SIFMA

Securities Industry and Financial Markets Association

February 12, 2008

The Office of Regulations and Interpretations
Employee Benefits Security Administration
Attn: 408(b)(2) Amendment
Room N-5655
U.S. Department of Labor,
200 Constitution Avenue, N.W.
Washington, DE 20210

Re: Section 408(b)(2) Amendment: Reasonable Contract or Arrangement Under Section 408(b)(2) – Fee Disclosure

Ladies and Gentlemen:

On behalf of the Securities Industry and Financial Markets Association ("SIFMA")[1], I write to provide comments regarding the Department of Labor's ("Department") proposed regulation under the Employee Retirement Income Security Act of 1974 ("ERISA") that will redefine what constitutes a "reasonable contract or arrangement" for purposes of the statutory exemption in Section 408(b)(2) from certain prohibited transaction provisions of ERISA. SIFMA's comments on the proposed class exemption published contemporaneously with these proposed regulations will be filed separately.

We urge the Department to hold a hearing on this very important proposal. As is clear from all the comments filed with respect to this regulation, it proposes sweeping and significant changes which have confused and disturbed the plan community. A regulation of this magnitude demands a full understanding of the range of issues that it raises, and we urge the Department to promptly schedule a hearing so that senior Department staff has the opportunity to consider the full impact of the proposed regulation on these important issues.

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[1] SIFMA is the product of a recent merger of the Securities Industry Association ("SIA") and the Bond Market Association. SIFMA brings together the shared interests of more than 650 securities firms, banks and asset managers. SIFMA's mission is to promote policies and practices that work to expand and perfect markets, foster the development of new products and services and create efficiencies for member firms, while preserving and enhancing the public's trust and confidence in the markets and the industry. SIFMA works to represent its members' interests locally and globally. It has offices in New York, Washington D.C., and London and its associated firm, the Asia Securities Industry and Financial Markets Association, is based in Hong Kong.

SIFMA and its members appreciate the opportunity to comment on the proposed regulations. While we support the goal of ensuring that plan fiduciaries have the information they need to ensure that compensation received by service providers is reasonable, the proposed regulation does not adequately account for the significant amount of disclosure that is already provided to plan fiduciaries, nor does it facilitate efficiency in delivering services to ERISA plans. We believe that the approach of the current framework – allowing a fiduciary to decide how much disclosure he needs, and how to obtain that disclosure efficiently – should not be discarded in the legitimate effort to raise the consciousness of plan fiduciaries regarding the information that may be relevant to their decisions. Historically, the Department has wisely avoided a "one-size-fits–all" approach when it comes to fiduciary duties (e.g., 29 CFR 2550.404a-1, PTE 84-14, PTE 90-1 and PTE 91-38, all of which rely on the appropriate plan fiduciary, assuming a minimum level of sophistication, to make decisions regarding plan services and transactions without dictating the rules by which he must govern his decision-making). We urge the Department not to abandon this approach.

The preamble to the proposed regulation notes that the Department believes that, in order to satisfy their ERISA obligations, plan fiduciaries need more information to assist them in assessing the compensation to be received by the service provider and potential conflicts of interest that may adversely affect the service provider's performance. Accordingly, the proposed rule will require that in order to be "reasonable" for purposes of qualifying for the Section 408(b)(2) exemption, any contract or arrangement between an employee benefit plan and certain service providers must include or reference certain disclosures by the service provider to assist the plan fiduciary in its evaluation of compensation and conflicts of interest.

Notwithstanding our serious concerns about the breadth and burden of the proposed rule, we think there are aspects of the proposal that should be retained. For example, we are pleased that the Department has taken a practical view on disclosure flexibility, and has concluded that a signed document between a plan fiduciary and the service provider is not required. We, too, have confidence in plan fiduciaries to understand what kind of services require a signed agreement and which do not. We are also pleased that the Department has determined that the excise tax rules should not be changed, and that IRAs and other similar arrangements should not be subject to these rules. We describe our views on all of these issues below. We then recommend areas where, in our view, we believe that the proposed amendments are overbroad and describe why we have concerns in these areas.

I. Practical Application

Disclosure Document

SIFMA applauds the Department's recognition that it would be onerous and expensive to require that all disclosure be in one document provided to each client at a particular time in a specified manner. Permitting service providers to incorporate by reference other documents such as the Form ADV, Statement of Additional Information (SAI), etc. will help decrease the burden and cost of complying with the new regulation. Of course, any additional burden on service providers translates into higher costs for plans and their participants. In addition, the complexity of rules regarding required disclosure may motivate small employers who simply have neither the time nor inclination to absorb and apply these rules to reconsider their plans. So too, employers without plans will be reluctant to take on the obligation of making sure that each necessary disclosure is obtained or risk the chance that the new class exemption will be unavailable. Employees of small businesses are a large part of the “uncovered” universe in terms of savings plans. We respectfully ask the Department to weigh the additional burden on and disincentive to sponsor and maintain plans before it imposes these burdens on plans and on plan sponsors, and especially small employers. We were pleased to see that the proposed rule permits disclosure to be incorporated by reference. We assume that the regulation will also permit substantive provisions to be incorporated by reference (such as whether the service provider is agreeing to act as a fiduciary). We ask the Department to confirm our reading of the proposed rule.

SIFMA would be pleased to work with the Department on any plan fiduciary education website or other seminar that will inform the plans of the importance of the information disclosed in these documents. We strongly believe that the Department’s approach on the disclosure documentation issue is the correct one and we urge the Department to retain that formulation in the final regulation.

