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Filed Electronically
Office of Exemption Determinations
Employee Benefits Security Administration
Attention: D-11933
U.S. Department of Labor
200 Constitution Avenue N.W., Suite 400
Washington, DC 20210

Re: **RIN 1210-AB82; Fiduciary Rule and Related Prohibited Transaction Exemptions**

Dear Sir or Madam:

We are writing in response to the Department of Labor's Request for Information Regarding the Fiduciary Rule and Prohibited Transaction Exemptions (the "RFI"). We previously submitted a letter in response to question 1, supporting a delay in the January 1, 2018, applicability date of the Best Interest Contract Exemption. This letter addresses question 7, relating to the possibility of an alternative streamlined exemption for mutual funds, and question 16, relating to enhancing the grandfather rule. As discussed more fully below, we greatly appreciate the thrust of both questions and strongly support the creation of a streamlined exemption for mutual funds as well as enhancements to the grandfather rule.

1. Streamlined Exemption for Mutual Funds

The RFI requests input on a possible prohibited transaction exemption based on the so-called clean shares letter, which was issued by the U.S. Securities and Exchange Commission to our firm on January 11, 2017. The clean shares letter elaborates on section 22(d) of the Investment Company Act of 1940, which establishes the framework for mutual fund pricing and has been understood to require that mutual fund families, and not recommending broker-dealers, set commissions on funds. The letter for the first time defines the circumstances in which a broker-dealer firm acting as a broker may set commissions. The result is a roadmap for a broker-dealer firm to set a harmonized commission schedule across all mutual funds offered by the firm and even across different types of securities, such as ETFs and individual securities, without violating section 22(d).

We agree with the Department that an exemption modelled on the clean shares letter is a good idea. The clean shares model allows a broker-dealer firm to address many of the conflicts of interest targeted by the Best Interest Contract Exemption through fund pricing,

rather than the adoption of internal conflict of interest mitigation policies. In effect, the clean shares model allows a broker-dealer firm to separate compensation for investment advice from the underlying investments in the same way that advisory programs separate compensation for investment advice from the underlying investments. In fact, in the clean shares model, the same clean share class could be used for a firm's brokerage and advisory programs, which would have the virtue of facilitating transparency to investors who are choosing between brokerage and advisory services. Clean share brokerage programs also have the virtue of making transparent the compensation associated with the broker-dealer's services.

The cornerstone of the proposed exemption should be a harmonized commission schedule so that the recommendation of one investment over another will not affect the amount of the commission payable to the broker-dealer firm. To the extent the commission schedule is uniform for all mutual funds regardless of fund family or asset type, the broker-dealer firm will not have an incentive to recommend one fund over another fund. The same logic applies between mutual funds and other securities, most notably ETFs, which could be available alongside open-end mutual funds on the same economic terms.[1]

Clean shares of course leave possible concerns about churning to generate commissions but this is a conflict of interest that financial firms have extensive experience supervising and mitigating. It is also merely the inverse of the conflict associated with most advisory programs which may include trading costs in the advisory fee and therefore need to monitor so-called reverse churning. We think mandating that firms adopt compliance procedures consistent with FINRA's requirement that brokers "observe high standards of commercial honor and just and equitable principles of trade" and adhere to a "quantitative suitability" standard with regard to transactions would be appropriate.

We understand that the exemption contemplated by the Department would preclude third-party fees to ensure that there are no other incentives for a firm to recommend one investment over another. However, we urge the Department to provide that other fees are not inconsistent with the exemption. In this regard, for example, we understand that some firms are contemplating approaches that may involve an ongoing asset-based fee charged at the account level alongside a commission. The ongoing fee would be much lower than the typical asset-based advisory fee and would provide compensation for ongoing service,

[1] We encourage the Department, however, to accommodate other investments which may not be amendable to a harmonized commission schedule. While individual equity securities may fit with a commission schedule alongside mutual funds and ETFs, there will be investments, such as individual fixed income securities or cash, which may not fit. It would be helpful if the clean shares exemption accommodated these investments with appropriate safe guards.

thereby preserving the underlying economics associated with traditional commissionable mutual funds.

