U.S. DEPARTMENT OF LABOR

EMPLOYEE BENEFITS SECURITY ADMINISTRATION

PUBLIC HEARING:

DEFINITION OF FIDUCIARY INVESTMENT ADVICE

MARCH 1, 2011

Department of Labor Auditorium

U.S. DOL FRANCIS PERKINS BUILDING

200 Constitution Avenue, N.W.

Washington, D.C.

P R O C E E D I N G S

MR. LEBOWITZ: Good morning. I'm Alan Lebowitz, Deputy Assistant Secretary for Program Operations here at the Employment Benefit Security Administration. Welcome to our public hearing on the Department's proposed regulation defining who is a fiduciary for purposes of rendering investment advice to an employee benefit plan or plan participants and beneficiaries.

Prior to introducing today's hearing panel and an introductory statement from EBSA Assistant Secretary Phyllis Borzi, I will address a few procedural matters. Notice of today's hearing was published in the Federal Register on January 12th with an invitation to interested to testify on the Department's proposed regulation. In response to that invitation, the Department received 38 requests, each of which is reflected in the agenda for today's hearing, which also was posted on EBSA's website.

Those requesting to testify have been organized into 13 panels generally consisting of three panel members each. For purposes of today's hearing, each panel member will be allowed ten minutes to present their testimony, and let me just emphasize the importance of sticking to that schedule. We obviously have a very full agenda both today and tomorrow, and we want to make sure that everybody who's on the list has an opportunity to present their views.

Following the conclusion of the testimony, all panel members, the government panel members will be afforded the opportunity to ask the witnesses questions. With regard to panel questions, I wish to emphasize that the government panel members are interested in developing the public record as fully as possible, and accordingly, no inferences, conclusions -- or conclusions should be drawn from any questions from government panel members.

Witnesses will testify in the order in which they appear on the hearing agenda. To assist us today, we have a few requests of those testifying. First, prior to your testimony, please identify yourself, your affiliation, and the organization that you're representing, if any. Second, as I said a few seconds ago, please limit your remarks to the allotted time of ten minutes. And in this regard, we will call your attention to our timer, which will assist in monitoring your time.

At the end of today's hearing, we will keep the hearing record open for 15 days for those testifying who wish to supplement their testimony and for those who wish to submit comments, views, et cetera, that did not have an opportunity to testify today. All submissions will be made available to the public on EBSA's website.

Finally, I will note that today's hearing is being transcribed, and the hearing transcripts will be made available to the public on our website within the next two weeks.

Now I'd like to introduce today's panel. On my far left is Assistant Secretary for Employee Benefit Security Phyllis Borzi. Next to me on the left is Michael Davis, Deputy Assistant Secretary of EBSA. On my immediate right, Tim Hauser, Associate Solicitor, Employee Benefit Security Division. Next to him is Joe Piacentini, EBSA Director of Policy and Research. And next to him is Fred Wong, Senior Employee Benefit plan

Specialist in the Office of Regulations and Interpretations.

Ms. Borzi?

MS. BORZI: Thanks, Alan. I just want to say a few words to kick off this hearing this morning.

First I'd like to thank all the EBSA staff who have worked to so hard to make this hearing happen, and especially Susan and Luisa. And I want to thank all of you for coming today to participate in this hearing. In particular I want to thank our colleagues from the SEC who have been working closely with us as we develop this regulation and with whom we've been engaged in ongoing collaboration and coordination, not just on this regulation, but also on various other pension-related provisions in the Dodd-Frank Act where that new statute might intersect with ERISA issues.

I also want to welcome our colleagues from the CFTC, with whom we also have been working again to -- on the Dodd-Frank issues. Our goal is to harmonize both statutes. And so whatever sets of rules both agencies put out, the regulated community will have clear and sensible pathways to compliance with both statutes, and we're confident that this goal can be achieved.

So I want to thank again our colleagues at the SEC and the CFTC. We've been working with the SEC for many, many years. Our work with the CFTC is just beginning, so I'm happy to have them join us today, and we want to continue to work with them.

I want to just take one other moment to thank one other person who's not here on the panel with us today and who normally would be on the panel. And I see him in the back of the room, and he'll probably be very angry for me to say -- because I said anything about him. But I want to thank Bob Doyle, who many of you know has long been an employee of EBSA and for the past 20 years has headed our Office of Regulations and Interpretations. Bob has recently announced that he's leaving the Department at the end of this week, and so he isn't up here on the panel because he's recused from being on the panel. But I just want to tell you all how much we're going to miss Bob, and he knows we're going to miss him -- I, in particular. I met Bob in 1979. We had a dispute over a proposed reg, and nothing has changed (laughter) in terms of our not always seeing eye to eye. On the other hand, I have a complete and utter respect for Bob, his expertise, and will miss both his expertise and his voice as we move forward on this and other regulations. So Bob, I just want to publicly thank you.

(Applause) Okay. Let's get to the matter at hand. By way of background and to provide some context for today's discussion of this proposed regulation, I just want to take a minute to describe the current law.

As you know, ERISA provides a simple statutory test for determining who is a fiduciary by reason of providing investment advice. Under this test, a person is a fiduciary if he or she renders advice for a fee or other compensation, direct or indirect, with respect to any monies or any other property of the plan. In 1975, however, the Department adopted a regulation that severely cut back the application of this statutory definition by creating a rigid five-part test for fiduciary status. Under this regulation, before investment professionals can be held to ERISA's fiduciary standards with respect to their advice, they must first render advice as to the value of property or make investment recommendations. They must do this on a regular basis; they must do this pursuant to a mutual understanding that the advice will serve as the primary basis for investment decisions, and that that person will render individualized advice to the plan based on the particular needs of the plan. If the adviser meets any -- fails to meet even any one of these criteria, it is not a fiduciary. So for example, if a plan hires an investment professional on a one-time basis to advise it on the expenditure of a million dollars on a single complex investment, the adviser has no fiduciary obligations, because the advice was given on a one-time basis rather than on a regular basis as the regulation requires. So it makes no difference under this regulation as to how important or non-important this particular advice was with respect to the plan.

You know since the Department promulgated the regulation in 1975, dramatic changes in the retirement marketplace have occurred, including the increased importance of investment advice. As you know, we have spent a good period of our time focusing on this question of investment advice. Our own experience with the regulations have led us all to question whether this 1975 regulation is still appropriate. And as you know, under the new executive order, we are directed to go back and look at all of our regulatory and other guidance to see whether they are still valid and useful, and this is part of that process.

As in most matters since 1975, the world has changed, including significant changes such as the introduction of 401(k) plans in 1978, three years after the current regulation was adopted. The shift from DB plans to DC plans; an increase in the types and complexities of investment products and services available both to plans and to IRA investors in the financial marketplace. This regulation addresses the conduct of investment advisers in both the plan and IRA context since, as you know, EBSA has long had the ability to regulate prohibited transactions in IRAs, although the enforcement for violating those provisions lies in the excise tax imposed by our colleagues in the Internal Revenue Service.

In enacting ERISA, Congress recognized that the security of American retirement plans depends on its fiduciaries. ERISA protects retirement benefits by holding important plan actors to fiduciary standards, protecting workers and retirees from conflicts of interest and providing remedies for violations. Thus, it's vitally important when we define important terms, like who is a fiduciary, we get it right.

The proposed regulation that we issued last October and the hearing we're holding today are part of our determined effort to get it right. We believe that the types of advisory relationships that give rise to fiduciary duties should be reexamined and that the rule should be updated so that plan fiduciaries receive the impartiality they expect when they rely on their adviser's expertise and advice. In so doing, we want to be sure that we have the information that we need to create a regulation that accomplishes this purpose and makes sense in the context of today's retirement plans and investment advice environment. We've already received 200 comment letters. Maybe some in this room besides us have read them all. And of course all of these are posted on our website.

We're now ready to continue the dialogue that we intend to have in order to get this right by adding your views on this proposal and adding your testimony to the public record. And as Alan noted, the hearing record is going to remain open for 15 additional days so that those of you who will testify today and tomorrow and those of you who haven't testified will have the opportunity, again as the executive order directs us, to have people comment on the comments on the comments. So there will be ample opportunity for public input here. And after the hearing is over and the record closes, we're going to work through the issues that have been raised both here in the comments and the various meetings that I know will be coming after the hearing is over. We're going to thoughtfully and carefully evaluate the suggestions and concerns we have heard. We're going to continue the dialogue with the regulated community, and we're going to refine the text of proposed regulation -- because after all, that's all it is, is a proposed regulation -- so that we'll be ready to issue final regulations by the end of the year in accordance with the timetable that we have announced publicly.

So again, I want to thank you all for your participation and your input, and so let's just start with the witnesses, Alan.

MR. LEBOWITZ: Thank you.

First panel, please: Norman Stein, Karen Prange, and Anne Tuttle.

MS. BORZI: I should have said one other thing, which is that I'm going to try to be here for most of today and tomorrow, and I apologize in advance to the witnesses whose hearing I won't actually -- whose testimony I won't actually hear, because I do have a couple of things that I have to do, to leave. But rest assured that my colleagues will brief me on what you said, and if you have any written statements, I'm going to be reading them.

MR. LEBOWITZ: Mr. Stein?

MR. STEIN: Good morning. I'm Norman Stein, and I'm testifying today on behalf of the Pension Rights Center. The Center is a nonprofit consumer organization that has been working since 1976 to protect and promote the retirement security of American workers and their families. The Department deserves high praise for these proposed regulations, which would replace current regulations adopted in 1975 that tightly circumscribe the circumstances under which a person or entity becomes a fiduciary when providing investment advice for a fee. The original regulations were not compelled by the statute, and in our view reflected an improper agency narrowing of the statutory language and congressional intent. In addition, as the Department suggests in its preamble, economic and legal developments in the field of investments and employee benefit plans have rendered the 1975 regulations anachronistic and at times at cross-purposes with the statute.

My statement today will cover five points: First, that the current regulations improperly constrict the statutory definition of fiduciary. Second, that the current regulations were promulgated in a different economic and legal environment than today, and as a result sometimes fail today to shield unsophisticated participants in retirement plans from investment advice tainted by conflicts of interest. Third, that the proposed regulation should not condition fiduciary status on whether a person provides individualized investment advice. Fourth, that the sales limitation on the definition of fiduciary status should not apply to advice given to participants. And fifth, that advice about distributions should be considered investment advice.

ERISA provides straightforwardly that a person is a fiduciary if he renders investment advice for a fee or other compensation, direct or indirect, with respect to any monies or other properties of such plan. In 1975 -- the 1975 regulations, however, narrowed the scope of this language by limiting fiduciary status to persons rendering investment advice that is regular, rather than one-time or episodic; that is given pursuant to an agreement or understanding that it will be a primary basis for investment; and that it is individualized to the particular needs of the plan. These limitations are not consistent with the plain meaning of the term "investment advice," and at least in retrospect can be said to have impeded the congressional goals of limiting self-dealing and of assuring prudent investment to plan assets. As the preamble to the proposed regulations notes, people providing investment advice not covered by the current regulations have considerable influence on the decisions of plan fiduciaries and participants, and yet can have conflicts of interest that result in lower returns and thus less retirement income.

The existing regulations were promulgated in 1975 at the dawn of the ERISA era. Since then, there have been significant changes in the retirement plan and investment landscape that have undermined whatever arguable justification there might have been in 1975 for the regulation's cramped scope. As the preamble to the proposed regulations notes, there has been a seismic shift in the retirement plan world, from defined benefit plans in which investment advice was generally rendered to sophisticated plan fiduciaries, to self-directed defined contribution plans in which investment advice is issued to individual participants, including my mother, many of whom have only rudimentary financial literacy.

Mutual funds and sellers and brokers for mutual funds who played a relatively small role in retirement plans at the time ERISA was enacted have become dominant players in the new economic order. The variety and complexity of investment products has also increased markedly over the last three decades. There have also been significant and unanticipated legal developments since the time the 1975 regulations were written. The Supreme Court in 1993 ruled that a participant generally is entitled to legal relief under ERISA only against a defendant who is a fiduciary whose breach of duty caused monetary loss to a plan. Legal relief is not available against a non-fiduciary even when that non-fiduciary knowingly and for personal profit assisted a fiduciary in the commission of such a breach. A participant can sue a person other than a fiduciary only for equitable relief, and the Supreme Court has narrowly circumscribed the extent to which equitable relief is available.

The Department of Labor, which filed amicus briefs arguing against these positions, could not have known in 1975 that the combination of its narrowly drawn regulation and ERISA preemption would effectively create a largely unregulated playing field for so many actors who have a direct and substantial impact on plan investment performance.

Another important change is simply the growth of assets held by qualified retirement plans. In 1975, defined benefit plans and defined contribution plans held $300 billion in assets. In 2007, qualified plans held over $6 trillion of assets, and this figure does not include individual retirement accounts. Retirement plans are thus today a critical market for virtually all serious capital market participants. It is simply where the money is. Notwithstanding a somewhat broader definition of the term "fiduciary," vendors of investment products and financial advisers will continue to serve the retirement plan market, even if they now will be required to provide prudent and impartial investment advice. Those who are unwilling to meet such a standard, in our view, have no business advising retirement plan participants on how to prepare financially for retirement.

The proposed regulations make a person who issues investment advice a fiduciary only if the advice is individualized to the needs of the plan, a plan fiduciary, or a participant or beneficiary. We are not certain why a person should be a fiduciary only if his advice to a plan or beneficiary is sufficiently individualized. Many plan participants and beneficiaries will be unable to discern a difference between individualized and non-individualized advice. Moreover, this aspect of the regulations may provide perverse incentives to some providers of investment advice to avoid tailoring their advice to the particular needs of the individual for the very purpose of avoiding fiduciary status.

At least with respect to participants, we would prefer that the regulations provide that advice that is directed to a particular participant to purchase or sell a particular security is investment advice, even though not necessarily individualized to the particular needs of the participant. If the final regulations take this position, as we hope it will, the Department can clarify in the preamble to those regulations that this will not prevent the furnishing of non-fiduciary investment education so long as the participant is not given specific investment recommendations.

The proposed regulations also provide that a person shall be considered to be a fiduciary investment adviser if such person -- I'm sorry, will not be considered a fiduciary investment adviser if such person can demonstrate that the recipient of the advice knows or under the circumstances should have known that the person who's providing the advice or making the recommendations in its capacity as a purchaser or a seller of a security or other property, whose interests are adverse to the interests of the plan or its participants or beneficiaries, and that the person is not undertaking to provide impartial investment advice.

While we believe that this limitation may be appropriate when such advice is provided to a sophisticated plan fiduciary, it is not appropriate when the advice is given to individual participants or their beneficiaries. The Center has worked with participants for 35 years, and based on our experience, it is our view that many plan participants will simply be unable to discern when advice is impartial or conflicted. In addition, even if there is express disclosure of a fiduciary's conflicts in a one-on-one meeting, whether in phone or by person, an unsophisticated investor will often regard the adviser as acting in his interests, notwithstanding the disclosure. Indeed, an adviser salesperson's success may depend on whether he can create in the customer the belief that the adviser is interested primarily in the customer's welfare, despite a declaration by the adviser of self-interest.

There is the further fact that most participants will not be knowledgeable about the types of fees and benefits that can accrue to the purchaser or seller of securities, and thus may not be able to evaluate the extent of the adviser's conflicts. Thus we strongly urge the Department to revise the seller limitation so that it only applies to advice and recommendations given to sophisticated plan fiduciaries.

The Department asked for comments on whether and to what extent the final regulation should define the provision of investment advice to encompass recommendations related taking a plan distribution. A recommendation to remove assets from the plan and invest them elsewhere is in effect a judgment about the relative merits of the plan options and the other investments. The person making the recommendation can have interests adverse to the plan participant, and the recommendation can have a substantial effect on a participant's retirement security, not only because of future investment performance but also because of the loss of an economically efficient means of taking retirement income and annuity form and tax considerations.

Moreover, under the current interpretation of the Department, the person giving advice in these circumstances has no obligation under ERISA to reveal conflicts of interest. We thus believe it is essential that the regulations treat advice on plan distributions for what it is -- a type of investment advice.

In sum, this is a much-needed regulatory change that will better protect plans and plan participants and facilitate more effective enforcement when misconduct is uncovered. The Pension Rights Center applauds the Department for pursuing this initiative that will benefit both the retirement plans and their participants and beneficiaries.

Thank you for the opportunity to be here this morning, even if I went ten seconds over.

MR. LEBOWITZ: Thank you.

MS. PRANGE: Good morning. I'm Karen Prange, Executive Director and Assistant General Counsel for JP Morgan Chase and Company. I'm here today representing our retirement plan services and worldwide security services lines of business.

We believe that the proposed regulation should be modified and re-proposed to eliminate unnecessary and subjective standards. Rather than determining whether a person is impartial or has adverse interests, the regulations will better serve plan sponsors and participants by requiring objective written disclosures from service providers, regardless of whether or not they will be acting in a fiduciary capacity. To enable plan sponsors and participants to continue receiving valuable services from providers, JP

Morgan also believes the various limitations described in the proposed regulation should be expanded or clarified to clearly exclude non-discretionary administrative services and distinguish between the provision of information and advice.

Finally, we believe that existing standards governing plan distribution, education and guidance are sufficient and need not be modified in the final regulations.

We would first like to address the potential industry impact of having the provision of information regarding plan distribution options swept into the fiduciary definition. The standards articulated by the Department in advisery Opinion 2005-23A are both appropriate and workable. Participants contacting a record-keeper's call center generally do so to obtain basic factual information about the plan, including its distribution and investment options. The analysis in the advisory opinion recognized that in most cases, answering questions and providing plan information about rollovers and other distribution options are ministerial functions, and participants will not have established any kind of trusting fiduciary relationship with the representative who assists the participant. Record-keepers must be able to provide information to participants about their rights to receive or defer a plan distribution and related concerns, such as tax consequences and rollover vehicles like IRAs, in the same manner as they are able to provide information regarding other plan features, such as contribution rights and the availability and related tax consequences of loans or hardship distributions, without becoming subject to ERISA's fiduciary requirements.

Next I would like to address the sales exception. We believe that the adverse and impartial standards as currently drafted are too vague. We propose that the applicability of the sales exception should turn on whether the service provider and plan sponsor understand that the advice is being provided in a sales context. Such an understanding could be imparted through a written disclaimer that the service provider is acting in a non-fiduciary capacity.

Also, record-keepers are frequently asked by plan sponsors to develop proposed investment fund menus during the sales process. These proposed menus are sometimes used to create a uniform basis upon which the fees of various record-keepers may be compared. The Department should clarify in the final regulations that developing such proposed fund menus does not constitute investment advice that gives rise to fiduciary status.

We believe the written disclosure standard for application of the platform exception is generally appropriate, but suggest that the Department expand this exception to apply to any objective data that a service provider supplies to the plan sponsor for the purpose of monitoring a plan's existing investment funds for all types of plans, as long as the provider does not make a specific investment recommendation based on the data. Narrowly interpreting this exception could deny plan sponsors and fiduciaries valuable tools for monitoring their plan investments. Further, the Department should expand this exception by either removing or clarifying that the exception is applicable when a service provider makes securities or other property available without regard to the individualized needs of the plan. Plan sponsors often ask record-keepers to create sample fund line-ups from the investments available on the record-keeper's platform to evaluate sales or marketing proposals. But by its very nature, this information may be deemed to take into account the individualized needs of the plan. However, if the information provided is accompanied by a disclaimer regarding the record-keeper's non-fiduciary status, it should not be considered the provision of investment advice.

Elimination or at least clarification of the individualized need standard is even more warranted in the context of the selecting or monitoring exception. Information supplied by a service provider for the purpose of assisting plan sponsors in monitoring the plan's investments would be meaningless if that information does not consider the individualized needs of the plan. As long as the information does not include a specific recommendation for a fund and does not include a disclaimer -- excuse me, and does include a disclaimer similar to the one previously mentioned, it should not be considered investment advice.

We also suggest that the selection or monitoring exception be decoupled from the platform exception. Currently the selecting or monitoring exception is tied to the activities described in the platform exception, so it appears to apply only to participant-directed defined contribution plans when sponsors of all types of plans rely on data and analysis to fulfill their fiduciary oversight obligations. For this purpose, service providers can provide various types of analytic and reporting services to plan sponsors based on the information and data they maintain. These services do not involve any discretion by the provider. Rather, they involve comparisons of plan data to criteria designated by the plan sponsor or the application of standardized algorithms such as comparing an investment manager's performance to a benchmark, reporting to a plan sponsor if an investment does not meet a manager's guidelines, or the generation of a list of potential investment managers based on plan sponsor specifications. In all cases, the service provider's analysis or reporting provides information to the plan sponsor, but contains no recommendations regarding actions that might be taken based on that information.

Therefore, we believe the Department should clarify in the final regulations that all non-discretionary analytic and reporting services do not constitute investment advice. Lack of such clarity may lead service providers to discontinue valuable non-discretionary analytic and reporting services.

With respect to the exception regarding preparation of general reports or statements, we suggest that the exception apply to any report or statement that merely reflects the value of an investment, regardless of whether the report or statement is provided due to regulatory requirements or on a continuous basis for a plan sponsor or participant's convenience. We believe the proposed regulation should make clear that service providers, such as trustees and custodians, reporting valuations of hard-to-value plan assets are not providing investment advice under ERISA. Service providers do not independently value these assets, nor do they typically review the valuations provided by third parties except to test the valuation's reasonableness based upon a standardized process. The service providers simply report the values provided by third parties without the exercise of discretion.

We urge the Department to revise the regulations to ensure that the standards for determining whether a service provider is a fiduciary are clear and objective, to enable providers to determine in advance whether or not their activities are fiduciary in nature and to design and implement their business model based upon whether they intend for their activities to be fiduciary activities and to avoid potential litigation due to uncertainty. The scope and generality of the proposed regulations will cause functions that were previously considered ministerial to become fiduciary, forcing service providers to reconsider the authoring of the services and related fees to address the increase in risk and oversight requirements.

Finally, we are concerned that a service provider may fall within the definition of a fiduciary merely because it has an affiliate that is a registered investment adviser. When a service provider offers a service and presents itself as a fiduciary with respect to that service, it should be subject to the fiduciary requirements of ERISA. However, we urge the Department to provide in the regulations that a service provider that offers an administrative service and provides a written representation that it is not acting as a fiduciary with respect to that service should be presumed not to be a fiduciary with respect to those services. Such a disclaimer puts the parties on notice that there is no mutual understanding that the services are intended to be fiduciary in nature, creates a clear delineation between the plan sponsor and service provider responsibilities, and will prevent dramatic increases in uncertainty and litigation based on after-the-fact claims of an understanding that a service provider's communication relating to plan assets could be considered investment advice.

I appreciate the opportunity to appear today on behalf of JP Morgan. Thank you.

MR. LEBOWITZ: Ms. Tuttle.

MS. TUTTLE: Good morning, and thank you for the opportunity to testify today. My name is Anne Tuttle, and I'm here today as the general counsel of Financial Engines.

We applaud the Department's proposal to update the definition of fiduciary. We support the Department's objective of improving protections for participants and beneficiaries. We applaud the Department for confirming that persons providing individualized investment advice be subject to ERISA standards of fiduciary conduct. We share the concern that the current regulation may no longer adequately protect the interests of participants. ERISA's fiduciary standards provide important protections against conflicts of interest and self-dealing. And particularly in light of changes in the financial industry, it is timely to reexamine the types of investment advice that should give rise to fiduciary duties under ERISA.

As the Department has pointed out, it's a 35-year-old rule. Thirty-five years ago when this regulation was adopted, financial engines did not exist. I was still in middle school. Our co-founder, Bill Sharpe, had not yet been awarded the Nobel Prize in Economics. But today, Financial Engines is the nation's largest independent investment adviser. Financial Engines launched its first advice service in October 1998 as it set out to accomplish Bill Sharpe's vision -- to provide high-quality, independent investment advice to everyone. There are other significant changes in the financial services industry and also in the role that 401(k) plans play in our society. The Department recognizes the need to respond to these changes by taking another look at the regulation.

From our perspective, it is both important and feasible that participants and plans be represented by those willing to act as a fiduciary. We work with eight of the largest retirement plan providers serving the defined contribution market to make our services broadly available. We offer services to plan participants through leading employers, including 129 of the Fortune 500, reaching over 7.3 million participants. To meet the needs of different investors, Financial Engines provides both discretionary investment management through a managed accounts service and non-discretionary investment advice through a non-aligned advice service. We act as fiduciary to the plan participants under both ERISA and the Investment advisers Act. Our managed accounts service also includes income-plus, which provides steady monthly payouts from a 401(k) that can last for life.

Today I wanted to discuss several aspects of the proposed regulation. The proposed regulation provides that investment education, information, and materials as described in Interpretive Bulletin 90-61, will not constitute investment advice under ERISA. Investment education is a valuable way to offer help to participants. However, we know that investors are confused about the roles and responsibilities of different financial professionals. Thus, we are concerned that an overly broad exclusion for investment education may not account for certain industry practices and the expectations of participants and beneficiaries when they are provided information and materials that are not generic in nature. Because participants who receive specific and tailored recommendations likely perceive those recommendations as advice, rather than general education, providers of such specific recommendations should be treated as fiduciaries under ERISA. The Department should specify that the exclusion for investment education will not apply where specific investment recommendations are provided. These modifications would help to provide clarity about what constitutes investment education and help to ensure participants and beneficiaries who take action based on customized recommendations are not left without ERISA's fiduciary protections.

The proposed regulation also provides that a person will not be considered a fiduciary with respect to the provision of advice or recommendations if such person can demonstrate that the advice recipient knows, or under the circumstances reasonably should know that the person is providing advice in the capacity of a seller or purchaser of a security or other product whose interests are adverse to that of the plan or participants, and that the person is not undertaking to provide impartial advice. Individual plan participants should not be expected to know that advice given with respect to securities and other products is not impartial.

We recommend that the Department modify the proposed limitation so that the exception does not apply where the recipient of advice pertaining to a security or other product is an individual plan participant. Alternatively, the limitation should more precisely describe the burden that must be met by a seller who seeks to avoid fiduciary status by claiming that an advice recipient should have known that the advice was not impartial.

We also note the Department's request for comment on advice regarding plan distributions. It's difficult to distinguish distribution advice from education and information, and several commenters have identified issues of fine-tuning that are worth examining. In other contexts, the Department has recognized that a buyer and seller of products cannot always stand in a fiduciary relationship. This appears to recognize a distinction for the activities that inform plans and participants of what is available to them. It doesn't necessarily follow that one is adverse by offering services to plans and plan participants. It should be permissible to offer additional services even if a preexisting fiduciary relationship exists. But once there is an agreement to provide a service, whether that agreement is with the plan on behalf of the participant or directly with participants, and if the subject of that agreement is to provide investment advice as defined in the regulation, the service provider should act as a fiduciary.

Finally, the Department notes uncertainty both as to the potential costs of the proposal, such as whether service provider costs would increase, and whether the service provider market could shrink because of concerns about higher costs. Financial Engines believes that our history and growth support the conclusion that it is neither onerous nor impossible for service providers to provide high quality investment advice in a fiduciary capacity to large numbers of plans and participants.

Financial Engines appreciates the opportunity to comment on the proposed regulation, and we support the Department's actions in seeking to better protect participants and beneficiaries. We welcome the opportunity to work with the Department and to provide any further assistance that may be useful.

MR. LEBOWITZ: Thank you.

MS. BORZI: Mr. Stein, you suggested that the seller exemption that we have in the regulation should be limited to sophisticated plan fiduciaries. Do you have some advice as to how you might define that or thoughts?

MR. STEIN: What, the investment advice? Well, I used the word "sophisticated" in hopes that that question wouldn't be asked.

(Laughter)

It does seem --

MS. BORZI: I wouldn't even consider myself sophisticated.

MR. STEIN: In discussions on the testimony, we thought there was a pretty clear -- and I think some of the comments that you received from small plans reflect this -- that there's a difference between a fiduciary for a plan sponsored by General Electric who's making decisions and a decision made by my brother who's a doctor and has a small plan for six people. And, you know, it's -- one way of approaching it, and we toyed with talking about this but decided not to, is to have the standard that has to be satisfied by the seller be more specific and include consideration or suitability of the advice to the particular fiduciary, what the fiduciary would fully understand the advice. So that's -- that's I think about as much as I could probably safely say now, although we could think about it some more and ....

MS. BORZI: Yeah. If you think about it some more, that would be useful for us to -- for you to give us that information.

Is Prange --

MS. PRANGE: Prange.

MS. BORZI: Prange, sorry.

MS. PRANGE: We like to use every letter. Okay.

MS. BORZI: You suggested that the solution to -- to some of thee things, particularly to the sales exemption, would be to allow a written disclaimer: I am not a fiduciary. Well, (a), I'm not sure that most participants know what that really means; but (b), the -- put aside the current regulation, the statute creates a functional test. So when a court decides whether somebody's a fiduciary or not, when the Department in its investigations and litigation decides whether somebody is a fiduciary or not, the decision is based on what they do, not what they call themselves. So how do you square that with your written disclaimer? When I was in private practice, I used to X out a lot of these written disclaimers in service provider contracts and simply substitute the statutory words.

MS. PRANGE: Hm-mmm.

MS. BORZI: So how -- how would you square that? How would --

MS. PRANGE: It would not be our intention that a disclaimer would supersede the actual performance of the service provider. I'm not -- we're not taking a position that the functional test should be eliminated or that if someone does act and engage in a fiduciary function, that they shouldn't be held to the standards. Our goal would be to have a disclosure regime that sets a level playing field at the onset of the relationship of what it is, what the intention is of the parties and what the role is intended to be of the service provider. But we agree that if the service provider then goes beyond those guidelines, that intended function, that they should be held to the fiduciary standards.

MS. BORZI: Okay. And how would, for instance, a participant know that? I mean, if you're their trusted financial adviser and you give advice which is -- crosses that line, how would the participant know that the line would be crossed?

MS. PRANGE: Well, I think in an individual participant situation, one of the issues with service providers such as JP Morgan is in our call centers, we have hundreds of employees who are engaging with plan participants across several plans. So we question first and foremost the building of that trusted relationship by a record-keeper such as our firm. I think that if the individual does reach out and builds that type of a relationship with someone, if there is a service provider who's offering an advice service or a managed account service where it's intended for that, then there's the expectation. But I think that we need to manage the expectation of plan sponsors and participants in the basic plan information that's delivered to them through the call centers in guiding them to proper decisions that they need to make.

MS. BORZI: Well, do your plan sponsors come in through the call centers as well? Don't you have a more personalized relationship with your plan sponsor clients?

MS. PRANGE: We do. We have specific relationships that are developed through client advisers, through relationship managers, and in that case as you said earlier, a plan sponsor is different than a participant. They are generally going to be somewhat more sophisticated, although maybe not a sophisticated investor. They are going into the marketplace and seeking services and investment options for their plan, and they need service providers like our firm who can bring information to them on which they can base their fiduciary decisions. But our position is that bringing that information and helping to educate plan sponsors and support them in those decisions is an appropriate place for a record-keeper such as our firm to sit in. If a participant -- I'm sorry, a plan sponsor -- feels that they are not sophisticated enough to make the decision on their own, we don't disagree that they should hire an investment adviser for that purpose to assist them in making that decision.

MS. BORZI: Who will be a fiduciary.

MS. PRANGE: Who will be a fiduciary.

MS. BORZI: Ms. Tuttle, you get a bye because you actually answered the question I was going to ask you about costs and burdens.

MS. TUTTLE: Excellent. Thank you.

MS. PRANGE: Good job.

MR. DAVIS: Mr. Stein, you said investment advice should not have to be individualized to qualify as sort of a fiduciary act. What specific advice would you give the Department on where to draw the line between investment education and investment advice in that context?

MR. STEIN: Well, in our written comments, what we suggested was that the test really be whether specific investment advice is directed to a particular participant rather than -- what our concern was with individualized investment advice is that if the advice -- if the person giving the advice doesn't really understand the needs of the participant, that would be -- that would not be investment advice if they had -- if they weren't aware of the particular needs of the individual with respect to their portfolio, and they were just making recommendations to everyone about a particular security, that that would not be individualized. So what we -- what we suggested was the test really should be whether there was advice concerning a specific investment directed to a participant or beneficiary. And that can be a definition of individualized, we -- we think.

MR. DAVIS: Okay. Thank you.

And then Ms. Prange, you talked about just the challenges that the reg as proposed would create. But you and Ms. Tuttle seem to disagree on whether the availability of advice would be affected. Was the basis of your comments that the regulation as proposed would actually reduce the availability of high quality advice? Do you think providers would be disincentivized to provide advice in this context?

MS. PRANGE: I don't think that they would be disincented to purposefully provide investment advice, either through an advice product or a managed account product. Our concern is that if the -- if the final regulation is not more specific, that those who provide investment guidance and education, data, may not provide as much or broad of information if the line is not clearly defined. We believe we need to provide in the marketplace the opportunity to provide information and guidance and education to both sponsors and participants alongside fiduciary products like advice and managed accounts.

MR. DAVIS: Ms. Tuttle, would you agree with that?

MS. TUTTLE: Yes, I think I agree that there is a distinction between investment education and investment advice. And it's not always easy to draw that line crisply. But I think looking at those concepts of is it directed to the participant; does it take into account participants' own circumstances, would be things that I would look to to say if you're doing that and you're making a specific recommendation, that you are then offering investment advice and should do so as a fiduciary. But it is completely permissible for folks to provide investment research or to otherwise educate the market, and participants may gain access to that. We hope that participants are looking -- reading the Wall Street Journal or otherwise trying to educate themselves about the choices they face. And I would agree that we want to encourage those kinds of activities and allow people to generally offer education about asset classes and risk and return and diversification without fearing that they must be a fiduciary to somebody with whom they may not have a personal or direct relationship.

MR. DAVIS: And one more question. In the preamble, the Department talked a lot about the change in age of the marketplace, the increasing need for high quality advice, in particular with respect to participant-directed accounts. What indicators are you guys seeing with respect to the reliance of participants on advice? Are you seeing greater reliance on advice? Have you seen markers that would suggest that this advice is even more important in the context of the products that you deliver today?

