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Employee Benefits Security Administration
Room N-5655
U.S. Department of Labor
200 Constitution Ave., NW
Washington, DC 20210

July 21, 2015

Re: Proposed Conflict of Interest Rule [RIN-1210-AB32]

The Pension Rights Center ("the Center") submits the following comments on the Department of Labor's proposed regulations on conflicts of interest and the definition of investment advice. The Center is a nonprofit consumer organization that has been working since 1976 to protect and promote the retirement security of American workers, retirees, and their families. The Center believes that the Department of Labor has produced an elegant and workable regulatory structure that protects retirement investors while also accommodating the reasonable and legitimate concerns of the financial industry. As we make clear in these comments, the regulations still have room for improvement to strengthen protections for consumers.

The proposed regulations would replace current ones, adopted in 1975, that tightly circumscribed the circumstances under which a person or entity becomes a fiduciary when providing investment advice to a plan or participant for a fee. The result of the original regulations is that ERISA failed to regulate much of the investment advice industry, allowing many financial advisers to provide workers and retirees with advice tainted by the conflicting interests of advisors or the firms for which they work. Too often this has meant that advisors focus on the fees generated by the advice, rather than on whether the advice is in the best interests of the saver.

In 2010, the Department of Labor recognized that these regulations were inadequate for protecting participants in the retirement savings systems as it has evolved since 1975, so it proposed a new rule on this subject. However, after reviewing comments from a broad array of stakeholders and a multi-day hearing, the DOL withdrew the proposed rule for further study,

The proposed regulations on which this letter comments is the result of several years of thoughtful consideration of comments on the withdrawn proposal; of serious study of the underlying economics of conflicted investment advice; of active coordination and consultation with other governmental agencies and the legislative branch; and of engagement with the investment industry, academics, and organizations concerned with consumer protection and retirement security. With all of this input and study, the Department has now produced more nuanced regulations that should improve the quality of investment advice for the tens of millions of participants in our tax-subsidized retirement savings system, while maximizing industry

flexibility to pursue legitimate business goals and to continue using historical compensation models for people who provide investment advice.

The Center disputes industry criticism that the rule is "unworkable." It appears that the Department of Labor has taken into account industry concerns in developing new principles-based prohibited transaction exemptions and in the careful structure and language of the proposed rule itself. The agency has threaded the regulatory needle to weave together a carefully-crafted proposal that should satisfy the majority of stakeholders.

The 1975 regulation on investment advice was not compelled by the statute. In our view, it was not faithful to the language and purpose of ERISA, and it improperly narrowed the definition of fiduciary. In addition, as the Department suggests in the preamble to the proposed rule, economic and legal developments in the fields of investments and employee benefit plans have rendered the 1975 position anachronistic and, at times, at cross-purposes with the statute. The new proposed regulations are much-needed and will mitigate structural conflicts that compromised the integrity of investment advice and resulted in unnecessarily high fees. Over time, the new rule should materially improve the retirement security of American workers.

These comments are divided into five sections: the first section provides background on ERISA and the 1975 regulations; the second section discusses why revision of the regulations is warranted, including a review of the Department's impact analysis; the third section comments on particular provisions of the proposed rule and also suggests some modifications of those rules; the fourth section considers exemptions from the prohibited transaction rules; and the fifth section responds to the Department's query on alternative proposed "best interest" proposals.

I. Background

When Congress passed ERISA in 1974, it included rules governing the conduct of fiduciaries. Senator Harrison Williams, Chair of the Senate Labor Committee and a key co-sponsor of ERISA in the Senate, explained the need for these rules when he presented the ERISA Conference Committee resolution reconciling the House and Senate versions of pension reform legislation: "Despite the value of full reporting and disclosure, it has become clear that such provisions are not in themselves sufficient to safeguard employee benefit plan assets from such abuses as self-dealing, imprudent investing, and misappropriation of plan funds."[1]

In other words, fiduciary standards were essential for the protection of participants in employee benefit plans. Congress crafted rules applying fiduciary standards not only to plan trustees, but to a range of individuals and entities whose actions affect the security and use of plan funds and the benefits of participants. These rules of conduct applied to "fiduciaries," which Congress defined as any person who fits one of the following categories:

(1) exercises any discretionary authority or discretionary control respecting management of a plan;[2]

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[1] Comments of Senator Harrison Williams, Legislative History of the Employee Retirement Income Security Act of 1974, Vol. III, at 4741(Aug 22, 1974)(comments concerning the Committee of Conference on H.R. 2).

