CENTER FOR CAPITAL MARKETS
COMPETITIVENESS

TOM QUAADMAN
EXECUTIVE VICE PRESIDENT

1615 H STREET, NW
WASHINGTON, DC 20062-2000
(202) 463-5540
tquaadman@uschamber.com

August 6, 2020

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

Submitted Electronically via Federal eRulemaking Portal: www.regulations.gov

Re: Application No. D-12011, ZRIN 1210-ZA29, EBSA-2020-0003 – Improving Investment Advice for Workers and Retirees

To Whom It May Concern:

The U.S. Chamber of Commerce's Center for Capital Markets Competitiveness ("Chamber") appreciates the opportunity to comment on the Department of Labor's ("Department") notice of proposed class exemption ("Proposed Exemption") permitting reasonable compensation for investment advice fiduciaries providing advice and engaging in certain principal transactions with Employee Retirement Income Security Act ("ERISA") plans, participants and Individual Retirement Accounts or Annuities ("IRA") holders.

We support the Department's clarification that the 1975 regulation that defines fiduciary is reinstated and the need for the Proposed Exemption. However, we believe that certain modifications, outlined in greater detail below, are necessary to improve the Proposed Exemption's utility. In addition, we are concerned that the new guidance outlined in the preamble to the Proposed Exemption constitutes a reinterpretation of the "five-part" test under ERISA that is contrary to the U.S. Court of Appeals for the Fifth Circuit's 2018 decision to vacate the Department's 2016 fiduciary rule.

The Chamber has been a strong advocate for our members in supporting regulatory policies that ensure access and choice to different types of financial services. Regulatory efforts that seek to limit choice and to increase litigation, no matter how well intentioned, end up reducing access and increasing costs for the people who most need financial advice or assistance.

Overview

ERISA was enacted in 1974, and in 1975, the Department issued a regulation interpreting when an entity or person is a fiduciary for purposes of providing investment advice for a fee under ERSIA Section 3(21).[1] In 2016, the Department replaced the 1975 regulation with a new regulation that expanded the definition of fiduciary with respect to investment advice.[2] At the same time, the Department also issued a new Prohibited Transaction Exemption[3] and substantially revised others.

In 2018, the Court of Appeals for the Fifth Circuit found the 2016 final regulation to be arbitrary, capricious, not in accordance with law, and in excess of statutory authority and vacated the 2016 regulation.[4]

In the years since the Fifth Circuit ruling, the Department of Labor and the Securities and Exchange Commission ("SEC") have been embracing policies that increase access and choice, while also ensuring strong protections for investors and plan beneficiaries. On June 30, 2020, the SEC's Regulation Best Interest ("Reg BI") went into effect, significantly enhancing protections for retail investors, including ERISA plan participants and people seeking assistance with rollovers, while preserving their choice of financial service providers. Importantly, with Reg BI the SEC chose to preserve choice in the marketplace and maintain the separate investment advisor and broker-dealer models.

We appreciate that in the Proposed Exemption, the Department is similarly embracing a regulatory approach that permits choice and opportunity, reduces regulatory burdens and facilitates greater access to affordable investment assistance and products from a wide array of service providers.

---

[1] 40 Fed. Reg. 50842 (Oct. 31, 1975)
[2] 81 Fed. Reg. 20946 (April 8, 2016)
[3] See 81 Fed. Reg. 21002 (April 8, 2016).
[4] *Chamber of Commerce of the United States v. U.S. Department of Labor*, 885 F.3d 360 (5th Cir. 2018).

Today, nearly 750,000 ERISA-covered retirement plans holding roughly $10 trillion in assets provide retirement benefits to about 140 million workers and their families.[5] In the preamble to the Proposed Exemption, the Department noted that an estimated $2.4 trillion in rollovers from ERISA-covered Plans to IRAs were expected between 2016 and 2020.[6] These numbers illustrate the critical importance for workers and retirees to be able to access quality financial assistance when they decide to rollover a workplace retirement plan. The Proposed Exemption is a key step forward in making that help more accessible and affordable.

<u>The Intent of the Proposed Exemption Is Efficient and Effective Regulation</u>

Unnecessary regulation is a costly burden on our economy. In retirement plans, the cost of unnecessary regulation is borne by workers and retirees who are struggling to save for a secure retirement. That's why this Administration's commitment to promoting deregulatory actions has been so critical. The Proposed Exemption is yet another example of a regulation that complies with Executive Order 13771,[7] providing strong protections for retirement investors, yet doing so in a way that eliminates duplicative or contradictory regulatory requirements.

