INVESTMENT ADVISER
ASSOCIATION

April 12, 2007

Office of Exemption Determinations
Employee Benefits Security Administration
Room N-5700
U.S. Department of Labor
Washington, DC 20210
Attention: Cross-Trading Policies and Procedures Interim Final Rule
Response submitted electronically by e-mail (e-OED@dol.gov)

Re: Interim Final Rule Regarding Policies and Procedures Governing Cross-Trading of Securities for ERISA Accounts

Ladies and Gentlemen:

The Investment Adviser Association[1] welcomes the opportunity to comment on the interim final rule issued by the Department of Labor regarding written policies and procedures governing cross trading of securities for ERISA accounts.

Cross-trading by actively managed pension plans is a very important issue for IAA members. The IAA has submitted letters and participated in a number of meetings regarding cross trades with the Department over the years. In May 1998, the IAA submitted a detailed letter to the Department in response to the Department's request for comments on cross-trades in March of that year. Most recently, on September 20, 2006, the IAA submitted testimony in support of the expansion of the cross-trading exemption to the members of the ERISA Advisory Council in the form of a joint panel with the Investment Company Institute.[2]

We commend the Department and its staff for recognizing the important benefits of cross trading for ERISA-covered investors and we appreciate the opportunity to express our views on the interim final rule. Specifically, we urge the Department to revise the interim final rule so that (1) the regulations solely address the content of policies and procedures and are consistent with the provisions of Rule 17a-7 of the Investment Company Act of 1940 ("1940 Act'); (2) the role of compliance officers in the

[1] The Investment Adviser Association (formerly the Investment Counsel Association of America) is a not-for-profit association that represents the interests of SEC-registered investment adviser firms. Founded in 1937, the Association's current membership consists of about 500 firms that collectively manage in excess of $8 trillion in assets for a wide variety of individual and institutional clients. For more information, please visit our web site: www.investmentadviser.org.

[2] The joint panel presented testimony to the Working Group on Plan Asset Rules, Exemptions, and Cross Trading of the ERISA Advisory Council on Employee Welfare and Pension Benefit Plans (the "EAC Working Group") and the IAA provided a written submission to the EAC Working Group.

interim final rule is consistent with the role of compliance officers set forth in the Investment Advisers Act of 1940 (the "Advisers Act"); and, (3) the minimum asset size requirements of the Pension Protection Act of 2006 ("PPA") are monitored on an annual, not quarterly, basis. We also urge the Department to implement the cross-trading recommendations of the EAC Working Group.

I. The Interim Final Rule Should be Revised so That the Regulations Solely Address the Content of Policies and Procedures, and are Consistent With the Provisions of Rule 17a-7 of the 1940 Act

In August 2006, Congress passed the PPA, which added an exemption to ERISA to allow investment advisers to engage in active cross trades for their ERISA clients with plan assets in excess of $100 million, subject to certain conditions. Among other requirements, the trade must be executed at the current market price of the security and no brokerage commission or fee can be paid to the investment adviser in connection with the trade. In addition, the adviser must execute the cross trade pursuant to written policies and procedures, must seek and obtain client consent, and must provide quarterly reports with detailed information with respect to each cross trade executed by the adviser on behalf of the plan. Finally, the adviser must provide an annual written compliance report to each client. These requirements are similar to the provisions of Rule 17a-7 of the 1940 Act applicable to cross trading by investment advisers to mutual funds.

The PPA also included a provision requiring the Secretary of Labor to issue regulations regarding the content of cross-trading policies and procedures required to be adopted by an investment adviser. Specifically, the PPA provided, "No later than 180 days after the date of enactment of this Act, the Secretary of Labor, after consultation with the Securities and Exchange Commission, shall issue regulations regarding the content of policies and procedures required to be adopted by an investment manager under section 408(b)(19) of [ERISA]." Those regulations, which were issued on February 12, 2007, in the form of an interim final rule, are intended to mandate the style, format, and content of an investment adviser's cross-trading policies and procedures under ERISA.

The IAA supports the Department's requirements that an investment adviser's cross-trading policies and procedures be "clear and concise," "sufficiently detailed," and "reasonably designed to ensure compliance" with the Act, as provided by the interim final rule. These standards clearly address the PPA's mandate to the Department to issue "regulations regarding the content of policies and procedures required to be adopted by an investment manager." We are concerned, however, that certain other requirements imposed by the interim final rule are disclosure obligations rather than "regulations regarding the content of cross-trading policies and procedures." For example, subsection F of the interim final rule requires the identification of "the compliance officer responsible for periodically reviewing the investment manager's compliance with section 408(b)(19)(h) of the Act," and "a statement of the compliance officer's qualifications for

the position." These types of requirements simply add disclosure obligations without specifically addressing the content of policies and procedures or providing meaningful protection to ERISA plans. In addition, these types of requirements are inconsistent with the ability of compliance officers to delegate certain tasks, as discussed below.

