SVIA

July 21, 2015

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

Office of Exemption Determinations
Employee Benefits Security Administration
Attn: D-11712, D-11713, D-11850
U.S. Department of Labor
200 Constitution Avenue N.W., Suite 400
Washington, D.C. 20210

Re: Comments on Definition of the Term "Fiduciary"; Conflict of Interest Rule – Retirement Investment Advice (RIN 1210-AB32); Comments on Proposed Exemptions D-11712, D-11713 and D-11850 (ZRIN 1210-ZA25)

Ladies and Gentlemen:

The Stable Value Investment Association (SVIA or Association) is pleased to comment on the proposed amendment to the Department's regulation under Section 3(21) of the Employee Retirement Income Security Act of 1974 (ERISA), which was published in the *Federal Register* on April 20, 2015 (referred to herein as the Proposed Regulation), and the related proposed class exemptions and proposed amendments to class exemptions that were published on the same day. The Proposed Regulation and related changes are of major importance to SVIA's 66 members representing every segment of the stable value investment community, including public and private retirement plan sponsors, insurance companies, banks, investment managers and consultants. SVIA's members collectively managed $706 billion in stable value assets as of December 31, 2014 for over 167,000 defined contribution plans on behalf of more than 17 million defined contribution plan participants.

SVIA is a non-profit organization dedicated to educating retirement plan sponsors and the public about the importance of saving for retirement and the contribution stable value can make toward a financially secure retirement. Stable value funds, which are used only in participant-directed defined contribution retirement plans, are designed to preserve principal, while providing investment returns similar to intermediate bond funds, as well as provide benefit-responsive liquidity to plan participants (meaning that participants can transact at contract value – principal plus accrued interest). As such, stable value funds play an important role in the investment option line-up for those plans that include them (approximately half of all defined contribution plans), as an available choice for plan participants looking for a relatively low-risk investment that provides protection of principal and steady income that, over time, has exceeded returns from money market investments.

Like most commenters, SVIA shares the Department's goal of ensuring that advisors to retirement plans and plan participants act in their clients' best interests. The focus of our comments is to make sure that the Proposed Regulation, and the accompanying prohibited transaction class exemptions, do not have unintended effects on the ability of defined contribution plans to use stable value as an investment option for their plan participants and beneficiaries, or on the ability of stable value managers to make investments or obtain the products and services they need for purposes of managing and administering these investment options.

A summary of SVIA's comments, as described more specifically below, is as follows:

- The counterparty carve-out should be clarified to cover the marketing and sale of services and insurance contracts, and be made available to cover transactions with plans of any size.
- If the counterparty carve-out is not so clarified, then
    - The proposed Best Interest Contract Exemption's relief should be clarified to be available for stable value products and services,
    - The proposed Principal Transactions Exemption's scope should be expanded to cover other types of investments used by stable value funds, and
    - The proposed "best interest" standard should not be a condition to exemptive relief under the Best Interest Contract Exemption, the Principal Transactions Exemption and PTE 84-24.
- The valuation carve-out should be expanded to cover valuation statements to single-plan investment options and plan participants.

As a general matter, the following comments are intended to highlight those issues of particular concern to the stable value area because of the manner in which they may impact stable value products and services. SVIA and its members also have concerns about several technical provisions of the Proposed Regulation and the related exemptions that may have broader impacts not specific to stable value, such as the contracting and disclosure conditions and data requirements under the proposed new exemptions, as well as with regard to the anticipated costs of coming into compliance and the need for a longer transition period. On these matters, we refer the Department to the comments being submitted by other financial services industry firms, including a number of our members, and trade associations that deal with those matters in more detail than this letter.

I. Description of Stable Value Investments

A. Types of Stable Value Investments

By way of introduction, we point out that there are two possible ways in which a plan can invest in stable value.

First, a plan may invest directly in a stable value product, such as a guaranteed investment contract sold by an insurance company or a bank investment contract sold by a bank. Under the terms of the contract, the insurance company or bank (as the case may be) agrees to repay principal, and to credit the principal with interest at a rate that is typically set for a predetermined period. The investing plan's assets include its interest in the contract, but not the assets underlying the contract. The contract is backed by the assets of the insurance company (either its general account or, in some arrangements, a dedicated separate account – which provides greater protection in the event of the insurance company's insolvency) or the bank, rather than a separate fund in which the plan is considered to hold an interest. The contract commits to pay out participant withdrawals at the book or contract value of the participant's interest in the contract – namely, the principal plus credited interest accrued to date.