MS. TUTTLE: Yeah. I think we have seen several studies do show that participants are both requesting advice, that there is some gaps in the financial literacy of many of Americans. And I think we do see that when advice is offered, it can improve the retirement outlook for many of the investors who are taking advantage of that advice.

MR. DAVIS: Ms. Prange, would you agree?

MS. PRANGE: I would. And I would add in addition to the participants' uptake on the products available, the plan sponsors embracing the products and using them in a QDIA circumstance has been very encouraging, as well.

MR. DAVIS: Thank you.

MR. HAUSER: I just have a couple of questions. But one thing that strikes me, and tell me if I am wrong -- it seems to me that all three of you agree that specific recommendations as to purchasing, holding, selling, lending, whatever ought to be treated as investment advice, assuming at least that the adviser isn't on the opposite side of the transaction from the participant. Is that right?

MS. TUTTLE: Yes.

MS. PRANGE: Yes.

MR. HAUSER: And so -- but there seems to be a disagreement beyond that about what should count -- what should count as having kind of the requisite -- I don't know what. Well, there seems to be a disagreement beyond that about what ought to count as advice, whether it needs to be individualized, what individualized might mean. But I'm not sure I exactly appreciate what the scope of that disagreement is. And so maybe, for example, starting with you, Mr. Stein -- a number of the commenters have worried that absent an individualized sort of requirement, things like analysts' reports, newsletters, you know, these kind of general documents that aren't really aimed at a particular person for advice in a particular context might get picked up by the reg. Do you think those sorts of things should get picked up?

MR. STEIN: Generally no, and I don't really think they would be picked up. I think a newsletter that doesn't -- that just provides information about various securities and doesn't say "buy this one" is not investment advice. I know a number of the commentators are concerned about those kinds of questions, but I -- you know, I think you can read far too much into these regulations, and at least in my view, courts have not been unusually sympathetic to the fringe kinds of claims that some people fear would be made.

MR. HAUSER: Okay. And then Ms. Prange, I assume you agree a hundred percent with that statement. Is that --

MR. STEIN: I think that's a joke.

(Laughter)

But --

MS. PRANGE: Perhaps I can say I don't disagree.

MR. STEIN: Okay.

MS. PRANGE: I think our perspective on it would be we have hundreds of employees in our call center. We train them; we educate them today, based on 96-1 and other guidance on giving participants education and guidance. We clearly don't want, as you've said, them inadvertently crossing a line that now takes our firm into a fiduciary standard, just because they're having a conversation with an individual participant. It would not be our goal that they would be giving individualized, specific recommendations of "invest in Bond Fund A." There may be the opportunity for the development of a distribution product similar to the advice and managed account products that have developed over time that could be a fiduciary service. But it needs to be clearly defined service with the investment advice functions within the service, and not inadvertent through a discussion one time with an individual participant.

MR. HAUSER: And so, is the line you're drawing or trying to draw with respect to these call center folks and the like centered on, you know, sort of answering ministerial sorts of questions about what the plan provides, what options are available to you, as opposed to actually making recommendations about how to invest your money? Is that --

MS. PRANGE: That's correct. We would not engage, we do not engage in specific recommendations to participants. We need the opportunity to discuss with them not only the investment options that have been made available in their plan for them to select from and the different characteristics of those, but also the plan provisions, including distributions and upon termination, what options do you have as a form of distribution, including leaving assets in the plan, taking a lump sum distribution, rolling funds over to an IRA provider.

MR. HAUSER: But not including recommendations as to, you know, what IRA provider to roll the money into or what investment option the money should be rolled into? Or --

MS. PRANGE: Definitely not from a service provider perspective to make a recommendation as to what investment those funds should ultimately end up invested in, whether it be a bond fund or an equity fund. Discussing with plan participants and helping them to navigate the options for distribution, including how to evaluate where they might go for rollover services, we think should be within the context of education and guidance. Many participants have come to the conclusion that they're going to take a distribution from the plan. They work through the tax implications and the poor decision of taking a lump sum distribution. They evaluate the plan's provisions and the investments that are available there and make a determination that they don't want to remain in the plan and need some opportunity to say, "Where would I even go for an IRA?" You can go to your own financial institution; you can go to other providers in the marketplace for those products.

MR. HAUSER: Thanks. And then one more question. And you also testified about advice with respect -- record-keeper sort of advice with respect to the fund line-up on a plan's investment menu. And again, if you could just maybe explain with a little more precision where you think that line ought to be drawn? I mean, for example, if the advice being given is "You should look at these specific funds," or "This is an especially good fund to be on your menu," would you say that advice also shouldn't count as fiduciary advice? Or are you trying to draw the line somewhere south of that?

MS. PRANGE: I think it would be predicated based on the information that the service provider has and on which they make that -- that statement. I'll use recommendation loosely here; right? Generally in our business, the plan sponsor will look to us to look across our platform and provide them information about funds that fall within certain criteria that they have identified. They're looking for a new bond fund, or to add a bond fund. So bringing forward what is available on our platform based on the criteria that the plan sponsor has set or current industry criteria, such as benchmarking, performance, fees, we believe should not fall within a fiduciary definition.

MR. PIACENTINI: Mr. Stein, at the beginning of your testimony you said that where advice is given in the presence of conflicts, an effect can be to have lower returns and lower retirement income. So my first question is, did you mean to apply that observation in plans and IRAs both? Both where the advice is given to individual participants or IRA owners and where it's given to plan fiduciaries?

MR. STEIN: Well, again, I think you come to the question about whether a plan fiduciary is sophisticated or not. But I think that the types of advice given by somebody with conflicts can -- can result in lower returns. And, you know, we know that similar funds somehow manage to charge very different fees, and the market doesn't seem to provide sufficient information to at least participants to really be able to measure that very easily.

MR. PIACENTINI: I think --

MR. STEIN: It's not a perfectly functioning market, I don't think, for these products.

MR. PIACENTINI: So I think I heard you say that it can have these effects. Is it your view or your experience that it does have such effects? And are those effects common and large, or not common and not large?

MR. STEIN: Well, I think there was -- wasn't there a GAO report on -- issued, I think it was in last year or 2009, which found that conflicted investment advice can in fact result in lower returns?

MR. PIACENTINI: But I guess I'm asking whether you have personal experience or other beyond -- the GAO report, I think, was a particular context, more broadly --

MR. STEIN: Well, I can give you a personal anecdote involving me. When I was -- when I was a visiting professor at University of Texas, I had -- somebody came in to sell a 403(b) annuity to me and it was an insurance company. This was in 1987. And he didn't really explain to me that -- the flat fees and that if I were only going to be at University of Texas for a year, it probably wasn't a very good product. Despite my wife's urging, I've never sold -- or never cashed in the insurance contract. It's $1,000 in 1987; today it's $1,030. I think he got a good commission, though.

MR. PIACENTINI: And your reference to the GAO study is actually a good transition to my other question for you. I think, if I remember the GAO study, it found that undisclosed conflicts might have these impacts that they reported. Is it your view that disclosure could correct the potential for this harm?

MR. STEIN: Well, it can mitigate it with respect to some participants. But I bought a car three years ago from a car salesman who told me, I get a commission, but the reason I'm in this business is I want you to get the most car for the least amount of money. And unfortunately, I believed him and I'll probably believe the next car salesman that tells me that.

MR. PIACENTINI: Thank you.

(Laughter)

Ms. Prange, your testimony referred in several instances to disclaimers, I guess a form of disclosure, as a positive provision that could be included in a rule. So is it your view that these kinds of disclaimers will -- will change the way people will view information they're getting, whether it's advice - - including will individual -- how will individual participants behave differently because of a disclaimer?

MS. PRANGE: So I believe that in today's disclosure regime, that is what we as an industry and what you as regulators truly believe, with plan sponsor disclosures and participant disclosures on our doorstep -- that we all believe that more disclosure, clear, concise disclosure to the individuals who are making decisions, and leveling the playing field or -- or setting the foundation for the relationship and the roles of each of the parties involved will have an impact on the decisions that are made.

MR. PIACENTINI: So I mean, are you drawing a comparison to the rule, for example, that the Department has issued that says that participants should be told about the fees associated with their investment options?

MS. PRANGE: That's correct.

MR. PIACENTINI: Because I think -- I think I'm asking a slightly different question, which is, you know, a disclosure about a relationship or how to interpret information that's being provided as opposed to just, you know, sort of factual disclosure about a particular option. So you think that the effects would be the same?

MS. PRANGE: I think -- I think what I'm saying is that it's a continuation of that thought process, that we believe that the current disclosures that are coming for plan sponsors and participants related to factual information, along with disclosures and disclaimers about the relationship and the roles of the parties will further enhance each other, and that it will put participants in a position, or plan sponsors in a position to understand the relationships of the parties and the decisions that are to be made by each.

MR. PIACENTINI: Thank you.

And one question for Ms. Tuttle. You made a reference to the uncertainty that was talked about in the economic assessment of the rule that the Department issued. And you pointed out that -- if I understood correctly; I'm going to paraphrase a little bit -- but good and independent fiduciary advice can be and is available in the marketplace now. So I guess my question is, is it your view that that holds for all of the different kinds of clients that are sort in play here, from IRA owners, plan participants, plan fiduciaries? Or are there some kinds of advice where that may not be true, where it may be that some other types of existing business models that may not be independent are really the only efficient way? Or did you intend your statement to apply sort of across the board to everything that's in play under this rule?

MS. TUTTLE: Yeah. I intended it to apply to the kind of business that we're in. We do not advise plan fiduciaries or plan sponsors. I am aware that there is a very active consultant community there. But we ourselves do not enter into those activities.

In terms of IRAs, again, we get lots of questions in our adviser center from participants who are asking about what they should do with their plan -- if they want to roll it over, they're ready to take a disbursement, they -- they're looking for help. We also get questions from plan sponsors asking what kind of help we might make available to their employees. We're not yet in that business. So in terms of what's available to IRA participants now, I don't have the degree of familiarity as to whether those existing structures can provide it. But we can envision, you know, a time when it is possible to provide similarly disinterested, objective advice to participants when they're facing that very complicated decision about rolling over the monies that they've accumulated throughout their working career. There may be many tax complexities. There are complexities around whether instruments such as long-term bond funds that could help them to best utilize the monies they've accumulated would be available through different vehicles that aren't available in an employer-sponsored plan. So I think there is a role there that will be developing and evolving, and we would think that's an area for further study and great care in regulating the ways that that industry can be nurtured and given the same kind of support that the Department has offered to other new products and innovation throughout the decades.

MR. PIACENTINI: Thank you.

MR. LEBOWITZ: Ms. Prange, I just have one question for you. It's sort of a follow-up. Go back to your -- to your call center and the people you have working there. And you started to describe a circumstance where people would ask questions about a rollover, about taking a lump sum distribution and want to understand, I guess, what -- what the process is and what they -- what options they have. So how -- how are your call center staff instructed in terms of responding to those specific questions? If an individual calls and said, well, what should I do with it? I have it in these funds; can I just put it into a JP Morgan account? I mean, what -- what do they tell them? How are they trained?

MS. PRANGE: They're trained generally to review the tax implications with a participant, of the different types of distribution methods. So you can leave the funds in your plan; you'll still have access to the investments that are currently offered in the plan. Take a distribution; you'll have tax implications there. You can roll it over. You can roll it over to an IRA. If a participant specifically asked whether or not there were JP Morgan IRA products available, they would be referred to another area of our company that offers those types of products to build a relationship there and establish an IRA. But generally the call center (inaudible) are directed to first and foremost ensure that the participants understand what their distribution options are and the tax consequences associated with it, with a goal of ensuring that they understand the need to protect their retirement assets long-term and to avoid situations where we see participants taking lump sum distributions and wasting the retirement assets that they've built.

MR. LEBOWITZ: So there's no specific -- it's up to the participant to ask a question about other JP Morgan services or products? Your people are trained not to say anything about it at all; is that right?

MS. PRANGE: Well, they're trained to walk through a dialogue with the participant to -- to ask the participant who is on the path of an IRA rollover, "Do you have a relationship with a financial institution that can provide you those types of services?" Banks often offer those; other mutual fund companies do. A participant who -- who does not have a current financial institution or does not seem to have any direction on where they might go for an IRA might be told that those products are available at JP Morgan if they have interest in those products. But then it's up to the participant to specifically state that they're interested in those products before they would be referred to someone in one of our broker-dealers that could assist them.

MR. LEBOWITZ: I guess -- I guess actually I had one other question for you. As I was listening to your testimony, I wasn't quite sure I understood what your -- what's the right word -- vision is. I mean, if you were constructing the regulation, what would it look like? What -- would it be principally a disclosure regulation? You put a lot of emphasis on clarity and on disclosure, I think. Is that basically it? If you check boxes that I gave people 27 pieces of paper, then that's enough, no matter what? Or does it still leave -- or it struck me that you were still leaving a lot of subjectivity and a lot of ambiguity about the actual relationship that might be created between the individual and -- and the adviser.

MS. PRANGE: I don't think that that was our intent. I think that the relationship between the individual and the adviser is one of our primary concerns, and that it's a -- that it's a mutual understanding of what that relationship is going to be, first and foremost. And that once established, then that the provider clearly discloses when -- when there's an opportunity for a conflict or when they are acting in a sales role as opposed to an advisory role.

MR. LEBOWITZ: Okay.

Thank you all very much.

Next panel: Marc Machiz, Charles Nelson, and Ken Bentsen.

(Pause)

Can we all settle down, please? Everybody sit down. Thank you.

Mr. Machiz?

MR. MACHIZ: Mr. Lebowitz, Madam Assistant Secretary and the rest of the panel -- good morning. My name is Marc Machiz. I'm here today to testify on behalf of the National Employment Lawyers Association, NELA. We represent the interests of participants and beneficiaries in plans.

So, two trustees on an expense account walk into a fancy restaurant and scan the menu. The first trustee, a devotee --

MR. LEBOWITZ: They would never do that, would they?

(Laughter)

Go into a fancy restaurant?

MR. MACHIZ: No, not a trustee. Well, it's a big plan. They have a lot of money.

The first trustee, a devotee of the efficient menu theory of fine dining, closes his eyes and points randomly at the menu and hits a free-range chicken -- a boring but relatively low-cost alternative. The second trustee looks up at the waiter and decides to ask his advice. "What's my best choice?" The waiter looks at him and says, "Got any food allergies?" "No." "For you, sir, the foie gras-encrusted Gila monster special with truffled oysters, I assure you it is magnificent." "But what's it cost?" The waiter scratches his chin, looks puzzled, and says, "Market price. I'd have to check in the kitchen and get back to you. But it's unforgettable. Hard on the goose, silk on the palate." (Laughter) At bottom, the opponents of the proposed regulation want plans to deal with investment advisers the way our trustees dealt with the restaurant. The trustees will tip the waiter for his advice, but they're not entitled to a disinterested dinner recommendation. The up-sale is not confined to fancy restaurants, though investment pitches are more likely to glaze over the recipient's eyeballs than wet the palate.

We're here to express our support for the basic policy choices made by the Department; discuss a few of the concerns raised in the comments; and make a few suggestions to better protect plan participants from poor or conflicted advice.

The thrust of the Department's proposed regulation is to require most people making money by recommending investments or managers to plans -- plan fiduciaries, plan participants -- to do so subject to ERISA's fiduciary duties. There are exceptions, importantly, where advice is provided by a principal dealing with a plan or an agent for such a principal. The would-be adviser may disclaim fiduciary status by informing the participant of his advice that he has interests adverse to the plan and will not undertake to provide impartial advice.

NELA thinks the Department's basic policy choice is both common-sense and consistent with the straightforward language of the statute. The task of the Department should always have been to define investment advice so as to distinguish it from mere education, generalized financial journalism, and simple sales or marketing where the parties were clear that they were on opposite sides of the transaction. If someone engaged in a trade adverse to a plan, it is fair to hold him to fiduciary standards unless he declares himself adverse to the plan. Even so, when the recipient of the advice is an individual participant or beneficiary, we question whether a simple declaration of adverse interest should be sufficient to relieve an adviser of fiduciary status. And that's what my colleague, Norm Stein, addressed in the prior panel.

Now SIFMA, as I understand it, objects that routinely making broker-dealers fiduciaries will interfere with transactions beneficial to plans by rendering them prohibited transactions. Whether exceptions should be made to prohibited transaction rules to allow transactions in which the fiduciary adviser or his affiliates have some financial interest is a matter appropriately left to the Department in the exemptions process. These issues will only arise when a person or entity who does have some financial interest in the advice being given will nevertheless be obligated to provide impartial advice. The exemption process was designed for precisely this purpose; we should let it work.

Indeed, NELA believes that the Department in some respects did not go far enough to protect plans, plan fiduciaries and participants from poor advice. Under the proposal, persons giving individualized investment advice may nevertheless avoid fiduciary status because they did not actually agree in advance that their investment advice would be individualized and agree that the advice to be provided may be considered in connection with making investment or management decisions. This is probably the most important point I want to make. Fiduciary status should depend solely on the nature of the advice provided for a fee. plans and plan fiduciaries in the ordinary course will contract for investment advice. Full stop. That's all the contract need say. It should be presumed that the advice may be used to make investment or management decisions. Why else are you contracting for it? Why else would -- simply omitting from the agreement to obtain advice a written requirement or a oral requirement that the advice be individualized or a recital about how the advice might be used should not relieve the adviser of fiduciary responsibility.

Ironically, SIFMA and others read the current regulation to permit them to avoid fiduciary status in exactly this way. By omitting some or all of the magic language of the regulation from their formal agreements with plan fiduciaries, they provide themselves with a shield from liability. As they would have it, no mere adviser is a fiduciary except one who agrees as a matter of contract to be a fiduciary. But SIFMA's approach provides no protection at all to participants, plans, or plan fiduciaries that are on the receiving end of bad investment advice. Instead, this approach protects those advising plans from being found to be a fiduciary.

In any event, we question whether the requirement that advice must be individualized makes sense at all when the advice is provided to individual participants and beneficiaries. Again, this was one of the issues addressed by Norm Stein in the Pension Rights Center testimony.

Some of those commenting have sought more specifics about what is meant by individualized advice. This is a fair question. We think it means simply advice directed at the recipient. When I call my broker and say, "Bernie" -- and that's Levine, not Madoff -- (laughter) -- "what should I buy?" And he says, "Marc, I think you should buy Cisco," that's individualized advice. It doesn't matter that he's telling all his clients to buy Cisco or only those with a high appetite for risk, or only those clients who like me are bald and fat. He's telling me what to do. Whether or not he has an intellectually respectable reason for giving me that advice should not affect whether the advice triggers fiduciary status.

But if I ask my broker to send me his firm's research on Cisco, and that research contains a buy rating and a price target available to all the firm's clients, that advice is not individualized and arguably should not carry with it fiduciary responsibility, at least when it's provided to plan fiduciaries. Again, the issue of confusion of individual plan participants comes up.

While the broker-dealers contend that they should be fiduciaries only when they agree to be fiduciaries, the appraisers insist that their duty to provide independent, professional, disinterested opinions of value is inconsistent with fiduciary status. Frankly, this perspective baffles us. The appraisers appear to believe that being a fiduciary would require them to give dishonest opinions of value that are shaded in favor of their plan client -- shaving the valuation when the plan is the buy and pumping it up when the plan is the seller. But plan fiduciaries seek appraisers to provide them with an honest opinion of value -- at least we hope so. Loyalty in an appraiser consists of providing an honest opinion, not a deliberate distortion. If a plan fiduciary asked a professional appraiser for a dishonest appraisal or to act in a transaction as an advocate of a value different from his honest opinion, the assignment would indeed violate the professional ethics of appraisers. The appraiser should turn the assignment down.

The appraisers seem to fear that holding them to a fiduciary standard of care will require them to do more than they must do now and prohibit them from qualifying their appraisals, by, for example, noting that they have not independently verified the company's financial statements in the way that an auditor does.

But nothing in ERISA requires a fiduciary who is not a trustee to do more than the job he's hired to do. The Department should make clear that an appraiser may limit the scope of his opinion. Fiduciary status will, however, carry with it co-fiduciary liability. If an appraiser learns of a breach by another fiduciary, he will have a duty to blow the whistle and not stand idly by.

The appraisers also argue that since they're already held to a professional standard of care, making them fiduciaries adds little protections for plans, but does increase costs. The fact is that a plan fiduciary who hires an appraiser will rarely pursue malpractice remedies where he may also be liable in connection with the same transaction as the appraiser. Making appraisers who act in transactions fiduciaries gives the Department, as well as plan participants, an important enforcement tool to assure that appraisers adhere to the high professional standards they already support as a profession.

In the proposed regulation, the Department excludes from the advice that gives rise to fiduciary status either marketing or making available platforms from which a fiduciary may designate investment alternatives in those cases where the person marketing or making available the platform disclaims an intent to provide impartial advice. To obtain an exclusion from fiduciary status, such a person should not merely disclaim an intent to provide impartial advice. He should disclose in detail the nature of his financial incentives to provide the particular choices in the platform. Otherwise, a person says, well, these choices aren't impartial, but why? Where is the hidden -- where is the hidden trap for me? That needs to be disclosed if people are going to get out from being fiduciaries.

Moreover, this exclusion makes little sense to us unless the platform in question provides a broad range of choices to the fiduciary that agrees to choose from it. On the other hand, if the platform provider wants to give advice as to which managers or options within a platform should be selected, then it seems to us that that becomes -- that that must be fiduciary, individual advice.

And finally, we are concerned that the preamble to the final regulation make clear how much of what is clarified in the regulation is already reflected in the Department's interpretation of the existing regulation. It is clear from reading the comments that some believe that advice with regard to the selection of investment managers is not investment advice within the meaning of the existing regulation.

But the Department has stated repeatedly that such advice can qualify as investment advice under the existing regulation. Likewise, advice given to plan fiduciaries, including advice to fiduciaries of pooled vehicles holding plan assets would be advice to a plan under the current regulation. Similarly, advice paid for by third parties after payment of commissions can be investment advice, as well, under the current regulation. It would be ironic indeed if parties used this clarification -- the clarifications in the new regulation to argue that their advice escapes coverage under the old regulation.

We wish the Department well with its efforts to assure that plans, plan fiduciaries, participants, and beneficiaries have available to them impartial and prudent investment advice. It may always be perilous for plans to send their trustees out for a fine meal at a fancy restaurant. But plan and participant investments are far too important to let advisers treat those investments as just one more daily special.

Thank you.

MR. LEBOWITZ: Mr. Nelson.

MR. NELSON: Good morning. And thank you for the opportunity to testify at this hearing. I think I now understand why I'm in the middle.

(Laughter)

My name is Charles Nelson. I'm the President of Great- West Retirement Services and Great-West Life and Annuity Insurance Company. WE are the fourth largest retirement plan record-keeper in the United States, providing 401(k), 401(a), 403(b), and 457 plan retirement services to 24,000 plan sponsors, 4.4 million retirement participant accounts, and $138 billion in assets.

ERISA's fiduciary provisions are the cornerstone of our voluntary employee benefit system, and I commend the Department for holding this hearing as an important first step in a process to fully understand and consider the proposal's effect on participants and plans. Let me first start by saying that my testimony today is not a defense of the status quo. There are legitimate concerns of the current regulation, and I think it is appropriate to review a standard established more than 35 years ago. There are provisions in the proposal we support. However, we find many more are ambiguous, and we are deeply concerned that others will set the retirement industry back 25 years by dramatically increasing costs to 401(k) participants and plan sponsors, eliminating advancements that provide DC plans with greater efficiencies and cost savings through open architecture investment platforms; and substantially curtailing plan distribution, communication, education, and counseling, reducing the availability of information participants need to make informed decisions about their distribution options.

We believe that the Department dramatically underestimated, or in the case of IRAs, did not estimate at all the cost of the proposal and its unintended consequences, while overestimating the benefits of the proposal. Our formal comment letter raised many issues for your consideration, but in my limited time this morning I will focus on several particular concerns.

We believe the Department's intended policies are not clear from the text of the proposal, preventing thorough public review and comment. Crucial terms such as the new form of fiduciary management advice are not defined, making it impossible for the regulated community to know with certainty what conduct is intended to be covered. Revising and re-proposing the rule for public review and comment will enable the Department to articulate a clear standard. Rather than speculating on what the rule might mean, commenters will be able to offer more meaningful comments on what the rule would actually do. We believe this is the best way to comply with the requirements of the regulatory process and ensure the rules result in greater protection, not greater litigation.

Despite our concerns about the proposal as a whole, we are encouraged that the Department included an exception for operating a platform and for providing information about the available investments. We are pleased the proposal recognizes that offering a platform of investment options is not a fiduciary act under current law and should not be under any new regulation. However, we believe the language in the exception is too narrow. A significant issue is that the platform must be made available, quote, "without regard to the individualized needs of the plan." If the intent of this language is to limit the exception to true platform providers, we support this intent. Unfortunately, it is all too common to see a DC plan adviser or consultant custom-build a target date or life cycle fund for a plan, but disclaim his or her fiduciary status. These fiduciary service providers should not be able to escape their duty by falsely claiming to be a platform provider. However, the individualized need language is too broad. A legitimate platform operator cannot provide its ordinary services without taking into account the individual and varying needs of its plan clients.

We are also concerned that it is not clear what the Department meant by limiting the exception to providing general financial information about platform investments. We offer our plan clients diagnostic tools providing comparisons between options using objective data regarding common fund metrics. Unless the rule clarifies that such tools are considered general financial information, platform providers likely will not offer them, making it harder and more expensive for plans to select and monitor options, particularly small plan providers or plan sponsors.

Similarly, we believe that general financial information should include information platform providers provide related to plan mapping and conversion, such as assistance in determining which platform options are similar to the prior plan investments. Finally, the platform exception should expressly state that the platform operator is complying with the process outlined in the Aetna Advisory Opinion 97-16A for removing and replacing investment funds are not providing investment advice.

The sales exception is also vital to platform operators. However, we are concerned that the exception as written would not work in practice. First, the proposal should expressly recognize that the sales exception is not limited to a specific point at the beginning of the relationship. Information related to sales is exchanged on an ongoing basis as plans make changes to fund line-ups or implement new design features months or years later. It is this aspect which will eliminate open architecture fund choices by plan sponsors, as providers will set fund line-ups and not be able to change them without risking becoming an investment fiduciary.

Secondly, we do not believe it legally accurate to use the term "adverse" to describe the service provider/plan relationship during a sale. Financial service providers are not engaged in caveat emptor transactions with their clients. Federal and state laws require financial service providers to take into account the needs of their clients under the prevailing duty of care. As a result of these legal duties, a regulated service provider cannot properly be considered adverse to his or her client. We believe the Department's intention can be achieved by using a better-suited phrase such as the adviser has a financial interest, rather than an adverse interest.

The exception for certain valuations for reporting and disclosure properly recognizes that not all valuations should be subject to fiduciary status, but it does not go far enough. We recommend exemptions not conditioned on reporting and disclosure, specifically: First, we urge the Department to clarify that passing through a valuation performed by another is not in itself a fiduciary act. Second, that -- clarify that the fair value pricing affected in connection with underlying open-ended registered investment company funds, for example, is also not a fiduciary act. And finally, we believe the proposal needs a general exception for valuations associated with insurance products. The concern in the preamble appears to focus on hard-to-value assets like closely-held employer stock or certain pieces of real estate. By contrast, group annuity insurance products and other insurance investment contracts are readily valued, but are not traded. We don't believe insurance companies and their employees should be fiduciaries for mechanically calculating a value of a contract for the purpose of a participant's minimum distribution requirement.

Another important issue is that the proposal may have inadvertently created ambiguity regarding the fiduciary status of bundled service providers. Aetna Advisory Opinion 97-16A expresses the Department's view that a record-keeper is not a fiduciary to the plan merely because of one of its affiliates is a fiduciary. We urge the Department to clarify in the proposal that a record-keeper in a bundled service arrangement will not be considered a fiduciary itself merely as a result of its affiliation with a person who is a fiduciary. Bundled service providers offer a very valuable and cost-effective service to plans, and without clarification of the paragraph, investment managers who also perform record-keeping will likely stop performing record-keeping. This will result in drastically reduced record-keeping competition, with a corresponding increase in record-keeping prices to plans and participants.

Finally, we are concerned about the future of advice to IRA holders and distribution counseling for participants. IRAs are inherently different. They are not ERISA plans. IRAs have no fiduciary-making decisions on behalf of participants, and thus no need for the highly protective structure of ERISA's fiduciary provisions. The Department chose to not apply the interim final 408(b)(2) rules to IRAs due to concerns about disjointed regulation across retirement products, and should do so again in this proposal.

We are also concerned that if a 401(k) plan distribution counseling becomes fiduciary investment advice, it will be even more difficult for participants to get the information they need to make informed decisions. Non-fiduciary service providers provide valuable information to workers, and preventing them from discussing distribution options or providing IRA rollover services would serve to limit the choices of individual workers.

Similarly, the Department should use its discretion again to avoid requiring Code 457 plan sponsors which are not covered by ERISA to be subject to these proposed regulations simply because a 457 plan participant seeks to roll over assets to an IRA.

We believe the Department has identified some valid concerns with the existing regulation. But we also believe that the proposal as written does not work. We should not create new problems while trying to solve old ones.

I appreciate the opportunity to help you work through this process and happy to answer any questions you may have.

MR. LEBOWITZ: Thank you.

Mr. Bentsen?

MR. BENTSEN: Thank you.

Good morning. I'm Ken Bentsen. I'm Executive Vice President for Public Policy and Advocacy at the Securities Industry and Financial Markets Association. We appreciate the Department's decision to hold this hearing on the proposal and hope that our comments are helpful to the Department as it assesses the impact of the proposal on plans and their participants.

We believe this regulation is far broader than the aims it seeks to address. It imposes fiduciary status without a relationship to a plan and creates prohibited transactions and co-fiduciary liability on entities who have no understanding with a plan or an IRA that any service at all will be provided.

The Department also states that participants and beneficiaries would directly benefit from the

Department's more efficient allocation of enforcement resources by providing greater protections than are available under the current regulation. However, no example or explanation of this benefit is provided that would justify these sweeping changes. We believe there is no evidence that the proposed regulation will be more protective, but a great deal of evidence that these protected accounts will suffer greater cost and fewer choices. New asset-based advisory fees to replace commission spread-based structure; additional transaction cost; elimination of investment options and alternative vehicles; constriction of the dealer market; limits on permissible assets in IRAs; and the elimination of pricing of anything other than publicly traded assets.

The Department suggests that the proposed regulation will benefit its enforcement program by helping to resolve difficult factual questions and enforcement challenges by removing the requirements that advice be provided on a regular basis, based on the parties' mutual understanding, and that it serve as the primary basis for plan investment decisions. This proposed rule would reverse 35 years of case law, enforcement policy, and the understanding of plans and plan service providers without any legislative direction to depart from the Department's contemporaneous understanding of the statute in order to make it easier for the Department to sue service providers. That seems to us to be an inadequate basis for proposing such a dramatic change. And of course, this enforcement rationale cannot apply to our IRAs, over which the Department has no enforcement authority.

This rule would appear to be, in fact, in conflict with recent action by Congress. Just six months ago in section 913 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Congress asked the Securities and Exchange Commission to conduct a study on investment advisers and broker-dealers and the distinctions between them when providing personalized investment advice, and further authorized the SEC to promulgate a rule establishing a uniform standard of care for the provision of such advice. SIFMA strongly supported this provision of the Dodd-Frank Act. The SEC has now presented its study to Congress and recommended that the Commission adopt such a standard that, based on the SEC study and direction from Congress, would appear to be quite different from the standard being proposed in the DOL's proposed rule.

In addition, FINRA has proposed changes to the Know Your Customer and Suitability rules. The preamble of the DOL's proposed regulation notes that the Department does not have the cost data regarding how that conclusion alone would implicate the prohibited transaction rules of ERISA and the code. One would hope that the agencies will coordinate rulemaking so that the change in the standard of conduct would be effective at the same time that this regulation and the changes in the necessary prohibited transaction trading exemptions were effective.

Importantly, the section 913 study does not suggest or recommend ERISA-like fiduciary duties with its attendant prohibited transaction, but rather a uniform standard of care that is business model fee-neutral and permits principal trading commission-based arrangements in sale of proprietary products -- all activities that ERISA's prohibited transaction rules would prohibit for fiduciaries. The SEC 913 study changes the standard of care without requiring all trading practices and products to be reconsidered. The SEC approach is carefully tailored to help retail accounts without increasing their cost, eliminating their choices, and making their trading less efficient.

If all brokers who provide market color or investment information are deemed to be fiduciaries regardless of the intentions of the parties, the vast majority of commission-based accounts may move towards fee-based asset arrangements. Securities and currency transactions that were formerly executed with a dealer as principal will be executed on an agency basis against a third party dealer, subjecting the account to an asset-based fee plus commissions and markups. The effect of these changes on the capital markets should be studied by the agencies with jurisdiction over the securities market.

The Department's proposals would deem a broker a fiduciary merely because it is complying with industry rules intended to set standards for brokers who are not investment advisers. Without some clarification, brokers may simply refuse to effect solicited trades for plans if, by calling a client with investment ideas or market color, they back themselves into fiduciary status. Accordingly, any suggestions, array of alternatives or recommendations from a futures merchant such as market or liquidity or time of day of a trade, regardless of whether the plan is represented by its own third party investment manager, may make the futures merchant a fiduciary and its receipt of a commission a prohibited transaction.

In addition, we are concerned about the impact on swap transactions. During the debate over the Dodd-Frank Act, Congress considered the question of a counterparty providing a fiduciary duty to plans, and it rejected such an approach because it wanted to be sure that plans could continue to engage in swaps. However, this proposal would make it nearly impossible for plans to engage in swaps, denying plans an important risk management tool used by most major plans and corporations.

The Department's cost estimates focus on the cost to service providers and not to the cost to plans and IRA holders. While we believe the Department greatly underestimated such costs, more importantly we think this emphasis is misplaced. The real question is the cost to plans and their participants and the impact on their retirement savings.