We are also concerned that, for cross-trading purposes, the interim final rule imposes obligations on investment advisers to ERISA plans that are more extensive and burdensome than the disclosure obligations imposed on investment advisers to mutual funds. Since the adoption of Rule 17a-7 over forty years ago, the policies and procedures set forth in the rule have been overwhelmingly successful in helping to prevent cross-trading abuses by investment advisers. The rule has served as an effective means of ensuring that cross trades are made in the best interests of the clients involved in the transaction.

Many of the provisions of the PPA are substantially similar to the provisions of Rule 17a-7. The parallels between the PPA and Rule 17a-7 are logical. The Department and the SEC share the same underlying policy considerations regarding cross-trade transactions. Both seek to ensure that a fiduciary fulfills its duties to clients by promoting cost savings and market efficiencies for clients while fully protecting the interests of such clients.

In the interim final rule, however, the Department went beyond Rule 17a-7's flexible formulation of requiring procedures "which are reasonably designed to provide that all of the conditions of [the rule] have been complied with," and added a series of what are in essence disclosure obligations solely applicable to investment advisers that engage in cross trades for ERISA accounts. For example, the interim final rule requires that an investment adviser's policies and procedures include "a description of how the investment manager will mitigate any potentially conflicting division of loyalties and responsibilities to the parties involved in any cross trade transaction." This description in the procedures is not needed given that all of the conditions imposed by Congress in the PPA already are intended to mitigate potential conflicts of interest. To the extent investment advisers serve as advisers to mutual funds and pension plans, the different requirements will make application of the rules and the adoption of policies and procedures unnecessarily burdensome. As a practical matter, it will be difficult for investment advisers to maintain cross-trade programs if different procedures apply to different types of clients.

The interim final rule should be consistent with and comparable to the Rule 17a-7 cross-trading provisions and any inconsistencies and additional disclosure obligations should be eliminated from the interim final rule to the extent possible. In addition, the Department should clarify the interim final rule to confirm that the cross-trading exemption set forth in the PPA permits cross-trading between investment advisers and

their affiliates, just as Rule 17a-7 permits cross trading between investment companies and their affiliates.[3]

II. The Interim Final Rule Should be Clarified or Revised so That the Department Does not Expand the Scope of a Compliance Officer's Responsibilities

Under the Advisers Act, compliance officers are responsible for reviewing the efficacy of policies and procedures required to be implemented by the Act. Specifically, pursuant to Rule 206(4)-7, a compliance officer is responsible for administering the policies and procedures adopted under the rule. Compliance officers do not guarantee compliance with rules and regulations. Instead, a compliance officer is responsible for making sure that policies and procedures are established, reviewed for adequacy and effectiveness, and tested for compliance purposes. Compliance with policies and procedures is not the sole responsibility of compliance officers, however. In recent public statements, SEC staff members have indicated that other investment advisory employees, such as business personnel, can, and in some cases should, also be responsible for compliance matters.[4]

We are concerned that certain provisions in the interim final rule could be interpreted as expanding the scope of a compliance officer's responsibilities beyond the requirements set forth in the Advisers Act, including the interim final rule provisions mandating that an investment adviser's policies and procedures be "fair and equitable to all accounts participating in its cross-trading program" and mandating that an investment adviser's policies and procedures include a requirement that the investment adviser "allocate cross trades among accounts in an objective and equitable manner." Although the wording of the interim final rule is similar to the PPA requirement that an investment adviser adopt and engage in cross trades in accordance with "written cross-trading policies and procedures that are fair and equitable to all accounts," the manner in which this is addressed in the interim final rule could be interpreted as being significantly more expansive than the comparatively narrow focus of the Advisers Act on the adequacy and effectiveness of an adviser's policies and procedures.

The Advisers Act requires an investment adviser to adopt policies and procedures that are *reasonably designed* to be fair and equitable or *reasonably designed* to ensure the allocation of cross trades among accounts in an objective and equitable manner. The

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[3] In that respect, "affiliate" should be defined to include any entity controlling, controlled by, or under common control with the investment manager.

[4] For example, Gene Gohlke, Associate Director, SEC Office of Compliance, Inspections and Examinations, recently stated that based on examinations of the annual review process conducted by the SEC staff last year, larger investment advisory firms seem to be relying too much on the Chief Compliance Officer to conduct annual reviews. Instead, according to Mr. Gohlke, it may be more effective to have business personnel at a firm more involved in the annual review process. *See* CCO Outreach National Seminar webcast (Nov. 14, 2006) at http://www.connectlive.com/events/secoutreach111406/.

interim final rule could be interpreted as requiring an investment adviser to adopt policies and procedures that are fair and equitable, somehow guaranteeing perfection. As such, the language of the interim final rule would suggest that there would never be a situation in which an investment adviser, in the course of reviewing policies and procedures, could make a determination that a trade was not allocated in a fair and equitable manner and correct the situation. The interim final rule thus also would be inherently inconsistent with the requirement set forth in the PPA that the compliance officer must provide, on an annual basis, a written report describing the level of compliance with the investment adviser's policies and procedures, and any specific instances of noncompliance. Accordingly, we suggest that the Department clarify that the interim final rule requires an investment adviser to adopt policies and procedures that are reasonably designed to be fair and equitable or reasonably designed to ensure the allocation of cross trades among accounts in an objective and equitable manner.

