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July 21, 2015

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

RE: Definition of the Term "Fiduciary"; 29 CFR §2509 and 2510

To Whom It May Concern:

fi360 [1] appreciates the opportunity to comment on the definition of "fiduciary" (hereinafter the "Proposal") under Section 3(21) of the Employee Retirement Income Security Act ("ERISA"), application of the Best Interest Contract Exemption ("BICE") to rollover advice, and impact of the Proposal on small accounts.

General Comments

fi360 generally supports the revised definition of fiduciary. We believe that an updated definition of a sec. 3(21) fiduciary is long overdue for reasons articulated by the Department of Labor (the "Department" or "DOL") in both the 2010 and current Proposal. Unfortunately, conflicted advice to self-directed plans, participants and IRAs is a systemic problem that demands regulatory action. We also look for a positive marketplace response from leaders in financial services who embrace a high fiduciary standard for all who provide investment advice.[2] The argument for a higher standard should not be

[1] fi360 offers a full circle approach to investment fiduciary education, practice management, and support. Its mission is to help its clients gather, grow, and protect assets through better investment and business decision-making. Its clients are fiduciaries under securities, pension and trust law, including investment advisers, managers, trustees and plan sponsors. With legally substantiated Practices as its foundation fi360 offers training, tools, and resources in support of that mission. fi360 manages the Accredited Investment Fiduciary® (AIF®), Accredited Investment Fiduciary Analyst® (AIFA®), and Professional Plan Consultant™ (PPC™) designation programs. At present, there are more than 7,900 active AIF, AIFA, and PPC designees. For more information, please visit http://www.fi360.com/.

[2] *See, e.g.,* Braswell, Mason, "Merrill Lynch's John Thiel urges colleagues to work with DOL on fiduciary rule," *Investment News*, Apr. 8, 2015. (Available at http://www.investmentnews.com/article/20150408/FREE/150409924/merrill-lynchs-john-thiel-urges-colleagues-

driven merely by regulatory mandates but, more importantly, by recognition that society expects professionals to adhere to a standard of care that places clients' interests first. [3] The General Accountability Office report on IRA rollover advice[4] confirms a systemic problem. That conclusion, combined with peer-reviewed literature documenting the cost of conflicted advice, and our own conversations with numerous advisors, calls for a pro-active response from regulators and industry.

fi360 generally supports the Proposal for legal, regulatory, and experiential reasons. From a legal perspective, as noted in the Proposal, ERISA requires plan fiduciaries to comply with fundamental obligations rooted in the common law of trusts. [5] Even before enactment of ERISA, over the centuries judicial precedent reposed a high fiduciary standard of responsibility on persons entrusted with managing or providing professional advice on third-party assets.[6]

Despite strong legal precedent under securities and trust laws recognizing advice as a fiduciary function, the distinction between fiduciary and non-fiduciary roles played by financial intermediaries has become muddled. Three decades ago, non-fiduciary salespersons could be more clearly distinguished from fiduciary advice-providers. Today, the lines are blurred. Salespeople now routinely render advice without fiduciary accountability and often use fiduciary-sounding job titles, including "financial adviser." Moreover, dual registrants (individuals who are affiliated with firms registered as investment advisers and broker-dealers) are now commonplace and represent the fastest growing segment of the adviser marketplace.[7] Hat-switching between fiduciary advice and non-fiduciary sales roles is permitted, even within a single client relationship. As a result, investors are confused, leading them to place their trust in salespersons that, under the law of agency, have a fiduciary duty to act in the best interest of their employer, not the customer. It is not that salespeople are inherently untrustworthy, but rather that they have significant conflicts of interest that make fulfilment of a duty of loyalty to the client unreliable.

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to-work-with-dol-on?NLID=daily&NL_issueDate=20150408&utm_source=Daily-20150408&utm_medium=in-newsletter&utm_campaign=investmentnews&utm_term=text.) *See* also Leonhardt, Megan, "Casady: Better DOL Rule Needs Only 'A Couple' of Improvements," *WealthManagement.com*, May 21, 2015. (Available at http://wealthmanagement.com/blog/casady-better-dol-rule-needs-only-couple-improvements.) .

[3] Numerous studies confirm that investors believe financial intermediaries act in their best interest. However, broker-dealers and investment advisers are subject to different regulatory structures but trends in the financial services market since the early 1990s have blurred the boundaries between them. *See, e.g.,* Hung, Angela A., Noreen Clancy, Jeff Dominitz, Eric Talley, Claude Berrebi and Farrukh Suvankulov. *Investor and Industry Perspectives on Investment Advisers and Broker-Dealers.* Santa Monica, CA: RAND Corporation, 2008. (Available at http://www.rand.org/pubs/technical_reports/TR556).