We do not believe that other conditions are necessary. The exemption contemplated by the Department should be streamlined in the sense that unlike the Best Interest Contract Exemption it should not include a contract with the investor. Rather, the exemption should depend solely on adoption of a harmonized commission schedule, anti-churning policies and procedures, and a prohibition on third-party fees. There is no need for a contractual private right of action given the structural nature of the solution.[2] This framework would provide an attractive exemption that could be instrumental in preserving commissions and therefore choice for investors about how to pay for investment advice.

We are, however, concerned about creating a bridge to clean shares. As the Department is aware, many broker-dealer firms are actively exploring the development of clean share programs, which is obviously a positive development. The clean shares letter was, however, issued on January 11, 2017, six months before the RFI was issued. There are numerous business and operational steps that need to be taken to develop a clean shares solution. Today, mutual funds typically are available on platforms or sub-accounting systems that are used to perform mutual fund-specific functions, such as aggregation to apply rights of accumulation and accounting to capture rights of exchange. These systems are ordinarily not designed to account for other investments. It will take some time (perhaps 18-24 months) for systems development to catch up to clean shares. Firms also need to determine how they want to price a clean shares program, train their financial advisers, develop communications materials and obtain investor agreement to participate. In short, very few broker-dealer firms -- if any -- will be able to launch a clean shares program in the near future.

Without a bridge to clean shares, firms will be forced to either eliminate access to commissionable investment advice or make the fundamental business changes required by the Best Interest Contract Exemption in order to continue offering traditional commissionable mutual funds. Both approaches would be incredibly disruptive for investors who could have little choice but to either move to a fee-based advisory program in order to maintain access to advice or enter into a Best Interest Contract only to be transitioned into a clean shares program shortly thereafter. Moreover, some smaller investors could needlessly lose access to investment advice altogether – at least for some period of time in this scenario.

The obvious solution is to make the transitional provisions of the Best Interest Contract Exemption available until such time as clean shares brokerage programs can be operationalized. This could be done by ensuring the applicability date of the Best Interest Contract Exemption is after broker-dealer firms have had sufficient time, for example, June 9,

[2] We understand that FINRA generally requires that broker-dealers adhere to conflicts of interest policies and procedures – regardless of the rule giving rise to the policy – suggesting an additional layer of possible enforcement.

2019, which is 24 months after the rule's effective date. If, however, the Department decides that the applicability date should be an earlier date, an alternative approach would be to craft the clean shares exemption to include relief for firms that are working diligently and in good faith towards adoption of a clean shares approach. The conditions should allow the transitioning broker-dealer firm to continue to recommend traditional commissionable mutual funds during the stub period between the applicability date under the Best Interest Contract Exemption and the first date the firm is reasonably able to launch its clean shares program. The conditions for transition relief should logically be the same conditions that apply during the transition period under the Best Interest Contract Exemption, namely the impartial conduct standards.

While we believe that clean shares will play an important role in preserving commissionable investment advice – that is, preserving investor choice, we do not think it should be the only option available for recommending mutual funds on a commissionable basis. The Department should strive to provide workable rules for a variety of different business models. In this regard, it is important that the Best Interest Contract Exemption facilitate broker-dealer recommendations of traditional Class A mutual fund recommendations.

Many of the features of the Class A share that raise conflicts of interest considerations are also beneficial to investors. Traditional mutual funds typically pay smaller commissions and ongoing service or 12b-1 fees for fixed income funds relative to equity funds. The difference in pricing between fixed income and equity is a marketplace development that strikes a balance between reasonable compensation to the broker-dealer and successful investor outcomes. Similarly, mutual fund families often eliminate commissions on exchanges between funds within the fund family ("rights of exchange") and provide reduced commissions based on prior investments with the fund family ("rights of accumulation"). Our experience is that rights of exchange and accumulation are widely utilized by financial advisors for the benefit of investors. For these reasons, our support for a streamlined exemption for clean shares brokerage programs should not be misconstrued as reducing the need for improvements to the Best Interest Contract Exemption or even an alternative exemption that would apply to recommendations of traditional Class A share mutual funds.[3]

