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By email: e-ORI@dol.gov

Office of Regulations and Interpretations
Employee Benefits Security Administration
Attn: Conflict of Interest Rule
Room N-5655
U.S. Department of Labor
200 Constitution Avenue, NW
Washington, DC 20210

Re: Response to Conflicts of Interest Proposed Rule (RIN 1210-AB32)

Dear Sir or Madam:

I am writing regarding the U.S. Department of Labor's (DOL) proposed Conflicts of Interest Rule (Proposed Rule) and related Exemptions, which address conflicts of interest in financial advice on pension-related assets. The Proposed Rule makes appropriate and important updates to the framework that governs the provision of investment advice. It is particularly needed now, as more Americans than ever before rely on 401(k) plans and IRAs as their primary vehicles for retirement savings. The exorbitant costs that conflicted advice imposes on retirement savers are well documented in the DOL's regulatory impact analysis. Rather than repeat that thorough analysis, in this letter I write to address five specific matters.

1. Investment Education. According to the Proposed Rule, providers of investment education or retirement education would not become fiduciaries solely due to the provision of that education. The Proposed Rule's provisions on this point would supersede the DOL's Interpretative Bulletin 96-1 (IB 96-1) and are important to ensure that investment advice is not given under the guise of being education.

The Proposed Rule excludes from the definition of investment education all communications that recommend investment products, specific plan or IRA alternatives, etc. (Proposed Rule Section 2510.3-21(b)(6)). The Proposed Rule provides that references to specific investment products or types of accounts, even as examples, result in the communication being ineligible for the investment education carve-out. This provision is particularly important and should be included in the final rule.

As proposed, the rule means that providers of investment education that is coupled with references to particular investments as illustrations or examples are fiduciaries and thus subject to applicable requirements of Title I of the Employee Retirement Income Security Act of 1974 (ERISA) and the Internal Revenue Code. This outcome is appropriate since some retirement savers would view such references or examples as investment advice even if it is not so intended by the provider. That could happen because a saver is not financially sophisticated. Or, it could happen as a result of normal human behaviors. Research shows that the anchoring effects of examples change the behavior of

even financially sophisticated retirement savers. Anchoring effects occur when an investor treats a reference point as implicit advice.¹

In sum, the final rule should retain the exclusion from the definition of investment education of communications that refer to specific investment products, account types, etc.

2. Advice and Recommendations. ERISA states that: “render[ing] investment advice for a fee or other compensation . . .”² causes the provider of that advice to become a fiduciary. Proposed Rule Section 2510.3-21(a) sets out a series of circumstances under which “recommendations” constitute advice and give rise to fiduciary status. Of particular importance is the inclusion of recommendations regarding investments, asset management, and valuations in IRAs. IRAs now hold more of Americans’ retirement assets than any other single type of retirement account or plan subject to DOL oversight. IRA holders are particularly vulnerable to the costs that flow from advisory conflicts of interest because, unlike most 401(k)s and other employer-sponsored plans, neither the employer nor any other plan fiduciary plays an intermediary role in selecting an investment menu for IRAs.

Data indicate that retirement savers are particularly vulnerable to recommendations to roll over assets in 401(k) or other employer-sponsored plans into an IRA or regarding distributions from IRA assets. A survey by the Committee on Investment of Employee Benefit Assets (CIEBA) found that most distributions from plans sponsored by CIEBA members were rolled over into an IRA. Forty percent of the assets rolled over from CIEBA plans went to IRAs maintained by the recordkeeper for the plan making the distribution. Such rollovers are not often in the best interest of the plan participant. IRAs typically carry higher fees than employer-sponsored plans such as 401(k)s. Not only do they pay higher fees because they chose to rollover, it appears that many participants fail to comparison shop among IRA providers. If they did, we would not expect to see forty percent of the rollovers going to whichever recordkeeper the 401(k) plan happened to use.

To protect the interests of all retirement savers, including those who save through IRAs where there is no employer intermediation of investments, the final rule must cover all aspects of advice given regarding IRAs, from the decision on whether or not to establish one or contribute assets, through the investment of those assets, and into the distribution phase.

