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ACCOUNTING & AUDIT

The Department of Labor Fiduciary Standard: Considerations for CPAs

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In April 2016, the Department of Labor (DOL) released the long-awaited Final Rule (Rule) amending the definition of the term “fiduciary” under the Employee Retirement Income Security Act of 1974 (ERISA)[1]. The Rule includes a conflict of interest rule applicable to retirement investment advice, as well as various exceptions and amendments affecting retirement plan transactions. More than 1,000 pages in length, there is much to digest for those in the business of providing advice to businesses and individuals regarding benefit plans and benefit plan investments. The Rule becomes applicable in April 2017.

While at first glance the Rule would appear to primarily impact those who recommend and sell investment products to ERISA plan trustees or beneficiaries, there are broader implications for CPAs and their firms.

Which clients are affected?

Benefit plans provided by private, for-profit employers and private, tax-exempt employers other than churches providing benefit plans are governed by the Rule. Individuals holding 401(k) accounts, individual retirement accounts (IRAs), and health savings accounts (HSAs) which provide investment options also are affected.

What types of benefit plans are affected?

The Rule applies to defined benefit and defined contribution plans qualified under Internal Revenue Code section 401(a), IRAs, and HSAs which provide investment options.

How has the Fiduciary definition changed?

Under the prior rule[2], in place since 1975, individuals or institutions that provided advice to clients on a regular basis about investments in employee benefit plans were subject to the fiduciary standard. A five-part investment advice test determined whether or not the party was considered a fiduciary adviser.

Under the Rule, the five-part test has been eliminated, and the definition of a fiduciary extends to persons who provide a recommendation about acquiring, holding, disposing of, or exchanging investments in an ERISA plan. It also extends to those providing advice about managing ERISA plans and investing plan assets. The Rule applies if a fee or other compensation is received for the recommendation, either directly or indirectly.

How does it impact CPAs in practice?

CPAs that provide investment advisory services have always been subject to the fiduciary standard. Under the Rule, the fiduciary standard now applies more broadly to anyone who provides recommendations about benefit plans or plan investments to plan sponsors or beneficiaries, and owners of 401(k) and IRA plans.

Some examples of commonly provided services that may cause CPAs to be considered fiduciaries under the Rule include:

- Recommendations to business clients about changes to existing employee benefit plans
- Recommendations to individuals about whether or not to hold, convert or roll over their existing IRAs and 401(K) plans upon retirement
- Recommendations to clients about the management of real estate held in an IRA

Areas of practice not impacted by the Rule include the issuance of valuations, appraisals and fairness opinions for employee benefit plans. The DOL has indicated this will be addressed in a separate regulatory initiative.

What are the legal liability implications?

The Rule affords a private right of action to plan sponsors, plan participants, and owners of IRAs. While it is too soon to determine how the Rule will affect litigation, lawsuits involving advice about benefit plans may increasingly allege violation of fiduciary duties under the Rule.

The DOL can likewise bring enforcement actions against advisors to plan sponsors, participants, and beneficiaries who do not provide advice in the best interest of their clients. CPAs who did not previously fall under the fiduciary definition now are also exposed to these enforcement actions.

Management Action Items

The Rule prohibits the inclusion of exculpatory language in written contracts limiting an investment advisor's liability for violation of the contract or precluding the client from participating in a class action lawsuit to enforce the terms of the contract. While this change may not affect litigation, CPA firms which have arbitration clauses in engagement letters or contracts should have them reviewed by legal counsel to avoid legal challenges to the enforceability of these clauses.

CPA firms that employ individuals licensed to sell securities or insurance, or have arrangements with third party providers to do so, need to carefully investigate

application of the Rule. The Rule contains extensive guidance regarding the conflict of interest rule applicable to commissions, brokerage fees, and certain other types of compensation. Products such as annuities and life insurance are commonly used in estate planning, and their recommendation or sale to IRA owners creates exposure to private rights of action against the CPA firm.

CPA firms that have entered into contracts with investment advisors, securities brokers, financial institutions or insurance companies should have these reviewed by legal counsel. These contracts may include arbitration provisions, indemnification and hold harmless agreements that are impacted by the Rule and increase liability exposure. These include "click-thru" license agreements and contracts used by online providers.

Insurance Action Items

Professional liability policies should be reviewed to ensure they provide coverage for investment advisory services. In light of the Rule, the ERISA policy exclusion should include an exception for the professional services provided to clients about benefit plans.

CPA firms employing individuals licensed to sell securities or insurance products should carefully evaluate insurance coverage. Professional liability policies typically exclude coverage for these activities, but coverage is offered as a supplemental endorsement. Policies provided by securities or insurance brokers for representatives employed by CPA firms should also be reviewed.

Insurance coverage should be reviewed for all third party providers doing business with the firm related to employee benefit plans. Their exposure to the Rule may have changed. Uninsured or underinsured third party service providers elevate risk to CPA firms as aggrieved parties will pursue all available means of recovery in pursuing investment losses.

Firms also should evaluate coverage under fiduciary liability policies purchased to protect sponsors of their own employee benefit plans.

Getting Help

The details of the Rule are complex, and go well beyond the scope of this article. Members of the Personal Financial Planning section of the American Institute of Certified Public Accountants can access many useful and contemporary resources on the AICPA website. Additional resources will become available through the AICPA

over time. Training courses on compliance with the Rule will be useful; consider those that are tailored to the types of advisory services offered by the firm to plan sponsors, plan participants and individual owners of IRAs and 401(k)s.

Consult with firm attorneys regarding engagement letters and contracts entered into by the firm with both clients and third party providers that involve advisory services on benefit plans and plan investments.

Lastly, review existing insurance coverage, and consider the need to increase policy limits or fill any gaps in coverage, consulting with your firm's insurance agent or broker.

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[1] Definition of the Term "Fiduciary"; Conflict of Interest Rule – Retirement Investment Advice, 29 C.F.R. §§ 2509, 2510, 2550 (2016)

[2] Definition of "Fiduciary", 26 C.F.R. §§ 4975 – 4979 (1975)

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