have learned, of the violation. If the violation did not result in investment losses to the retirement investor or the financial institution made the retirement investor whole for any resulting losses, the financial institution can correct the violation and notify the Department within 30 days of correction. The financial institution must notify the persons responsible for conducting the retrospective review described in Q19 of the violation and correction, and the violation and correction must be specifically set forth in the written report of the retrospective review.”*

## Corrective Action for Violation

- Can Correct Within 90 Days After Learning of the Violation
- No Loss to Client or Client Made Whole by Firm
- Notify U.S. Department of Labor within 30 Days of Correction
- Notify Reviewer Conducting Annual Retrospective Review
- Include/Reference in Annual Retrospective Review Report

## Resources

### ***IRA Rollovers***

- ***Webinars***

*IRA Rollover Compliance Under PTE 2020-02 (2/24/2022)*

*IRA Rollovers Under U.S. Department of Labor's PTE 2020-02 (10/28/2021)*

- ***Form ADV – Sample Language – Rollover Recommendation***

*<https://www.ria-compliance-consultants.com/product/form-adv-sample-language-ira-rollover-recommendation/>*

- ***Suitability – Retirement Plan Rollover – Client Acknowledgement***

*<https://www.ria-compliance-consultants.com/product/suitability-retirement-plan-rollover-client-acknowledgement/>*

- ***WSP/CoE Section Update – IRA Rollover Recommendations***

*<https://www.ria-compliance-consultants.com/product/wsp-coe-section-update-ira-rollover-recommendations/>*



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