Another form of stable value product is a synthetic guaranteed investment contract, in which the plan owns a portfolio of fixed-income securities and enters into a "wrap" contract with an insurance company or bank (or an affiliate of an insurance company or bank). The wrap contract provides protection for the portfolio against loss of principal and accrued interest (subject to exceptions specified in the contract, such as certain employer-initiated rather than participant-directed events – *e.g.*, termination of the plan or termination of the fund as a plan investment option), so that plan participants are able to make withdrawals from the stable value investment at book or contract value even if the fair market value of the underlying portfolio has declined. (The ability of the participants to make withdrawals at book/contract value without regard to whether the portfolio's underlying fair market value has declined, referred to as being "fully benefit-responsive," is a key feature of stable value products.)

The second, and currently more common, way for plans (particularly smaller plans) to invest in stable value is through a commingled fund, in the form of a bank collective investment fund or an insurance company separate account. A collective fund has the advantage of being able to diversify among multiple stable value providers and products. Such a fund may invest in guaranteed investment contracts, bank investment contracts and synthetic investment contracts, and also short-term investment funds for the temporary investment of cash received, being disbursed or awaiting investment, as well as to meet investment guidelines' requirements for the fund to hold a cash buffer to cover withdrawal requests. A commingled insurance company separate account also provides a popular means for smaller plans to participate in a vehicle where the assets are aggregated in a larger portfolio, which is generally easier to manage, and participating plans may benefit from economies of scale.

Because these types of funds are structured as bank collective funds or insurance company separate accounts in which ERISA-covered plans invest, their assets are treated as plan assets subject to ERISA. Thus, the parties who manage and provide advice with respect to the funds' investments are fiduciaries subject to ERISA's fiduciary responsibility provisions.

B. Marketing of Stable Value Products and Services

Plans obtain the stable value products and services described in the preceding section in several different ways. The following list identifies the principal arrangements entered into by plans; there may be other forms not specifically mentioned here but they are generally variations of the listed arrangements:

- *Stable value commingled funds:* Plan fiduciaries typically gain access to such a fund by entering on behalf of the plan into a collective fund participation agreement or a group annuity contract (including an “omnibus” annuity contract where multiple unrelated plans can participate in the commingled fund through a single contract).

- *Insurance company general account and separate account products (including guaranteed investment contracts):* The plan fiduciaries may establish the plan’s stable value investment option (or a portion of the stable value option) through a contract with an insurance company, where the contract may represent an obligation of the insurance company’s general account or be funded through one or more insurance company separate accounts.

- *Wrap contracts:* As indicated, wrap contracts are necessary to enable stable value funds that invest in securities portfolios to provide benefit-responsive liquidity for participant transactions. Plans obtain wrap coverage either indirectly through using a commingled fund, or directly where the plan’s stable value option is in the form of a separately managed account.

- *Investment management and wrap administration services:* If the plan fiduciaries decide to establish a stand-alone stable value investment option under the plan rather than using a commingled fund, they may manage that option themselves or retain firms with specific expertise in stable value to do so. Under a “synthetic” guaranteed investment contract arrangement, there are two types of management involved. First, there is administration of the “wrap” contracts that enable the stable value option to provide “benefit-responsive” liquidity to the plan participants. Second, there is the management of the investments underlying those contracts, primarily fixed income securities. Whether or not the stable value option uses “synthetic” arrangements, it may also invest in guaranteed investment contracts or similar instruments, money market funds (either mutual funds or collective investment funds), and stable value commingled funds.

II. Potential Impacts on Stable Value Fund Business

The Proposed Regulation and related class exemptions may impact both the ability of financial services firms to offer stable value products and services to defined contribution plans, and the management and operation of plans’ stable value investment options.

The primary concern raised by the Proposed Regulation is whether the normal course of marketing and selling these products and services to a plan could constitute a “recommendation” that is "specifically directed" to the plan fiduciaries, and therefore "investment advice" that would make the marketing/selling entity a fiduciary. The Association believes this should not be the case.