And even the list of uncertainties has not once mentioned IRAs. IRAs hold more than $4.3 trillion of assets as of March 20, '10. The vast majority of these assets are in self-directed accounts. The cost to such account holders would be significant, in our view. Data collected for a study SIFMA commissioned from Oliver Wyman comprised of 33 percent of households and 25 percent of retail investments suggested over 95 percent of households with investments hold commission-based accounts, with a strong preference among the small investor segment. These accounts hold $58 billion of fixed income securities purchased through commission-based accounts. If these self-directed non-fiduciary accounts were to be deemed fiduciary accounts as proposed, all fixed income securities would be required to be purchased from broker-dealers unaffiliated with the account's primary broker, at an additional cost of 23 to 27 basis points each year. While PTE 86-128 permits fiduciaries to select themselves or an affiliate to effect agency trades for a commission, there is no exemption that permits a fiduciary to sell a fixed income security or any other asset on a principal basis to a fiduciary account. The result of that prohibition is that the broker would trade away from his own firm, charging commission to the trade on top of the markup charged by the selling dealer.

It's also important to note that a potential effect would be that most of these plans, if not all of these plans, would become -- that would be governed by this new fiduciary standard would shift completely to an advisory fee model, which based on our data indicates a much higher cost. And I would point out that SIFMA represents both brokers and investment advisers, but we also recognize there is a difference in the cost provided for that service.

The Department suggests that the cost of complying with the new regulations will be $10 million in 2011 for existing service providers to analyze their plan relationships and almost one million each year thereafter for new service providers to do a compliance review. The analysis does not include banks, trust companies, fund administrators, private funds, FX dealers, all of whom sell products to plans and may be fiduciaries under the proposed regulation. The analysis does not include advisers, which we think is mistaken, since the rule imposes additional fiduciary requirements on advisers simply because of the status test for fiduciaries and advisers. The Department's estimates are based on the Form 5500 data and thus ignore the entire IRA universe.

The estimates ignore the costs of retooling all of the systems which create a compliance structure for the 4,500 broker-dealers in this country alone, ignoring the insurance agents, banks, and trust companies, consultants, appraisers, record-keepers, each of whom will have similar costs. The estimates also ignore the costs of retraining hundreds of thousands of professionals, of revising every plan service provider contract, of changing how transactions are effected in the principal markets such as fixed income and currency, and the cost of the scores of exemptions that will be required. The estimates also ignore the additional fees and commissions that plans and IRAs will incur to do all transactions away from the broker-dealer, resulting in both markups and commissions. The estimates ignore the constraints that the regulation will put on dealers who disseminate research or opinions publicly or privately to the plan sponsor or to fiduciaries. The trading cost to plans of dealing only with smaller dealers who are institutional only are critical components of any cost study, in our opinion. Finally, the estimates ignore the cost of the litigation that will ensue because of the lack of certainty or the lack of mutual understanding between parties.

On behalf of its members, SIFMA respectfully urges the Department to reconsider its proposed changes to the definition of "fiduciary" regulation, to reassess its economic analysis, and to confer with FINRA, the SEC, and the CFTC on the interaction of these changes with these requirements of Dodd-Frank. Thank you for permitting us to testify today, and we'd be happy to answer your questions.

MS. BORZI: Well, I thank all three of you for your testimony. And in the spirit of the new executive order, in lieu of my asking each of you questions, I'd like each of you to ask your panelists, because the executive order wants comments on comments. So why don't we start with you, Mr. Bentsen. What question would you have for your fellow panelists?

MR. BENTSEN: Well, that was a curveball that I thought might be asked, but I can't say I'm completely prepared. But --

MS. BORZI: That's the point.

(Laughter)

For all of you to be unprepared.

MR. BENTSEN: Kind of like a dissertation presentation.

MS. BORZI: I used to be an academic.

MR. BENTSEN: I know, so .... Well, I think that I would ask Marc, where we're concerned, you raised questions, the issues involving disclosure of publicly available data, and questions related, for instance, to research reports and the like. And that if that were -- if I were to ask my broker to provide me information or my broker sends me a research report but it's not deemed personal to me, that's not necessarily investment advice. I guess our concern is that the rule is so broadly written and research -- analysts' reports, for instance will often have a buy, hold or sell provision on it. How are -- how is -- how are we not to know, if we're doing that through our affiliate and we're providing it to you, that all of a sudden we don't become a fiduciary under this rule, particularly after the fact? And so our concern is things like may consider the provision of advice is so broad that we really don't know if at any time after the fact we're going to be considered a fiduciary and held responsible for advice that wasn't really given directly to that individual.

MR. MACHIZ: There's a question in there somewhere, and I intend to find it. The -- oddly enough, your statement is to me is -- parallels very much the question that I was -- that I was looking to ask you, which is why is it that SIFMA, in writing its testimony, seems to assume that almost any interaction between a broker-dealer and a client, for example you mentioned a call with regard to market color, that the stock has moved. Getting back to my broker Bernie, he calls me and he knows what I own a lot of, and if there's news on a story -- there's a news story that's moved one of those particular stocks, either that I own or I've told him I'm interested in, he calls me up and says, Hey, Marc, did you see, you know, your stock just cut in half because they announced that, you know, some disastrous FDA motion? And I say, Thanks a lot, Bernie. I appreciate the telephone call. But why are calls like this, which are simply intended to provide information, why do you presume that that's what the Department meant by individualized advice? I agree with you: if all that kind of interaction between -- that is basically informational and is not, you know, "sell that pig" were deemed to be fiduciary advice, I think your members would indeed have a huge problem.

But one thing: (a), I don't believe the Department meant that, and (b), I suspect -- although they won't say that because they're trained not to tell us what they're going to do -- to us today, I suspect they'd be happy to clarify that the meaning of advice, individualized or otherwise, that they're describing would -- at least when it's provided to plan fiduciaries -- is much narrower than what -- than what I think SIFMA fears that it -- that it is.

MR. BENTSEN: Well, then to the Assistant Secretary's point, this may be very instructional to you. Because from our standpoint, this goes -- in our view, this is so overly broad and vague, we don't know. And so we don't have the clarity. And so from our vantage point, that creates huge risks for us in what we provide, and that results in really one of two options, in our view, from the standpoint of members who provide services either to plans or to the IRA market. And that is one, you stop; and two, particularly as it relates to IRAs, you convert them completely to an asset-based account as opposed to -- as opposed to a commission-based account. And based upon our data, particularly for smaller IRAs where trades are very limited, the asset-based account is going to cost more.

So to our -- in our view, that is contrary to what the intent -- some of the intent, we would think, behind this rule is, which is to be to the benefit of the -- of the beneficiary, and that would be working against the beneficiary. But to be fair, I think the exchange raises the concern that we have that there is a lack of clarity.

MR. MACHIZ: Right. And I guess the question that I would ask you is why -- why is it that SIFMA thinks the way to resolve that lack of clarity is -- seems to be to simply allow a broker-dealer to enter into a contract that says we are not going to provide you with individualized advice or advice that will serve as a primary basis, and by having entered into that agreement, assuming that really is the agreement, you say, well, okay, now whatever I say, I have this agreement, so I may provide individualized advice, but I didn't agree to provide it and therefore I'm not a fiduciary. That, I fear, is how I read your testimony. Did I misunderstand it?

MR. BENTSEN: No, I think -- I think our view is that disclosure and contractual agreements matter and that they provide a roadmap by which participants on both sides of a transaction know how to act. This is exactly what the Securities and Exchange Commission is trying to deal with as they are in the process of considering writing a rule. What are the responsibilities of the parties? And from our vantage point, if there's not clarity, then there's tremendous risk. And we don't think there's sufficient clarity in this proposal.

MR. MACHIZ: Yeah. I guess I would advert to the -- to the cross-examination that Mr. Lebowitz did of the lady from JP Morgan who insisted that all her call center did was provide information. And as long as she was saying that, I said yeah, provide information -- not a problem, that's what -- that's what call centers are supposed to do. But it turns out that in the course of that interaction they find out that somebody doesn't already have a relationship, oops, that person gets steered to a salesperson, someone else at JP Morgan.

So what you agree to do and what you do are not necessarily the same thing. What you say you're doing and what you do may not be the same thing unless someone takes the trouble to inquire deeply.

MR. BENTSEN: Well, I think from our vantage point, and where our members operate, what we agree to do is what the law and regulation says that we're supposed to do, and it's subject to enforcement by -- in the case of a broker, it's subject to enforcement by the Securities and Exchange Commission and FINRA. I might point out -- and this in a discussion on section 914; we can talk about 913 maybe when we talk about Dodd-Frank, but we talk about Dodd-Frank all the time -- and that --

MS. BORZI: As do we.

MR. BENTSEN: Well, good.

MS. BORZI: And our colleagues in the SEC and the CFTC.

MR. BENTSEN: But the point being is that, you know, that our view is you can't divorce this proposal from section 913 and where the SEC is going, and likewise you can't really divorce section 913 from 914 and the oversight of advisers and brokers. But that's a discussion for another day.

MS. BORZI: Mr. Nelson, you may be in the middle, but I'm going to give you the last question.

MR. NELSON: Well, I really wanted to find a little bit more out about that foie gras, but I'm going to pass over that one and go to a different topic. I've got to --

MS. BORZI: It's the one thing I won't order on the menu.

MR. NELSON: This one's for Ken. And, you know, I'm just trying to kind of follow, because I think we are somewhat aligned here in that -- would you -- would SIFMA be a proponent of revising and re-proposing the rule for public review and comment rather than proceeding down the current path that we are by the calendar year this year?

MR. BENTSEN: Absolutely. Because I think from our standpoint, largely for two reasons. One is that again, the SEC, in our view, is going to move forward with establishing a new uniform standard of care and a uniform fiduciary standard of care for brokers and advisers that will apply to many of the activities -- certainly the IRA market -- encompassed by that. And second of all, we think that the

Department has not done sufficient cost analysis, and I think that's -- I think that's stated as such, as it relates certainly to the IRA market. And we don't think it's done it broadly enough as it relates to the service provider market, as well. So we think that the -- that we would all be better served if this was withdrawn and more study was done. I appreciate the fact, I know the Department, you know, is talking to the Commission. But the Commission and the Department and other Commission all seem to be going different directions, that there could be better coordination, because our members will have to deal with all of these rules.

MR. MACHIZ: Do I get to answer that question?

MS. BORZI: I just want to point out that it's easy for you to say from the outside that there's no coordination or not enough coordination. But I want to assure you that we are talking with our colleagues, and we have no interest -- none of the three agencies have any interest in making it more difficult for compliance with either Dodd-Frank or ERISA. So I need to say that on the public record, even though I've said it once before.

Thank you all.

MR. DAVIS: Mr. Nelson, you talked -- you started your comments by saying that there were some legitimate concerns that the Department was trying to accomplish with this regulatory initiative. Can you just expand on where you have concerns and where you think the Department might be appropriately focused with respect to this initiative?

MR. NELSON: Expand on the items that I -- that we're agreeing with?

MR. DAVIS: Yes.

MR. NELSON: There are a number of items that we would agree with. And I think some of the things that have actually even come out in the interim proposed 408(b)(2) regulations on the fee disclosure. We believe fee disclosure will go a long way -- a long way with the contractual requirements associated with those for documenting to clarifying the relationship between interested parties, whether they be fiduciary or non-fiduciary, relative to a plan sponsor. So we think a number of those items really do help the process. And I think the discussion around sales exemptions, as I stated, is a step in the right direction. But the language just wasn't quite clear enough to really kind of gather the entire process, to gather in that it is not just a point of sale, that it's really an ongoing relationship; and we've got to be able to capture that communication on an ongoing basis under that same umbrella. So a couple of examples.

MR. DAVIS: And do you think disclosure as a standard is enough in most cases to eliminate a lot of the concerns that you've seen or that perhaps members of your team have seen?

MR. NELSON: Yeah. I actually believe the Department has made tremendous progress with 408(b)(2) especially, also with the follow-up on 404(a) that's coming later this year. So I think much progress has been made and will be made as a lot of agreements between providers and plan sponsors get documented to the degree that is required within those regulations and get communicated to the plan sponsors. We don't believe that we should start to find a cure for something before we've actually identified whether there's going to be a result -- additional results from the 408(b)(2) or 404(a) that need to be fixed.

MR. DAVIS: And Mr. Machiz, have you in your work seen examples of the types of conflicts that the Department is attempting to address that you could share just generically?

MR. MACHIZ: When you're talking about the types of conflicts, I mean, we've seen situations where individual people are giving advice that is resulting in tremendous fees to them, that are giving bad advice and that those conflicts are -- the ability to generate those fees create those conflicts. I mean most, you know -- most obviously and most recently, the various people who were -- found themselves recommending to plan fiduciaries that they -- that they invest with Mr. Madoff. You ask, well, why did they do that? Why did they do that notwithstanding that they -- that many of them had to one degree or another figured out that he must be illegitimate, or might be? And the answer is, because it was a beautiful thing to market. He was --

he had this pristine record. And so if you could market Bernie's track record, either directly or indirectly through another fund, you were in a position to earn a huge fee.

MR. DAVIS: Mr. Bentsen, you talked about to the extent that brokers would have to migrate from a commission-based model to a fee-based model that in your studies, the costs would go up overall. I'm just -- could you expand a little bit more just specifically why would the costs go up, and would they go up in all situations? Just give us a little bit more specificity.

MR. BENTSEN: There are a couple of reasons. One, in our -- commission-based models, obviously, are done on a trade-by-trade basis. So particularly if you have accounts that trade very little, like IRAs, the annual cost is going to be fairly limited. Commission -- asset-based accounts generally run at about a point on an annual basis. I think the Department's own guidance in some cases has been that they could run up to a point and three-quarters on an annual basis. And our study -- the study that we had Oliver Wyman conduct as part of our submission to the SEC, and I believe we submitted it with our comment letter to the Department as well, they found in certain instances -- we looked at different types of asset trades. So we looked at fixed income securities, for instance. And we found that there was a difference because in an asset-based model, a true fiduciary model, in addition you wouldn't be able to -- you'd have to trade on an agency basis and not a principal basis, that the cost spread of trading fixed income securities on an agency basis versus a principal basis would be 23 to 27 basis points annually. So that's where we derive our view that there's a price differential between a commission-based and an asset-based.

Now to be fair, and as I said, we have members -- we represent members that have both registered representatives and registered investment advisers. And in many cases, firms will have dually registered individuals, and they will -- they will provide the service based upon what the client is asking for. But what our study also found is among the households we looked at, the vast majority had some form of a commission-based account. Customers seem to be choosing that type of account. And it could be that they're choosing it on price; it could be that they're choosing it, that they want -- they like having a self-directed account. But it does have a price implication.

MR. DAVIS: And you think the sellers exception as currently drafted in the regulation wouldn't go far enough to preserve some of those existing business models?

MR. BENTSEN: We don't believe so. We don't think -- we certainly don't think that it would -- we don't think it would allow a sufficient exemption for principal transactions, and we are confident that it doesn't provide an exemption for swaps business. So that would be more on the plan side. And we're concerned when you consider the rest of the rule and questions of whether someone could subsequently be deemed a fiduciary because of the -- of the -- may consider in some of the other issues that the risk of being ultimately deemed a fiduciary would cause it to be -- cause a transaction, a principal transaction, to be a prohibited transaction, and the liability associated with that would cause many firms to just back away and say just do it as an asset-based in an agency basis.

MR. DAVIS: Thanks.

MR. LEBOWITZ: Mr. Bentsen, was there anything in the reg you liked?

MR. BENTSEN: We appreciate the fact that -- that you had -- that you have -- the process that you have established. We appreciate the fact that you agree to extend the comment period at least to get past the time that the SEC submitted their study. I think that was beneficial to all of us who wanted to comment on seeing where the SEC staff was going. We appreciate the fact that you have a hearing and that you have developed a process which allows us to bring our concerns. We - you know, contrary perhaps to at least some of my fellow panelists -- you know, we think that the current standard as it relates to the businesses that we're looking at has worked. We think that the Department has been taking steps through some of the disclosure recommendations to try and address it. But beyond that, you know, no, we're not -- we don't find a lot in it as it is currently written that we would be supportive of.

MR. LEBOWITZ: You weren't convinced that there are any problems that the current reg does not adequately address?

MR. BENTSEN: Well, the current reg, as we read it in the preamble is written to address problems in areas which aren't primarily a focus -- and there are others here to talk about those. But in terms of the IRA market, where we have a serious concern, you know, it doesn't appear to us that that was necessarily the intent in the way that the rule was written. And it seems to us that it also runs head into -- and again, I appreciate the Department's coordination with the other agencies -- but it runs head into a standard that is in the process, we believe, of being established.

MR. LEBOWITZ: Mr. Hauser?

MR. HAUSER: Maybe if I could start with you, Mr. Nelson. I just had a question about a valuation point you made, which is that you wanted -- you wanted the regulation to be written in such a way that when your company, and I guess others, are valuing insurance products, they'd be able to pass on the underlying values of those contracts. And you referred to it essentially as involving a mechanical calculation of value. And I guess my question is for the specific products you have in mind, how mechanical is that calculation? I mean, are there hard-to-value assets in there? Are there questions about pricing; are there judgment calls to be made? Or is it truly just a matter of plugging in market prices, adding it up, and discounting based on a disclosed formula or something?

MR. NELSON: Interesting question, because in underlying open-ended registered investment company funds, a mutual fund, there are examples of fair value pricing that occur on a very frequent basis that need to occur. Those funds are often wrapped in annuity products, as well, by insurance companies. So you have kind of a compounding feature. Now, many of those products in variable annuities or the fixed annuities would be valued on a daily basis. But they are not, as the regulation stated, necessarily traded, you know, in an exchange-type format. So that's where a lot of our concern kind of came around in the language, is that it really kind of seemed to fuss with the valued-but-are-not-traded component. So it's -- many of them are valued. There are certainly issues with some of the valuations, as we said with even going beyond insurance company products. But it's the traded component and the language that fussed us.

MR. HAUSER: And so what -- I mean, just so I have a sense of it, what kind of products are you talking about in particular?

MR. NELSON: It'd be talking about variable annuities, accumulation -- variable and accumulation annuities in retirement plans, which are predominantly used in the smaller plan 401(k) market. There would also be fixed general account annuities, as well, and some separate accounts.

MR. HAUSER: Okay. And in connection with the seller's exception that's built into our regulation, there's a suggestion -- I don't know that I have it in front of me, but one of the commenters -- I think AARP suggested that, well, maybe a seller's exception makes sense, but it ought to have a fairly comprehensive sort of statement of the conflict. Because you made the point that well, you don't think you "adverse" exactly captures what the nature of this relationship is. But AARP has suggested that you ought to be able to get the seller's exception if you're on the other side of the transaction. And then it's coupled with comprehensive disclosure of the fees and conflicts; a statement of the conflict; full disclosure of the sources and amount of fees; and then a clear and unequivocal acknowledgment that there is a conflict. Would that kind of -- if we were to write a regulation that required that level of disclosure as part of this seller's exception, and said if you have that disclosure, you're good to go and you're not a fiduciary, either as a safe harbor or just as a mandate, would that be something you'd be willing to endorse?

MR. NELSON: Well, I think that's something we should look at. I think the more that you have on an ongoing basis and understand that are exchanging information, that it's not a point in time relationship, and that certainly disclosing -- if a record-keeper has an affiliate that has a fund and how much revenue comes from that fund I think are all perfectly and appropriate things that need to be communicated in that type of a process and should, when you do those types of things, should certainly not make you a fiduciary.

MR. HAUSER: Maybe turning to Mr. Bentsen, I guess where I'd like to start is with the IRA market, because it seems to me that's obviously a very big part of the concerns expressed by SIFMA in its comments. And as I read SIFMA's comments as well as a number of the other comments, I get a sense that there is a perception, at least in the comments, that the effect of the Department's regulation in this space would be to preclude commission-based sort of arrangements and to completely up-end current fee arrangements. I guess in that connection my question is, the regulation as drafted, and obviously it can be expanded or narrowed, but -- and we are listening to people's concern -- but the regulation as drafted has a seller's exception, which is designed to enable people who are truly counterparties to be counterparties, not fiduciaries. There is 86-128, a class exemption, which covers security transactions and permits commissions to be taken and has virtually no conditions with respect to IRAs at present. There is 84-24, which covers commission-based arrangements and annuities and mutual funds. There is at least theoretically going to be a 408(g) sort of exception. How -- and the Department has, as Mr. Machiz noted, broad authority under the class exemption procedures to grant exemptions where they're administratively feasible and in the interests of participants and beneficiaries and protective of their interests. And so presumably if there's a particular fee practice that on balance is beneficial to participants, that in the sense that they would in fact have worse performance because of additional fees or the like would be something we could look at and grant an exemption for. Given all those things, I guess my question is one, how extensive is the problem? What exactly is the universe of transactions in which you think really commission-based arrangements are just going to be rendered impossible? And second, why isn't the Department's -- you know, it seems to me implicit in your -- the comments is a view that the Department simply shouldn't even have the authority in this context to impose conditions on arrangements such as principal transactions involving these folks and the like, because we -- I mean, we certainly can grant exemptions in this context for fee-based transactions that are reasonable, but it might come at the cost of conditions.

MR. BENTSEN: Well, I think -- you know, I think even in how you laid that out underscores both the complexity and the lack of clarity that the market approaches this. So -- and the point that you make that if there are problems, that we could -- you know, that we could fix these problems through -- either through adjusting this rule or subsequent rulemaking. But absent that, our concern is, is we look at the market today and we look at the way the rule is constructed, that either directly not allowed or indirectly because of concerns that other activity would trigger a fiduciary status and then affect a principal trade related to this creates a concern for us.

So I would -- I think we would appreciate the fact that you recognize that we've raised a concern about it, and hopefully others have raised a concern about this, and that there may be ways to fix it.

MR. HAUSER: Right. Well, the problem, I guess, with asking an overly complex question is we don't quite get focused. But at least with respect to 84-24 and 86-128, those are class exemptions that already exist. And the seller's exception is laid out in the reg, and it may or not may be broad enough, but these provisions already permit a huge amount of commission-based arrangements to move forward, don't they?

MR. BENTSEN: I mean, our view again is that the way we read -- with what's in place now and the way that we read -- the way that we read the proposed rule is that it would -- it would greatly constrict the ability to move forward under the current structure in being able to do commission-based with principal transactions for the IRA market. Now I'd be happy to come back to you for the record taking into consideration the other items and maybe piece that together in more detail for you, why those provisions don't give us the sense of relief that you seem to think we should have.

MR. HAUSER: Okay. And I'd appreciate that. And I guess with respect to principal transactions, and I think the other area you mentioned in your comments were fixed income securities, also I think primarily probably principal transactions, were at issue. I mean, those are areas where there are pretty direct conflicts of interest between broker-dealers and their customers, aren't they? I mean at least in the sense that there isn't, to the extent that you're selling a product yourself in a market that's thinly traded and there's not a readily available market price, there's a potential for you to take advantage of the customer. And the question I have is one, would you concede that that's true; and two, if that is true, why shouldn't we be in a position to create exemptions that place some conditions on those kind of dealings between your members and relatively unsophisticated investors?

MR. BENTSEN: Well first, I would not concede that that's true. And second of all --

MR. HAUSER: Okay.

MR. BENTSEN: -- I would make the point that across the broad retail market, not just the IRA market but the broad retail market, that market holds a tremendous amount of fixed income securities, both taxable and tax-exempt. And obviously in this instance, tax-exempt would not be applicable. And this is an issue that the SEC in the broader market has dealt with, and an issue that the SEC is trying to deal with as they're trying to establish a uniform standard of care of how you deal with potential conflicts in terms of principal trading. But at the same time, our data has shown, as we discussed earlier, that customers receive the benefit in terms of the cost as a result of being able to engage in principal transactions. And we would argue that Congress, in considering Dodd-Frank, made it clear that they did not want to preclude the ability for principal transactions with retail customers, and in fact the way we read where the SEC staff at least has recommended that they would be moving in that direction as well, that that could be addressed more through a disclosure regime.

MR. HAUSER: Well, I guess following -- so in a disclosure regime, this is just a question I've wondered about maybe -- maybe anybody on the panel can answer it, but starting with you. If you're a relatively unsophisticated investor and you're dealing with a broker-dealer who may call himself a financial adviser or a financial planner, and you're advised of the conflict, what is it you do with that information? How do you -- how do you use the disclosure of the conflict to then protect yourself from advice that scares you into investments that are actually disadvantageous to you?

MR. BENTSEN: Well, I think that's a question that -- you know, I think that's a question that people confront, you know, whether it's in the investment or any other part -- or any other part of their daily lives, of -- and, you know, we have operated our markets very much on the basis of a disclosure regime and in agreements between two parties. And so, you know, what's the alternative to that of not having -- not having a disclosure regime? It's having a purely discretionary account where you're giving all your assets to one individual and, you know, creating goals with them and then having them do it but you limit your choice. Investors seem to choose, based upon the data we've looked at, overwhelmingly that they want to have in many cases self-directed accounts, which are commission-based accounts. So I think you have to balance that with the types of regulations that you're -- you know, that you're trying to put in place.

MR. HAUSER: Right. I suspect investors, though, often assume that the person they're talking to, you know, has their best interests at heart and would in fact be accountable if the advice, you know, was biased, was steered to support a bias and the like. And I guess I just -- it strikes me that from, you know, most investors' standpoint, certainly most unsophisticated investors, the difficulty they have is that on one side of the transaction you have somebody who, you know, spends some significant amount of time acquiring financial expertise. The participant doesn't have that expertise, nor do they necessarily know exactly how a conflict is going to play into what recommendations they're getting. And the mere fact that there was disclosure of that conflict may actually encourage them to believe that this guy really does have my interests at heart -- look how honest he was, he told me about the conflict. And I'm just wondering, how does conflict alone get past that, and why isn't, you know, putting some conditions on the ability of parties to interact in this conflicted way not a good thing?

MR. BENTSEN: Well -- sorry, go ahead.

MR. NELSON: There are already conditions and restrictions. Most all have our securities license with FINRA. They would have a six, seven, or a 63. They would also be subject to state insurance if they're selling an insurance product. And all of those have, you know, suitability requirements, so if you're going to sign someone up, you've got to go through the suitability.

MR. HAUSER: Hm-mmm.

MR. NELSON: And in the insurance regulations you have the similar types of things there. So there's multiple layers already. I don't think we need another layer on top of that.

MR. HAUSER: Okay. And just one last set of questions for Mr. Bentsen. And that's just that in the comment you -- or that SIFMA provided to us, you included a Powerpoint with some financial data. And I guess my first question is, can we have the study that's behind that Powerpoint? Would you be willing to furnish that to us?

MR. BENTSEN: This is the Oliver Wyman study?

MR. HAUSER: That's the -- yes.

MR. BENTSEN: It's actually part of the public record with the -- with the SEC 913.

MR. HAUSER: Okay. That'd be terrific if you could pass that on to us. And does the part that's a part of the public record explain in particular how the particular SIFMA members were chosen for the survey?

MR. BENTSEN: It has a section that explains the methodology that was used.

MR. HAUSER: Okay. Thank you. And the same goes -- I think at the tail end of the Powerpoint, there's a set of data points about the likely sort of compliance costs. Are the methodologies for that laid out, as well?

MR. BENTSEN: I believe so.

MR. HAUSER: But is --

MR. BENTSEN: I'll look and check and get back to you if it's not.

MR. HAUSER: Okay. Appreciate it.

MR. PIACENTINI: I think I want to preface my couple of questions by saying that in asking them, I am thinking about IRAs as well as plans, so please interpret them that way.

And so the first question picks up on something that Tim was just talking about. So I think probably everybody -- maybe everybody would agree that there is sort of an asymmetry in the client/adviser relationship a lot of the time. Maybe not really big plan fiduciary as the advisee, but in a small plan or IRA and so forth, the adviser is the expert; the client is relying on the expert. Is that something we all agree on?

MR. BENTSEN: I mean, I think our view is that the -- that the client is buying -- you know, is choosing to buy a service from -- from a financial adviser who may be a registered representative, may be a registered investment adviser, and they're choosing the type of service that they want to buy.

MR. PIACENTINI: Right. But I guess my question is a little different. I'm just suggesting that as they're choosing this service, that part of that relationship is that they are relying on this person as the one who knows a lot about this topic and that they themselves don't. Almost like when you go to your doctor. If you're not medically trained, they're the expert, and they're -- you're going to rely on them. Is that -- do we share that view?

MR. BENTSEN: Well, I think -- I think we share the view, and the reason of why we think that there should be a uniform standard of care between investment advisers and brokers, and hence why -- not because of us, but Congress itself determined that that was necessary and authorized the SEC to do so.

MR. PIACENTINI: All right. So then let me maybe shift a little bit and ask you in the hypothetical. So if it's true that there is this asymmetry and that the adviser, whatever their business model is -- and you talked about business model neutrality -- whatever their business model is, that they have a much better understanding both of the subject material on which they're advising, the basis for and the merits of the advice that they're providing, and the presence of potential conflicts of interest and what the implications of those conflicts might be. So if it's the case that they know more about all those things than the client, then should I interpret, or why should I interpret, what turns out to be the dominant model as one that's necessarily more favorable to consumers? Why in an asymmetric market like that would it necessarily come to pass that the business model that's most common would be the one that's the most favorable to consumers?

MR. BENTSEN: I mean, that's your hypothetical question, so I think you have to look at the data and determine, you know -- what we're looking at is the empirical data and what investors are choosing.

MR. PIACENTINI: Right. And I can see that that's the most common business model.

MR. BENTSEN: And it would appear that it's also being chosen based upon price.

MR. PIACENTINI: Right. I'm not sure -- the statistics that are in the Wyman report are one thing. But I think it's pretty clear that that's a very common, probably dominant business model. I'm not questioning that.

Does anybody else want to weigh in?

MR. MACHIZ: I'm not sure I have a direct answer to your question. But there's a -- underlying a lot of the conversation that's come before is the notion that these transactions are going to -- that's coming from SIFMA is that these transactions are going to be unworkable. And I'm not sure -- somewhere about ten minutes ago the conversation left the planet on which I was living, because we have granted that there is and perhaps to be expanded a principal exception that's going to allow these brokers to say, hey, I'm selling you stuff. I'm on the other side of this transaction. Maybe the word "adverse" will have to be changed, although I would caution against changing it in a way that gives people comfort and makes them think there isn't really a conflict. So the premise that the world can't operate as it operates now with commissions, I'm not convinced. I'm not -- you know, I'm missing -- I lose it at first principles.

MR. PIACENTINI: Okay. So maybe, if I can place myself back on earth, my motivation here is in thinking about the costs and benefits of different kinds of arrangements or in rules that might encourage or discourage one arrangement over another to one degree or another. And I'm very appreciative of the information that SIFMA and others have provided that help us think more than we already have about some of the kinds of costs. So I guess I'll just limit myself to one another follow-up sort of along those lines, and it's to one dimension of the cost consideration that I don't think the SIFMA comment and some of the others went into as much. And that has to do with whether -- and again, this goes to business model neutrality -- but whether there really is any difference in the results that will be achieved by the consumer depending on the presence of conflicts and what provisions are or are not in place to mitigate or make transparent those conflicts. Because there is some academic and other research -- the GAO study was mentioned. There are other things, including some that are cited in our proposal, that suggest that people who are engaging in markets where these conflicts exist sometimes end up with poorer performance than those who don't, and that we ought to take that into consideration as well.

So any reactions to that?

MR. NELSON: Well, I think we live in a world that is full of business relation conflicts, and that in our everyday life, we're engaging in a variety of transactions, whether it's for a product or a service. And I don't think this is really all that different, and I actually have faith in the American consumer here and -- as well as the distributors of products, both advisers and consultants, that with good disclosure on what their fees might be and contractual arrangements around what their services are being provided, that a consumer can make an informed decision. I do get obviously very concerned when we try to, I would say, maybe overreach a bit on the regulation and limit the consumer's ability to make a decision, an informed decision, because we've restricted providers of service so much.

MR. LEBOWITZ: I want to thank the panel and also thank the people coming behind them, because we've run a little late and violated my own rule. We may have some additional questions for this panel and certainly maybe for some of the other panels to come. And so we may be presenting questions to them in writing, and those questions and responses will be included in the public record.

MR. MACHIZ: And I have copies of my testimony, which I didn't get a chance to hand out.

MR. LEBOWITZ: Thank you.

(Pause)

The next panel: David Cerner, Ross Bremen and Kent Mason.

(Pause)

For those who are staying, if you'd take your seats and we're going to move on now. Thank you.

Mr. Certner?

Could we have some order here, please? Would people please sit down? Thank you.

Mr. Certner.

MR. CERTNER: Thank you, members of the panel. I am David Certner, the legislative counsel and legislative policy director at AARP. And we thank you for the opportunity to discuss the important issues surrounding who is and who is not a fiduciary under ERISA.

AARP has consistently asserted that investment advice must be subject to ERISA's fiduciary rules, based on sound investment principles and protected from conflicts of interest. The recent financial turmoil and scandals underscore the imperative that such advice is independent and non-conflicted and that the standards governing industry practice involved in rendering investment advice are fair, clear, and easy to understand.

Since ERISA's enactment in the '75 regulation defining fiduciary, it's pretty clear that retirement plans and investments have changed dramatically. As a result, there is no longer any justification, if every there was one, for the current regulations non-statutory based interpretation of "fiduciary." With the shift from DB plans to the self-directed DC plans, investment advice is now given to individuals who may have poor general literacy, with 43 percent of adults with a high school or higher degree falling into a basic or below-basic literacy levels. And as we know, financial literacy, certainly as illustrated by the recent FINRA study, is even lower.

Not only has the emphasis shifted to individual investment advice and 401(k) plans, but the variety and complexity of investments available has radically changed. For example, there were no such things as collateral debt obligations or target date funds back in '75.

And finally, I think we've seen that numerous Supreme Court decisions have left many participants who have been wronged actually without a remedy, effectively leaving unregulated the many entities that deal with the plans. Given all of these changes and others in the benefits industry, we think that doing nothing would simply leave plans and their participants and beneficiaries unprotected.

