THE NATIONAL LAW REVIEW

Reasonable Compensation for IRAs: When and How Long? Interesting Angles on the DOL’s Fiduciary Rule #26

Wednesday, November 2, 2016

DrinkerBiddle

Article By Drinker Biddle & Reath LLP
Fred ReishFredReish.com

Financial Institutions & Banking
Labor & Employment
All Federal

This is twenty-sixth article about interesting observations concerning the fiduciary rule and exemptions.

This article is a little different than most of my previous posts. However, it is equally as important. To get to the point, I am writing this article about reasonable compensation for advice to IRAs because of a common misunderstanding about the requirement.

In the last month or two, I have seen a number of articles and heard several comments to the effect that it will be difficult to determine reasonable compensation for IRAs because the rule is so new. Stated a little differently, the point is that the reasonable compensation requirement for IRAs will first become effective on April 10, 2017. That is not correct.

Section 4975(c)(1)(C) provides that the “furnishing of . . . services . . . between a plan and a disqualified person” is a prohibited transaction. However, section 4975(d)(2) permits, as an exception to that general prohibition, “any contract, or reasonable arrangement, made with a disqualified person for . . . services necessary for the establishment or operation of a plan, if no more than reasonable compensation is paid therefor.” (Section 4975(e)(2) defines a “disqualified” person as “a person providing services to the plan.” Then, 4975(e)(1)(B) defines a “plan” as “an individual retirement account.” And, (C) includes “an individual retirement annuity.”)

In other words, the reasonable compensation limitation is not new. It’s been with us for decades.

But, if that’s the case, why hasn’t there been more discussion and, in the bigger picture, more enforcement of the rule? There are two reasons. The first is that, by and large, the rule has been ignored. How is that possible? That’s because only the Internal Revenue Service can enforce the rule, but it hasn’t. In this case, the 15% excise tax under section 4975 would be enforced against the service provider, that is, the adviser. But, if the rule has been in effect for years without much publicity, why is there so much discussion now?

The answer is that the Department of Labor has, in conjunction with the fiduciary rule, issued two exemptions—84-24 for life insurance policies and fixed rate annuities, and the Best Interest Contract Exemption (BICE) for any and all investments that can be sold to plans and IRAs. Both of those exemptions—which are needed where prohibited compensation results from the investment or insurance recommendation—limit the adviser’s compensation for recommended investments and insurance products to be no more than a reasonable amount. In the case of BICE, for example, the Financial Institution (e.g., the broker-dealer) must agree that its compensation and the adviser’s compensation for their services will not exceed a reasonable amount. IRA and plan investors will be able to pursue breach of contract claims for excess compensation.

So, while the law limiting the compensation of advisers (and Financial Institutions) is not new, the enforcement mechanism will be.

While the new rules seem burdensome, I believe that a variety of services will be developed to assist Financial Institutions in determining reasonable compensation for different levels of services related to different types of products.

The views expressed in this article are the views of Fred Reish, and do not necessarily reflect the views of Drinker Biddle & Reath.

Part 1- Interesting Angles on DOL's Fiduciary Rule #1

Part 2 - Best Interest Standard of Care: Interesting Angles on the DOL's Fiduciary Rule #2

Part 3 - Hidden Preamble Observations: Interesting Angles on the DOL's Fiduciary Rule #3

Part 4 - TV Stock Tips and Fiduciary Advice: Interesting Angles on DOL's Fiduciary #4

Part 5 - Level Fee Fiduciary Exemption: Interesting Angles on DOL's Fiduciary Rule #5

Part 6 - Fiduciary Regulation And The Exemptions: Interesting Angles on the DOL's Fiduciary Rule #6

Part 7 - Fiduciary Regulations And The Exemptions : Interesting Angles on the DOL's Fiduciary Rule #7

Part 8 - Designated Investment Alternatives: Interesting Angles on the DOL's Fiduciary Rule #8

Part 9 - Best Interest Standard and the Prudent Man Rule: Interesting Angles on the DOL's Fiduciary Rule #9

