Annuity

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Department of Labor “Fiduciary Rule” Resource

Your Potential Fiduciary Obligations

Important information for producers offering retirement products in the qualified marketplace

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Overview

In late 2020, the Department of Labor (DOL) under the Trump Administration created new rulemaking which likely impacts those advising and selling in the qualified marketplace. While it was unclear whether the Biden Administration would allow the rule package to proceed, that question was answered when the new administration allowed it to become effective on February 16, 2021. The rulemaking itself can be broken down into two parts: **(1)** a reinstatement of the Five-Part Test for determining "who" is a fiduciary (along with a new interpretation, which effectively broadened the scope of who now meets this test) and **(2)** the creation of a new "prohibited transaction exemption" (or "PTE"). Both of these will be discussed further below, but taken together, they likely create new compliance obligations at the producer level. The following resource document is designed to break down the new rulemaking into an easily understood summary, explaining its overall impact and further explaining what it means for you and your business. The last page will also provide a summary of how North American is handling the new rulemaking, as well as a description of new compliance requirements you will likely need to undertake in the qualified annuity market. It is also important to note that the Biden Administration's DOL has announced forthcoming rulemaking that will likely impact fiduciary status and existing PTEs. This proposal may be released as soon as Dec. 2021, but it would not take effect immediately. As a result, this DOL resource document may be subject to change.

Background and current status of the DOL Fiduciary Rule

April 2016	February 2017	June 2018	February 2021	February 1, 2022
Obama Fiduciary Rule Published	Trump Memo to examine Fiduciary Rule	5th Circuit vacates Fiduciary Rule	New Trump DOL PTE and reinterpretation allowed to go forward	End of temporary non-enforcement and rulemaking in full effect

As you can see above, the DOL "fiduciary rule" has had a turbulent ride since the original Obama rulemaking. While it will likely still undergo further rewrites, for now, producers need to understand their new potential obligations and what steps are needed to comply. Note also that while other regulatory bodies have been hard at work at creating new rules impacting recommendations of annuity products over the past few years (e.g., SEC's Regulation Best Interest and the new NAIC Annuity Suitability "Best Interest" Rule), the latest DOL rulemaking operates as an additional layer over those rules. In other words, compliance with other "best interest" rules does not eliminate the need to also comply with the new DOL rules and vice versa.

New fiduciary rulemaking – Two key parts

As mentioned above, the new rulemaking centers around two key parts:

Reinstatement of the Five-Part Test for Determining Fiduciary Status (with new interpretations)	New Prohibited Transaction Exemption (PTE 2020-02)
Since 1975, we have relied on the "Five-Part Test" for determining ***who*** qualifies as an "investment advice fiduciary" under ERISA (DOL) and Internal Revenue Code rules. The Obama era Fiduciary Rule briefly removed this test, but the subsequent 5th Circuit Court decision vacated that rewrite. The recent rulemaking effectively reinstated the old 1975 Five-Part Test word-for-word, but coupled it with a new "interpretation" of how the DOL will treat each of the five parts in the test, effectively expanding the scope of who meets the test (and thus becomes an ERISA fiduciary). The end result is that more activities and more types of advice will be swept into the definition, creating a new need for producer compliance with certain fiduciary obligations and prohibited transaction rules when selling in the qualified market.	When a producer meets the definition of "investment advice fiduciary" pursuant to the expanded Five-Part Test, the *receipt* of a commission for the sale of the recommended annuity is considered a "prohibited transaction" and requires an "exemption" to be paid. This exemption to the prohibited transaction is how we get the term "Prohibited Transaction Exemption" (or PTE) under DOL rules. Essentially, if you meet the requirements of a PTE, you are allowed an exemption to whatever the prohibited action may be, such as an ERISA fiduciary receiving a commission in a qualified sale. The DOL created a new PTE as part of this rulemaking which it believed would be broadly applicable under most distribution models. It is called "PTE 2020-02" and it is discussed further below.

