New Fiduciary Rules Impact Some HSAs

Issued date: 06/12/17

New rules are effective June 9, 2017 that affect investment advisors with respect to health savings accounts ("HSAs") with investment options (as well as retirement plans and IRAs). The new rules address advisors, not employers specifically, and HSAs are not the primary target of the new rules; however, there a few important items for employers to note.

Background

Both ERISA and the Internal Revenue Code impose strict rules on fiduciaries. Even though HSAs are not generally subject to ERISA, they are subject to the Code's version of the prohibited transaction rules which deem anyone offering investment advice for direct or indirect compensation to be a fiduciary.

The rules, in part, require fiduciaries to act solely in the best interest of plan participants and beneficiaries and to not profit from their positions as fiduciaries.

HSA funds may be placed in conservative investments, although only a small percentage of HSAs are set up to so allow.

Summary

Recent regulations expand the types of advice and circumstances that result in fiduciary status and are intended to better protect participants from questionable advice such as investing in high commission products, calling into question the motives of the person providing the advice.

Fiduciary status arises when a person offers certain investment-related recommendations. The 2016 regulations clarify that fiduciary advice is limited to individualized advice directed to specific parties. It may be delivered by a person who:

A. Represents or acknowledges fiduciary status;

B. Provides the recommendation under a written or verbal agreement, arrangement, or understanding that the advice is based on the "particular investment needs" of the investor (e.g., HSA owner); or

C. Directs the advice to a specific investor about the advisability of a particular investment or management decision.

Along with the 2016 regulations, the DOL finalized two new prohibited transaction exemptions ("PTEs") that allow the now-expanded group of fiduciaries providing investment advice to receive compensation otherwise prohibited under the fiduciary rules.

1. The Best Interest Contract (BIC) exemption

This exemption allows qualifying financial institutions and individual investment advice fiduciaries associated with those institutions to receive compensation despite a potential conflict of interest, if all of the following apply:

- There is a written contract.
- The financial institution and the advisers provide investment advice that is, at the time of the recommendation, in the best interest of the HSA account holder.
- The recommended transaction does not cause the fiduciary to receive, directly or indirectly, compensation for their services that is in excess of "reasonable compensation."
- Statements by the financial institution are not materially misleading at the time they are made.

2. Eligible investment advice arrangement

This exemption applies to an adviser who does not receive any fee or other compensation (including commissions, salary, bonuses, or anything of monetary value) that varies depending on the basis of an account holder's selection of a particular investment option. All of the following must apply to the arrangement:

- It must be authorized by the HSA account holder.
- Either:
  - The adviser's compensation does not vary depending upon the basis of investments (the "level" fee requirement); or
  - The advice is given using a computer model that is certified and provides unbiased allocation advice based on relevant information about the account holder and generally accepted investment theories.
- Certain disclosure obligations are met.
- An annual audit requirement is met.

Potential Impact on Employers

A plan sponsor (or service provider or other party) can provide educational information without becoming a fiduciary. For this purpose, educational information means general communications that a reasonable person would not view as an investment recommendation, general circulation newsletters, remarks, or presentations in widely attended speeches and conferences or general marketing materials. This exclusion covers communications between employees, such as human resources department staff who communicate to other employees about the plan provided they are not registered or licensed advisors under securities or insurance laws and only receive their normal compensation for work performed by the employer.

Employers should ensure they do not:

- Provide information to their employees about HSAs which crosses the line from general investment education to investment advice; or
- Benefit in some way from the advice being given.