[4] Jeszeck, Charles A., "Labor and IRS Could Improve the Rollover Process for Participants," U.S. Government Accountability Office, Mar. 7, 2013. (Available at http://www.gao.gov/products/GAO-13-30.)

[5] "Definition of the Term "Fiduciary," *Federal Register,* Vol. 80, No. 75, Apr. 20, 2015, at 21932.

[6] In addition to imposing a fiduciary duty for managing the property of others, federal and state securities laws also generally require persons paid compensation for offering or providing investment advice to register as investment advisers and act in a fiduciary capacity. Moreover, the 'shingle theory' under common law also generally holds securities brokers to a fiduciary standard when they hold discretion over customer assets or have established a relationship of trust and confidence with the customer.

[7] The North American Securities Administrators Association, which jointly administers the Investment Adviser Registration Depository, in January 2014 estimated the number of dual registrants at 262,166.

As such, the DOL initiative rightfully asserts that those who operate in a position of trust by purporting to give objective professional advice must be accountable under the statutory definition of an ERISA fiduciary.

As a consequence, financial regulations must be updated to assure that those who render personalized advice are accountable under a strong fiduciary standard of care, and financial services firms that offer advice must be prepared to operate in a culture of professional responsibility firmly rooted in the fiduciary standard. The proposed DOL rule seeks to strengthen regulations regarding advice rendered to retirement investors. Separately, Securities and Exchange Commission Chair Mary Jo White has announced that the SEC will be moving forward with rulemaking authorized under Section 913 of Dodd-Frank.[8] In this regard, we believe that the Department has in good faith promulgated a Proposal that is in alignment with securities rules of the SEC and Financial Industry Regulatory Authority ("FINRA") to the extent permitted by law.[9]

Finally, fi360 draws upon many years of experience in forming a conclusion that the regulation of pension and retail investment advisors needs to be updated. For more than 15 years fi360 has provided training to financial advisors on fiduciary best practices and tools to assist them in developing prudent processes. Our direct interaction with advisors and special expertise in standards of investment fiduciary conduct provide us unique insights regarding the prevalence and impacts of conflicts of interest. During training sessions, our educators routinely inquire as to whether advisors in attendance have clients, friends, or family members who have suffered financial losses due to tainted advice from a previous experience. Invariably, the overwhelming majority of class participants provide confirmation that biased investment advice is not an isolated event. As a result, while we believe that the majority of

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[8] de la Merced, Michael J., "S.E.C. Chief Voices Support for Higher Advice Standard for Brokers," *The New York Times*, Mar. 17, 2015. (Available at http://www.nytimes.com/2015/03/18/business/dealbook/sec-chief-voices-support-for-higher-advice-standard-for-brokers.html?ref=topics&_r=0.)

[9] Some critics of the Proposal have questioned whether the DOL worked substantively with the SEC on harmonizing their respective fiduciary standards. While Congress had different legislative purposes in enacting the federal securities laws and ERISA, it is our belief that the DOL has, in fact, adapted important features of securities regulation into the Proposal. These include: 1) a carve-out from the fiduciary definition for swap and security-based swap transactions; 2) another carve-out for self-directed trades of the brokerage customer; 3) including treating referrals to investment professionals as fiduciary in nature (which is analogous to the SEC's 'solicitor's rule' under Rule 206(4)-3 of the Investment Advisers Act of 1940 [the "Advisers Act" that requires disclosure of conflicts], as well a corresponding requirement widely adopted by state securities administrators that solicitors paid to make referrals to federal or state-registered investment adviser firms register with the firm as an agent and hence become associated fiduciaries; 4) increased use of disclosure as a remedy for managing conflicts of interest (comparable to conflict-of-interest disclosure rules under the Advisers Act); 5) DOL's suggestion that it rely in the Rule on client communication rules of the Financial Industry Regulatory Authority ("FINRA") to determine whether investment advice has been offered; 6) the SEC's temporary rule governing principal transactions with certain advisory clients; and 7) borrowing language from the Dodd-Frank requirement that, if the SEC promulgates a uniform fiduciary standard for brokers and advisers, they must act in the best interest of the client *without regard to the financial or other interests* of the firm. [Italics indicate duplicate language in Dodd-Frank and the Proposal.] *See* Dodd-Frank Act, Sec. 913(g) and Proposed Best Interest Contract Exemption, 29 CFR Part 2550, *Federal Register*, Vol. 80, No. 75, Apr. 20, 2015, at 21984.

both fiduciary and non-fiduciary financial advice-providers do seek to serve their clients' best interest, good intentions are often thwarted in sales cultures where conflicts are systemic. Whether consciously or subconsciously, most people are influenced by financial incentives. At a time when most American workers face an uphill battle to prepare financially for retirement, the added costs associated with conflicts makes the challenge more daunting. Our experience gained through direct observation is backed by independent academic research such as by Dr. Daylian Cain of Yale University on the practical effects of conflicts of interest and disclosure,[10] and the Council of Economic Advisers[11] on the high cost of conflicts to investors.

