Marc R. Bryant
Senior Vice President
Deputy General Counsel
Fidelity Investments
245 Summer Street V13E, Boston MA 02210
617.563.0276 MARC.BRYANT@FMR.COM

August 11, 2017

Submitted electronically

The Honorable Jay Clayton
Chairman
Securities and Exchange Commission
100 F Street, NE
Washington DC 20549-1090

Re: Standards of Conduct for Investment Advisers and Broker-Dealers

Dear Chairman Clayton:

Fidelity Investments[1] ("Fidelity") appreciates the opportunity to respond to your request for comment on standards of conduct for investment advisers and broker-dealers.[2] Fidelity supports the Securities and Exchange Commission's (the "SEC" or "Commission") efforts to seek additional information on this important topic as it evaluates potential regulatory actions in light of current market activities and risks.

Fidelity has been an active industry participant in regulatory discussions concerning standards of conduct for broker-dealers and investment advisers. We responded to the SEC's 2013 Request for Data and Other Information[3] and have commented extensively to the Department of Labor (the "DOL") on its Fiduciary Rule[4] (the "DOL Fiduciary Advice Rule" or

---

[1]Fidelity was founded in 1946 and is one of the world's largest providers of financial services. Fidelity provides recordkeeping, investment management, brokerage and custodial/trustee services to thousands of Internal Revenue Code section 401(k), 403(b) and other retirement plans covering approximately 25 million participants and beneficiaries. Fidelity is the nation's largest provider of services to individual retirement accounts ("IRA") with more than 7 million accounts under administration. Fidelity also provides brokerage, operational and administrative support, and investment products and services to thousands of third-party, unaffiliated financial services firms (including investment advisors, broker-dealers, banks, insurance companies and third party administrators) that in turn provide a variety of services to plans, participants and IRA owners.

[2]Public Statement by SEC Chairman Jay Clayton: *Public Comments from Retail Investors and Other Interested Parties on Standards of Conduct for Investment Advisers and Broker-Dealers* (June 1, 2017) *available at*: https://www.sec.gov/news/public-statement/statement-chairman-clayton-2017-05-31 (the "Public Statement")

[3]Securities and Exchange Commission, *Duties of Brokers, Dealers and Investment Advisers* Release No. 34-69013 (March 1, 2013) Fidelity comments *available at*: https://www.sec.gov/comments/4-606/4606-3117.pdf

[4]Department of Labor, *Definition of the Term "Fiduciary"; Conflict of Interest Rule – Retirement Investment Advice* 81 FR 20946 (April 8, 2016). Also, see Fidelity's responses to the DOL's *Request for Information Regarding the Fiduciary Rule and Prohibited Transaction Exemptions*, 82 FR 31278 (July 6, 2017) which are included as an appendix to this letter.

the "Rule"). We implemented the Rule's expanded definition of Investment Advice and the applicable provisions of the Best Interest Contract Exemption as of June 9, 2017 and have communicated business changes resulting from the Rule to our institutional clients and retail customers.

We believe that the DOL's new framework for regulating investment advice under ERISA and the prohibited transaction provisions of the Internal Revenue Code is misguided and has resulted in reduced choice, increased confusion, and increased costs for long-term investors. In recent comments submitted to the DOL, attached in Appendix B to this letter, we offer a legal analysis that demonstrates that the DOL Fiduciary Advice Rule is inconsistent with underlying policies and statutory language of ERISA as well as the priorities of the Administration to encourage and empower Americans to make their own financial decisions. Considering this legal analysis, and the detrimental impact of the Rule on long-term investors, we have urged the DOL to change the Rule to exclude recommendations to participants who exercise independent control over their accounts or who select their own advice providers, and to coordinate with the SEC on a better approach to regulating investment advice in retirement accounts.

We believe that the SEC, as the primary regulator of investment advisers and broker-dealers, should take the lead role in reviewing standards of conduct applicable to investment advisers and broker-dealers. With respect to broker-dealers, we view FINRA's existing suitability standard as an already highly effective best interest standard of conduct that protects investor interests, is appropriately tailored to a broker-dealer business model, and is subject to strong and long-standing SEC and FINRA enforcement practices. If the SEC determines that further enhancements to the existing FINRA based standard of conduct are necessary, the SEC should closely coordinate with the DOL to ensure that a uniform, securities law-based standard of conduct applies across retirement and non-retirement accounts. In drafting any resulting regulations, the SEC should also clearly define the scope of the broker-dealer's obligations when offering investment advice and develop standards of conduct that are principles-based and primarily implemented through disclosure consistent with the SEC's long-standing approach to broker-dealer regulation.

EXECUTIVE SUMMARY

- The DOL's Fiduciary Advice Rule has: 1) resulted in increased cost and less choice for long-term investors; 2) created investor confusion by adding a new standard of conduct to an already complex regulatory regime; and 3) failed to recognize that existing securities law regulatory regimes already require investment advisers and broker-dealers to act in their customer's best interest when offering personalized investment advice;

- The DOL Fiduciary Advice Rule should be changed to exclude recommendations to participants who exercise independent control over their investment choices or who select their own advice providers;

- The SEC should take the lead role in reviewing standards of conduct applicable to investment advisers and broker-dealers when providing investment advice to individual investors' retirement and non-retirement accounts;

- FINRA's existing suitability standard is a highly effective best interest standard of conduct that protects investor interests, is appropriately tailored to broker-dealers' business models and relationships with their customer, and is consistently enforced by the SEC and FINRA;

- If the SEC determines that further enhancements to the existing FINRA-based standard of conduct are necessary, the SEC should closely coordinate with the DOL to ensure that a uniform, securities law-based standard of conduct applies across retirement and non-retirement accounts. In drafting any resulting regulations, the SEC should also clearly define the scope of the broker-dealer's obligations when offering investment advice and develop standards that are principles-based and primarily implemented through disclosure consistent with the SEC's long-standing approach to broker-dealer regulation; and

- The SEC should not make any changes with respect to the existing fiduciary standard under the Investment Advisers Act of 1940 (the "Advisers Act") for registered investment advisers.

Each of these points is discussed in further detail below.

<u>The DOL Fiduciary Advice Rule has resulted in less choice, increased cost, and increased confusion for long-term investors.</u>

The DOL Fiduciary Advice Rule has caused significant unintended consequences for long-term investors. By defining almost any communication by a broker-dealer or investment adviser to a plan participant, IRA owner or plan fiduciary as ERISA Fiduciary Advice, it has substantially increased the likelihood that a broker-dealer or investment adviser will be deemed a fiduciary under ERISA subject to the Rule's onerous restrictions and obligations.

The onerous requirements of the Rule have caused many firms to change their business models from a transaction-based fee structure, where the broker-dealer is paid only through trades that it executes in the investor's account, to a fee structure based on assets under management. As a result, many investors are now required to pay an asset-based fee to receive exactly the same services that were previously provided to them for no additional fee under a transaction-based fee structure. The DOL Fiduciary Advice Rule has thus made it harder and more expensive for retail investors, particularly investors with low balance accounts or investors who simply want to use their broker-dealer to execute a limited number of trades per year, to get the advice they need for their long-term savings goals.

For some time, policymakers and regulators have expressed concern that retail investors are confused as to the standard of conduct that applies to their financial advisor. The DOL Fiduciary Advice Rule has increased investor confusion, rather than reduce it. Many investors and regulated entities are now faced with standards of conduct, disclosure requirements, and enforcement mechanisms for their retirement accounts that are different than for their non-retirement accounts. The outcome is confusing to retail investors who reasonably question why certain products, services and fees are not the same across their accounts, even if the provider is the same.

The Rule has also imposed unworkable obligations and excessive compliance costs on broker-dealers and potentially accelerated an already precipitous decline in the number of broker-dealers in the U.S. capital markets.[5] As a retail broker-dealer subject to the Rule, we face the challenges of a bifurcated DOL-SEC/FINRA compliance structure across customer accounts and complex and burdensome conditions that must be met to receive transaction-based compensation. As a correspondent clearing broker-dealer, we have observed the large number of companies considering scaling back on their brokerage business and/or switching to investment advisor fee-based arrangements because of the DOL Fiduciary Advice Rule, an outcome which, as described above, we believe will ultimately make it harder and more expensive for retail investors to get the advice they need to help save for retirement.

<u>The DOL Fiduciary Advice Rule fails to recognize the strong, existing regulatory and enforcement regimes for broker-dealers and investment advisers, which include a best interest standard of conduct and disclosure of material conflicts</u>.

The DOL Fiduciary Advice Rule treats a broker-dealer subject to the Rule as a fiduciary under ERISA in almost all aspects of the broker-dealer's business. This broad-based approach to fiduciary status largely fails to recognize the longstanding distinction between "selling" and "advising" and ignores the carefully constructed securities law regulatory regime established by Congress under the Advisers Act and Securities Exchange Act of 1934 (the "'34 Act") that has been implemented by the SEC through more than seventy years of regulation and guidance.

The regulatory regimes for investment advisers and broker-dealers are designed to protect investors while also offering them different choices in the financial services marketplace. Broker-dealers primarily engage in "selling" activities and registered investment advisers primarily engage in "advising" activities. Congress understood this distinction and, in recognition of it, created separate regulatory structures for broker-dealers and investment advisers that are tailored to each entity's business activities.

---

[5] *See* Brookings Center on Regulation and Markets Report *Dwindling numbers in the financial industry* by Hester Peirce (May 15, 2017) *available at*: https://www.brookings.edu/research/dwindling-numbers-in-the-financial-industry/ noting that "the number of broker-dealers has declined fairly consistently over the last decade. In March 2017, there were 3,989 BDs registered with the SEC compared to 5,892 in March 2007, a more than thirty percent drop."

Registered investment advisers offer securities advice for a fee to investors. Under the Advisers Act, a registered investment adviser is a fiduciary to its clients with a duty to act in its customer's best interest when offering investment advice for a fee, including an obligation not to subordinate clients' interests to its own. An adviser that has a material conflict of interest must either eliminate or disclose to its clients all material facts relating to the conflict.