Further, we suggest that the Department clarify that the interim final rule does not expand the scope of a compliance officer's responsibilities beyond the requirements set forth in the Advisers Act. At a minimum, the Department should clarify that the compliance officer is not required to certify every cross-trade transaction. Instead, the compliance officer can "periodically review" purchases and sales, as set forth in the PPA, in order to focus on the adequacy of policies and procedures. In addition, the Department should clarify that the compliance officer can rely on others to evaluate the consistency of cross-trade transactions with policies and procedures, based on a review of a sample number of transactions, in order to provide reasonable assurances that the policies and procedures are being followed on a consistent basis.

In the interim final rule, the Department also asks for comment regarding "whether the scope of the compliance officer's responsibilities under the regulation should be expanded to encompass compliance with all of the requirements of the statutory exemption." The interim final rule provides that the standards set forth in the rule "apply solely for purposes of determining whether an investment manager's written policies and procedures satisfy the content requirements of section 408(b)(19)(H) of the [PPA]."[5] Any expansion of a compliance officer's responsibilities as posited by the Department's request for comment would be inconsistent with a compliance officer's responsibilities under the Advisers Act. The compliance officer's review should be limited to the adviser's compliance with policies and procedures required by section 408(B)(19)(H) of the PPA.

[5] Section 408(b) (19) (H) of the PPA sets forth one of the conditions applicable to the cross-trade exemption. Specifically, it requires that "the investment adviser has adopted, and cross-trades are effected in accordance with, written cross-trading policies and procedures that are fair and equitable to all accounts participating in the cross-trading program, and that include a description of the manager's pricing policies and procedures, and the manager's policies and procedures for allocating cross trades in an objective manner among accounts participating in the cross-trading program."

III. The Interim Final Rule Should be Revised to Modify the Procedures for Compliance With the Minimum Asset Size Requirement of the PPA

The interim final rule requires a description of the procedures for ensuring compliance with the $100,000,000 minimum asset size requirement of the PPA. According to the interim final rule, "a plan or master trust will satisfy the minimum asset size requirement as to a transaction if it satisfies the requirement upon its initial participation in the cross-trading program and on a quarterly basis thereafter."

The IAA appreciates that the Department addressed the timing of determining the minimum threshold requirement in the interim final rule. While we agree that a plan or master trust should be required to satisfy the requirement upon its initial participation in the program, we respectfully suggest that monitoring should be done on an annual basis, and not a quarterly basis. Quarterly monitoring of a plan's asset size would be burdensome, expensive, and unnecessary. Presumably, the $100 million threshold was included in the PPA because a determination was made that at that level, plan fiduciaries would have the sophistication necessary to monitor cross-trade transactions executed on behalf of the plan.[6] A plan fiduciary, however, does not become less sophisticated if the plan dips below the $100 million threshold during the course of the one-year period.

In addition, quarterly monitoring adds another layer of bureaucracy for investment advisers without adding any benefit to ERISA plans. Investment advisers typically do not have information about the entire size of a plan since their role often is limited to managing part of a plan. Therefore, pursuant to the interim final rule, many investment advisers would be required to get quarterly certification of the plan's size from the sponsor or custodian. Such certification would be burdensome and expensive for both the investment adviser and the plan sponsor.

IV. The Department Should Implement Recommendations Made by the ERISA Advisory Council Working Group to the Secretary of the Department

The IAA respectfully requests that the Department implement cross-trading recommendations made to the Secretary of the Department by the EAC Working Group in November 2006. After considering testimony from a number of organizations, the EAC Working Group made several recommendations to the Secretary. We appreciate that the Department addressed one of the recommendations for the Department to provide guidance regarding circumstances in which assets may fluctuate above and below the $100 million threshold established by the PPA. Other recommendations made by the EAC Working Group include extending exemptive relief: (1) to allow cross trading by plans meeting a $50 million threshold; (2) to allow cross trading by pooled funds with at least one investor meeting the minimum asset size; and (3) to allow cross trades between

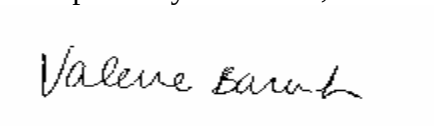
[6] As noted in prior correspondence and testimony, the IAA has advocated that absent any such threshold, there are fiduciary standards and numerous regulatory safeguards in place to provide protection to all plans, regardless of size.

plans maintained by employers in the same Controlled Group provided that ERISA plans within the same Controlled Group meet, in the aggregate, the minimum threshold requirements.

V. Conclusion

We appreciate the opportunity to provide our views on these important issues and would be pleased to provide any additional information the Department or its staff may request. Please do not hesitate to contact the undersigned if the Department or its staff has any questions regarding these matters.

Respectfully submitted,



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