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Office of Exemption Determinations  
Employee Benefits Security Administration  
Attention: Application No. D-12011  
U.S. Department of Labor  
200 Constitution Avenue N.W., Suite 400  
Washington, DC 20210

**RE: Improving Investment Advice for Workers & Retirees (ZRIN 1210-ZA29)**

Dear Sir/Madam:

The Investment Company Institute<sup>1</sup> appreciates the opportunity to comment on the proposed exemption, Improving Investment Advice for Workers & Retirees (“Proposed Exemption”)<sup>2</sup> issued by the Department of Labor (“Department”). The Proposed Exemption would provide an exemption from the prohibited transaction rules of the Employee Retirement Income Security Act of 1974, as amended (“ERISA”) and the Internal Revenue Code of 1986, as amended (“Code”) for investment advice fiduciaries. Additionally, the preamble to the Proposed Exemption includes a number of statements regarding the Department’s interpretation of the five-part test (“Five-Part Test”) forming a component of the Department’s regulation defining who is a fiduciary under ERISA and the Code by reason of providing investment advice. The Department solicited comments on the Proposed Exemption and its statements regarding the Five-Part Test.<sup>3</sup>

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<sup>1</sup> The Investment Company Institute (ICI) is the leading association representing regulated funds globally, including mutual funds, exchange-traded funds (ETFs), closed-end funds, and unit investment trusts (UITs) in the United States, and similar funds offered to investors in jurisdictions worldwide. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. ICI’s members manage total assets of US\$25.2 trillion in the United States, serving more than 100 million US shareholders, and US\$6.5 trillion in assets in other jurisdictions. ICI carries out its international work through ICI Global, with offices in London, Hong Kong, and Washington, DC.

<sup>2</sup> 85 Fed. Reg. 40834 (July 7, 2020).

<sup>3</sup> 85 Fed. Reg. 40834, 40840.

The ICI commends the Department's effort in issuing a new fiduciary proposal that *is intended* to align the standard of care for ERISA fiduciaries providing investment advice with the conduct standards in the Securities and Exchange Commission's ("SEC") Regulation Best Interest ("Reg BI") and the fiduciary duty of registered investment advisers under securities laws. As such, the Proposed Exemption presents an important step toward aligning standards of care for all investors, whether they are saving in a retirement account or other investment accounts. Consistent standards would help investors achieve better financial outcomes while increasing efficiency and preserving investor choice and access to advice.

To achieve these intended goals and truly provide retirement savers with the benefits that an aligned regulatory structure offers, the Department must—

- Clarify preamble discussion on Five-Part Test to ensure alignment with SEC's Reg BI and the Fifth Circuit's holding in *U.S. Chamber of Commerce v. U.S. Department of Labor* ("Fifth Circuit Decision").<sup>4</sup> While we do not believe it was the Department's intention, we are concerned that the Department's statements regarding the application of the Five-Part Test can be read to be inconsistent with the unambiguous provisions of the Department's investment advice regulation as well as the Fifth Circuit Decision, which requires a relationship of "*trust and confidence*" to be present for fiduciary status. We also believe that the preamble statement that compliance with Reg BI by non-fiduciary broker-dealers could trigger fiduciary status for ERISA purposes under the Five-Part Test can be interpreted as disregarding the critical distinction the SEC made between broker-dealers and registered investment advisers. We include illustrated recommendations for clarification of the preamble statements below. The failure to clarify the Department's preamble statements would leave the fiduciary definition plagued by many of the same concerns that the 2016 rulemaking raised.
- Make certain changes to its Proposed Exemption to ensure it meets its intended purpose. These changes should include:
  - Removing the condition requiring a fiduciary acknowledgement. Such a condition is unnecessary and is not consistent with the Fifth Circuit Decision in that compliance with this condition of the Proposed Exemption would effectively supplant satisfaction of the Five-Part Test.
  - Eliminating duplicative, overlapping disclosure requirements. Doing so would help to avoid investor confusion and be consistent with the Department's intent to align the Proposed Exemption with other regulatory requirements.

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<sup>4</sup> 885 F.3d 360 (5th Cir. 2018).

- Eliminating the Annual Retrospective Compliance Review and Certification or, at a minimum, making it administratively workable. The requirement that a Financial Institution's chief executive officer provide the certification is unrealistic, overly burdensome and unnecessary to achieve the desired result.
- Eliminating the Eligibility provision, or, at a minimum, rethinking who should have the authority to decertify a Financial Institution's or Investment Professional's ability to rely on the exemption. The same officials who drafted the Proposed Exemption should not be permitted to judge compliance.
- Revising the exemption to cover robo-advice. The exclusion of robo-advice is illogical and should be reconsidered. Personalized investment advice compliant with the Impartial Conduct Standards and other conditions of the Proposed Exemption could be provided through robo-advice programs.
- Modifying the Proposed Exemption to narrow the availability of compliance records to only authorized employees of the Department or Internal Revenue Service ("IRS") (as applicable).
- Modifying the exclusion for certain transactions involving a named fiduciary or plan administrator by raising the independence threshold to five percent, and expanding the Proposed Exemption's coverage to clearly permit advice in connection with Pooled Employer Plans.<sup>5</sup>
- Revising the standard for policies and procedures to require that they be "reasonably designed" rather than "prudently designed" to comply with the Impartial Conduct Standards.
- Eliminating any implication that the requirement to correct a prohibited transaction creates a fiduciary duty owed to IRAs.
- Reevaluating the statement that certain investments can be recommended to a Retirement Investor in a manner consistent with the Best Interest Standard only where there is ongoing monitoring of the investment. This statement appears at odds with the Department's prudence regulation and imposing such a monitoring requirement should be done only through notice and comment rulemaking.
- Expanding the definition of Covered Principal Transaction to include sales to a plan or IRA of closed-end fund shares.