Requirement of a Contract or Arrangement

The proposed regulation requires the disclosure of compensation and services to be in writing. There does not appear to be any requirement that the written disclosure be in the form of a “contract” (indeed, the regulation specifically refers to “contract or arrangement”) nor that it be signed by either the plan fiduciary or service provider. We are pleased that the Department has recognized that signed contracts are not typical for many service providers to plans. In many industries, such as securities brokerage, the disclosure that is most meaningful is provided with the trade confirmation. In the brokerage industry, the executing broker provides disclosure in the form of a confirmation after the transaction is effected, containing information about the transaction itself (such as the date, time, identity, price and number of shares involved), about its capacity (i.e. whether it is acting as an agent or a principal); its compensation (for agency trades, compensation includes its commission); the source and amount of any remuneration received or to be received from a third party by the broker in connection with the transaction; whether any odd-lot differential (or equivalent fee) has been paid in connection with the execution of an order; and specified information in the case of any transaction in a debt security. This disclosure is not provided in writing in advance (and it would be entirely impractical to do, since so much of the transaction disclosure depends on facts not known in advance) and it may not always be provided on a plan-by-plan basis to the investment managers that utilize the broker’s services.

Paragraph (c)(1)(ii) requires that every "contract or arrangement" that falls within the scope of the proposed regulation be in writing. We believe the Department understands, and we urge you to specifically confirm, that the regulation will not require a broker to provide particularized disclosure with respect to each plan managed by an investment manager in advance of the effective date. Such a requirement would be problematic for investment managers that have been in existence for a long time and typically do not have written agreements with their brokers – the arrangement is established by virtue of the broker providing services to the investment manager. It will be exceptionally burdensome for these managers to set out in writing every contract or arrangement they have entered into that falls within the scope of the proposed regulation.

We urge the Department to permit current disclosure and agreement practices in the securities brokerage industry to continue, without the costly and burdensome requirements imposed by the proposed rule. Operationally, most of our members have systems through which disclosures are mailed centrally from the home office automatically upon account opening or sent after trade execution. One of the benefits of this centralization is that the home office controls the delivery of the disclosures to ensure consistent compliance with the delivery requirements under securities laws.

We hope the Department will clarify that for brokerage services, providing a written disclosure document in advance will not be required for a number of additional reasons: all of the services which may be provided to a particular client may not be known in advance of the relationship, all of the relationships that may apply to a particular plan relationship with a service provider cannot be known in advance of the relationship, since the conflicts will change over time depending upon the services the clients select and the client's investment decisions; and every form and amount of compensation will be impossible to determine in advance of the relationship as these too are dependent upon the services and investments the plan selects over time.

As the Department is aware, obtaining client signatures after a relationship has commenced is difficult and expensive. The Department has recognized this fact in the numerous exemptions that it has granted which permit deemed consent where a client receives information and can object and, if he does not, is deemed to have consented. See, for example, PTE 86-128, PTE 2000-25, PTE 2007-1. With respect to the hundreds of thousands of service arrangements currently in place, the notion that without a signature, the services constitute a prohibited transaction will throw plan financial affairs into chaos.

Consider for example the mailing service that mails statements and plan communications on behalf of the recordkeeper to all plan participants. If the plan refuses to sign the contract with the mailing service, it most assuredly will cease providing the service, if to do so in the absence of a signed agreement will require reimbursement of all fees and even the payment of an excise tax. Thus plan participants will not receive these essential mailings. Similarly, assume that a broker dealer who merely executes trades discloses the fact that it is not acting as a fiduciary. The responsible plan fiduciary refuses to sign the arrangement, choosing not to give up a possible position of leverage. So the broker refuses to execute trades. Or take a subcustodian to a prime broker, who is a foreign bank with no U.S. presence, who refuses to provide any disclosure or to sign any agreement; must the investment manager be advised that he may no longer buy and sell securities in the market of that local subcustodian? In light of these examples and thousands more, we urge the Department not to require signed agreements.

Amendment to 4975 of Internal Revenue Code

The proposed regulation did not include an amendment to the regulations under the Code. We assume that the Department has determined that the rules governing the payment of excise taxes should remain unchanged. We strongly support that view, and urge the Department to finalize the regulation with no change to this determination. SIFMA endorses the goal of the proposal – to require fiduciaries to obtain and consider all relevant fee and conflict information before engaging service providers—but appreciates that service providers should not be penalized through excise taxes if the fiduciary fails to do so. We think the regulation strikes a careful balance between a fiduciary's obligation to obtain, and a service provider's obligation to provide, critical information without placing confiscatory tax burdens on either.

In addition, we applaud the Department's decision not to apply the proposed amendment to IRAs and other Section 4975-only plans. We think it is entirely clear that the new requirements do not apply to any "plan" within the meaning of Section 4975(e) other than plans covered under Title I of ERISA. As the Department recognizes, the cost of complying with these new rules for IRAs and other "4975 only" arrangements would be enormous. Thus, we urge the Department to reiterate and clarify that the rules for determining excise taxes remain unchanged, both for plans covered by ERISA and plans covered by Section 4975 of the Code.

II. Areas of Concern

Effective Date

Regardless of the changes between the proposed regulation and the final rule, we are sure that the Department appreciates that a wide range of service contracts with ERISA-governed plans will be affected. Under the proposed revisions, the changes will become effective 90 days after publication of the final regulation, which is a very short time frame to bring a very broad range of contracts into compliance. It will be impossible, especially in light of the potentially extensive clarification required in the final rule, for service providers to evaluate and revise their existing and prospective service contracts and arrangements, and implement entirely new systems and procedures to track the disclosures required by the proposed rule. To ensure that service providers have sufficient lead time and resources to develop, test and implement procedures and systems that can achieve accurate and thorough compliance with changes to the proposed rule, we strongly urge the Department to postpone the effective date of any such changes.