Key Takeaway:

As part of the new rulemaking effort, DOL reinstated but also reinterpreted the old Five-Part Test for determining who qualifies as an investment advice fiduciary and thus expanded the universe of producers who will be required to comply with a Prohibited Transaction Exemption (such as the new PTE 2020-02 or other existing PTE) in order to receive a commission on the sale of a qualified annuity.

Determining fiduciary status – "Am I a fiduciary?"

Five-Part Fiduciary Test (and Previous Interpretation)

As noted above, since 1975, industry has relied on the "Five-Part Test" for determining who qualifies as an ERISA (DOL) investment advice fiduciary. Under the Five-Part Test, a producer is deemed to render fiduciary investment advice to an employee benefit plan (or IRA) if the producer:

(1) Renders advice as to the value of securities or other property, or makes recommendations as to the advisability of investing, 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;

(4) The advice will serve as a primary basis for investment decisions with respect to the plan or IRA assets; and

(5) The advice will be individualized based on the particular needs of the plan or IRA.

Over time, most interpreted the above to exclude those producers who sold qualified annuities within the construct of an IRA because the producer usually did not meet the "regular basis" prong (#2 above). Generally speaking, it was presumed that the "regular basis" prong required more than just a single sale and subsequent reviews with the IRA owner; it instead required, for instance, ongoing monitoring and perhaps even the ability to manage investment decisions on behalf of the IRA. In addition, it was commonly believed that insurance producers failed to meet the "mutual agreement" prong (#3 above) because both the producer and the IRA Owner would need to agree that the relationship would be fiduciary in nature.

New interpretation of the Five-Part Test and what it means for you:

While the Trump Administration's DOL formally reinstated the old Five-Part Test, it provided a new "interpretation" of each of the five parts, which challenged the assumptions industry has long held about each of the prongs. For instance, DOL stated that the "regular basis" prong can be met even if a producer is meeting with a consumer for the first time and providing, for instance, IRA rollover advice that is "intended" to be the start of an ongoing relationship. The DOL also stated that it's important to look at the expectations of the parties involved at the time a recommendation is made and stated that when parties "reasonably" expect an ongoing advice relationship at the time of the recommendation, the regular basis prong can be satisfied. However, DOL recognized that there are times when the regular basis prong is not met, such as when there is truly only a "single instance of advice" or "sporadic interactions" between the producer and the consumer. As a result, it is important for you to determine, based on your specific circumstances and specific to each recommendation you make in the qualified market, whether you'll be continuing an ongoing relationship with the consumer or not – and also consider what the consumer believes your relationship will be after the recommendation has been made.

The DOL further stated that the "mutual agreement" prong of the Five-Part Test is based on the "reasonable understanding of each of the parties," and further provides that written disclaimers of fiduciary status may not be determinative. In other words, DOL intimates that you may meet the mutual agreement prong if you hold yourself out as rendering best interest advice, and the consumer believes you are doing so in a relationship of trust and confidence – even if you disclaim fiduciary status. DOL also provided that it may consider marketing and other materials to help evaluate the parties' "reasonable understanding" with respect to the relationship created. As you can see based on the above, the DOL broadly reinterpreted and challenged long-standing assumptions about the 1975 Five-Part Test, effectively creating more situations where producers likely meet each of the five prongs and thus must comply with additional DOL rules.

Key Takeaway:

While the DOL reinstated the old Five-Part Test for determining who is a fiduciary under ERISA rules, the new interpretations of the five prongs (such as the "regular basis" prong and the "mutual agreement" prong) create more presumptions of fiduciary advice in the qualified marketplace. As a result, if you provide best interest advice on qualified money that is individualized to the needs of the consumer, intend to create an ongoing relationship with the consumer, and provide your advice for a fee or other compensation (direct or indirect), it may be advisable to presume you meet the test and thus take additional steps for compliance.

A reminder about Prohibited Transaction Exemption (PTE) rules

If you are deemed to be an "investment advice fiduciary" pursuant to the Five-Part Test described above, you will be subject to ERISA fiduciary duties and will need to comply with the requirements of a prohibited transaction exemption (or "PTE") in order to receive a commission. As a reminder, the DOL views the receipt of an insurance commission as a "prohibited transaction" if you meet the definition of fiduciary. Thus, in order to receive a commission, you must comply with the terms of an "exemption" to the "prohibited transaction" which will then permit the commission to be received.