Part 10 - FINRA Regulatory Notice: Interesting Angles on the DOL's Fiduciary Rule #10

Part 11-ERISA and the Internal Revenue Code: Interesting Angles on the DOL's Fiduciary Rule #11

Part 12- Potential Prohibited Transactions: Interesting Angles on the DOL's Fiduciary Rule #12

Part 13-Investment Policies: Interesting Angles on the DOL's Fiduciary Rule #13

Part 14- Investment Suggestions: Interesting Angles on the DOL's Fiduciary Rule #14

Part 15- Best Interest Contract Exemption: Interesting Angles on the DOL's Fiduciary Rule #15

Part 16 - Adviser Recommendations: Interesting Angles on DOL's Fiduciary Rule #16

Part 17 - Level Fee Fiduciary: Interesting Angles on DOL's Fiduciary Rule #17

Part 18- Best Interest Contract Exemption and IRA Advisor Compensation: Interesting Angles on the DOL's Fiduciary Rule #18

Part 19- Interesting Angles on the DOL's Fiduciary Rule #19: Advisors' Use of "Hire Me" Practices.

Part 20- Three Parts of "Best Interest Standard of Care": Interesting Angles on the DOL's Fiduciary Rule #20

Part 21- Retirement Plan Documentation and Prudent Recommendation: Interesting Angles on the DOL's Fiduciary Rule #21

Part 22-Banks and Prohibited Transactions: Interesting Angles on the DOL's Fiduciary Rule #22

Part 23-Prohibited Transactions: IRA and RIA Qualified Money: Interesting Angles on the DOL's Fiduciary Rule #23

Part 24 - Differential Compensation Based on Neutral Factors: Interesting Angles on DOL's Fiduciary Rule #24

Part 25-Reasonable Compensation Versus Neutral Factors: Interesting Angles on the DOL's Fiduciary Rule #25

Part 27 - Definition of Compensation: Interesting Angles on DOL's Fiduciary Rule #27

Part 28 - What About Rollovers that Aren't Recommended?: Interesting Angles on the DOL's Fiduciary Rule #28

Part 29- Capturing Rollovers: What Information is Needed?: Interesting Angles on the DOL's Fiduciary Rule #29

Part 30- Three Kinds of Level Fee Fiduciaries . . . and What's A "Level Fee?": Interesting Angles on the DOL's Fiduciary Rule #30

Part 31 - "Un-levelizing" Level Fee Fiduciaries: Interesting Angles on the DOL's Fiduciary Rule #31

Part 32 - What "Level Fee Fiduciary" Means for Rollover Advice: Interesting Angles on the DOL's Fiduciary Rule #32

Part 33- Discretionary Management, Rollovers and BICE: Interesting Angles on the DOL's Fiduciary Rule #33

Part 34- Seminar Can Be Fiduciary Act: Interesting Angles on DOL's Fiduciary Rule #34

Part 35- Presidential Memorandum on Fiduciary Rule: Interesting Angles on the DOL's Fiduciary Rule #35

Part 36 -Retirement Advice and the SEC: Interesting Angles on the DOL's Fiduciary Rule #36

Part 37 - SEC Retirement-Targeted Examinations: Interesting Angles on the DOL's Fiduciary Rule #37

Part 38- SEC Examinations of RIAs and Broker-Dealers under the ReTIRE Initiative: Interesting Angles on the DOL's Fiduciary Rule #38

Part 39- FINRA Regulatory Notice 13-45: Guidance on Distributions and Rollovers: Interesting Angles on the DOL's Fiduciary Rule #39

Part 40 - New Rule, Old Rule - What Should Advisers Do Now?: Interesting Angles on the DOL's Fiduciary Rule #40

Part 41 - While We Wait: The Current Fiduciary Rule and Annuities: Interesting Angles on DOL's Fiduciary Rule #41

Part 42 - Rollovers under DOL's Final Rule: Interesting Angles on DOL's Fiduciary Rule #42

Part 43 - BICE Transition: More Than the Eye Can See - Interesting Angles on DOL's Fiduciary Rule #43