For the securities industry alone, the disclosure required by the proposed regulation goes far beyond any disclosure requirement currently in existence, particularly in the institutional brokerage market. Even if no signed, written disclosure is required by the final rule, the disclosure required will take months to produce and disseminate. SIFMA requests that the effective date of any changes to the regulations under Section 408(b)(2) of ERISA be delayed at least eighteen months from the final publication date, so that service providers can properly digest clarifications the Department makes and prepare for the implementation of the final rule. Ninety days is simply not an adequate amount of time to draft, review, vet for legal compliance, and circulate even the most straightforward disclosure. Where the consequences for failure are so high, and the amount of disclosure so voluminous, in the context of financial institutions that are in so many different lines of business, all of which could require significant conflict disclosure, it is impossibly burdensome to provide only a few weeks to fully comply with the new rule. We think this very short effective date period is particularly troublesome when, with respect to the Form 5500, the Department so appropriately recognized that compliance with these rules would take over a year and provided nearly 14 months as a transition period.

SIFMA proposes that the final regulations should not be made effective any earlier than eighteen months after their publication of the final rule in the Federal Register. Furthermore, existing relationships should be grandfathered. While we understand the Department's concern over the potential to abuse a grandfather provision, many arrangements span several years or have no specific term (for example, those terminable on thirty days notice). Rather than providing no relief, we urge the Department to adopt a grandfather rule for arrangements already in existence until they are formally extended, renewed or materially modified.

When Congress enacted ERISA, it provided a transition period of two and a half years to bring service contracts into compliance with the Act (see Section 414(c)(4)). We believe that the scope of necessary changes required by the proposed rule is at least as extensive, if not more extensive, then when Section 408(b)(2) was enacted. As noted earlier, revising documentation for all agreements will take years. Revising all existing documentation for each existing client in the short term is just not manageable. Contrary to the estimates in the economic analysis accompanying the proposed regulation, the requirement that service providers must redocument the arrangements of each and every client of every service provider, after having revised all existing documentation but needing to ensure that each client understands and is comfortable with the disclosure, will take weeks for each client. Asset managers with hundreds of plan clients and brokers with tens of thousands of plan clients will be overwhelmed with the task before them. The impact on plan sponsors should not be ignored. Each plan may have a dozen or more service providers; the burden and cost on those plans, and the disruptions to their businesses, of being inundated in a relatively short time, with new and potentially confusing documentation may prove to be very significant. We have no doubt that the Department wants this communication to be careful and thorough. With that in mind, we urge the Department to give service providers the time to do it correctly.

Regulation under Section 404

The primary purpose of the regulation appears to be to protect plans from imprudent fiduciary decision-making in the hiring and monitoring of service providers. We believe that ERISA already provides such protection. Section 404(a)(1)(B) requires a plan fiduciary to act prudently—i.e., to consider all relevant facts—in hiring a service provider. If the fiduciary fails to do so and the plan is harmed, the fiduciary is liable to the plan for any damages under Section 409(a). In the past, the Department has defined the disclosure necessary for a plan fiduciary to make a prudent decision under Section 404. Additionally, by mandating specific disclosures, the regulation creates a new or implicit baseline of prudence for the engagement of service providers, depriving fiduciaries of their traditional discretion to expend limited resources only on information that is relevant and appropriate. This position is contrary to Section 404(a)(1)(B), which establishes prudence as a relative concept, driven by the facts and circumstances at hand. We respectfully suggest that the Department consider issuing its fee and disclosure guidance under Section 404(a)(1)(B), rather than changing the requirements of Section 408(b)(2) for all service providers.

Fiduciaries Under the Advisers Act

The proposal applies to three categories of services providers. The first category includes "service providers who provide services as a fiduciary under ERISA or under the Investment Advisers Act of 1940 ("Advisers Act")."[2] It is unclear what service providers the Department intends to capture by referencing fiduciaries under the Advisers Act.[3] However, we think this reference is overbroad, and will sweep in individuals who, under the long-established definition of fiduciary under ERISA, are simply not fiduciaries under this statute. Additionally, we think the formulation chosen by the Department

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[2] 72 Fed. Reg. at 70989 and 70991 (December 13, 2007) ("Subsection (B) of paragraph (c)(1)(iii) requires that the service provider identify whether it will provide services to the plan as a fiduciary, either as an ERISA fiduciary under section 3(21) of ERISA or as a fiduciary under the Investment Advisers Act of 1940.")

[3] It may be that the Department is intending, through this language, to suggest that an adviser to a mutual fund, because it is an adviser under the Advisers Act, is a service provider to an ERISA plan that purchases a share of that mutual fund. As noted elsewhere in these comments, we strongly disagree with the notion that an adviser to a vehicle which does not hold plan assets is subject to section 406 of ERISA and requires the relief provided under section 408(b)(2). If the Department believes that this language will require mutual fund advisers to enter into service arrangements with ERISA plans that meet the disclosure requirements of the proposed rule, we disagree with that conclusion and suggest it has no legal basis under ERISA or the Department's own regulations.

ignores the statute and the Department's own regulation on entities that do not hold plan assets.

