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Submitted Electronically – e-ORI@dol.gov and e-OED@dol.gov

Office of Regulations and Interpretations
Employee Benefits Security Administration
Room N-5655 (RIN 1210-AB32) and Suite 400 (ZRIN 1210-ZA25)
U.S. Department of Labor
200 Constitution Avenue NW
Washington, DC 20210

Re: Definition of the Term “Fiduciary” (RIN 1210-AB32)
Best Interest Contract Exemption (ZRIN 1210-ZA25)
Principal Transactions in Certain Debt Securities Exemption (ZRIN 1210-ZA25)

Dear Sir or Madam:

Charles Schwab & Co., Inc., (“Schwab”), on behalf of itself and its affiliates, appreciates the opportunity to provide supplemental comments on the Department of Labor’s (“Department”) rule proposal that would expand the definition of fiduciary investment advice and propose new or modified prohibited transaction exemptions (the “Proposal”).¹ We are writing to provide additional comments on matters raised during the hearings. This letter is in addition to our original comment letter submitted on July 20, 2015 (“First Comment Letter”).

Schwab is pleased that many of the comments and questions posed by the Department at the hearings in August show a desire to strike an appropriate balance between protecting retirement savers while still preserving choice and access to a broad range of investing products and services necessary to meet diverse individual and plan needs. We continue to support the Department’s efforts to update the definition of fiduciary investment advice under the Employee Retirement Income Security Act of 1974, as amended (“ERISA”) to better protect retirement savers from conflicts of interest that erode savings, while maintaining choice and access without disrupting current business models.

¹ Notice of Proposed Rulemaking, Definition of the Term “Fiduciary”: Conflict of Interest Rule—Retirement Investment Advice, 80 Fed. Reg. 21928 (Apr. 20, 2015).

In our First Comment Letter, we described many aspects of the Proposal with which Schwab agrees, as well as those which present significant concerns. We provided a number of suggestions for changes to address the Department's laudable goal of mitigating conflicts, while at the same time ensuring that those in need of education and advice are not adversely impacted as a result of unintended consequences.

We expand below on three critical points raised in our First Comment Letter, as highlighted by the hearings.² Our recommended changes on these three points would go a long way in harmonizing the Department's overall proposal with current practices under both FINRA and SEC Investment Adviser Act rules. To do so, the final rule must:

1. Allow education-only conversations when firm representatives provide distribution and rollover assistance so that retirement savers have the information and help necessary to make informed decisions upon termination of employment. The Department can do this by adding language to the education carve-out under Section 6(i) and providing some concrete examples as guidance.
2. Enable referrals to and recommendations of fiduciary investment advice programs such as those provided by independent investment advisors or are available through managed account or wrap fee platforms. The Department can do this by modifying or creating a Best Interest Contract Exemption for advice programs to include more tailored contract and disclosure requirements that are consistent with Form ADV under the Advisers Act.
3. Preserve access to online tools and resources that millions of retirement savers rely on today to make informed investment decisions on their own, including tools that reference specific investments provided that the user controls the tool, and the tool output does not recommend or favor certain securities over others. The Department can do this by adopting fully the guidance and requirements under NASD (now FINRA) Notice to Members 01-23.

Without making changes in the final rule to address these areas, the benefits of the Proposal will not be realized and retirement savers will be inadvertently harmed.

1. The final rule must allow education-only conversations when firm representatives provide distribution and rollover assistance.

Schwab's First Comment Letter agreed with the Department's statement that the Proposal has the potential to better define the boundaries between fiduciary advice and education, to improve access to educational services and to exclude from fiduciary status education

² In response to the Department's request that commenters provide specific language changes, Schwab's First Comment Letter includes four Exhibits which mark-up the proposed rule text. Our First Comment Letter addresses four other areas of concern and a number of pragmatic implementation measures that we do not repeat in this letter.

that does not constitute personal recommendations.³ We also expressed our concern that the Proposal as written would undermine those goals and significantly reduce the availability of educational information, with the serious unintended consequence of eroding retirement savers' ability to make informed distribution and rollover decisions.