You might recall from the Obama-era Fiduciary Rule a focus on two key PTEs that received a lot of attention – the "Best Interest Contract Exemption" and a newly revised "PTE 84-24." Those were both considered PTEs that could be utilized in order to receive otherwise conflicted commissions. When the 5th Circuit vacated the Obama-era Fiduciary Rule, it also wiped out the Best Interest Contract Exemption as well as revisions that were made to PTE 84-24 (thus reverting it to the pre-Obama 2006 version). Soon after the court ruling, the DOL issued Field Assistance Bulletin 2018-02, which essentially stated that so long as producers complied with the "Impartial Conduct Standards" (that is, best interest advice, no materially misleading statements, and receipt of no more than reasonable compensation), the DOL would provide PTE enforcement relief. For many, though, this PTE enforcement relief was no longer necessary because the revocation of the entire Obama Fiduciary Rule back in 2018 simply placed most insurance producers back in the position they were prior to the rulemaking (where they rarely met the Five-Part Test for fiduciary and thus didn't need a PTE).

As part of the new rule package, however, the expanded scope of the Five-Part Test raises the likelihood that an insurance producer will need to utilize a PTE. It should also be noted that the new package included an extension of Field Assistance Bulletin 2018-02, which extended PTE enforcement relief until Dec. 20, 2021, at which point the DOL would be enforcing compliance with PTE rules. In late October, DOL issued Bulletin 2021-02, which further extended this enforcement date to February 1, 2022.

Key Takeaway:

If you meet the Five-Part Test for fiduciary, you will need to comply with an available prohibited transaction exemption (PTE) in order to receive commissions on the sale of qualified annuity products, and the important compliance date is Feb. 1, 2022.

New PTE 2020-02

The landmark piece of the 2020 rulemaking from the Trump Administration's DOL was the creation of a new prohibited transaction exemption, PTE 2020-02. In creating this new PTE, the DOL stated its intention was to attempt to align with the SEC's Regulation Best Interest, which was finalized in 2019 and became effective in June 2020. The new PTE is broad in scope and, if its terms are met, permits the receipt of various types of compensation, such as insurance commissions, revenue sharing, 12b-1 fees, trailing commissions and more. While the DOL stated that its goal was to make PTE 2020-02 broadly available for use through many types of distribution, it included in the exemption a requirement for co-fiduciary sign-off and supervision from a limited list of "Financial Institutions." Similar to the Obama-era Best Interest Contract Exemption, only **(1)** Insurance Companies, **(2)** Broker-Dealers, **(3)** Federal and State Registered Investment Advisers, and **(4)** Banks qualify for this status, which presents a precarious compliance position for some in the independent distribution marketplace (more on this on the following page).

PTE 2020-02 also requires a number of conditions to be met by both the producer and the supervising Financial Institution. Among them, both the producer and Financial Institution must comply with **(1)** the Impartial Conduct Standards (best interest advice, no materially misleading statements, and receipt of no more than reasonable compensation), **(2)** New Disclosures (including a written fiduciary acknowledgment, description of services and conflicts, and, if there is a rollover, an explanation of why the rollover recommendation is in the consumer's best interest), **(3)** Financial Institution policies and procedures designed to mitigate conflicts of interest and ensure compliance with the Impartial Conduct Standards, **(4)** a requirement that the Financial Institution undergo an annual retrospective compliance review, and **(5)** new recordkeeping requirements.

While the DOL stated in the rulemaking package that PTE 2020-02 may be utilized for independent insurance producers and provided a few scenarios under which it could potentially be accomplished, DOL further stated that other PTEs may be utilized in lieu of PTE 2020-02. The PTE most applicable as an alternative to PTE 2020-02 is **PTE 84-24**, which will be discussed in the next section.