Breadth of the Term

We are concerned that this language effectively amends 29 CFR 2510.3-21 to include, in the definition of fiduciary under ERISA, any individual who is a fiduciary under the Advisers Act. This departure from settled law will confuse plan fiduciaries and service providers alike, and will distort the definition of fiduciary far beyond the limits that Congress contemplated. We do not disagree that investment advisers have fiduciary duties under the Advisers Act. Although the word "fiduciary" does not appear in the Advisers Act, the Supreme Court in *S.E.C. v. Capital Gains Research Bureau,*[4] held that Section 206 of the Advisers Act imposes fiduciary duties on investment advisers. However, the definition of adviser in the Advisers Act is far broader than the definition of fiduciary under ERISA.

Section 202(11) of the Advisers Act defines investment adviser as "any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities […]." [5] It is clear on its face that Advisers Act Section 202(11) takes in a far broader range of individuals than does ERISA Section 3(21). Any person captured by the Advisers Act definition is a fiduciary under the Advisers Act, whereas under ERISA, that person would not be a fiduciary to any particular plan in the absence of some mutual understanding that the plan was intending to rely on the investment adviser's advice as a primary basis for its investment decisions. The Department's language would sweep in service providers who

[4] *S.E.C. v. Capital Gains Research Bureau*, 375 U.S. 180, 192 (1963) (holding that the Advisers Act "reflects a congressional recognition of the delicate fiduciary nature of an investment advisory relationship, as well as a congressional intent to eliminate, or at least to expose, all conflicts of interest which might incline an investment adviser - consciously or unconsciously - to render advice which was not disinterested.")

[5] The Act generally excludes from the definition the following entities: i) a bank, or any bank holding company; ii) any lawyer, accountant, engineer, or teacher whose performance of such services is solely incidental to the practice of his profession; iii) any broker or dealer whose performance of such services is solely incidental to the conduct of his business as a broker or dealer and who receives no special compensation therefore; iv) the publisher of any bona fide newspaper, news magazine or business or financial publication of general and regular circulation; v) any person whose advice, analyses, or reports relate to no securities other than securities which are direct obligations of the United States; or vi) such other persons not within the intent of this paragraph, as the Commission may designate by rules and regulations or order.

would never be deemed fiduciaries under ERISA.[6] Any person who engages in a business with the elements of the definition of "investment adviser" in Section 202(11) of the Advisers Act is a fiduciary under the Advisers Act. We respectfully disagree that an individual who may be a fiduciary under the Adviser's Act but who is not a fiduciary under ERISA should be required to identify himself as a fiduciary in order to take advantage of ERISA Section 408(b)(2).

There are scenarios in which a specific service provider may be subject to fiduciary standards in the Advisers Act under one set of circumstances, but not under another by virtue of the types of services the adviser is providing. For example, a dual registrant – a registered broker dealer who is also registered as an investment adviser under the Advisers Act – may act exclusively as a broker for a plan and therefore not be governed by the Advisers Act in the performance of those duties. This language is particularly problematic when considered in connection with the requirement that all arrangements between fiduciaries and plans specifically recite whether the service provider is a fiduciary. As the Department surely understands, the determination that an individual is a fiduciary under ERISA depends on whether he meets the statutory requirements for discretionary management and control, or the provision of investment advice for a fee on a regular basis where both parties mutually understand that the advice is intended as a primary basis for the plan fiduciary's decisions. That, as described above, is decidedly not the definition of fiduciary under the Advisers Act. We urge the Department to delete this troubling reference to a statute outside its jurisdiction.

Non-Plan Asset Vehicles

In addition, the reference to fiduciary under the Advisers Act suggests that even investment advisers who are not subject to fiduciary requirements under ERISA will be required to make the proposed disclosures. For example, we question whether the Department, under certain circumstances, intends to circumvent the plan asset rule by treating persons with investment management authority over assets that are not "plan

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[6] The scope of the Advisers Act is quite different from ERISA's. Section 206 of the Advisers Act prohibits misstatements or misleading omissions of material facts and other fraudulent acts and practices in connection with the conduct of an investment advisory business. Since the Court's decision in *S.E.C. v. Capital Gains Research Bureau*, 375 U.S. 180 (1963), the SEC has confirmed that an investment adviser has fiduciary duty obligations in several Advisers Act Releases. See e.g., *In the Matter of Michael L. Smirlock*, Investment Advisers Act Release No. 1393 (November 29, 1993) (referencing *S.E.C. v. Capital Gains Research Bureau*, the SEC stated that the Advisers Act "imposes on investment advisers an affirmative duty to their clients of utmost good faith, full and fair disclosure of all material facts, and an obligation to employ reasonable care to avoid misleading their clients."). Section 206 applies to all firms and persons meeting the Advisers Act definition of investment adviser whether registered with the SEC, a state securities authority, or not at all. *See Prohibition of Fraud by Advisers to Certain Pooled Investment Vehicles*, Investment Advisers Act Release No. 2628 (August 3, 2007) http://www.sec.gov/rules/final/2007/ia-2628.pdf; *See also, General Information on the Regulation of Investment Advisers* (May 10, 2005) *http://www.sec.gov/divisions/investment/iaregulation/memoia.htm*.

assets" like ERISA fiduciaries, even though they are not.[7] Specifically, a fund or vehicle without plan assets managed by an investment manager providing investment advisory services to a fund or vehicle does not have a contract or arrangement with the plan and will not be compensated directly by the plan. We believe that the Department could not intend to ignore its own plan asset regulations in suggesting that the performance and management fees a manager of a non-plan asset vehicle receives may be considered indirect compensation paid by a third party (the fund or vehicle) under the proposed rule and somehow subject to Section 408(b)(2).[8] However, our concern is heightened because of the reference to the receipt of fees in connection with the services provided "**or the financial products in which plan assets are invested".** Despite the fact that there has been much debate about the meaning of these words, we have concluded that they can only do mischief. A person providing services to an entity that is not a plan and that does not "hold plan assets" under the Department's regulations is not a service provider under ERISA solely on account of those services. Such a person neither needs relief from the prohibited transaction provisions of ERISA nor the protection of this regulation.