Broker-dealers offer investors a range of services from pure trade execution to non-discretionary advice which, under the Adviser's Act, must be incidental to the broker's business and cannot be offered for a distinct fee.[6] While broker-dealers are generally not considered a "fiduciary", broker-dealers are required to deal fairly with their customers and have an obligation, among others, to make recommendations that are consistent with the customer's best interest and that prevent the broker from placing his or her interests ahead of the customer's interests ("suitability obligation"). Under SEC and FINRA rules, broker-dealers are also required to disclose material conflicts of interest.[7]

Importantly, broker-dealers already have an obligation to act in a customer's best interest. As described by FINRA:

> In interpreting FINRA's suitability rule, numerous cases explicitly state that "a broker's recommendation must be consistent with his customer's best interests." The suitability requirement that a broker make only those recommendations that are consistent with the customer's best interests prohibits

[6]Rule 202(a)(11) under the Adviser's Act defines an "Investment adviser" as "any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities; but does not include… (C) any broker or dealer whose performance of such services is solely incidental to the conduct of his business as a broker or dealer and who receives no special compensation therefor;"

[7]For example, among other requirements, the '34 Act prohibits broker-dealers from making misstatements or misleading omissions of material facts, and fraudulent or manipulative acts and practices, in connection with the purchase or sale of securities; Section 15(c) of the '34 Act prohibits a broker from effecting any transaction in or inducing or attempting to induce the purchase or sale of any security by means of any manipulative, deceptive, or other fraudulent device or contrivance; FINRA Rule 2010 (Standards of Commercial Honor and Principles of Trade) states that a firm "in the conduct of its business, shall observe high standards of commercial honor and just and equitable principles of trade"; and FINRA Rule 2020 (Use of Manipulative, Deceptive or Other Fraudulent Devices) provides that no firm "shall effect any transaction in, or induce the purchase or sale of, any security by means of any manipulative, deceptive or other fraudulent device or contrivance." Moreover, in recent years, FINRA has issued guidance and examined member firms on their conflicts of interest disclosure and policies. See generally, FINRA Report on Conflicts of Interest (October 2013) *available at*: https://www.finra.org/sites/default/files/Industry/p359971.pdf

> a broker from placing his or her interests ahead of the customer's interests.[8]

FINRA routinely reminds broker-dealers of their suitability obligations through FINRA issued Regulatory Notices, guidance and interpretive letters. Moreover, FINRA's suitability rule is backed up by strong and active SEC and FINRA enforcement programs designed to protect investors and ensure that bad actors are weeded out of the industry. Examples of instances where FINRA and the SEC have found brokers in violation of the suitability rule, by placing their interests ahead of the customers' interests, include the following:

- A broker whose motivation for recommending one product over another was to receive larger commissions;

- A broker whose mutual fund recommendations were "designed 'to maximize his commissions rather than establish an appropriate portfolio' for his customers"; and

- A broker who recommended speculative securities that paid high commissions because he felt pressured by his firm to sell the securities.[9]

These examples are illustrative of the type of misconduct the DOL mistakenly suggested was un-regulated and therefore in need of a DOL-imposed remedy. We believe that the existing securities law regulatory framework for broker-dealers and investment advisers has worked well for investors and the U.S. capital markets. To the extent there are areas where a broker-dealer best interest standard of conduct diverges from an investment adviser-style fiduciary standard, those areas should be seen as appropriate adaptations that recognize differences in business models and relationships. If those deviations are objectionable, we believe that they would be better addressed through additional disclosure as determined by the SEC, and not through an entirely new and inconsistent regulatory regime promulgated by the DOL.

<u>A path forward for the DOL and SEC.</u>

In a recent comment letter submitted to the DOL in response to its RFI, (attached in Appendix B to this letter), we offer a legal analysis that shows why the DOL Fiduciary Advice Rule should not apply to participants who exercise independent control over their accounts under ERISA or who select their own advice providers. We analyze inconsistencies between the DOL Fiduciary Advice Rule, ERISA's fiduciary framework, and the rules of ERISA section 404(c) that govern the liability of fiduciaries for participant directed investments and conclude

[8] FINRA Regulatory Notice 12-25, *Suitability: Additional Guidance on FINRA's New Suitability Rule* (May 2012) at page 3 *available at*: https://www.finra.org/industry/notices/12-25

[9] Id.

that the DOL has failed to reconcile the consequences of imposing ERISA fiduciary standards on advice to *participants* as opposed to advice to *plans and plan fiduciaries.* Our analysis presents a compelling reason for regulators to question whether an investment advice provider should be subject to ERISA's fiduciary framework where participants exercise independent control over their accounts or select their own advice providers, and why subjecting investment advice providers, such as broker-dealers, to ERISA fiduciary responsibility, as the Rule purports to do, is inconsistent with the statutory language of ERISA, its underlying policies, and the priorities of the Administration to encourage and empower Americans to make their own financial decisions.

Given this legal analysis, we believe that the path forward is for the DOL to change its Rule and develop prohibited transaction relief that is aligned with the standards of conduct of an advice provider's primary regulator, such as the SEC in the case of SEC-registered broker-dealers.[10] Under this proposed approach, an advisor's primary regulator would establish the standard of conduct applicable to that advisor when offering investment advice, be it a registered investment adviser, broker-dealer, bank or insurance company. Advice to retail investors in retirement accounts would generally be regulated by the SEC when provided by a registered investment adviser, by the SEC/FINRA when provided by a broker-dealer, by the Office of Comptroller of the Currency ("OCC") when provided by an OCC regulated bank, and by the applicable state insurance regulator when provided by an insurance company. Advice to plan sponsors by any advisor would continue to be regulated by the DOL.

With the DOL's current examination of the Rule pursuant to President Trump's Presidential Memorandum of February 3, 2017[11], the SEC and DOL have a new opportunity to work together to create a coordinated regulatory framework for advice providers across account types and provide investors more choice in investment options and compensation arrangements. We believe that the SEC and DOL should seize this opportunity to work together, as the failure to fix the Rule will carry significant costs for investors.

<u>The SEC should review and consider an enhanced best interest standard of conduct for broker-dealers</u>.

As the primary regulator for broker-dealers, we believe that the SEC is the appropriate entity to consider rulemaking with respect to standards of conduct for broker-dealers with respect to investment advice. This would begin with the standard of conduct under the existing suitability requirements and other regulatory obligations that already apply to broker-dealers under the '34 Act and rules of FINRA and other self-regulatory organizations of which the broker-dealer is a member and, if the SEC finds it necessary, would include enhancements to that

[10] *See* Appendix B infra.

[11] *Presidential Memorandum on the Fiduciary Duty Rule* 82 FR 9675 (February 7, 2017) available at: https://www.gpo.gov/fdsys/pkg/FR-2017-02-07/pdf/2017-02656.pdf

standard of conduct. For too long, the question of whether broker-dealers should be subject to an SEC promulgated standard of conduct when offering personalized investment advice about securities to retail investors has been discussed and languished without SEC action.[12] The SEC has the authority to commence rulemaking on a standard of conduct for broker-dealers pursuant to Section 913 of the Dodd-Frank Act and the SEC's Staff Study.[13] SEC rulemaking on a standard of conduct for broker-dealers fits squarely within the SEC's mission to protect investors, maintain fair, orderly, and efficient markets, and to facilitate capital formation. Moreover, a proliferation of state securities regulators have recently enacted, or expressed interest in creating, their own standard of conduct requirements for broker-dealers and federal action on this topic would provide firms and investors much needed uniformity.[14]

<u>Any enhancements to a standard of conduct for broker-dealers by the SEC should be principles-based and primarily implemented through disclosure consistent with the SEC's long-standing approach to broker-dealer regulation.</u>

Disclosure has been the core of Congress' and the SEC's regulatory approach for broker-dealers since the inception of the '34 Act. We believe that any enhancements to current rules with respect to information on the broker-dealer's products and services, compensation and material conflicts of interest can be best addressed through the Commission's long standing policy of disclosure-based regulation.

SEC rulemaking should clearly define the scope, nature and duration of the broker-dealer's standard of conduct when offering personalized investment advice about securities to retail customers. This could be accomplished through simple, plain English disclosure that would be meaningful to investors. We propose that, if it is deemed necessary, such disclosure should include two key features:

- First, it should include a statement describing the scope of the broker-dealer's services on which it is advising, whether the advice provided is point-in-time or

---

[12]We do not have an opinion at this point in time as to whether the SEC should engage in rulemaking on this topic directly or delegate authority to FINRA to develop rules, as long as rulemaking can be finalized in a prompt manner and in coordination with the DOL.

[13]Staff of the U.S. Securities and Exchange Commission, *Study on Investment Advisers and Broker-Dealers as Required by Section 913 of the Dodd-Frank Wall Street Reform and Consumer Protection Act* (Jan. 2011) *available at*: https://www.sec.gov/news/studies/2011/913studyfinal.pdf

[14]For example, on June 2, 2017 Nevada Governor Brian Sandoval approved legislation that effectively imposed a state fiduciary duty on broker-dealers and that became effective on July 1, 2017. Additionally, New Jersey has legislation pending that would impose a state fiduciary duty on broker-dealers, and New York considered similar legislation earlier this year. Other state legislatures intend to propose similar legislation, and if this trend continues it could result in an untenable patchwork of various and potentially conflicting standards.

ongoing and the range of investment options that the broker-dealer will consider in making investment recommendations; and

- Second, it should disclose the compensation or ranges of compensation payable to the broker-dealer for the types of investment options that the broker-dealer might recommend, as well as a description of any other material conflicts of interest.

Once the relationship between the broker-dealer and customer is established, all of the broker-dealer's recommendations within the disclosed engagement framework must be in the best interest of the investor.

In 2010, FINRA requested comment on a concept proposal to require broker-dealers, at or prior to commencing a business relationship with a retail customer, to provide a written statement to the customer describing the types of accounts and services it provides, as well as conflicts associated with such services and any limitations on the duties the firm otherwise owes to retail customers.[15] In essence, this document would act similarly to a Form ADV Part 2A for registered investment advisers. FINRA suggested that such a document would not only provide useful information to a retail customer, but also would help clearly define the scope of the duties owed to that customer. We agree. As it considers how to implement standards of conduct for broker-dealers, we recommend that the SEC review and consider FINRA's 2010 concept proposal, as well as comments on the proposal, which seeks to address this issue in the context of the business model and regulation of broker-dealers.

<u>An SEC standard of conduct for broker-dealers should encompass all of an investor's accounts and interactions.</u>

Retail investors seeking personalized investment advice about securities from a broker-dealer typically want advice across the range of assets they own whether held in non-retirement retail brokerage accounts, IRAs, or employer sponsored retirement plan accounts. A significant challenge with the DOL Fiduciary Advice Rule is that it imposes a bifurcated compliance regime on broker-dealers who must implement the DOL Fiduciary Advice Rule across only a portion of their customers' accounts. The outcome is confusing to retail investors who reasonably question why certain products, services and fees are not the same across their accounts, even if the provider is the same.