## **I. The Department Must Clarify Its Discussion of the Five-Part Test**

On the same day it issued the Proposed Exemption, the Department implemented the Fifth Circuit Decision vacating the Department's 2016 fiduciary rule by re-codifying the Department's 1975

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<sup>5</sup> A Pooled Employer Plan ("PEP") is an individual account plan established to provide benefits to the employees of two or more unrelated employers and is treated as a single pension benefit plan. PEPs are defined in Section 101 of the Setting Every Community Up for Retirement Enhancement Act of 2019 ("SECURE Act"), which was included as Division O of the Further Consolidated Appropriations Act, 2020 (H.R. 1865).

investment advice regulation (“Regulation”), including the Five-Part Test, in the Code of Federal Regulations.<sup>6</sup> We appreciate this action and believe the Five-Part Test is the appropriate fiduciary advice definition. We believe reinstatement of the Five-Part Test is the necessary result of the Fifth Circuit Decision.

At the same time, however, the Department also elected to withdraw its 2005 advisory opinion<sup>7</sup> construing the Five-Part Test in connection with rollover recommendations and to provide *new* interpretations of the application of the Five-Part Test to rollover recommendations.<sup>8</sup> We are concerned that the Department’s new interpretations of the Five-Part Test are inconsistent with the unambiguous language of the Regulation and the Fifth Circuit Decision, which requires a relationship of “trust and confidence” to be present for fiduciary status to follow.<sup>9</sup> The Department’s interpretation of the regular basis and primary basis prongs of the Five-Part Test deserve special scrutiny because the Fifth Circuit Decision identified these prongs to be critical in capturing a fiduciary relationship.<sup>10</sup> Additionally, while the Department claims that its interpretation would “align” with the views of other regulators, we believe that the preamble, by suggesting that compliance with Reg BI by non-fiduciary broker-dealers could trigger fiduciary status for ERISA purposes under the Five-Part Test, overlooks the critical distinction the SEC consistently has made between broker-dealers and registered investment advisers. We include recommendations for clarification of the preamble statements below.

#### **A. Clarification of the Regular Basis Prong**

The preamble to the Proposed Exemption states that “advice to roll assets out of the Plan into an IRA where the advice provider will be regularly giving financial advice regarding the IRA in the course of a more lengthy financial relationship would be the start of an advice relationship that satisfies the ‘regular basis’ requirement.”<sup>11</sup> This interpretation is inconsistent with the plain language of the Regulation, which defines the circumstance under which “[a] person shall be deemed to be rendering ‘investment advice’ *to an employee benefit plan,*” and requires that advice be rendered “on a regular basis *to the plan,*” i.e., the particular plan or IRA at issue. As the Department acknowledges, “a recommendation to roll assets *out of a Plan* is advice with respect to the moneys or other property *of the Plan.*”<sup>12</sup> Under the unambiguous terms of the Regulation, the other four elements of the Five-Part Test, including the

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<sup>6</sup> 85 Fed. Reg. 40589 (July 7, 2020).

<sup>7</sup> DOL Advisory Opinion 2005-23A (December 7, 2005), available at: <https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/advisory-opinions/2005-23a>.

<sup>8</sup> 85 Fed. Reg. 40834, 40838–40.

<sup>9</sup> 885 F.3d at 365.

<sup>10</sup> 885 F.3d at 366.

<sup>11</sup> 85 Fed. Reg. 40834, 40839.

<sup>12</sup> 85 Fed. Reg. 40834, 40839 (emphasis added).

regular basis requirement, also must be satisfied with respect to “the Plan.” A subsequent advice relationship with respect to assets held outside the relevant plan (i.e., assets held in the rollover IRA) is simply not germane for purposes of the Five-Part Test, which by its own terms applies on a plan-by-plan basis. Instead, any ongoing advice regarding the IRA would only be relevant in determining whether the advice provider is a fiduciary with respect to the IRA.

The Department’s new interpretation would also mean that recommendations given at a time when no relationship of trust and confidence is present would be considered fiduciary investment advice if in the future more recommendations are given, or it is “anticipated” they will be given.<sup>13</sup> As stated above, however, the Fifth Circuit Decision makes clear that ERISA and the Code require a relationship of trust and confidence to be present *at the time a recommendation is made* for the recommendation to constitute fiduciary investment advice.<sup>14</sup> It cannot be that subsequent activity, or the anticipation of subsequent activity, confers fiduciary status on the first client interaction. That result would also be hard to square with the Fifth Circuit Decision finding that sales activity cannot be considered fiduciary investment advice.<sup>15</sup>

In order to properly account for the Fifth Circuit Decision, we request that the Department include a statement in the preamble to the final exemption consistent with the following:

*The Department desires to clarify its discussion of the regular basis prong of the five-part test. When the Department stated that a rollover recommendation may be the start of an advice relationship that satisfies the “regular basis” requirement, we wished to clarify that our view that fiduciary status with respect to a plan (including an IRA) would begin to apply only at that time when a sufficient amount of advice is given with respect to the assets of the plan such that advice is given “on a regular basis to the plan.” Only advice given after the regular basis requirement is met with respect to the plan’s assets would be considered fiduciary investment advice to the plan—the five-part test does not retroactively look back to advice that is given before the regular basis requirement is met or anticipate advice being provided in the future and hold such advice to ERISA’s or the Code’s fiduciary standard. It is “ordinarily inconceivable,” as the Fifth Circuit stated, that a relationship of trust and confidence forming the basis of a fiduciary relationship is present at the time when an initial rollover recommendation is provided.<sup>16</sup> For the avoidance of doubt, an initial rollover recommendation on its own would not meet the regular basis requirement.*

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<sup>13</sup> 85 Fed. Reg. 40834, 40839-40.

<sup>14</sup> 885 F.3d at 382 n.15.

<sup>15</sup> 885 F.3d at 380.

<sup>16</sup> 885 F.3d at 380.