Second, the Proposed Regulation may also have impacts on the management and operation of stable value investment options. As noted above, stable value options are structured as bank collective funds and insurance company separate accounts for multiple plans, as well as separately managed accounts for individual plans, which are treated as ERISA plan asset entities.[1] These funds and accounts are typically managed and operated in reliance on the class exemptions for qualified professional asset managers (QPAMs) (PTE 84-14), in-house asset managers (INHAMs) (PTE 96-23), bank collective investment funds (PTE 91-38) and/or insurance company separate accounts (PTE 90-1), as applicable, to the extent exemptive relief is necessary. However, if a broker-dealer, insurance company or other party engaging in a transaction with the stable value investment option were treated as an investment advice fiduciary with respect to that transaction, these exemptions would not provide a sufficient level of relief from the ERISA prohibited transaction rules. We do not believe that this is an appropriate result, as there has been no indication in the past (at least in the stable value context) that QPAMs, INHAMs, banks or insurance companies have unduly relied to a plan's detriment on the recommendations of conflicted broker-dealers or other counterparties or service providers.

Our concerns both with respect to marketing stable value products and services, and with respect to the management and operation of stable value investment options, could be addressed through the proposed counterparty carve-out in the Proposed Regulation and the proposed class exemptions if certain changes are made, which we discuss in the next section.

III. Specific Comments on Counterparty Carve-Out and Proposed Exemptions

A. Counterparty Carve-Out Should be Clarified to Cover Services and Insurance Contracts and Expanded to Cover Plans of Any Size

Given the breadth of the proposed "investment advice" definition, unless the Department makes changes to the definition to clarify that normal course marketing and sales activities do not give rise to fiduciary status, the Association is concerned that providers of stable value products and services could be deemed to be fiduciaries just because they make such products and services available to plans. The Association believes that the "counterparty carve-out" in subsection (b)(1) of the Proposed Regulation should be available as an exception for such activities (including responses to plans' requests for proposal (RFPs), which are clearly marketing rather than advisory in nature) from fiduciary status, subject to the following two issues.

First, the carve-out, by its terms, covers advice "with respect to an arm's length sale, purchase, loan or bilateral contract between the plan and the counterparty, or with respect to a proposal to enter into such a sale, purchase, loan or bilateral contract." The Association would

[1] General account assets funding stable value group annuity contracts, if structured to meet the "guaranteed benefit policy" requirements, are not considered ERISA plan assets.

understand, and asks the Department to confirm, that this language covers a purchase or sale of interests in a commingled fund (whether in the form of a bank collective investment fund or an insurance company separate account), as well as entering into a participation agreement or annuity contract providing for such purchases and sales. What is not as clear is whether the other categories listed above, including other types of insurance or bank contracts and contracts for investment management or wrap administration services, would be covered by the term "bilateral contract."

Strictly speaking, the term "bilateral contract" would cover any contract between two parties. However, many contracts in the stable value space may actually involve more than two parties, including not only the plan (or its trustee or other authorized representative) and the service provider but also the plan sponsor and possibly an affiliate of the service provider, so they technically may not qualify. Further, because the term "counterparty" is typically associated with investment transactions, such as swaps, and not necessarily with service arrangements or stable value wrap coverage, there is the concern that services were intended to be excluded, and that the term could be interpreted to exclude other types of contractual arrangements common to the stable value area such as guaranteed investment contracts and wrap contracts. The Association asks the Department to clarify that the term "bilateral contract" is intended to cover any contractual arrangement between a plan and a third party, including for services or for benefit-responsive coverage (such as a guaranteed investment contract, wrap contract or similar arrangement), and that joining multiple parties to the contract (such as, but not limited to, the plan sponsor or an affiliate of the third party that is contracting with the plan) will not cause the contract to fail to be considered a "bilateral contract" for purposes of this provision.