ERISA fiduciary investment advisors are not limited to one type of license or product. They can be investment advisors, representatives of broker-dealers, insurance producers or other types of financial professionals. In addition to complying with their own particular regulatory requirements, these professionals must also comply with ERISA's and the Internal Revenue Code's ("Code") specific rules. As a result of these simultaneously applicable regulatory regimes, compliance when advising ERISA plans and participants can be difficult and burdensome, increasing expenses that are passed on to retirement investors.

The Proposed Exemption is designed to harmonize the securities and ERISA and Code standards to the extent possible. Modeled on Reg BI, the Proposed Exemption enables broker-dealers and other securities professionals to more easily structure a compliance process that will meet both sets of requirements. This intentional approach to regulation—identifying common areas where similar requirements can be met with common documents or processes—facilitates investment assistance and advice in an area where more is needed.

[5] "Private Pension Plan Bulletin Abstract of 2017 Form 5500 Annual Reports Data," Employee Benefits Security Administration, July 19, 2019.
[6] 85 Fed. Reg. 40839 (July 7, 2020), citing a 2019 Cerulli Associates study.
[7] See, Executive Order 13771, Reducing Regulation and Controlling Regulatory Costs, 82 Fed. Reg. 9339 (January 30, 2017).

<u>Suggested Improvements to the Class Exemption:</u>

The Chamber reviewed the Proposed Exemption, and we believe its effectiveness can be enhanced with certain modifications. The Department requested comments on many issues in the Proposed Exemption, and we appreciate the opportunity to respond.

<u>Financial Institution Entity Definition</u>

The Department made it clear in the preamble to the Proposed Exemption that it intended the Exemption to apply to many different business models for delivering financial services. To use the Exemption, an investment professional must have a corresponding financial institution. The Proposed Exemption limits the definition of financial institution to banks, insurance companies, broker-dealers and registered investment advisors, but the Department asked for comment regarding other entities that should be considered. In particular, the Department asked about insurance intermediaries.

We appreciate the Department acknowledging that insurance carriers may contract with intermediaries such as independent marketing organizations ("IMO"), field marketing organizations ("FMO") or brokerage general agencies ("BGA") to provide supervision and oversight. We believe that the Department should also permit these intermediary entities to operate as financial institutions under the exemption if they wish to do so. We do not perceive any material risks to retirement investors from having these organizations serve in that capacity, and it would provide some additional choice and regulatory flexibility.

<u>The Proposed Exemption and Fiduciary Disclosure</u>

We appreciate that in modeling the Proposed Exemption on Reg BI, the Department was closely tracking the requirements of that regulation. In Reg BI and Form CRS, the SEC wanted to ensure there was no confusion about the capacity in which the broker-dealer was acting. This likely is the basis for Section II(b)(1) of the Proposed Exemption, which requires that before engaging in a transaction, a financial institution must provide "written acknowledgment that the Financial Institution and its Investment Professionals are fiduciaries under ERISA and the Code, as applicable, with respect to any fiduciary investment advice provided by the Financial Institution or Investment Professional to the Retirement Investor." However, we recommend removing the provision from the Proposed Exemption for the following reasons.

First, the purpose of the Reg BI and Form CRS disclosures is to prevent confusion about whether the advice is being received by a broker-dealer or a registered investment advisor. This purpose is irrelevant with regard to the Proposed Exemption.

Second, given the Department's new guidance, it may not always be clear at the outset whether a client relationship will involve ERISA fiduciary advice under the five-part test in the 1975 regulation. For example, the new guidance suggests that meeting the "regular basis" test will be very dependent on the facts and circumstances related to ongoing or anticipated ongoing relationships. As the Department writes, "…the rollover recommendation <u>may</u> be seen as the first step in an ongoing advice relationship that <u>could</u> satisfy the regular basis prong of the five-part test <u>depending</u> on the facts and circumstances" [emphasis added].[8] By making a financial institution disclose in writing that it is a fiduciary when it is not clear yet whether the investment professional or the financial institution are, in fact, fiduciaries, the Department forces the financial institution to choose to either acknowledge a status it may not have or forego using the Proposed Exemption it needs if fiduciary status is later determined. The Proposed Exemption should be available for use when fiduciary status if not yet clear if it is to function as the Department intends.

Third, the financial institution may not itself be a fiduciary in all circumstances in which the investment professional is a fiduciary. Because the Proposed Exemption is modeled on Reg BI, which was designed for broker-dealers, it does not contemplate the very different business models where the investment professional is independent of the financial institution and it is not reasonable to assume common fiduciary status.