## B. Clarification of the Primary Basis Prong

The Department’s preamble statements also could be interpreted to effectively remove the “primary basis” prong from the Five-Part Test by putting new emphasis on reading “a” primary basis in the meaning of the prong and supporting a view that there can be more than one and perhaps several “primary bases.”<sup>17</sup> Such a reading not only ignores the most natural reading of the word “primary” in the primary basis prong,<sup>18</sup> it also disregards the Department’s own prior statements acknowledging the difficulty in avoiding the plain meaning of the word.<sup>19</sup> Of course, such an interpretation would also disregard the fact that throughout the Fifth Circuit Decision, the Court described the test as looking at whether the advice is “the” primary basis, rather than “a” primary basis, for an investment decision.

We have serious concerns about the suggestion that there may be more than one “primary basis” for an investment decision.<sup>20</sup> Such an interpretation has the appearance of an attempt to expand the Five-Part Test in order to capture more interactions than are warranted under the plain language and meaning of the Department’s investment advice regulation. The Fifth Circuit criticized the Department’s similar attempted expansion in connection with the 2016 rulemaking. Attempted expansion through a preamble statement—without notice and comment rulemaking—does not remedy the failings of that prior effort.

Further, the preamble to the Proposed Exemption also states that “where advice is provided pursuant to a best interest standard such as the one in the SEC’s Regulation Best Interest, or another requirement to provide advice based on the *individualized* needs of the Retirement Investor, the parties typically should reasonably *understand* that the *advice* will serve as at least a *primary basis* for the investment decision.”<sup>21</sup> This interpretation suggests that recommendations broker-dealers provide that comply with Reg BI may by themselves satisfy up to four prongs of the Five-Part Test *per se*. The only prong not implicated by this statement is the regular basis prong. The interpretation also suggests that satisfaction of the individualized advice prong of the Five-Part Test may mean the primary basis prong has automatically been met.

We believe the Department’s interpretation mistakenly elevates Reg BI to a fiduciary standard. In fact, the Dodd-Frank Wall Street Reform and Consumer Protection Act gave the SEC authority to decide

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<sup>17</sup> 85 Fed. Reg. 40834, 40840.

<sup>18</sup> The definition of “primary”: “of *first* rank, importance, or value,” limits the concept of primary to a singular item. Merriam-Webster Dictionary, available at <https://www.merriam-webster.com/dictionary/primary> (*emphasis added*).

<sup>19</sup> The Department itself recognized such a reading when, in the 2016 preamble discussion justifying the elimination of the “primary basis” prong, the Department acknowledged the difficulty of establishing fiduciary status by having to prioritize advice when multiple advisors are consulted. 81 Fed. Reg. 20955, 20956 (Apr. 8, 2016).

<sup>20</sup> 85 Fed. Reg. 40834, 40840.

<sup>21</sup> 85 Fed. Reg. 40834, 40840 (*emphasis added*).

whether to impose a fiduciary standard on broker-dealers, and the SEC chose to not do so.<sup>22</sup> Instead, the SEC provided detailed guidance on when advice provided by broker-dealers would be viewed as solely incidental to the conduct of their business as broker-dealers, meaning the advice would not require the broker-dealer to register as an investment adviser and be subject to a fiduciary duty under the Investment Advisers Act of 1940.<sup>23</sup> Accordingly, alignment of Reg BI and the Five-Part Test would require that the Department acknowledge that broker-dealers generally are not considered fiduciaries.

Moreover, we disagree with any suggestion that the primary basis prong will be met whenever the individualized basis prong has been met. If that were the case, then the primary basis prong would be superfluous. That reading conflicts with well-established rules of statutory and regulation interpretation whereby one provision is not read to render another provision superfluous.<sup>24</sup>

In order to align the Department's interpretation with the SEC's Reg BI and to properly reflect the mutual exclusivity of each of the prongs of the Five-Part Test, we respectfully request that the Department include a statement in the preamble to the final exemption consistent with the following:

*The Department desires to clarify its discussion of the primary basis requirement of the five-part test, which requires a mutual agreement that the advice "will serve as the primary basis for investment decisions with respect to plan assets." The prior statements made by the Department should not be read to suggest that the primary basis requirement would automatically be met with respect to a plan (including an IRA) whenever any individualized advice or advice pursuant to the SEC's Regulation Best Interest has been provided to a Retirement Investor. Rather, it is the Department's intention that the word "primary" be read naturally to identify advice of first importance or value in the investment decision. Whether the primary basis prong has been met with respect to a plan will be based on all the facts and circumstances. We note, however, that a reasonable Retirement Investor would not be considered to rely on a Financial Institution's advice as the primary basis for his or her investment decisions where he or she is aware that the Financial Institution is not rendering advice pursuant to a relationship of trust and confidence but rather is pitching or touting the quality of its products and services in a sales discussion.*

### **C. Clarification That Hold Recommendations Are Not Covered Advice**

In addition to its statements interpreting the Five-Part Test as it relates to rollover recommendations, the Department stated in the preamble to the Proposed Exemption that the Proposed Exemption

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<sup>22</sup> 84 Fed. Reg. 33318, 33322 (July 12, 2019).

<sup>23</sup> 84 Fed. Reg. 33681 (July 12, 2019).

<sup>24</sup> *RadLAX Gateway Hotel, LLC v. Amalgamated Bank*, 566 U.S. 639, 645 (2012).

would provide exemptive relief for a recommendation to “hold” an investment.<sup>25</sup> The Five-Part Test is clear, however, that fiduciary investment advice status will only arise from recommendations to invest in, purchase, or sell securities or other property.<sup>26</sup> By its plain terms a “hold” decision is neither a recommendation to purchase or sell securities. As the Department is aware, the 2016 fiduciary rule would have covered advice to hold, but it was vacated.<sup>27</sup> Because the Department cannot by interpretation amend the Five-Part Test to include provisions the vacated 2016 fiduciary rule would have included, the Department should clarify in the preamble to the final exemption that a hold recommendation is not covered advice for purposes of the Five-Part Test.

