



Insights: Alert

## PTE 2020-02 for Investment Advice Fiduciaries: Overview and Checklist

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Overview: In general, the prohibited transaction rules (in ERISA and the Tax Code) (1) prohibit fiduciaries that provide investment advice to plans subject to Title I of ERISA (including 401(k) plans, pension plans and profit-sharing plans) (“ERISA Plans”) and IRAs (collectively, “Plans”) from receiving compensation that is paid from third parties or that varies based on the fiduciaries' advice and (2) prohibit fiduciaries from engaging in principal transactions, including purchases and sales with Plans on behalf of their own accounts. Section 408(b)(2) of ERISA provides an exemption for compensation received by a service provider to a Plan, but it does not provide relief where the service provider is a fiduciary that has any authority to require the Plan to pay an additional fee to the fiduciary (including when fiduciary investment advice is provided on a nondiscretionary basis). Similarly, Section 408(b)(17) of ERISA provides an exemption for purchases and sales for adequate consideration between a Plan and a party in interest, but does not apply where the third party is a fiduciary or provides fiduciary investment advice with respect to the assets involved in the transaction.

PTE 2020-02 allows Financial Institutions and Investment Professionals “who provide fiduciary investment advice to Retirement Investors to receive otherwise prohibited compensation and engage in riskless principal transactions and other principal transactions.” This prohibited transaction exemption is important because the Department of Labor (“DOL”) recently withdrew the so-called “Deseret Letter,” it issued in 2005, which held that advice regarding a rollover from an ERISA Plan (such as a 401(k) plan) generally would not be considered fiduciary investment advice. As a result, the DOL now takes the position that a Financial Institution may be a fiduciary when it gives advice to roll assets out of an ERISA Plan and subsequently receives a fee for management of those assets in an IRA or engage in riskless and certain other principal transactions with respect to the rollover to an IRA. This exemption may cover transactions other than rollover advice, but the exemption does not apply to Financial Institutions and Investment Professionals that give discretionary advice with respect to a transaction.

Fiduciary investment advice is defined under a five-part test under which a financial institution or investment professional: (i) renders advice to the Plan 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; (ii) on a regular basis; (iii) pursuant to a mutual agreement, arrangement, or understanding with the Plan or Plan fiduciary (including an IRA owner), that (iv) the advice will serve as a primary basis for investment decisions with respect to Plan assets, and that (v) the advice will be individualized based on the particular needs of the Plan.

In the DOL's view, disclaimers of a mutual understanding that investment advice may be relied upon are not determinative, but may be considered in determining whether a mutual understanding exists. The DOL said that it



will consider the reasonable understandings of the parties, including whether “firms and investment professionals hold themselves out in their oral communications, marketing materials, or interactions with retirement investors as making individualized recommendations that the investor can rely upon to make an investment decision that is in the best interest of the investor, and the investor, accordingly, relies upon the recommendation to make an investment decision.” Generally, a “boiler plate disclaimer would be insufficient to avoid fiduciary status. Further, first-time advice related to a rollover transaction may satisfy the “regular basis” requirement when the rollover is intended to be the beginning of a long-term relationship. The DOL said even if a firm or investment professional has not provided investment advice before the rollover transaction, the investment advice will satisfy the regular basis requirement when the firm or investment professional “expects to regularly make investment recommendations regarding the IRS as part of an ongoing relationship.”

Although PTE 2020-02 became effective on February 16, 2021, the DOL said that it would not, as a matter of enforcement policy, pursue claims for breaches of fiduciary duty or prohibited transactions between 2005 (when the Deseret Letter was issued) and February 16, 2021 that would not have been considered fiduciary conduct under the Deseret Letter. In addition, as a matter of enforcement policy, through December 20, 2021, the DOL will not challenge fiduciary breaches or prohibited transactions with respect to investment advice fiduciaries who are working diligently and in good faith to comply with the impartial conduct standards.