Second, the carve-out is only available with respect to transactions with either (1) an employee benefit plan that has 100 or more participants, or (2) an independent plan fiduciary that has responsibility for managing at least $100 million in employee benefit plan assets, whether for a single plan or multiple plans.[2] While plans that operate their stable value funds as separately managed accounts will generally fall into these categories, either by themselves or through retaining a professional stable value manager or wrap administrator that manages at least $100 million in employee benefit plan assets, this may not always be the case. Smaller plans seeking to make stable value available as a plan investment option also need to have access to the same types of products and services.[3] If the counterparty carve-out is not expanded by the Department, then smaller plans will have little access to information about stable value products beyond the marketing of a platform of investments. The education carve-out, as proposed,

[2] While the preamble to the Proposed Regulation makes clear that these are two separate categories, that is less clear in the regulation itself, and some write-ups on the Proposed Regulation have suggested that a plan must meet both tests to qualify for the carve-out. The Association asks that in the event the Department does not extend the counterparty carve-out to cover transactions with plans of all sizes, the Department make clear in the regulation, either in the lead-in language in subparagraph (A) or by reorganizing subparagraphs (B) and (C), that these are alternative categories, so that an independent fiduciary with responsibility for $100 million or more in plan assets may act on behalf of a plan with less than 100 participants and rely on this carve-out.

[3] With regard to investments by plans in commingled funds that are bank collective investment funds or insurance company separate accounts, the Association understands that the exemption in Section 408(b)(8) of ERISA should be available to the extent that the bank or insurance company is treated as an "investment advice" fiduciary to the plan.

would not be available because that carve-out prohibits mention of any specific stable value fund or annuity product.

For this reason, the Association asks the Department to expand the availability of the counterparty carve-out to transactions with plans of any size. This way, provided the same conditions of the carve-out apply and the same representations are given and acknowledged, smaller plans will not be unduly restricted in seeking access to stable value products and services, and stable value investment options for such plans would not be unduly restricted in transactions with broker-dealers, insurance companies and other counterparties.

B. Proposed Best Interest Contract (BIC) Exemption's Conditions Should be Clarified to Apply to Certain Stable Value Products and Services

In the event that the Department is unwilling to expand the counterparty carve-out to plans of any size – which we believe would be the preferable and most effective approach – stable value providers could still seek to come within the BIC Exemption for dealings with smaller plans.[4] However, there are several issues and limitations under the BIC Exemption that would need to be addressed before it could be used to cover transactions in stable value products and services.

First, the BIC Exemption, as written, is not available in connection with advice to fiduciaries of *participant-directed* plans. It is only available for advice to the plan sponsor of a *non-participant directed* plan, to the extent the plan sponsor acts as a fiduciary. Therefore, to make the BIC Exemption available for plan fiduciary decisions to use stable value products and services, the BIC Exemption would need to be expanded to cover advice to fiduciaries of participant-directed plans, including not just plan sponsors but any person serving in such a role (including, but not limited to, individuals serving as plan trustees or a plan committee).

Second, the BIC Exemption does not cover the provision of services. Specifically, by its terms, it is available only for the purchase, sale or holding of an "Asset," a defined term that does not include services. Therefore, to provide the necessary relief for stable value arrangements, the BIC Exemption would need to be expanded to cover contracts for the provision of services. Alternatively, as indicated above, it is our view that the better manner in which to address the marketing and sale of services would be through the counterparty carve-out. Given that the conditions of the BIC Exemption are specifically focused on the purchase and sale of certain types of assets, using the counterparty carve-out would avoid the need to revisit those conditions to accommodate service arrangements.

Third, situations may arise in which a plan that typically has 100 or more participants falls only slightly below the 100 participant mark, or a plan that typically has fewer than 100 participants only slightly exceeds that figure, due to what may be short-term variations in the plan participant population. This becomes an issue because a party relying on the BIC Exemption is required to acknowledge fiduciary status by contract, whereas a party relying on

4 In addition, for sales of stable value-related insurance contracts, parties effecting the sale should be able to rely on PTE 84-24 for relief.

the counterparty carve-out is not deemed a fiduciary. Vacillating back and forth from fiduciary status to non-fiduciary status based on a fluctuating participant count would create a confusing conundrum for both the plan and the party providing the ongoing advice. This result further militates for extending the counterparty carve-out to cover transactions with small plans.