## **II. Comments on the Proposed Exemption**

The Proposed Exemption represents an improvement from the Best Interest Contract Exemption<sup>28</sup> issued as part of the Department’s 2016 rulemaking, but certain important changes are needed to ensure that it serves to help investors achieve better financial outcomes while increasing efficiency and preserving investor choice and access to advice.

### **A. The Department Should Remove the Requirement to Acknowledge Fiduciary Status**

Among other disclosures that must be provided to Retirement Investors before engaging in a covered transaction, Financial Institutions would be required to provide a written disclosure acknowledging “that the Financial Institution and its Investment Professionals are fiduciaries under ERISA and the Code, as applicable, with respect to any fiduciary investment advice provided by the Financial Institution or Investment Professional to the Retirement Investor.”<sup>29</sup> We respectfully request that the fiduciary acknowledgment be removed or replaced with a disclosure of the Proposed Exemption’s best interest standard.

Acknowledging fiduciary status when providing an investment recommendation is not consistent with the Fifth Circuit Decision. Compliance with this could effectively supplant satisfaction of the Five-Part Test, causing Financial Institutions and Investment Professionals to become subject to a fiduciary standard even in situations where they otherwise would not have been. As a result, some Financial Institutions that do not intend to trigger fiduciary status under ERISA and the Code will not seek to rely on the Proposed Exemption as a prophylactic measure and will either rely on other exemptions or provide only investment education to Retirement Investors contemplated by Interpretive Bulletin 96-1.

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<sup>25</sup> 85 Fed. Reg. 40834, 40838.

<sup>26</sup> 29 C.F.R. § 2510.3-21(c)(1)(i).

<sup>27</sup> 81 Fed. Reg. 20946, 20997 (Apr. 8, 2016).

<sup>28</sup> Final Best Interest Contract Exemption, 81 Fed. Reg. 21002, 21081 (Apr. 8, 2016).

<sup>29</sup> Proposed Exemption § II(b)(1).



We believe this result would be unfortunate for Retirement Investors, who generally desire to receive personalized investment advice and would benefit from advice that is consistent with the Impartial Conduct Standards. If Financial Institutions were not required to acknowledge fiduciary status, they could provide assistance and comply with the conditions of the exemption even where they do not believe their activity should be considered fiduciary investment advice. This result would be in the interest of both Retirement Investors and Financial Institutions.

Moreover, we believe there are more effective ways to inform Retirement Investors of the duties owed to them than an acknowledgement of fiduciary status. In this respect, the word “fiduciary” is a legal term whose meaning depends on the circumstances.<sup>30</sup> For example, there are significant differences between the status of a fiduciary with respect to an ERISA plan and a fiduciary with respect to an IRA. Such a statement also could cause confusion in light of other regulatory requirements to disclose the nature of a client relationship for broker-dealers and investment advisers.<sup>31</sup> If the Department determines that some statement of the standard of care owed by Financial Institutions and Investment Professionals is necessary, a statement of the Proposed Exemption’s Best Interest Standard would be more helpful to Retirement Investors due to its specificity and consistency with applicable law.

## **B. The Department Should Eliminate Duplicative, Overlapping Disclosure Requirements**

In addition to the written acknowledgement of fiduciary status that must be provided prior to engaging in a covered transaction, the Proposed Exemption requires a description of the services and material conflicts of interest.<sup>32</sup> To avoid investor confusion resulting from multiple, overlapping disclosures and in support of the Department’s intent to align the Proposed Exemption with other regulations, we urge the Department to clarify that compliance with the comprehensive disclosure requirements under the federal securities laws applicable to registered broker-dealers and investment advisers will be deemed to meet the disclosure requirements of the exemption.

We note that registered broker-dealers and investment advisers are required to provide Form CRS to customers at the beginning of the customer relationship.<sup>33</sup> Disclosures concerning conflicts of interest arising from fees and costs, for example, must be included in Form CRS.<sup>34</sup> Statements regarding

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<sup>30</sup> 84 Fed. Reg. 33492, 33531 n.477 (July 12, 2019).

<sup>31</sup> For example, Form CRS, adopted by the SEC in 2019, requires investment advisers and broker-dealers registered with the SEC, and their respective associated persons, to deliver a relationship summary to retail investors at the beginning of the relationship. The relationship summary provides investors with information about a firm’s applicable legal standard of conduct, among other things.

<sup>32</sup> Proposed Exemption § II(b)(1).

<sup>33</sup> 17 C.F.R. §§ 240.17a-14; 275.204a-5.

<sup>34</sup> 84 Fed. Reg. 33492, 33526.

conflicts arising from proprietary products, third-party payments, revenue sharing, and principal trading are also required to be included to the extent applicable.<sup>35</sup>

To supplement Form CRS, Reg BI requires that broker-dealers disclose, prior to or at the time of a recommended transaction, all material facts relating to (i) the scope and terms of the relationship; and (ii) conflicts of interest associated with the recommendation.<sup>36</sup> Additionally, broker-dealers must establish, maintain, and enforce policies and procedures reasonably designed to, among other things, (i) identify and, at a minimum, disclose, conflicts of interest associated with the recommendation, and (ii) identify and disclose any material limitations placed on the securities or investment strategies that may be recommended to a retail customer (such as proprietary or other limited range of products) and any conflicts of interest associated with such limitations.<sup>37</sup> For registered investment advisers, Form CRS supplements pre-existing requirements to disclose material conflicts of interest and other key information about the investment advisory relationship in Form ADV Part 2A.<sup>38</sup>

Accordingly, registered broker-dealers and investment advisers are already subject to comprehensive conflict of interest disclosure requirements that overlap with the requirement in the Proposed Exemption to disclose conflicts of interest. To support the Department's intent to align the Proposed Exemption with other regulations and avoid investor confusion resulting from multiple disclosures, the Department should clarify that compliance with the conflict of interest disclosure requirements applicable to registered broker-dealers and investment advisers would be deemed to satisfy the Proposed Exemption's conflict of interest disclosure requirement.