A broker-dealer should be subject to one set of rules for all of its retail customers. That is, an SEC promulgated standard of conduct for broker-dealers should apply across all broker-dealer accounts, both non-retirement and retirement. This type of comprehensive standard of conduct would help eliminate considerable confusion for retail investors and streamline

[15] *Disclosure of Services, Conflicts and Duties* FINRA Regulatory Notice 10-54 *available at*: http://www.finra.org/sites/default/files/NoticeDocument/p122361.pdf Fidelity comments *available at*: http://www.finra.org/sites/default/files/NoticeComment/p122723.pdf

compliance costs for broker-dealers. Moreover, this type of comprehensive standard of conduct is achievable if the DOL coordinates with the SEC by making the changes to the DOL Rule that we recommend in our recent comment letter (attached in Appendix B to this letter), including developing prohibited transaction relief that is aligned with the standards of conduct of an advice provider's primary regulator, such as the SEC in the case of SEC-registered broker-dealers.

<u>The SEC should not make any changes with respect to the existing fiduciary standard under the Advisers Act for registered investment advisers.</u>

As the SEC reviews the standard of conduct for broker-dealers when offering personalized investment advice about securities to retail customers, we do not believe that the Commission should make any changes to the existing standard of conduct for investment advisers under the Advisers Act. We believe that the existing principles-based fiduciary duty under the Advisers Act has worked well for investment advisers and their clients and see no reason to modify this well-functioning model. Note that our recommendation to the DOL, if followed, would enable this existing principles-based fiduciary standard to apply uniformly to investment advisers with respect to both the retirement and non-retirement accounts of their retail customers.

* * * * *

In conclusion, Fidelity believes that the SEC should review and consider an enhanced best interest standard of conduct for broker-dealers that is clearly defined, disclosure and materiality-based, and that applies across all of an investor's brokerage accounts and interactions. We also support accompanying DOL prohibited transaction relief that aligns with the standards of conduct of an advice provider's primary regulator. We urge the SEC and the DOL to work together on these rulemakings so that we can continue to meet the needs of America's retirement investors.

* * * * *

Fidelity would be pleased to provide further information, participate in any direct outreach efforts the Commission undertakes, or respond to questions the Commission may have about our comments.

Sincerely,

cc: **United States Securities and Exchange Commission**
The Honorable Kara M. Stein, Commissioner
The Honorable Michael S. Piwowar, Commissioner
David Grim, Director, Division of Investment Management
Heather Seidel, Acting Director, Division of Trading and Markets

United States Department of Labor
The Honorable Alexander Acosta, Secretary
Timothy D. Hauser, Deputy Assistant Secretary for Program Operations, Employee Benefits Security Administration

Financial Industry Regulatory Authority
Robert Cook, Chairman and Chief Executive Officer, FINRA
Robert Colby, Chief Legal Officer, FINRA

Attachment: Appendix

Appendix

Fidelity comment letters in response to Department of Labor, *Request for Information Regarding the Fiduciary Rule and Prohibited Transaction Exemptions*, 82 FR 31278 (July 6, 2017).

Appendix A: Fidelity comment letter to the Department of Labor dated July 21, 2017 which requests further delay of the January 1, 2018 Best Interest Contract compliance requirements.

Appendix B: Fidelity comment letter to the Department of Labor dated August 7, 2017 which outlines a new legal argument that *participant* advice – as opposed to advice to *plans and plan fiduciaries* – should not be subject to ERISA regulation and that advice to individual participants is more properly regulated by the financial services regulators.

Appendix A

Ralph C. Derbyshire
Senior Vice President and
Deputy General Counsel

FMR LLC Legal Department

Mail: 200 Seaport Blvd., V7A Boston, MA 02210
Office: 245 Summer Street, Boston, MA 02210
Phone: 617-563-0296 Fax: 508-357-8568
Ralph.Derbyshire@fmr.com

SUBMITTED ELECTRONICALLY

July 21, 2017

Office of Exemption Determinations Employee Benefits Security Administration
U.S. Department of Labor
Suite 400
200 Constitution Avenue, NW
Washington, D.C. 20210

Attention: D-11933

Re: *Request for Information Regarding the Fiduciary Rule and Prohibited Transaction Exemptions (RIN 1210-AB82)*

Ladies and Gentlemen:

Fidelity Investments[1] ("Fidelity") appreciates the opportunity to respond to the request for information on a potential delay of the January 1, 2018 applicability date for certain provisions of the BIC Exemption, Principal Transactions Exemption, and amendments to PTE 84-24 (the "RFI") published by the Department of Labor ("Department") in the Federal Register on July 6, 2017.[2] As one of the nation's leading retirement services providers, Fidelity has a deep and long-standing commitment to working with the Department on its rulemaking in the area of investment education and advice.

Our goal is to ensure that investment advice is provided in the investor's best interest and that the rules for investment advice allow savers continued choice and access to the products and services they need. As we have stated in our previous comment letters on the rule, we continue to believe that the Department's new framework for regulating investment advice under ERISA and the prohibited transaction provisions of the Code is misguided. As the long-standing primary regulator charged with investor protection, the Securities and Exchange Commission ("SEC") should lead the rulemaking on this topic through coordinated and constructive engagement with the Department to develop a workable solution that results in uniform fiduciary protections for

---

[1] Fidelity was founded in 1946 and is one of the world's largest providers of financial services. Fidelity provides recordkeeping, investment management, brokerage and custodial/trustee services to thousands of Code section 401(k), 403(b) and other retirement plans covering approximately 25 million participants and beneficiaries. Fidelity is the nation's largest provider of services to individual retirement accounts ("IRA") with more than 7 million accounts under administration. Fidelity also provides brokerage, operational and administrative support, and investment products and services to thousands of third-party, unaffiliated financial services firms (including investment advisors, broker-dealers, banks, insurance companies and third party administrators) that may in turn provide investment advice to plans, participants and IRA owners.

[2] *Request for Information Regarding the Fiduciary Rule and Prohibited Transaction Exemptions*, 82 FR 31278 (July 6, 2017). Capitalized terms not otherwise defined have the meaning ascribed to them in the RFI.

investors and a uniform set of rules for all advisers. A delay in the January 1 applicability date would provide the SEC and Department an opportunity to jointly consider public comments on the experiences of investors and the regulated community thus far in connection with the implementation of the rule and constructively determine the best path forward.

Further, as we stated in our comment letter of April 17, 2017 relating to a delay in the Rule pending the examination directed by the President's memorandum of February 3, 2017, we have deep concerns with the Department's decision to make the Rule applicable while it conducts the examination. By making the Rule applicable on June 9, 2017, before it had considered comments on the examination, the Department effectively ensured the very frictional costs and disruption to retirement investors and the marketplace that a delay would have avoided. Plans, participants and IRA investors now run a significant risk that they will be subject to multiple changes in the investment-related services they receive over the next several months. Failing to delay the additional requirements scheduled to become effective January 1, 2018 will only exacerbate this situation, resulting in further confusion and dissatisfaction, as well as potentially increase costs to retirement investors. Since we expect to advocate for a complete reset on the rulemaking to allow for a coordinated approach between the Department and financial services rulemakers, the Department should not underestimate the impact of imposing the additional disclosure, contract and other aspects of the January 1, 2018 requirements on tens of millions of customers who will then potentially face implementation of a completely different set of rules in a short period of time.

A simple, concrete example illustrates this point. One of the additional requirements of the BIC exemption that becomes applicable on January 1, 2018 is a written contract with IRA customers. Under section II(f)(2) of the BIC exemption, the contract cannot contain any waiver or qualification of the customer's right to bring or participate in a class action. That provision is currently being challenged in litigation and, in a brief filed on July 3, 2017[3] the Department declared that it would no longer defend the prohibition on class-action waivers. If the court finds the provision invalid, section II(f)(4) of the BIC exemption then provides that the prohibition can be severed from the BIC exemption (for contracts subject to the jurisdiction of the court that finds the provision invalid). Requiring advisors to move forward in the contracting process in compliance with a class action requirement that the Department itself no longer supports and that may be invalidated will create confusion and disruption of customer relationships, potentially requiring execution of multiple contracts as the exemption is modified either through court action or Department rulemaking.

The RFI itself provides other examples. The Department specifically asks for input on whether the BIC exemption's disclosure requirements can be simplified or restructured, whether the contract requirement is necessary or could be eliminated, and whether potential streamlined exemptions could be created that would presumably eliminate the need for advisers to comply with some or all of the BIC exemption's January 1 requirements if other requirements are met. Action on any of these possibilities could change, eliminate or render moot the January 1, 2018 requirements and could thus subject retirement savers to multiple disclosure and compliance approaches absent postponement of their current applicability date.

---

[3] Brief for appellees filed July 3, 2017 in *Chamber of Commerce v. U.S. Dept. of Labor,* (5th Cir. No. 17-10238).

Moreover, the additional requirements scheduled to become effective January 1, 2018 are not needed to achieve the goals of the Rule as evidenced by the Department's final rule adopting a 60-day extension of the Rule's applicability date. In connection with the adoption of the delay, the Department stated that the imposition of the Impartial Conduct Standards alone will avoid the losses that retirement investors would have otherwise incurred by a longer delay. If that is the case, then the additional costs involved in complying with the requirements that are scheduled to take effect on January 1, 2018 are unnecessary because they are not required to obtain the benefits that the Rule purports to achieve. We estimate that those costs of compliance for Fidelity are in the tens of millions of dollars. If the Impartial Conduct Standards alone effectively avoid investor losses and preserve their investment gains between June 9, 2017 and January 1, 2018, then the significant additional disclosure and other requirements that are scheduled to become effective on January 1, 2018 cannot be justified.

Accordingly, we request that the Department delay the additional January 1, 2018 requirements until a reasonable period following the conclusion of the examination directed by the President's Memorandum and the consideration of the RFI responses. The length of the delay should depend on the results of those efforts. If there are no changes to the Rule, the requirements should become effective six months from the date those results are announced. This six-month period would roughly correspond to the period between the June 9, 2017 general applicability date of the Rule and the original January 1, 2018 applicability date of the additional requirements. If there are changes to the Rule following the examination and RFI, the Department should provide sufficient additional time from the date those changes are announced in light of the specific changes made to the Rule. In all events, the Department should announce the postponement of the January 1, 2018 applicability date as soon as possible.