ERISA, as the Supreme Court has noted, is a "comprehensive and reticulated statute".[9] Congress intended that parties in interest to plans would be able to identify themselves by reference to a clear list of persons described in Section 3(14). While Congress intended the definition of fiduciary to be a functional test, it did not intend that a broker dealer selling securities owned by a mutual fund be considered a party in interest under ERISA by means of being a service provider to a plan, simply because a plan owned a publicly traded share of that mutual fund. Such a rule would be impossible to comply with, largely because a broker has no access to the identity of shareholders of the mutual fund. Indeed, the statute clearly authorizes a mutual fund to represent that when a broker deals with the mutual fund, it is not dealing with plan assets.[10] Similarly, the mutual fund itself does not necessarily know whether its shares are held by plans, especially where the purchases are made through omnibus accounts.

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[7] See, e.g., ERISA section 3(21)(B) which states, in pertinent part, that "[i]f any money or other property of an employee benefit plan is invested in securities issued by an investment company registered under the Investment Company Act of 1940, such investment **<u>shall not, by itself, cause such investment company or such investment company's investment adviser or principal underwriter to be deemed to be a fiduciary or party in interest as those terms are defined in this title…."</u>** (emphasis added)**;** ERISA section 3(42), which defines the term "plan assets" to state that "…the assets of any entity shall not be treated as plan assets if, immediately after the most recent acquisition of any equity interest in the entity, less than 25 percent of the total value of each class of equity interest in the entity is held by benefit plan investors."

[8] See, e.g., 29 CFR 2510.3-101(c) (definition of "operating company").

[9] Nachman Corp. v. Pension Benefit Guaranty Corporation, 446 U.S. 359, 361 (1980).

[10] See also 29 CFR 2510.3-101.

Even if we agreed that a mutual fund adviser had some disclosure duty to a plan under ERISA, which we strongly do not, it is impossible to place that burden on a fund adviser who is unable to identify whether its shareholders are plans. Mutual fund shares and limited partnership interests are securities, governed by disclosure obligations specified with particularity under the Investment Company Act of 1940, regardless of who the investors in the entity may be. It seems far beyond the Department's authority to require that mutual funds' disclosure under ERISA to a plan investor be different than or additional to that required by the Securities and Exchange Commission for all investors. Thus, in the context of services provided to non-plan asset vehicles, we urge the Department to delete the phrase "or the financial products in which plan assets are invested" and clarify that the regulation does not intend to make service providers to mutual funds and non-plan asset vehicles subject to ERISA, and in need of exemptive relief at all.[11]

Level of Specificity regarding the Disclosure of Fees and Services

The Department should provide clarification on the level of specificity in regard to the disclosure of fees and compensation. Brokerage commissions illustrate how it can be difficult (and in some cases impossible) for a service provider to determine the exact dollar amount of indirect compensation. As you know, services and fees may not be provided or allocated on a plan by plan basis so it may not be possible to report or allocate amounts on that basis. Indeed, many broker-dealers are not aware that the account for which they are trading is owned by a particular plan. This difficulty was acknowledged in the Final Rule and Notice regarding the Annual Reporting and Disclosure Revision of Annual Information Return/Reports which allows for the description of a formula used to calculate or determine the compensation rather than the exact amount of compensation for certain service providers.[12] We urge the Department to provide flexibility that would permit the plan fiduciary to request an estimate or rely on the disclosure available in trade confirmations.

This is a particular problem in the institutional brokerage area, but requires clarification in the area of retail brokers as well. For example, we urge the Department to allow a retail broker acting as a consultant to a 401(k) plan to inform the plan fiduciary that different mutual fund families pay different fees (also known as service fees, trailers, or 12b-1 fees) to the broker, and within a fund, different share classes pay different levels of such fees to the broker, without having to specifically disclose the rates for all share

[11] We are not clear, for example, how this language would be reconciled with an investment by a plan in General Motors common stock. To the extent such equity is a "financial product in which plan assets are invested," we are hard pressed, as an intellectual matter, in understanding how the various relationships that General Motors may have with its vendors could be of relevance to a plan. While the example may seem fanciful, the Department's muddying the waters on what constitutes a "service provider" relationship in a non-plan asset context unfortunately confuses what we believe to be a settled issue.

[12] 72 Fed. Reg. at 64742 (November 16, 2007)

classes of all funds that the plan fiduciary could ever select. When the plan fiduciary has made its selection, the rate of the trailer or other fee can be disclosed. Once the plan fiduciary has the applicable fee rates, and the level of assets in each fund (which is readily available from his custodian), he can easily estimate the fees received by the broker. In our view, that is significant and helpful additional disclosure which will not overwhelm the plan fiduciary but will allow him to understand what his consultants may receive.

A related issue is the level of specificity relating to the description of services. It is possible that an ancillary service not contemplated in a service contract is provided by a service provider. Any ancillary service will likely be provided free of charge because, in most cases, the amount the plan is paying the service provider for the service will remain the same. It is also possible, in fact likely, that the specific services themselves are subject to diverse descriptions by different vendors – for example, we are hard-pressed to clearly articulate all of the various forms of "recordkeeping" that a plan may require at the participant, investment or trust level. For example, a recordkeeper may include in its services the reconciliation of trades but may not charge separately for that service and may not list it as part of the services since in most recordkeepers' viewpoints, reconciliation is part and parcel of recordkeeping.

