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Rollover Recommendations: The DOL Fiduciary Rule Stay and What Remains

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In light of the stay of the implementation of the new DOL fiduciary rule and current PTE 2020-02, this

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article discusses instances when the current DOL fiduciary rule and current PTE 2020-02, unaffected by the current litigation and stay, might apply to a rollover recommendation by and advisor.

The implementation of the Department of Labor's (DOL) new fiduciary rule and the amendments to PTE 2020-02 has come to a grinding halt following the stay of the September 23, 2024, effective date by two Texas federal district courts, pending the outcome of the lawsuits challenging the rule and the amended PTE. The resolution of this litigation, including appeals, could take years, and in the meantime the new fiduciary rule and the amendments to PTE 2020-02 will not take effect (and may possibly never go into effect). As a result, the current DOL fiduciary rule continues to apply and a more limited range of recommendations by broker-dealers, registered investment advisers and their representatives (collectively, advisors) will result in fiduciary status. As we discuss in this article, we think that there may be at least three instances when the current DOL fiduciary rule will apply to a rollover recommendation by an advisor, and in those instances the firm and the advisor may need the relief provided by PTE 2020-02 (that is, the version adopted by the DOL in 2020, which is unaffected by the current litigation and stay).

The "Current" DOL Fiduciary Rule

The DOL currently defines fiduciary advice based on a long-standing five-part regulatory test. The scope of this definition as it applies to rollover recommendations has changed over time; first with 2005 guidance issued by the DOL, then with a reinterpretation by the DOL in 2020, and most recently, with a Florida court decision in 2023.

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The starting place for understanding the scope of the definition is the 1975 5-part test, which says that a person is a fiduciary to an Employee Retirement Income Security Act (ERISA) plan or an individual retirement account (IRA) if:

1. the person is providing advice about investments for a fee;
2. on a regular basis;
3. under a mutual understanding with the plan fiduciary, plan participant, or IRA owner;
4. that the advice will serve as a primary basis for investment decisions with respect to plan or IRA assets; and
5. that the advice is based on the particular needs of the plan, participant or IRA owner.

Based solely on this five-part test, an advisor with no pre-existing relationship to an investor can make a one-time rollover recommendation without being considered a fiduciary because the advisor would not satisfy the regular basis component of the test.

The DOL confirmed this position in 2005 when it issued Advisory Opinion 2005-23A, commonly referred to as the Deseret letter. There, the DOL indicated that if the person was not already a fiduciary advisor to the ERISA plan, then the rollover recommendation would not be considered a fiduciary act under the 5-part test. On the other hand, the DOL said that if the person was already a fiduciary advisor to the ERISA plan, then a rollover recommendation would be considered a fiduciary act.

The DOL withdrew the Deseret letter in 2020 in the Preamble to PTE 2020-02 when it reinterpreted the "regular basis" requirement for rollovers by taking the position that a person is providing advice on a regular basis if: (1) the person has a preexisting advice relationship with the investor on tax-qualified retirement assets, or (2) anticipates that the rollover recommendation is the first step in an ongoing financial relationship concerning the tax-qualified retirement assets. Even though the Deseret letter was withdrawn, based on this reinterpretation, it appears that the DOL continues to believe that a rollover recommendation by an advisor who is already a fiduciary advisor to the plan will constitute fiduciary advice.

Then, in 2023, the court in *America Securities Association (ASA) v. U.S. Department of Labor*, [Case No. 8:22-cv-33 (M.D. Fla. Feb. 13, 2023)] set aside the DOL's expanded interpretation of the regular basis requirement for rollover recommendations from a plan to an IRA where the advisor has no preexisting fiduciary relationship with the plan. In reaching this decision, the *ASA* court reasoned that the regular basis requirement applies to the particular plan from which the rollover is made and could not be connected to the rollover IRA (because the IRA was a separate "plan").

In sum, based on the DOL's reinterpretation as limited by the ASA decision, the following can be concluded about rollover recommendations under the current DOL fiduciary rule: if an advisor has no preexisting fiduciary relationship with the plan and recommends a rollover from the plan to an IRA, it is not a fiduciary act. But what about rollover recommendations that fall outside this limitation? We think that there may be at least three circumstances in which a rollover recommendation could be considered a fiduciary act under the current DOL fiduciary rule as interpreted by the DOL and the *ASA* court.

Rollover Recommendations That May Still Be Considered Fiduciary Advice under the Current DOL Fiduciary Rule

Preexisting Fiduciary Relationship with the Plan

If an advisor is a fiduciary to the plan and that advisor (or another advisor with the firm) recommends that a plan participant roll over to an IRA with the advisor, it seems likely that this rollover recommendation would be considered fiduciary advice under the current DOL rule.