Key Takeaway:

New PTE 2020-02 is broadly applicable to many types of distribution and broadly permits various types of compensation to be paid. However, it is limited only to those producers working through certain prescribed "Financial Institutions" – insurance companies, broker-dealers, state and federal RIAs, and banks. The required conditions of PTE 2020-02 may fit certain distribution models better than others.

PTE 84-24 (2006 version)

As stated above, insurance producers selling annuities in the qualified market may now meet the Five-Part Test for fiduciary status and may thus need a PTE to get paid a commission. DOL's new rulemaking created PTE 2020-02 as a potential option, but suggested that other exemptions may also fit. One such PTE is PTE 84-24, which many in the industry have relied upon as the go-to for exemptive relief for annuity sales since the 1970s. One important benefit of PTE 84-24 is that it does not require a fiduciary acknowledgment to the consumer, allowing it to be used both as a PTE for circumstances under which the producer knows he or she has met the Five-Part Test for fiduciary **AND** in cases where the producer may not be certain about whether the test has been met but wants to utilize a PTE just in case that determination is later made. As a result, PTE 84-24 is a flexible PTE which many in the independent distribution space prefer to the new PTE 2020-02.

As a reminder, the Obama-era version of PTE 84-24 was ultimately overturned by the 5th Circuit, and thus all the limiting factors in that version of 84-24 were removed (e.g., limiting only to fixed-rate annuity contracts). Thus, the current version of PTE 84-24 is the 2006 version, which is broadly described in the table below. The requirements can be broken into two sections for ease of understanding: Non-Disclosure Requirements and Disclosure Requirements. See below:

PTE 84-24 Non-Disclosure Requirements	PTE 84-24 Disclosure Requirements
These requirements are not specific to the required client disclosure/ acknowledgment, but are nevertheless important for compliance with PTE 84-24: • Transaction effected in the insurance producer's **Ordinary Course of Business** • No more than **"reasonable compensation"** paid • **Recordkeeping Requirement** (retain disclosure and acknowledgment form and any additional information or documents provided to client for a period of 6 years) • **Arm's Length Transaction** (you and client are required to be on equal footing and have no shared financial interest in the transaction)	These requirements are specific to the required client disclosure/ acknowledgment. Every sale will require this disclosure to be provided to the client **prior to the execution of the transaction** and also saved in your records. The disclosure must include: • Your **relationship** as independent agent to the insurance company • Your **sales commission** (expressed as a percentage of premium for first year and for each succeeding renewal year) • A **description of charges**, fees, discounts, penalties, or adjustments under the recommended contract
Customer Acknowledgment	
Following receipt of the PTE 84-24 Disclosure and assuming compliance with the Non-Disclosure Requirements above, the customer will be presented an **acknowledgment** (which may be a part of the disclosure itself) that provides a space for the customer to sign and acknowledge in writing the receipt of the disclosure and a notation that he/she approves the sale on behalf of the IRA.	

As you can see, this PTE is largely disclosure-driven and directed at the producer level and does not include the many additional requirements of PTE 2020-02 (including the need for a supervising Financial Institution). As a result, many view this PTE as more workable than PTE 2020-02 for the independent producer space. That said, it is important to know that compliance with PTE 84-24 ultimately falls on the producer's shoulders. This is because only the producer knows the exact circumstances at the time of sale, including whether fiduciary status may or may not have been met, as well as the ultimate compensation that will be received on the sale of the product (and any additional compensation, if any, paid by a third party to the producer). While North American will create compliance resources to assist with PTE 84-24, including a sample disclosure form that may be utilized, it is ultimately the producer's responsibility to put them into action and to keep records of the signed disclosure form for each qualified sale where PTE 84-24 is utilized.

As you'll recall from the above discussion on the potential for inadvertently triggering the Five-Part Test for fiduciary, it may be a best practice to utilize PTE 84-24 whenever you recommend the purchase of an annuity with qualified money and you receive compensation. This is because PTE 84-24 can be used both in circumstances where there is a clear fiduciary relationship and in circumstances where it is unclear but may later be determined. Having complied with a PTE in the latter circumstances will help protect you from potential excise tax liability that may be assessed by virtue of triggering fiduciary status and not complying with any PTE.