* * *

We would be pleased to respond to any questions or comments regarding this letter.

Sincerely,

Ralph C. Derbyshire

cc: **United States Securities and Exchange Commission**
The Honorable Jay Clayton, Chair
The Honorable Kara M. Stein, Commissioner
The Honorable Michael S. Piwowar, Commissioner

Financial Industry Regulatory Authority
Robert Cook, Chairman and Chief Executive Officer, FINRA
Robert Colby, Chief Legal Officer, FINRA

Appendix B

Ralph C. Derbyshire
Senior Vice President and
Deputy General Counsel

FMR LLC Legal Department

Mail: 200 Seaport Blvd., V7A Boston, MA 02210
Office: 245 Summer Street, Boston, MA 02210
Phone: 617-563-0296 Fax: 508-357-8568
Ralph.Derbyshire@fmr.com

August 7, 2017

Office of Exemption Determinations
Employee Benefits Security Administration
U.S. Department of Labor
Suite 400
200 Constitution Avenue, NW
Washington, D.C. 20210

Attention: D-11933

Re: *Request for Information Regarding the Fiduciary Rule and Prohibited Transaction Exemptions (RIN 1210-AB82)*

Ladies and Gentlemen:

Fidelity Investments[1] ("Fidelity") appreciates the opportunity to respond to the request for information on new exemptions or changes to the fiduciary rule and related prohibited transaction exemptions (the "RFI") published by the Department of Labor (the "Department") in the Federal Register on July 6, 2017.[2] As one of the nation's leading retirement services providers, Fidelity has a deep and long-standing commitment to working with the Department on its rulemaking in the area of investment education and advice.

Our goal is to ensure that investment advice is provided in the investor's best interest and that the rules for investment advice allow savers continued choice and access to the products and services they need. As we have stated in our previous comment letters on the Rule, we continue to believe that the Department's new framework for regulating investment advice under ERISA and the prohibited transaction provisions of the Code is misguided. As the long-standing primary regulator charged with investor protection, the Securities and Exchange Commission ("SEC") should lead the rulemaking on this topic through coordinated and constructive engagement with the Department to develop a workable solution that results in uniform protections for investors and a uniform set of rules for advisors.

Most of the RFI requests information in connection with the impact of the rule on the availability of investment advice, the development of new products and services and the costs of

[1] Fidelity was founded in 1946 and is one of the world's largest providers of financial services. Fidelity provides recordkeeping, investment management, brokerage and custodial/trustee services to thousands of Code section 401(k), 403(b) and other retirement plans covering approximately 25 million participants and beneficiaries. Fidelity is the nation's largest provider of services to individual retirement accounts ("IRA") with more than 7 million accounts under administration. Fidelity also provides brokerage, operational and administrative support, and investment products and services to thousands of third-party, unaffiliated financial services firms (including investment advisors, broker-dealers, banks, insurance companies and third party administrators) that may in turn provide investment advice to plans, participants and IRA owners.

[2] *Request for Information Regarding the Fiduciary Rule and Prohibited Transaction Exemptions,* 82 FR 31278 (July 6, 2017). Capitalized terms not otherwise defined have the meaning ascribed to them in the RFI.

compliance. In the Attachment to this letter, we have outlined suggested changes to the Rule and the BIC Exemption that would help address the continuing concerns we have with the Department's rulemaking in this area. However, we would like to focus our comments on an independent legal basis that we believe compels the Department to rethink the scope and nature of the Rule itself. This legal basis is grounded in the policies and concerns underlying the enactment of ERISA and exposes as yet unresolved inconsistencies between the Rule, ERISA's fiduciary framework and the rules of ERISA section 404(c) that govern liability of fiduciaries for participant-directed investments.

A careful analysis leads to the inevitable conclusion that, despite the Department's more than 20-year old interpretive position, the statutory language of ERISA and its underlying policies do not support imposing ERISA fiduciary standards on advice to *participants* (individuals responsible for their own retirement assets) as opposed to advice to *plans and plan fiduciaries* (institutional fiduciaries such as trustees and plan sponsors responsible for overseeing the retirement assets of others). This analysis also shows that the Rule is inconsistent with the priorities of the Administration to encourage and empower Americans to make their own financial decisions.

Advice to Individuals, including Participants, Should Be Subject To Standards of Conduct Defined by Financial Services Regulation, and Not ERISA

The extensive regulation of the financial services industry in the United States is fragmented. The primary financial services regulators vary depending on the activities of the provider and the products they sell – the SEC for registered investment advisers, FINRA for broker-dealers, the OCC or state regulators for banks and state-level regulation for insurance companies. This fragmented regulatory framework is particularly problematic for retail investors looking to navigate the market for financial services and is precisely the reason Congress enacted Dodd-Frank section 913. As stated by the SEC staff:

> Broker-dealers and investment advisers are regulated extensively, but the regulatory regimes differ, and broker-dealers and investment advisers are subject to different standards under federal law when providing investment advice about securities. Retail investors generally are not aware of these differences or their legal implications. Many investors are also confused by the different standards of care that apply to investment advisers and broker-dealers. That investor confusion has been a source of concern for regulators and Congress.[3]

The Department's rulemaking to establish the best interest standard through ERISA and the Internal Revenue Code prohibited transaction rules only adds to the fragmentation and confusion. Investors are now faced with different standards of conduct, disclosure requirements and enforcement mechanisms for retirement and non-retirement accounts – effectively doubling the complexity of the regulatory framework in one stroke.

[3] *Study on Investment Advisers and Broker-Dealers: As Required by Section 913 of the Dodd-Frank Wall Street Reform and Consumer Protection Act*, SEC Staff (January 2011).

ERISA does not require this additional level of regulatory complexity nor does ERISA's statutory framework as envisioned by Congress clearly support it. As the Department has pointed out many times, ERISA was enacted in 1974 prior to the existence of participant-directed 401(k) plans, the widespread use of IRAs, and the now commonplace rollover of plan assets from ERISA-protected plans to IRAs.[4] At that time, defined benefit plans were the predominant workplace retirement arrangement and participants have no role in plan investment decision-making in a defined benefit plan. Therefore, Congress could not have envisioned that participants would have primary responsibility for investment decision-making in the retirement plans that today provide the main source of their retirement income and, consequently, the important role that investment advice to participants might play in retirement security.

The Department uses this change in the retirement landscape to justify exercise of its rulemaking power under ERISA to effect the broad and sweeping changes that the Rule is making to the financial services industry. An equally valid point of view, though, is that these changes in the retirement landscape require a closer look at the policy of regulating individual participant investment decisions under a statute intended to regulate institutional fiduciaries of employee benefit plans. Participant-directed individual account plans such as typical 401(k) plans are more in the nature of employer-sponsored and maintained investment platforms than traditional pooled employee benefit plan arrangements, and participants treat their plan accounts much like any other investment account they maintain. Now more than ever, individual investors need to make holistic investment decisions across their savings accounts whether in individual plan accounts, IRAs or retail brokerage accounts. Therefore, advice to individuals with respect to those accounts should be subject to the same regulatory framework.

The legal path to this consistent regulatory framework already exists under the statutory provisions of ERISA. However, it requires new thinking about the way ERISA's advice rules operate that test basic assumptions underlying more than 20 years of interpretation by the Department. This new thinking is based on a legal analysis that shows that subjecting advice to *participants* – as opposed to advice to a *plan or a plan fiduciary* – to ERISA's fiduciary responsibilities is not supported by the statutory provisions of ERISA that apply where a participant exercises independent control over his or her account. The key points of this analysis are as follows:

- ERISA provides a precise framework for the allocation of fiduciary responsibilities with respect to the investment of plan assets which does not readily accommodate fiduciary status for advisors selected by *participants* and not the *plan or another plan fiduciary*.

- An important component of this framework is ERISA section 404(c) which insulates *all* plan fiduciaries, including investment advisors, from liability *for any loss* so long as they do not improperly influence participant decision-making. This means that an investment advice provider should not be subject to ERISA's

[4] 81 FR 20946 (June 9, 2016).

standards of conduct when providing advice to a participant who is exercising independent control over his or her account.

- Advice to plan fiduciaries should be subject to ERISA standards because it impacts decisions those fiduciaries make on behalf of the plan. Participants are not fiduciaries under section 404(c) and investment advice they choose to receive impacts only that participant's account.

- Participants remain protected by the vast body of financial services laws and regulations that define appropriate conduct for the firms and their representatives that are subject to them.

Although different in approach and detail, the protections to investors under the laws and regulations of the SEC, FINRA, OCC and state regulators are very substantial and rigorously enforced. With respect to registered investment advisers and broker-dealers, the SEC has stated:

> Investment advisers and broker-dealers are subject to extensive regulation and oversight designed to protect clients and customers, whether retail or other. Both regulatory regimes require investment advisers and broker-dealers to adhere to high standards of conduct in their interactions with retail investors, which are intended to encourage both broker-dealers and investment advisers to act in the interests of their investors and minimize conflicts of interests when providing personalized investment advice or recommendations.[5]

Since commission-based compensation is a primary focus of the Rule, particularly notable are the protections imposed under FINRA rules applicable to broker-dealers. In fact, the much-maligned and mischaracterized "suitability" requirement has been expressly interpreted by FINRA and the court to impose an obligation on broker-dealers to act in their customer's best interest when making investment recommendations. This prohibits a broker-dealer from putting its own interests ahead of the customer's.[6] In connection with the sale of commission-based annuities, another primary focus of the Rule, the so-called Harkin amendment to the Dodd-Frank act is an implicit recognition by Congress of the sufficiency of state suitability regulation of annuity sales.[7] Extensive protections also exist for customers of banks[8]. There is no need to introduce ERISA's separate, distinct and additional fiduciary regime when these existing regulators are already charged with investor protection and have decades of carefully considered rules and principles that do so. In short, the litigation risk and prohibited transaction excise tax exposure that are a direct consequence of the Rule will only increase the costs of providing investment advice to individuals while adding nothing substantive to the securities regulatory framework that already protects investors.

---

[5] Staff of the Securities and Exchange Commission, *Study on Investment Advisers and Broker-Dealers* (January 2011) at 102 (https://www.sec.gov/news/studies/2011/913studyfinal.pdf).
[6] FINRA Regulatory Notice 12-25 (July 9, 2012), FAQ 1.
[7] Section 989J of the Dodd-Frank Wall Street Reform Act of 2010.
[8] *See, e.g.*, 12 CFR part 9; Office of the Comptroller of the Currency, *Personal Fiduciary Activities* (February 2015) (found at https://www.occ.gov/publications/publications-by-type/comptrollers-handbook/am-pfa.pdf).