The provision of non-fiduciary education to support retirement savers' ability to make informed in-plan as well as distribution and rollover decisions is especially important in the context of a one-on-one conversation between a service representative and a retirement investor, whether this is part of an onsite meeting, call center or other interaction. As discussed in the hearings, this issue is of great concern not only to service providers but also to plan sponsors, who have a substantial interest in encouraging employee engagement about their plan options.⁴ The Department itself has recognized the value of call center support, stating that guidance from call center representatives that "doesn't include a specific recommendation and is limited to education" would not be fiduciary advice and therefore that the Proposal would likely make call center guidance "more available and robust, not less."⁵

During the hearings, the Department stated several times that a recommendation (and thus fiduciary investment advice) is not triggered unless there is a "call to action" with respect to a particular investment or investment strategy.⁶ The Department further stated that it intended to draw the line where FINRA drew the line on what constitutes a recommendation - where an investment professional tells a retirement saver where to put his or her money or what strategy to use;⁷ in other words where a specific investment or distribution recommendation is directed to a retirement saver.

Some financial service providers including Schwab have established policies and procedures, including call center guidelines, to enable education-only conversations to provide rollover assistance without a call to action or recommendation about what the participant should do. We follow the provisions of FINRA Regulatory Notice 13-45 in this regard, which states:

Some firms and their associated person provide education information to plan participants concerning their retirement choices. Firms that permit

³ U.S. Department of Labor, "Fiduciary Investment Advice Regulatory Impact Analysis" ("Regulatory Impact Analysis"), available online at <http://www.dol.gov/ebsa/pdf/conflictsofinterestria.pdf>, (Apr. 14, 2015) at 214, 223. The Regulatory Impact Analysis also appears at 80 Fed. Reg. 21951.

⁴ Transcript of Proceedings, U.S. Department of Labor Employee Benefits Administration, In the Matter of: Conflict of Interest Proposed Rule, Related Exemptions and Regulatory Impact Analysis Hearing (Aug. 10, 2015) at 1117.

⁵ Regulatory Impact Analysis at 224, 226.

⁶ Transcript at 107-108, 718.

⁷ *Id.* at 134.

educational information only should adopt measures reasonably designed to ensure that the firm and its associated persons do not make recommendations . . . to plan participants. These measures should include training concerning what statements may trigger [recommendations and application of FINRA’s suitability rule], and consideration of the compensation arrangements that could cause an associated person to make a recommendation.⁸

At Schwab, and consistent with FINRA’s guidance, representatives discussing a participant’s options can generally describe the features of an IRA at Schwab including the range of investment products and services generally available. However, they do not recommend to a participant that he or she stay in the plan, rollover to another plan, or open a rollover IRA. Describing the alternatives that a terminated participant has - including an IRA rollover - is critical to enabling the participant to make an informed decision. The final rule should allow these education-only conversations to continue.

This is consistent with the Department’s concern that any investment advice specifically directed to participants and IRA holders be covered by the new fiduciary definition. In Schwab’s case, although the vast majority of IRA holders are self-directed, some do seek investment advice after an IRA is opened. The Schwab representatives who provide investment advice are within a management structure separate and distinct from that of call center representatives providing distribution and rollover educational information to terminated participants. Schwab agrees with the Department that the provision of such investment advice at that point should be subject to an ERISA requirement to act in the retirement saver’s best interest and to a prohibited transaction exemption. However, the educational assistance prior to the terminated participant’s decision to take a distribution and roll over the assets - where there is no “call to action” and where no individualized recommendations are made with respect to the distribution - does not constitute fiduciary advice and should not be so characterized.

We understand the Department’s concern that a financial institution’s provision of distribution and rollover assistance to a terminated participant in some cases may be integrated with the provision of investment advice for how to invest the distribution proceeds in the IRA. This may be true of some financial institutions but it is not true for all.

Forcing education-only service models at the point of a rollover to perform a fiduciary review to obtain information to make a distribution recommendation would raise serious pragmatic concerns. For example, during a conversation describing options it is often unknown whether a participant will ultimately elect to rollover into an IRA or will want or need any investment recommendations. Characterizing this as a fiduciary conversation and requiring that all the necessary information be gathered and analyzed to make an actual recommendation would create additional time and costs for plan participants who

⁸ FINRA Regulatory Notice 13-45 (“Rollovers to Individual Retirement Accounts”) (Dec. 2013) at 5.

might only want to know their options in order to make their own decisions and do not want or need the additional questioning and services of a fiduciary.