Our comments on a limited number of issues that we believe require additional clarification follow.

Carve-Outs from the Definition of Fiduciary.

Platform Providers/Selection and Monitoring Assistance.

One of the carve-outs from the definition of fiduciary in the Proposal is available to certain service providers such as recordkeepers and third-party administrators that provide a "platform" or selection of investment options for participant-directed plans. Under paragraph (b)(4) of this exemption, merely identifying investment alternatives meeting objective criteria or providing objective financial data regarding available alternatives to the plan fiduciary would not cause a platform provider to be a fiduciary investment adviser.

Although not clearly fitting in the categories cited in the Proposal, fi360 seeks clarification that analytical tools and objective data services provided to others fits within this carve-out or is otherwise excluded. For example, fi360 offers a paid subscription service that can be used by investment fiduciaries and others to apply an objective process to analyze, place on a watch list, or flag for replacement in a plan or IRA account investment alternatives such as mutual funds, ETFs, variable annuity subaccounts, and separately managed accounts based upon specific due diligence criteria. The fi360 tools also allow a subscriber to assess mutual funds and ETFs based upon an automated analysis of the investment products using nine due diligence criteria that results in the fi360 Fiduciary Score®.[12] The criteria are used to benchmark the investment option to similar products within asset classes derived from Morningstar data. The factors used to calculate fi360's Fiduciary Score are:

1. Regulatory oversight of the product
2. Length of investment or portfolio manager's track record
3. Organization stability
4. Amount of assets under management
5. Style drift
6. Correlation of the investment product to its benchmark

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[10] *See,* Moore, Don A., Cain, Daylian M., Loewenstein, George, and Bazerman, Max H.; *Conflicts of Interest: Challenges and Solutions in Business, Law, Medicine, and Public Policy*, (Cambridge University Press, 2010).

[11] *See*, generally, "The Effects of Conflicted Investment Advice on Retirement Savings," Council of Economic Advisers, February 2015. (Available at https://www.whitehouse.gov/sites/default/files/docs/cea_coi_report_final.pdf.)

[12] Available at http://www.fi360.com/products-services/tools-overview/fi360-fiduciary-score.)

7. Expense ratios and other fees
8. Risk-adjusted performance to its peer group
9. Relative performance over time to its peer group

The tools provided by fi360 are specifically intended to help investment fiduciaries apply prudent processes consistent with a high fiduciary standard of care. For example, entering the list of a plan's designated investment alternatives (or funds, ETFs and variable annuities in a retail client's portfolio, as the case may be) into the analytical scoring process allows investment fiduciaries to objectively assess whether the individual investments are appropriate. A disproportionate number of low fiduciary scores would indicate the investment selection is not performing up to its assigned benchmark. Neither Morningstar nor fi360 has predetermined the effect of the screening system on any investment product, fi360 is not paid 'placement fees' or other financial incentives by third parties to favor certain investments over others, and fi360 encourages users not to rely solely on the product analysis in determining suitability. Other factors may include, but are not limited to, a comparison of objectives in the investment policy statement, demographic composition of plan participants, risk tolerance of an individual client, and so forth.

Another analytical tool available to fi360 subscribers includes an asset allocation optimizer that assesses the plan investment options or retail portfolio in terms of risk and return. fi360 licenses the methodology through a patented process developed by an unaffiliated RIA.[13] The optimizer displays the efficient frontier[14] for investment allocations based on risk and return for 11 broad asset classes and displays a sample or real portfolio (after entry of data) for comparison to the efficient frontier.

In both instances, fi360 believes that, based on the discussion of the platform provider carve-out in the proposing release, data-servicing and analysis firms like fi360 or Morningstar would meet the general intent of the carve-out and should not be treated as a plan fiduciary. Similar to the Department's use of examples in describing activities that would meet or not necessarily meet the requirements of the best interest contract exemption ("BICE"), fi360 also recommends that the Department provide examples of carve-outs in the adopting release that pertain to paragraph (b)(4) of the definition or create a separate carve-out for independent data-service providers.