AARP has also consistently asserted that retirement plan money, which receives a tax incentive and must meet certain tax qualification requirements, deserves a higher level of protection than other types of investments. And therefore the Department should continue to coordinate with the SEC, as you've noted. But we urge that the Department not delay its regulation. While SEC action in this area is obviously important, the two agencies are dealing with overlapping but also sometimes different problems. So in short, we strongly support the Department's decision to update the current definition of fiduciary to better protect the interests of the plans and the participants and beneficiaries.

AARP submits that the regulation should clearly and succinctly state a general rule of the standards under which an entity will be considered a fiduciary. Quite simply, if an entity informs a fiduciary, such as a trustee, or a participant that the fiduciary or participant should purchase a certain investment and the entity is receiving a payment, either directly or indirectly, through the plan for providing that advice, such as a commission, then the entity is a fiduciary. This is true regardless of whether, among other things, there's a preexisting arrangement; whether or not of the frequency of the advice; whether there's understanding that the advice will serve as the primary basis for the fiduciary or participant decision; whether or how the advice is individualized; what the risk tolerance of the fiduciary or the participant is; or the composition of the portfolio. In fact, we think this is a fairly simple rule. If there's advice and there's payment involved, then there's a fiduciary standard.

Entities that are providing the advice concerning proxy voting, selection of investment managers, portfolio asset allocations, selection of the investments from a 401(k) platform, among other activities should also be considered fiduciaries, and that these activities are no different than persons recommending the purchase of a specific investment. The bottom line is that these activities relate to the value of the investments.

We would note that if the Department decided to keep the exemption to the definition of fiduciary based on whether the recipient of the advice knows that they are receiving advice which may be adverse to them, then the participants and the beneficiary should be excluded from any such exemption. This broad exemption would dilute the value of the remainder of the proposed rule as well as the PPA's investment advice provisions. Most importantly, it leaves participants and beneficiaries, many of whom, as noted, have a significant lack of financial sophistication, quite unprotected.

We do agree, however, that mere research or rating of investments, without more, does not make the research or rating entity a fiduciary. Nor should entities that simply provide investment education which discusses broad concepts, such as asset allocation, diversification, and risk tolerance be considered fiduciaries.

We talk about appraisals in fairness opinions. Private and government enforcement actions concerning appraisals and fairness opinions have been, in our opinion, inconsistent and generally inadequate to protect the retirement security of participants and beneficiaries. There has been more than one case where these evaluations have been abusively manipulated to reach a certain result or price.

The similarities between valuations and appraisals with other investment advice is most apparent where a business is valued or appraised for sale or purchase. Like other investment advice, the purchase or sale of the company will be based on the valuation or appraisal. Valuations and appraisals are also performed annually to determine the value of benefits should a participant terminate employment and request a distribution from an ESOP. Although many commentators have argued that these valuations should not be considered fiduciary actions in their determination of benefit amounts, we would note that a court would most likely review the appraiser's valuation under an abuse of discretion standard and thereby would, quite frankly, limit any liability to the appraiser. And as a result, we support the inclusion of valuations and appraisals as fiduciary actions because of their impact on the value of the plan and its benefits.

The Department also asked for comments on whether advice concerning distributions should be covered under its fiduciary definition. AARP believes that the answer really turns on both where the plan assets lie and whether the entity providing advice has a plan relationship with the participant. In other words, is there a potential conflict? As an example, if a participant asks the current provider whether to take a distribution, at what time, in what form, and where and how to invest these plan assets, then the provider is providing investment advice to an individual and should be considered a fiduciary. I mean, in contrast, once the plan assets have been distributed and completely removed from the retirement plan, the individual is no longer a plan participant. But decisions concerning plan distributions themselves are critical to achieving the plan objective of providing retirement security, and decisions made at that time are often effectively irreversible, due to tax consequences and other transaction costs.

In conclusion, we look forward to our continuing work with the DOL to ensure that plans and participants have the full protections under ERISA. Thank you.

MR. LEBOWITZ: Thank you.

Mr. Bremen?

MR. BREMEN: Good morning, and thank you for your time today. My name is Ross Bremen, and I'm a partner in NEPC's defined contribution practice. NEPC is one of the largest consulting firms in the country. We service over 290 plan sponsors and about $350 billion in assets. We're independent, and we represent the interests of plan sponsors and plan participants. We're not investment managers and we are not folks that offer investment products.

I should also point out that we're not attorneys, so our comments reflect our experiences as practitioners as opposed to a legal review of the issues.

The Department has stated that the types and complexities of investment products available to plans have increased, and thus there is a need to reexamine advisory relationships. The Department has also expressed a concern that when advisers are not deemed to be fiduciaries, they may not disclose conflicts to fiduciaries that expect impartiality. We share these concerns.

Today more than ever, plan sponsors regularly ask service providers if they're willing to accept fiduciary status, if they'll serve as a co-fiduciary, or if they manage assets. And while they ask these questions and they get responses, they may not know how to interpret or evaluate the answers. As proposed today, three different answers may have the same meaning. Alternatively, the same answer, that a party is a fiduciary, may have different meanings.

While discretionary managers charge higher fees and seem to accept a higher degree of fiduciary responsibility, the proposed regulations seem to hold all fiduciary advisers to a similar standard. In cases where the same services are being provided, it's our view that organizations should not be able to claim different levels of fiduciary responsibility for those same services. We believe that plan fiduciaries need advice that helps them meet their duty, and while we do think that providers should be able to limit the activities in which they have responsibility, we do not believe providers should somehow be allowed to disclose away or contract away what are clear fiduciary obligations. Ultimately we believe it's critical that plan sponsors, who have a duty to their participants, have a clear understanding of what protections are afforded to them when hiring a service provider.

We support the Department's effort to foster greater clarity, consistency, and transparency. To help fiduciaries achieve necessary levels of understanding, we would ask the Department to focus in three areas.

First, clarify the status of a discretionary versus a non-discretionary fiduciary. Second, further specify the definition of advice. Third, reconsider whether the platform and sales exemptions are the appropriate exceptions to the rule.

First, clarify the status of a discretionary versus a non-discretionary fiduciary. plan fiduciaries are responsible for prudent investment of retirement plan assets. For pension plans, this means that asset allocation decisions need to be made and investment managers need to be selected. Investment committees approach this task in very different ways. Some outsource discretionary management to third parties, while others hire non-discretionary advisers for advice. plan fiduciaries know they must make prudent decisions and are not permitted to fully transfer their obligation to a third party.

It's our opinion that under the current system, plan sponsors do not know if greater protections are afforded when discretionary managers are hired. While discretionary managers knowingly assume control of decision making and accordingly charge higher fees, many plan sponsors believe that they themselves are ultimately responsible for all decisions whether or not the party assumes greater control or not, and choose to work with a non-discretionary adviser.

We believe that service providers who operate in a similar capacity -- in differing capacities should not be held to the same fiduciary standard. For example, a defined contribution record-keeper who happens to assist with a single action, such as a share class selection, is not exerting as much control or providing as much advice as an adviser who advises on most investment activities or a manager that has control of all activities. The fact that a plan sponsor may pay significantly higher fees for a discretionary manager suggests that the industry shares our belief and attributes different levels of responsibility to these advisers. Intuitively, while it might seem clear that these different entities are not equivalent in terms of the role they play, under the current system the parties, even specific individuals, could each be held liable for losses sustained by the plan as a result of rule violations. We ask that the Department help fiduciaries in the marketplace understand to what extent control matters.

Second, further specify the definition of advice. We understand why the Department has put forth a more inclusive proposal. It's our belief that advice is more often fiduciary in nature than service providers may claim. Many commenters have asked that various activities be classified as non-fiduciary in nature. If the Department finds reason to comply with these requests, it's our belief that the Department will need to be very specific with regard to what constitutes non-fiduciary advice. In some cases service providers provide responses to plan fiduciaries based on objective criteria set forth by the plan fiduciary or an independent third party. In such cases, it's our opinion that the service providers are not taking on a fiduciary obligation. However, in many other instances some level of subjectivity is introduced by the service provider. If a fund is being mapped on a like-to-like basis, there must be some assessment of what "like" means and whether the managers are sufficiently similar to pursue such an approach. When preferred manager lists are maintained by service providers, some level of subjective input is required, regardless of whether the screening or narrowing of the universe is plan-specific or not. When managers are reviewed, in addition to performance comparisons, there are often assessments made as to whether the options continue to be appropriate, and service providers are often determining which information to provide, thus introducing some level of subjectivity. When service providers are providing subjective advice, we believe they're taking on a fiduciary role.

Third, reconsider if the sales and platform exemptions are the appropriate exceptions to the rule. Once again, we reiterate our view that advice is more often fiduciary in nature than many service providers may claim. And this is true even in instances where clear conflicts of interest may exist. The proposed regulations provide both a platform exemption and an exemptions for individuals selling a security. In the case of the platform exemption, the Department suggests that in some instances the service provider is offering investments in which the provider has a financial relationship, while in others the plan fiduciary is relying on the service provider to provide impartial investment advice. From our perspective, this raises a fundamental question. How does a plan fiduciary know where the platform ends and the impartial advice begins? Some platforms could include hundreds of options, all with financial relationships, and the service provider might help the fiduciary choose among them. Is this fiduciary advice? In another instance at the other extreme, a platform might include only a handful of investment options. And while the plan fiduciary might acknowledge that there is a financial arrangement with the investment managers in this limited platform, he/she might still be relying on the service provider to provide a series of options that meet ERISA standards.

The other exemption in the proposal relates to the selling of securities. Some comment letters have suggested that the language might be broadened to include the sale of services. The idea would be similar to the platform exemption in that there would be an understanding on the part of the plan fiduciary that natural conflicts would exist, and as such, there should be no expectation of impartial advice. Today it's common for service providers to be required to provide hypothetical line-ups and other potential forms of advice and new business processes, so there's a clear logic to this whole line of thinking. And we will only ask that the Department be very careful in approaching clarifying language. In our view, the sale continues, or it could continue, on an ongoing basis. If there is a need for assistance with share class selection of a particular vehicle or need to change funds in the future, given the indirect forms of compensation service providers receive, the service provider in a sense is continuously selling securities in which it has a financial interest.

We applaud the Department for tackling this very challenging definition of a fiduciary issue. We appreciate the complexities of the issue. On the one hand, a broader definition would foster greater disclosure of conflicts and more accountability to plan fiduciaries. On the other, service providers may choose to avoid providing some levels of service or charge plan fiduciaries higher fees to compensate them for perceived risks. If a more narrow definition is pursued, the challenge will be to define the line in the sand very clearly so that it's clear to plan fiduciaries when they're working with a fiduciary and when they're not. In our view, as many commenters have indicated in their written submissions, plan fiduciaries rely on the data provided to them by service providers, and not all plan fiduciaries make use of independent third parties for advice. Even if they do, today not all third parties communicate the same level of fiduciary standing.

It's critical that plan fiduciaries have advice to them that helps them meet their fiduciary duty. Ultimately if it does turn out that service providers need to assume greater levels of fiduciary responsibility, it might actually be the best outcome for plan fiduciaries and plan participants if they get improved levels, necessary levels, conflict-free levels of advice.

Thank you for your time this morning.

MR. LEBOWITZ: Thank you.

Mr. Mason?

MR. MASON: Good morning. My name is Kent Mason. I'm a partner in the law firm of Davis & Harman, though I'm thinking of moonlighting at Marc Machiz's restaurant later, but ....

(Laughter)

I'm speaking here today on behalf of the American Benefits Council, and we thank the Department for holding this hearing and very much appreciate the opportunity to testify.

I think we understand the Department's desire to update and improve the definition of fiduciary. However, I think in this first cut of this proposed regulation, we have concerns that the proposal cuts too broadly and could have some adverse effect on, I think one of the earlier speakers distinguished between advice, and not necessarily inhibiting advice, but inhibiting investment education and information. And I'm going to walk through eight specific issues, sort of a, you know, the pension version of a Letterman Top Ten minus two. But obviously much funnier.

The first, the "may be considered" threshold seems too low to us. Let's just take an example. I've got a participant who sought out an adviser. They've gone to the adviser; they got their fund line-up; they're sort of settled on it, and they run into -- that particular participant runs into an H.R. person who works for their company. And says, "Gee, you know, I've been fretting about this. Do you think this line-up makes sense? Is it similar to what you see for other people in my situation?" And the H.R. person says, "Hey, you know, I'm not an expert, but it does look similar to what other people are doing. It seems to make sense." That may be considered. That, under our reading of the regulation, that's fiduciary advice. That's not what fiduciary advice is all about. In other words, fiduciary advice, fiduciary standard under ERISA, is the highest standard on -- highest fiduciary standard under the law. and it shouldn't be triggered by casual sort of discussions in the hall. It should only be triggered by a mutual understanding that the advice will play at least a significant role in investment decisions of the recipient. That's issue one.

Issue two. We've had a lot of plan sponsors reach out to us and say, wait a second, you know.

Here's our situation. We have a plan committee of senior executives who make all the decisions with respect to the plan, including big-picture investment decisions: what investment manager to pick, et cetera. But underneath those senior executives is a whole crew of middle-level employees who sort of frame the issues for them, sort of do the research, talk to the investment managers. And all of that research, all of that sort of -- those recommendations, all those middle managers would be fiduciaries under this regulation. And that would be -- finding people to sort of serve in that role is problematic. Getting fiduciary insurance for those people -- problematic. Cost of that fiduciary insurance -- frightening. These are not the decision makers. These are middle level people that help the senior guys frame the issues. We've got to get them out of the definition. We have plan sponsors very concerned about that.

The seller exception: I think with the deletion of the primary basis and the regular basis rule, it puts enormous pressure on the distinction between selling and advising. Because every time I sell, I'm going to say to you, "Hey, this is a good deal for you." That's what selling's about. So I'm making a recommendation. And so I think Alan at one point said, "Is there anything you like?" I think the introduction of the seller exception was a major step forward, and I really think it sort of -- we applaud the department for that. I think it just needs to be expanded and clarified. Let me sort of walk through three examples which illustrate our perspective.

First scenario: Mutual fund family is going out selling its target date fund. Seems clearly covered, selling a product. Scenario two: Another mutual fund family is selling its model portfolio services to compete with target date funds. They're basically selling the same thing. One is covered; one is clearly not, because the second one's a service. No coverage. They're selling the same thing. Third scenario, which I've heard some people say is covered, some people say it's not covered. An adviser with a clear and disclosed commercial relationship to the first mutual fund family sort of sells that mutual fund family's target date fund. Clearly sort of being compensated for this. They're not the principal selling; they're sort of somewhat third party selling with a commercial relationship with the manufacturer of the product. Covered or not covered? The answer is, all three are exactly the same situation. All three are selling and should all three be covered by the seller exception.

Fourth issue: plan menu. I'm going to come at this a little bit differently. I want to come at this I'm a service provider, and I go to a hardware store owner with 12 employees. And I say, "Hey, you know, you're getting up there in age. You really ought to be putting in a plan." And I say, "Here are the 300 options -- investment options that we offer. And by the way, here's this phone book full of data, historical data on all 300. And by the way, when you go through that phone book, good luck, because you have fiduciary duty to make the right choices. And your only alternative to going through the phone book with fiduciary duty is to pay that guy down the street X thousand dollars to make that choice for you." Well, I mean I can tell you, from dealing with these things for many, many years, that hardware store owner's not going to have a plan. Because they're not going through that phone book and they're not paying that guy down the street X thousand dollars. So we -- it's essential that we give the providers some tools to assist. It doesn't mean they give necessarily sort of "this is exactly what you should do." But in our written comment, we sort of give a whole lot of things, some of which, I think, the woman this morning from JP Morgan sort of alluded to that are very important in helping that hardware store owner go through and make selections.

Fifth issue, and this is something, Phyllis, you've touched on a couple of times and I just want to reiterate the importance, which is coordination consistent with the executive order. But coordination with other agencies, you know, in our mind I think we want to emphasize that it is -- and again I want to use your words, just because I'm agreeing with you -- it is not coordination in the sense of telling each other what you're doing, but actually I think you were saying harmonizing the rules. And we can't overemphasize that. And let me -- I want to talk about two examples here.

One -- and again, you alluded to this, and this is the CFTC -- under the law, under the rules, the CFTC would actually require swap dealers who are entering into a swap with a plan to perform functions that would make them fiduciaries. And because they're the other side of the transaction, if they're a fiduciary, it's a prohibited transaction. So the net effect is no more swaps with plans. There needs to be a categorical rule under these regulations that says anything required by the business conduct standards of the opposing party does not make the opposing party a fiduciary. Otherwise, swaps are shut down.

The SEC issue: As everybody knows, the SEC is conducting a study of the fiduciary status of broker-dealers. I think our point here again -- it's coordination on a single standard. The SEC staff has just come out with a study saying having dual standards is confusing and harmful to participants. So if there is a dual standard, one by the SEC and one by the DOL, that is, in the view of the SEC study, harmful and confusing to participants.

Seventh issue, and again, people have talked about this a lot so I'm just going to be very, very brief. In some cases under the regulation, individualized advice is not required, such as a firm newsletter, a brokerage firm newsletter could be fiduciary advice. I think that's been well discussed by other speakers, and I'll just leave it there. But we don't view the brokerage firm newsletters as fiduciary advice.

And the last thing I want to hit is the management of securities. We sort of read the preamble in terms of the issues you wanted to address, and I think we perfectly understand those issues that you want to address. I think our concern is that term is very broad and somewhat frightening. And let me give you an example.

I've got a new trustee, for example, and I'm negotiating a trustee agreement with that trustee. Well, the trustee manages plan assets. So advice with respect to structuring that trust agreement, that's advice with respect to the management of plan assets. So every company personnel who participates in that negotiation -- contract people, ERISA people, securities people -- all those people are fiduciaries. And the scariest part is, so are the people on the other side. The people on the other side are also plan fiduciaries, because in negotiations, you're all been saying, "Here's a good provision for you." If you say that once as a member of the other side -- I'm going to have to take ten more seconds -- if you say that once, you become a fiduciary, and there is no seller exception. Because the seller exception doesn't apply to services. It only applies to products. So every trust agreement would be an automatic prohibited transaction. You need to narrow -- in our view, you need to narrow that definition of what management is to get the sort of well-intended targets you were looking for.

I thank you very much for giving me the extra few seconds, and I'd be pleased to answer any questions, though I'm scared of Phyllis.

(Laughter)

MS. BORZI: Believe me, I'm going to try to get us back on time, because I surely don't want people to miss their lunch.

Mr. Bremen, have you had the kind of experience that I had when I was in the private sector? I understand your distinction between discretionary --

I think I do -- I understand between individuals involved and what did you call them, discretionary -- I thought you called them fiduciaries. But that's -- I don't know -- but it seems to me a non-discretionary fiduciary is an oxymoron. Could you tell me what you meant by that?

MR. BREMEN: Sure. So a discretionary manager is a investment manager who had control of the decisions. They have the ability to analyze data and then pull the trigger. So I think that part of it is pretty clear.

The non-discretionary fiduciary is the adviser who has no control. They have the ability to present recommendations to some other party; ultimately that other party has control. And so they could say no; they could say yes. And so ultimately if you're an adviser and the -- the party with control doesn't take your advice and something goes wrong, does that adviser have the same amount of responsibility as the discretionary manager who has control of all decisions?

MS. BORZI: Okay. I think I understand that better.

MR. BREMEN: Yes.

MS. BORZI: In your experience as a practitioner, have you ever had the kind of experience that I had when I was in private practice where a service provider would approach our clients, represent that he or she was accepting fiduciary responsibility, perhaps even put it in the written agreement that they agreed to be a fiduciary, and then something went wrong. And the Department would come to investigate or they'd get sued by participants, and then the service provider basically walked away from the written representation that they were a fiduciary and hid behind the five-part test to claim they weren't a fiduciary?

MR. BREMEN: So --

MS. BORZI: Have you ever had that experience?

MR. BREMEN: No. I have not been part of a situation like that. No, but I think -- I think the --

MS. BORZI: But what if somebody --

MR. BREMEN: Yeah, I --

MS. BORZI: -- somebody agrees to be a

fiduciary, even puts it in writing. Do you think they should be able to walk away from that?

MR. BREMEN: So I -- so no, I think the challenge is that sometimes there can be differences when it comes to interpreting what the contract said or what the arrangement was. So clearly for a firm like ours where we assume fiduciary responsibility, there could conceivably be cases where we feel we're not a fiduciary. And so I think I gave the example or I mentioned that we believe people can limit the amount of exposure they have because they might agree to be a fiduciary, you know, for a variety of activities, but maybe not some other activity where they have no oversight. So I think the devil's in the details.

MS. BORZI: So, but -- so then you really do agree with Ms. Prange, who said that you could basically disclaim fiduciary duty in some areas?

MR. BREMEN: Well, so my belief is that you're not -- you should be able to not be accountable for certain activities if you're not performing those functions. If you --

MS. BORZI: Agreed, if you're not performing the functions you shouldn't be accountable. But if you agree to perform X, Y and Z --

MR. BREMEN: And then you go beyond and you are, in fact, performing those functions?

MS. BORZI: Right. Even though you say I've only -- I'm only a fiduciary with respect to X, Y and Z.

MR. BREMEN: Well, then, it feels to me in a clear situation like that that you're providing your services as part of your broader arrangement.

MS. BORZI: Okay. I think the other two of you I'll give a bye. Kent, I can see, is relieved.

(Laughter)

But that's because I have other colleagues --

MR. DAVIS: And actually that's -- that's my first question, actually, Mr. Mason. The -- I wasn't clear about your comments. You had eight points that you wanted to address with respect to the reg, and a lot of them seemed to be drafting issues. I just wanted to know -- does ABC accept the basic premise of the reg that the marketplace has become a lot more complicated and, you know, with respect to these advice arrangements, that there would be value in revisiting the definition of fiduciary in the context of the current environment?

MR. MASON: I don't think we have any sort of opposition at all to sort of the revisiting. In other words, it is a different environment. I think that the sort of the point of sort of the improving and updating the regulation is not something that we have any opposition to. I think -- I mean, I think this is a very healthy dialogue here, because, you know, are there sort of things that could be improved about the current reg? Absolutely. And I think as I mentioned sort of earlier during my comments, I think the introduction of a seller exception is an important movement forward. Because I think a lot of this turns on disclosure, and the idea that somebody could communicate to a participant or a plan without full disclosure of sort of their role, I think we think is not the right thing. So I think that sort of moving forward in a direction where sort of their disclosure can clarify the relationship between the two people -- I don't want to call them adviser/advisee -- but between the receiver of information and the giver of information I think is a great step forward. And I think we have a lot of concerns about the current reg, but the process we think is an excellent one. I mean, the hearing here and sort of the extension of the comment period and the -- you know, we look forward to the dialogue on this.

MR. DAVIS: Mr. Bremen? Is that the way to pronounce it?

MR. BREMEN: Yes.

MR. DAVIS: Sorry if I mispronounced. Can you talk a little bit more about plan distributions and what you're seeing in that space? Do you think -- we asked for comment in this area in the reg. Could you just talk a little bit about what you're seeing there? Do you think there'd be some value in extending this conversation of investment advice to plan distributions, and how those conversations are happening?

MR. BREMEN: Sure. So it's clearly a huge issue. If you can't keep participants in a plan where they get the benefit of all the good work that goes into the plan -- the low fees, the good investments, and so forth -- plan participants need some strong vehicle that they can use to ensure that they make it to the finish line. And some -- some plans will actually force participants out if they're age 65 and they're inactive.

So there needs to be assistance for those folks. Historically speaking, any number of service providers have contracted with, say, a single service provider, an insurance company, to provide an annuity solution. There are some other services out there. Kelli Hueler has a product which is a platform where you have multiple insurance companies that are competing. And then there are even other products out there. Because this is such an important issue and because participants really are unable to make a decision on their own, it stands to reason that they require some sort of assistance. So it -- without being the expert in this particular area, it seems reasonable to me that parties that push them towards one product or another, you know, are giving those individuals advice and should be held accountable for the decision to guide them one way or another.

MR. DAVIS: Then you also made a statement earlier about advice being more fiduciary in nature than a lot of service providers want to admit. Could you expand on what you meant by that? Are there examples that you want to share?

MR. BREMEN: Sure. So in the defined contribution world, for example, there are so many activities, whether you're picking a share class, whether you're picking a fund line-up, whether you're helping -- which would be the initial managers you select. If you replace fund managers with other managers, that's what we would refer to as a search. If you help with a mapping, you take one manager out and you migrate those assets to another fund -- you know, all of these activities we would say are fiduciary in nature, because you are selecting the securities the participants are going to be able to invest in. Today as you look across the spectrum of advisers, if you will, it could very well be the record-keeper who is providing assistance, and they may claim not to be a fiduciary. You may have investment consultants that provide the service that may or may not claim to be a fiduciary. And then along the spectrum you have, you know, other parties that may provide that service, and they may claim to be a fiduciary, and then you may still further have the discretionary folks that come in in one way or another. So at least today, you have all of these different parties providing the same service, and yet very clearly some are saying that they're fiduciaries and others are not.

MR. DAVIS: Finally, Mr. Certner. Previous testimony has suggested, at least some have suggested, that the reg as currently proposed will actually reduce the availability of high quality advice, that you see providers decide not to offer it for various reasons. Are those concerns that you share, based on just the things that you see with your members?

MR. CERTNER: Well, obviously the environment has changed over the last ten years, where I think there's a greater understanding about the needs in defined contribution plans. I think the marketplace in that respect has been responding in trying to provide different levels of first, education and then advice to individuals. But -- and from our perspective, we obviously want to encourage advice. But it seems to us a false choice if the choice is between, you know, sort of no advice and bad advice. I mean, we should be able to encourage good independent, non-conflicted advice and encourage the market to move in that direction, not simply to settle for this notion of well, the only advice we can provide is from people who have conflicts. I mean, that just doesn't make sense to us. I think the market, I think, has responded over the last decade, and I think with greater encouragement and clearer rules, we can continue to do that.

MR. DAVIS: Thank you.

MR. LEBOWITZ: So Kent, just maybe you can take a crack at Phyllis' question, you know, the circumstance being an adviser enters into an agreement which says -- in which it says, "I will act in a fiduciary capacity," and then subsequently we come along, open investigation, assert that there was a breach of that fiduciary responsibility. And so the adviser should be stuck with that, right, no matter what? They shouldn't be able to say, well, now let's take a look at the five-part test or however many parts are left to the test?

MR. MASON: I mean, guess my reaction to that is if I as a, sort of a plan or a plan participant do the adviser on the other side who steps up to the plate and says, I am a fiduciary, I guess I have -- it causes me to put my trust in that person to sort of represent me and sort of pursuant to the standards under ERISA. And I think consistent with, I think, your -- the first of your status requirements -- if I acknowledge that I'm a fiduciary with respect to my actions. I mean, that to me -- you know, that to me sort of says, I as a participant or a plan have the right to rely on you as a fiduciary, and the fact that you try and wriggle out later by sort of arguing well, I said it, but maybe I didn't sort of completely live up to it -- I'm not sure we'd have a lot of sympathy there.

MR. LEBOWITZ: Okay. So that's what you mean by mutual understanding?

MR. MASON: Yeah. I mean, I think that -- you know, I think my example sort of on the other end is sort of things that nobody would dream of that their fiduciary relationship has started up. But where it is clear that there is a fiduciary relationship that started up, I don't think we're having any sympathy for the people who sort of say no, I sort of want to sort of take advantage of the fact that even though my participant viewed me as a fiduciary, I -- it's not convenient to sort of live up to that.

MR. HAUSER: Just a couple of quick questions for you, Mr. Mason. The -- I guess for the most part, I don't know if you would take this as reassuring or not, but for the most part it seems to me your eight-point list did go to drafting sorts of issues. You know, the reality of it is that, at least as I read the comments, it seemed to me there's a bit of a tendency to aggressively and broadly read the sweep of the fiduciary provisions and to read the exceptions extraordinarily narrowly, which is kind of the opposite of what plaintiffs normally do. But anyway, that's the level a lot of the comments have proceeded on, and it strikes me, for example, I mean just to use one example, whether or not we achieved it with the language, there's no intention at the Department to prohibit swap dealers from being able to act adversely to plans, when it's clear that they're on the opposite side of the transaction. And we don't really see any inconsistency at all between the two statutory regimes here. So that's pretty plainly just a drafting question, at best.

But so the two questions I have, though, are one, I think the last example you gave had to do with somebody who was giving legal, and I suppose there might be other services, but they're giving legal services and they really are just giving legal services. But is your point of view that the rule ought to be that as long as they're giving legal services, for example, that that shouldn't be covered by the exception? Or -- and it's only when they cross the line and actually start giving financial advice that they might be potentially liable as advisers for a fee? Or do you just think that certain classes of people like attorneys, accountants and the like should just get a pass, regardless of whether or not they do cross the line and start giving kind of conventional financial advice?

MR. MASON: Yeah. I mean, can I answer also your sort of implicit question from where you're outset? Because I actually completely agree with what you said about a lot of this is drafting. And I think that a lot -- because of how central this issue is, who's a fiduciary, that there's a lot of angst. And I think we're feeling it. I'm sure if you're reading comment letters, you're feeling it, too. And so I -- I was talking to one person at the Department, and I said you know, I think two-thirds of our comments, we would all sort of sit down and agree with. It's just sort of a matter of really putting it -- clarifying it, you know, sort of really starkly in the regulations. So I -- I really do agree with your point, Tim, you know.

On your question, I don't think -- I think there are really two issues on that sort of trust agreement issue, but let me answer your specific question. If a lawyer sort of gives legal advice, as for example, "This would be a prohibited transaction. To enter into this swap would be a prohibited transaction. Therefore, I advise against it," that to me is -- you know, could be conceived as legal advice under here. In fact, under my sort of angst theory, that would be fiduciary advice under the reg. But you know, I don't think that was really intended, and I put that in sort of a drafting thing, that if it's pure legal advice, it's not fiduciary advice. If they do cross the line and say, gee, you know, I give you some legal advice, but I, you know, "I'm pretty darned good with investments, too," and start saying and "and this is what I do here and this is what I do here," and there's a clear sort of relationship that grows in terms of sort of adviser/advisee, well, then, they've just crossed the line. And so the fact that they're a lawyer doesn't mean they're insulated from sort of -- from these rules. It just means that when they're acting as such, that they are -- that these rules are not implicated. If they cross the line and establish an adviser/advisee relationship where there's a mutual understanding that the lawyer's advice is going to be given -- have a significant role in investment decisions, then there absolutely should be a fiduciary.

I do think also that this trust agreement issue is broader. It's not just legal. You know, there are also negotiation points. So with someone who's a non-lawyer just says I want this provision to be different from that provision, from the way it's drafted, they would also be -- they would also be a fiduciary under the sort of angst theory of this -- of this reg. And so I don't think it's a pure legal advice point that I was making.

MR. HAUSER: And -- and so you brought up this point about the mutual agreement again in that answer. And I guess a question I have is, well, what -- how -- what does it take in your view to have the kind of mutual agreement, you know, that should be respected? It seems to me there's -- some of the comments from the industry groups talked about the problem of the unwitting fiduciary. But there's also the problem of the kind of unwitting advice recipient who thinks he's dealing with somebody who's a financial adviser and who's in a position of trust who maybe calls himself a financial planner or a financial analyst or a financial adviser, but you know, buried somewhere in the document is -- the documentation is something that says essentially, while I'm giving you advice, you know, you should never just rely on my advice, but rather should consult other professionals and sources. Is that good enough? What kind of disclosure should count, and how do we protect people from thinking they have somebody who stands in a position with respect to them when they really don't?

MR. MASON: And I -- actually I think that's a great question. I'm not sure I have a sort of a perfect answer. I mean, in some sense we're all sort of groping for that, because I don't see it under the regulation, either. In other words -- in other words, we sort of established this threshold, and the threshold -- and I think this is sort of a function of the proposed reg -- is sort of casting the net so broadly that basically anybody who says something about investments is a fiduciary. You know, because it may be considered. And so I'm sort of at loss, like who is really my fiduciary in this situation? Who do I really -- who can I really trust? And you're sort of saying well, if we back off of that and we put this significant role concept into place, how is it that the participants are going to understand who's on their side and who's against them? And I don't have a perfect answer, but I think our recommendation would be do it as much as possible through disclosure. In other words, if I don't want to be the primary basis of the sort of significant role in your decision making, I would say I disclaim fiduciary status. I have some financial interests which may sort of lead me in one direction as opposed to another. And you should seek other advice if you sort of -- if you want to sort of get someone who doesn't have a financial interest.

That -- and again, sort of going back to a question Phyllis would have asked earlier, that would never be dispositive. If I disclaim that and I act differently, I'm still a fiduciary. But at least I'm putting the participant on notice that I'm not sort of taking on that mantle.

I don't know if that's a full answer to your question, Tim, but I think it's a hard question, and I'd like to think about it some more. But I would like to do it through disclosure as opposed to -- I worry that what we've done is we've cast the net too broadly and we're going to inhibit sort of basic -- sort of exchange of information.

MR. HAUSER: Maybe to Joe, why don't you go ahead? I'll come back if there's time.

MR. PIACENTINI: I don't have a question.

MR. HAUSER: Then I'm back.

(Laughter)

I mean, I guess the question I have that I asked of the last panel, too, is I understand the desire to make this a disclosure regime. Which of course isn't generally what ERISA is. I mean, ERISA has disclosure features, but it also requires that if you're a fiduciary, you act in unconflicted ways. And I think part of the premise for that is there are certain situations, at least, where people can't effectively guard against the conflicts. So I kind of have the same question for you. I'm an unsophisticated investor. I don't have years of training in finance. I am not going to be able to intelligently invest my assets without guidance. I've come to you for guidance, and you tell me, "I may have a financial interest in some of the products that I recommend to you. Now," you know, putting your arm around me, "let's talk about how I can plan your financial future so you're secure in your old age." What is it I do with the information about the conflict? How do I protect myself?

MR. MASON: Well, I'm not sure I'll call him co-counsel yet, but you can answer.