Fourth, acknowledgment of fiduciary status under ERISA and the Code is irrelevant to the design and operation of the Proposed Exemption, which imposes a different "best interest" standard through the Impartial Conduct Standards. The Proposed Exemption protects participants and beneficiaries not through fiduciary status, but through its own conditions and requirements.

For these reasons, it is not appropriate to require a written fiduciary status acknowledgment before engaging in a transaction because it may reduce the ability to use the exemption without providing additional protection to retirement investors.

[8] 85 Fed. Reg. 40840.

Best Interest and Ongoing Monitoring

The Proposed Exemption does not generally require ongoing monitoring. We support that decision (and, of course, support allowing the investment professional and the retirement investor to mutually agree to include monitoring services in their arrangement). However, we are concerned by the preamble statement that "[i]nvestments that possess unusual complexity and risk, for example, may require ongoing monitoring to protect the investor's interests."[9] Just as the SEC determined not to impose monitoring obligations in Reg BI, we think the Proposed Exemption should not require monitoring unless the parties agree to do so. The unusual complexity or risk standard is not defined and will only introduce confusion as to when a monitoring obligation might arise. Rather than attempting to determine what investments are covered by this provision, we recommend striking it and leaving it to the parties to determine when they wish to contract for monitoring services.

Annual Report and Certification

Section II(d) of the Proposed Exemption requires the financial institution to review the effectiveness of its policies and procedures and to certify its compliance. The Department requires the chief executive of the institution to sign the report to ensure, "…that more than one person determines whether the financial institution is complying with the conditions of the exemption and avoiding non-exempt prohibited transactions."[10] The Department notes that "If the chief executive officer does not have the experience or expertise to determine whether to make the certification, he or she would be expected to consult with a knowledgeable compliance professional to be able to do so."[11]

While the Chamber appreciates the intent of these provisions, we are unsure as to how this heightened liability risk would improve the compliance of firms subject to the requirements of the Proposed Exemption. Should the Department ultimately decide that such a certification is necessary, then we think the goals advanced by this approach are best served by having the report certified by the chief compliance officer or equivalent official. As the Department acknowledges, the CEO is likely to have to consult a "knowledgeable compliance professional" in many cases. Given the Department's purpose in having the report inform improvement to the policies and procedures, requiring the chief compliance officer to fill this role will help ensure that the information is both understood and acted on by the financial institution.

[9] 85 Fed. Reg. 40843 (July 7, 2020).
[10] Id. at 40848.
[11] Id.

Eligibility

In the Proposed Exemption, a financial institution that is convicted of a crime under ERISA Section 411 is ineligible for the Proposed Exemption. A financial institution would also be ineligible if another financial institution within its control group is convicted of a crime under ERISA Section 411. Similar to the definition of controlled group of corporations under Code Section 1563, control group is defined as whether an entity has an 80 percent direct or indirect ownership.

Although we agree that a financial institution that is convicted of a crime under ERISA Section 411 should not be eligible for the Proposed Exemption, we do not believe that the conviction of one entity in the control group should per se make all other entities ineligible. Specifically, it is not realistic for the Department to expect that a financial institution will know whether an otherwise unrelated entity that happens to be part of the same control group has committed a crime triggering the 10-day review process with the Department. A common parent is not an indicator of any other connection between corporate entities. Financial institutions are often completely separate in every material way from other companies owned by a common parent.

The Proposed Exemption gives the Department strong enforcement authority to make inquiries if it has concerns. This authority seems sufficient to address any issues without automatically rendering ineligible a financial institution for something a different entity did and of which the financial institution was not aware.

Recordkeeping

Under the Proposed Exemption, a financial institution would be required to maintain records for six years that demonstrate compliance with the exemption and make such records available not only to the Department and its employees, but also, among others, "to any participant or beneficiary of a Plan, or an IRA owner that engaged in an investment transaction pursuant to this exemption" and such individual's authorized representative. Given the other required individual disclosures, we do not believe that it is necessary to require that a financial institution provide compliance disclosures to participants, beneficiaries, IRA owners and especially not to their authorized representatives. Such a requirement will not help individuals understanding of their investments, but rather will encourage the plaintiff's bar to make such request as fishing expeditions to spawn litigation.

<u>Principal Transactions</u>

While we appreciate the inclusion of certain principal transactions in the Proposed Exemption, we believe the definition of "Covered Principal Transaction" at Sec. V(c) should be expanded. This limited definition is a significant difference between SEC and Department requirements. Reg BI does not prohibit principal transactions, but instead the SEC addresses these issues through disclosure and consent. The same standard should be applied to the Proposed Exemption, and the definition modified accordingly.