Respecting ERISA's statutory framework for participant advice provides a path to restore a uniform standard of conduct that applies to both retirement and non-retirement accounts. Otherwise, the Department's advice rule overlaps financial services regulation for retirement accounts, increases complexity and compounds the very investor confusion that Congress sought to address through Dodd-Frank section 913.

ERISA's Statutory Framework

ERISA establishes a comprehensive fiduciary framework governing both the investment and administrative activities of employee benefit plans. It requires that every plan have at least one named fiduciary responsible for operation and administration of the plan.[9] In the case of a funded plan, it also requires that the plan have a trustee with exclusive authority and discretion to manage and control the assets of the plan.[10] And it imposes high standards of conduct on fiduciaries, including duties of prudence and loyalty.[11]

ERISA includes detailed provisions for allocating fiduciary responsibilities to investment managers and among other fiduciaries to ensure that all aspects of administering the plan and investing its assets are subject to fiduciary oversight.[12] Under ERISA, the trustee has *exclusive* authority to invest the assets of the plan. The only exceptions are where the trustee is subject to directions of a named fiduciary or where a named fiduciary appoints an investment manager as defined in section 3(38).[13] This section in turn requires that the investment manager acknowledge fiduciary status with respect to the plan. In this way, any person designated by a named fiduciary to provide discretionary investment management services to a plan is brought within ERISA's fiduciary framework with a clear allocation of responsibility among the plan's fiduciaries.

In terms of allocation of responsibilities for nondiscretionary investment advice, ERISA states that if the plan so provides a named fiduciary may employ a person "to render advice with regard to any responsibility such fiduciary has under the plan."[14] Although this provision does not use the term "*investment* advice", guidance issued in 1975 by the Department interpreted this term as relating to the investment responsibilities of the fiduciary.[15] This provision empowers named fiduciaries to use investment advisors and dovetails with the definition in section 3(21)(A)(ii) which then makes persons who provide such investment advice themselves fiduciaries to the plan. These provisions say nothing about the responsibility of persons providing nondiscretionary investment advice to participants.

Within this comprehensive framework governing investment fiduciaries, ERISA provides for an important exception from the fiduciary responsibility provisions for participant-directed

[9] ERISA section 402(a)(1).
[10] ERISA section 403(a).
[11] ERISA section 404(a)(1).
[12] ERISA section 402(b) and (c).
[13] ERISA section 403(a)(1) and (2).
[14] ERISA section 403(c)(2).
[15] 29 CFR section 2509.75-8, FR-15.

plans under ERISA section 404(c):

> (c) CONTROL OVER ASSETS BY PARTICIPANT OR BENEFICIARY –
>
> (1) (A) In the case of a pension plan which provides for individual accounts and permits a participant or beneficiary to exercise control over the assets in his account, if a participant or beneficiary exercises control over the assets in his account (as determined under regulations of the Secretary)—
>
> (i) such participant or beneficiary shall not be deemed to be a fiduciary by reason of such exercise, and
> (ii) no person who is otherwise a fiduciary shall be liable under this part for any loss, or by reason of any breach, which results from such participant's or beneficiary's exercise of control….

The breadth of this provision is striking. First, participants are categorically not fiduciaries even though they are exercising discretionary control over plan investments. This immediately raises the question of how a party independently selected by the *participant* (who is by statute not a fiduciary) causes such party to become a fiduciary *to the plan* without the knowledge or action of someone who is already a plan fiduciary such as the trustee or a named fiduciary.

Second, Section 404(c) provides that "no person who is otherwise a fiduciary" is liable for a loss that results from the participant's exercise of control. Taking the words at face value, an investment advice fiduciary is covered by section 404(c) unless investment advice somehow deprives the participant from exercising control.[16] Importantly, the relief from liability is solely with respect to liabilities *under this part* which is a reference to the fiduciary obligations under Part 4 of Title 1 of ERISA. A fiduciary remains subject to liability under other provisions of law, including the financial services laws and regulations.

There is Reason to Question the Extension of ERISA Fiduciary Standards to Participant Advice

Nothing in the language of section 3(21)(A)(ii) either compels or precludes the conclusion that investment advice to *participants* makes a person a fiduciary with respect to the *plan*. Instead, the statute's application to investment advice to participants has been a matter of interpretation by the Department over the past four decades.

The Department's original regulation defining investment advice enacted in 1975 made clear that this definition applied only to "'investment advice' to an employee benefit plan."[17] There is no reference whatsoever to advice to participants in the regulation. In fact, one of the

[16] Section 404(c)'s also encompasses the plan sponsor or other plan fiduciary that hires an advice provider. That is, "no person" includes the plan sponsor or another plan fiduciary, and thus the sponsor or other plan fiduciary is not liable for a loss resulting from a participant's exercise of control under section 404(c).
[17] 29 CFR section 2510.3-21(c)(1).

requirements of the prior regulation was that the advice be provided pursuant to an agreement that the advice will serve as a primary basis for investment decisions. The agreement must be between the advice provider and "the plan or a fiduciary with respect to the plan."[18] Since the participant under section 404(c)(1)(A)(i) is not a fiduciary, this requirement would never be met for investment advice provided to a participant where section 404(c) applies or when the advice provider is independently selected by the participant.

Prior to issuing the new investment advice rule, the Department had expressly provided guidance on advice to participants on only two occasions.[19] On neither occasion did it provide any analysis or discussion on why it was appropriate to treat advice to participants as subject to ERISA's fiduciary standards of conduct. More importantly, the Department never addressed whether an investment advice provider has fiduciary liability for its advice in the context of section 404(c).

First, in 1996 the Department issued Interpretive Bulletin 96-1 ("IB 96-1).[20] For the first time in this guidance, the Department set forth its views "concerning the circumstances under which the provision of investment-related information to participants and beneficiaries in participant-directed individual account pension plans will not constitute the rendering of 'investment advice' under the Employee Retirement Income Security Act of 1974, as amended (ERISA)." However, the Department offered no discussion or rationale for why advice to a participant constituted or was equivalent to advice to an employee benefit plan and thus why it should constitute investment advice within the meaning of the 1975 regulation at all. It merely asserted without discussion that the investment advice regulation applies when determining whether a person renders investment advice to a plan participant who can direct investment of an individual account "because section 3(21)(A)(ii) applies to advice with respect to 'any moneys or other property' of a plan and 29 CFR 2510.3-21(c) is intended to clarify the application of this section…."[21] It even went so far as asserting that an agreement with the participant or beneficiary would satisfy the regulatory definition of investment advice which was contrary to the clear language of the regulation in effect at that time requiring an agreement with the plan or a fiduciary with respect to the plan.[22]

While the Department deemed advice to participants to give rise to fiduciary status, it also recognized that section 404(c) limited fiduciary liability for participant advice in the preamble to IB 96-1:

> Although section 404(c) of ERISA, 29 U.S.C. 1104(c), and the Department's regulations, at 29 CFR 2550.404c–1, provide limited relief from liability for fiduciaries of pension

[18] 29 CFR section 2510.3-21(c)(1)(ii)(B).
[19] In addition to the two instances discussed below, the Department also issued regulations under Sections 408(b)(14) and (g) with respect to a prohibited transaction exemption for participant advice created through the Pension Protection Act in 2006. These regulations are also discussed below.
[20] 29 CFR. section 2509.96-1.
[21] 29 CFR. section 2509.96-1(c).
[22] *Id.*

> plans that permit a participant or beneficiary to exercise control over the assets in his or her individual account, there remains a need for employers and others who provide investment information with respect to pension plan assets to know what standards apply in determining whether an education activity may give rise to fiduciary status."[23]

If section 404(c) were completely inapposite to a fiduciary providing participant investment advice, it would have been much more straightforward for the Department to have stated that the guidance was necessary because section 404(c) provides no relief for investment advice fiduciaries. Instead, the Department clearly implied that section 404(c) applies in circumstances where the participant exercises control over the account but there still "remains a need" for additional guidance. In addition, footnote 2 of the bulletin indicates that issues relating to the circumstances under which information provided to participants may affect the ability to exercise "independent control" for purposes of section 404(c) are beyond the scope of the interpretive bulletin, and that no inferences should be drawn regarding such issues.[24] If investment advice fiduciaries were never entitled to section 404(c) protection, this statement likewise would have been unnecessary. Having clearly recognized the problem, the Department never attempted to reconcile its assertion that participant advice constituted fiduciary activity with the fact that section 404(c)'s fiduciary protection would effectively render ERISA's fiduciary standards of conduct irrelevant with respect to such advice.

No further guidance was issued regarding participant investment advice until 2005. At that time, the Department in an advisory opinion addressed the provision of discretionary investment management services to a participant in a section 404(c) plan that selected and hired the advice provider and concluded that the discretionary manager would be liable for imprudent decisions because they "would not have been the direct and necessary result of the participant's exercise of control, even though the participant selected the person to manage the assets in his or her individual account".[25] The Department did not specifically address the provision of non-discretionary investment advice in the advisory opinion, although it cited IB 96-1 in noting generally that it "has taken the position that [the] definition of fiduciary also applies to investment advice provided to a participant or beneficiary in an individual account plan that allows participants or beneficiaries to direct the investment of their account."[26]

The Department's 2016 investment advice rulemaking is the first time that participant advice has been expressly referenced in a regulatory definition of investment advice by the Department. However, when it issued the advice rule, the Department dismissed the applicability of section 404(c) outright in a manner that is both inconsistent with the statements made in connection with IB 96-1 and that fails to consider how section 404(c) operates or ERISA's allocation of fiduciary responsibilities where the participant exercises independent control. The sum total of the discussion of section 404(c) in the rule's preamble is as follows:

---

[23] 61 FR 29586 (June 11, 1996).
[24] 29 CFR. section 2509.96-1(b), *fn 2*.
[25] DOL Advisory Opinion 2005-23.
[26] *Id.*