The following checklist summarizes the conditions of the exemption, as well as additional DOL commentary in the form of Frequently Asked Questions, which are available at: [New Fiduciary Advice Exemption: PTE 2020-02 Improving Investment Advice for Workers & Retirees Frequently Asked Questions | U.S. Department of Labor \(dol.gov\)](#).

The DOL has also provided Frequently Asked Questions for retirement plan investor, which are available at: [Choosing the Right Person to Give You Investment Advice: Information for Investors in Retirement Plans and Individual Retirement Accounts | U.S. Department of Labor \(dol.gov\)](#).

#### PTE 2020-02 Checklist

PTE 2020-02	Transactions Covered	Comments
II(b)(1)	Financial Institutions and Investment Professionals (and Affiliates and Related Entities) can engage in transactions for which they provide fiduciary investment advice in which they receive reasonable compensation, including in a transaction that includes a rollover from an ERISA Plan to an IRA.	
II(b)(2), V(d)	Financial Institutions and Investment Professionals can provide fiduciary investment advice with respect to the purchase or sale of an asset in a riskless principal transaction or a Covered Principal Transaction (which is defined as (i) a sale to a Plan of certain debt securities or a principal	

PTE 2020-02	Transactions Covered	Comments
	transaction covered under another exemption or (ii) a purchase from a Plan of securities or investment property).	
II(b)(3)	<p>This Exemption does not apply to the following situations:</p> <p>(1) Plans for which the investment advice fiduciary, or an affiliate, is (i) employer of employees covered by the Plan or a named fiduciary of the Plan or (ii) plan administrator selected by a fiduciary that is not independent of investment advice fiduciary;</p> <p>(2) roboadvice (investment advice generated solely by an interactive web site with computer-based models or applications and without any personal interaction); or</p> <p>(3) discretionary fiduciary investment arrangements.</p>	
II	<p>Investment Professionals and Financial Institutions must comply with (i) the Impartial Conduct Standards, (ii) Disclosure Requirements, (iii) Policies and Procedures Requirements, and (iv) the Retrospective Review Requirement. All of these requirements are discussed below.</p>	

PTE 2020-02	Parties Eligible for Relief	Comments
V(e)	Financial Institution is one of: (1) a registered broker-dealer; (2) a registered investment adviser; (3) an insurance company; (4) a bank; or (5) an entity that is described as a Financial Institution in an individual exemption granted by the DOL.	
V(h)	Investment Professional is each of: (1) a fiduciary of a Plan by providing fiduciary investment advice, (2) an employee, independent contractor, agent or representative of a Financial Institution, and (3) a person who satisfies the applicable federal and state regulatory and licensing requirements of insurance, banking and securities laws (including self-regulatory organizations), as applicable, with respect to the transaction.	
III(a)	<u>Eligibility</u> : A Financial Institution or Investment Professional is ineligible for the exemption for 10 years following:	

PTE 2020-02	Parties Eligible for Relief	Comments
	<p>(1) any conviction of a crime described in ERISA section 411 arising out of providing investment advice to Retirement Investors (unless the DOL grants a petition that allows the Financial Institution to continue to use the exemption) or</p> <p>(2) receipt of ineligibility issued by the DOL for engaging in systematic pattern or practice of violating the conditions of this exemption.</p> <p>There is a one-year winding period for Financial Institutions in which the exemption may be relied upon after becoming ineligible, but this does not apply to an Investment Professional.</p>	