<u>**The Comments Interpreting the Five-Part Test**</u>

We appreciate the Department's reinstatement of the 1975 regulations pursuant the Fifth Circuit's vacatur of the 2016 final regulation. Given that the court vacated the rule, no further action or interpretation of the 1975 rule is necessary. As such, we suggest that the preamble to the final Exemption exclude any reference to or interpretation of the five-part test.

The Fifth Circuit Court of Appeals noted that, "The 1975 regulation captured the essence of a fiduciary relationship known to the common law as a special relationship of trust and confidence between the fiduciary and his client…the DOL's original regulation specified that a fiduciary relationship would exist only if, *inter alia,* the adviser's services were furnished 'regularly' and were the 'primary basis' for the client's investment decisions."[12]

We are concerned that the new interpretation, which significantly changes the Department's historical views on the meaning of these key terms, eliminates the clarity of the prior interpretation. Under the new interpretation, it is very difficult to know when a particular recommendation would be ERISA fiduciary advice. Such an important issue should not be premised on potential future interactions that cannot be known with certainty at the time a recommendation is made. It is important that both retirement investors and investment professionals are able to follow a clear and administrable standard that is consistent with the decision by the Fifth Circuit.

---

[12] *Chamber of Commerce of the United States v. U.S. Department of Labor*, 885 F.3d at 365.

“Hire Me” Conversations

Under the five-part test, courts have clearly indicated that a financial professional urging a participant or IRA owner to hire her is not acting as a fiduciary when she “sells” her own services. We request the Department make clear that is not fiduciary advice and the Proposed Exemption is not necessary when a person is referencing her own hiring. Typically, when a financial advisor discusses a rollover with a plan participant, it is in the context of hiring that financial advisor to provide ongoing services via a brokerage or advisory IRA account or an IRA annuity. When a service provider is interviewing for a role, it is not reasonable for the parties to expect that a recommendation to be hired would form a primary basis for the client’s decision. Such a rule would turn long established fiduciary case law on its head.

Oftentimes, the financial advisor educates the client on the factors to consider as required by FINRA Notice 13-45 and then explains that the client must make the decision as to whether to roll over because the financial advisor either does not have adequate information to make a recommendation or does not want to move beyond education to investment advice. In such a situation there would not even be a recommendation let alone a mutual understanding that a recommendation would form a primary basis of any decision to roll over.

Regular Basis

We are also concerned by the Department’s interpretation in the preamble of how to apply the “regular basis” part of the five-part test, particularly as applied to a situation where the financial advisor has no relationship with the plan. The Department states that even if the IRA rollover recommendation was the first recommendation related to the participant, it could meet the regular basis test if the financial advisor intends to provide ongoing recommendations once the rollover to an IRA occurs. In such a scenario, there would be one, and only one, recommendation ever made with respect to the employer-sponsored retirement plan. Any further recommendations would be made to the IRA owner and would relate to the IRA. Therefore, the one-time rollover recommendation would not be part of an ongoing relationship with the plan sufficient to give rise to ERISA fiduciary status.

Also, if a financial advisor recommends that a client rollover from a 401(k) plan to a brokerage IRA (which recommendation must be made in the client’s best interest under Reg BI), that is a one-time recommendation with respect to the 401(k) plan and any advice provided thereafter would be with respect to the IRA and incidental where compensation received is for any transactions and not for the advice provided. In neither case would there be "on-going advice for a fee." The Department should make this clear in the preamble.

The Department appears to be attempting to interpret the term "regular basis" in a way that is not consistent with a plain reading of the regulation in order to expand the scope of ERISA's fiduciary advice with respect to rollovers. Not only does this raise significant concerns about the lack of clarity of the new standard, but it is unnecessary. Reg BI already imposes the best interest standard on rollover recommendations that the Proposed Exemption emulates. Recommendations related to annuities will be subject to the best interest standard in the modified NAIC model rule #275. Sales recommendations will not rise to the level of fiduciary advice in any case, as the Department acknowledges.

Accordingly, we ask the Department to rescind any references to the new interpretations announced on June 29, 2020 in the preamble to the final exemption.

Conclusion

We commend the Department's work on the Proposed Exemption and urge a rapid grant of the final Exemption with the adoption of our suggested modifications. We also urge that the new interpretation of the five-part test in the preamble be removed in the final Exemption to restore clarity and prevent confusion about the scope of fiduciary investment advice. We thank you for your consideration of these comments.

Sincerely,

Tom Quaadman
Executive Vice President
U.S. Chamber Center for Capital Markets
Competitiveness