[2] ERISA § 3(21)(A)(i).

(2) exercises any authority or control respecting management or disposition of a plan's assets;[3]

(3) renders investment advice for a fee or other compensation, direct or indirect, with respect to any monies or other property of a plan, or has any authority or responsibility to do so;[4] or

(4) has any discretionary authority or discretionary responsibility in the administration of a plan.[5]

The 1975 regulations addressed the third aspect of the definition – a person who renders investment advice for a fee. The regulations narrowed the statutory language (which broadly provided that a person is a fiduciary if he/she renders investment advice "for a fee or other compensation, direct or indirect, with respect to any moneys or other property of" a plan) to two narrow circumstances: first, if a person has discretionary authority or control with respect to purchasing or selling securities or other property for a plan;[6] and second, if a person renders investment advice to a plan on a *regular* basis, pursuant to an agreement or understanding that the advice will be a *primary* basis for the plan's investment decisions, and that the advice is *individualized* to the particular needs of the plan.[7]

This rule is often described as a five-part test, with a person found to be a fiduciary only if all five parts of the test are met. A person who provided investment advice could thus easily avoid being characterized as a person "who renders advice under the statute" fiduciary responsibility simply by indicating that he did not intend his recommendations to be the primary basis for an investment decision or by not providing advice on a regular basis.

The regulations also provided, in effect, a definition of the type of advice that concerned plan investments: advice concerning the value of securities or property, or advice concerning the advisability of investing in, purchasing, or selling securities or other property.

A year after the 1975 regulations were promulgated, the Department held that a consultant who provided an evaluation of employer securities for an ESOP was not a fiduciary under the regulatory definition, because the valuation would not "involve an opinion as to the relative merits of purchasing the particular employer securities in question as opposed to other securities," and would thus not serve as a "primary basis" for plan investment decisions nor "constitute advice as to the value of securities."

The 2010 proposed regulations offered a simpler and more easily understood, enforceable, and administrable test that bore increased fidelity to the statutory language and was designed in part to address developments over the intervening 35 years in the areas of retirement plans and investments. The new test would have provided that a person renders investment advice for a fee

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[3] ERISA § 3(21)(A)(i)

[4] ERISA § 3(21)(A)(ii)

[5] ERISA § 3(21)(A)(i

[6] We note that a person who has such authority would be an investment adviser even without the "investment advice for a fee" component of the statutory definition, since the person would be exercising discretionary control of a plan asset.

[7] C.F.R. § 2510.3-21(c)(1)(ii)(B).

under ERISA if the person gives certain types of advice to a plan, plan fiduciary, or plan participant or beneficiary, and also falls within certain categories of persons.

The Pension Rights Center was generally supportive of the 2010 regulations, although we criticized some provisions of the regulation, especially a seller's exemption, which we argued should be restricted in scope to fiduciaries of large plans. The regulations also asked for comments on whether advice on plan distributions should be characterized as investment advice, a position that the Center and other consumer groups generally supported.

Some segments of the investment industry criticized the proposed regulation, arguing that it would prohibit certain common compensation arrangements, which might result in retirement savers with small account balances losing access to investment advice.

They also argued that the proposed 2010 regulation could create fiduciary status in unintended situations -- for example, when employees of a plan sponsor help the plan sponsor review investment and potential investment options for the sponsor's 401(k) plan. There were also comments that argued that individuals who valued property for plans, particularly employer stock and employee real property, were already adequately regulated by state law and industry standards and that enveloping them in fiduciary status would add costs to plans without adding commensurate value for plan participants.

Over the next several years, the Department considered these and other comments and also conducted a thorough analysis of the benefits and costs of a new rule. On April 14, 2015, after concluding that the rule's benefits vastly exceeded its costs, it proposed a new carefully-crafted rule.

The new rule reflects many of the comments on the withdrawn rule. For example, it generally limits the seller exemption to sales presentations to certain fiduciaries of larger plans, who would have the sophistication to evaluate the merits of particular investments and to make their own informed judgments about the merits of particular investments. The rule also specifies that advice on plan distributions is investment advice. The rule further adds new principles on the distinction between investment education and investment advice to prevent attempts to camouflage investment advice as investment education.

The proposed rule also includes changes prompted by concerns raised by industry. The new rule, for example, has an expanded list of carve-outs, and is accompanied by new prohibited transaction exemptions and amendments to existing prohibited transactions -- most significantly an exemption for investment advisers and financial institutions who enter into a contract with a retirement saver and agree to act in the client's best interest and to mitigate and control conflicts.