3. Best Interest Contract. The Proposed Rule contemplates the adoption of a “Best Interest Contract” prohibited transaction exemption, which would give advice providers the flexibility to continue to receive compensation in the nature of commissions, 12b-1 fees, and revenue sharing. The Best Interest Contract exemption is based on fiduciary concepts in traditional trust law and requires that advice provided to retirement savers be in compliance with impartial conduct standards. To qualify for the Best Interest Contract exemption, the adviser and retirement saver (and, if there is one, the adviser’s institution) must have a contractual relationship, the nature of which is described in the Proposed Rule. In preparing the final rule, the DOL should be mindful of two potential issues.

¹ See B. Douglas Bernheim et al., *The Welfare Economics of Default Options in 401(k) Plans*, 11, March 27, 2015, <http://andreyfradkin.com/assets/Defaults-and-Welfare-Complete.pdf> (forthcoming AMERICAN ECONOMIC REVIEW) 11 (explaining that anchoring effects cause participants to view a plan’s default contribution rate as having a “stamp of approval”).

² ERISA § 21(A)(ii).

a. Low Fee Exemption. The DOL requested comment on whether a streamlined version of the Best Interest Contract exemption should be available for advisers offering high-quality, low-fee investment products. I have concerns about any streamlined exemption but if the DOL decides to provide one, it should be limited to mutual funds that register under the Investment Company Act. As the DOL notes in the Proposed Rule, a condition of a streamlined exemption for mutual funds could be based on the fees and expenses required to be reported in each fund's prospectus.

I have three concerns with providing a streamlined exemption to mutual funds that qualify as high-quality, low-fee investments. First, defining "high-quality" will be challenging, both on a conceptual and technical level. One conceptual approach, which may in itself not fully capture the meaning of "high-quality," may focus solely on fee levels. Here, if "low-fee" is defined with reference to the fee and cost categories defined by the Securities and Exchange Commission (SEC), it will be important to account for the complexity of those categories. That complexity may permit mutual funds to shift their business models and, thus, shift fees among categories to qualify as a low-fee investment. For example, if the definition of low-fee excludes mutual funds that charge a sales load (or a load above a specified amount), the mutual fund may simply restructure to shift the revenue formerly received through the load charges to another category of fee or expense. Also, some funds, such as target-date funds, embed the advice in the product. That makes it difficult to compare those funds on an apples-to-apples basis with funds that do not embed advice. Finally, the calculation of fees often requires the assumption of a holding period in order to compare fees that are charged per period with one-time fees such as a load charge. The accuracy of the comparison depends on the accuracy of the holding period assumption.

Second, defining what constitutes a "low fee" fund may inadvertently cut off aggressive fee competition. Funds may have little incentive to try to reduce fees below the low-fee threshold.

Third, retirement savers who invest without receiving investment advice may view all funds that meet that standard as appropriate for their personal circumstances even though the funds may vary in risk and other important characteristics.

Finally, it is not appropriate at this time for the DOL to adopt a streamlined exemption for any types of investments other than straightforward mutual funds. Any suggestions submitted during this comment period for additional products to be covered by a streamlined exemption should be considered at a later date. Qualifying additional products for a streamlined exemption would increase the risk that the final rule would be gutted by exceptions as financial institutions develop inappropriate products that fall within the technical definitions of eligibility. Instead, the DOL should review suggested additions after the DOL has had experience with and data from the Best Interest Contract exemption.

b. Enforcement. Enforcement is an important element in the creation of a comprehensive plan to protect retirement savers. I have studied and written extensively on ERISA remedies for more than 20 years. The statute is not a model of clear drafting and, as currently interpreted leaves some injured plan participants without any remedy. I have come to realize that appropriate civil remedies for injured individuals are critical to provide redress and to encourage compliance. This is at least as true in the context of investment advice as it is in any other regulatory context.

The Proposed Rule's requirement, as part of the Best Interest Contract exemption, of a written contract that meets a minimum standard ensures that IRA owners have an individual right of action for breach of the impartiality standards or warranties. Retirement savers who receive advice on ERISA plan investments would have rights of action under ERISA's remedial sections and under contract law. For both IRA and ERISA plan investors, the contractual rights fulfill the critical functions of ensuring redress for injury and providing incentives for compliance. These provisions must be retained in the final rule to protect the rights of retirement savers.