### **C. The Annual Retrospective Compliance Review and Certification Should Be Eliminated, or at a Minimum Changed to Be Made Workable**

Section II(d) of the Proposed Exemption conditions exemptive relief on Financial Institutions' completion of an annual compliance review. The methodology and results of the review must be memorialized in a written report presented to the Financial Institution's Chief Executive Officer and Chief Compliance Officer, and the Chief Executive Officer must certify within six months of the end of the annual review period:

- review of the report;

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<sup>35</sup> 84 Fed. Reg. 33492, 33533.

<sup>36</sup> 17 C.F.R. §240.15l-1(a)(2)(i).

<sup>37</sup> 17 C.F.R. §240.15l-1(a)(2)(iii). The rule further requires that the broker-dealer's policies and procedures must be reasonably designed to prevent such limitations and associated conflicts of interest from causing the broker-dealer to make recommendations that place its interest ahead of the retail customer's interest, and that the policies and procedures provide for mitigation or elimination of certain conflicts of interest.

<sup>38</sup> SEC, General Instructions For Part 2 of Form ADV, available at <https://www.sec.gov/about/forms/formadv-part2.pdf>.

- that the Financial Institution has in place policies and procedures prudently designed to achieve compliance with the conditions of the exemption; and
- that the Financial Institution has in place a prudent process to modify such policies and procedures as business, regulatory and legislative changes and events dictate, and to test the effectiveness of such policies and procedures on a periodic basis.<sup>39</sup>

Finally, the report, certification, and supporting data must be retained for a period of six years and made available to the Department within 10 business days of request.<sup>40</sup>

These obligations are unworkable for several reasons and should be eliminated from the final exemption. The Department does not provide support for the need for such a retrospective review, other than noting that it is similar to other regulatory requirements for broker-dealers and investment advisers, and claiming that the costs associated with the annual retrospective review and report “would likely be low.”<sup>41</sup> We disagree with the Department’s cost estimates and believe that current penalties for noncompliance and the existing enforcement authority of the Department and IRS will be sufficient. If the Department does not remove the annual retrospective review condition, we recommend the following changes in the final exemption to make the condition more administratively workable.

First, the requirement that a Financial Institution’s Chief Executive Officer provide the certification is unrealistic, overly burdensome and unnecessary to achieve the desired result. A Chief Executive Officer’s responsibilities are too varied, and the time necessary to assess the Financial Institution’s compliance mechanisms would be too great for the Chief Executive Officer to be able to provide the certifications. Requiring an executive without a realistic ability to make the certifications based on personal knowledge would potentially cause the certifications to merely become a check-the-box exercise. Instead, the certifications should be supplied by an appropriate compliance professional with oversight of the Financial Institution’s sales practices and policies and procedures. We respectfully request that the Department revise the condition so that the Financial Institution’s Chief Compliance Officer, or equivalent position, provides the certifications.<sup>42</sup>

Second, the certifications that must be made regarding the Financial Institution’s compliance policies go beyond the policies and procedures condition of the Proposed Exemption, which makes the Financial Institution’s obligations unclear. The Department could make the requirements consistent

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<sup>39</sup> Proposed Exemption § II(d)(2)–(4).

<sup>40</sup> Proposed Exemption § II(d)(5).

<sup>41</sup> 85 Fed. Reg. 40834, 40855.

<sup>42</sup> Rule 206(4)-7 under the Investment Advisers Act of 1940, which the Department cites in footnote 71 of the preamble, requires that an adviser’s Chief Compliance Officer be responsible for administering the firm’s compliance policies and procedures.

and more certain by making the following change to Section II(d)(3)(B) and deleting as superfluous subsection (C):

(B) The Financial Institution has in place policies and procedures *reasonably designed to comply with Section II(c)*. ~~prudently designed to achieve compliance with the conditions of this exemption; and~~

~~(C) The Financial Institution has in place a prudent process to modify such policies and procedures as business, regulatory and legislative changes and events dictate, and to test the effectiveness of such policies and procedures on a periodic basis, the timing and extent of which is reasonably designed to ensure continuing compliance with the conditions of this exemption.~~

Third, the Department should remove the requirement that the report, certification, and supporting data be provided to the Department within 10 business days of a request. The requirement to quickly turn over documents is unnecessary because the Department already has well-established enforcement mechanisms that allow it to obtain documents from Financial Institutions through voluntary requests and subpoenas.<sup>43</sup>

If the Department does not remove the requirement to provide the materials in an expedited manner, then we would request that the Department clarify that Financial Institutions will not lose the exemption should they fail to meet the deadline, provided a good faith effort is made to provide the materials to the Department. For example, Financial Institutions would have real difficulty meeting the 10-business day deadline if the Department does not provide the request to an employee of the Financial Institution who is aware of the Proposed Exemption or who has the authority to direct that the materials be released to the Department. Financial Institutions who require more time because they must direct the request to the appropriate employee should not be penalized.

#### **D. The Eligibility Section Should Be Eliminated in Favor of the Department's Existing Enforcement Mechanisms**

Under Section III, Financial Institutions and Investment Professionals may lose eligibility to rely on the Proposed Exemption for a 10-year period upon the occurrence of a conviction of a crime described in section 411 of ERISA or a finding by the Department's Office of Exemption Determinations that the Financial Institution or Investment Professional has:

- engaged in a systematic pattern or practice of violating the conditions of the exemption in connection with otherwise non-exempt prohibited transactions;

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<sup>43</sup> See ERISA § 504.