MR. BREMEN: So I think the -- certainly disclosure is a great first start. But I think as we said, that we don't think that you can disclose away fiduciary responsibility, which I think is what you're suggesting. And so just because somebody discloses -- someone claims to be a fiduciary, they disclose that they have conflicts, if those conflicts are significant and sort of impair the ability to give good advice, the Department should have the ability to pursue what are sort of horrendous, you know, heinous activities if an investment consultant discloses conflicts.

Say that we -- say that an investment consultant discloses that -- and this is not something that we do, but say that an investment consultant receives compensation from an investment manager for some sort of activity that it engages in. And the plan fiduciary still hires that investment consultant, and then it comes to light that because of the relationship with these different investment managers -- they receive compensation for managers going to a conference or whatever, it somehow led the -- it impaired the investment consultant's ability to give unbiased advice. It seems the Department should have the ability to pursue action in a case like that. I think that certainly disclosure is a great first step, but disclosure in itself shouldn't mean that it puts everybody in the fair and clear of what would be termed fiduciary violations

MR. HAUSER: And Mr. Mason, do you agree with your co-counsel's answer and we'll call it a day?

MALE: Maybe not.

MR. MASON: I enjoyed it. I mean, gives more time to think and all that sort of thing.

(Laughter)

You know, it's interesting, because you're saying ERISA's a disclosure regime, and I understand that. I think when you -- when you move away from regular basis and primary basis, and I'm not trying to second-guess that one way or the other, you -- and this is what I mentioned in the testimony. You put enormous pressure on this distinction between selling and advising. That's what sellers do. Sellers recommend. They advise. That's their business. That's their job, is to say, "This is great for you." And so what you're really doing by taking away those two requirements -- and again, I'm not -- I'm just saying you've shifted the world so that you have to become a disclosure regime, which you recognize by creating the seller exception. So -- so we're not really now -- you know, once we sort of take away the primary basis and regular basis, we have to become a disclosure regime by -- otherwise nobody could sell anything. And so I -- and so I think to me, what I'm saying is if we're across that line, we need to sort of look at how to communicate it effectively. And do I want it to be on page 27 of a 27-page document? I mean, that's not communication. That's not a disclosure. In other words, effective disclosure is what we're looking for. I'm selling you something.

MS. BORZI: So in that case, really what

you're saying is you have to say, "I'm selling you something. This is good for you, but man, it's even better for me." Isn't that the kind of disclosure? If you're going to make money and a substantial amount of money by directing the participant to X rather than Y, isn't that the kind of disclosure you have to make?

MR. MASON: Well, I don't want to say it's sort of better for me. This is -- if you come with my fund, look at the great -- the history we've had. We've done very well for our investors. And what you --

MS. BORZI: Look at what my salary was last year. I've done very well for myself.

MR. MASON: Yes. Yes. And then say, "I don't make money when you go over there."

MS. BORZI: Yeah.

MR. MASON: "I make money when you come here, and you should know that when you're talking to me." And I don't think we have any sort of problem with that kind of disclosure --

MS. BORZI: We've got a model notice, Tim.

(Laughter)

MR. MASON: No, but seriously --

MR. LEBOWITZ: There's an element of this that requires an understanding on the part of the recipient of this disclosure, of this material, as to what you're saying; right?

MR. MASON: Yeah.

MR. LEBOWITZ: It could be on the first page; it doesn't have to be on the 27th page --

MR. MASON: Well, I --

MR. LEBOWITZ: -- and still be incomprehensible.

MR. MASON: Well, you know, I mean I -- I guess Phyllis is -- you're being facetious, but maybe --

MS. BORZI: Moi?

MR. MASON: -- only half facetious. Moi, right. You know, I think the dialogue here in terms of sort of crafting something that is clear and effective is something that we're -- it's in all of our interests. And I actually mean that very -- don't -- don't look at me that way.

(Laughter)

But you know, I do think, and so I think we can achieve this. And I think that we get to a good result.

MR. HAUSER: I'm not sure which way I was looking at you -- (laughter) -- but did -- but would you -- you know, AARP has suggested one circumstance, and maybe more broadly. I mean, are there some circumstances where really the sale, the seller's exception ought to be more restrictive than it is because the sale is really ancillary to what is fundamentally an advice relationship? That the relationship, the participant, the beneficiary, the IRA holder has is primarily with somebody who's giving them advice on how to invest, and occasionally the investor crosses over a line to sell them something, too. I mean, should there be a carve-out for that sort of situation?

MR. MASON: Well, I mean, I guess I'm having a little trouble sort of envisioning your facts, you know, in a sense that if I'm sort of -- I'm normally indifferent with respect to the advice. In other words, I have sort of -- I'm a flat fee. But in certain respects, I could benefit. I mean, I -- and I think we would want to work on some sort of particularized sort of disclosure to say, "Here I don't have any financial interest in your decision. Over here, I have a distinct financial interest in your decision, and you should know about that."

MR. HAUSER: Yeah.

MR. MASON: But the world is built on this. I sort of listened to Norman this morning and sort of saying, he sort of believed the car dealer when he was sort of saying it was a good deal for him. We all have to sort of -- that's what the whole rest of the world is built on sort of listening to the sales pitches and sort of distinguishing. And -- and sort of listening to different sales pitches and sort of seeing who's going to sort of give me the sort of the straightest answer and the best product. So I mean, I don't know why --

MR. CERTNER: I'd just like to add one thing to that, though. Because this is a little bit different context than people just going out in the world and making a purchase. You're in the plan, so you're in a closed universe. And so the adviser that's been put before you is a probably a closed one that's been selected by the employer. And an individual generally tends to trust their employer. And so this person that's being put in front of him is already coming with a different kind of aura as an adviser, regardless of some kind of -- the disclosure regimen than just somebody going out in the world and shopping among people. So I think it's a very different environment here, and I think there's a much higher duty that's required.

MR. LEBOWITZ: Thank you very much.

We will break for lunch and try to get back on schedule. So we'll reconvene at 1:15. Thank you.

(AFTERNOON SESSION)

MR. LEBOWITZ: We can reconvene. The first panel this afternoon is Karin Feldman, Jim McCarthy, and Steve Saxon. Ms. Feldman?

MS. FELDMAN: Good afternoon. I am Karin Feldman, the Benefits and Social Insurance Policy Specialist at the AFL-CIO, and I thank you for the opportunity to present the views of the AFL-CIO and it's more than 50 affiliates representing over 12 million working men and women across the country. We appreciate the opportunity to testify at the hearing today on the Department's proposed rule defining an individual who will be considered a fiduciary, as the result of providing investment advice to a plan or a plan participant. The AFL-CIO supports the Department's decision to update the rule issued more than 35 years ago, and we appreciate its taking the initiative in doing so.

In our view, the proposed expansion of the scope of advice and recommendations that may constitute investment advice is appropriate. We appreciate the specific inclusion of advice or recommendations with respect to the management of securities or other property, as there should be no question that the selection of individuals to manage plan investments falls within the scope of investment advice. That has been the Department's view for many years, and providing explicit regulatory guidance will be helpful to plan fiduciaries.

Perhaps the most significant change or the one that has definitely gotten the most attention are the modifications of the current five-part test for determining whether someone is a fiduciary rendering investment advice. The elimination of the existing requirements that advice be provided on a regular basis, and that it be the primary basis for investment decisions appropriately recognizes that fiduciary status should not depend on these fine distinctions. The proposed rule, in our view, more closely reflects the expectations of plan fiduciaries when they retain investment advice providers, and we believe it will better protect plans and plan participants.

We also wanted to take this opportunity to respond to the Department's request for comments on whether the provision of investment advice should include advice about taking a plan distribution. The AFL-CIO urges the Department to reconsider the conclusion it reached in Advisory Opinion 2005-23A, and include recommendations relating to plan distributions as investment advice. The recommendation to take a distribution and invest the proceeds of that distribution outside the pension plan reflect, if you will, an adviser's opinion about the investment and distribution options under the plan compared to those that might be available in the market. The decision to take a distribution will impact a participant's future retirement security. It could affect future investment returns and the fees charged on any investment. It could affect the availability of payment options, including lifetime income options, and the benefit amount paid under any such option. It could affect the availability of benefits from related plans, such as retiree health care or death benefits. So the ultimate decision to take a distribution is an extraordinarily significant one for a participant, and we believe treating those who make recommendations with respect to that distribution, as fiduciaries, will afford additional protection to participants as they make this critical decision. We think it is especially important that participants be made aware of any financial interest that advisers may have in making investment recommendations, although we are not certain that simple disclosure will be enough.

We have two concerns with respect to the proposed rule that we hope are clarified. One of them was discussed at length perhaps at the last panel; the breadth of the seller's exception set forth in proposed paragraph C(2)(i). While it's even debatable whether this exclusion is appropriate with respect to plan fiduciaries, in our view, it is certainly not appropriate for plan participants. In our view, individuals providing advice to plan participants should and must always be fiduciaries, and they should and must be truly independent advisers. The simple offer of a disclaimer will not be understood, and we don't think, in any event, it goes far enough, because, as has been pointed out, it's unclear what a participant ought to do when faced with that disclaimer. We also have some concerns that the proposed limitation, as applied to participants, undermines the already inadequate protections for conflicted advice afforded by the statutory investment advise prohibited transaction exemption, in sections 408(b)(14) and 408(g) of the statute, and as the members of the Panel well know, much more than disclosure is required under that statutory regime.

Our other concern, which was also touched on during the last panel, is the breadth of the proposed rule and its unintentional potential to treat professionals, who provide services to the plan fiduciaries within the scope of their professions, to treat them as providing investment advice. We do agree that it probably could be addressed simply with modifications to the language or clarifying comments, and we also agree that, if a professional steps across the line, then, consistent with the Department's long-held view about whether professionals, like attorneys, accountants and actuaries could be fiduciaries, it really depends on the actions that they take and what they do, and it should be no different in this instance.

And so we appreciate the opportunity to testify this afternoon, and look forward to attempting to answer your questions.

MR. LEBOWITZ: Thank you. Mr. McCarthy?

MR. McCARTHY: Good afternoon. My name is Jim McCarthy, and I am a Managing Director of Morgan Stanley Smith Barney, in charge of retirement services for our corporate and individual clients. Unlike Kent

Mason, I brought with me co-counsel, who I knew I would agree with. Bill Ryan, seated to my right, is an Executive Director of Morgan Stanley's Legal Compliance Department, responsible for ERISA and tax-qualified issues. Together we would like to thank the Department for the opportunity to address you today to comment on the proposed regulation regarding investment advice and that prong dealing with the fiduciary standards under ERISA.

As we described in our comment letter, we believe the Department should re-propose an amended regulation, or, at a minimum, defer the proposed regulation for further study for the following reasons.

First, as the Department notes, simultaneous regulatory efforts addressing market conduct and fiduciary status have been undertaken by the SEC and the CFTC that's been copiously talked about today. As we read them, the proposed regulation has significant -- has certain specific conflicts in many more places where it is not at all clear to us how these competing frameworks would interact.

Second, it is conceded by the Department that several types of implementation costs of the proposed regulation are currently labeled simply unknown. Additionally, given the number and complexity of the technology systems involved, the effective date, while currently specifically indeterminate, is at 180 days post-publication, calibrated at a point that we believe is physically impossible to achieve. We have some historical data on actual implementation costs and timelines versus prior Department estimates that we think will be helpful for the Department in assessing this claim.

Third, as both the Department and other commentators have noted, we believe that the impact analysis of the proposed regulation has not adequately considered the market impact, both economic and in terms of client choice. The sea change would have unplanned plan participants and IRA holders. I will spend the majority of my later time addressing this issue. First, I will ask Bill to focus on -- just a few minutes on the impacts on our institutional and asset management business, keeping the aggregate remarks within our 10 minutes.

MR. RYAN: Well thank you, Jim, and good afternoon, everyone. I'd like to spend a minute or two discussing -- and I really am going to keep it to a minute or two -- discussing what the regulation may inadvertently do with respect to the availability of plans and plan asset funds to do business with brokers and other counter-parties, and this is both as a broker, as a counter-party, we would say this, and also as an investment manager, since we have both businesses.

Now I think we have talked about the CFTC comments in our comment letter. We also talked about the SEC, section 913 Rule. We are just going to focus on five points in particular, and notice it's three less than Kent Mason, in talking about how the CFTC rules and this proposed regulation interact. As you already probably are painfully aware, the CFTC Business Conduct Rules require swap dealers to provide counter-party or a prospective counter-party with detailed information on the material risks of the swap, the swap scenario analyses, designed in consultation with the counter-party and daily marks and evaluations.

I am not going to try to give a full description of these, but in terms of the five points in particular we would like to focus the Department's attention on.

First, under the proposed regulation, if you are in fact registered as an investment adviser and providing advice for a fee you, are in fact presumed to be a fiduciary. Most counter-parties in the institutional trading market are, in fact, dual-registered as both broker dealers and investment advisers. Under that standard it would generally mean that the broker dealer is presumed to be a fiduciary simply by fact of its registration, and these are all principal transactions where we are the counter-party, our financial interests are diverging from the plans, so the prohibitive transaction concern that we have is real.

Second, if the valuation of daily marks required by Dodd-Frank for swaps, which, even if negotiated between us and the fiduciary, may include non-public information is now under the regulation presumed to be fiduciary; that means, in order to comply with one federal requirement, Dodd-Frank, in providing the information, we may violate ERISA in actually entering into the transactions at all since that simple provision of information could be deemed and should in fact be considered to be part of a fiduciary relationship.

Third, under the current proposal, if all that is required for investment advice under ERISA to be fiduciary is that the communications may be considered as part of a transaction -- and also, when you put that next to the fact that the CFTC rules actually require that you provide this information so it can be considered by the counter-party, we are again concerned about our ability to do the transactions at all.

Fourth, if we are required to, under Dodd-Frank, to make sure the plan representative has sufficient knowledge or information, and we do that by questioning, we again are concerned about whether or not those questions rise to a fiduciary status.

And finally, since the presumption under the regulation that all these actions are the fiduciary, even if we disclaim in writing fiduciary using the seller's exemption, we are not clear that the scope covers any of the subsequent and required oral conversations described above. As the Department has indicated, this can in fact be modified orally.

So whatever comes out of the process, we and others, we believe, need a clear statement from both the regulators, in coordination, that trying to adhere to one set of regulations doesn't in fact cause us to violate another.

Jim?

MR. McCARTHY: Thank you, Bill. First, a bit of context about our retail business. Through Morgan Stanley Smith Barney, Morgan Stanley serves as the broker, custodian and investment adviser for over 3.2 million accounts, of which approximately 2.7 million are IRAs and 500,000 are plans. The value of these $400 billion dollars. We offer a wide range of products and services, such as: plan documents and serving as custodian; brokerage accounts offering the full range of products; equity fixed income notes; other products for which we serve as an underwriter or an agent; mutual funds, both proprietary and not; ETS bank products, et cetera. Most of this business is generally priced on a commission or spread basis. We offer relationships with a wide variety of 401(k) plan recordkeepers and investment providers where we assist in vendor selection and participant education, again, as a broker; investment advisory services for assets, both custody with us and at other institutions, with firm acts and investment advisers under the adviser Act, and from retirement clients, as an acknowledged fiduciary under ERISA.

In reviewing the Department's proposed regulation, we are primarily concerned about and would like to emphasize the following three points.

First, we believe the Department may not have fully appreciated the effective interplay of these rules with the other regulatory initiatives. Both Secretary Solis and the Chairman of the SEC, Mary Schapiro, have acknowledged the importance of coordinating; however, it is clear that the critical objectives in implementing any new fiduciary retail standards cited in the SEC study do not appear to be dealt with anywhere in the proposed regulation. These include the preservation of customer choice, the importance of retaining different delivery markets for products and services, differential pricing for such products and principal trading.

Second, we believe the cost estimates, as to both the cost of implementation as well as the client costs, have been seriously understated. As an example we would offer our own experience to date in complying with the Department's various disclosure projects, notably, the Form 5500 and the upcoming 408(b)(2) disclosure requirements. For the 5500, we would note that the cost estimate proposed by the Department was slightly north of $15 million dollars for the entire service industry, with approximately a two percent market share in the private defined contribution and private defined benefit markets. Morgan Stanley alone has spent, to date, in excess of $17 million dollars in internal and external costs in complying with these requirements.

For 408(b)(2), the construction of various disclosure reports and website offerings to make available and indirect compensation was estimated industry-wide of $59 million. Our spending, not yet complete, is already in the millions. Regrettably a significant portion of this work may, in fact, turn out to have been throw away work, as the imposition of the broader fiduciary status of the proposed regulation will cause certain exemptions to be unavailable, and thus redefine what narrow subset of compensation costs will be permissible going forward. I would emphasize that the enumerated costs of the fiduciary proposal, which we view as the most complex and far-reaching of the three, is currently $2 million dollars.

Third, and most importantly, given the way the regulation has been drafted, we believe that the vast majority of our accounts will need to be treated as ERISA fiduciary accounts. We believe that the impact of this would be no principal trading; which, in the fixed income market, removes a key member of the competitive set; limits access to certain investments the clients want and dictates agency trading, which is frequently more expensive for the retail client to execute; little or no access to underwriting or syndicates in which we act as a lead underwriter, thus impairing the capital raising capacity of corporations and governments, and again depriving clients of desired investments; and no holding of property that does not have an independent market or valuation agent; shifting many of these accounts billed from a commission basis to an all-in advisory fee, which is ironic, in that the SEC and FINRA sanctioned firms that bill clients for accounts that don't transact frequently. In addition to the loss of choice and the likelihood of additional out-of-pocket expense, we believe that the regulations will result in an overall less competitive, higher priced environment. There will be very high costs of re-engineering and ongoing compliance, which will force certain providers from the market, and we believe there will be greater and greater amounts of operational and stress risk capital, which will need to be allocated to these businesses. As everyone learned in the financial crisis, capital is not free. The capital needs will be driven by our regulators -- I'm going to take another 15 to 20 seconds, if that's okay -- our regulators -- ERISA is a prescriptive statute with a default that says everything is a violation. This will narrow the number of exemptions available. Under LaRue, since 2008, you have a vast multiplication in the number of people who can bring suit, and we know that this operational and risk capital, right; those costs will have to be socialized across the marketplace.

So with that I will conclude my remarks. Thank you for the opportunity to testify. We stand ready to answer any questions you may have.

MR. LEBOWITZ: Thank you. Mr. Saxon?

MR. SAXON: Thank you. I am Steve Saxon, I am a partner in a law firm in Washington, D.C., here today on behalf of a number of plan service providers offering a variety of services from investment consulting, recordkeeping, insurance and investment management. We appreciate the opportunity to be here, and I'm going to highlight just a few of the comments that are in our written submission.

Our initial concern is that the proposal applies the fiduciary definition to persons providing investment advice to plans, as defined by the Internal Revenue Code. This expansion should not be adapted for two reasons. First, it provides no additional protection for plans outside of the protections already offered under the Code, although the Code contains provisions generally paralleling risks as prohibited transactions rules, the Code does not otherwise establish standards of conduct for fiduciaries, nor does the Code permit plans or participants to bring suit for breaches of fiduciary duty or prohibited transactions. Secondly, the Department should coordinate with the SEC expanding the fiduciary definition. Under Dodd-Frank, the SEC was directed to study the standards of care that should apply to broker dealers registered under the Securities Exchange Act of 1934. The SEC released a study only in January, and it makes recommendations with respect to a number of issues central to the proposed regulation; for example, the study recommends a uniform standard of conduct for brokers and investment advisers. Accordingly, we urge the Department to review this study and coordinate with the SEC on the proper standard of conduct applicable to broker dealers and investment advisers before finalizing the proposal.

Next I would like to talk about Deseret. The final regulation should affirm the Department's Advisory Opinion, the 2005-23A addressed to Deseret Mutual Benefit Administrators. In this guidance the Department opined that advising a plan participant to take a permissible plan distribution, even when combined with a recommendation as to how the distribution should be invested, does not constitute investment advice, because it does not involve a recommendation or advice concerning a particular investment of the plan. This position was taken by the Department a mere five years ago. We request that the Department not re-write its requirements related to distribution-related discussions with participants. If financial institutions are going to be deemed to be fiduciaries when they provide distribution consulting services, they will simply stop providing those services or participants will be left without information relating to the consequences of plan distributions.

Distribution consulting typically involves a participant who has already made the decision to liquidate his or her individual account balance in the plan. In these cases the participant is not seeking the adviser's opinion about whether doing so is prudent; he or she is seeking advice on the appropriate investments to make following the distribution. In such cases, advice on the distribution proceeds no longer relates to the assets of the plan, and therefore cannot constitute fiduciary activity with respect to the plan. This is particularly important to discourage leakage. In a recent report the GAO found that the substantial majority of leakage from retirement plans was in the form of cash-outs at a job change. The report found that providing information to participants about the long-term effects of these cash-outs would reduce leakage. If the Department changes its existing positions set out in the Deseret opinion, it would essentially remove distribution consulting from the marketplace. This would make it far more likely that this source of information would not reach the participants, and thus exacerbate the leakage problem.

Next, I would like to address the status issue. We think the Department should eliminate the status of a person as a relevant factor under the proposal. With few exceptions, a person's status has never been a basis on which to conclude that the person is a fiduciary with respect to a plan. By structuring the proposed regulation in this way, the Department has established an approach that is incompatible with one of the major tenants of ERISA, that fiduciary status is determined by function. The Department should instead require ongoing services in an explicit and mutual agreement between the parties in order for a person to be deemed to be an investment advice fiduciary. A second problem with the status element of the proposed regulation is that it is unclear how the Department intends a person's status in one context to affect the person's interactions with the plan in a different context. It is well-established under the law that a person may provide both fiduciary, non-fiduciary services to a single plan; in other words, a single organization or person can wear two hats, one a fiduciary hat, the other a non-fiduciary hat. The scope of fiduciary status under ERISA has always been limited by the understanding that a person is a fiduciary only to the extent that he or she performs certain functions. The functional test has been acknowledged repeatedly by the Supreme Court in such cases as Peagram and Mertens. The Department relied on this same concept in the Aetna Advisory Opinion, the 1997 opinion that they issued to me, where recordkeeping activities were deemed non-fiduciary even though an affiliate managed the essence of the plan. Although we do not believe it was the Department's intent to do so, the proposed regulation could be read as a significant departure from this longstanding approach. We request that the Department clarify this issue.

Next I would like to talk about some of the limitations. With regards to the limitations proposed by the fiduciary definition, the final regulation should broaden the scope of limitations to make clear that ordinary, routine sales activities are non-fiduciary. In the context of marketing or making a menu of funds available, our experience has been that plan fiduciaries frequently request a sample or model investment line-up from a prospective recordkeeper.

These services provide useful information to plan fiduciaries and, in many cases, the plan fiduciaries will not consider a prospective service provider that refuses to provide these services. Therefore, our group requests that the Department either clarify that this limitation would accommodate such a request, or broaden the limitation so that it does. These basic sales presentations are necessary to the proper functioning of plans and should not be discouraged by the threat of fiduciary liability.

The final regulation should also clarify the types and frequency of disclosures that plan service providers must make in order to comply with the limitations provided under the proposed regulation. The proposed regulation requires that a person acting as a seller must disclose that the person who is providing advice has interests which are adverse to the interest of the plan, and that the plan is not undertaking to provide impartial investment advice. This requirement forces the service provider to choose between two options; accept fiduciary status or brand itself a conflicted adviser. In any business built on relationships, sellers and buyers both benefit when the buyer feels as though he has received good value. Automatically characterizing the seller relationship as adverse is inaccurate and inappropriate. It would be far more useful for the seller to note that it is not giving advice, but merely proposing a sale, if accompanied by a disclosure simply stating that the seller receives compensation on the products that are sold and that the compensation received may vary by type of products sold, then this would give the recipient better information to form his or her opinion on whether to purchase the product or service being sold.

Finally, I would like to address valuation issues. I must say that most of what was contained in the proposed regulation was not unexpected to me, but the Department's position on valuation was a surprise. To the extent that the Department is concerned about valuation, it should study the issue in light of the recent comments received, and if necessary, should engage in a separate rulemaking process specifically addressing valuation issues. The group is concerned that imposing fiduciary status on persons providing an appraisal fairness opinion or information as to the value of securities of property is overly broad and counter-productive. By way of example we are concerned that custodians will either charge a lot more or exit the business if deemed to be fiduciaries. In any event, the limitation related to reporting a disclosure should not be -- it should not operate to broaden the scope of fiduciary status. As written, this limitation is confusing, because it operates to expand rather than limit the scope of the fiduciary definition. The sub-section implies that preparing valuation reports for other than reporting and disclosure is a fiduciary act. To say that every statement not made for reporting and disclosure purposes that reflects the value of plan investment constitutes advice would be incredible, and we believe, unjustified under the proposed regulation. The Department needs to fix this.

In addition, we are concerned that by characterizing the preparation of a valuation statement as a fiduciary activity, the proposed regulation inadvertently includes a number of activities that simply should not be fiduciary in nature. This would cause many parties -- I have about 10 seconds left -- this would cause many parties, such as appraisers and sub-custodians, to become ERISA fiduciaries to plans where those parties have no direct contractual arrangements with ERISA plans, or even an ability to identify the ERISA plans to which they owe fiduciary duties.

I'll end it there. Thank you very much.

MR. LEBOWITZ: Thank you.

MS. BORZI: Mr. Saxon, let me start with you. Could you tell us who is in your group that you represent? Neither of the comments, the written comments, nor --

MR. SAXON: Yeah. I'll send you a whole list of credits.

MS. BORZI: Okay, great. We'd just like --

MR. SAXON: It's investment consultants, investment managers, banks, insurance companies --

MS. BORZI: Well, we would like to know who they are.

MR. SAXON: I'll send you a list.

MS. BORZI: Okay, great. Let me ask you one more question, and that is, you, as well as many of our other industry witnesses, have used the term coordination; you keep telling us we need to coordinate with the SEC and the CFTC. What exactly do you mean, because one of the other witnesses said talking isn't enough; so what exactly do you mean by coordinating?

MR. SAXON: I actually think that you probably will coordinate. I think that you will designate staff in your department to talk to the folks over at the SEC, to jointly meet and get an understanding of what their concerns, what their purposes are, --

MS. BORZI: Mmm-hmm (in the affirmative).

MR. SAXON: -- how they are going to affect their mission.

MS. BORZI: Well you are not suggesting we -- I mean, ERISA and Dodd-Frank are two very different statutes, very different purposes, very different structures, and to the extent that there is some intersection, it has to do with the types of entities that provide services to ERISA plans and IRA-holders;

so you are not suggesting in this advocacy of coordination that we defer to these other agencies?

MR. SAXON: No. I have always been on the side of the DOL in that regards, so . . . for 31 years. But, what I am saying is that if you have an understanding of where they are going and the changes that they are going to make and how those changes are going to impact how broker dealers and investment advisers operate and that will impact their business, then you need to take that into account so that we don't have one federal agency saying that you must do this, you must disclose this, and we have another federal agency saying something that's quite different, or even probably more likely they are going to set up -- they will just set up a disclosure regimen, and we need to understand where they are going with respect to their disclosure so that we can set up ours in a way that compliments what they are doing, so they are not working at cross purposes.

MS. BORZI: So the word I prefer to use is harmonize, because it seems to me that illustrates, first of all, the nature of the discussions we have had, certainly with the SEC even before the regulation was proposed, because we sent it to the SEC and got their comments and input, before we even sent it forward within the Department or to OMB, because we were trying to be sure that we were harmonizing their regime and our regime. But, the reason I ask you this question about are you -- when you use the word coordinate are you really talking about deferral, is because Mr. McCarthy said something that some of our other witnesses said as well, which is: you want assurances that compliance with one law will make you compliant with another law; so that suggests to me -- I mean that isn't the way laws work in general.

MR. RYAN: Madam Secretary, if I could?

MS. BORZI: Sure, absolutely. Could you explain that to me?

MR. RYAN: Of course. I think Morgan Stanley's concern with respect to the CFTC Rules, in particular, is that the specific legal duties that are required from an entity, as we sort of enumerated, appear to, in fact, be exactly within the scope of what the Department thinks is fiduciary advice. So if that, if we are wrong in that, we are more than happy to be wrong on that, but what we were looking for, at least in the CFTC context, was some clear assurance by the Department that complying with the Business Conduct Rules itself did not implicate negatively on -- by the provision of information marks, et cetera, our ability to serve as a counter-party.

MR. McCARTHY: We weren't looking for a pass --

MR. RYAN: No.

MR. McCARTHY: -- by complying with the CFTC versus the DOL; we just don't want to be in a position of serving one and causing a problem with the other.

MR. RYAN: Right.

MS. BORZI: Yeah. I can understand that. Again, that's why we refer this to a process of harmonization rather than one agency basically strong-arming the other, because it's certainly clear to me, and feel free to disagree if you do, that the fiduciary duties under ERISA are much higher -- the highest standard that we know in the legal world, which is not to denigrate the legal standards in the other statutes, but when you are a fiduciary with respect to a plan under ERISA, it's a higher standard than some of these other statutes.

MR. RYAN: Agreed.

MS. BORZI: And so I get a little concerned when -- I am with you completely, which is the reason that we have been working with these other agencies; that we don't want to put the regulated community in a position where compliance with one law puts them out of compliance with another, but people regularly -- there are regularly multiplicity of laws that a single entity is subject to, and I am not sure where there is any guarantee that the multiple laws that you are subject to, whether they be federal laws or state laws, are exactly the same.

MR. McCARTHY: But --

MS. BORZI: So our goal is to harmonize, but I just want you to understand that harmonization does not mean that we are simply going to roll over and play dead. I hear people say, well you need to wait to see what the FCC is doing or the CFTC, because you can't move forward under your statutory authority until we see what they do. That suggests to me that what you are suggesting to us is that our efforts are inferior to those other agencies' efforts, and I hope that's not what you are saying, but please tell me if that is what you are saying?

MR. RYAN: It is clearly not what we are saying.

MR. McCARTHY: Yeah. Can I take that?

MR. RYAN: Feel free.

MR. McCARTHY: So I think there are two points, right?

MS. BORZI: Mmm-hmm (in the affirmative).

MR. McCARTHY: One is not what we are saying, right, but as the --

MS. BORZI: I didn't want to put words in your mouth; that's why I gave you the opportunity to open it up.

MR. McCARTHY: No. No. But, as the operators of businesses, right, that need to comply with various regulators, we do -- we have two interests, right? One, in making sure that the cost benefit, right; that the solutions aren't proposed, right, against problems that are either nonexistent or less severe than we perceived them to be, and that's what these public forums talk about, right; like, what is the severity of the solution versus the size of the problem? And you have asked some very pointed questions about what people have experienced, you know, in practical everyday life.

The second thing is, just as a practical matter, from a timing standpoint, it's about, you know, can you exercise your statutory authority; but it is the practical implication of saying to a systems community, listen, you need to go program these things and it's got to be done in six months, and you book up their time, right, and there are only so many surgeons that can be around the body at one time, and then another regulator drops out of the sky and says here is another set of requirements that has to be done in a different timeframe, right? Some of these things become physically impossible, right? So we are definitively sensitive to the implementation practicality.

MS. BORZI: And I am completely sympathetic to those arguments. We don't -- there is no mileage in it for us, to drive up plan costs needlessly, because all that does ultimately is take money from benefits.

MR. McCARTHY: Right, the social costs.

MS. BORZI: So we don't start with the idea that we are unmindful of costs, but it's possible, just possible that the cost benefit analysis that we do might vary from the cost benefit analysis that you do. But, the point of this dialogue is so that everybody understands what people perceive the costs and the benefits to be. So I really appreciate your comments.

MR. McCARTHY: If I can make one suggestion?

MS. BORZI: Sure.

MR. McCARTHY: So, in the Federal Impact Statement that's included in all these rulemakings, there is a discussion of the methodology by which the cost benefits -- there are surveys and there are profiles and there are outside entities that presume that -- I am not sure, right? And it may happen that I just didn't get the letter, but I am not sure that there is a process whereby people say, listen, our initial estimate on this was X; and then two years later, when the project is done, we go out and survey the community and figure out the order of magnitude, like, how good were we at estimating, because I would tell you my experience is that the gap is large, right?

MS. BORZI: It's always large, because what you are doing is measuring behavior. I mean all of you and many of the witnesses on our other panel have said advice will dry up, you know; this will cost a gazillion dollars. Well, you know, that's -- you are estimating what the behavior will be.

MR. McCARTHY: No, no. I am saying I can show you $17 million dollars worth of checks we wrote in regard to the 5500 against a $15 million industry-wide estimate, right? I can show you those canceled checks, right?

MS. BORZI: Sure.

MR. McCARTHY: So, in terms of just refining this process, right, I would --

MS. BORZI: It's a continual refinement of the process.

MR. McCARTHY: Right.

MS. BORZI: that's why, when we put out a regulation, you are asked to comment not just on the substance of the regulation, but on the regulatory impact analysis, because, as I said at the beginning, we want to get it right and we want to get it right not just on the substance, but we want to have a genuine, and to the best we can, accurate estimation of what this is going to cost. But, that's why we need to work together, and if you have got that kind of information, that's helpful to us.

MR. McCARTHY: Great.

MS. BORZI: Michael?

MR. DAVIS: Yeah. That's actually what I wanted to ask about, just costs. Mr. McCarthy, you talked about the costs that your firm experienced for the Form 5500. You said there were millions spent on 408(b)(2). I just want to get a sense, as you think about this regulation and then maybe also back to 408(b)(2), how would you categorize those different costs? Is that systems? Is that training? Can you break it down into more specific categories so we can understand it better?