We suggest several alternatives to address the above concerns.

First, the Department could adopt the proposed modifications to the investment education carve-out previously provided by Schwab (see Exhibit 3 to our First Comment Letter), to clarify that it is possible to have education-only materials and conversations that “describe the investment products and services available . . .” [*this would be new language for proposed section (6)(i)*] “without reference to the appropriateness of any individual investment alternative or any individual benefit distribution option” [*this is existing language in proposed section (6)(i)*]. Making this change would assure consistency with FINRA Regulatory Notice 13-45.

Second, the Department could provide concrete examples of situations where education, rather than fiduciary advice, is provided, such as the following:⁹

1. A participant is terminated from employment and contacts the call center to request information regarding his benefits. The call center representative explains the distribution alternatives available under the terms of the participant’s retirement plan, explains the four distribution options available (keep in plan, rollover to the terminated employee’s new employer’s plan, cash-out, or rollover into an IRA), including the availability of the institution’s or an affiliate’s IRA product in the event the participant elects to receive a distribution and roll over his assets. The representative does not ask or seek to review the participant’s current plan holdings or make any recommendations about how the proceeds of any distribution should be invested. The call center representative receives no financial incentives or other compensation that varies based on the distribution option ultimately elected by the terminated participant.
2. A third party plan administrator or plan sponsor sends a letter to all terminated participants that explains the four potential distribution options available, reminds them of the need to consider the benefits and limitations of each option before making a decision, and provides contact information in the event they have questions or would like to discuss their options. Consistent with the plan services agreement, a financial institution as a service provider to the plan sends a letter which describes the features of that institution’s IRA should the terminated participant decide that an IRA rollover is appropriate to their situation. Although the letters are addressed to each terminated participant, they are not otherwise individualized or customized with respect to each participant, nor is there a call to action to invest distribution proceeds in any way. If the terminated participant contacts the financial institution’s call center for assistance, the protocols in the first example above are followed.

⁹ These are in addition to examples we provided in our First Comment Letter.

3. An employee contemplating retirement contacts a call center, walks into a branch office of a financial institution or attends an onsite retirement planning session in order to obtain general information concerning planning for retirement and distribution options. The employee takes no action at that time. Later, the employee elects on his or her own to rollover to the financial institution. After the IRA is opened, the terminated participant seeks investment advice.
4. A financial advisor at a broker-dealer firm contacts a client who recently terminated employment. During the conversation, the financial advisor suggests to the terminated participant what investments to purchase in an IRA rollover at the firm.

In the first two hypotheticals above, there is no fiduciary advice recommendation. These are education-only conversations. In the third hypothetical, a recommendation occurs only at the time of, and with respect to, the financial institution's provision of any investment advice with respect to the IRA assets. In the fourth hypothetical, there is an "integrated" recommendation of distribution and securities recommendations. A firm that engages in such conduct will be making a fiduciary recommendation and will need to comply with a prohibited transaction exemption.

We are all aware of the "leakage" issue, where terminated participants cash out their plan benefits, with severe negative impact to their retirement savings. The DOL's Proposal, designed to increase retirement savings, could lead to greater leakage unless it allows room for education-only conversations and written communications. A discussion of the terminated participant's four options is necessary to avoid the loss of retirement savings. Firm representatives should be encouraged to provide this information to individuals who may or may not become IRA customers without risk of fiduciary liability. Schwab's education carve-out language suggestions and guidance through examples would assure that this much needed non-fiduciary assistance continues to be provided, while still addressing the conflicts with which the Department is concerned.

2. The final rule must enable recommendations of Advice Programs in the client's best interest, without imposing unnecessary burdens.

Many firms offer a wide array of fee-based programs to meet the diverse needs of retirement savers, from simple and low-cost programs to more complex and high cost programs. These include nondiscretionary investment advice for a fee, registered investment advisors recommending their own services, referrals to independent investment advisors, and managed account or "wrap programs" under Rule 204-3 of the Advisers Act (collectively, "Advice Programs").