> ERISA section 404(c) provides relief for acts which are the direct and necessary result of a participant's or beneficiary's exercise of control. Although a participant or beneficiary may direct a transaction in his or her account pursuant to fiduciary investment advice, that direction would not mean that any imprudence in the advice or self-dealing violation by the fiduciary investment adviser in connection with the advice was the direct and necessary result of the participant's action. Accordingly, section 404(c) of ERISA would not provide any relief from liability for a fiduciary investment adviser for investment advice provided to a participant or beneficiary. This position is consistent with the position the Department took regarding the application of section 404(c) of ERISA to managed accounts in participant directed individual account plans. *See* 29 CFR 2550.404c–1, paragraphs (f)(8) and (f)(9).[27]

The Department's assertion that its position on the application of section 404(c) to nondiscretionary advice is consistent with its position on managed accounts overlooks critical distinctions between a discretionary investment manager and a nondiscretionary provider of investment advice within ERISA's fiduciary framework. A discretionary manager has full authority to manage plan assets and therefore, by definition, its actions in managing the account are not the result of the participant's exercise of control. A nondiscretionary provider of investment advice makes recommendations that will only affect a participant's account if the participant chooses to implement the recommendation. In other words, a participant who receives nondiscretionary investment advice continues to exercise some level of control over investment decisions by choosing to implement them while a participant who appoints an investment manager does not. Regardless of the merits of the Department's position on the application of section 404(c) to discretionary managers, it is irrelevant to the application of section 404(c) to nondiscretionary advice providers.[28]

Even apart from this fundamental distinction between discretionary management and non-discretionary investment advice for purposes of section 404(c), it is questionable whether comparing a discretionary investment manager selected by a trustee or named fiduciary to a non-discretionary investment advice provider independently selected by a participant would be appropriate under ERISA's fiduciary framework. As explained above, exclusive authority for managing plan assets resides in the trustee. The only exceptions are where the trustee is subject to the direction of a named fiduciary or the named fiduciary appoints an investment manager. Unless the participant is a named fiduciary, which is rarely the case, the trustee (who has custody and controls the assets of the plan) cannot follow the directions of an investment manager independently selected by the participant without risking liability based on the trustee's exclusive responsibility for managing investments of the plan. Therefore, a discretionary manager is not properly appointed as a fiduciary under ERISA unless appointed by a named fiduciary as an

[27] 81 F.R. 20965-66 (April 8, 2016).

[28] The Department has similarly adopted a regulation providing that section 404(c) does not apply to protect a plan fiduciary from liability for the imprudent selection or monitoring of designated investment alternatives under a plan. 29 CFR 2550.404c–1(d)(3). As with a discretionary investment manager, a participant has no control over the selection of designated investment alternatives by the plan fiduciary. Thus, this position is similarly inapposite to a non-discretionary investment advice provider.

investment manager under the plan.[29] Admittedly, a participant could give effective control to a managed account provider without involvement of the plan fiduciary by giving the manager access to his or her account (e.g., by sharing log-in credentials). However, this is more properly viewed as essentially having the manager act as a proxy for the non-fiduciary participant rather than the manager itself exercising control over the account as a plan fiduciary. In any case, if a discretionary manager is not viewed as properly appointed when appointed independently by the participant, then it would be a perverse result indeed for a nondiscretionary investment advisor selected by a participant, without any involvement of the trustee or named fiduciary, to be treated as a plan fiduciary.

In any event, the preamble's cursory statement on section 404(c) provides no analysis and simply states that a provider's investment advice is not the direct and necessary result of a participant's exercise of control. But this merely states the obvious. Any action by a fiduciary that would form the basis for liability under ERISA must have been taken by the fiduciary itself and not the participant. If that fact alone disqualified a fiduciary from section 404(c) protection, then no breach by a fiduciary would be subject to 404(c) protection, and the Department's rationale would render section 404(c)'s protection essentially meaningless.

One potential rationale for not relieving an investment advice fiduciary of liability under section 404(c) is to assert that investment advice effectively prevents a participant from exercising control over his or her account, notwithstanding that the participant must act to implement the advice. Under the new advice rule, advice includes any communication that can be reasonably understood as a suggestion that a participant take or refrain from taking an action. It is not clear how, for example, a mere suggestion that a participant consider investing in a plan's target date mutual fund would deprive a participant from exercising control over his or her account as a practical matter. But asserting that is so nevertheless merely assumes the intended result and begs the key question that the Department has not addressed throughout this rulemaking – what are the circumstances under which information provided to a participant by an investment advice provider may affect the ability of the participant to "exercise control" within the meaning of section 404(c)?

In fact, the Department regulation adopted in 1992 specifically outlines what is required for a participant to exercise control over the account in order to qualify for the relief of section 404(c).[30] The basic concepts underlying the section 404(c) regulation are that participants must have access to a sufficiently broad range of investment choices, be able to exercise choice freely from among those investments and have access to sufficient information to make an informed choice. While some of these requirements are quite onerous, the basic purpose of section 404(c) is to encourage plans to allow individual participants to have choice in how they invest their assets.

The regulation also requires that the participant's exercise of control be "independent" which is defined as follows:

---

[29] This is recognized in the two examples cited by the Department in the advice rule's preamble both of which contemplate a plan fiduciary designating the investment managers selected by the participant. *See* 29 CFR 2550.404c–1, paragraphs (f)(8) and (f)(9).

[30] 29 CFR 2550.404c–1

> (c)(2) *Independent control.* Whether a participant or beneficiary has exercised independent control in fact with respect to a transaction depends on the facts and circumstances of the particular case. However, a participant's or beneficiary's exercise of control is not independent in fact if:
>
> (i) The participant or beneficiary is subjected to improper influence by a plan fiduciary or the plan sponsor with respect to the transaction;
>
> (ii) A plan fiduciary has concealed material non-public facts regarding the investment from the participant or beneficiary, unless the disclosure of such information by the plan fiduciary to the participant or beneficiary would violate any provision of federal law or any provision of state law which is not preempted by the Act; or
>
> (iii) The participant or beneficiary is legally incompetent and the responsible plan fiduciary accepts the instructions of the participant or beneficiary knowing him to be legally incompetent.[31]

In short, under section 404(c), a fiduciary may not subject a participant to improper influence and may not conceal material non-public facts (unless revealing them would violate applicable law), but is otherwise not subject to liability under ERISA so long as the participant has full information and a full opportunity to implement his or her own investment choices.[32]

The section 404(c) regulation goes even further where a participant or beneficiary exercises control over the assets in his account to engage in a sale, exchange or leasing of property, or a loan with a plan fiduciary or an affiliate of such fiduciary. The regulation states that such exercise of control will not be "independent" unless the terms of the transaction are "fair and reasonable" to the participant or beneficiary at the time of the transaction.[33] A transaction will be deemed to be fair and reasonable to the participant or beneficiary if he pays no more than, or receives no less than, adequate consideration as defined in ERISA section 3(18) in connection with the transaction. As explained in the preamble to the section 404(c) regulation, these standards were adopted from established principles relating to the circumstances under which consent of a beneficiary of a trust will relieve a trustee from liability for breach of his fiduciary duties, citing to the Restatement of Trusts.[34] What this means is that, under section

---

[31] 29 CFR section 2550.404c-l(c)(2).

[32] The focus on "improper" influence in the regulation is particularly striking. If investment advice meeting a fiduciary standard – which would presumably constitute "proper" influence – also served to prevent a participant from exercising independent control, then the regulation would not have used the word "improper" rather than simply referencing "influence" generally.

[33] 29 CFR section 2550.404c-l(c)(3).

[34] 57 FR 46906 (October 13, 1992), *see* text at FN 25 citing *Restatement (Second) of Trusts,* section 216 (1959) which provides:

(l) Except as stated in Subsections (2) and (3), a beneficiary cannot hold the trustee liable for an omission of the trustee as a breach of trust if the beneficiary prior to or at the time of the act or omission consented to it.

(2) The consent of the beneficiary does not preclude him from holding the trustee liable for a breach of trust, if–

404(c), the trustee of the plan can engage in a principal transaction with a participant so long as the trustee does not exert improper influence and the terms of the transaction are fair and reasonable. What is important to infer here is that the definition of independent control is intended to protect the participant in transactions with a plan fiduciary or plan sponsor where the overwhelming balance of power in the transaction rests with the institutional plan fiduciary, as opposed to protecting the participant from himself or herself.

While the preamble to the Department's advice rule provides no real explanation of how the Rule comports with section 404(c), the Rule itself clearly goes far beyond the existing regulatory framework. The new investment advice regulation imposes ERISA fiduciary standards of conduct on any person that makes "a communication that would reasonably be viewed as a suggestion that the advice recipient engage in or refrain from taking a particular course of action" with respect to a participant's investment of his or her account. Imposing prudence and loyalty standards on anyone who makes a "suggestion" is a far cry from imposing those standards only when the person exercises "improper influence" or "conceals material non-public facts". That is a remarkable extension of the conduct standards beyond those that apply under section 404(c). It essentially implies that once a participant receives such a suggestion, the participant is no longer competent to evaluate it independently.

In addition, the failure to reconcile the Rule with section 404(c) is perhaps most clearly evidenced by a provision in the 404(c) regulation which states: "A fiduciary has no obligation under Part 4 of Title I to provide investment advice to a participant or beneficiary under an ERISA section 404(c) plan."[35] This provision appears in the section of the regulation defining what constitutes the exercise of independent control, and was included to make clear that a plan need not provide investment advice in order for section 404(c) to apply. IB 96-1 states similarly that there is no requirement under the section 404(c) regulation to provide either investment education or investment advice.[36] However, if there were an obligation for a fiduciary to provide investment advice to comply with section 404(c), and the fiduciary providing the advice had liability for that advice under section 404(c) as it does under the new investment advice rule, the result would be circular. In other words, if a fiduciary must provide investment advice in order to ensure that the participant exercises independent control, but the recommendations in connection with that investment advice give rise to liability notwithstanding section 404(c), a fiduciary could never fully insulate itself from liability as section 404(c) specifically contemplates. The fact that the Department felt the need to clarify this in the section 404(c) regulation demonstrates that

---

(a) the beneficiary was under an incapacity at the time of such consent or of such act or omission; or
(b) the beneficiary, when he gave his consent, did not know of his rights and of the material facts which the trustee did not reasonably believe that the beneficiary knew; or
(c) the consent of the beneficiary was induced by improper conduct of the trustee.

(3) Where the trustee has an adverse interest in the transaction, the consent of the beneficiary does not preclude him from holding the trustee liable for a breach of trust not only under the circumstances stated in Subsection (2), but also if the transaction to which the beneficiary consented involved a bargain which was not fair and reasonable.

