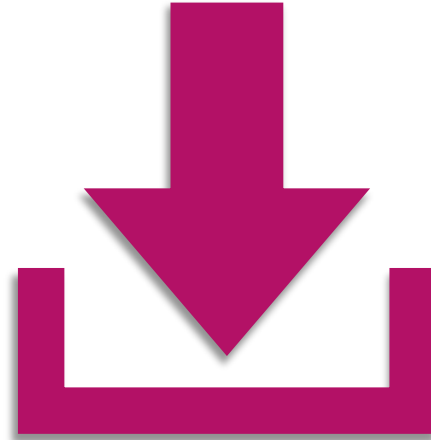




Conducting an Annual Retrospective Review of IRA Rollovers for DoL's PTE 2020-02

Download Our Slides

<https://www.ria-compliance-consultants.com/DoL-Annual-Retrospective>



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- ▶ **Purchase CE Course** – If the course is approved by NASAA for IAR CE, you will then need to purchase the course at <https://www.CE4Advisers.com> .
- ▶ **IAR Acknowledgement** – Sign the IAR CE Acknowledgement & Attestation.
- ▶ **Practice Quizzes** – You will need to complete a practice quiz on each lesson.
- ▶ **Final Quiz** - You must complete each lesson and receive a score of **100%** on the final quiz to receive IAR CE credit (assuming the course has been approved by NASAA).

Content Questions & Technical Help

If you have questions about the content of this course or need technical help, please contact us via the email address below:

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Your Instructor



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Course Overview

- ▶ *Regulatory Resources*
- ▶ *Fiduciary Under ERISA/IRC & Conflicted Advice*
- ▶ *Summary of PTE 2020-02*
- ▶ *Retrospective Annual Review*
- ▶ *Corrective Action*
- ▶ *Order by Fed. Distr. Ct. in FL*
- ▶ *SEC Exam Priority*
- ▶ *Questions*

Limited Focus

- ▶ This Training Will Be Focused Upon the Annual Retrospective Review for an Investment Adviser Firms/IARs **Who Make IRA Rollover Recommendations as Part of Advisory Services**
- ▶ Assumes You Have Received Previous Training About General Requirements of PTE 2020-02

Regulatory Resources

- ▶ *PTE 2020-02* at <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* at <https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/faqs/new-fiduciary-advice-exemption>
- ▶ *Field Assistance Bulletin 2021-02* at <https://www.dol.gov/agencies/ebsa/employers-and-advisers/guidance/field-assistance-bulletins/2021-02>
- ▶ *American Securities Association (ASA) v. U.S. Department of Labor, Case No. 8:22-cv-330 (M.D. Fla. Feb. 13, 2023)* at <https://casetext.com/case/am-sec-assn-v-united-states-dept-of-labor>
- ▶ *SEC's 2023 Examination Priorities* at <https://www.sec.gov/files/2023-exam-priorities.pdf>

Fiduciary under ERISA/IRC

A firm or investment professional provides fiduciary investment advice to the extent he or she “renders investment advice for a fee or other compensation, direct or indirect, with respect to any money or other property of such plan, or has any authority or responsibility to do so.”

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

Fiduciary under ERISA/IRC

Five-Part Test for a Firm or Individual

1. Render advice to the plan, plan fiduciary, or IRA owner as to the value of securities or other property, or make recommendations as to the advisability of investing in, purchasing, or selling securities or other property,
2. On a regular basis,
3. Pursuant to a mutual agreement, arrangement, or understanding with the plan, plan fiduciary, or IRA owner, that
4. The advice will serve as a primary basis for investment decisions with respect to plan or IRA assets, and that
5. The advice will be individualized based on the particular needs of the plan or IRA.

*All five parts of the test must be met.

Fiduciary under ERISA/IRC

What Is Advice on “Regular Basis” Related IRA Rollover?

- ▶ A single, discrete instance of advice to roll over assets from an employee benefit plan to an IRA would not meet the regular basis prong of the five-part test.
- ▶ When 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 subject to ERISA or the Internal Revenue Code, the advice to roll assets out of the employee benefit plan is part of an ongoing advice relationship that satisfies the regular basis prong.
- ▶ **When the investment advice provider has not previously provided advice but expects to regularly make investment recommendations regarding the IRA as part of an ongoing relationship, the advice to roll assets out of an employee benefit plan into an IRA would be the start of an advice relationship that satisfies the regular basis requirement.**
- ▶ The five-part test extends to the entire advice relationship and does not exclude the first instance of advice, such as a recommendation to roll plan assets to an IRA, in an ongoing advice relationship.

No Conflicted Advice

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 the U.S. Department of Labor



Conflict of Interest

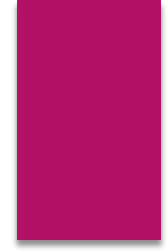
Converting IRA from Commission to Fee

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

Conflict of Interest Equity/Fixed Income Assets Subject to Different Fee Rates

To the extent that there is a different advisory fee rate for equity assets versus fixed income assets, an investment adviser compensation can vary based upon his or her advice/decision and this creates a conflict of interest for the investment adviser when making investment recommendations or managing such account.

Summary of PTE 2020-02



- ❖ *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

What Is an Annual Retrospective Review?