MR. McCARTHY: Sure. Just in terms of the

5500, right, I'll be within a 10 percent kind of tolerance accurate. So we spent $17 million dollars in terms of systems, right, including systems consultants to write requirements and so forth. We spent $7 or $8 million dollars. Now, just -- I want to, in the interest of full disclosure, that's two very large platforms, because we had acquired Smith Barney, right, in a joint venture with Citigroup, so we had two large broker-dealer platforms to do the same work on, right? And the way this works is you would anticipate is we have spent probably $10 million on the first platform and $7 on the second, because we were more efficient and so forth. But, we have spent, as I said, $7 or $8 million dollars on systems work and systems consultants. We spent another $2.5 or $3 million dollars on temp staff, right, to organize the data and get all the -- to review all the sources of fees and revenues and so forth, right, because there is a giant reconciliation that has to be done. We have to take all of this data and kind of match it up. And then the last part of the spend was -- what did we spend, probably a quarter of a million or half a million dollars on legal --

MR. RYAN: It was worth every penny.

MR. McCARTHY: Yes. And then the last part of the spend is, yeah, we had to put in 26 or 28 additional operational people to operate the system, right, that didn't exist before that now exists. So when it's all said and done, right, it equals $17 million dollars, and we can break it out more precisely for you.

MR. DAVIS: But, as you think about the current regulatory initiatives we are talking about today, definition of fiduciary, and you talk about costs and the cost burden, where do you think the cost burden would be created most specifically; would that be a change of business model within the systems again; would that be . . .

MR. McCARTHY: It's a really good question because -- so ERISA is prescriptive, right, which means you have to look at everything to make sure you are not violating a law, right? Because you live in the sea of no until you can get to the island of yes. And, from that perspective, you have to examine every process flow, right? How do you process a mutual fund? How do you process an equity ticket? How do you process a structured investment rate? How do you charge fees, and so forth? So all of those things need to be kind of tracked through. So that is a large amount of chasing the wiring, right; some of which is five years old and some of which is 35 years old. You have to chase the wiring through the entire house to figure out where everything goes, and what are the points of -- where, you know, unshielded things are together and they may short, right? I am staying with that metaphor. So from that perspective, right, we will spend just -- my guess is we'll spend $4 to $8 million dollars with PWC or something -- I am not awarding a bid right now, but with some, you know, kind of systems consultancy, right, to help us with that, right? Because your choices are either maintaining a lot of staff or flexing up using consultants. We will spend probably $2 to $4 million dollars in terms of actual systems programming time. The big issue for us, right, is not going to be -- and that's a big -- so that's a big number, right? My guess is, you know, all in out-of-pocket costs, $10 to $12 million dollars. The bigger issue is there are a whole bunch of things that we do today that we are going to have to do very differently, and that means that whether it's revenue that stops happening, right, or has to be redone in a different way or disclosure. We have 4.5 million retail clients, so one of the things that was in that operational expense that I talked about was we had to send a lot of mailings to clients, right? We had to -- you know, and every time you have to mail something three million times it's expensive, right, not good for the planet; so, from that perspective. So I would say mostly it's about assessment and it's about the build, right? Those are the costs that you would recognize. There is a lot of business practice rework that will come out of this where people will say, hey, we used to do it this way, now we need to do it this way. A lot of the -- as I said before and I think other people have said it, a lot of business will move to flat fee wrapped accounts, right? It's just -- it's going to be the nature of you either have to stop doing something, or you have to price it very differently.

MS. BORZI: Well again you are assuming that commissions are not . . .

MR. McCARTHY: No. I am not assuming that commissions don't matter, right, but if you are doing a business that you either have to tear it down and rebuild the whole thing, right, it may be easier to convince the client, right, and the client is not -- they are not all lambs, right? You know some of them are tigers. It might be easier to convince the client, to say, listen, effectively we were charging you 45 or 105 basic points or whatever it is, right; why don't we just wrap this together, remove the conflicts, right, and go forward? So there will be a lot of transition as far as that goes.

MS. BORZI: And some product transitions?

MR. McCARTHY: Right, and some product transitions. Right. And I haven't talked it -- I haven't even thought about what happens on the institutional platform.

MR. RYAN: That's right. And I think, at least from that side, some of the products and services, people have gone -- I have linked to that principal trading and fixed income and structured notes and underwriting. So, if you think of all of these accounts on the retail space as in fact fiduciary, which is generally where we are presuming, not only are we putting in a wrapped construct, because we think it actually is less likely to be a problem, but we are also excluding certain products, because they can't be offset in terms of the few structures that's put forth in Frost. They can't -- there are no effective ways to necessarily deal with this outside of an open- end mutual fund product. We tend to believe that these are fairly easy -- well easier anyway, to locate, describe and candidly offset. So even within the retail construct it's not only just moving them two products, but it's also, in our view, limiting the types of products that they will be in. And, we know from internal surveys that they are in a lot of these (inaudible) counseling candidly a brokerage IRA sitting next to advisory IRAs with the same client because they wanted certain products that weren't available in the advisory space.

On the institutional side, truthfully, the harmonization point is well-taken. It is literally -- literally though our concern is the cost, and it is the exposure that we have as an institution financially for a risk-based analysis in trying to comply with the prohibited transaction rules.

MR. DAVIS: Thank you.

MR. LEBOWITZ: Mr. Saxon, you testimony in connection with the status, you said that status shouldn't be a relevant factor; that it should be an analysis, but status should require ongoing services and -- and an explicit mutual agreement, arrangement or understanding. So let's go back to this morning's discussion that we had with Kent Mason and others about the circumstance where an adviser and the client sign an agreement, and the agreement establishes a relationship that says -- where the adviser says I am going to be a fiduciary and that's what the plan/client expects. And then later on the adviser says, well, maybe I really wasn't a fiduciary. I may have told you I was, or maybe they tell it to use -- maybe I told them I was, but I didn't really mean it or I didn't really do the things that your current five-part test requires. So is that what you are saying; you want that to continue, right? You want to be able to walk away from your commitment to your clients when you tell them you are a fiduciary, and then say well maybe not, particularly if you lost money as a result of my advice?

MR. SAXON: Here is where I am coming from, and I apologize -- I would like to address your disclaimer point at the same time -- that if you have a contract where you acknowledge fiduciary status, it gets a little bit more complicated than this, but let's assume that it's an investment management-type contract where none of us would -- where you are picking securities, and then the person later on tries to take the position that they weren't recommending securities at all; the facts would be that they were picking securities, and I don't have a problem whatsoever with calling them a fiduciary. I do think though that it's more complicated because sometimes you have contracts where you have the same institution providing investment advisory services alongside a, say a recordkeeping or an administrative component, and what

I want to be crystal clear about is that while we can acknowledge fiduciary status with respect to the aspects of the contract where we fit within 3(21) of ERISA, where we have traditionally taken the view that our recordkeeping administrative services are non-fiduciary, we have a problem with taking the position that because you are a fiduciary under one aspect of the contract, you become a fiduciary with respect to everything that occurs in the contract. This --

MS. BORZI: Well that wasn't what we were suggesting.

MR. SAXON: Okay. That's good. The disclaimer point, I actually have it -- I have litigation in the Federal District Court with respect to this kind of issue. If someone disclaims fiduciary status, in my mind, it becomes a facts and circumstances test. Unfortunately, you probably have an acknowledgement from a plan sponsor that they signed a piece of paper saying, given all the things that you are doing as a service provider, I acknowledge that you are not a fiduciary even though they might be, they might be providing all kinds of investment advice where we would all agree that you are a fiduciary. In those cases, I don't have a problem in holding that person, notwithstanding the disclaimer. It might have been imprudent for the plan sponsor to enter into that contract --

MS. BORZI: Or maybe he wouldn't even know?

MR. SAXON: -- but I would apply the functional test and say, look, if you are providing advice and there is an understanding that the plan sponsor is relying on that advice, and there is an understanding that they are relying on that advice, then you are a fiduciary, and I am comfortable with that notwithstanding the language in the contract. I have another case where we have an investment consultant that had a disclaimer in their contract, and they sat before a trustees meeting year after year on a quarterly basis and made recommendations, not just in front of the trustees, but they made recommendations in front of the outside accountant and the third-party administrator, and everybody heard that person make specific recommendations that you need to be in this particular fund, and then when the fund went south they took the position that they were not a fiduciary. I don't have a problem with bringing a lawsuit against them to the extent that their actions were imprudent.

MR. HAUSER: I just, again, for you, Mr. Saxon, just two line drawing sorts of questions. The first is, I wasn't sure what you were saying with respect to recordkeepers and other folks' advice as to what goes on a fund line-up. Under what circumstances would you think that kind of advice ought to be fiduciary, and under what circumstances would you say it shouldn't be treated as fiduciary advice?

MR. SAXON: Yeah. That's a very tough question. I think the simple answer is that where you provide a generic line-up or a menu, even though you have ratcheted down the number of funds from say 1,000 funds to 100 funds, if you are doing that without any particular plan in mind, you are doing that because you are applying various performance screens to get the very best funds available. The issue is where you are sitting down with the plan sponsor and you offer -- let's say you offer three or four funds in a particular asset category, and you -- I would still say that you are in a non-fiduciary position where you are still providing information on three or four funds, and even if it's, you know, qualifying-type information; this one does this better; this manager has been around a long time; these guys are good in down market, the problem would surface where the plan sponsor says to you, okay, tell me which of these funds I absolutely -- which of these funds is best for me given that you know all about everything that I am doing? And in that, you know, -- and they have been working with them for a long time, then I think that, at that point, you are risking crossing the line. Does that help you?

MR. HAUSER: Well, I am not sure. But, should it matter who is coming -- when you talked about performance screens, should it matter where the performance screens are coming from; whether it's you selecting the sorts of screens that you think that the plan ought to be applying, or whether it's kind of the converse --

MR. SAXON: I really don't --

MR. HAUSER: -- and the plan is saying, here are the benchmarks, find the entities that (inaudible) these?

MR. SAXON: The screens that will involve -- some screens involve analysis against other managers in a particular peer group; others compare against various kinds of benchmarks. What you are suggesting is that because I apply some of my own technical skills on a subjective basis that I have crossed a line. I don't think that should be the key element. I think the key element should be the understanding between the recipient of the advice and the reliance of that and the understanding that they have that this -- I am relying in making this decision based on what you are telling me; rather than the kind of screen that I develop and how -- and what objectivity or subjectivity I have in the screen.

MR. HAUSER: But the way you described it there, it's not necessarily a mutual understanding as to the person's legal status, but rather as to the level of reliance in making a particular fund choice, is that right?

MR. SAXON: Right. Yeah.

MR. HAUSER: Okay. And then the second

question I had, just a similar line-drawing question; I appreciate that you were surprised by the inclusion of valuation firms in the regulation, but even the five-part, you know, test regulation specifically includes advice as to the value of the asset as one of the categories covered in advice; so is there no -- under what circumstances would you think advice as to the value of an asset should be fiduciary, if any?

MR. SAXON: Right. You know, it's funny that you ask that question that way, because I -- we were prepping for this yesterday and I said to my guys, I said, look, if you look at the existing regulation it talks about valuation, and they said to tell to tell you -- so I am going to pass this along to you -- that you have never looked at valuation advice as fiduciary advice before, so this is the first time you are doing it -- but, I have to concede, you look at the regulation, the regulation says what it says, but here is the problem. The problem is that you have a number of appraisal and valuation firms out there that, unlike almost anybody else that we are talking about today in the retirement services space, these folks, they don't understand ERISA; they have never thought of themselves as being ERISA fiduciaries; they have trouble understanding the concept of the highest standard that Madam Secretary was talking about; and they, more likely than anybody else, will exit this business or find some other way to provide services because they are not organized. They don't have the insurance. They don't have expertise to serve as ERISA fiduciaries. But, here is the -- if there is a concept of a solution it would be the following; that wherever you have a valuation provider that's providing that information to some other fiduciary who is making that decision, like a trustee, -- so I am a trustee and I need some expert advice with respect to this property that I am either purchasing or selling, so I go out and I get a valuation firm. The firm doesn't know -- they might even know that they are doing this with respect to a plan; they just know that a financial institution has called them and they have this property, they want them to do -- in accordance with all of their appraisal standards that apply, the MAI standards that they are going to value this property, they are providing that information to the fiduciary. If you look at the way the Department has dealt with this in the exemption process for years and years, that fiduciary takes that valuation as one element of their overall decision-making process. They can rely on it. If the valuation provider did a bad job, then they can sue them for breach of contract. But, I think that you still -- in terms of the protections that the participants have, you still have, in the solution that I have given, you still have a fiduciary on the hook for making that decision and relying on that valuation, and they have to ask the right questions; they have to get the right kind of reputable valuation firm in there, et cetera, to make that decision.

MR. LEBOWITZ: That's current law, isn't it? That's no different from the current?

MR. SAXON: Well sometimes the current law, you don't always have -- you don't always have a reputable fiduciary between making that decision, but, yeah, both, pretty much it is.

MR. LEBOWITZ: Well, I mean, in terms of -- in terms of the target of a lawsuit it's going to be the decision-maker?

MR. SAXON: Yes.

MR. LEBOWITZ: But, the decision-maker is unarmed really? The only information the decision-maker has is from the valuation firm; has no capacity to second-guess it?

MR. SAXON: Well they, under ERISA, they have to ask questions.

MR. LEBOWITZ: So they need a second valuation?

MR. SAXON: They have to go beyond -- well sometimes they do get --

MR. LEBOWITZ: So they need a second valuation to judge the first one, --

MR. SAXON: No, but you have to sit down and --

MR. LEBOWITZ: -- and then maybe a third one to judge the second one?

MS. BORZI: And then they are all out of the test, the five-part test?

MR. SAXON: First of all, as you know, you have to make a prudent decision on selecting the valuation firm to make sure that they have the right kind of qualifications and experience. You would look at -- you would tear apart the valuation if they, for example, they had a -- if they had a list of comparables that were somewhere between 98 and 100, but they selected a value of 110 for this particular asset, you would have to ask them well why; everybody else is between 98 and 100?

MR. LEBOWITZ: Yeah. I mean I think there is a reason why fiduciary, plan fiduciary decision-makers hire a valuation firm to advise them, because they are not capable of tearing apart the valuation. That's not what they do. They do whatever their business is. That's what they do.

MR. SAXON: But, I mean, I'd like to flip it around, because I have been -- I have sat across from you guys for so many years where you have told me that that fiduciary has a responsibility to ask questions.

MR. LEBOWITZ: Because that's the inevitable consequence of the current regulation; that's where it leads us. It doesn't lead us to the individual whom we think is really the culpable party, or at least being able to include the individuals whom we think are culpable in the fiduciary breach into, you know, into a legal action.

MR. SAXON: Well, we disagree on that one.

MR. LEBOWITZ: We have to move on too. Joe?

MR. PIACENTINI: Okay. I'll limit myself to just one question, and it's for Mr. McCarthy. I think it was in response to a question from Mr. Davis that you talked about what you called business practice re-work, and you said something about how an account that was, you know, where the revenue was generated one way, how that might be able to be restated as an equivalent flat fee, or something to that effect? Did I understand that correctly, or can you elaborate a little bit on that?

MR. McCARTHY: Yeah. I wouldn't say restated, right; I would say restated, right. So you would go to an account, right, that traded with X frequency at Y revenue rate, which produced Z total revenue, and you would say, listen, we are doing business, but because you have a tendency to buy fixed income from us and structured notes, right, those two things are potentially verboten under the new regime; so, in order for us to remove that conflict, right, we should enter into an agreement where you give us Z revenue and you can buy anything, right, whether it's a money market fund or a structured product or whatever, and at the end of the day, right, we take all of the product versus product financial incentive, right, one way or another out of it, right, because you basically levelize all the choices. Now, when I talk about that, right, that is entirely dependent on where the Department comes out on the issue of where levelization happens, right? Today I would say very proudly that we have a regime where, you know, we sold our proprietary retail asset management business, right, so we don't have a retail asset management business, but, you know, whether it's -- whatever the product is within the category, compensation is leveled. Now, I can't tell you that we figured out a way to say, hey, here is an annuity, right, that produces revenue of 200 bases points versus a mutual fund that produces revenue of bases points, because those two things are two fundamentally different structures, and when people try to equate them and say, well you have an incentive to do this, it also does a different thing for the client, right? It has an entirely different cost structure, not just as a result of the expense of distribution, but the expense of the underlying construct, the hedges and so forth, right? So one of the things that we are concerned about, right, is how we address to a client the fact that -- client situations are complicated, right, and the solutions generally will tend to be a quill (ph), right? It's not going to be all of one thing or all of another. So from a -- we deal with asset allocation all the time. We have a generation in and nearing retirement that is precariously saved, at best, and so we have to think about not just asset allocation, right; we have to think about product allocation, in terms of how much of it is market correlated versus how much of it is guaranteed and so forth and put those things together, and all of them, right, we are frequently not the manufacturer, but all of them have different kind of economic dynamics, right? We are concerned, right, about how we have to -- we are in a highly regulated business, so we already disclose all this to the client, right? The question is how we have to characterize the interplay between those different things, right? And that's one of the things they are waiting with -- to figure out where this goes. Does that help?

MR. PIACENTINI: Thank you.

MR. LEBOWITZ: Thank you. The next panel is Ted Novy, Marla Kreindler, and Theresa Atanasio. Mr. Novy?

MR. NOVY: Thank you. Good afternoon. My name is Ted Novy, and I am an attorney in Aon Hewitt's Legal Department. I lead its retirement outsourcing team. I want to thank you and the Department today for the opportunity to testify at these proceedings. Aon Hewitt has extensive experience in both designing and administering retirement plans for mid- and large-sized employers. We are the largest independent provider of administrative services for retirement plans serving more than 11 million plan participants. With Americans' retirement income needs in mind, we support the Department for moving to update the definition of fiduciary. In particular, my testimony today will address the question that the Department posed in the preamble; namely, whether and to what extent investment advice should encompass recommendations related to taking a plan distribution? Aon Hewitt recommends that the Department answer this question in the affirmative; namely, that the final regulation should include recommendations to participants to take plan distributions from their plan accounts. As the Department well knows, many Americans face serious challenges and risks with respect to their retirement concerning inflation, longevity, and market fluctuation. It's no wonder that many Americans are looking for assistance with their retirement challenges; however, too few are equipped to manage their retirement challenges alone, so they rely upon others for assistance. Within the mid-sized and large-sized qualified plan environment, many participants receive access to unbiased advice, guidance and education. The individual retail market also provides a host of options to address these retirement needs, but those choices can be overwhelming to even an informed consumer. Furthermore, when participants from a qualified plan to an individual retail market, they may experience higher fees, which can erode their retirement savings. Also, confused participants are at a greater risk of purchasing products that are inappropriate for their needs, or making decisions based on biased guidance. In some cases there may be benefits to the retirement market, the retail market, that make the move outside the plan worthwhile, but participants must be fully informed about the advantages and the disadvantages.

As we discussed in our comment letter, we believe that the Department should include in the definition of investment advice recommendations to take a plan distribution for two primary reasons. The first is that the participant's decision to take a plan distribution is comprised of two significant decisions affecting the participant's plan assets; namely, whether to liquidate current investments, and how to manage the distribution of funds. Secondly, we also wish to suggest that the failure to include distribution advice under the final regulation may result in an unintended consequence; that is, it may create a bias towards a recommendation from an adviser for a participant to take a distribution so that the adviser is not an ERISA fiduciary, and may provide advice with respect to investments, in which the adviser has a financial interest.

From a participant's perspective, the decision to take a plan distribution is comprised of two smaller, but significant decisions. The first is the participant must decide whether to liquidate current investments. Investment decisions to buy or sell a particular plan investment are at the core of the participant's management of his or her account. This is true whether the sale of the investment is merely as a prelude to investing in another plan investment option, or as a precursor to a plan distribution. Furthermore, the decision becomes even more complicated when the distribution recommendation is with respect to less than a total distribution of the participant's account. The participant is forced to make a decision concerning which investments to retain in the plan and which investments to liquidate and distribute with respect to the distribution advice.

In other words, the participants must decide on the suitability of the investments that stay and those investments that liquidated and the funds that go.

Second, a participant must decide how to manage the distribution of funds from his or her plan account; that includes the time, tax year, the manner, the form, and the future custody of the plan distribution. The decision of where to invest assets outside the plan and to whom to entrust with the custody of those assets is a significant decision. A participant must make this decision, however, prior to the actual distribution while the funds remain in the plan and therefore are plan assets. When the adviser provides advice with respect to either of these decisions, or both, the assets in question remain or are already in the plan; that is, they are still in the plan. Together these two important and inter-related decisions regarding the investment of plan assets can play a significant role in the participant's future retirement savings.

In Advisory Opinion 2005-23(a), the Department determined that a recommendation to take a distribution did not constitute an investment advice because the assets would be invested outside the plan. However, at the time the adviser provided that distribution recommendation, the assets in question were still within the plan; therefore, differentiating between a recommendation to invest in plan options or to invest in options outside the plan create an inconsistency in the application of ERISA fiduciary rules. Or, maybe to phrase the question in this way; why should the advice to liquidate an investment position and take a distribution be treated any differently than the decision to liquidate an investment position and re-invest in a different plan option. This inconsistent position appears to create a potential bias, as I mentioned, towards a recommendation to take a distribution so that the adviser is not subject to fiduciary standard, standard funds of ERISA, and also recommend potentially an investment in which the adviser has a financial interest. We suggest -- that is, Aon Hewitt suggests, that while a participant has assets invested in the plan, any recommendation is a recommendation as to the management of the participant's securities in the plan. Such advice should therefore constitute investment advice under ERISA.

With my remaining time I would like to discuss the costs and benefits related to a more inclusive definition of investment advice. By extending the regulation to include recommendations to take a distribution, we believe the associated costs would be minimal, and the benefits to the participants and beneficiaries would greatly outweigh those costs. We also anticipate that these recommendations with respect to the management of plan assets, if applied consistently, would result in more participants remaining in the plan and not being subject to steerage or inappropriate advice. Retention of assets within the plan provides a participant or beneficiary with a number of rights and protections, including spousal protections that they may not receive outside of the

plan. Examples of those benefits and protections are: they benefit from the protective oversight of a plan fiduciary, who must exercise his or her fiduciary duty with respect to the plan; they also have access to unbiased advice and decision-making tools, and these tools are normally priced at a significant discount compared to individual investment advice that's available in the retail market; there is also a more specialized and tailored plan communications; they would receive fee disclosure, and they would also benefit from the leverage buying power that employer plans can bring to bear. Recommendations to participants and beneficiaries to take a distribution from the qualified plan should be considered in the context of these potential advantages and dollars. Including such recommendations in the definition of investment advice will result in a more balanced and unbiased recommendation considering all options available to the plan participant. That said, we do not believe that the provision of general education and information about the advantages or the details surrounding a distribution should invoke fiduciary status.

In closing, we support the Department's goal of updating the rule for changes in the financial industry, and the expectations of plan participants and beneficiaries. As I have explained, we believe that the goals can best be achieved, in part, by expanding the definition of investment advice to include recommendations to a participant to take a plan distribution. We appreciate the opportunity to share our thoughts with the Department. Thank you.

MR. LEBOWITZ: Thank you.

MS. KREINDLER: Thank you. Good afternoon. Thank you for the opportunity to testify at this important hearing. My name is Marla Kreindler, and I am a partner with Winston and Strawn. I am pleased to testify today on behalf of DCIIA, the Defined Contribution Institutional Investment Association.

Formed last year, DCIIA is dedicated to enhancing the retirement security of American workers through Defined Contribution plans. Our members are leaders in the defined contribution community and include institutional investment managers, consultants, recordkeepers, and others that support our core beliefs. Winston and Strawn is proud to serve as counsel to DCIIA.

To start, we support your commitment to

protect D.C. plans through regulatory initiatives, and thank you for the opportunity to offer our perspectives. In today's testimony, I'll address some of the topics that we included in our comment letter, including recommended revisions and clarifications to the proposed rule, our views on advice regarding distributions, and also our recommendations to withdraw, and, as appropriate, re-propose the rules and provide sufficient time for transition for these important changes.

Turning to our comments to the proposed rule, we support efforts to clearly provide for when a person acts as a fiduciary, and also certainly support fiduciary best practices. At the same time, we believe changes to these fundamental rules should be carefully considered and revised so as not to create unintended consequences or be over-broad. For example, we ask that you consider retaining the requirements that advice be individualized to the needs of the plan, and that the advice be provided as part of a mutual understanding that the advice form the primary basis in the plan's decision-making. Of course, if primary basis were viewed as too limiting, we suggest then, you know, a reasonable solution such that there will at least be a mutual understanding that the advice would constitute a significant factor in the plan's decision-making. Otherwise, we are concerned that these changes could result in significant uncertainty and cause the providers of generic advice to become ERISA fiduciaries. Importantly, we also believe these conditions should apply; so meaning, primary basis and individualized advice and significant factor, at least to registered investment advisers, ERISA fiduciaries and affiliates of registered investment advisers and fiduciaries to have the benefit of speaking and testifying a little later. To answer the question, we are not objecting to when someone acknowledges that they are a fiduciary to being held to the fiduciary standards, but the point is, is that when someone is only an investment adviser or a fiduciary for other reasons, or an affiliate of such a person, that they shouldn't be swept into these rules. So we also suggest that the types of advice covered by the proposed rule, it basically be revised to ensure that only investment advice and not other types of advice be covered. Advice provided by brokers, accountants, lawyers could be swept into the definition of fiduciary advice, and we advise that the precedence, some of which were cited in the preamble to the exceptions under the Investment adviser's Act, which specifically excludes advice provided by brokers, lawyers, accountants and others, under appropriate circumstances, would be something that could be used as a model for this purpose.

Regarding the exceptions, you know, again, we commend you for including exceptions in the proposed rules for sellers or counter-parties, and for investment platform providers. We believe these exceptions are helpful, but, you know, again, suggest that they be revised. For the counter-party or seller exception, we encourage you not to limit the exception to the purchase and sale of securities or property. For example, D.C. plans routinely contract for and conduct RFPs for services. Those responding should not be concerned that their RFP responses would become fiduciary advice. The exception should also apply to other types of plan transactions that may not technically be purchases and sales, such as extensions of credit and finance transactions. As well, we believe that the requirement that a party to be adverse may unnecessarily exclude transactions with parties whose interest are more aligned and less conflicted. And, as others have said, the exception could apply to a broker, but here the key is that if -- the way that the proposed regulation was drafted, that the individualized advice, mutual understanding and primary basis threshold conditions are not required and are not met, so you have someone that is operating where none of those requirements or conditions are met. So there is not individualized advice, not a mutual understanding, no primary basis, then we believe that the broker certainly in that situation should be able to not be a fiduciary when providing information, including about all fees and expenses, and conflicts of interest to the plan.

On a drafting note, we also suggest that the exception be clarified to include not only the initial transaction in question, but modifications and amendments to the transaction.

For the investment platform provider exception, we ask that you clarify the accepted ways in which the information and guidance may be used. In our experience, plans look to platform providers to assist them with narrowing the large number of options that may be available in different ways, as we have heard today. Sometimes plans seek advice through an investment manager or consultant; other times, platform providers may engage independent third-parties to construct a narrow list of funds that may be focused on -- that is not focused on the individualized needs of the plan. In other cases, plan fiduciaries directly request specific information and data to help them meet their fiduciary responsibilities. Narrowing is performed to identify specified significant factors, such as investment performance, cost, manager tenure, et cetera. When these narrowing services are based on objective or third-party criteria, we believe these services alone need not make a platform provider a fiduciary.

We also respectfully request that you

consider adding an additional limitation for when sophisticated parties agree that the provider of advice is not a fiduciary. In our experience, there will be circumstances when a sophisticated plan fiduciary may wish to receive advice that is more limited in scope and not fiduciary in nature. Sophisticated parties for this purpose could include investment managers or other professional fiduciary advisers. It could also include other persons that are sophisticated in these matters. In these cases where the plan is represented by an independent fiduciary sophisticated in these matters, it is clearly disclosed and understood that the services are not intended to be fiduciary, and the advice is impartial and not conflicted, as the outcome of the plan's investment decision. We believe an additional exception should be warranted.

Regarding distributions, we would like to take a minute to address your request for comments. Participants who are nearing retirement have a great need for financial help, but can also be vulnerable to the negative effects of poor conflicted advice. We believe that you should provide guidelines that clearly set out who is and isn't a fiduciary when providing advice on plan distributions, but also suggest a safe harbor for plan sponsors, who select and monitor financial advisers to assist retiring participants, as well as a safe harbor for advisers that set forth the type of information that may be provided to retiring participants. For example, something similar on the lines of your Interpretive Bulletin 96-1, but written in this case with distributions in mind, we believe would be helpful.

Supporting the ability of financial advisers to educate participants about investment alternatives available, as well as about general issues and education is important, particularly as products are continuing to change in this area with lots of emphasis on retirement income today. At the same time, we also believe that advisers who are outside the plan should not be afforded greater access to or influence over plan participants and current plan service providers and believe that there needs to be a balance there as well.

In our comment letter we spoke about some of the cost estimates and coordination, and have listened to your comments today on harmonization of regulatory initiatives and agree that that is desirable. Thank you for that. At the same time, we believe that sharing these perspectives, such as the helpful comment we heard earlier about swaps in written guidance would help address the questions that are being raised in this area.

To conclude, we again would like to thank you for your efforts in considering further the proposed rule and addressing industry comments. We acknowledge that these issues are complex, yet important. Given the very significant and potentially sometimes unintended consequences of the proposed rule, we respectfully suggest that the rule be withdrawn and re-proposed after consideration of the wide range of comments received in today's hearings. Lastly, because the current regulations have been in existence for over 35 years and business practices and systems, as we have heard, have developed over time on that basis, we suggest a transition period of at least two years from issuance of any final rules.

Thank you again for this opportunity to speak to you today. We are happy to answer any questions you may have regarding our comments and this testimony.

MR. LEBOWITZ: Thank you. Theresa?

MS. ATANASIO: We had negotiated that I would have an extra minute from yours, but it looks like it's not going to happen.

Good afternoon. My name is Theresa Atanasio. I am Vice President and ERISA counsel for Ameriprise Financial, a diversified financial services, which being in business for over 110 years, is a leader in financial planning and a member of the Insured Retirement Institute. The Insured Retirement Institute is a non-profit association dedicated to the growth and better understanding of guaranteed lifetime income products that contribute to a secure retirement. IRI represents all segments of the annuity insured retirement product and retirement planning industries with over 300 member organizations, including insurance companies, broker dealers, banks, investment management firms and industry service providers. For the sake of focus and time, I will direct the majority of my testimony today to the practical impact of the Department's proposed regulations on the $4.5 trillion dollar IRA market, as well as the impact on small business owners, who sponsor a retirement plan for themselves and their employees.

Although we agree with the Department's desire to provide clarity around who is a fiduciary for purposes of providing investment advice under ERISA, we believe that the unintended consequences of the rules will have a substantially negative impact upon the very persons the Department is trying to protect. In that regard, many broker dealers, including Ameriprise Financial, support the SEC's efforts to create a uniform fiduciary standard that would apply to brokers and other financial professionals. However, the important difference is that the SEC standard would not prohibit commission-based sales or the sale of proprietary products. It would not favor one business model asset-based advisory fee over another commission-based brokerage. Although the Department's proposed regulations are limited to divining who is a fiduciary under ERISA in the Code, we are concerned about what happens once the definition is expanded to cover everyday activities of broker dealers, insurance agents and financial advisers as they attempt to help their clients. These financial advisers are typically not considered fiduciaries under ERISA today, so they are allowed to provide to their clients, who hold qualified accounts, comprehensive information and access to the full suite of products and services available to non-qualified accounts, including commission-based products, such as mutual funds and annuities. Again, we are not seeking to avoid a fiduciary status, but rather we are supportive of the SEC's uniform standard that would not prevent small business and IRA owners from working with the financial professional of their choice. As you know, approximately 41 percent of U.S. households, or 48.6 million Americans use IRAs to save for their retirement. Making financial advisers fiduciaries under ERISA will reduce both the choice of investments and types of services these IRA owners can access, and will increase their costs and create confusion for both them and the advisers seeking to help them. It also creates inconsistencies and confusion relative to the work being done by the SEC to streamline and simplify the regulatory and investor experience.

As a result of the Department's proposed regulations, financial professionals have to either level fees across a diverse array of investments, use a computer program, or navigate and comply with a patchwork of complex, prohibitive transaction exemptions issued decades ago, and whose applicability has been eroded over time by Department guidance. Practically speaking, trying to use a flat fee model across stocks, bonds, mutual funds and annuities that pay differing compensation results in driving IRA and small business retirement plan owners into wrap programs, which charge a fixed asset-based fee irrespective of the level or type of transaction. While a great option for many investors, wrap programs can be more expensive and are not a good choice for investors who have long-holding periods and individual investments. For these investors, entering into or maintaining a wrap account would actually be more expensive than a commission-based account, and in conflict with existing securities laws. IRA owners would be the most negatively impacted. IRAs, workplace savings, SEPs and Keoghs account for 51 percent of the mass affluence investible assets. Unlike plan participants, IRA owners often don't have access to education or help with investment choices; they need and desire the help of professional advisers.

The remainder of my testimony will be focused on real world examples that highlight some of the concerns I have noted for you. My first example is one where a broker is working with an IRA owner in a mutual fund-based investment account. Mutual funds charge differing fees with equity funds generally charging higher fees and money market funds charging the lowest fees. Under current law, if a fiduciary under ERISA recommends an investment that pays that fiduciary more than another investment, she would be committing a self-dealing prohibitive transaction. On the other hand, if she recommends that a 25-year-old investor purchase solely money market funds, she would be making an unsuitable recommendation and also breaching her fiduciary duty to act in the best interest of the investor; therefore, the client would not be able to invest in different funds offered by the broker.

My second example is one that happens every day. A long-time client walks into a broker's office and asks for investment ideas for his portfolios. The client holds three brokerage accounts: a self-direct brokerage window under his employer's 401(k); an IRA brokerage account funded from the rollover from the client's former employer; and a non-qualified brokerage account funded with after-tax savings. The broker knows that the client plans to use all three of these accounts to fund the client's eventual retirement. The broker explains that she cannot provide any recommendations relating to the client's IRA and 401(k) brokerage accounts; however, with respect to his non-qualified brokerage account, she tells the client she likes the energy sectors, and in particular, Exxon common stock. The client later logs on-line and purchases Exxon in his IRA brokerage account. Arguably the broker could be deemed an ERISA fiduciary under the proposed definition.