Best Interest Contract Exemption ("BICE" or "BIC Exemption").

Overall, the BIC Exemption is a reasonable approach to addressing the challenge of accommodating variable compensation situations without compromising foundational fiduciary principles. The task of reconciling the inherent conflict of variable compensation with the fiduciary duties of loyalty and care will require considerable effort due to the specific requirements of BICE. We view the requirements to assume fiduciary status, warrant the determination that advice rendered

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[13] For more information on New Frontier, which developed the Optimizer, please go to http://www.newfrontieradvisors.com/index.html (last visited July 2015).

[14] The efficient frontier is a term used in modern portfolio theory to describe a quantitative measure of expected return for a given level of risk. Or in other words, a method for establishing the appropriate mix of stocks and bonds and other asset classes to allow the portfolio the best chance to earn the highest return commensurate with the lowest level of risk, or portfolio volatility, based on the client's long-term investment goals and risk tolerance.

serves the client's best interest, and accept contractual accountability as especially necessary to help assure fulfillment of the fiduciary duties of loyalty and care.

We are aware that the DOL is considering certain clarifications and refinements to the BIC Exemption based upon public comments by Department officials. We are confident that the technical comments we could make regarding such important conditions as the timing of execution of a BICE contract will be covered by others and addressed with more specificity by the Department. Therefore, we will restrict our comments about the BIC Exemption to a specific situation of special concern for advisors who routinely accept fiduciary accountability and adhere to fiduciary obligations.

It is our understanding that a fiduciary advisor to a retirement plan will need to rely upon the BIC Exemption to recommend a rollover of assets to an IRA for a plan participant if the advisor will receive higher compensation on the assets held in the IRA than when the assets were in the ERISA plan. This, we understand, would be true even if the advisor is a fiduciary at all times and provides services on a level compensation basis with no compensation from any third parties. In our view, a separate exemption for rollover advice may be appropriate for situations such as this.

The rollover decision is a one-time event[15] and we suggest the DOL consider creating an exemption designed to handle the point-in-time situation when a fiduciary retirement advisor to a plan is called upon to assist a plan participant with a rollover decision. Specifically, the exemption should address the circumstance where the fiduciary retirement plan advisor provides participant-level rollover advice and also offers to provide ongoing, level-fee advice to any participant who decides to roll their plan assets to an IRA, albeit at a compensation level that is higher than the advisor would earn if the assets were retained in the plan, distributed, or moved to another plan.

Conceptually, this limited rollover advice exemption would be BICE-like in that it would require written confirmation of fiduciary accountability, policies and procedures to assure impartial assessment of all of the options available to the participant, and thorough disclosure of the costs and conflict involved if the advisor is chosen to provide advice on the IRA assets (i.e., additional compensation for the advisor once the assets are in the IRA). However, this situation is much more straight-forward than examples provided in the Proposal involving third-party payments and variable compensation. Moreover, in this circumstance, the assets will still be in the plan at the point in time when the rollover advice is rendered, not when the participant's account is rolled over into an IRA or a new plan. The DOL maintains direct regulatory oversight authority over plan assets; therefore, no special contract would seem to be required to ensure recourse for a fiduciary breach related to the rollover advice.

BICE – Definition of an 'Asset.'

Under the Section VIII Definition of 'Asset,' for purposes of relying on the Best Interest Contract Exemption the range of investment products would be restricted ' to traditional, highly liquid and easy-to-price investment products. The products meeting this category include bank deposits, CDs, mutual funds, ETFs (including exchange-traded REITS), U.S. Treasury securities and corporate bonds. Excluded from the definition are security futures, puts, calls, and options.

[15] By 'one-time event' we are referring to the point in time that the rollover decision for that account is made by the participant. Obviously, over a lifetime workers changing employers may face a rollover decision more than once.

We strongly support the proposed restriction on the range of investment products permitted under the BIC Exemption to those products for which there is an active market and reliable pricing. We can envision product innovations and changes that may prompt product providers to urge approval from the DOL for expansion of the list of permitted products. For example, so-called alternative funds are ETFs registered with the Commission. However, both the SEC and FINRA are concerned about the marketing of these and other complex products that may pose risk to investors. FINRA has in recent years issued warnings in connection with the sale of complex products[16] and the SEC recently solicited public comment on the risk of complex ETFs, in particular highly leveraged or inverse products designed to amplify short-term returns by using debt and derivatives.[17]

Whether these or other products prove to be prudent additions to a retirement portfolio of the future remain to be seen. As such, we recommend that the Department outline the process that will be used to decide what products in the future may be deemed permissible under BICE. We also seek specific clarification as to whether it is the Department's position that any and all pooled funds registered under the Investment Company Act of 1940 would meet the definition of 'Asset' under BICE, or whether it would prohibit certain products, such as "alternative" ETFs?