- intentionally violated the conditions of the exemption in connection with otherwise non-exempt prohibited transactions; or
- provided materially misleading information to the Department.<sup>44</sup>

With respect to the Office of Exemption Determinations' findings, the Proposed Exemption provides that the Department would provide a written warning and one in-person conference prior to declaring a Financial Institution or Investment Professional to be ineligible.<sup>45</sup>

We respectfully request that the Department remove Section III from the final exemption in its entirety, or at a minimum, remove the ability of the Office of Exemption Determinations to find Financial Institutions and Investment Professionals ineligible. The Department provides no evidence supporting the need for the eligibility section. Indeed, the Department already has the ability to limit use of prohibited transaction exemptions through its well-established enforcement mechanisms. In this respect, the Department has the ability under ERISA to enter into settlement agreements with Financial Institutions and Investment Professionals providing services to ERISA plans requiring them to structure their advice programs in reliance on other exemptions (or to not engage in prohibited transactions), or pursue judgments or consent decrees requiring them to do so.<sup>46</sup> The provisions allowing the Department to find Financial Institutions and Investment Professionals ineligible through an informal procedure appears to be an attempt to bypass ERISA by providing the Department with a new enforcement mechanism not found in the statute. Moreover, to the extent the Department would find Financial Institutions and Investment Professionals ineligible based on advice provided to IRAs, the Department would be exceeding its statutory enforcement jurisdiction.<sup>47</sup>

In order to comply with the Proposed Exemption, Financial Institutions would expend significant sums building new compliance systems and complying with the exemption on an on-going basis.<sup>48</sup> Moreover, Financial Institutions may expend significant time and resources designing new advisory programs that rely on the Proposed Exemption as the sole means of prohibited transaction exemptive relief for the activities involved in such programs. If the Department can make ineligibility determinations through an informal and uncertain process, however, Financial Institutions may determine the risks of creating such advisory programs outweigh the benefits.

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<sup>44</sup> Proposed Exemption § III(a)(2).

<sup>45</sup> Proposed Exemption § III(c)(2).

<sup>46</sup> ERISA § 504.

<sup>47</sup> 885 F.3d at 364.

<sup>48</sup> The Department acknowledges some of these costs in the regulatory impact analysis included in the preamble to the Proposed Exemption. 85 Fed. Reg. 40834, 40851-61.

The Department's finding, which would deprive Financial Institutions and Investment Professionals of the exemption, would also implicate due process requirements.<sup>49</sup> Due process requires that decisions be made in an impartial, unbiased manner. We are concerned that the Office of Exemption Determinations, however, cannot fulfill this role in an impartial manner because of its deep involvement in creating the Proposed Exemption. By way of illustration, the concept of separation of powers requires separate branches of government to make laws, implement such laws, and adjudicate compliance with such laws. Contrary to this principle, the Proposed Exemption's eligibility provision would inappropriately place staff of the Office of Exemption Determinations in all three of these roles:

- Legislative—in terms of drafting the Proposed Exemption;
- Executive—to the extent they investigate whether Financial Institutions and Investment Professionals have complied with the Proposed Exemption;<sup>50</sup> and
- Judicial—finding Financial Institutions and Investment Professionals to be ineligible.

Additionally, due process would require that the Department's findings not be arbitrary.<sup>51</sup> The Proposed Exemption, however, does not obligate the Office of Exemption Determinations to follow any policies or procedures that would ensure consistency in making decisions. And the Office of Exemption Determinations has demonstrated in the past that it will not adopt such policies and procedures if it is not required to do so.<sup>52</sup>

#### **E. The Proposed Exemption Should Cover Robo-Advice**

The Proposed Exemption does not apply to robo-advice, which is defined as investment advice generated solely by an interactive website in which computer software-based models or applications provide investment advice based on personal information each investor supplies through the website, without any personal interaction or advice with an Investment Professional.<sup>53</sup> We believe covering robo-advice under the scope of the exemption would help Retirement Investors, and the Department therefore should reconsider this exclusion. Personalized investment advice compliant with the Impartial Conduct Standards and other conditions of the Proposed Exemption could be provided through robo-advice programs. Although the Department points to the statutory investment advice exemption added to ERISA by the Pension Protection Act of 2006 as available to cover robo-advice, the availability of an alternate exemption does not mean the Proposed Exemption should not cover robo-

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<sup>49</sup> *Cleveland Bd. of Educ. v. Loudermill*, 470 U.S. 532, 541 (1985); *Mathews v. Eldridge*, 424 U.S. 319, 334 (1976).

<sup>50</sup> The Proposed Exemption does not make clear how the Office of Exemption Determinations would develop information leading to its findings.

<sup>51</sup> *Clark County, Nev. v. F.A.A.*, 522 F.3d 437, 441 (D.C. Cir. 2008).

<sup>52</sup> Individual Retirement Accounts, Formalizing Labor's and IRS's Collaborative Efforts Could Strengthen Oversight of Prohibited Transactions, GAO-19-495 (June 2019), available at <https://www.gao.gov/assets/700/699575.pdf>.

<sup>53</sup> Proposed Exemption § I(c)(2).

advice. For example, a number of the transactions the Proposed Exemption would cover, including recommendations of mutual funds and annuities, are already covered by other prohibited transaction exemptions.<sup>54</sup> The Department should apply the same rationale and remove the exclusion applicable to robo-advice.

#### **F. Only the Department and IRS Should Have Access to Records Related to the Advice**

As currently drafted, Section IV of the Proposed Exemption requires that Financial Institutions make records pertaining to compliance with the Proposed Exemption available not only to the Department, but also to plan participants, beneficiaries, and IRA owners that engaged in an investment transaction pursuant to the exemption, fiduciaries to a plan that engaged in an investment transaction pursuant to the exemption, and any contributing employer or employee organization whose members are covered by a plan that engaged in an investment transaction pursuant to the exemption. We respectfully request that the Department narrow the availability of compliance records under the Proposed Exemption to cover only authorized employees of the Department or IRS (as applicable).