There are a number of reasons for reaching this conclusion. First, the *ASA* decision did not address these facts, that is, whether recommending a plan to IRA rollover where the advisor has a preexisting fiduciary relationship to the plan would be considered fiduciary advice. Second, under the Deseret letter and under the DOL's reinterpretation, this recommendation would be considered a fiduciary act because of the advisor's preexisting fiduciary relationship with the plan. If the rollover recommendation is considered fiduciary advice and the plan is subject to ERISA, then the advisor's recommendation will need to satisfy the ERISA duties of prudence and loyalty. Also, if the recommendation results in compensation that the advisor or the firm would not have otherwise received (for example, the IRA management fee or a commission on recommended IRA investments), the advisor and the firm will need to satisfy the conditions in current PTE 2020-02 in order to avoid a non-exempt prohibited transaction.

Preexisting Fiduciary Relationship with the Plan Participant

Let's suppose that instead of advising the plan, the advisor is managing a participant's plan account and, therefore, the advisor and the advisor's firm are already fiduciaries for the assets in the participant's plan account. Under these circumstances, if the advisor or another advisor with the firm recommends that the participant roll the plan monies to an IRA with the firm, it is likely that the DOL would consider the rollover recommendation to be a fiduciary act.

This is because the advisor's preexisting fiduciary relationship with the plan participant falls within the scope of the DOL's reinterpretation of regular basis (that is, the advisor is providing advice about the participant's account on a regular basis and the rollover recommendation is a continuation of that) and is outside the facts addressed by the *ASA* court. Therefore, if the account is part of an ERISA plan, the advisor's recommendation will need to satisfy the ERISA duties of prudence and loyalty. And, if the compensation resulting from the rollover (for example, the IRA management fee) results in additional compensation, a prohibited transaction will result unless the advisor and the firm satisfy the conditions in current PTE 2020-02.

IRA to IRA Transfers

Another circumstance when a rollover recommendation could be considered a fiduciary act under the current DOL fiduciary rule is when an adviser recommends that an IRA be transferred to an IRA managed by the advisor's firm. (While most people wouldn't consider IRA transfers to be "rollovers", they fall within the DOL's definition of a rollover.) Under the DOL's re-interpretation, this recommendation would satisfy the regular basis component of the 5-part test because it is the first step in an ongoing financial relationship concerning the IRA assets, that is, it is connected to subsequent recommendations about investing the IRA assets.

Although this type of recommendation was not directly addressed by the *ASA* court, the DOL could take the position that it was not part of the court's adverse decision on the basis that the IRA is the same "plan" with respect to that particular investor (for example, Mrs. Robbins' IRA) and management of the IRA is merely being transferred from the current firm to the advisor's firm (or, in other words, the continuing advice is to the same "plan"). Therefore, the regular basis component of the 5-part test is met. If the IRA transfer results in compensation that the advisor would not otherwise receive, the advisor and the firm will need to satisfy the conditions of the current PTE 2020-02 in order to avoid a prohibited transaction.

Compliance with PTE 2020-02 in Its Present Form

In sum, there are at least three circumstances when an advisor's rollover recommendation may be considered a fiduciary act and as such, the advisor and the firm may need to satisfy the conditions of the current PTE 2020-02 in order to avoid a prohibited transaction. In its current form, PTE 2020-02 requires satisfaction of the following four conditions:

1. The advisor and the firm must comply with "Impartial Conduct Standards," consisting of: (a) adherence to a best interest standard (that is, a standard that mirrors the ERISA duties of prudence and loyalty); (b) reasonable compensation; (c) best execution standards; and (d) no materially misleading statements.
2. The firm must furnish a disclosure to the investor before implementing the rollover that consists of: (a) an acknowledgement of the firm's and the advisor's fiduciary status under ERISA and/or the Internal Revenue Code; (b) a description of services and material conflicts of interest; and (c) a statement of the specific reasons as to why the rollover or IRA transfer is in the investor's best interest (the rollover disclosure). A rollover for this purpose is broadly defined to include a plan to IRA rollover, IRA to plan rollover, plan to plan rollover, IRA to IRA transfer and a change of retirement accounts (for example, from a commission-based account to a fee-based account). The amended PTE 2020-02, which is now stayed, would have limited the rollover disclosure to apply only to rollovers from an ERISA plan.
3. The firm must establish and enforce policies and procedures to ensure compliance with the Impartial Conduct Standards and to mitigate conflicts of interest.
4. The firm must conduct a retrospective review at least annually reduced to a written report that is reviewed and certified by a senior executive officer no later than six months after the end of the period covered by the review.

We understand that there are many firms that have already established processes to comply with current PTE 2020-02 and some may have updated those procedures to reflect the amended PTE. Firms that have updated these procedures to conform to the amended PTE will need to make sure that the rollover disclosure is provided for all covered rollover recommendations, not just rollovers from an ERISA plan.

Conclusion

Even though the new expansive DOL fiduciary rule—and its coverage of one-time recommendations—is stayed, there are still circumstances under which the current DOL fiduciary rule could apply to rollover recommendations. Firms and their advisors should identify those rollover recommendations and ensure that there are processes in place to comply with the conditions of PTE 2020-02 (in its current form). ■