Today, under the Investment Advisers Act, Advice Programs must be recommended in a retirement saver's best interest under a fiduciary standard with full disclosure of compensation and any conflicts of interest. Under the Department's Proposed Rule, recommendations of Advice Programs would also meet the ERISA definition of

“fiduciary.” This is because they are “recommendation as to the management of securities,” or a “recommendation of a person who” will be compensated for providing investment advice.¹⁰

Compensation to the financial institution may vary depending on whether and which Advice Program is recommended. Accordingly, an exemption must enable advisers to continue to make these recommendations while acting in the retirement saver’s best interest, without subjecting the financial institution to a potential prohibited transaction.

We appreciate the Department’s comments throughout the hearings in recognition of the need to modify the BIC exemption. Although recommendations of Advice Programs was not explicitly discussed, Ms. Borzi commented in her introductory remarks that the Department had received extensive comment letters regarding the BIC exemption, including those that suggested ways to “clarify the availability of exemptions for services, rollovers and other transactions affected by perceived ambiguities or omissions in the text of our proposal,”¹¹ and that “to the extent there’s an ambiguity, we can remove all possible doubt.”¹² We urge the Department to do so with respect to the recommendations of Advice Programs.

As discussed in Schwab’s First Comment Letter, the proposed BIC Exemption does not apply to recommendations of Advice Programs because the BIC is structured to provide relief for recommendations of “Assets” rather than recommendations of advisory services. Even if it were applicable to such recommendations, the proposed BIC would be unworkable in the context of Advice Programs. For example, discretionary money managers are not permitted to publicly disclose ahead of time the investments they are planning for the accounts they manage, rendering certain BIC disclosure provisions impossible to satisfy.

Schwab’s proposed BIC exemption for Advice Programs (Exhibit 1 to our First Comment Letter) provides a workable and enforceable approach that protects the interests of retirement savers while leveraging the existing Form ADV disclosure brochures advisers already must provide today prior to investing client assets. The BIC contract provisions can be integrated into the customary investment management agreement, signed at the time a retirement saver hires an adviser (after the recommendation to enroll in the Advice Program is made but before money is invested).

¹⁰ Much of the testimony during the hearings focused on the importance for firms to market their services directly to retirement savers, so-called “hire me” conversations, without being deemed to render fiduciary investment advice under ERISA. We generally agree. However, recommending an Advice Program is a type of “hire me” conversation that should be subject to fiduciary protections, provided that an applicable exemption from the prohibited transaction rules is also adopted.

¹¹ Transcript of Proceedings at 15.

¹² *Id.* at 16.

Schwab's proposal also addresses the concern raised during the hearings that financial incentives might impact advice contrary to the best interest standard,¹³ as it includes a requirement that the individual adviser making the recommendation receive the same compensation for any recommendable Advice Programs or investment strategy selected within an Advice Program, removing the incentive to recommend one Advice Program over another. Schwab's view is that this "modified BIC" for Advice Programs should be a standalone exemption, rather than be part of the "asset" BIC exemption, to provide clarity and certainty that might be lost if the exemptions were combined.¹⁴

3. The final rule must preserve online tools and resources for self-directed investors, without such assistance being viewed as fiduciary investment advice.

The education carve-out for "interactive investment materials" under Proposed Rule 2510.3-21(b)(6)(iv) would exclude materials that "include or identify any specific investment alternative available." This could be read to exclude hundreds of online tools available today for self-directed retirement savers to make their own informed investment decisions. To clarify that this is not intended, the preamble to the final rule should adopt fully the guidance and requirements under NASD (now FINRA) Notice to Members 01-23.

The Department stated in the Proposal that FINRA guidance "provides useful standards and guideposts for distinguishing investment education from investment advice under ERISA," and specifically solicited comments on whether the Department should adopt some or all of the FINRA standards "in defining communications that rise to the level of a recommendation for purposes of distinguishing between investment education and investment advice under ERISA."¹⁵ Reliance on FINRA guidance regarding what constitutes a recommendation was also referenced throughout the hearings.¹⁶

¹³ *Id.* at 88.