As demonstrated by examples one and two, brokers will be unable to sell mutual funds or service commission-based brokerage accounts holding ERISA or IRA assets. Instead clients would be forced into advisory wrap accounts where the broker can be paid an asset-based fee. For clients that hold investments with long holding periods, this would likely result in higher fees and less retirement income. Instead of paying five percent once up front, they may pay one percent per year for 20 years. Advisory wrap accounts are generally not available to clients with small account balances, so these individuals would receive no help with respect to their qualified accounts. Furthermore, certain types of investments, such as annuities, are generally not sold in wrap advisory accounts for good reasons.

First, the sale of an annuity requires substantial up-front work by the financial adviser to determine which annuity is best for the client, which riders are appropriate, and how much of the client's portfolio should be invested in an annuity.

Second, educating clients regarding the need for guaranteed retirement income, and helping them understand the need to part with an access to a portion of their funds as a trade-off for guaranteed income is not an easy process.

Third, these products often have much longer holding periods than mutual funds, as they are purchased to address long-term goals. Even in a variable annuity, there may be a managed account option that does not require additional support by an adviser, and therefore no justification for charging an ongoing advisory fee. The end result of these regulations would be to make IRA owners less likely to have access to guaranteed income.

My fourth example highlights the benefits of a commission-based model for small business employers. Small employers often have very little time to devote to establishing a retirement plan and even less money to do so. Brokers introduce small employers to the idea of adopting a retirement plan often over several years. Fee-only planners do not usually operate in this marketplace because small employers are not willing to pay an advisory fee to set up a plan. Frankly, in most cases, even the commission on the small start-up plan is not enough to justify the time a broker spends educating the employer regarding the benefits of adopting a retirement plan. In most cases the broker is hoping to establish a long-term financial relationship with the small employers and key employees. Removing the financial incentives for brokers to work with small employers will not suddenly make the economics work for fee-only planners. The end result would be fewer small employers adopting retirement plans for their employees.

My final example underscores the premise that clients are best served through long-lasting relationships with their financial adviser. We are concerned that the Department's regulations would be that individuals would receive advice on their 401(k) assets from one professional, advice on their IRA assets from another, and advice on any other assets from a third financial professional. For instance, if a broker recommends with respect to a client's 401(k) client and becomes a fiduciary to the plan as a result, then according to the Department, a recommendation by that broker to roll assets into an IRA sponsored by the broker's firm would be a prohibited transaction. This would result in brokers avoiding providing information relating to a client's 401(k) account for fear of being excluded from advising the client with respect to her distribution decision. The reality is that the biggest mistake made by plan participants is not that they roll their plan assets to an IRA, but that they cash out their retirement plan when they switch jobs. While some commentators have raised concerns that plan participants may receive conflicted advice, these concerns are easily solved through disclosure.

In conclusion, due to the unintended consequences I have outlined here today, we would ask the Department to carve out IRAs from the proposed regulations until such time as it has studied the needs, expectations and services being provided to this diverse marketplace. Today, more than ever, Americans are seeking professional help with all of their accounts in order to plan for a secure retirement; that is why it is vitally important that the Department not consider the definition of who is an investment advice fiduciary under ERISA in a vacuum. Rather, the

Department must consider the impact of such a change on the retirement plan marketplace giving the SEC's fiduciary standard, existing prohibitive transaction rules, and exemptions in effect today.

Thank you.

MR. LEBOWITZ: Thank you.

MS. BORZI: Ms. Kreindler, I have just a couple of questions for you. You veered into the Norman Stein territory of sophisticated investors asking us to distinguish between sophisticated and non-sophisticated investors, and the one thing I heard you say was, for instance, if there were an independent fiduciary . . . are there some other things that you might want to include into that ambit of sophisticated investors?

MS. KREINDLER: Yeah. Sure. I mean that, to me, was a clear example, where, when you have an independent fiduciary that they may -- you know, so the example there would be that they are working with one investment manager and they want to talk to some of their other providers to see what other perspective they may have, but they clearly don't want to pay for it as additional fiduciary advice; they are just asking for information. And, you know, so that would be a clear answer of where the manager is the one that is seeking the information, or the professional. But, other cases could be, you know, scenarios where the party, themself -- you know, so you think of large plan sponsors that have asset size where they routinely manage and definitely have a level of sophistication that can be comfortable saying -- as you did, in a way, in your QDIA regulations, that named fiduciaries should be able to set up custom target glide paths, and be able to do that as sophisticated parties. And so, on a similar analysis, they could also fall within that.

MS. BORZI: On the participant's side, it seems like that would be a much heavier or much more difficult thing to do.

MS. KREINDLER: It could --

MS. BORZI: G. Warren Buffett wouldn't need this kind of advice for his IRA. I wonder if he even has an IRA -- but -- he probably has several of them actually. So how would you do that on the participant's side?

MS. KREINDLER: Yeah. So this exception, in particular, was meant to be separate from and independent of the counter-party or seller exception, and so this really was intended to say that sophisticated fiduciaries --

MS. BORZI: Okay.

MS. KREINDLER: -- will need advice that could be limited in scope and should not have to pay for it as fiduciary advice.

MS. BORZI: There was one other thing that you said that caught my attention and I just -- I don't want to -- I want to make sure that I correctly scribbled down what you said -- I think you said that it's one thing if the adviser within the plan is giving people advice, and that would be fiduciary advice. I think this was in the context of the distribution question. But, I think you said it would be another thing if advisers out of the plan were given special -- outside of the plan were given special access; am I quoting you correctly?

MS. KREINDLER: What we are trying to say is we think the rules should not be biased one way or another to provide special access or, you know, additional relief, if you will, to those either inside or outside of the plan. We think both services are important and critical to have open as a choice for plans and plan sponsors to adopt.

MS. BORZI: Well, the discussion we were having this morning with a couple of the witnesses had to do with -- and the discussion we had in connection with the call center questions really had to do with the adviser who was inside the plan, who, because of that inside the plan special relationship, had access to participants, who then might be steered to another business division or another profit center within the same company or the same group of companies; so I assume your concern there -- I mean our concern and the witnesses who raised this concern was that those folks should not be given some special access, or people shouldn't be steered to another branch of the same company, or another division or another operating center of the same company simply because they had the business from the employer within the plan. I mean how would you respond to that?

MS. KREINDLER: So I think our point really was that the regulation should not create a preference for one over the other. I think the question that you are asking maybe, if I can restate it, is --

MS. BORZI: (inaudible).

MS. KREINDLER: -- yeah -- is really that when someone provides that type of referral or relationship, then is that something that is fiduciary and may be beyond some of the exceptions that are provided, and I think that's an interesting question and one that -- you know, when we look at and when we responded on the platform exception really was -- when the information being provided is generic, when it's -- also at the same time when it is being -- not being individualized, et cetera, then we think that exception applies to that. But, to the extent the line goes beyond that, then, yeah, it raises other questions.

MS. BORZI: So you were more focusing on the advice versus education question, is that it?

MS. KREINDLER: Correct. Yeah. Correct.

MS. BORZI: Okay. Michael?

MR. DAVIS: Ms. Kreindler -- did I pronounce thatch correctly?

MS. KREINDLER: Yes, exactly right.

MR. DAVIS: Okay. I want to make sure I get it right. I wanted to understand about DCIIA. So you represent investment managers, consultants, recordkeepers, insurance companies, plan sponsors. In some cases there might be issues that those subcomponents may have divergent views, and I don't -- we have had representatives from different -- of these subgroups who have expressed different views, so the perspectives that you expressed, I assume with a consensus view among your membership, but can you talk more about just the complexion of your membership? Is it dominated by plan sponsors, or which group dominates?

MS. KREINDLER: You know, so -- thank you. It's a very good question and it's, as a new organization, it's something that we work with.

MR. DAVIS: Right.

MR. KREINDLER: To start with though, what we have found pretty much across the board is where we find consensus among our members is the fact that everyone is really committed to moving the ball forward and to creating better outcomes and better solutions for participants, and so together the group wants to do that. And I didn't include in a long list all the different types of members that we have, because I only had 10 minutes, you know, but the point is that it is institutional investment managers serve on the Board, insurance companies, recordkeepers, providers. I am with a law firm and serve as counsel, and other law firm members are involved too. And, sponsors are involved in an advisory board capacity and are involved at our Executive Committee level, but it is something where we solicit input from providers for the solutions that they are looking for within the marketplace. And, what will be of assistance to them and to meet their needs and try to always keep that ahead of us, and yet at the same time try to address the various different concerns that are being raised about the defined contribution system, and work together to try and create something that's a better product and for better solutions. So, at this point we have really found many opportunities more so for consensus, even recognizing that, yes, we do have members that might have testified and had different comments on these particular regulations.

MR. DAVIS: Okay. But you said plan sponsors acting in an advisory capacity; they are not on the Board, is that correct?

MS. KREINDLER: Yeah. They are currently members of our Executive Committee, correct, and then otherwise it's providers --

MR. DAVIS: Okay.

MS. KREINDLER: -- of various different types.

MR. DAVIS: Okay. And, Aon Hewitt, Mr. --

MR. NOVY: It's Novy. That's all right, Mr. Davis.

MR. DAVIS: You are right. You talked a lot about obviously the distribution issue, --

MR. NOVY: Exclusively.

MR. DAVIS: -- and obviously you guys work with a lot of clients, a lot of plans; --

MR. NOVY: We do.

MR. DAVIS: -- have you seen a lot of

situations where there have been -- maybe the advice was conflicted in the context of plan distributions where you have seen assets get directed in a way that perhaps without these conflicts they would not have been directed in that way, or are there specific conversations that you have observed that you have a lot of concern about?

MR. NOVY: No. I don't think that we are in a position to -- and we haven't made it a practice to assess or evaluate the content of the advice. What we do see though is, upon either termination of employment or separation of service, whatever the circumstance might be, or age, particular attainment of age, the individuals are taking large, if not total distributions, large distributions, and moving it in ways in which have forced us, through many studies, to really look at why is this happening? I think one term that is used in the industry is leakage. And, I think part of the concern is that a portion of these lump sums are losing value not only in the sense of not being rolled over to another tax-sheltered investment, but also the types of fees that we are seeing, these higher fees -- and I think the question really -- it begs the question, do participants really understand the value that they are getting by leaving -- or receiving by leaving their investments in the plan, as opposed to taking a rollover, or an indirect rollover, however their actual form of distribution might actually be? So I don't want to -- just to be clear, Mr. Davis, we are not evaluating the content of the advice.

MR. DAVIS: Okay. That's helpful. Thanks.

MR. NOVY: Sure. Tim?

MR. PIACENTINI: I am struggling how to refine a question I have sort of tried to ask witnesses already. It goes to this question of broker business model. Maybe I'll start this way? Ms. Atanasio?

MS. ATANASIO: Correct.

MR. PIACENTINI: You talked about how sometimes the broker may not --

MR. LEBOWITZ: Can you move the mike closer?

MR. PIACENTINI: -- may not receive, in some sense, adequate compensation in the early stages of business development, and then you said that a flat fee adviser -- that their business model isn't suddenly going to make that possible, but for a broker it's possible. Can you elaborate on that a little bit? I mean what's going on there?

MS. ATANASIO: Sure. The first broker is working under a commission-based model, and so they are looking at differing compensation depending on which investments the individual invests in, and of course there is FINRA and SEC in insurance disclosure around all those fees and the differing compensations.

MR. PIACENTINI: You talked about a small plan --

MS. ATANASIO: Sure.

MR. PIACENTINI: -- where they might be hoping to develop a longer term relationship with the owner, --

MS. ATANASIO: Right.

MR. PIACENTINI: -- with some of the (inaudible).

MS. ATANASIO: Sure. Many times advisers will -- you know, let's say the President or the owner of a small company, and will be working with him or her on all of her portfolios and her household assets, and will say, you know, you should probably look into establishing a retirement plan for you and you are employees. It's a good idea. And, of course, the employer says, no, you know, I am investing in my business right now. I don't have a lot of money to do that, you know. I really got to focus on building my business. And they say, well okay, let's talk about it a little bit more on Tuesday, and they come back on Tuesday and they say, okay, well, it really would be a good idea for you and here is how we can do it. And then that's where the commission-based model works, because it's fairly inexpensive, and even though the broker has worked, you know, maybe three weeks for this maybe smaller commission, what he or she is hoping for is that that owner will say, you know, now come and meet Bob over here in my company, and I think you did a good job for me; whereas, you know, small business owners, you know, do not want to pay somebody $1,500 up front, $3,000 up front to establish a 401(k) plan because of the very reasons I discussed, which is they are trying to invest in their business. They don't really have that kind of money. And, fee-only planners are not really in that market, you know, just because economics don't really work for them. So, if you don't have access to sort of this commission-based model and they won't pay for the advisory fee model, then you end up with no 401(k) plan. Did that answer -- okay.

MR. LEBOWITZ: Thank you. I just had one question, Theresa. At the end of your testimony you said -- toward the very end, you said something about disclosure. I think you said that concerns about conflicts could be easily addressed through disclosure, you said.

MS. ATANASIO: Mmm-hmm (in the affirmative).

MR. LEBOWITZ: But, given the discussion we had this morning --

MS. ATANASIO: Right.

MR. LEBOWITZ: -- about disclosure and, at least some views that it's inadequate to really -- particularly in the context of the receiver of the disclosure really appreciating --

MS. ATANASIO: Right.

MR. LEBOWITZ: -- what the significance of the information is and, at the end of the day, having some idea of what to do with that information; maybe you would like to elaborate a little bit more?

MS. ATANASIO: Sure. I think, you know, there is a great deal of disclosure out there regarding fees and services, and I guess, you know, our viewpoint is -- let me make sure I think through this -- you are right, ERISA is not a disclosure-based regime. And, I think, you know, I am directing most of my comments to the IRA market, which has not really historically been the subject of sort of an ERISA regime, and I think, you know, the SEC is working extremely hard to harmonize and create a fiduciary standard that's going to cover these IRA assets. And I think they will do a great job at it. I think it will be a good, uniform fiduciary standard, and I think to the extent that the Department believes that it has not gone far enough and does not protect those assets, then at that time it could issue additional guidance, perhaps after studying the diverse needs of the marketplace and in greater detail.

MR. LEBOWITZ: Thank you. Thank you, all.

MS. ATANASIO: Thank you.

MR. NOVY: Thank you.

MR. LEBOWITZ: The next panel, Ed Ferrigno, Tom Roberts and Larry Goldbrum.

MR. DAVIS: You guys ready?

MR. FERRIGNO: Yes.

MR. DAVIS: Okay. Let's get started. Ed?

MR. FERRIGNO: Thank you for this opportunity to comment on behalf of the Profit-sharing 401(k) Council of America, commonly known as PSCA. I am Edward Ferrigno, and I serve as PSCA's Vice President for Washington Affairs.

PSCA is a 64-year-old non-profit association representing companies that sponsor profit-sharing 401-K and similar plans. PSCA's members range in size from very small firms to conglomerates with hundreds of thousands of employees.

PSCA supports the Department's initiatives with some reservations that are discussed later in this testimony. The elimination of this objective regular basis and primary basis test will reduce uncertainty for plan sponsors, participants and beneficiaries, and service providers. Today the potential exists for plan fiduciaries and participants to believe that they are receiving impartial advice, while the provider believes that ERISA's fiduciary standards are not applicable. PSCA believes that removing this misunderstanding by applying the fiduciary standard regardless of the regularity of the advice, or to what degree the recipient will consider it is a very positive development. PSCA urges the department to reverse its position that a recommendation to take a distribution, even when combined with a recommendation as to how the distribution should be invested does not constitute investment advice. The decision by a participant or a beneficiary to request a distribution of their account assets and how to subsequently invest those assets can profoundly affect an individual's retirement. We believe the public policy benefit of our position is self-evident, and that a recommendation to take a distribution constitutes a recommendation to sell a particular investment.

The expansion of activities that will be considered advice under the proposed rule raises concerns that the provision of marketing informational and educational materials will be constrained by new liability concerns. PSCA believes the Department shares our concerns, as evidenced by provisions in the proposed rule relating to limitations for selling activities, actions pursuant to interpretive bulletin 96-1, and marketing and assistance provided under platform arrangements. We have several suggestions in this regard.

The Department should clarify in the preamble in the body of the final rule that educating participants about distribution options, including discussions of the advantages and disadvantages of seeking a distribution and managing retirement assets outside the plan does not constitute advice. As long as these communications do not include a clear recommendation to seek a distribution, they should not be treated as advice.

Education information advice regarding the tax effects of taking a distribution should not constitute a provision of advice under the proposed rule. This important information is frequently sought by or provided to plan participants that are contemplating taking a distribution of their plan assets.

In the course of the Department's joint inquiry with the Department of Treasury on lifetime income products, the Agencies requested comments regarding the provision of information to help participants make choices regarding management and spend-down of retirement benefits. PSCA and several other organizations identified the expansion and clarification of Interpretive Bulletin 96-1 to explicitly apply to the provision of information, to help participants and beneficiaries make better informed retirement income decisions. We urge the Department to take this action in conjunction with the development of this rule.

PSCA believes that the limitations in subparagraph (c)(2)(I) for selling activity should be referred to as a provision of a sales proposal, not the provision of advice. A plan fiduciary who makes a decision regarding the investment of plan assets pursuant to a sales proposal is not acting in response to advice. Our concern is that a plan fiduciary that acts on conflicted advice may be liable for a fiduciary breach. We suggest, for purposes of clarity, that the language in paragraph (c)(2)(I) be amended to read: "Knows, or under the circumstances, reasonably should know that the person is providing a sales proposal in his capacity as a purchaser or seller."

The proposed rule specifies in (c)(2)(II)(B) that marketing or making available securities or other property from which a plan fiduciary may designate investment alternatives under a fund platform or similar arrangement does not constitute the provision of advice if certain disclosures are made.

Subparagraph (c)(2)(II)(C) provides the general financial information and data to assist a plan fiduciary's selection or monitoring of such securities or property does not constitute the provision of advice if certain disclosures are made. PSCA strongly supports these provisions and urges the Department to retain and expand them in the final rule. The relief provided for the provision of general financial information and data is currently limited to information provided in conjunction with offering a platform arrangement. It should be available for all plans regardless of whether or not it is offered in conjunction with a platform arrangement.

It's common for fund investment managers to provide newsletters, economic market analyses and forecasts to plan fiduciaries. For example, the recent worldwide debt crisis and its effect on capital markets, the economic impact of the political crises in the Middle East and Africa, or reports about emerging markets, such as China or Brazil, might be discussed in these reports.

Another common topic of analysis is Washington's political environment and its potential impact on industries and markets. These reports and analyses may influence a plan fiduciary's decision about the selection and monitoring of plan investments. PSCA believes that the Department does not intend that these activities constitute the provision of advice. We request the final rule include specific provisions that clarify our interpretation.

Under the proposed rule the provision of advice or an appraisal or fairness opinion concerning the value of securities or other property of an employee benefit plan constitutes a provision of advice. The Department simultaneously announced that the proposed rule supersedes this position in Advisory Opinion 76-65A, where it held that making valuations to be used in establishing an ESOP (ph) does not establish a fiduciary relationship because a plan did not yet exist, and an advice provided to an existing ESOP regarding the value of employer securities also does not constitute the provision of advice. These changes will create a new fiduciary relationship for a large group of service providers that provide valuation and appraisal services for all types of retirement plans. According to the preamble of the proposed rule, the Department would expect a fiduciary appraiser's determination of value to be unbiased, fair and objective, and to be made in good faith, and based on a prudent investigation under the prevailing circumstances unknown to the appraiser. PSCA supports this standard of conduct and generally supports the assumption of fiduciary status by plan service providers that deal with plan investments. However, we also share the significant concerns in the retirement plan community about the increased costs that may result from their proposed changes. For example, questions have been raised of whether the Department's standard of impartiality is consistent with the fiduciary duty of loyalty. The magnitudes of the cost and the willingness of providers to provide valuation services under the proposed rule are, we believe, undetermined. We expect that additional information about the costs and benefits of this proposed change will be provided in this hearing, and we are hopeful that a clearer understanding of the impact of this proposal will result. At a minimum, valuations fairness opinions and appraisals of assets traded on generally recognized markets should never be considered the provision of advice.

Additionally, the Department's position in Advisory Opinion 76-65A that, where a plan is not yet in existence, a fiduciary relationship within the meaning of section 3(21)(a) cannot be established is widely recognized as established law that applies to all retirement plans subject to ERISA. We urge the Department to clarify that it is superseding this particular finding in the Advisory Opinion.

Thank you for considering my comments.

MR. DAVIS: Thanks so much. Mr. Roberts?

MR. ROBERTS: Good afternoon. My name is Tom Roberts, and I am Chief Counsel with ING Insurance U.S., testifying on behalf of the American Council of Life Insurers.

ACLI member companies represent more than 90 percent of the assets in premiums of the U.S. life insurance annuity industry, and offer insurance contracts and other investment products and services to qualified plans, including defined benefit pension and 401(k) arrangements, and to individuals through individual retirement arrangements, or in a non-qualified basis. ACLI member companies also are employer sponsors of retirement plans for their own employees.

We appreciate this opportunity to offer our views of the proposed rule with the Department.

ACLI submitted written comments describing 11 key concerns, and today I focus on three of them: one, the importance of the seller's limitation; our suggestions to ensure that all interested parties clearly understand when advice is subject to ERISA; and lastly, our concerns regarding the proposed rules applicability to IRAs, and the need for further inquiry on the nature of these programs, and the products and services offered to support them.

The proposed rule would dramatically enlarge the universe of persons who owe duties of undivided loyalties to ERISA plans, and to whom the prohibited transaction restrictions of ERISA and the Internal Revenue Code would apply. It substantially broadens the concept of rendering "investment advice for a fee". ACLI appreciates the Department's concern that, under some circumstances, the current rule impinges the Department's ability to bring enforcement actions in situations that are clearly abusive. We share the Department's interest in seeing that plans and participants, who seek out and are promised advice that is impartial ultimately receive advice that adheres to the rigorous standards imposed by ERISA. At the same time, we are concerned that the proposed rule's pursuit of this objective interferes with investment sales and distribution practices that are customary in the marketplace, well understood, and commonly relied upon by financial services providers, plans and participants alike. We are concerned that these changes will result in plans, plan participants and IRA owners having less access to investment information, and/or increased costs. Our comments seek to preserve the Department's enforcement objective while avoiding unnecessary disruption and negative impacts to plans, participants and individuals.

First, we would like to address the seller's limitation of fiduciary status. In the preamble to the proposed rule, the Department notes that, in the context of selling to a purchaser, communications with the purchaser may involve advice or recommendations, and that those communications ordinarily should not result in fiduciary status. We believe that this point is absolutely critical to the development of a workable rule. Persons who are engaged in the sale and the distribution of investment products and services need to have confidence that ordinary course sales recommendations will not, in hindsight, be subjected to a fiduciary standard that disallows the payment of sales commissions and other traditional forms of distribution related compensation.

Parties engaged in transactions with ERISA plans and IRAs need clear, unambiguous rules by which to determine their duties and obligations. Financial institutions, such as life insurers and their sales representatives, should not be treated as fiduciaries under ERISA when they are engaged in selling activities, and are clear that they are acting in a sales capacity. As written, the wording of the seller's limitation, which describes sellers and their agents, may raise some uncertainties about the availability of the seller's limitation for other distribution channels, such as independent insurance agents, insurance affiliated and unaffiliated broker dealers and resident investment advisers that offer life insurance products; whether exclusively, or as many other products from a variety of different product manufacturers. It is essential that these parties be covered by the limitation. The seller's limitation is only available when the recipient of the advice knows or has a basis for knowing that the interest of the selling firm and its distributors are adverse to the interest of the plan and its participants. We think that the word adverse is not the right word to explain that a seller is not impartial. While the seller of a financial product has a financial interest in the outcome of a transaction, we think that it is inappropriate to describe that financial interest as necessarily entailing broad adversity of interest. As responsible providers, we have an interest in seeing that our customers are well-served, that they are happy with their products and services, and that they find our products and services useful to the attainment of financial goals. We believe the seller's limitation should make the point that the seller of an investment or an investment product has a financial interest in the transaction it is recommending. And, so long as purchases are provided with that information, they will have the requisite basis for evaluating the recommended transaction in light of the seller's financial interest, and will be in a position to understand that the selling firm's recommendation is not impartial.

We think the rule should provide an example or examples of circumstances in which a person reasonably demonstrates that the recipient of information knows that a recommendation is being made by a seller. For example, a written representation would suffice if it clearly notes that the person is a seller of products and services; that the person and, if applicable, its affiliates will receive compensation for the selection of the products and services; and that such compensation may vary depending on which product is purchased, or which investments under a product or products are selected. This type of representation would provide a clear indication to the plan, plan fiduciary or participant that the person is a non-impartial seller of products and services, and it would also address the Department's stated concern about undisclosed conflicts of interest. The Department should clarify that the seller's limitation covers all aspects of both an initial sale and the subsequent ongoing relationship between a plan, plan fiduciary, or individual and an investment provider, or any agent, broker, and/or registered investment adviser involved with the sale of the investment provider's products and services. This would include information and recommendations regarding the use of a product; for example, advice regarding the choice of investments available under a product's menu of investments. It is common for Defined Contribution plans to request of potential investment providers a sample menu of investments from among a provider's available investments, which, in the opinion of the provider, best match the plan's current investment options. There should be no expectation that any such recommendation is impartial, or that the plan seeks advice upon which it will rely for its investment decisions. The nature of this relationship should not change after a sale. A product provider, agent, broker, and/or registered investment adviser may continue to make recommendations regarding products and services, and there should be no expectation that these recommendations differ in nature following the initial sale.

I'd like to address next written

representations. In its preamble, the Department expresses the belief that explicitly claiming ERISA fiduciary status, orally or in writing, enhances the the adviser's influence and forms a basis for the advice recipient's expectation that the advice rendered will be impartial. The proposed rule reflects that view by applying fiduciary status to all persons offering those acknowledgments and disallowing the availability of the seller's limitation to such persons. We think prudence dictates that where a plan, plan participant or individual seeks out impartial disinterested advice delivered in a manner consistent with ERISA's fiduciary standard of conduct, then the plan, plan participant or individual should obtain the appropriate acknowledgement in writing in order to secure the acknowledgement in a permanent form. We are concerned about the potential proof issues that are inherent in claims that an adviser provided oral representations of fiduciary status. advisers may be hard put to dispute erroneous or otherwise fictitious claims that oral assurances of fiduciary status were provided. And, for these reasons, we request that the rule be modified to apply only to persons who represent or acknowledge in writing, electronic or otherwise, that they are acting as a fiduciary within the meaning of ERISA with respect to the advice they are providing.

Lastly, we suggest that the Department separately consider a rule for IRAs. We request that the Department take additional time to study the IRA and self-employed markets, and to carefully consider the economic impact of the proposed rule on both individuals and providers of products and services. The Department is separately considering welfare benefit plans under the recently issued 408(b)(2) regulations. We would ask that the Department do likewise for IRAs and for self-employed plans, and hold them apart from the scope of a final rule. The Department should take time to consider the IRA and the Keogh marketplace, and the economic impact that a change to the current rules would have on this retail marketplace. In addition, the Department should consider changes in the regulatory environment affecting retail products; in particular, there are regulatory efforts that are underway by the Securities and Exchange Commission regarding the standard care under the securities laws for broker dealers and investment advisers that provide personalized investment advice about securities to retail customers. On January 21st, 2011, the SEC issued a study on broker dealers and investment advisers, and we think it is essential that the SEC and DOL efforts lead to rules that are complimentary and harmonized in nature. We urge the Department to provide the public sufficient opportunity to consider the SEC's regulatory efforts, and to offer additional comments on the proposed rule.

As we read the proposed regulation, the seller's limitation applies to IRAs. It is common for advisers and for agents to engage customers and perspective customers on their particular goals and objectives in order to better understand their product and service needs. Based on those conversations an adviser might explain the pros and cons of various investment vehicles, including variable annuities, mutual funds, brokerage accounts, banking products, fixed annuities, alternative investments, and several types of advisory accounts, and within each of these types of securities and property, advisers and agents can usually recommend several different specific securities that may have different features. Compensation paid by product and by service will vary. For instance, compensation charged for executing a stock trade will differ from compensation received for selling an annuity. The seller's limitation, with an appropriate indication of the seller's interest, makes it possible to recommend products and services to customers.

I would like to thank the Department again for holding this hearing, and thank you for inviting the ACLI to testify. I am happy to answer any questions you may have.

MR. DAVIS: Right on time. Thanks, Mr. Roberts. Mr. Goldbrum?

MR. GOLDBRUM: Good afternoon. My name is Larry Goldbrum, and I am General Counsel of the SPARK Institute, an industry association that represents the interests of retirement plan service providers, including recordkeepers, mutual fund companies, insurance companies, bank, investment managers and others. Thank you for the opportunity to share our views with you.

The SPARK Institute supports clarifying and updating the definition of who is a fiduciary; however, we urge the EBSA to consider the following five guiding principles as it makes any changes to the rules.

First, any new definition must be clear and precise. It is crucial that service providers are able to structure their products, services and compensation arrangements with reasonable certainty about whether they will be a fiduciary. Absent clear and precise guidance, service providers will be at substantial risk of unintentionally and unwillingly becoming fiduciaries and engaging in prohibitive transactions. Unfortunately the proposal includes broad changes that are unclear and will result in unintended consequences. Additionally, the availability and scope of the proposed exceptions are unclear. Unintentional fiduciary status will be a realistic possibility for service providers. For example, we are concerned about investment platform providers' ability to provide non-fiduciary information and assistance to plan sponsors, to help them narrow down the investment choices available to a plan; for example, from 1,000 funds available on a platform to 30 possible alternatives. We are also concerned about a provider's ability to rely on the seller's exception, because of the complexities associated with the selling process and how and when plan sponsors make plan investment decisions. For example, investment decisions may be made after a General Services Agreement is signed, but the plan sponsor will expect the seller to continue to provide the information and assistance that was provided before the agreement was entered into. The stakes for the service providers are very high because a misinterpretation of the rules or an unintentional violation could affect a provider's entire line of products and services and all of its plan relationships. We urge EBSA to provide clear and precise guidance, and to consider the value, importance and complexity of plan products and services.

Second, any new regulations must provide flexibility and preserve choices. Today's service providers have the ability to structure their products and services so that they can provide fiduciary and non-fiduciary services that plans need and demand. We believe that service providers and plan sponsors should have flexibility and discretion in determining and agreeing on the service provider's role, and whether a fiduciary relationship is mutually expected. The proposal substantially lowers the threshold for when a service provider will be considered a fiduciary, and in some instances, treats some services as investment advice that, in our view, should not be treated as such. As a result, service providers will be forced to discontinue providing many services that plan sponsors demand, or to charge substantially higher fees in order to account for the higher risk and responsibility that comes with being a fiduciary. Many plan sponsors do not want and cannot afford to hire someone to serve in a fiduciary capacity, to provide the limited non-fiduciary assistance that they can get today. If plans are forced to hire fiduciary services, plan participants will ultimately bear the burden of higher fees. We believe that this does not advance EBSA's other goals of facilitating lower cost ways for

American workers to save for retirement.

Additionally, our comment letter included a safe harbor recommendation that would allow service providers and responsible plan fiduciaries to determine and agree, in writing, on the provider's role and whether a fiduciary relationship is mutually expected. The provider would have to disclose the financial interest it may have regarding plan decisions. We recognize that under certain circumstances EBSA would be unwilling to allow the provider and plan representative to agree to non-fiduciary status. For example, when the provider exercises discretion, or when it provides individual investment advice that is clearly and mutually intended to be the primary basis for the plan investment option decisions, those circumstances should be clearly defined in any final rule. We urge EBSA to consider including the safe harbor in its final rule.

Third, any new regulation must avoid unintended potential harm. We are concerned that the proposal is likely to cause such harm and be disruptive to the retirement plan community in at least two ways.

First, as I already mentioned, service providers will likely have to discontinue providing services or start charging higher fees to account for being a fiduciary. Some organizations that represent financial advisers that typically provide fiduciary services will try to convince EBSA that this is a good outcome. Such views seemingly underestimate the issues, concerns and potential harm that are identified in the majority of the comments submitted to EBSA. While the proposal may be good for those who want to serve and charge for serving as a plan fiduciary, it will likely be harmful and disruptive to the vast majority of the retirement plan community, particularly small plans that cannot afford to hire outside fiduciaries.

Second, services providers should not be subject to the significant risks that an arrangement to provide non-fiduciary products and services will be treated after the fact as a fiduciary relationship. Class action attorneys have discovered retirement plans as potentially fertile grounds for large settlements from perceived deep pocket defendants; typically large plan sponsors and service providers. Although they have had limited success on the merits of their cases, the greater risk of hindsight recharacterization of relationships, the increased threat of litigation and the costs to defend against them will have a chilling effect on the retirement plan community.

Our fourth guiding principle is that any changes should be measured and harmonized with other initiatives. The proposed changes are significant and we are encouraged that EBSA is working with the SEC, as it evaluates regulatory action that will have a direct impact on the standards of care and fiduciary obligations of brokers and financial advisers.

We urge EBSA to continue to engage the retirement plan community, as it is doing today, as it evaluates the issues and concerns raised by many different organizations. We believe that significant changes to the proposal are needed, and that the retirement plan community would benefit greatly if EBSA reproposed the modified rule. This will ultimately result in a more harmonized set of regulations governing these matters in a more effective and transition for everyone, including plan sponsors.

Contrary to what has been suggested by the limited number of groups encouraging EBSA to move quickly in finalizing the proposal, uncertainty and consistencies will not benefit or -- help or benefit anyone except for the litigators and perhaps those who want to expand the number of plans for which they provide fiduciary services. I am encouraged by the comments I heard this morning, that perhaps many of our changes and our issues and concerns would fall into the category of line drawing and drafting, so I do want to mention that. That was encouraging.