Moreover, if the service is covered by a single fee there is simply no need to unbundle that fee to describe all of its components. For example, a broker may charge a plan 5 cents a share. That commission includes exchange fees, the cost of confirming, the cost of clearing and settling, and any access charges if the trade is executed on an electronic communication network. There is simply no reason for a plan to receive disclosure that goes into that amount of detail. In addition, there may be charges that no one would expect to be incurred, (such as ACAT fees, section 31 fees, inactivity fees, legal transfers, accommodation transfers, extensions, returned items, statement copies, overnight/express mail, trade corrections, confirm copies, and foreign securities transfers) that would not be anticipated and should not need to be disclosed in advance, so long as they were disclosed promptly after they were incurred.[13] Where a broker has a fee schedule available on request, and makes its availability known to the plan fiduciary, we believe the rule should be satisfied. In addition, we believe there are certain payments or concessions that a broker may receive that are not on account of a particular plan or

[13] Section 31 of the Exchange Act authorizes the Securities and Exchange Commission to collect fees from FINRA (formerly the NASD) on the aggregate dollar amount of sales transacted by or through any FINRA member firm other than on a national securities exchange for securities subject to prompt last-sale reporting. Section 3 of Schedule A to the NASD By-Laws provides that "[e]ach member shall be assessed a regulatory transaction fee..[which] shall be determined in accordance with" Exchange Act section 31 (the "Section 31 Fees").

particular trade (such as payment for order flow, discounts on fees associated with ECNs or trading venues, moderate entertainment, conferences and meetings). We strongly believe that the proposed rule, like the instructions to the Form 5500, should state that if payments are received that are not allocable to a particular plan but paid because of an entire relationship, they need not be disclosed as compensation within the meaning of this regulation.

In this connection, we urge the Department to consider a safe harbor for disclosure under the regulation, such that any disclosure that meets the requirements of the securities laws will be deemed to meet the disclosure requirements of Section 408(b)(2).

Thus, we hope that the Department will confirm that insignificant, event-triggered fees that are not disclosed as well as other inadvertent omissions would not constitute a prohibited transaction. In this connection, we urge the Department to consider a rule similar to that in the insurance company general account regulation, 29 CFR 2550.401c-1(i)(5), which allows noncompliance to be cured in a reasonable period of time.

We believe the regulation should provide that if a service is provided that has not been disclosed, its full disclosure within a reasonable period after discovery, should regain the protection of Section 408(b)(2). Accordingly, we would urge the Department to revise the regulation so that it relates to particular services and not to the entire arrangement, and to permit prompt corrections of disclosure failures. Such a change might read as follows:

(c) Reasonable services – (1) No service provided to an employee benefit plan . . . is reasonable within the meaning of Section 408(b)(2) of the Act . . .unless" the following requirements are satisfied: "(ii) the services are described in writing". We would then add a new sub clause (vii) which would provide that in the event of an inadvertent failure to disclose a service, prompt correction of that disclosure failure shall not cause the requirements of this section to fail to be satisfied.

We also would like the Department to reconsider the 30-day period for advising plan fiduciaries of changes. As we have explained in other contexts, 30 days is a very short time to notify hundreds, if not thousands of plan fiduciaries. We strongly urge the Department to increase this time period to 90 days, or the end of the quarter following the quarter in which the change occurs.

Agents and Subcontractors

The Department has recognized that not all entities that provide services are providing those services to plans. In many cases, those services are provided to another service provider. So for example, an executing broker may hire a different broker to clear and settle trades[14] and always hires a depository to custody securities on an electronic basis. Prime brokers hire foreign local subcustodians, who are effectively providing services to the prime broker to enable him to do his job worldwide. The printer and mailing service provides services to the recordkeeper; so, for that matter, does the U.S. Postal Service, Federal Express, UPS and other delivery services. They may be part of plan services but they are providing those services to the recordkeeper who has undertaken to communicate with plans, with mutual funds, with the IRS, with the bank custodian. We believe that it is important for the Department to distinguish between entities that provide services to plans, and entities that provide services to other service providers. Under current law, it is not critical to make this distinction because even if one were to consider the U.S. Postal Service to be a plan service provider, the U.S. Postal Service could rest easy, knowing its services were appropriate and necessary, reasonably priced, and terminable on short notice. However, under the proposed rule, it makes an enormous difference whether the entity is a service provider to plans, or only to other service providers. We urge the Department to make clear that where an entity has no independent contact with a plan, its services performed for other service providers does not make them parties in interest to plans, and does not subject them to Title I of ERISA. In addition, we hope the Department will make clear that pursuant to the disclosure requirements, a service provider is not required to list all services, all compensation and all conflicts of any "agents" of the service provider.

Bundled Arrangements

The proposed regulation provides a special rule for bundled services that are priced as a package. The rule permits the disclosing service provider to report compensation on an aggregate basis, which is very helpful. However, it then goes on to say that fees must be separately reported "to the extent such party receives or may receive compensation or fees that are a separate charge directly against the plan's investment or that are set on a transaction basis, such as finders fees, brokerage commissions, and soft dollars". We are concerned that this exception may swallow the rule. For example, consider where a plan enters into a wrap program, paying one fee to cover asset allocation by the wrap provider, asset management by affiliated and unaffiliated managers, and all brokerage through the wrap provider's affiliate. Since the entire fee is a charge against the plan's investment, all of the fee components would have to be disclosed separately. We urge the Department to revise the exception to permit the service provider to provide such other reasonable information as the plan fiduciary may request about the components of the bundled fee.