The Department has authority to enforce and oversee compliance with the terms of the exemption, at least with respect to ERISA-covered plans. Extending availability of compliance records to employers, unions, and, in particular, participants, beneficiaries and IRA owners and their authorized representatives (plaintiff's lawyers), raises the risk of unnecessary litigation. In addition, it would appear to grant plan sponsors (or contributing employers with respect to a multiple employer plan) access to records of a Financial Institution's recommendations to individual participants. We do not believe the Department intended for such a result. Given the Department's indication that it does not intend to create a private right of action as between a Financial Institution or Investment Professional and a Retirement Investor,<sup>55</sup> limiting access to the appropriate regulator should be sufficient.

Finally, we note that the Department should not be permitted to request documents regarding advice or recommendations pertaining to IRAs, as such ability is outside of its regulatory jurisdiction. By attempting to extend its enforcement authority to the IRA space—authority conferred to and generally reserved exclusively to the IRS—the Department runs the risk that the Proposed Exemption would succumb to the same legal roadblocks discussed in the Fifth Circuit Decision that necessitated vacatur of the Best Interest Contract Exemption. The Department could resolve this issue simply by revising the Proposed Exemption to exclusively grant the IRS, rather than the Department, access to documents regarding advice or recommendations pertaining to IRAs.<sup>56</sup>

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<sup>54</sup> PTE 77-4; PTE 84-24.

<sup>55</sup> 85 Fed. Reg. 40834, 40844.

<sup>56</sup> Final Best Interest Contract Exemption, 81 Fed. Reg. 21002, 21081 (Apr. 8, 2016).

**G. The Department Should Revise the Proposed Exemption’s Independence Requirement and Clarify Its Application for Pooled Employer Plans**

The Proposed Exemption, in its current form, would exclude transactions involving ERISA Plans where the Financial Institution or any affiliate is a named fiduciary or plan administrator, unless selected to provide advice by a fiduciary who is independent.<sup>57</sup> In determining whether an independent fiduciary is in fact “independent,” the Department subscribes to, among other conditions, a two percent revenue test—a percentage threshold markedly lower than the Department’s definitions of “independence” in other contexts.<sup>58</sup> Additionally, this condition raises questions concerning the independence requirement in the context of a Pooled Employer Plan, where a Financial Institution or its affiliate would serve as the Pooled Plan Provider, meaning it would be a named fiduciary and administrator with respect to the Plan.<sup>59</sup> We respectfully request that the Department raise the independence threshold to five percent and revise the Proposed Exemption to clearly permit advice in connection with Pooled Employer Plans.

**H. The Requirement That Policies and Procedures Be “Prudently Designed” Is Unnecessary and Inconsistent with Other Regulatory Conduct Standards**

The current text of the Proposed Exemption would require that Financial Institutions create policies and procedures “prudently designed” to comply with the Impartial Conduct Standards of the Proposed Exemption.<sup>60</sup> As it is the Department’s intent, as expressed in the preamble, to create standards that align with other regulatory conduct standards, we respectfully request that the Proposed Exemption’s policies and procedures requirement be revised to “reasonably designed” so that the text is in accord with the text of Reg BI.<sup>61</sup> Broker-dealers must have policies and procedures “reasonably designed” to comply with Reg BI, which recently became effective. It is unclear what the difference between “prudently” and “reasonably” designing policies and procedures would entail.

**I. The Requirement to Correct Prohibited Transactions Does Not Create a Fiduciary Duty Owed to IRAs**

We are concerned that in the preamble to the Proposed Exemption, the Department seems to suggest that the requirement that prohibited transactions be corrected may mean that affirmative duties are

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<sup>57</sup> Proposed Exemption § I(c)(1).

<sup>58</sup> See, e.g., DOL Adv. Op. 2001-09A (Dec. 14, 2001), wherein the Department applied a five percent independence threshold.

<sup>59</sup> See ERISA § 3(44)(A)(i), added by section 101 of the SECURE Act.

<sup>60</sup> Proposed Exemption § II(c)(1).

<sup>61</sup> 17 C.F.R. § 240.15l-1(a)(2)(iii).



owed to IRAs.<sup>62</sup> But the Fifth Circuit Decision makes clear that Congress did not intend to impose fiduciary duties with respect to IRAs.<sup>63</sup> The Department should clarify in the preamble to the final exemption that this is not the correct reading of its preamble statement and that it does not intend to disagree with the Fifth Circuit Decision.

**J. A Requirement to Monitor Accounts for Certain Investments is Unnecessary and Could Have Negative Market Consequences**

In the preamble to the Proposed Exemption, the Department expresses doubt that certain investments can be recommended to a Retirement Investor in a manner consistent with the Best Interest Standard absent monitoring of the investment on an ongoing basis.<sup>64</sup> This statement appears to be at odds with the Department's prudence regulation, which does not contain such a monitoring requirement.<sup>65</sup> When issuing the prudence regulation in 1979, the Department made clear that it was not intending to establish certain classes of investments as prudent or not prudent for plans.<sup>66</sup> To impose an account monitoring requirement, however, would prevent certain Financial Institutions that do not offer account monitoring from recommending certain classes of investments to plans and IRAs.

Further, Reg BI does not impose an account monitoring obligation upon broker-dealers.<sup>67</sup> In fact, the SEC has stated that continuous account monitoring is an activity that may cause a broker-dealer to be deemed to be providing investment advice that is not solely incidental to its brokerage business, requiring the broker-dealer to register as an investment adviser.<sup>68</sup> Thus, the Department imposing an account monitoring requirement on broker-dealers could cause them to change their business models to become investment advisers. The Department's statement therefore upsets the careful line the SEC drew between the activities of broker-dealers and registered investment advisers within the SEC's 2019 rulemakings. Accordingly, we respectfully request that the Department clarify that the Proposed Exemption does not impose an account monitoring requirement.

**K. The Department Should Expand the Definition of Covered Principal Transaction**

The Proposed Exemption provides only limited relief for non-riskless principal transactions. With respect to purchases by a plan or IRA, the definition of Covered Principal Transaction is limited to

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<sup>62</sup> 85 Fed. Reg. 40834, 40842 n. 50.