- ▶ A Review Which Is Reasonably Designed to Assist in Detecting and Preventing Violations of, and Achieving Compliance with, the Impartial Conduct Standards and P&P
- ▶ A Best Practice Is that Reviewer of Annual Retrospective Review Is Different from Senior Executive Who Will Be Certifying
- ▶ Should 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



Background Written Report of Review

Methodology and Results of the Annual Retrospective Review Must Be in a Written Report to Investment Adviser's Senior Executive Officers

Background Certification of Review

- ▶ 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



Background

When Must the Review Be Performed

Review, Report & Certification Must Be Performed and Completed Within 6 Months of the Previous Year

Background

Record Retention of the Report

- ▶ 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

Questions to Answered During the Review

Impartial Conduct Standards

- Was the best interest standard of care met for every rollover recommendation?
- Did the investment adviser firm receive only reasonable compensations and satisfy the SEC's best execution standard for each rollover recommendation?
- Were there any misleading statements related to a rollover recommendation?

Required Disclosures Prior to Rollover

- Did the investment adviser firm and investment adviser rep acknowledge in writing that they were fiduciaries under ERISA and IRC?
- Did the firm disclose in writing its conflict of interest related to retirement plan rollover?
- Was there a written explanation of the specific reasons why rollover recommendation was in the best interest of the client?

Policies & Procedures

- Did the firm establish policies and procedures to ensure compliance with Impartial Conduct Standards?
- Were the policies and procedures of the firm written in such a way that a reasonable person would conclude that they do not create an incentive for the firm and investment adviser representative to place their interests ahead of the interest of the client?
- Did the firm's policies and procedures require the documentation of the specific reasons why the recommendation is in the best interest of the client?

Annual Retrospective Review

- Was an annual retrospective review performed (within 6 months of year-end) by the firm and did a senior executive officer sign the report of the review?

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
 - Is the statement ambiguous and the client's unclear of the firm & rep's fiduciary status?
- ▶ 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 Prudent Review & Analysis (Continued)

- ▶ 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 in writing assumptions/limitations of benchmark data?
- ▶ Did the IAR disclose in writing the reasons for the recommendation provided to the client in writing?

Items to Review - ICS

- ▶ 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 in 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 3rd Party Money Manager)?
- ▶ Did the Firm Have Procedures to Identify & Mitigate Conflicts of Interest?

Examples of How to Mitigate Conflicts of Interest

- ▶ 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 3rd 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

Violations

*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 of the violation and correction, and the violation and correction must be specifically set forth in the written report of the retrospective review.”*

See <https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/faqs/new-fiduciary-advice-exemption> at Question 20.

Corrective Actions for Violations

- ▶ 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

American Securities Association v. U.S. Dept. of Labor

- ▶ In February 2023, U.S. Fed District Ct (M.D. Fla.) Ruled DoL's Interpretation ("Regular Basis" Interpretation under FAQ-7) of 5-Part Test of Who Qualifies as "Fiduciary" Is "Arbitrary and Capricious"
 - Interesting Point: Ct. Determined FAQ-15 (i.e., Best Interest - Plan's Services, Investments & Expenses Need to Be Obtained And Compared to Services, Expenses and Investments Offered In The Rollover IRA) Consistent with Prudent Process
- ▶ DoL Has Not Yet Indicated Whether It Will Appeal The Ruling Which Could Be Reversed by U.S. Court of Appeals
- ▶ DoL Has Indicated Proposing a New Fiduciary Definition In Near Future
- ▶ Even without FAQ-7, If Providing Ongoing Advice to IRA Owners, Plan Fiduciary and Plan Participant, Can Still Be a Fiduciary Under 5-Part Test and Need PTE 2020-02 Against Conflicted Advice
- ▶ Consult with Legal Counsel Before Making Any Decision Not to Follow PTE 2020-02

SEC's 2023 Exam Priorities Includes Rollovers

*“Examinations may also focus on recommendations or advice to certain types of investors, such as senior investors and those saving for retirement, and specific account recommendations, **such as retirement account rollovers** and 529 plans.”*

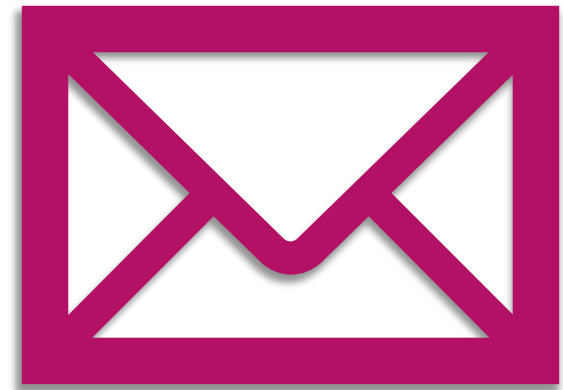
Examples of Compliance Tools

- *Webinars*
- *Form ADV – Sample Language – Rollover Recommendation*
- *Suitability – Retirement Plan Rollover – Client Acknowledgement*
- *WSP/CoE Section Update – IRA Rollover Recommendations*
- *Sr. Executive Certification*
- *Retirement Plan Benchmarking Software or Book*

Questions

Please submit any question online or email with any questions about the content of this course.

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Thank You