Disclosure Concerning Conflicts of Interest

The proposed rule provides that a contract or arrangement must require that the service provider disclose specific information regarding conflicts of interest for the service provider in its performance of services for the plan. Service providers generally

[14] See DOL Advisory Opinion 82-49A.

will have to disclose any financial or other interest in transactions in which the plan will participate; describe material financial, referral, or other relationship it has with various parties that creates or may create a conflict of interest for the service provider pursuant to the contract or arrangement; and identify whether a service provider can affect its own compensation from whatever source without prior approval of an independent plan fiduciary. The proposed rule is so broad that it will be virtually impossible for some of the larger financial service providers to enumerate every single existing or potential conflict of interest. We believe it is vital that the Department provide a solution for larger service providers whose services permeate the industry and for whom almost every contract or arrangement gives rise to existing or potential conflicts of interest.

As you are aware, securities firms are subject to restrictions with respect to non-cash compensation. SIFMA has been a strong advocate for guidance from the Department that would be consistent with FINRA rules. Again, we would ask that the Department carefully consider some guidance on this point. As we discussed in the context of the Form 5500, we urge the Department to clarify the types of activities that would result in compensation to a service provider. Without some type of relief on the scope of this proposal, plan sponsors and plan service providers will likely stop attending seminars and other educational events out of concern that attendance resulted in compensation being paid to the provider.

We support the provision of a generic disclosure to plan fiduciaries regarding the types of education, seminars, gifts, and entertainment that may be received. The regulation should provide, however, that this disclosure should only be provided annually since the firm may have amended policies relating to their relationships. We would like to be able to amend and supplement our comments, and in particular, provide proposed language for the final regulation.

Other Exemptions

The Department specifically asked for comment on the relationship between these proposed regulations and other statutory exemptions which may cover services. As noted earlier, there are a number of exemptions other than Section 408(b)(2) that could provide relief for a service contract depending on the nature of the responsible plan fiduciary or the type of service provided. Some are provided in the statute, such as bank ancillary services and investment advice; others are class or individual exemptions. For example, the qualified professional asset manager exemption ("QPAM exemption") under PTE 84-14, the "in house asset manager" exemption under PTE 96-23, the bank collective trust exemption pursuant to PTE 91-38, the insurance company pooled separate account exemption under PTE 90-1, and the insurance company general account exemption under PTE 95-60, all premise the services relief based on the sophistication of the approving fiduciary. Those exemptions assume and require that the fiduciary approving the services arrangement is both supervised under other state or federal regulatory regimes and is sophisticated and experienced in fiduciary conduct. It would run counter to that entire exemption scheme to single out service contracts as the one area where a sophisticated regulated fiduciary could not use its own judgment to assess the disclosure it is given prior to entering into the contract. As you know, those exemptions cover the most sophisticated and arcane investment instruments, loan arrangements and uses of plan assets. It is simply not reasonable to suggest that such a fiduciary is experienced enough to enter into such investment transactions without meeting the kind of very specific conditions in the proposed rule, but lacks the sophistication to hire a broker to execute transactions on the New York Stock Exchange without meeting all of the conditions in the new rule.

Indeed, in 1998, the Department, in reviewing the issue of derivative contracts, wisely chose to lay out its thinking through its general authority to interpret the Act's prudence requirements, and not to amend all of the exemptions covering principal transactions to impose, as conditions for exemptive relief, a new set of guidelines for fiduciaries.[15] As the Department noted in the preamble to its prudence regulation, it is not for the Department to substitute its judgment for that of a fiduciary in looking at any particular transaction.[16] The Department has taken the position since 1975 that more than one exemption can cover particular transactions. We think it would be a real departure – and a mistake -- for the Department to take the position here that services may only be exempt under Section 408(b)(2). Similarly, Congress has just enacted an advice exemption that has its own conditions and requirements. We do not see the authority under ERISA for the Department to take the position that these carefully crafted statutory conditions in the advice exemption are somehow neutered by the Department's regulations under Section 408(b)(2).

Similarly, to the extent that other statutory exemptions provide relief for services, we are not convinced that the Department has the statutory authority to eliminate those exemptions as a source for relief. See in this connection, the statutory exemption for bank ancillary services. Finally, we believe that there are certain exemptions that the Department issued without detailed conditions because the type of service is so straightforward and clear on its face that detailed conditions are unnecessary. In addition,

[15] See DOL Information Letter to Hon. Eugene Ludwig, Comptroller of the Currency (March 21, 1996) ("Investments in derivatives are subject to the fiduciary responsibility rules in the same manner as are any other plan investments. Thus, plan fiduciaries must determine that an investment in derivatives is, among other things, prudent and made solely in the interest of the plan's participants and beneficiaries. In determining whether to invest in a particular derivative, plan fiduciaries are required to engage in the same general procedures and undertake the same type of analysis that they would in making any other investment decision.")