C. Proposed Principal Transactions Exemption's Scope Should be Expanded to Cover Investments Used by Stable Value Funds

The proposed BIC Exemption, as drafted, would not provide relief for a purchase or sale transaction directly with an "investment advice" fiduciary, other than the relief in Section VI for insurance and annuity contracts. Therefore, for a smaller plan's stable value investment option to be able to engage in the purchase or sale of securities with "investment advice" fiduciaries in the absence of the counterparty carve-out, other exemptive relief would be necessary. Such relief would be provided by the proposed class exemption for principal transactions (the Principal Transactions Exemption).

However, the scope of relief under this exemption is limited to "Debt Securities," as defined in Section VI(d). This definition covers U.S. corporate debt securities, U.S. Treasury securities and U.S. agency securities. While these comprise a large percentage of the investments of stable value investment options, they are other types of investments that are not covered. These can include swaps (which may or may not qualify for the swap carve-out in subsection (b)(2) of the Proposed Regulation, depending on the type of swap and the identity of the counterparty), other types of derivatives, municipal securities, non-U.S. fixed income securities (such as foreign sovereign debt), and asset-backed securities (including mortgage-backed securities). In addition, while sales of wrap or other stable value-related contracts that are in the form of insurance contracts should be covered by PTE 84-24, sales of wrap or other contracts that are not insurance contracts would not be covered by either PTE 84-24 or the BIC Exemption. In order to be effective for stable value investment options, the scope of the Principal Transactions Exemption would need to be expanded to cover these categories of investment instruments and contracts.

D. Proposed "Best Interest" Standard is Not an Appropriate Condition to Exemptive Relief

The three exemptions that may be relevant to stable value – the proposed BIC Exemption, the proposed Principal Transactions Exemption, and PTE 84-24 – would all incorporate a "best interest" standard as a condition to exemptive relief. In the two new exemptions, there would be the additional requirement that the "best interest" standard be made a contractual obligation of the party seeking the relief. "Best interest" is defined as acting prudently and without regard to the financial or other interests of the advising party. The preamble to the exemptions indicates that this definition is intended to effectively mirror the duties of prudence and loyalty under section 404 of ERISA, as applied in the context of fiduciary investment advice.

As indicated at the outset, SVIA shares the Department's goal of ensuring that advisors to retirement plans and plan participants act in their clients' best interests. However, imposing a "best interest" standard as defined in the proposals under the terms of an exemption on a fiduciary's dealings with ERISA plans appears unnecessary and could potentially be confusing and disruptive.

The basic concern of the Association is whether such a standard is an appropriate condition to exemptive relief. Currently, prudence is not part of the terms of an exemption, instead being treated as a separate requirement. The Department's notices granting exemptions point out that the exemptions do not provide relief from the ERISA duties of prudence and loyalty (this language is also included in the current proposals), and practitioners often emphasize to their clients that a transaction may be prudent and still violate the prohibited transaction rules. For this reason, particularly as to transactions where prudence may be difficult to evaluate objectively, imposing this standard could make it far more difficult for a plan fiduciary or a financial services firm to know with any certainty whether it is ever in compliance with the new or revised exemptions, despite the Department's instruction that investments should not be evaluated based on hindsight. Since a finding of imprudence would now have prohibited transaction ramifications, this could increase the risk of engaging in transactions under the affected exemptions and lead firms to seek ways to address the increased risk, such as through increasing their fees to take into account potential litigation costs or making investments that are lower-risk but may ultimately generate lower investment returns (which itself could present potential litigation risks).

While the Department justifies this requirement by highlighting the current absence of such standards for IRAs, the new standards would not be limited to IRAs. They would also apply to ERISA plans, even though ERISA plans are already covered by the ERISA section 404 fiduciary requirements, and would also become a part of several existing exemptions such as PTE 84-24 that have never included such a condition. While the Department adds in the preambles that an exemption permitting transactions that violate the prudence and loyalty standards would be unlikely to meet the test for granting an administrative exemption under ERISA and section 4975 of the Internal Revenue Code, such a statement stands in contrast to 40 years of history under those provisions of not making prudence or loyalty an explicit condition to relief. To the contrary, exemptions granted by the Department rely instead on indirect methods to confirm that a transaction is prudent, such as reliance on an independent fiduciary or independent appraisal or through initial and ongoing disclosure and approval requirements. We are not aware of any studies or data indicating a need to incorporate such requirements into the terms of ERISA prohibited transaction relief, which would appear unnecessary given that they already apply by terms of the statute.