See also III Scott, Trusts section 216 (3rd ed.1967); Bogert, Trusts section 941 (2d ed. 1960).

[35] 29 CFR 2550.404c–1(c)(4).

[36] 29 CFR. section 2509.96-1(b), *fn 1*.

investment advice fiduciaries were to be protected from liability for advice to participants under section 404(c). The new advice rule reversed this long-standing position without analysis or discussion and now stands in conflict with the language of the 404(c) regulation and section 404(c) itself.

The extent to which the investment advice rule deviates from ERISA's statutory scheme for allocation of fiduciary responsibilities is also clearly evident in the area of distributions. The Rule provides that a recommendation to take a distribution from a plan is "investment advice" under ERISA. If that is true, then the distribution decision must be an incidence of managing the plan's assets. However, the trustee under ERISA has *exclusive* authority to manage the assets and section 404(c) is the only provision available to relieve that trustee from liability for participant's decisions. On what legal principle is the trustee relieved from liability for a participant's decision to take a distribution from the plan where section 404(c) does not apply (for example, a distribution from a defined benefit plan)? No one would take the position that a trustee of a defined benefit plan should be liable for a distribution made solely at a participant's request pursuant to the terms of the plan. Yet, the logic of the Department's advice rule would require that result since the distribution, even though it was made without any input from the trustee, would nevertheless be the exclusive responsibility of the trustee under those circumstances. The problem is not with ERISA and section 404(c) but with the Department's attempt to impose liability under the advice rule in connection with participant-decision making under ERISA in ways never contemplated by ERISA itself.

This Analysis is Supported by the Statutory Exemption for Participant Advice Enacted by Congress in 2006

Congress amended ERISA through the Pension Protection Act of 2006 to include a new prohibited transaction exemption for the provision of investment advice to participants.[37] This marked the first time that the statute itself explicitly referred to participant investment advice. A fair question is why a prohibited transaction exemption is needed if advice to participants is not subject to ERISA's fiduciary framework. Where a plan complies with section 404(c) thus protecting all fiduciaries from liability, a prohibited transaction exemption may seem unnecessary and superfluous.

However, section 404(c) does not say that a person providing advice is not a fiduciary. In fact, advice providers selected by another plan fiduciary may be fiduciaries under ERISA. However, section 404(c) provides that an advice provider will not have liability as a fiduciary under ERISA if its requirements are met. Accordingly, in the plan context, there is still a reason to provide certainty about the application of the prohibited transaction rules which govern the conduct of fiduciaries. Moreover, in the IRA context, the individual account holder is the fiduciary with respect to the account so prohibited transaction relief is needed for investment advice in that context as well.

[37] ERISA Sections 408(b)(14) and 408(g).

Importantly, the conditions that Congress imposed under the exemption are completely consistent with ERISA's fiduciary framework as described above. For example, the exemption requires that an advice provider apply generally accepted investment theories, use relevant information about the participant, use objective criteria to provide asset allocation portfolios and, importantly, operate "in a manner that is not biased in favor of investments offered by the fiduciary adviser".[38] These requirements, in particular the "not biased" requirement, would be unnecessary if the advice provider were always otherwise required to meet ERISA's duties of prudence and loyalty. The reason they are needed is that while an advice provider is a fiduciary, it has no liability for failing to comply with the prudence and loyalty standards of conduct where the requirements of section 404(c) are met, and thus Congress chose to impose these requirements through the prohibited transaction exemption.

It is worth noting as well that, while Congress imposed these conditions when creating the prohibited transaction exemption under ERISA, it did not require as a condition of the exemption that an advice provider meet the standards of prudence and loyalty themselves or to contractually obligate itself to do so. Yet, less than four years after enactment of the Pension Protection Act, the Department began its effort to issue an advice rule which not only purports to impose such standards of conduct with respect to advice to all participants and IRA owners, but to do so in a way that complicates the overall regulatory framework and increases the potential for confusing investors.

Excluding Participant Advice from the ERISA Fiduciary Framework is Consistent with Individual Choice

Section 404(c) is premised on the notion that where an individual has full information about a transaction, and is not subject to improper influence, the individual can make his or her own choices. It allows individual choice free from ERISA's fiduciary constraints and therefore encourages plans to offer investment choice. The investment advice rule discourages individual choice by imposing ERISA liability on advisors assisting participants with those choices in situations where Congress clearly intended to promote individual choice. The point is not that advisors should be free to act without constraints on their conduct. The point is that their conduct should be governed not by ERISA but by financial services regulators. The only time ERISA's strict fiduciary responsibility provisions should come into play is when the advisor's conduct deprives the individual of control in the manner contemplated by the section 404(c) regulation.

The Department's advice rule effectively treats advice to a participant as advice to the plan or plan fiduciary thereby bringing all advisors within ERISA's fiduciary framework. This is a questionable result as both a matter of law and a matter of policy. Until the Rule was revised, few had reason to challenge this conclusion because most investment assistance could be structured to avoid fiduciary status. With the vast expansion in scope of fiduciary liability imposed by the new Rule, the examination of the Rule should consider how this Rule as a whole integrates into

[38] These requirements apply where the advice is provided through a computer model. Similar requirements apply under the Department regulation where the advice is provided through an entity that receives a level fee.

ERISA's fiduciary framework and section 404(c). For the reasons above, we believe that advice to a participant should be treated as investment advice under section 3(21)(A)(ii) of ERISA only where the participant is not exercising independent control as defined in the section 404(c) regulation – specifically where there is a potential harm to the plan or there is risk that a plan fiduciary such as the trustee or plan sponsor is taking advantage of the participant. This approach creates a path for consistent regulation of investment advice to individuals through financial services regulation.

A New Legal Framework for Investment Advice

The approach taken by the Department in the BIC Exemption and other prohibited transaction provisions of the Rule imposes a substantive standard of conduct on fiduciaries providing advice to participants and IRA owners that is difficult to reconcile with ERISA or the Internal Revenue Code. This results in different standards of conduct for investment advice providers to plan participant accounts and IRAs than other types of non-retirement accounts with the resulting potential for complexity and confusion on behalf of retail investors.

However, the Department can apply the Rule consistent with ERISA's fiduciary framework and return responsibility for regulating conduct to the appropriate prudential regulator with two simple fixes. Taking these steps would ensure consistency between Department regulation and financial services regulation in the area of investment advice to retail investors, creating a uniform standard of conduct regardless of account type. The two fixes are:

- Change the definition of investment advice so that it continues to include advice to the plan and plan fiduciaries but does not include recommendations to participants who exercise independent control over their investment choices as defined in the section 404(c) regulation or who select their own advice providers.

- Issue a new prohibited transaction exemption that covers all transactions recommended by a regulated financial services firm so long as the recommendations comply with the standard of conduct required by its primary financial services regulator.

The first step would reinforce the primacy of ERISA's pre-existing fiduciary framework under section 404(c) over the Rule, and make it clear that the Rule only applies in circumstances where the participant is not exercising independent control or selecting his or her own advice provider. Put another way, any time a participant is exercising independent control or selecting his or her own advice provider, that participant's advice provider should be subject to its primary regulator, not to the Department's investment advice rule.

The second step would then ensure that no advice could be provided to participants or IRA owners unless the advice provider complied with its primary regulator's standards of conduct. The Department should create a new, streamlined prohibited transaction exemption the sole condition of which would be that the regulated financial services firm providing advice must have complied with the standard of conduct specified by its primary financial services regulator (SEC for registered investment advisers; SEC/FINRA for broker-dealers; the OCC for federal banks and state banking authority for banks supervised by a state; state insurance commissioners for insurance companies). This approach would result in a uniform standard of conduct established by an advice provider's primary regulator for advice to participants and IRA owners that would be the same as the standard of conduct applicable to such customer's other account types.

The Department's advice rule would continue to apply to advice to employee benefit plans and their fiduciaries, as well as advice to participants who do not exercise independent control and do not select their own advice providers. However, this scope is in keeping with ERISA's traditional fiduciary framework.

We would be pleased to respond to any questions or comments regarding this letter.

Sincerely,

Ralph C. Derbyshire

cc: **United States Securities and Exchange Commission**
The Honorable Jay Clayton, Chair
The Honorable Kara M. Stein, Commissioner
The Honorable Michael S. Piwowar, Commissioner

Financial Industry Regulatory Authority
Robert Cook, Chairman and Chief Executive Officer, FINRA
Robert Colby, Chief Legal Officer, FINRA

Attachment to Fidelity Investments
Comment Letter on RIN 1210-AB82
dated August 7, 2017

The body of our comment letter requests that the Department change the Rule and allow the SEC and other financial services regulators to establish standards of conduct with respect to investment advice to plan participants and IRA account holders. If the Department does not adopt this approach, this attachment sets forth a number of alternative changes to the Rule and the BIC Exemption that should be made with respect to participant investment advice. This attachment also sets forth other changes to the Rule and the BIC Exemption applicable to investment advice to plans and plan fiduciaries in any case.

The Fundamental Problem with the Rule

The fundamental problem with the Rule is that, with very limited exceptions, the broad definition of investment advice does not distinguish between an advisor's discussion and sale of its own services and the advisor's actual recommendation of investment products and services. The Rule therefore treats the advisor as a fiduciary with respect to its own services and compensation, in some cases before a fiduciary relationship even exists. This would be the case both for advisors with transaction-based compensation and advisors selling fee-based advisory services. That approach is both unprecedented in fiduciary law and not commercially viable, potentially requiring an advisor to recommend its competitors over itself even if its own services are wholly appropriate for the investor. We have previously commented extensively on the problems this approach creates and have proposed specific solutions for the Department's consideration.[A1] We will not reiterate those comments here but they warrant full consideration as the Department conducts this examination of the Rule.

One additional point of note, though, is that the failure to distinguish between sales communications and investment advice results in a bias under the Rule against the broker-dealer business model where customers incur a fee and broker-dealers receive compensation only in connection with transactions executed for the customer. For more than 80 years, the law has recognized the fundamental distinction between broker-dealers and investment advisers. This distinction is appropriate because there is a fundamental difference between selling and advising. We believe this is a fundamental distinction worth preserving. The reason is that the advice model almost always implies payment of an identifiable separate charge to the customer for the advice received. For discretionary advisers (who make investment decision on behalf of customers) and for nondiscretionary advisers who regularly advise customers, this model makes sense. However, for small investors, payment of an ongoing fee is often uneconomic because of minimum fee requirements that advisers must impose as a business matter. In addition, investors of any size who want to make their own investment decisions and only need periodic assistance from an adviser, paying an ongoing advisory fee for advice that is not needed is uneconomic. The Rule's bias toward the advisory model clearly will result in more limited investor choice in contravention

[A1] *Fidelity Investments* comment letter submitted July 21, 2015 at: https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB32-2/00658.pdf and comment letter submitted April 17, 2017 https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB79/01385.pdf.

of the Administration's stated objective to empower individual choice. Fidelity is acutely aware of this problem as we seek to maintain ways to preserve investor choice for our large and diverse customer base.