¹⁴ With respect to other proposed exemptions: Schwab has a few additional comments. Because of the risk management and investing benefits that options provide to IRA holders, we add our voice to the chorus asking the Department to add options to the list of permissible "Assets" under the BIC. Regarding the Principal Transaction Exemption, in addition to the points made in our First Comment Letter, Schwab requests that the Department include under the exemption the full range of agency securities, include agency- and GSE-guaranteed mortgage-backed securities. The latter are guaranteed by Ginnie Mae, Fannie Mae, or Freddie Mac, and on average carry equal or superior credit risk and liquidity characteristics compared to agency-issued debentures. Brokered CDs should also be included, as this is overwhelmingly a new-issue market in which dealers buy directly from underwriters and then offer the CDs to clients at a price that includes a customary dealer concession. (Schwab does not charge a commission or other transaction fee on such CD purchases, retaining the dealer concession as its only compensation.)

¹⁵ 80 Fed. Reg. at 21938.

¹⁶ Transcript at 109, 134, 156.

Under FINRA’s guidance, a recommendation is distinguished from a general communication based on whether the content, context, and manner of presentation indicate a call to action for the particular investor. Merely generating a list or mentioning specific investments or securities – which is common to many self-directed tools such as screeners, portfolio analyzers, and research – is not the test, standing alone.

Many of the online tool examples provided under the FINRA 01-23 guidance are not recommendations because they are not particularized communications to individual investors.¹⁷ Attributes of the tool examples 01-23 provides that would not fall within the definition of “recommendation” include:

- customers use and direct the tool on their own, including selecting the available criteria;
- customers can request a list of securities that meet objective criteria, and the firm does not control generation of the list to favor certain securities; and
- algorithms for the tools are not programmed to produce a list of securities based on subjective factors.

On the other hand, attributes of tool examples 01-23 provides that would fall within the definition of “recommendation” include:

- electronic communications that target customers or groups of customers encouraging or suggesting the particular customer(s) purchase highlighted securities;
- a portfolio analysis tool that allows a customer to indicate an investment goal and input personal information such as age, financial condition, and risk tolerance, and then produces specific securities that meet the investment goals indicated by the customer; and
- analysis of a customer’s financial activity or situation results in “pushing” specific investment suggestions to the customer’s attention.

The latter three examples would be “calls to action” consistent with the Department’s proposed definition of a “recommendation.” The former three examples, although they result in a useful list of securities for a self-directed investor to consider, are not specific or targeted suggestions that a customer buy a security and therefore are not recommendations.

Consistent with FINRA’s guidance under 01-23, and to avoid a potential and serious disruption to self-directed retirement savers, the Department should adopt a stand-alone education carve-out for *Portfolio tools for self-directed investors* under Section 2510.3-21(b)(6), to cover research and self-directed tools that list potential investments, provided that such tools “do not make recommendations as to the appropriateness of any individual investment products for the plan or IRA or a particular participant or beneficiary or IRA

¹⁷ Similarly, other FINRA rules treat equity research and ratings for individual stocks, whether online or otherwise, as educational and not investment advice because such research is not individualized to the needs of any participant or account holder.

owner.” This would also be consistent with the Department’s proposed carve-out for *Plan information* under (6)(i).¹⁸ The complete language for this approach can be found under Exhibit 3 to Schwab’s First Comment Letter.

Conclusion

Schwab appreciates the opportunity to provide these supplemental comments following the hearings. We welcome the opportunity to work with the Department more on this critically important initiative.

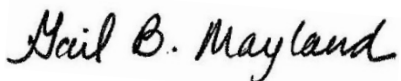
As stated in our First Comment Letter, retirement savers are entitled to investment advice in their best interest at a reasonable price. This is Schwab’s business model today. We support the Department’s objective to assure this basic fiduciary protection for all retirement savers. Schwab’s proposed changes are designed to ensure that in protecting retirement savers from conflicts of interest, final rules do not inadvertently harm them by unduly restricting the transmission of important information and guidance to plan sponsors, participants and beneficiaries, and IRA owners. In addition to protecting retirement savers, the goal must be to facilitate informed investing and retirement decisions by preserving choice and access to a wide range of self-directed tools and Advice Programs that meet individual needs.

We would be pleased to respond to questions or provide any additional information.

Very truly yours,



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¹⁸ In the absence of this consistency, customers of broker-dealers like Schwab will be able to access these self-directed tools for purposes of their taxable accounts but not their IRAs. From a retirement saver’s perspective, this will seem nonsensical.