PTE 2020-02	Impartial Conduct Standards	Comments
II(a)(1), V(b)	<p><u>Best Interest:</u> Investment advice must be in the Best Interest of the Retirement Investor. Advice must satisfy the following standards:</p> <p><i>Prudence standard:</i> advice must be made with care, skill, prudence, and diligence that a prudent person acting in a like capacity and familiar with such matters would use, based on investment objectives, risk tolerance, financial circumstances, and needs of Retirement Investor.</p> <p><i>Loyalty standard:</i> advice providers may not place their own interests ahead of the Retirement Investor. For example, a Financial Institution or Investment Professional cannot, when advising between two otherwise equally available options, advise the Retirement Investor to choose an option that is better for the Financial Institution or Investment Professional and worse for the Retirement Investor.</p>	
II(a)(2)(A)	<p><u>Reasonable Compensation:</u> Financial Institution, Investment Professionals, and their affiliates and related entities can charge only reasonable compensation for providing investment advice. Reasonableness will depend on market price of service(s) provided and/or underlying asset; scope of monitoring; and complexity of product.</p>	

PTE 2020-02	Impartial Conduct Standards	Comments
II(a)(2)(B)	<u>Best Execution</u> : Financial Institution, Investment Professionals, and their affiliates and related entities must seek to obtain best execution of investment transaction reasonably available under circumstances, as required under securities law.	
II(a)(3)	<u>No Materially Misleading Statement</u> : Any statements made by the Financial Institution or Investment Professional about recommendations and other relevant matters (ex: fees and compensation, or material conflicts of interest) must not be materially misleading.	

PTE 2020-02	Disclosure Requirements	Comments
II(b)(1)	<u>Fiduciary Status</u> : Financial Institutions and Investment Professionals must provide written acknowledgement to the Retirement Investor that they (and affiliates and related entities) are fiduciaries under ERISA and the Code. Ambiguous statements that would leave a reasonable investor unsure of fiduciary status are insufficient for parties relying on the exemption.	
II(b)(2)	<u>Scope of Services and any Material Conflicts of Interest</u> : Financial Institutions and Investment Professionals must provide a written description of services provided and a written description of the Financial Institution's (and Investment Professional's) material conflicts of interest that is in all material respects accurate and not misleading. For example, conflicts associated with proprietary products, payments from third parties, and compensation arrangements should be disclosed.  The DOL emphasizes that this disclosure cannot be a "check the box" activity; it should be designed to allow a reasonable person to understand the scope and severity of the relevant conflicts of interest.	
II(b)(3)	<u>Rollover Advice</u> : Financial Institutions must document the specific reasons for a rollover recommendation. The relevant factors may include the following: <ul style="list-style-type: none"> <li>• the alternatives to a rollover, including leaving the money in the investor's employer's plan, if permitted;</li> <li>• the fees and expenses associated with both the plan and the IRA;</li> <li>• whether the employer pays for some or all of the plan's administrative expenses; and</li> </ul>	

PTE 2020-02	Disclosure Requirements	Comments
	<ul style="list-style-type: none"> <li>• the different levels of services and investments available under the plan and the IRA.</li> </ul> <p>The Financial Institution and Investment Professional should consider other investment options in the Plan, the consideration and documentation of any fee-based arrangements after the rollover, and the impact of any increases costs as a result of the rollover (and why the rollover is appropriate even with these additional costs).</p> <p>The Financial Institution and Investment Professional should make diligent and prudent efforts to obtain information about the Retirement Investor's Plan, including information about expenses, asset values and risk, and returns based on information the Retirement Investor provides in any Plan document or based on information provided in a Form 5500. The Financial Institution and Investment Professional should document and explain the assumptions used in its recommendation.</p>	
Preamble	<p><u>Sample language:</u></p> <p>When we provide investment advice to you regarding your retirement plan account or individual retirement account, we are fiduciaries within the meaning of Title I of the Employee Retirement Income Security Act and/or the Internal Revenue Code, as applicable, which are laws governing retirement accounts. The way we make money creates some conflicts with your interests, so we operate under a special rule that requires us to act in your best interest.</p> <p>Under this special rule's provisions, we must:</p> <ul style="list-style-type: none"> <li>• Meet a professional standard of care when making investment recommendations (give prudent advice);</li> <li>• Never put our financial interests ahead of yours when making recommendations (give loyal advice);</li> <li>• Avoid misleading statements about conflicts of interest, fees, and investments;</li> <li>• Follow policies and procedures designed to ensure that we give advice that is in your best interest;</li> <li>• Charge no more than is reasonable for our services; and</li> <li>• Give you basic information about conflicts of interest.</li> </ul>	