The Best Interest Contract exemption permits financial firms considerable flexibility with respect to how they compensate investment advisers and institutions, including the use of indirect compensation, such as revenue sharing and 12b-1 fees. One of the new fiduciary carve-put provides that appraisers are not fiduciaries when they render appraisals, fairness opinions, or statements of value to an ESOP. The preamble to the regulations indicates that the Department is separately considering issues related to ESOPs.

II. Revision of the 1975 Regulations is Warranted

a. The 1975 Regulations Improperly Narrowed the Meaning of Investment Advice under the Statute

The centerpiece of Title I of ERISA is its definition of fiduciary and the rules that govern a fiduciary's conduct. In particular, fiduciaries are required to act in the exclusive interest of plan participants and their beneficiaries and to exercise prudence in the exercise of their plan responsibilities. Title I of ERISA also prohibits a fiduciary from causing a plan to engage in a prohibited transaction with a party in interest, and the Internal Revenue Code imposes a significant tax on the amount involved in a prohibited transaction. An important effect of the rules governing fiduciary behavior is to limit self-dealing and other conflicts of interest of fiduciaries, which Congress determined was critical to the goals it enacted ERISA to advance. Who is a fiduciary is critical to the statutory scheme.

Section 3(21)(A) of ERISA defines the term fiduciary and plainly states that a person is a fiduciary if he or she "renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so." The 1975 regulations narrowed the scope of this language by limiting it to investment advice that was "regular," rather than one-time or episodic; advice that was rendered pursuant to an agreement or understanding that it would be a "primary basis" for investment; and advice that is "individualized" to the particular needs of the plan.

These limitations are not consistent with the plain meaning of the term "investment advice," and, given the remedial character of ERISA, can be said to have impeded rather than to advance the congressional goals of limiting self-dealing and of assuring prudent investment of plan assets. The regulatory definition is also inconsistent with judicial language indicating that Congress generally intended the term fiduciary to be "broadly" construed.[8]

b. Speculation on the Reasons for the 1975 Regulatory Constriction on the Statutory Language

The preamble to the 1975 regulations did not provide a clear explanation for why the Department narrowed the statutory meaning of investment advice. If there was any additional explanatory material, it no longer exists. It is possible that the Department wished to reassure banks and other financial institutions that the new statute did not create new legal uncertainty when they did routine work for plans. Moreover, 1975 predated the line of Supreme Court decisions that held that relief against non-fiduciaries was limited to traditional equitable remedies, so the question of who was a fiduciary would have appeared to be less consequential than it does today.

Moreover, as we discuss further below, the retirement plan world was different in 1975 from what it is today. Forty years ago, defined benefit plans held most retirement assets, covered the majority of plan participants, and almost always paid benefits in annuity form. And in 1975, defined contribution plans were typically invested in pooled, professionally managed portfolios

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[8] *See*, e.g., *LoPresti v. Terwilliger*, 126 F.3d 34, 40 (2nd Cir. 1997).

rather than in assets selected by individual participants. Thus, even in the defined contribution employer plans of yore, participants were generally shielded by plan fiduciaries and their advisors from individual responsibility for investments. At the time, Individual Retirement Accounts were still curiosities and comprised a small portion of total national retirement savings. And Congress had not yet added section 401(k) to the Internal Revenue Code.

The Department of Labor would have had to display nearly perfect clairvoyance to predict that the intervening 40 years would make the individual participant the fulcrum for investment and retirement distribution strategies and a significant consumer of investment advice. It did not and thus did not foresee the regulations' negative future effects.

And two other points are relevant here: first, the Department of Labor employees who wrote the 1975 regulations had only limited experience in fiduciary regulation, having been transferred to the Pension Welfare Benefits Administration from the Fair Labor Standards Administration after the enactment of ERISA. Second, consumer-oriented and labor organizations apparently did not comment on the regulations, so there was little counterpoint to industry support for the rule.