<sup>63</sup> 885 F.3d at 381.

<sup>64</sup> 85 Fed. Reg. 40834, 40843.

<sup>65</sup> See 29 C.F.R. § 2550.404a-1.

<sup>66</sup> Preamble to ERISA Section 404 Regulation, 44 Fed. Reg. 37221, 37225 (June 26, 1979).

<sup>67</sup> 84 Fed. Reg. 33318, 33321.

<sup>68</sup> 84 Fed. Reg. 33681, 33687.

certain listed transactions, primarily involving debt securities, CDs, and unit investment trusts. According to the preamble, the Department seeks comment on all aspects of the Proposed Exemption's treatment of principal transactions.

As an initial matter, we note that the Proposed Exemption's very limited relief for non-riskless principal transactions is inconsistent with the treatment of principal transactions under SEC rules. More specifically, under Reg BI, the SEC does not prohibit principal transactions; rather, Reg BI addresses conflicts raised by these transactions through the rule's disclosure and conflict of interest provisions.<sup>69</sup> The Proposed Exemption's approach of permitting only those principal transactions involving a specified set of investments is unnecessary as it ignores the important safeguards provided under securities law with respect to principal transactions. It also effectively conflicts with ERISA's prescription against the creation of "legal lists" of permissible investments.<sup>70</sup> As explained above, the Department has traditionally avoided establishing certain classes of investments as prudent or not prudent for plans.<sup>71</sup>

At a minimum, we urge the Department to expand the definition of Covered Principal Transaction to include sales to a plan or IRA of closed-end fund (CEF) shares during the initial public offering (IPO). Like an open-end mutual fund, a CEF is a pooled investment vehicle that offers shares almost exclusively through a public offering registered under the Securities Act of 1933, with applicable fees, expenses, and offering costs fully disclosed in an initial prospectus. CEFs differ from open-end mutual funds in that they are generally not offered continuously and typically have a fixed number of shares issued during the IPO. Notably, CEFs generally do not issue redeemable shares; after the IPO, investors buy and sell shares on the secondary market at prices established through market trading. The exchange and market participants provide investors with price transparency and liquidity throughout the trading day. Because a closed-end fund does not need to maintain cash reserves or sell securities to meet redemptions, the fund has the flexibility to invest in less-liquid portfolio securities.

Both at the time of the CEF IPO, and throughout the life of the CEF, the valuation of a CEF's portfolio is subject to important investor protections under the Investment Company Act of 1940, including board-approved valuation procedures and ongoing board oversight. Similar to open-end funds, a per share net asset value is generally determined and published on each business day, which enables investors to consider the underlying value of a fund's net assets per share compared to the share

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<sup>69</sup> The SEC explains, in the preamble to Reg BI, that the rule does not prohibit a broker-dealer from making recommendations where conflicts of interest are present, including recommending a security underwritten by the broker-dealer or a broker-dealer affiliate, including initial public offerings, and recommending a transaction to be executed in a principal capacity. The broker-dealer must, however, ensure that its interests are not placed ahead of the investor's interest by satisfying Reg BI's requirements. 84 Fed. Reg. 33318, 33334.

<sup>70</sup> Congress explained that it did not intend for ERISA to contain a legal list of investments. S. Rep. No. 93-383, 1974 U.S.C.C.A.N. 4889, 4984 (Aug. 21, 1973).

<sup>71</sup> Preamble to ERISA Section 404 Regulation, 44 Fed. Reg. 37221, 37225.

price trading on an exchange following the IPO. For these reasons, CEFs do not present the type of price transparency, liquidity, and conflicted incentive concerns noted by the Department for securities typically traded in principal transactions.<sup>72</sup>

CEFs offer an important choice for long-term investors in IRAs and tax-deferred accounts—they offer investors access to less-liquid investments, they may use leverage as part of their investment strategy to seek higher returns (but with higher risk), and many seek to provide regular distributions to shareholders. Because these funds are offered at inception as principal transactions, restricting their availability could hurt investors—both retirement and other investors—in ways that cannot be remedied simply by allowing plans and IRAs to purchase these funds in the secondary market. We therefore urge the Department to modify the Covered Principal Transaction definition so IRA owners and other savers in retirement accounts can have the opportunity to participate in CEF IPOs.

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We appreciate the Department’s consideration of the above comments. Please feel free to contact Susan Olson (202-326-5813 or [solson@ici.org](mailto:solson@ici.org)), David Abbey (202-326-5920 or [david.abbey@ici.org](mailto:david.abbey@ici.org)), or Elena Chism (202-326-5821 or [elena.chism@ici.org](mailto:elena.chism@ici.org)) with any questions.

Sincerely,

/s/ Susan Olson

/s/ David Abbey

Susan Olson  
General Counsel

David Abbey  
Deputy General Counsel – Retirement Policy

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<sup>72</sup> 85 Fed. Reg. 40834, 40840. To the extent that the Department has concerns about the risk of underwriters “dumping” shares on investors during the IPO process, we believe the concern is not relevant here given differences in the IPO process for CEFs as compared to operating companies. In a typical operating company equity IPO, the issuer consults with its underwriters and sets a specific capital target the offering must raise at a valuation determined by a negotiation between the issuer and the underwriters. That capital goal is prominently featured on the front of the offering’s preliminary prospectus. In contrast, the assets raised in a CEF IPO depend solely upon investor demand discerned during the initial offering period, not a pre-determined capital goal. In addition, no valuation concerns are present as the CEF holds only cash proceeds immediately following the offering that are then promptly invested in a pool of securities in accordance with the fund’s investment mandate. For the CEF IPO, the underwriting syndicate members are committing only to the shares needed to fill their clients’ indications of interest—rather than issuer and syndicate goals. Beyond that, the underwriters hold little or no additional inventory. Additionally, for CEF IPOs, pricing is known at the outset and high transparency and liquidity opportunities continue after launch.