PTE 2020-02	Policies and Procedures Requirement	Comments
II(c)(1)	<p><u>Written Policies and Procedures:</u> Financial Institutions and Investment Professionals must establish, maintain, and enforce written policies and procedures prudently designed to ensure compliance with impartial conduct standards.</p>	
II(c)(2)	<p><u>Prudent Design of Written Policies:</u> The written policies, viewed as a whole, must be prudently designed to mitigate conflicts of interest and avoid misalignment of interests, including interests in proprietary products and revenue sharing arrangements.</p> <p>Financial Institutions need to be cautious in creating certain types of compensation structures for Investment Professionals, including any quotas, bonuses, prizes, or performance standards that a reasonable person may conclude would create an incentive that is not in the best interest of a retirement investor. For example, if Investment Professional receives more compensation from a Financial Institution for one product over a comparable product, a reasonable person may conclude that the Investment Professional has an incentive to recommend a certain product. Supervisory oversight of investment recommendations (including recommendations near compensation thresholds, key liquidity events like rollovers, or recommendations for proprietary products or principal-traded assets) may provide benefits in some situations, but does not provide an effective substitute for meaningful mitigation of conflicts of interest in many situations.</p> <p>Financial Institutions should have a review process for new investment products and, if necessary, decline to recommend a product if the Financial Institution cannot mitigate the conflicts of interest with the compensation standard.</p>	
II(c)(3)	<p><u>Specific Reasons for Rollover Transactions:</u> Financial Institution has to document reasons why a rollover is in best interest of the Retirement Investor. See "Rollover Advice" in the "Disclosure Requirements" section above.</p>	

PTE 2020-02	Retrospective Review Requirement	Comments
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PTE 2020-02	Retrospective Review Requirement	Comments
II(d)(1)	<u>Annual Review</u> : Financial Institution needs to conduct a retrospective review (at least annually) that is designed to assist in detecting and preventing violations of, and achieving compliance with, impartial conduct standards and policies and procedures.	
II(d)(2)	<u>Written Report</u> : Methodology and results of the retrospective review need to be conveyed in written report provided to a Senior Executive Officer (including a chief compliance officer, CEO, CFO, president or like officer).	
II(d)(3)	<u>Certification</u> : Senior Executive Officer has to certify the following on an annual basis: (i) he or she reviewed the retrospective review; (ii) the Financial Institution has in place policies and procedures designed to achieve compliance with the conditions of the exemption; and (iii) the Financial Institution has in place a prudent process to modify such policies and procedures to ensure continuing compliance.	
II(d)(4)	<u>Due Date</u> : The report, review, and certification has to be completed by 6 months after end of period.	
II(d)(5)	<u>Recordkeeping</u> : The report, certification, and supporting data has to be retained for 6 years and must be made available to an authorized IRS or DOL official within 10 business days of a request.	

PTE 2020-02	Self-Correction	Comments
IV(a)	<p>A Financial Institution can make a self-correction of violations of this exemption if:</p> <ul style="list-style-type: none"> <li>(1) the violation did not result in investment losses to the Retirement Investor (or, if a loss did occur, if the Retirement Investor was made whole);</li> <li>(2) the Financial Institution corrects the violation and notifies the DOL of the violation and correction by email (<a href="mailto:IIAWR@dol.gov">IIAWR@dol.gov</a>) within 30 days of correction;</li> <li>(3) the Financial Institution issued corrected the violation no later than 90 days after it learned of (or reasonably should have learned of) the violation; and</li> <li>(4) the Financial Institution notifies the person responsible for</li> </ul>	



PTE 2020-02	Self-Correction	Comments
	conducting the retrospective review during the applicable review cycle and the violation and correction are set forth in the written report.	

## Related People

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