As a result, in 1975, the Department may well have perceived that the rule would reassure the financial industry about the impacts of the new statute while imposing few if any costs on the ability of American workers to build financial security for retirement. The view about costs, as we now know, was a wildly inaccurate perspective with destructive consequences. The regulations were not only inconsistent with the statute but have, as the Department of Labor's regulatory impact study now clearly demonstrates, diminished the financial security of millions of Americans.

c. The Evolution of the American Retirement System Since 1975

There have been significant changes in the retirement plan and investment landscape that have undermined whatever arguable justification there might have been in 1975 for the regulations' cramped scope. As the preamble to the new rules note, there has been a seismic shift in the retirement plan world from defined benefit plans—in which investment advice was generally rendered to sophisticated plan fiduciaries—to self-directed defined contribution plans—in which investment advice is issued to individual participants, who often lack significant investment experience and knowledge. Mutual funds, and sellers and brokers for mutual funds, who played a relatively small role in retirement plans when ERISA was enacted, have become dominant players in the new economic order. The variety and complexity of investment products has also increased markedly over the last four decades.

There have also been significant and unanticipated legal developments since the 1975 regulations were promulgated. As we noted, the Supreme Court in 1993 ruled that a participant generally is entitled to legal relief under ERISA only against a defendant who is a fiduciary whose breach of duty caused monetary loss to a plan. Legal relief is not available against a non-fiduciary even when a non-fiduciary knowingly and for personal profit assisted a fiduciary in the commission of such a breach. A participant can sue a person other than a fiduciary only for traditional forms of equitable relief. The DOL, which filed amicus briefs arguing against these positions, could not have known in 1975 that the combination of its narrowly drawn regulation, the limitation on available remedies, and ERISA preemption would effectively create an ineffectively regulated

playing field for so many actors who have a direct and substantial impact on plan investment performance.

Another important change is simply the growth of assets held by qualified retirement plans. In 1975, defined benefit plans and defined contribution plans held $300 billion in assets. In 2015, these plans held about $8.6 trillion dollars of assets. Individual Retirement Accounts account for another $7.4 trillion, and insurance annuities an additional $2.9 trillion.[9] Clearly, retirement plans are today a critical market for virtually all serious capital market participants. It is, simply, where the money is.

Thus, in today's new order, the people and institutions who help individual participants and small 401(k) plans navigate the complex geography of investing for retirement are essential to helping Americans prepare financially for retirement. Where in 1975 they may have stood on the periphery of the statutory scheme, today they stand in its epicenter. To exempt them from the statute's prohibitions against conflicts and self-dealing undermines Congress' goals in enacting ERISA and in encouraging plans with generous tax subsidies.

d. The Negative Costs of the 1975 Regulations Have Been Substantial

Because of the 1975 regulations' artificial constriction of the meaning of investment advice, many individuals and institutions that provide investment advice have been effectively immunized from meaningful ERISA regulation. While they have been subjected to regulation under other regimes, those other regimes do not always impose a best-interest standard or prohibit conflicts of interest. As a result, many vendors of investment recommendations have operated under conflicts of interest.

Conflicts of interest can incentivize investment advisors to recommend investments that maximize fees to the advisor, when the client is better served by investments that generate lower fees. Conflicts of interest can also lead advisors to recommend that retirement savers take distributions from plans in which fees are low and roll over the distribution into Individual Retirement Accounts, where fees are typically higher and legal protections reduced. Similarly, investment advisors have financial incentive to encourage pension plan participants to take lump-sum payments in lieu of a plan annuity, foregoing the substantial benefits of an annuity.

Moreover, exotic, complex investments often pay higher fees to those who recommend and sell them, even though such investments may be expensive and present risks that make such investments suboptimal for many retirement savers. Actively managed funds designed to maximize income generate higher fees for brokers who recommend and sell them, but such funds often invest in riskier assets than other funds and thus may not be optimal for older investors who should not bear such risk. Yet the Center has seen cases in which octogenarians have been advised to invest a majority of their assets in volatile funds or in other high-risk securities. Relying significantly on independent research, the Department documented substantial gains to retirement investors from the proposed rule, perhaps as high as $1 trillion over a 20-year period.

[9] Federal Reserve Board of Governors, Flow of Fund Accounts of the United States, Table L.226, pg. 127, June 11, 2015.

Even if a fraction of these gains were realized for participants, the revised rule's benefits would dwarf the compliance and other costs associated with it.

We anticipate several arguments being raised against the regulatory analysis. First, we believe that some commentators will argue that the research relied upon by the analysis is inconclusive and that the potential benefits are speculative, because there is no way to determine whether most investment advisors in fact act on conflicts of interest. But the notion that a class of actors—in this case investment advisors—are immune from conflicts of interest, is a counterintuitive assertion with virtually no empirical support. While there are certainly some investment advisors that successfully resist yielding to conflicts of interest and/or are subject to business models and compensation structures that control them, many advisors who receive higher compensation for selling certain products than others will act, consciously or not, to maximize their own compensation at a significant cost to their clients. Moreover, advisors who do not act on such conflicts should not incur substantial costs from complying with the proposed rules.