The only way the final Rule recognizes a distinction between selling and advising for individual investors is a provision that purports to permit an advisor to recommend itself to a customer without that recommendation being treated as investment advice. This has become known as the "hire me" exception. However, the Department has been clear that when a recommendation to "hire me" effectively includes a recommendation on how to invest or manage plan assets, that recommendation could be considered investment advice under the Rule.[A2] This approach is wholly inadequate because financial services providers must be able to discuss the details of specific products and services they offer and are appropriate for the investor to have an effective "hire me" discussion. Following are suggested changes to address this fundamental problem:

Changes to the Rule

Require a Reasonable Level of Reliance by the Investor

The Rule subjects investment assistance to a fiduciary standard even where there is no expectation of reliance on the advice or advisor by the investor and no understanding or expectation on the part of the investor that such assistance is unbiased and is in his or her best interest. Rather, there need only be an understanding that the advice "is specifically directed to the advice recipient for consideration in making investment or management decisions…." Nor does the Rule provide any way for an advisor and an individual to avoid a fiduciary relationship, even if the parties were to enter into an express agreement to the contrary. For example, the Rule would subject an explicit sales pitch by a broker-dealer to an IRA owner to fiduciary standards, even if both the advisor and the IRA owner agreed that such communication was not intended to be unbiased advice in the IRA owner's best interest.

Such an all-encompassing definition goes beyond traditional and well-established principles of fiduciary law. Under common law, a fiduciary duty may arise when "either one of the parties, in entering [a] transaction, expressly reposes a trust and confidence in the other or because of the circumstances of the case, the nature of their dealings, or their position towards each other, such a trust and confidence is necessarily implied."[A3] The Rule imposes a fiduciary duty even where the investor does not expressly or impliedly place trust and confidence in the advisor by relying on the advice as being unbiased and in the investor's best interest.

The Department should align the Rule with long-standing principles of fiduciary law by requiring a reasonable expectation of reliance by the advice recipient. The Department could accomplish this, for example, by modifying the definition of investment advice to require that, based on the content, context and presentation of such advice, it is reasonable for the advice

[A2] 81 FR 20968 (April 8, 2016).

[A3] See *United Jersey Bank v. Kensey*, 306 N.J.Super. 540, 551, 704 A.2d 38 (App.Div.1997), citing *Berman v.Gurwicz*, 189 N.J.Super. 89, 93, 458 A.2d 1311 (Ch.Div.1981)(internal ellipses omitted).

recipient to rely on such advice as being unbiased and in the recipient's best interest with respect to such recipient's investment or management decisions. This requirement is already effectively included in the definition to the extent that the definition treats all investment advice as fiduciary in nature where the investment advice provider states that it is acting as a fiduciary within the meaning of ERISA. Such a statement would render it reasonable for an advice recipient to rely on the advice as being unbiased and in the recipient's best interest. But, as currently proposed, there is no corollary to this rule that would treat conduct as non-fiduciary in nature even where there is an express understanding that a fiduciary relationship is not intended.

Expand the Carve-Out for Independent Fiduciaries

If reliance is made a component of the definition of investment advice as described above, there is no need for a seller's carve-out because it would be clear from the context that there is no expectation that the seller is providing unbiased advice. However, if the Department does not introduce the component of reliance, it needs to rethink the approach taken to address the problem the Rule creates for any advisor selling investment products or services. The problem is that statements made in the sales context will almost always constitute investment advice under the Rule's current formulation because they are directed to a person and intended to encourage the purchase of a particular product or service.

The Department recognizes this problem and creates an exception for "independent fiduciaries with financial expertise" which has become known as the sophisticated fiduciary exclusion or SFE. However, the SFE does not apply to either small plans or individuals.

As the basis for limiting the exclusion, the Department states that "[r]esearch has shown that disclaimers are ineffective in alerting retail investors to the potential costs imposed by conflicts of interest, of the fact that advice is not necessarily in their best interest, and may even exacerbate these costs."

We disagree that the disclosures proposed by the Department – i.e., fairly informing the counterparty of either the existence and nature of the seller's financial interests in the transaction or that the seller is not undertaking to provide impartial investment advice or act as a fiduciary – would not be effective with respect to investors other than large plan sponsors. The conclusion that retail investors are incapable of understanding this disclosure is contradicted by the prominent role that disclosures play under the BIC Exemption which is largely intended for use in connection with transactions involving individuals. Nor are long-standing, well-settled principles of fiduciary law consistent with such an assumption, as they do not impose fiduciary status on a person unless there is express or implied trust and reliance on the person by the investor and they clearly recognize and permit the need for beneficiaries to waive fully and fairly disclosed self-dealing conflicts. While financial products and services may be complex, understanding the dynamics of a sales transaction is fundamental to the commercial activity that is part of everyone's daily life and the ability to waive fully and fairly disclosed conflicts is essential to the establishment and proper functioning of fiduciary relationships. Therefore, the Department should expand the SFE to apply to small plan sponsors, participants and IRA owners.

Clarify that Recommendations to Enroll In or Contribute to A Plan or IRA is Not Advice

The RFI asks whether recommendations to make or increase contributions to a plan or IRA should be expressly excluded from the definition of investment advice. Such recommendations are not included within the plain language of the definition of advice under the Rule. The Department recently issued FAQs that confirm this result. However, the Department had issued FAQs on two separate occasions that have caused some to question the Department's position in this regard.[A4] In both FAQs, the Department concluded that the described activity would not constitute advice, but none of the described activity included a recommendation to contribute to a plan or IRA as opposed to mere information about the benefits of contributing in the abstract. The absence of a clear statement that a recommendation to contribute to a plan would not constitute advice has caused some to infer that the Department may believe that such a recommendation would constitute advice, notwithstanding the plain language of the Rule. To the extent this ambiguity has a chilling effect on such recommendations, it clearly undermines the strong public interest in encouraging retirement savings. In light of the uncertainty caused by the Department's FAQs on this issue, we respectfully request that the Department include a clear statement in the Rule confirming that recommendations to enroll in or to make or increase contributions to a plan or IRA do not constitute fiduciary advice within the meaning of section 3(21)(A)(ii).

Changes to the BIC Exemption

The approach that the Department has taken with the BIC Exemption for the transition period currently in place through January 1, 2018 is sufficiently protective of plans, participants and IRA owners. In fact, the Department has implicitly acknowledged as much by assuming that the savings to investors that it attributes to the Rule and the BIC Exemption would be achieved by allowing the Rule to become applicable on June 9, 2017. This is precisely the exemptive approach we had suggested in our comment letter on the proposal and we continue to support this approach. In addition, following are the key changes that we urge the Department to make to the BIC Exemption:

Expand the Exemption to Large Plans

The BIC Exemption only applies to investment advice provided to plan participants and beneficiaries, IRA owners, and sponsors of small plans (less than $50 million). Given the protections inherent in the BIC Exemption, there is no reason to deny an investment advice provider that wants to assume fiduciary status with respect to a large plan the ability to rely on the BIC Exemption.

Expand the Exemption to Cover Online Only Computer Model Advice

The BIC Exemption excludes online-only computer model interactions unless an individual advisor is involved in providing the information generated by the model to the investor. That is, online advice is covered so long as a human advisor reads the online results to the investor rather

[A4] *See* Conflict of Interest FAQs (408B-2 Disclosure Transition Period, Recommendations to Increase Contributions and Plan Participation), FAQ 2 and 3 (August 2017), Conflict of Interest FAQs (Part II – Rule), FAQ 9 and 10 (January 2017), and Conflict of Interest FAQs (Transition Period), FAQ 12 (March 2017).

than the investor reading the online results himself or herself. There is no justification for excluding advice in an online format solely because a human being has not read it out to the investor. On that basis alone, the Department should simply expand the BIC Exemption to cover online advice outright.

Using the PPA computer model rule is not an appropriate solution. Among other issues, this would force reliance on two separate exemptions in the extremely common situation where the advice recipient begins the interaction online but then calls to ask for personal assistance from a phone representative. The legislative history of ERISA section 408(g) evidenced the intent of Congress not to override regulatory guidance regarding alternative ways of structuring certain permissible advice arrangements. The exclusion of online-only advice from the BIC Exemption contradicts that approach.

Expand the Exemption to Cover Participants Employed by Financial Institutions

The BIC Exemption does not allow a financial institution to rely on the exemption to provide investment advice to participants in the plans that it maintains for its own employees. The Department's reasoning in adopting this approach is that because of the "special nature" of the employment relationship, the financial institution should not be permitted to profit from the investments of employees because that would not be in the best interests of the plan participants.

This approach is inconsistent with the Department's historical treatment of financial institutions as plan sponsor. For example, the Department stated in the preamble to the ERISA section 404(c) regulation proposed in 1991:

> The Department is persuaded, however, that in the case of plans sponsored by certain financial institutions which have appropriate professional expertise in investment management, the designating fiduciary need not be independent. In enacting ERISA, Congress recognized the need to accommodate such plans by fashioning special rules. For example, section 408(b)(4) of ERISA permits a bank to invest the assets of an in- house plan in deposits of that bank and section 408(b)(5) permits an insurance company to issue contracts to a plan covering its own employees. The stated Congressional policy underlying these exemptions is that it would be "contrary to normal business practice" for a bank or insurer to purchase the products of another company of its own in-house plans. Moreover, the Department has recognized in certain administrative exemptions that it would be contrary to normal business practice for a company whose business is financial management to seek financial management services from a competitor, e.g., Prohibited Transaction Exemptions 77-3 and 82-63.

There is no reason why these same considerations should not be reflected in the BIC Exemption to cover investment advice provided to employees of financial institutions. In many cases, for compliance reasons, those employees are required to maintain their financial assets with the firm itself. Denying those firms the ability to provide employees investment advice means they would have no access to advice whatsoever, unless a third party advice provider is hired at additional expense.