Part 44 - Basic Structure of Fiduciary Package (June 9): Interesting Angles on DOL's Fiduciary Rule #44

Part 45 - DOL Fiduciary "Package": Basics on the Prohibited Transaction Exemptions: Interesting Angles on the DOL's Fiduciary Rule #45

Part 46 - How Does an Adviser Know How to Satisfy the Best Interest Standard?: Interesting Angles on the DOL's Fiduciary Rule #46

Part 47- "Real" Requirements of Fiduciary Rule: Interesting Angles on DOL's Fiduciary Rule #47

Part 48- The Last Word: The Fiduciary Rule Applies on June 9- Interesting Angles on the DOL's Fiduciary Rule #48

Part 49- The Requirement to Disclose Fiduciary Status: Interesting Angles on the DOL's Fiduciary Rule #49

Part 50- Fourth Impartial Conduct Standard: Interesting Angles on DOL's Fiduciary Rule #50

Part 51- Recommendations to Transfer IRAs: Interesting Angles on the DOL's Fiduciary Rule #51

Part 52 - The Fiduciary Rule and Exemptions: How Long Will Our Transition Be?: Interesting Angles on the DOL's Fiduciary Rule #52

Part 53 - Fiduciary Rule and Discretionary Investment Management: Interesting Angles on DOL's Fiduciary Rule #53

Part 54 - The DOL's RFI and Possible changes to BICE: Interesting Angles on the DOL's Fiduciary Rule #54

Part 55- DOL's RFI and Recommendation of Annuities- Interesting Angles on DOL's Fiduciary Rule #55

Part 56-Recommendations of Contributions as Fiduciary Advice: Interesting Angles on the DOL's Fiduciary Rule #56

Part 57- Relief from 408(b)(2) Requirement on Change Notice: Interesting Angles on the DOL's Fiduciary Rule #57

Part 58- Recommendations to Contribute to a Plan or IRA- Interesting Angles on the DOL's Fiduciary Rule #58

Part 59- What Plans and Arrangements Are Covered by the Fiduciary Rule: Interesting Angles on the DOL's Fiduciary Rule #59

Part 60- What the Tibble Decision Means to Advisers: Interesting Angles on the DOL's Fiduciary Rule #60

Part 61- The Fiduciary Rule, Distributions and Rollovers: Interesting Angles on the DOL's Fiduciary Rule #61

Part 62 - Is It Possible To Be An Advisor Without Being A Fiduciary? - Interesting Angles on the DOL's Fiduciary Rule #62

Part 63-Policies and Procedures: The Fourth BICE Requirement - Interesting Angles on the DOL's Fiduciary Rule #63

Part 64 -What Does the Best Interest Standard of Care Require?-Interesting Angles on the DOL's Fiduciary Rule #64

Part 65- Unexpected Consequences of Fiduciary Rule - Interesting Angles on the DOL's Fiduciary Rule #65

Part 66- Concerns About 408(b)(2) Disclosures: Interesting Angles on the DOL's Fiduciary Rule #66

Part 67- From the DOL to the SEC - Interesting Angles on the DOL's Fiduciary Rule #67

Part 68-Recommendations of Distributions - Interesting Angles on the DOL's Fiduciary Rule #68

Part 69- Compensation Risks for Broker-Dealers and RIA**s:** Interesting Angles on the DOL's Fiduciary Rule #69

Part 70-The Fiduciary Rule and Recordkeeper Services: Interesting Angles on the DOL's Fiduciary Rule #70

Part 71- Recordkeepers and Financial Wellness Programs: Interesting Angles on the DOL's Fiduciary Rule #71

Part 72-The "Wholesaler" Exception: Interesting Angles on the DOL's Fiduciary Rule #72

Part 73- Recordkeeper Investment Support for Plan Sponsors: Interesting Angles on the DOL's Fiduciary Rule #73

Part 74 -One More Fiduciary Issue for Recordkeepers: Interesting Angles on the DOL's Fiduciary Rule #74