Some have also argued that the rules will result in investment firms deciding to withdraw from offering advice to investors with small account balances and from providing assistance to smaller plans. But such predictions are speculative, based on selective and questionable assumptions and/or manipulated "survey" data. One study commissioned by a "coalition" of unidentified businesses concludes that 30 percent of small-plan employers will drop their plan if the new regulations take effect. However that survey suggested to respondents that they will be unable to obtain assistance from financial firms if the proposed rule is adopted before it asked if they will continue to sponsor their plans.

Moreover, the "best interest contract" exemption from the prohibited transaction rules will permit firms to continue to compensate advisors with various forms of commission and indirect payments. In addition, our market economy is remarkably resilient and has a genius for creating innovative mechanisms to serve markets. The proposed rule will not reduce the demand for investment advice, and innovative firms will continue to find efficient ways to service and profit from that demand. We have confidence that financial advisors can provide investors with good advice at least as efficiently as it can provide conflicted advice.

We also note that some opponents of the new rule display a chameleon-like assessment of the sophistication of the average investor. On the one hand, they argue that investors are sophisticated enough to evaluate the impact of conflicts of interest of their advisors, but on the other hand implying that the same investors may be unwilling to pay for investment advice unless the cost of that advice is hidden from them.

e. The Current Regulations Create Legal Uncertainty

The 1975 regulations incorporate inherently vague concepts into the definition of investment advice, which impede enforcement efforts under the statute. The regulations do not define what is meant by providing advice on a "regular basis," what is meant by advice that will be "a primary basis" for the plan's investment decisions, nor what is meant by advice that is "individualized to the plan's" needs. These must be determined on a case-by-case basis. The inherent ambiguity and subjectivity of these concepts creates uncertainty in the law and strains

Departmental, judicial, and private resources in litigation of issues not related to the core concept of investment advice.

The problems of the regulatory definition are illustrated in judicial decisions. *In Farm King Supply, Inc. Integrated Profit Sharing Plan and Trust v. Edward D. Jones & Company*, 884 F.2d 288 (7th Cir. 1989), a plan followed a brokerage firm's conflicted investment advice and suffered a loss, but the court held that the brokerage firm was not a fiduciary because "there was no mutual understanding that Jones' advice would be a *primary basis* for Plan investments." In another case, *Bhatia v. Dischino*, 2010 WL 1236406 (N.D. Tex. March 30, 2010), the trial court held that an actuarial consulting firm was not a fiduciary under the regulations, because the plaintiffs did not plead adequate facts to show that the firm "rendered advice on a regular basis as part of a mutual agreement that such advice serve as the primary basis of investment decisions."

The Department has explained that developing proof of the elements of the regulations, even where proof exists, has slowed and impeded enforcement of ERISA for the Department of Labor. The lack of support in the statute for the conditions in the regulation and the difficulties for enforcement are reasons enough for the regulation. But the Center would like to point out that Congress intended that ERISA would be enforceable by ordinary participants and beneficiaries who, unlike the Department of Labor, do not have subpoena power and have no ready access to the documents and testimony that would demonstrate fiduciary status under the detailed existing regulation. This has always been a severe impediment to enforcement of fiduciary responsibility by private plaintiffs, but it has been greatly exacerbated in recent years because the Supreme Court has adopted a "plausibility" standard for the evaluation of complaints on a motion to dismiss.

As a consequence, complaints alleging fiduciary status may be dismissed if they fail to allege factual support for some element of the regulation, and factual support will typically be unavailable or limited without discovery. See e.g. *Glen Ridge Surgicenter, LLC v. Horizon Blue Cross Blue Shield of New Jersey*, *Inc*., No. 08-6160 (JAG), 2009 WL 3233427, at *6 (D.N.J. Sept. 30, 2009) ("[P]roof of [defendant]'s fiduciary status is an element of the fiduciary duty claim, and 'a formulaic recitation [in the complaint] of the elements of a cause of action will not do.'" (quoting *Bell Atl. Corp*. v. *Twombly,* 550 U.S. 544 (2007)); see also *Braden v. Walmart Stores, Inc.,* 588 F.3d 585, 598 (8th Cir. 2009) (discussing the problem that participants are often without access to information that would allow them to plead factual support for each element of a claim).