[16] See 44 Fed. Reg. 31,639 (June 1, 1979) ("…the Department does not view compliance with the provisions of the regulation as necessarily constituting the exclusive method for satisfying the requirements of the 'prudence' rule. Rather, the regulation is in the nature of a 'safe harbor' provision; it is the opinion of the Department that fiduciaries who comply with the provisions of the regulation will have satisfied the requirements of the 'prudence' rule, but no opinion is expressed in the regulation as to the status of activities undertaken or performed that do not so comply.")

we think PTE 75-1, Part I was promulgated with the recognition that written arrangements between every plan and all the various brokers it may use is simply not the practice in the industry for any client. We do not believe that the Department should substitute its judgment for that of the Securities and Exchange Commission on how relationships between brokers and clients should be documented, and the disclosure that brokers should be required to give.

A broker-dealer has disclosure obligations under general “anti-fraud” provisions of federal securities laws. While these provisions are very broad, the SEC has adopted rules, issued interpretations and brought enforcement actions that define some activities prohibited under these provisions. For example, Rule 10b-10, promulgated under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), requires broker-dealers to give or send *written* notice disclosing to customers certain information before the completion of a transaction. Along with information about the transaction itself (such as the date, time, identity, price and number of shares involved), the broker-dealer must provide information about its capacity (i.e. whether it is acting as an agent or a principal); its compensation (for agency trades, compensation includes its commission); the source and amount of any remuneration received or to be received from a third party by the broker in connection with the transaction; whether any odd-lot differential (or equivalent fee) has been paid in connection with the execution of an order; and specified information in the case of any transaction in a debt security.[17] Other examples of written disclosures to be made by broker-dealers include notification to customers that the broker-dealer will effect transactions in “penny stocks” as well as risk disclosure in connection with that transaction[18] and, written disclosure of the capacity in which the broker-dealer is acting with regard to transactions involving a broker-dealer’s participation in the distribution of a new issue securities when extending credit to customers in connection with the new issue during the distribution period or 30 days thereafter. [19] In addition to written disclosures required to be given by broker-dealers, other disclosure obligations under general anti-fraud provisions of federal securities laws exist. For example, under the so-called “shingle” theory, a broker-dealer represents to its customers that it will deal fairly with them, consistent with the standards of the profession. Based on this representation, the SEC over the years has set forth duties including the duty to disclose certain material information (i.e., information the customer would consider important as an investor) and fully disclose any potential conflict of interest.[20] These are not insubstantial disclosures and they form the basis for a complex and comprehensive scheme of regulation in the securities industry. In our view, they should be sufficient, and should not be supplanted by a competing and possibly inconsistent regime under ERISA. We strongly urge the

[17] Rule 10b-10 promulgated under the Exchange Act

[18] Rules 15g-2 through 15g-9 of the Exchange Act

[19] Section 11(d)(2) of the Exchange Act

[20] Guide to Broker-Dealer Regulation; Division of Market Regulation U.S. Securities and Exchange Commission (December 2005) http://www.sec.gov/divisions/marketreg/bdguide.htm

Department to leave other exemptive relief unaffected by these new rules under Section 408(b)(2). We believe it is entirely appropriate for any applicable prohibited transactions exemption to continue to apply notwithstanding the exemption in Section 408(b)(2).

Carve Out for Small Plans

We believe that the Department correctly determined that small plans would be overwhelmed with new reporting and disclosure requirements in the final instructions to the Form 5500. The most underrepresented cadre of employees covered by savings and pension plans are those employed by small employers, for whom the rules and regulations governing these plans are too expensive, too confusing, too burdensome and too complicated. We urge the Department to consider exempting small plans from the requirements of the new rules. We think such an exclusion is completely consistent with the Department's decision not to make these rules applicable to IRAs and even more important, because employer sponsored plans need to be supported and encouraged even more aggressively than IRAs.

Gifts and Entertainment

SIFMA urges the Department to reconsider the requirement to make advance disclosure of gifts, entertainment, conferences, meetings and the like. Such items are obviously not disclosable with any kind of specificity in advance. We urge the Department to change the proposal in this regard in three ways. The first is to allow service providers to generally disclose the kinds of gifts, entertainment, conferences, meetings and the like that they might receive. The second is to provide that with respect to any gifts, entertainment, conferences, meetings and the like that a service provider actually receives, disclosure is given at that point to the plan fiduciary, subject to the following exception, which is our third point. The regulation should specifically provide that (i) where gifts, entertainment, conferences, meetings and the like are received by the service provider because of an overall relationship with the giver, and not directly because of the plan, no disclosure need be made; and (ii) even where the gifts, entertainment, conferences, meetings and the like are received directly because of the plan, if the amounts do not exceed the de minimis rule in the Form 5500 instructions, no notice need be given.

Plan Sponsor Payments

We firmly believe that where a plan sponsor provides the payment to a service provider, the service provider needs no exemptive relief from Section 408(b)(2) or any other exemption. The service provider has not used plan assets for its own benefit and the plan sponsor is not involved in a fiduciary act when it decides to pay, or how much to pay, a particular service provider. We urge the Department to make this distinction clear.

Form 5500 Concerns

As we have discussed with Department staff, we continue to be concerned about various provisions of the Form 5500, some inconsistencies in approach, and certain provisions found in the instructions but seemingly contradicted in the preamble. We urge the Department to continue to review the Form 5500, and to review comments on the proposed amendments to the Section 408(b)(2) in the context of the Form 5500 as well.

* * * *

On behalf of our members, we thank you for considering our comments regarding the proposed revisions to Section 408(b)(2) of ERISA and we respectfully request the opportunity to supplement and amplify our comments. Please do not hesitate to contact the undersigned should you wish to discuss the issues raised in this letter.

Sincerely,

Liz Varley

Liz Varley
Managing Director, Government Affairs

cc: Brad Campbell
Alan Lebowitz
Bob Doyle
Tim Hauser