4. DOL Regulation. It is important for DOL to move forward at this time with the Proposed Rule instead of waiting for the SEC to act on fiduciary regulation. Having appropriate regulation in place is necessary for the DOL to fulfill its mission of protecting retirement savers. As I have written elsewhere: "Changing workforce demographics, plan typology, and ERISA jurisprudence have all played a role in causing fiduciary principles to become integral to—and integrated in—the larger statutory framework."³ Fiduciary standards, including the prohibited transactions provisions, have become the workhorse of pension regulation.

Retirement savers hold about \$17 trillion in private sector employer-sponsored retirement plans and IRAs. ERISA's protection of those retirement savers is situated in a policy landscape that provides tax incentives for workers to save for retirement. The tax incentives constitute some of the largest items in the federal tax expenditure budget. The government and all taxpayers have a particular interest in protecting the assets saved with the support of those incentives from predatory or other self-interested behavior.

Some opponents of the Proposed Rule argue that the DOL should not regulate the provision of investment advice, but, instead should cede regulatory authority to the SEC. Those opponents are wrong. Under ERISA and Reorganization Plan No. 4 of 1978, DOL is charged with regulatory authority over the meaning of investment advice and the prohibited transaction exemptions. To fulfill its mission of protecting tax-favored retirement accounts, DOL must define the scope of fiduciary status. Disclosure and honesty, the hallmark of SEC regulation, is necessary but insufficient in the retirement savings universe. The Proposed Rules are not rules to ensure a fair playing field and to keep markets honest, as would be the SEC's focus—they are rules to ensure that tax-supported savings are used to provide those who earned those savings with financial security in retirement.

ERISA's regulation of investment advice under the fiduciary standards and prohibited transaction rules was neither an error nor a mirror of the SEC's mission to regulate advice under the Investment Adviser's Act. The SEC only has authority to regulate advice given on securities. Retirement savers invest in many categories of assets other than securities, including real estate, commodities, precious metals, etc. What makes sense from a uniformity of regulation standpoint is that advice given on all categories of investments in 401(k)s and IRAs be subject to the same fiduciary standards. Only regulation by the DOL can provide that uniformity. And, only the DOL can regulate advice on whether to roll over assets from an employer plan to an IRA. The SEC has no authority to regulate advice on that decision, which, as discussed above is a decision on which savers appear to be particularly vulnerable to conflicted advice.

³ Dana M. Muir, *Reflections on ERISA's Fiduciary Provisions: An Integral and integrated part of the Statute*, 6 DREXEL L. REV. 539, 543 (2014).

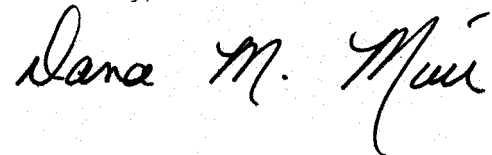
Some opponents of the Proposed Rule seem to be arguing that it is too much to expect all professional providers of investment advice to act in the best interest of their clients when providing advice on retirement savers. They claim that if all advisers are held to that standard then advice will suddenly become unavailable to many retirement savers.

Outside the advisory industry, however, a broad range of individuals and entities for many years have successfully provided services to retirement plans while complying with the fiduciary standards. That list includes employers, large and small, trustees, company board members, investment committee members, and many, many investment advisers. It is difficult to believe that the rest of the financial services industry, which has shown remarkable adaptability in its ability to provide services at a profit, will not find efficient ways to provide advice that puts clients first.

5. Alternative Proposals. Some organizations, including the Securities Industry and Financial Markets Association (SIFMA) and the Financial Services Roundtable (FSR), have made proposals that they characterize as providing protections similar to those that would be provided by the Proposed Rule. When read carefully, though, the SIFMA and FSR proposals fail to provide the level of protection needed by retirement savers. Specifically, although the SIFMA proposal is written in terms of client ‘best interest,’ the carve out for the sale of proprietary or an otherwise limited range of products permits any adviser at any time to evade the best interest rule by limiting the products on which advice is provided. And, the proposal’s requirement that advice be given with “care, skill, prudence, and diligence” does not solve the problem of conflicts of interest. Traditional fiduciary standards are composed of two separate requirements. One is the duty of care, which is what the language just quoted imposes. The other is the duty of loyalty – that a fiduciary act in the best interest of the client. The SIFMA proposal makes loyalty optional. Optional obligations are not obligations.

Thank you for your consideration of these comments.

Yours truly,

A handwritten signature in black ink that reads "Dana M. Muir". The signature is written in a cursive style with a large, prominent 'M' and 'U'.

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