In practice, some carriers may be providing you a template of the PTE 84-24 disclosure and acknowledgment form that you can use to comply with the exemption. Your obligations may vary by carrier, with some requiring you to submit the PTE 84-24 form to the company along with new business. Others may require you to keep the documentation in your records, but provide an acknowledgment to the company that you are aware of your potential obligations and have complied. Some carriers may require you to fill in your sales commission on the PTE 84-24 disclosure form while others may pre-populate it for you. Be mindful of the various carrier requirements so that your PTE 84-24 compliance process is complete before submitting an application to the carrier. For more on North American's process, see below.

Key Takeaway:

PTE 84-24 may be a more appropriate fit for independent producers compared to PTE 2020-02 and requires a specific disclosure/acknowledgment form to be provided to the customer that discloses your relationship to the carrier, your commission, and a description of charges and fees for the recommended product. In addition, the client must acknowledge receipt of the disclosure and you should keep copies of all documents involved in the sale for at least 6 years.

Doing business with North American

As you have come to expect from North American, we are prepared to provide you all the resources and information you need to understand your new compliance obligations under these new DOL rules. As part of that commitment, we have created a new producer microsite that is focused 100% on DOL resources, and which includes this guide, a template PTE 84-24 Disclosure and Acknowledgment form, and a short video called "DOL in 5" that summarizes what you need to know in just five short minutes. We invite you to visit the microsite for more information, and we will keep it updated as we learn more about any future rules or new interpretations impacting you or your business. As always, though, please note North American cannot provide individualized tax or legal advice to you, so if you have questions specific to your situation, be sure to consult an attorney or tax professional.

As described above, most producers will likely need to have a PTE in place by Feb. 1, 2022. The PTE option that many independent producers plan to leverage is PTE 84-24. If this is the choice you make, be sure to access the PTE 84-24 Disclosure and Acknowledgment form so you are familiar with it and ready to use it come Feb. 1st. (Note, if you work with a broker dealer, be sure to ask the broker dealer about its DOL plans as some may require the use of the new exemption, PTE 2020-02). For your convenience, we have created a blank template version of the PTE 84-24 form on the producer microsite, which you may use for North American qualified annuity recommendations. You are not required to use this template, however, if you have a different version you prefer because we will not be requiring it back as an in good order requirement. This is because the obligation under PTE 84-24 is at the advice provider level, including the requirement to maintain a signed copy of the form. Our template generally covers the requirement to disclose your relationship with the insurer and the description of fees/charges. It leaves blank the sections which only you would know – the ultimate compensation received and consumer information (and signature). **Reminder: we will not require this form back, but PTE 84-24 does require you to keep and maintain a signed copy in your records.**

The only new requirement you will see from North American is a new producer acknowledgment in our Consumer Profile Form which states the following:

> *"I understand that if I have made a qualified annuity recommendation as a "fiduciary" (within the meaning assigned to that term by ERISA and the Internal Revenue Code) I am solely responsible for complying with the conditions of an available U.S. Department of Labor prohibited transaction exemption (e.g., PTE 84-24) covering my receipt of sales-related compensation"*

This acknowledgment serves as a reminder to the producer to assess at the time of sale whether fiduciary status may have been triggered, and further comply with the terms of a PTE if indeed the producer believes that may be the case. If the sale is nonqualified, the acknowledgment is not applicable.

While North American will not require any specific documentation or proof of compliance as an in good order requirement, that may be subject to change in the future, as new rules or interpretations arise. For now, though, be sure to visit the DOL producer microsite and familiarize yourself with your potential fiduciary and PTE requirements.

Key Takeaway:

North American has developed optional DOL compliance resources for producers which are located on our new DOL producer microsite, including a blank PTE 84-24 Disclosure and Acknowledgment template form, which you may leverage for qualified sales. North American will not require the return of this form or any other DOL information as an in good order requirement (though note the new producer acknowledgment in the North American Consumer Profile Form). North American encourages producers to become familiar with all new DOL requirements and be prepared comply with an applicable PTE beginning Feb. 1, 2022.

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