Consideration of a High-Quality, Low-Cost Exemption

The Department requested comments on the practicality of introducing a prohibited transaction exemption for variable compensation earned for advice pertaining to certain high-quality, low-cost investments. This exemption presumably could take the form of a simplified, less demanding version of the BIC Exemption. We do not support the introduction of such an exemption. Cost is just one due diligence factor to be considered, and defining "high-quality" would be very difficult in an exemption. One of the great strengths of the fiduciary standard is that it is principles-based and currently relies on a prudence standard for determining suitability. Prescriptive rules do not adapt well to a changing marketplace and are susceptible to circumvention by innovative product design. The current five-part definition of fiduciary serves as a case in point.

It is important to note that the BIC Exemption is prescriptive and is, in our view, susceptible to both becoming outdated and dysfunctional over time. In our view, BICE (with vigilant oversight) is an acceptable way to deal with current marketplace realities without compromising fundamental fiduciary principles. We expect BICE will ultimately become unnecessary as marketplace participants find that a collaborative relationship that avoids conflicts, rather than preserves and manages them, is far more beneficial to all parties.

Impact of the Proposal on Small Accounts.

The Department's economic analysis must rely on objective metrics and datasets. Several years ago fi360 and other organizations sponsored an academic review of the impact of a fiduciary standard on the brokerage industry which was submitted to the Department for consideration. The paper found that, using variations in the common law standard for brokers among the 50 states, the number of registered representatives (stock brokers) doing business within a state as a percentage of total

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[16] *See* NASD Notice to Members 01-23 and FINRA Regulatory Notices 11-02, 12-25 and 12-55.

[17] *See* "SEC Publishes Request for Public Comment on Exchange-Traded Products," News Release, Securities and Exchange Commission, Jun 12, 2015. (Available at http://www.sec.gov/news/pressrelease/2015-118.html.)

households did not vary significantly between states with a strict common-law fiduciary standard and those with none. Nor were brokers constrained in their ability to serve lower-wealth clients, according to the study's findings, or limited in their ability to offer a broad range of products providing commission compensation.[18]

This is not to suggest that every segment of the financial services industry will find it easy and inexpensive to transition to the professionalization of investment advice under a uniformly high standard of fiduciary conduct. For those firms in which a sales culture is firmly entrenched, the transition will be especially difficult.

The transition is certainly feasible. Fiduciary advisors are succeeding in the marketplace today, serving clients across the full spectrum of investable assets. Technological innovations are making financial tools and advice more accessible than ever before. Financial product changes are underway that remove compensation conflicts and improve quality. Most importantly, advisors are becoming increasingly aware that conflicts of interest can impair judgment and damage client relationships. We have a high degree of confidence in the ability of financial services professionals and companies to be innovative and adaptive to changing circumstances in ways that strengthen the fiduciary standard.

Conclusion

The essence of every professional advisor's job is to do what is right for clients and to do it well. This translates to fulfilment of the foundational fiduciary duties of loyalty and care and correspondingly, a profitable business based on trust. This is true regardless of whether we are talking about medical, legal, or financial advice. It is simply unacceptable that financial advice is the one exception from among these professions that involve some of the most important decisions consumers will ever make in their lives – and a regulatory void allows some practitioners to avoid fiduciary accountability.

The DOL has rightfully proposed a principles-based approach to this question. Principles are core values that can be flexibly applied to accommodate specific situations but these standards must not be compromised. We appreciate the effort the Department is devoting to be flexible and responsive to the needs of the marketplace participants without compromising core fiduciary principles that are essential to serving investors' best interests.

We truly appreciate the opportunity to provide our views on this critical policy initiative. Please do not hesitate to contact us at (412) 221-0292 if you have any questions or would like additional information.

Sincerely,

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[18] Finke, Michael S. and Langdon, Thomas Patrick, *The Impact of the Broker-Dealer Fiduciary Standard on Financial Advice* (March 9, 2012). (Available at SSRN: http://ssrn.com/abstract=2019090 or http://dx.doi.org/10.2139/ssrn.2019090.)

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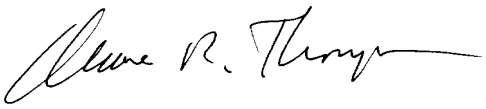

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