In addition, the wording with respect to the duty of loyalty differs from the statutory language. Instead of requiring the investment adviser to act "solely in the interest" of the Retirement Investor, the "best interest" provision requires the investment adviser to act "without regard to the financial or other interests" of the investment adviser, its affiliates or any "other party." While it appears from the Department's explanation that the Department would intend the language to be interpreted in a substantially similar manner to the ERISA duty of loyalty, the language differences may conceivably be read in practice to suggest differences in application.

For these reasons, the Association requests that the relief under the BIC Exemption, the Principal Transactions Exemption and PTE 84-24 not be subject to compliance with a "best interest" standard. If the Department believes that such a standard continues to be necessary for dealings with IRAs, then the Association requests in the alternative that, to avoid confusion, duplication and the possibility of inconsistent interpretations due to the language differences, the "best interest" standard under these exemptions not apply to employee benefit plans that are subject to Part 4 of Title I, Subtitle B of ERISA. Because these standards already apply to ERISA plan fiduciaries by statute, incorporating them into an exemption is unnecessary and inconsistent with 40 years of practice in the exemptions area.

IV. Valuation Carve-Out Should be Expanded to Cover Valuation Statements to Single-Plan Investment Options and Plan Participants

The Proposed Regulation would include within the scope of "investment advice" an appraisal, fairness opinion, or similar statement concerning the value of securities or other property, if provided in connection with a specific transaction involving the acquisition, disposition or exchange of such securities or other property (subsection (a)(1)(iii)). Recognizing, however, that routine valuations should not trigger fiduciary status, the Department included a "financial reports and valuations" carve-out in subsection (b)(5). As relevant here, this carve-out covers a statement of value to (1) an investment fund, such as a collective investment fund or pooled separate account, in which more than one unaffiliated plan has an investment, and (2) a plan, plan fiduciary, plan participant or beneficiary solely for purposes of compliance with ERISA or Internal Revenue Code reporting and disclosure provisions and the regulations, forms and schedules thereunder, and any applicable reporting or disclosure requirement under a federal or state law, rule or regulation or self-regulatory organization rule or regulation.

The first of these categories would cover valuations provided to stable value commingled funds. However, neither category would appear to cover statements of value provided to single-plan stable value investment options. There does not appear to be any reason to exclude valuation information, such as a brokerage statement, provided to the fiduciaries managing a single-plan stable value investment option. Further, neither category would cover information provided in the normal course (not pursuant to a specific reporting or disclosure requirement) to plan participants and beneficiaries regarding the value of a stable value investment option, whether a commingled fund or a single-plan arrangement.

We recognize that the expanded definition under the Proposed Regulation would cover valuations only where they are provided in connection with a specific transaction. Even so, the possibility exists that a plan participant or beneficiary may decide to enter into a specific transaction, such as an investment option transfer or a distribution, based on valuation information provided in the normal course – such as a benefit statement, on a plan website or in response to a phone inquiry regarding current account values. As such values are provided as factual information regarding the participant's account, and are not intended as recommendations as to whether to proceed with a particular transaction, they should not be treated as fiduciary "investment advice" for purposes of the Proposed Regulation. The same would be true for valuations provided to a plan fiduciary managing a single-plan stable value investment option. A broker-dealer providing a brokerage statement to such a fiduciary is doing so to apprise the fiduciary of the current value of investments held in the account, not as a recommendation to buy or sell such investments.

The role of a statement of value as not constituting any form of recommendation or advice is even clearer in the context of stable value. Guaranteed investment contracts, wrap contracts and similar stable value instruments – which generally represent the main investments of a stable value investment option – are valued at their contract or book value, which is determined by the provisions of the governing agreement, usually by means of a formula and/or an interest rate that is set in advance of the period for which the value is being generated. There is no discretion or judgment being applying in determining these values.

For this reason, the Association requests that the financial reports and valuations carve-out be expanded to include statements of value provided to (1) plan fiduciaries who manage a plan investment option for a single plan or related plans, and (2) plan participants and beneficiaries regarding the current value of investments held in their plan accounts.

SVIA thanks the Department for consideration of these comments. The Association is happy to answer any questions and to work with the Department on this important regulatory initiative.

Sincerely,

Gina Mitchell
President