Part 75 - The Fiduciary Rule: Mistaken Beliefs-Interesting Angles on the DOL's Fiduciary Rule #75

Part 76 - Discretionary Management of IRAs: Prohibited Transaction Issues for RIAs- Interesting Angles on the DOL's Fiduciary Rule #76

Part 77 - The Fiduciary Rule: Mistaken Beliefs (#2): Interesting Angles on the DOL's Fiduciary Rule #77

Part 78 - The Fiduciary Rule: Mistaken Beliefs (#3): Interesting Angles on the DOL's Fiduciary Rule #78

Part 79 - The Fiduciary Rule: Mistaken Beliefs (#4)- Interesting Angles on the DOL's Fiduciary Rule #79

Part 80 - Enforceable During Transition?: Interesting Angles on the DOL's Fiduciary Rule #80

Part 81 - The Fiduciary Rule Prohibits Commissions… or Not (Myth #6): Interesting Angles on the DOL's Fiduciary Rule #81

Part 82 - Undisclosed (and Disclosed) 12b-1 Fees: The Different Views of the SEC and DOL - Interesting Angles on the DOL's Fiduciary Rule #82

Part 83 - Part 2 of Undisclosed (and Disclosed) 12b-1 Fees: Interesting Angles on the DOL's Fiduciary Rule #83

Part 84- What Does the 5th Circuit Decision Mean for Rollover Recommendations?: Interesting Angles on the DOL's Fiduciary Rule #84

Part 85 -The Fiduciary Rule: What's Next (Part 1)? : Interesting Angles on the DOL's Fiduciary Rule #85

Part 86- The Fiduciary Rule: What's Next (Part 2)?: Interesting Angles on the DOL's Fiduciary Rule #86

Part 87 - The Fiduciary Rule: What's Next (Part 3)?: Interesting Angles on the DOL's Fiduciary Rule #87

Part 88 -The Fiduciary Rule: What's Next (Part 4)? : Interesting Angles on the DOL's Fiduciary Rule #88

Part 89 - The 5th Circuit Decision, Prohibited Transactions, and New Non-Enforcement Policies: Interesting Angles on the DOL's Fiduciary Rule #89

Part 90 - Parallels Between the SEC Regulation Best Interest and the DOL Best Interest Contract Exemption (Part 1): Interesting Angles on the DOL's Fiduciary Rule #90

Part 91- Parallels Between the SEC Regulation Best Interest and the DOL Best Interest Contract Exemption (Part 2): Interesting Angles on the DOL's Fiduciary Rule #91

Part 92 - SEC Proposed Reg BI and Recommendations of Rollovers (Part 1): Interesting Angles on the DOL's Fiduciary Rule #92

Part 93 - SEC Proposed Reg BI and Recommendations of Rollovers (Part 2): Interesting Angles on the DOL's Fiduciary Rule #93

Part 94 - SEC Proposed Reg BI and Recommendations of Rollovers (Part 3) : Interesting Angles on the DOL's Fiduciary Rule #94

Part 95 - Regulation Best Interest Recommendations by Broker-Dealers: Part 1- Interesting Angles on the DOL's Fiduciary Rule #95

Part 96 - Regulation Best Interest Recommendations by Broker-Dealers: Part 2- Interesting Angles on the DOL's Fiduciary Rule #96

Part 97 – Regulation Best Interest Recommendations by Broker-Dealers: Part 3 - Interesting Angles on the DOL's Fiduciary Rule #97

Part 98 – Regulation Best Interest: Consideration of Cost and Compensation- Interesting Angles on the DOL's Fiduciary Rule #98

Part 99 – Investment Advisers and the SEC's Interpretation of Their Duties: Interesting Angles on the DOL's Fiduciary Rule #99

Part 100 - Investment Advisers and the SEC's Interpretation of Their Duties: Part II- Interesting Angles on the DOL's Fiduciary Rule #100

© 2019 Drinker Biddle & Reath LLP. All Rights Reserved

Source URL: https://www.natlawreview.com/article/reasonable-compensation-iras-when-and-how-long-interesting-angles-dol-s-fiduciary