2. Enhancing the Grandfather

We greatly appreciate the Department's decision to include a grandfather rule in the Best Interest Contract Exemption. Without a grandfather rule, millions of Americans holding long-term investments in traditional mutual funds would have been forced out of those

[3] The transition period under the Best Interest Contract Exemption provides real world experience with reconciling the fiduciary standard with commissionable mutual funds and can serve as a laboratory for the types of conflicts of interest mitigation policies that might preserve the benefits of traditional commissionable mutual fund pricing while ensuring that investors benefit from appropriate consumer protections.

investments, unless their broker-dealer was willing to adhere to the Best Interest Contract Exemption. As market developments have shown, not all broker-dealers are embracing the Best Interest Contract Exemption, even the transition version, and some have stopped recommending commissionable mutual funds in IRAs. And, even for firms that are committed to commissionable mutual fund investments, many financial advisers are shifting their business model towards fee-based advisory programs. Without the grandfather rule, many investors would have been moved to an advisory program in circumstances in which it was in the investor's best interests to stay in their existing investments with their current advisor. The benefits to investors as well as the avoidance of chaos cannot be easily overstated.

However, the grandfather date -- June 9, 2017 -- makes little sense now that the Department has delayed application of the transition notice requirement that was scheduled to go into effect on June 9, 2017. The only difference between the standard of conduct for grandfathered assets and the standard of conduct for recommendations that are made during the transition period was the required notice of conflicts of interest. As a result of the delay, the same impartial conduct standards apply to both grandfathered assets and non-grandfathered assets recommended during the transition period.

The rational for applying the grandfather rule on June 9, 2017, as opposed to January 1, 2018, was never entirely clear and we certainly do not see a rationale given the deferral of the notice requirement. Especially when one considers that the rule may change in light of the RFI, it would obviously not be fair to impose retroactive requirements. The right thing to do is to make the grandfather date the applicability date. This would provide certainty to broker-dealer firms who are making recommendations during the transition period and would also minimize disruption for investors.

The other major improvement that we believe should be made to the grandfather rule is an enhancement to cover recommendations to make additional purchases into grandfathered securities. As constructed, the grandfather applies to recommendations to hold, exchange pursuant to a rights of exchange policy, or sell an investment that was recommended prior to the June 9, 2017 effective date; it does not allow an advisor to recommend an additional investment into a grandfather security other than one made pursuant to a pre-existing systematic purchase program.

Without the ability to buy more of an existing grandfathered investment, the grandfathering rule has limited utility for investors who are likely to make additional purchases. Financial advisors working with investors who are still accumulating are forced to either maintain two programs – one grandfathered and one non-grandfathered – or consolidate all of the client's investments in a single non-grandfathered account. Two programs covering a single investor is confusing and deprives investors of the benefit of discounts based on size of investment, such as fee breakpoints. The result is that we have seen widespread usage of the

grandfather rule for investors who are not likely to make additional purchases, such as investors in the de-cumulation or drawdown stage. But more often than not we have seen investors who are making additional investments moved into fee-based advisory programs which are the most common non-grandfathered program. Fee-based advisory programs make sense for many investors but the inability to make additional purchases without tainting the grandfather should not be the reason why investors move into these programs.

The rule we propose is a narrow one. It would not apply to investments into new securities and it is not a "relationship grandfather." It is a logical extension of the grandfathering of hold recommendations. If a hold recommendation is in an investor's best interests, it will often be the case that a recommendation to add to that position is in the investor's best interests.

The need for an enhanced grandfather rule is particularly acute because we have not yet reached the point at which the grandfather rule is most important. We will only know whether the grandfather rule has been widely utilized and minimized disruption when we reach the applicability date. It is at this point that the choice between grandfathering and compliance with the Best Interest Contract Exemption or any other exemption will truly apply. We think an enhanced grandfather along the lines we suggest would be incredibly beneficial to investors and could greatly reduce investment cost and disruption.

We appreciate the opportunity to comment.

Respectfully submitted,

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