A SUMMARY:
DOL Final Rule – Prohibited Transaction Exemption 2020–02

Who Is An Investment Fiduciary?
Under the 1975 regulation, for advice to constitute "investment advice," a financial institution or investment professional[1] who is not a fiduciary under another provision of the statute must—

(1) render advice 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[2], 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.

A financial institution or investment professional that meets this Five-Part test, and receives a fee or other compensation, direct or indirect, is an investment advice fiduciary under ERISA and under the Internal Revenue Code (IRC).

Further, under ERISA section 3(21)(A)(ii), a person is a fiduciary with respect to a plan to the extent he or she renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so.

Prohibited Transactions
ERISA and the IRC establish prohibited transaction provisions that generally exclude fiduciaries, with respect to workplace retirement plans (Plan or Plans) and individual retirement accounts and annuities (IRAs), from engaging in self-dealing and receiving compensation from third parties in connection with transactions involving the Plans and IRAs. The provisions also prohibit purchasing and selling investments with the Plans and IRAs when the fiduciaries are acting on behalf of their own accounts (i.e. principal transactions).

Under these prohibited transaction provisions, a fiduciary may not deal with the income or assets of a Plan or an IRA in his or her own interest or for his or her own account, and a fiduciary may not receive payments from any party dealing with the Plan or IRA in connection with a transaction involving assets of the Plan or IRA. DOL has authority under ERISA

[1] an individual who is a fiduciary of a Plan or an IRA by reason of the provision of investment advice, who is an employee, independent contractor, agent, or representative of a Financial Institution, and who satisfies the federal and state regulatory and licensing requirements of insurance, banking, and securities laws (including self-regulatory organizations) with respect to the covered transaction, as applicable. Similar to the definition of Financial Institution, this definition also includes a requirement that the Investment Professional has not been disqualified from making investment recommendations by any insurance, banking, or securities law or regulatory authority (including any self-regulatory organization).
[2] Any employee benefit plan described in ERISA section 3(3) and any plan described in Code section 4975(e)(1)(A).

6409 81st Street
Cabin John, Maryland 20818, U.S.A.
(703) 847-4380, www.ExperientialWealth.com

section 408(a) and IRC section 4975(c)(2) to grant administrative exemptions from the prohibited transaction provisions.

New Exemption

On December 18,2020, the Department of Labor (DOL) published the Prohibited Transaction Exemption 2020–02[3], known as Improving Investment Advice for Workers & Retirees. This exemption is available to registered investment advisers, brokerdealers, banks, and insurance companies (Financial Institutions) and their individual employees, agents, and representatives (Investment Professionals[4]) that provide fiduciary investment advice to Retirement Investors[5]. The new exemption allows Plan investment advice fiduciaries to receive compensation, including as a result of advice to rollover assets from a Plan to an IRA, and to engage in principal transactions. The exemptions are made effective as of February 16, 2021.

Financial Institutions and Investment Professionals can receive a wide variety of payments that would otherwise violate the prohibited transaction rules, including, but not limited to, commissions, 12b–1 fees, trailing commissions, sales loads, mark-ups and mark-downs, and revenue sharing payments from investment providers or third parties.

Conditions for Relief

The prohibited transaction exemption:

A. conditions relief based on the Investment Professional and Financial Institution investment advice fiduciaries providing advice in accordance with the Impartial Conduct Standards.
   The Impartial Conduct Standards have three components:
   (1) A best interest standard;
   (2) a reasonable compensation standard; and
   (3) a requirement to make no misleading statements about investment transactions and other relevant matters.

B. conditions relief based on Financial Institutions to acknowledge in writing their and their Investment Professionals' fiduciary status under ERISA and IRC when providing investment advice to the Retirement Investor, and to describe in writing the services to be provided and the Financial Institutions' and Investment Professionals' material conflicts of interest.

   Financial Institutions must document the reasons that a rollover recommendation is in the best interest of the Retirement Investor and provide that documentation to the Retirement Investor. Financial Institutions are required to adopt policies and procedures prudently designed to ensure compliance with the Impartial Conduct Standards and conduct a retrospective review of compliance.

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

[4] https://www.dol.gov/newsroom/releases/ebsa/ebsa20210413

[5] A Retirement Investor is defined as (1) a participant or beneficiary of a Plan with authority to direct the investment of assets in his or her account or to take a distribution, (2) the beneficial owner of an IRA acting on behalf of the IRA, or (3) a fiduciary of a Plan or an IRA.

C. provides relief for Financial Institutions to enter into principal transactions[6] with Retirement Investors, in which they purchase or sell certain investments from their own accounts.

Exemption Applies to Rollover Advice
A recommendation to roll assets out of a Title I Plan **is advice** with respect to moneys or other property of the Plan. An investment advice fiduciary (a person who satisfies all of the requirements of the five-part test) making a rollover recommendation would be required to avoid prohibited transactions under ERISA and IRC. This prohibited exemption now provides relief if all conditions are meet by the investment advice fiduciary and the adviser's financial institution.

Pure Robo-Advice Excluded From Exemption
Result from investment advice generated solely by an interactive website in which computer software-based models or applications provide investment advice that do not involve interaction with an Investment Professional (referred to herein as "pure roboadvice") is excluded from exemptive relief.

"Hybrid" robo-advice arrangements, which involve both computer software models and personal investment advice from an Investment Professional, are permitted under the exemption.

Proprietary Products and Limited Menus of Investment Products
The best interest standard can be satisfied by Financial Institutions and Investment Professionals that provide investment advice on proprietary products or on a limited menu of investment options, including limitations to proprietary products 129 and products that generate third party payments. Conditions of the exemption can be satisfied by providing complete and accurate disclosure of their material conflicts of interest in connection with such products or limitations and adopting policies and procedures that mitigate conflicts 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.

This summary, prepared by Philip Chao, is for general informational purpose only and should not be deemed as delivering any legal or regulatory guidance or advice regarding the subject matter. Please refer to THE FINAL REGULATION[7] in its entirety for a more complete understanding and application. Please consult with legal and regulatory counsel before taking any action.

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[6] involve the purchase from, or sale to, a Plan or an IRA, of an investment, on behalf of the Financial Institution's own account or the account of a person directly or indirectly, through one or more intermediaries, controlling, controlled by, or under common control with the Financial Institution. Because an investment advice fiduciary engaging in a principal transaction is on both sides of the transaction, the firm has a clear and direct conflict of interest.

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