

# Changes for Producer Award Trips at IMOs? Fiduciary Rule Suggests Turbulence Ahead

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In April 2024, the U.S. Department of Labor issued its long-awaited retirement security rule, also known as the fiduciary rule, broadening the definition of who is an “investment advice fiduciary” under the Employee Retirement Income Security Act. Although independent marketing organizations (IMOs) are not necessarily covered directly by the rule, they would likely need to make changes to their incentive trip programs because of the rule’s requirements for insurers and their producers. Litigation brought by industry groups has recently stayed the effective date of the rule, and the DOL is appealing the stays. So it is up in the air whether — and with what revisions — the rule might go into effect. At a minimum, however, the rule reflects a possible shift in the regulatory climate that warrants an assessment of the types of changes IMOs might be considering.

**Producers as “Fiduciaries”** The DOL’s retirement security rule would make producers “fiduciaries” where purchasers use assets from certain retirement accounts to fund their purchase of some insurance products such as fixed or fixed index annuities. This includes purchases with rollover funds from any account covered by ERISA or section 4975 of the Internal Revenue Code, including some 401(k) plans, private pensions, and individual retirement accounts.

**IMOs’ Role: Contests and Trips** IMOs support many producers (including independent insurance agents) who make such sales. For example, IMOs may provide producers with office space, training, compliance services, marketing, and even incentive compensation. An independent agent will work with an IMO to better compete with larger, more established insurance agencies. To incent additional sales, many IMOs run contests throughout the year and offer luxury trips as prizes for top producers. These trips often include international destinations, lavish accommodations, the opportunity to bring a companion, and amazing experiences like safaris.

**Contests and Trips Result in Prohibited Transactions by Producer/Fiduciaries** Both ERISA and the Internal Revenue Code prohibit producers who are fiduciaries from receiving compensation (such as incentive trips from third parties) for sales related to recommendations of fixed annuities they make. Unless an exemption is relied upon, such a “prohibited transaction” would trigger excise taxes and other possible liabilities for the fiduciary. Compliance with an exemption, however, keeps transactions from being prohibited under ERISA and

the Internal Revenue Code. For producers working with multiple insurers, the 2024 amendment to prohibited transaction exemption (PTE) 84-24 is the exemption they would most likely use.

**Consequences of Reliance on PTE 84-24** PTE 84-24 requires, among other things, that producers' recommendations in a sales context be both prudent and loyal to the purchaser. Further, it requires that insurers not use quotas, bonuses, special awards, etc. that a reasonable person would conclude are likely to encourage a producer's noncompliance with those duties of prudence and loyalty. Insurers must also have procedures in place that detect and mitigate conflicts of interest and ensure compensation practices are not creating incentives for producers' noncompliance with the exemption. PTE 84-24 does not by its terms impose these requirements directly on IMOs. Nevertheless, producers seeking to rely on the exemption, as well as insurers, will want assurances that IMOs' contests and trips are consistent with the requirements. They may even seek written representations and warranties from IMOs in that regard. As a practical matter, therefore, IMOs will be pressured to conform their contests and trips to the requirements of PTE 84-24. Although the DOL did not ban any specific form of compensation in its final retirement security rule, it did specifically call out exotic travel as an area of concern and questioned whether prize trips are consistent with PTE 84-24. The preamble to the rule seems to imply that, if a trip is that amazing, it will encourage producers to make imprudent or disloyal recommendations to get that last sale and qualify for a trip, in violation of PTE 84-24. The DOL did state that trips for educational conferences may be appropriate. But merely adding educational programming to exotic, luxury award trips will not necessarily make them permissible. Based on the preamble, it would still turn on whether the trip would be viewed as likely to result in recommendations that are disloyal or imprudent. Accordingly, all the facts and circumstances around each trip will need to be weighed, and clear answers often may prove elusive. Trips based on specific production levels for a single product, over a limited time, are likely candidates for change. Broader criteria for awarding a trip would help to weaken any argument that a producer's desire to win a trip improperly motivated any given recommendation. For example, the criteria for being awarded a trip could include the sale of a broader range of products over a longer time period, as well as criteria aligned with client goals, such as client satisfaction, client retention, or client retirement readiness scores. The more exotic prize trips may need to be scaled back to just "nice" trips. Adding educational content also might help. In addition to its requirements for prudence and loyalty, PTE 84-24 also requires that producers not receive more than "reasonable compensation." Reasonable compensation in the ERISA context has never meant the cheapest but has always meant reasonable based on the market, considering total cost, and the services provided. It is a facts-and-circumstances analysis. Accordingly, it may often prove difficult to obtain clarity as to whether a given luxury trip awarded as a production bonus would constitute unreasonable compensation. However, to the extent that IMOs restructure incentives to be more conservative, as discussed above, the trips they award would be at less risk of being considered unreasonable compensation. On the other hand, trips awarded by IMOs that do not participate in any such trend toward conservatism may increasingly be regarded as outside of industry norms and therefore more at risk of being considered unreasonable compensation.

## Authored By

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