III. Comments on Proposed Regulations

The Center strongly supports the Department's proposed rule generally and has the following specific comments.

a. Distribution Advice and Management of Securities

The Department of Labor's current position is that advice on whether to take a distribution from a plan does not in itself result in fiduciary status for the person rendering such advice. Section 2410.3-21(a)(1) of the proposed rule would reverse this position by providing that ". . . a

recommendation to take a distribution of benefits" is investment advice. See also Section 2410.3-21(a)(2) ("a recommendation as to the management of securities or other property to be rollover over or otherwise distributed from the plan or IRA" is investment advice). We believe that this aspect of the rule is critical to the retirement security of millions of Americans and that such advice should meet the dictionary meaning of investment advice.

We note that the decision on whether to take a lump-sum distribution from a plan can have profound effects on someone's future financial security in retirement. In some cases, the decision to move assets from a defined contribution plan to an individual retirement account by rollover or direct transfer can result in the retirement saver paying higher fees for similar investment assets and can also result in loss of access to plan investment options that may not be available in an IRA. The effects of such a decision can be especially profound in a pension plan, where a participant loses the benefits of having benefits paid as an annuity or, in the case of a married participant, a joint-and-survivor annuity.

While there are certainly situations in which a distribution of benefits from a plan, defined benefit or defined contribution, is warranted, in many situations -- if not the great majority of situations -- such a decision will have significant costs to the participant taking the distribution. The person providing advice to take a distribution, however, typically has strong financial incentive to recommend taking the distribution. In a draft paper, which we attach as an appendix to these comments, the authors provide an example of how conflicts of interest can lead to poor advice in the context of rollovers.

We thus strongly support this proposed change to current law.

b. Circumstances Under Which a Person Renders Investment Advice

The proposed rule provides that a person who provides investment advice is a fiduciary if the person either represents or acknowledges fiduciary status or if the advice is rendered "pursuant to a written or verbal agreement, arrangement or understanding that the advice is individualized to, or that such advice is specifically directed to the advice recipient for consideration in making investment or management decisions with respect to securities or other property of the plan or IRA." Proposed Rule Section 22510.3-21(a)(2)(ii).

We are concerned that the reference to an agreement, arrangement, or understanding may be interpreted as required bilateral or shared understanding by both the retirement investor and the advisor that advice is being directed toward the advice recipient. We believe that a person or entity may provide investment advice even in the absence of such a bilateral or shared understanding. More specifically, we believe that a person offers investment advice if, under the totality of circumstances, it appears that a person is offering advice to another person regarding an investment or management decision related to assets of a plan or IRA, regardless of whether there is a bilateral, common, or shared understanding that advice is being provided.

c. Sales Carve-out

The 2010 proposed regulations provided that a person shall not be considered to be a fiduciary investment adviser if such person can demonstrate "that the recipient of the advice knows or,

under the circumstances, should have known, that the person is providing the advice or making the recommendations in its capacity as a purchaser or seller of a security or other property, or as an agent of, appraiser for, such a purchaser or seller, whose interests are adverse to the interests of the plan or its participants or beneficiaries, and that the person is not undertaking to provide impartial investment advice." We believe that this accommodation is appropriate when a "sales" presentation is provided to a sophisticated plan fiduciary, but not when it is given to individual participants or their beneficiaries.

In our experience, most plan participants will not be able to discern whether advice is impartial or conflicted. In addition, even if there is disclosure, in a one-to-one meeting, whether in person or by phone, an unsophisticated investor will often regard the adviser as acting in his interest. This is particularly true if the participant does not have access to other advisers. Indeed, an adviser's success may depend on a client's belief that the adviser is interested primarily in the customer's welfare, despite a declaration of self-interest. There is the further fact that most participants will not be knowledgeable about the types of fees and benefits that can accrue to the purchaser or seller of securities.

The new proposed rule eliminates the sales exception for individual participants. The sales exception remains as part of a carve-out for counterparty transactions, but this carve-out is appropriately limited to sophisticated plan fiduciaries. Eliminating the sales exception for individuals is a critically important revision to the proposed rule and we urge the Department to retain it in the final rule.

d. Investment Education Carve-out

The proposed rule, like the 2010 proposed rule before it, provides that a person does not become a fiduciary when that person only provides investment education. The 2010 proposed rule referred to previous guidance distinguishing investment education from investment advice. See DOL IB 96-1. That guidance permitted investment education to include references to investment products (as illustrations) sold by the provider of the education. Research has shown that such references can have powerful anchoring effects, and this can be expected to influence recipients favorably to the products referenced. In effect, such educational activities comprise a sophisticated sales presentation and should be regarded as such. Thus, we believe the proposed regulations, which do not allow investment education to refer to specific products, are far more protective by creating a stronger line between investment education and invest advice, and this distinction is critical and should be retained in the final rule.

