

Beware of DOL Prohibited Transactions

Advisory fiduciaries need to avoid the minefield of specific ERISA and IRC customer protection rules.

So many advisors work with retirement plans and retirement investors but have little appreciation of the corresponding ERISA/Department of Labor prohibited transaction issues. I recently sat down with my colleague and our ERISA expert, Ryan Walter, to discuss the details.

Both the Employee Retirement Income Security Act of 1974, as amended, and the Internal Revenue Code contain specific sets of prohibited transactions that apply when rendering services to ERISA plans and/or participants and IRA owners, respectively.

There are three enumerated prohibited transactions that apply to ERISA and IRC fiduciaries. To paraphrase these prohibited transactions applicable to ERISA and IRC fiduciaries:

1. Dealing with the assets of the plan in the fiduciary's own interest (referred to as the "Self-Dealing Provision");
2. The fiduciary acting in any transaction involving the plan on behalf of a party whose interests are adverse to the interests of the plan or its participants or beneficiaries; or,
3. Receiving any compensation for the fiduciary's own account from any party dealing with the plan in connection with a transaction involving the assets of the plan (the "Anti-Kickback Provision").

When an advisor provides a recommendation to an ERISA or IRA client, and that recommendation results in a direct or indirect increase in compensation to the advisor, the advisor should carefully consider whether the advice will constitute a prohibited transaction.



DOL EXEMPTIONS

The Labor Department, recognizing that the broad application of prohibited transaction rules would prohibit many common and beneficial industry practices, provides several prohibited transaction exemptions.

Included in the universe of potential prohibited transaction exemptions is Prohibited Transaction Exemption 2020-02, or DOL Rule, which provides exemptive relief from the above-referenced fiduciary prohibited transactions under both ERISA and the IRC. By adhering to the DOL Rule's requirements, then, otherwise prohibited transactions can become permissible.

In short, the DOL Rule requires advisors to:

- Adhere to the Impartial Conduct Standards.
- Provide a written acknowledgment of ERISA and/or IRC fiduciary status.
- If applicable, document and disclose the rationale behind why an ERISA rollover and/or IRA transfer is in the client's best interest.
- Maintain and enforce compliance policies and procedures designed to ensure compliance with the Impartial Conduct Standards and the DOL Rule in general.

- Conduct a retrospective annual review in an effort to detect and prevent violations of, and achieve compliance with, the Impartial Conduct Standards and the conditions of the DOL Rule.

Importantly, advisors must remain aware that the DOL Rule does not provide prohibited transaction relief for transactions involving ERISA or IRA assets if the advisor, its representatives, or an affiliate is:

1. the employer of employees covered by the plan; or
2. a named fiduciary or plan administrator, or an affiliate thereof, who was selected to provide advice to the plan by another fiduciary who is not independent of that firm, its representatives, and their affiliates.

The relief provided by the DOL Rule also excludes discretionary actions on the part of the advisor. The protections that are included in the DOL Rule were designed specifically for non-discretionary investment advice arrangements. Consequently, if an advisor uses its discretion to engage in a prohibited transaction, the protections of the DOL Rule will not be available to the advisor.

Ryan cautions, if you have concerns that your compensation arrangements, investment strategies or methods of providing advice may trigger one or more of the above prohibited transactions, promptly address such concerns with counsel who is experienced in identifying and addressing prohibited transaction issues. In short: don't dabble, get real counsel regarding these critical issues. **IA**

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