e. Applicability of Proposed Rule to IRAs

As a general comment, we laud the clarity with which the proposal states that the proposed rules will apply equally to IRAs as well as ERISA plans. IRA assets now constitute about one third of all private retirement savings. While plan participants continue to earn their private retirements benefits almost entirely in employer plans, the investment of those savings after termination of employment, including the distribution of those benefits throughout their retirement years, is increasingly being made from IRAs to which they have rolled the lump sum benefit they earned under their traditional pension plan or their 401(k)-type plan. After such a rollover, there is no ERISA protection or employer support, and this has led to some high-fee abuses The argument

that the Department should not be regulating IRAs ignores that Reorganization Act No. 4 of 1978 expressly granted the Department of Labor regulatory authority to define the term "fiduciary" for purposes of both the Internal Revenue Code and ERISA.

f. Carve-out for ESOP Advisors

The proposed rule generally provides that an appraisal, fairness opinion, or similar opinion is investment advice and a person who provides it generally a fiduciary. Prop. Rule Section 2510-21(a)(1)(ii). The rule, however, includes a carve-out for persons who provide such investment advice to an ESOP. The Labor Department indicates that it is separately studying issues relating to ESOPs and presumably the issue of whether appraisers of employer securities.

The carve-out, even if only temporary, is unfortunate, since proper valuation of stock in an ESOP maintained by a closely-held corporation is critical to the fairness of such ESOPs. Whether incorrect valuations are frequent or infrequent is a contested issue, but when it happens participants in plans suffer and should have recourse if the appraiser acted improperly. There is no reason to grant ESOPs a special agency exemption from an essential part of ERISA's fiduciary structure.

In any event, there is no clear evidence that ERISA fiduciary liability would result in significantly higher costs to plans, especially given the procedural and substantive obstacles that private parties and the Department of Labor face in ERISA fiduciary litigation. We would urge the Department to either remove the carve-out or provide that the carve-out will sunset within a reasonable period of time.

g. Carve-Out for Platform Providers

The proposed rule includes a carve-out for providers of investment platforms, so that they do not become fiduciaries when a person "merely markets and makes available to an employee benefit plan… a platform or similar mechanism from which a plan fiduciary may select of monitor investment alternatives, including qualified investment alternatives." Yet marketers of investment platforms can limit the investment options from which a fiduciary may choose and may be influenced by the payments they will receive from the vendors of the investment products available on the platform. We thus believe the broad carve-out may permit conflicts that should be controlled. We suggest eliminating this carve-out and substituting a prohibited transaction exemption that requires disclosure and mitigation of conflicts.

IV. Comments on Prohibited Transaction Exemptions

The proposed rule was accompanied by a package of new prohibited transaction exemptions and amendments to existing exemptions. The package is meticulously constructed, and the heart of it -- the Best Interest Contract exemption -- succeeds in mitigating the impact of conflicts while preserving substantial flexibility for financial institutions to market their products and compensate those persons who recommend and sell them. Notwithstanding the Department's success in creating the package, there is room for improvement at the margins and we provide some comments to this end. We also respond to the Department's request for comments on whether it should adopt a streamlined exemption for low fee, quality investment vehicles.

a. The Best Interest Contract Exemption Should Be Amended to Clarify that It Applies to Rollover Advice Provided by Either a Third-Party Call Center or Advisors Not Affiliated with the Plan.

Some comments on the proposed Best Interest Contract exemption suggest that it is not applicable to advice concerning plan distributions. While we read the exemption to clearly cover such advice, the Department should make the language more specific to clarify that it applies to distribution and rollover advice, which as detailed earlier, is critical to protecting workers and retirees. The Department should also consider whether special contract formation rules might be appropriate when advice is being provided through persons at a call center, although any such rules should be tailored to ensure that the participant fully understands the nature of the contract at the point of initial communication with the call center and that the execution of the written contract occurs within a reasonably short period following the initial communication.

b. The Exemption Should Not Endorse Arbitration When Fiduciary Advice is Rendered to a Plan or to a Participant or Beneficiary in a Plan.

The proposed Best Interest Contract exemption requires the contract to provide for resolution of disputes and explicitly sanctions binding arbitration for individual claims. In our view, this undercuts ERISA's private enforcement scheme and the express Congressional purpose of "providing ready access to federal courts." ERISA Section 1(b), 29 U.S.C. 1001(b).

The exemption should be amended to bar mandatory arbitration clauses in disputes involving a plan fiduciary and a plan participant or beneficiary. Such clauses should be limited to disputes regarding investment and management decisions related to an existing Individual Retirement Account, where there are no existing federal remedies other than the imposition of the Section 4975 tax on amounts involved in prohibited transactions. The exemption should also prohibit contractually modifying the ERISA statute of limitations for claims against fiduciaries and should similarly prohibit contractual restrictions of other ERISA jurisdictional, remedial, or substantive provisions.

c. Thoughts on the Appropriateness of a Streamlined Exemption for Certain Investment Options.

The Department of Labor has asked for comments on whether it should provide a streamlined version of the Best Interest Contract exemption for advisors offering high-quality, low-fee investment products. In our view, there would be several difficult conceptual problems to negotiate in order to create such an exemption. Such difficulties include defining the concepts of low-fee and high-quality for investment products.

We are also concerned that such designation may itself become the equivalent of a consumer seal of approval, which may result in investors focusing only on such products and perhaps not developing appropriate investment strategies. Such designation might also have profound consequence in future product development, stifling innovation. Nevertheless, the notion of a streamlined exemption is intriguing and is worth exploration but perhaps not on the same time track as this proposed rule.

V. Alternative "Best Interest" Standards

SIFMA and others have offered alternative proposals that they characterize as based on a "best interest" standard that they argue would not impose unnecessary burdens on the industry nor result in unintended consequences. These proposals, however, are at best an uneasy, uncertain, and inadequate compromise between suitability-type and true best-interest standards. The proposals tolerate disclosure as a remedy to conflicts of interest – which we know does not work; and the factors that would be used to measure compliance are sufficiently numerous that the overall effect is one of vagueness and subjectivity and not dissimilar from the standards now used to measure compliance with a suitability standard.

In short, the proposals require identification of conflicts rather than meaningful mitigation of conflicts. While they reflect a minor shift in emphasis, at their heart the proposals wrap a suitability standard in more attractive packing. Such proposals are not suited toward ensuring that the tens of millions of retirement savers are given advice unfiltered through the myriad conflicts that distort its quality in the current world.

They are a last-ditch effort by the industry to defeat a well-crafted rule that was developed over years with the input of all stakeholders. They are no substitute for the rule.

Conclusion

Our nation depends on employee plans and individual retirement plans to help Americans build financial security for their retirement. At the individual level, the success of this enterprise means comfort and dignity in retirement; at the aggregate level, it serves and implements vital societal goals.

It is for these reasons that Congress subsidizes the retirement system with generous tax subsidies, and it is for these reasons that Congress enacted ERISA to ensure that the system serves and protects the interests of plan participants.

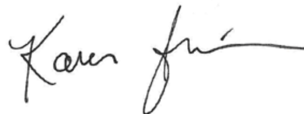
Some have argued that our securities laws can adequately protect the interests of retirement savers and, by implication, that the more protective ERISA regime was neither needed nor intended by its Congressional authors. This is simply wrong and misguided. Securities law is intended to ensure honesty in markets and to check fraud and sharp practices. It is based on disclosure and honest behavior.

ERISA, on the other hand, was designed to ensure that Americans can build adequate financial security for that period in their life when they no longer participate in the workforce and to ensure that their reasonable expectations are protected. It is for these reasons that ERISA is organized around a fiduciary standard—the highest standard of behavior in law—to eliminate rather than merely to disclose conflicts of interest. As Harrison Williams, one of ERISA's two principal sponsors in the Senate, observed about the statute's fiduciary anatomy, "…despite the value of full reporting and disclosure, it has become clear that such provisions are not in

themselves sufficient to safeguard employee benefit plan assets from such abuses as self-dealing, imprudent investing, and misappropriation of plan funds."[10]

The Department has worked mightily to construct a regulatory regime consistent with this purpose. It has modified its 2010 proposal to reflect legitimate industry concerns. It has consulted and coordinated with the Securities Exchange Commission and others to ensure that its rules do not undermine the SEC's own mission nor create unnecessary burdens for business. The Department deserves high praise for its efforts to date, and we encourage it now to complete its work -- so essential to the protection of the American worker -- with due expedition.

Respectfully Submitted,



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[10] Comments of Senator Harrison Williams, supra, note 1.