Our fifth guiding principle is to allow adequate time for compliance. The proposed changes raise very complex issues and will dramatically impact the products and services available to plans, and could have devastating consequences for any provider, who unintentionally and unwillingly becomes a fiduciary. We urge EBSA to allow 18 months from the date that any rule is published for the retirement plan community to evaluate the rules, determine how to comply with them, and for service providers to educate their customers about the rules, and to modify their service arrangements.

Finally, with respect to distribution counseling, the SPARK Institute supports EBSA's efforts to safeguard the interests of participants in connection with plan distributions, and encourages it to develop further guidance, but not in connection with the current effort to redefine who is a fiduciary. EBSA has received many comments on this topic with differing views; however, most agree that plan participants want and need assistance when deciding whether to take a distribution, what distribution to take, and what to do with the proceeds. Groups will disagree over who a participant can trust when seeking help on these issues. We agree that a plan fiduciary should neither be able to act in its own interest, nor be able to influence its own compensation when helping a plan participant with these decisions. We also believe that it is equally, if not more important, for EBSA to consider the concerns about unknown advisers who make cold calls to plan participants, and their ability to exercise greater influence when participants are unable to get the assistance that they need from the plan sponsor and incumbent service providers. Moreover, we do not believe that the solution to this problem is to deem all distribution counseling to be fiduciary activities. That would have a chilling effect on the availability of health. Instead, we urge EBSA to issue additional guidance that is comparable to IB-96-1 that clearly defines acceptable distribution counseling, assistance and education that can be provided by the plan sponsor and incumbent service providers, including plan fiduciaries.

On behalf of the SPARK Institute I want to thank you for the opportunity to share our views.

MR. DAVIS: Thanks so much. We'll turn to the Panel for questions, but first, for the record, I just want to note you guys have harmonized your own choice of wardrobe today. It's very impressive. In the spirit of harmonization, I just want to note that for the record.

MR. GOLDBRUM: It's a shame that we couldn't get a picture.

MS. ATANASIO: Is that a commentary?

MR. DAVIS: We'll start with Virginia.

MS. SMITH: Actually, I noticed that halfway through and for a few minutes I couldn't listen to the testimony.

I do have a couple of questions. My first one is for Mr. Ferrigno. I am intrigued by your recommendation that the Department reverse its position that a recommendation to take a distribution, even when combined with a recommendation as to how the distribution should be invested, does not constitute investment advice, and my question is, do you come to this position based on experience that you have seen? Can you give examples of situations that would cause you to make this recommendation?

MR. FERRIGNO: Well, I mean, we have never thought it made sense from the day it was issued; that, to us, it was self-evident that clearly telling someone to sell their assets in their plan and seek a distribution would constitute advice. And, we always felt that that particular piece of advice was at least as important to the plan participant as any other advice that we could get.

MS. SMITH: Have you seen abusive situations?

MR. FERRIGNO: There are definite abuses from outside advisers that target certain companies that have extremely rich profit-sharing programs, and --

MS. SMITH: Okay.

MR. FERRIGNO: -- and there are stories of people who have been talked into quitting. Even internally there is some level of discomfort in the plan sponsor community regarding rollover activity.

MS. SMITH: Okay. Mr. Roberts, when you were talking about the seller's limitation you emphasized quite a bit about disclosure and all of the things that should be disclosed, in order to take advantage of the seller's limitation, but the one thing that I didn't hear is the amount of the compensation. Do you think that that should be part of the disclosure?

MR. ROBERTS: The amount of the compensation? Well, I mean -- I am with that -- that takes me back to is I know that, you know, some of the prohibited transaction exemptions that were issued years ago provide disclosure-based relief where the amount of the compensation is disclosed. And, what I am thinking of particularly is PTE-8424, which covers insurance agents, and part of taking advantage of 8424 is to disclose the fact that you are being compensated what the amount is to an independent plan fiduciary who would make the purchase decisions. So, philosophically, disclosing the amount of compensation I don't think troubles me.

MS. SMITH: And just one more, if I may? The second point that you made, Mr. Roberts, was that -- that the determination of fiduciary status should only be based on written representations, and I tried to follow what your suggestion was, and it seemed to me -- and correct me if I am wrong -- that what you were saying was really that the burden should be shifted to the plan level fiduciary to get this written acknowledgement of fiduciary status; is that what you were saying?

MR. ROBERTS: Not quite. You know where I was going is that the seller's limitation becomes awfully important to our members, because our members are insurance companies who are in the business of selling insurance products. We are all about selling insurance products, and we need to make sure that we don't find ourselves strained into a situation where we might be deemed to be fiduciaries with an impermissible conflict of interest, so we seek the seller's exception. And, what troubles us in the proposed regulation is that you lose the benefit of the seller's exception if you have asserted that you are acting as a fiduciary under ERISA. So the point I was trying to make is that given the gravity of the loss of that seller's exception to us, we think it should only be subject to being forfeited, if you will, if the assertion or the acknowledgement of ERISA fiduciary status is made in writing; in other words, so you don't have someone saying, you can't take advantage of the seller's exception because you told me you were acting as an ERISA fiduciary, and you get into a quarrel of, well, no, we didn't. We think that something of that magnitude ought to be put in writing if it's going to lead to the loss of that exception.

MR. DAVIS: Mr. Goldbrum, you, in your testimony, you said that if the regulation went forward as proposed there are certain services that would be discontinued, certain retirement services, advice services perhaps. Can you be more specific; what specific would be discontinued and why?

MR. GOLDBRUM: Yeah. Our comment focused mainly on the relationship between the vendor and the plan sponsor, so some examples that we included in our comment letter related to the whole narrowing of the number of funds that are available on a vendor's platform. If the information that a plan sponsor is seeking, whether it's through an RFP because they are asking for a sample line-up or they are asking for specific information in order to narrow a field of funds from thousands down to perhaps the several dozen from which they can choose from, that's considered a fiduciary activity. Then we are concerned that service providers will simply stop providing that assistance and say that in order for us to maintain the service arrangement that we are proposing with you and the fee arrangement that we are proposing with you, we are unable to provide you any information that would cause us to be a fiduciary, or we may have a potential conflict. And we don't think that that's a desirable outcome. We think that, you know, there is a line that can be drawn that would allow service providers to continue to provide information on objective criteria that would help a plan sponsor narrow the field, and then ultimately the plan sponsor would make the final decision. I think based on some of the earlier testimony today, you know exactly where that line will be. You know I don't think that I have the answer for you today as we sit here, but I think that's part of the process that we are encouraging the Department to go through and engage the retirement plan community, so we can see where that line is, and if the line is clear so that both the service provider and the vendor -- the vendor provider and the plan sponsor know where that line is and have mutually similar expectations of what the relationship is.

MR. DAVIS: Thanks.

MR. HAUSER: Mr. Roberts, and this is following up on Virginia's question, but I think the way you put it was, well, if somebody wants a fiduciary sort of relationship with its intending consequences, the burden really ought to be on them to seek it. But, at least when you are talking about, you know, people who aren't plan fiduciaries, but rather are participants, accountholders of one sort or another, I would think that more typically they have an expectation that they are getting fiduciary conduct, and that it's almost the reverse; if you want to assert the seller's exception and you want a very bright line approach to take to avoid it, why wouldn't the burden be on you to get -- essentially to give a statement that's in writing that says I am a seller, I am conflicted, here are the fees I am going to get, and you acknowledge -- and here are the rights you lose if I am not a fiduciary, you know, you won't have a remedy, a loss remedy, you won't be entitled to prudence and loyalty under ERISA, and then say -- and have a signature line that says, never -- you know, yes, you are good to go. Please, don't treat -- don't be a fiduciary. I mean would that be -- that kind of approach work?

MR. ROBERTS: Well, I don't think -- you know I don't think our members have talked about anything quite as extensive as you have just described, but I will say we have talked a fair amount about the fact that -- you know, in situations where we are selling products or services, we want to make sure that the person to whom we are selling understands that, and so we would be comfortable with putting a written statement out saying you should know that we are not an impartial provider of investment advice; we have a financial interest in this transaction and whatever goes along with that. You know in my dialogue with Ms. Smith earlier, what I was trying to get at is, we were concerned about the possibility that even after you had done all of that, you might still lose the benefit of the seller's exception if the person to whom you were selling stood up and said, ah, but, you know, yesterday he told me he was acting as an ERISA fiduciary orally. We think that the threat of losing the seller's exception on the basis of claims of unwritten statements is extremely troubling and problematic, and we think that, given the magnitude of potential loss, it is not unreasonable to ask for a requirement that the loss of the seller's exception occurs when a written representation of ERISA fiduciary status has been given.

MR. HAUSER: Well, would that need to be, in your view, done as a requirement for fiduciary treatment, or could it simply be a safe harbor; you do a statement in this form, you get the participant's signature and acknowledgement, and if you do that, you won't be treated as a fiduciary?

MR. ROBERTS: Well, you know, really my remarks are not aimed at one who is acting as a fiduciary, but rather aimed at the situation where one makes no bones about the fact that they are acting as a seller, but that they are subject to the loss of the seller's exception by claims of unwritten assertions of fiduciary status.

MR. HAUSER: Right. No, I understand, but I guess my question is just in terms of writing a regulation, as I understood while you were saying it, was almost as if, well, this ought to be a requirement of falling outside of the seller's exception is that there be this written statement, but what about just a safe harbor sort of document? I mean, would that just as easily meet your goal?

MR. ROBERTS: You mean a --

MR. HAUSER: I mean essentially a rule that will say, if you have this kind of statement, that kind of argument is going to be unavailing?

MR. ROBERTS: I think we would be quite receptive to that sort of approach.

MR. HAUSER: And then I know, Mr. Goldbrum, you didn't want to do any line drawing, but you know, what -- do you have any advice you would care to give when it comes to this business of giving advice or information, however you want to characterize it, in connection with narrowing down essentially the options on a fund menu or on a plan menu?

MR. GOLDBRUM: With the caveat that I may decide to supplement what I say or revise it, but, yes, I mean, to the extent that you are providing generic information or you are helping serve a plan sponsor narrow down the field based on objective criteria. We mention this in our comment letter. So, you know, when you are looking at historical returns, comparison to a peer group, you know, Morningstar ratings, whatever objective criteria, and you are running the funds that are on your platform through those screens, you know, that should still be considered non-fiduciary assistance. You know there are other situations that we talked about where there are -- in the comment letter where there are problems; you know, handling the plan conversions, you know; what does a plan do with the assets while they are shifting from an old provider to a new provider? plan sponsors are going to want help in understanding, well, should we liquidate all the assets to cash and hold them in cash temporarily; should we put them in some sort of equity fund temporarily while we are conducting the conversion? You know those are other questions that plan sponsors will have where they really do need help from someone who understands the situation, and we are concerned --

MR. HAUSER: It sounds like they need investment advice.

MR. GOLDBRUM: No. I don't think that that is investment advice. I think that that is sort of education of what the different options are; what are the advantages and disadvantages of them so that they can ultimately make an informed decision for themselves. And I think that's where some of the art is in the line drawing is sort of understanding the practical situations, and there are probably about four or five of them that we identified in our comment letter, that service providers are faced with where plan sponsors are coming to them and saying, help us understand what our choices are and what the advantages and disadvantages of those are. And, to the extent that the Department can provide guidance on that as to, you know, what is acceptable education to a plan sponsor in making those decisions versus where does -- where do you become a fiduciary would be very, very valuable. And, I think that should be done in conjunction with any change, because to simply change the definition of fiduciary without telling the industry what is it you can do would be a concern.

MR. HAUSER: Thanks.

MR. PIACENTINI: I guess let me pick up on Tim's question and take it in a little bit different direction. So, if this narrowing down of a menu off of a platform, if that is a fiduciary act, then you said that that would introduce costs, I think?

MR. GOLDBRUM: Well, there are two things that can happen: the plan service providers can simply decide that they are unable to provide that information and assistance because it will cause them to be a fiduciary, and under their fee structure, perhaps engaging in prohibited transactions; or they can decide to re-price their products to factor in the increased responsibility and risk that comes along with being a fiduciary.

MR. PIACENTINI: So I guess my question is, how big is that? Do you see this as a large risk that will be expensive to take on? I mean, I am trying to juxtapose that against your characterization of this process as being one that is based on objective criteria and so forth. It sounds like it's pretty clear-cut and maybe doesn't have much risk, so how do I put that together?

MR. GOLDBRUM: Yeah. You know there are probably others that are, you know, more of the direct service providers that may be able to give you a better sense and may have tried to quantify that, but let me say this; you know, generally the information and the assistance that is provided in the process today is provided at no additional cost. It's, you know, something that can be done and provided cheap, relatively cheaply. But, when you tell a service provider, okay, you are now a fiduciary and you have to figure out what is suitable for that particular plan and what is best for that particular plan, it's going to involve more due diligence; it's going to involve extensive monitoring of and for that plan, and there will be some price to it; whether it's 50, 75, 100 basis points a year, I'm just not able to tell you.

MR. PIACENTINI: Okay. And then one different question, and I guess this is maybe for Mr. Ferrigno. So you talked about your view that a recommendation to distribute an account should be advice; Mr. Novy, in the preceding panel, I think had a similar view, but also went further to say that he thought that the cost of that being fiduciary advice would be minimal. Do you share that view?

MR. FERRIGNO: Yeah, I do. I do. Absolutely. You know, most people today will tell you that they don't provide -- they don't steer people to take a distribution, so basically codifying that shouldn't be a problem.

MR. PIACENTINI: Okay. Thanks.

MR. WONG: I just have one question that I hope is very narrow. It's for Mr. Roberts. I think, in talking about the seller's limitation, you indicated that, by the way, we drafted and used the term agent, it might not encompass other parties involved in the distribution of investments, who might need to take advantage of it. Can you go into a little bit more detail about who some of those parties are and why you are and why using the agent might not capture them?

MR. ROBERTS: Well, you know, true confession; you know, it's partially concerned with the drafting. It's also partially a concern about some of the remarks that were made by various officials from the Department in terms of explaining the regulation immediately after it was published. There was some confusion and some concern frankly amongst our members that, at different points in time, it seemed that it was not clear how far the seller's exception extended; that certain folks, who we would have thought naturally would be recognized as acting in a sales capacity as agents of a seller, if you will, sometimes seem to be covered, and other times seem not to be. So my remarks were really aimed at trying to pin that down once and for all, and to go back to the language that was in the preamble, which seemed to recognize that, if you are engaged in selling activity and you are willing to say you are engaged in selling activity, there shouldn't be a problem in terms of casting you inside the seller's exception and not as an ERISA fiduciary. So when we look at all of the various sales channels we have, we just want to make absolutely sure that they are all available for coverage under that sales exception; whether they are independents; whether they are captives, general agents, what-have you.

MR. DAVIS: Okay. No more questions?

(No audible response).

MR. DAVIS: Okay. Thanks so much.

MR. ROBERTS: Thank you.

MR. DAVIS: We'll call Panel 7. Brian? Here he comes.

MR. GRAFF: I almost didn't make it.

MR. DAVIS: Okay. I think we'll get started with Brian Graff, first on the agenda.

MR. GRAFF: Hi, Michael.

MR. DAVIS: How are you?

MR. GRAFF: On behalf of ASPPA and its sister organizations, NAIRPA (ph)(the National Association of Independent Retirement plan advisers) and CIKR (ph) (the Council of Independent 401(k) Recordkeepers), I thank you for this opportunity to testify today on this important subject.

My testimony today will focus on two points: one, we generally support the proposed change to the basic definition of investment advice, and want to encourage you to stay the course; two, we believe that it is critically important that these rules not apply to IRAs, as such application would effectively create an uneven marketplace playing field, to the ultimate detriment of participants.

Regarding the proposed change to the definition of advice, many of those testifying today, as well as many comments filed, suggest that there is no need to change a definition, since the current definition provides clarity and certainty. We agree, sort of. The current definition does provide clarity on how a non-registered broker or adviser can avoid providing what is considered ERISA investment advice, and thus provides clarity on how a broker or adviser can avoid being subject to ERISA's fiduciary duties. The current definition also certainly is confusing to plan sponsors, who really have no idea whether or not their broker or adviser is providing advice for the protections of ERISA. A recent survey of plan sponsors reported that 60 percent of small business plan owners indicated they received advice on their plan. Well, if that's ERISA investment advice, what are we all arguing about? That would mean that almost two-thirds of small plans are getting served by a fiduciary adviser. Of course, what we believe is that the investment advice most of these small business owners and plans are receiving is actually non-ERISA investment advice, whatever that means, which is really the point. There is nothing clear and certain about that, particularly to a small business owner trying to provide a retirement plan for his or her employees. When a broker or adviser is helping a small business owner set up a 401(k) plan and says to the owner, these are the 20 investment options that you should offer to your plan, that owner naturally thinks he or she is getting advice. If you never heard of the current five-part definition, wouldn't you? In our members' experience, small business owners are rather surprised when they are informed that the advice that they have received for their ERISA-covered 401(k) plan is not actually ERISA-covered investment advice. The idea that the same advice would theoretically have to be given two, three, maybe four times for the advice to be considered ERISA investment advice, under the current rules, it's a victory of form over substance. What should matter most is the perception of plan sponsors, and to them, particularly small business owners, advice is advice is advice. Marketplace confusion about the roles and responsibilities of brokers and advisers is not a new issue, and is definitely not limited to retirement plans. The SEC recently issued a study recognizing that the recipients of advice are often confused about the duties and obligations of the persons providing advice. Some commentators have argued that the Department should postpone its consideration of the proposed regulation until the SEC has completed its work on a fiduciary standard for brokers and advisers to avoid potential inconsistencies. We strongly disagree. The issues and implications of advice given to ERISA plans are very different than retail level advice. For instance, advice given to a plan sponsor directly impacts other individuals, namely participants, and thus it's appropriate for the Department to develop its own standards specifically designed for ERISA plans. It's also important to point out that the proposed regulation would not, as some commentators have suggested, preclude commission-based brokers and advisers from working with sponsors, and thus would not eliminate an important distribution channel for plans. Under the so-called limitation of the proposed regulations, such brokers and advisers would be able to exempt themselves from the regulation provided certain disclosures are made to the recipient of the advice. Admittedly, we believe these disclosures are over-broad and unduly harsh. The vast majority of professional brokers and advisers are dedicated and qualified, and are very much focused on the interest of their clients. No broker or adviser could ultimately be successful in their practice, if their interest were adverse to their clients, and to require disclosure indicating as such, as the proposed regulation does, is just not fair in our view.

In these instances, what we believe is most important to be disclosed to recipients of advice are three things: one, that the broker or adviser is not acting as an ERISA fiduciary, and thus the advice given is not afforded the protections of ERISA; two, that the broker or adviser's advice may not be impartial since he or she is compensated by the provider of the investment options being considered, and the amount of the compensation may be affected by the investment selected; and three, the amount of compensation the broker or adviser is reasonably accepted to receive based on the investments selected, which ties nicely into what the Department has already done in its ERISA section 408(b)(2) regulations. This kind of disclosure will reasonably and effectively give plan fiduciaries the information they need to understand what role their broker or adviser is playing, and what financial relationships exist between the broker or adviser and the plan investment providers. However, it is also critical that this disclosure be clear and conspicuous and not allowed to be buried in a lengthy service agreement. We suggest the Department provide a model notice along these lines. Interestingly, such a disclosure framework would actually be very much in line with what was suggested by the SEC staff in its recent study; namely, a possible fiduciary standard would not preclude commission-based compensation, but would rather require a clear disclosure.

We believe what we are suggesting would address the current confusion of plan sponsors and will level the playing field between those providing advice that are currently ERISA fiduciaries and want to be, and those that are not ERISA fiduciaries and don't want to be. In other words, if a broker or adviser provides to a plan what any layperson would think is advice, the broker or adviser will either: one, be subject to the duties and responsibilities of an ERISA fiduciary; or two, disclose they are not acting as an ERISA fiduciary, and that their advice may not be impartial due to compensation received from the investment providers. That's it. What could be more clear and certain that that?

I'd like to spend a few minutes now talking about IRAs. The proposed regulation as currently written, as you know, would apply to IRAs. Further, the proposed regulation asks for comments on whether the definition of investment advice should extend to recommendations related to taking a plan distribution, namely, IRA investments. We strongly recommend that the regulation should not apply in either case. There is no debate that IRAs are an important retirement savings vehicle. Over 40 percent of American households owned IRAs, and they are the primary tool for retirees to manage their retirement assets. But, IRAs are different than ERISA-covered plans. As the Department itself said to the preamble to the fee disclosure regulations, IRA holders have considerable flexibility in the choice of their IRA provider, or the ability to roll over their balances to an IRA provider of their choice. The Department thus appropriately concluded that the participant fee disclosure regulation should not extend to IRA-based plans. We believe the Department should do the same here with respect to IRAs in general.

IRAs are different than ERISA plans in another critically important respect; in contrast to the thorough enforcement regime applicable to ERISA plans, there is no federal agency that currently has a comprehensive enforcement program for IRAs. The fact is, IRA enforcement appears to be more often occurring at the state level, and is hodge-podge at best. Recent warnings issued by the states of Kansas and Oregon about investing IRAs in fractional shares of viatical (ph) settlements are a good example. The fact that states have felt the need to get involved in IRAs is testament to the current lack of federal enforcement. If the Department decides to extend these regulations to IRAs, this is what will happen. Players in the retirement industry who are more formally regulated with extensive compliance departments, like the firms represented by my colleagues on this Panel, will comply with the rules, and those less formally regulated, who know there is no practical enforcement of the rules, will choose not to comply. While responsible firms will have limitations on their ability to distribute IRAs, less responsible firms will practically have free reign giving them a competitive advantage and uneven playing field. Consumers will be exposed to a significantly great risk as a consequence. Further, if the Department chooses to apply the definition of investment advice to plan distributions, including distributions to IRAs, retirement plan service providers who already have existing relationships with participants will be severely hampered from discussing IRA options with them. These service providers have done an excellent job building programs to work with employees approaching retirement, to encourage them to roll over their retirement savings and prevent leakage from the retirement system. The IRAs they offer have investment options that are generally consistent with those available to the employee in the plan, are high quality, and have reasonable fees. If these service providers are effectively precluded from offering IRAs to employees, that means participants will be potentially left exposed to less responsible vendors making it easier for some vendors to offer retirees IRAs investing in viatical settlements which is certainly not a result anyone would want.

Some people in our industry has described the IRA market as the Wild West. If you apply these regulations to IRAs, you will, metaphorically speaking, be taking the guns away from the good guys leaving only the bad guys with guns. Forgive me, that's not a fair fight. Simply put, any regulatory initiative in the IRA area must be supported by an active, comprehensive enforcement regime to ensure consistent application. In the absence of such enforcement, we strongly encourage you to exclude IRAs from these rules.

Thank you, and I would be happy to take any questions.

MR. DAVIS: Thank you, Mr. Graff. Mr. Stevens?

MR. STEVENS: Thank you, and I thank the Department for holding this hearing, and I congratulate you on your stamina and diligence. I guess you have been at this since about 9 o'clock this morning?

Fiduciary status entails one of the highest obligations known to the law. It also entails some of the heaviest liabilities known to the law. It underpins the entire ERISA compliance structure, and thus we believe that rules governing who is a fiduciary need to provide clarity. They should not impede commonplace financial interactions. They must allow plans and retirement savers to obtain investments that meet their needs, and also to gather a range of market input into their decision-making process.

Now the Department's current rule is 35 years old, and we agree that the Department should review its rule in light of changes in how Americans save for retirement. But, what has not changed in those 35 years is the need to make very clear the line between commonplace financial market interactions and true advisory relationships. The rule adopted in 1975 did not narrow the definition of investment advice, as some now suggest, but rather implemented Congress' intent that ERISA not disrupt established business practices of financial institutions interacting with employee benefit plans. In our judgment, revisions to the rule should embrace the following principles. Persons who deal with plans or IRA investors must know whether or not they are fiduciaries. Fiduciary status should attach only to genuine advisory relationships where a position of trust and confidence exists. Simply selling an investment product or a service cannot be a fiduciary act without more, and the rules should not discourage the assistance that recordkeepers engaged to administer plan accounts provide to help fiduciaries prudently select and monitor plan menu investments. Now, in our judgment, to this end, the Department should revise it's proposal as follows.

First, the rules should create fiduciary duties only when the adviser provides advice or recommendations individualized to the plan or participant. Unfortunately the proposal does not require that the investment recommendation be specific to either. General statements about an investment or a class of investments, indeed all manner of ordinary business interactions, could be swept in. Many firms send out market newsletters, for example, that might suggest where interest rates or the price of gold are headed. When someone calls an IRA provider about a rollover, a call center representative might advise that X fund is designed to meet a particular investment objective, or that Y fund is a target date fund designed for people who expect to retire around a particular date. While providing no investment advice as such, no reasonable person would believe those sorts of interactions create or should create an advisory relationship of trust and confidence.

Second, the rule should not deem an entity to be a fiduciary based on a person's status, such as whether the entity or its affiliate is an investment adviser as defined in the Investment adviser's Act of 1940, if meeting that definition is unrelated to how the entity and the plan sponsor or participant interact. Determining whether someone gives advice under ERISA requires looking at the interaction itself and not whether that person or an affiliate is an adviser under the adviser's Act, the Department and the Courts consistently and properly have viewed ERISA fiduciary status as a functional test based upon what you do. Now, to be sure, advisers do owe a fiduciary duty under the securities laws, but this duty extends only to their clients; that is, to those institutions or individuals with whom the adviser has a mutual agreement to provide investment advisory services for compensation. It does not apply to every person with whom the adviser or its affiliates or any of its employees interacts. If Congress had wanted every firm that meets the adviser's Act definition to be an ERISA fiduciary, it could and would have said so. It did not. Moreover, the Department should clarify that fiduciary status requires a mutual agreement that the person will be providing individual advice that the recipient will consider in making investment decisions. This should be objectively determined; so parties dealing with plans and IRA customers in good faith are not forever in doubt about their obligations and their potential liabilities.

Third, our letter suggests several ways to improve the exceptions in the proposal. The exceptions are essential to making the rule work. We strongly urge the Department to retain the exceptions for participant investment education and information related to platform investments, so as not to discourage the assistance and education the recordkeepers provide to plan fiduciaries making decisions on plan menu investments, and to participants deciding how to allocate their accounts. As our letter points out, these exceptions also should be available for IRAs.

The Department also should retain and clarify the exception for selling an investment product. As proposed, transactions that might entail advice are exempt if it can be demonstrated that the recipient knows or should know the person is providing any advice in its capacity as a seller or an agent of a seller, whose interests are adverse to the interests of the plan or its participants, and that the person is not undertaking to provide impartial investment advice. In this context the Department should make clear first that the exception is available to a broad range of sellers and agents; for example, it should be available when a mutual fund is sold directly by the fund company or its affiliated distributor, and when a fund is sold through a broker dealer. Second, the exception should not require that a seller characterize itself as adverse. The sale of a mutual fund is not a zero sum game where one side benefits only at the expense of the other.

Fourth, the Department should carefully consider how the rules relate to rollovers and IRAs. In our view, it should maintain its position that the recommendation to take an otherwise permissible distribution is not investment advice; otherwise, it will chill the routine process in which a worker leaves a job, contacts a financial services firm for help in rolling over a 401(k) balance, and the firm explains the investments it offers and the potential benefits of a rollover. This is simply not investment advice with respect to the old 401(k) plan even if the result is a liquidation of the prior employer's 401(k) account. And I would add here that, if the Department does say that advising on a rollover is investment advice, it should take the same position with respect to an employer advising a participant not to rollover. There has to be symmetry if the rollover decision is an advisory one and entails a fiduciary obligation. And, from the employer's perspective, that would require considering -- and I think this is an impossibility -- the range of all the possible rollover options that the employee might consider, and also whether its plan offerings are or are not suitable for an individual at that point in his or her career, including someone who may be approaching retirement. I think that illustrates why it shouldn't be looked at as investment advice on either side of the coin, although we can all agree that advising participants about the pros and cons of one strategy or the other is a good idea.

In addition, we think the Department should complete and publish an analysis of the costs of the proposal on IRA investors and providers. While the proposal's language reaches non-employer-based IRAs, the Department's economic analysis, which derives from Form 5500 data, does not consider the cost of the proposal on IRA investors and providers at all. The proposal will generate costs for IRA savers, in that the prohibited transaction rules prohibit commission compensation to fiduciaries in many instances. If financial advisers must move from a commission structure to a wrap fee in the IRA market to comply with those prohibited transaction rules, this may, in many cases, result in higher fees to IRA investors, especially given the long-term nature of any IRA investments. In addition, there are costs to IRA savers if financial advisers must curtail the information and services they offer to avoid crossing into fiduciary status.

Finally, we strongly urge the Department to look at the entire proposal in light of the comments it has received, to draft appropriate revisions, and issue a re-proposal. This would be in keeping with President Obama's recent direction to make sure that interested parties are given a full and fair opportunity to comment on significant regulatory proposals. And, it is in the best interest of Americans saving for retirement that the final rule is clear and workable, and that like it's predecessor, can stand the test of another 35 years.

Thank you all very much.

MR. DAVIS: Thank you, Mr. Stevens. Mr.

Sweeney?

MR. SWEENEY: Thank you, Mr. Davis. My name is John Sweeney. I am an Executive Vice President with Fidelity. I am responsible for planning and advisory services there. Fidelity Investments is the leading provider of investment management, retirement planning, portfolio guidance, brokerage, and many other financial products and services to more than 20 million individuals and institutions, as well as through 5,000 financial intermediary firms. Fidelity is the number one provider of IRAs and workplace savings plans providing recordkeeping and other services to other 8.5 million IRA accountholders, and over 11 million covered participants with close to 17,000 401(k) plans.

During my 13-year career at Fidelity I have held a variety of roles that have centered on the development and management of a wide range of investor products and services. At present I am responsible for the development and management of Fidelity's planning and guidance tools for investors.

Our team sits as a shared resource between the divisions that serve retail investors and divisions providing recordkeeping services to our employer-sponsored retirement plans. The structure of our team is purposely aligned with customer needs rather than the account that they are invested in. Investors don't ask us, how do I save in my 401(k); rather, they ask us, how do I save to meet all of the goals that I have? Many investors that we have are members of the proverbial sandwich generation; one that has many competing needs for a finite amount of savings. An investor is often trying to pay down mortgage debt, save for their own retirement, and might be trying to save for a child's education at the same time they are preparing for an aging parent. Fidelity provides a continuum of products and services so that the investor can choose how they want to interact with us. The simplest end of the spectrum, we offer target date retirement funds, like Fidelity's freedom funds, that provide diversified, age-appropriate investment options in the form of a mutual fund that adjusts out the allocation as the investor ages. Many investors want additional assistance with their investments and we offer a range of planning and educational tools to help investors answer questions like, how much should I save in my 401(k); how do I construct a diversified portfolio to meet my investment needs; how much income will I need in retirement; and what choices are available to me to help construct a reliable stream of retirement income.

For customers who want Fidelity to manage their portfolios, we offer a managed account service. And finally, for customers who have more complex planning needs, we offer a referral to an independent financial adviser. My testimony today will focus on that second category of interaction where Fidelity provides education to investors and prospects free of charge regardless of the type of account that the investor holds.

The current investment environment, as you know, is declining -- you know, market declines through 2008 to the first quarter of 2009, investors without an understanding of asset allocation, time horizons and risk tolerances may have panicked and left the market. Without the benefit of guidance many remain sidelined today unsure of how to re-engage with their portfolios.

Those who understood the role of equities, bonds and cash, and a diversified portfolio, and had the perspective to remain focused on their long-term goals remained invested, and, in most cases, continued to contribute to their 401(k)s even as the market declined.

Beginning in March 2009, as the markets rebounded, those shares purchased when assets were depressed began to appreciate. By the end of 2010, our review corporate-defined contribution plans and 11 million participants revealed that the average account balance for participants continually invested for the last year had rebounded 55 percent to almost $72,000, reaching a 10-year high. More importantly, for participants continually invested for the last decade, this was not a lost decade. In fact, the average 401(k) balance increased from $59,000 at the end of 2000 to $183,000 at the end of 2010, which is a combination of continuous contributions, plus appreciation of the underlying securities.

As you can well imagine, the last couple of years have tested investors' resolve. Investors looked for answers from their financial services providers.

As financial services providers are providing services for many different types of accounts: taxable accounts, brokerage accounts, and the range of investment options available for retirement, we had many inquiries from our customers over the last couple of years and they delivered some very clear messages to us. One, now, more than ever, investors need our help. Since 2008, the number of investors attending seminars at our branches have increased nearly 30 percent; so, in response, last year we hosted 20,000 live investor forums with more than half a million investors attending an event at either an investor center or at their workplace.

In response to customer requests for more insight, we increased the frequency of our investor viewpoints, targeted educational articles on a wide range of investor topics. These have been read four-and-a-half million times.

And finally, in response to customer inquiries about what to do with their portfolios, we have seen a dramatic increase in the usage of our guidance tools, such as portfolio review and retirement income planner, and last year Fidelity provided more than 1.4 million guidance center actions to both customers and prospective customers, free of charge.

To summarize, our data has shown us that what is a clear investor need during good economic times becomes an absolute necessity during times of market volatility.

The second point is that much of our help assists those who need it the most; the low balance and younger participants. We know that for most workers the primary way that that they receive financial education and guidance is through their workplace savings plan. While some may claim that low and moderate income workers are not savers, our data shows that 53 percent of eligible employees who make between $20,000 and $40,000 do participate in their plan, and 71 percent of employees making between $40,000 and $60,000 participate in the workplace savings plans. These numbers increase significantly for those who have auto enrollment features as part of their plan. And, based on an analysis that we did last year of workplace utilization of our My plan Guidance Tools, nearly three out of four plan participants were under the age of 50. It's unclear where this group of investors could turn for immediate, no cost guidance of this type.

The third major finding that we have is that guidance improves investor outcomes. Based on a six-month workplace analysis that we did last year, participants who used our guidance tools increased their deferral savings rates, on average, by about three percent. When it comes to asset allocation, 40 percent of the people who use our on-line investment modeling tool, Portfolio Review, initiated a change to their asset allocation. And, we continue to innovate and respond to investor needs.

Nearly three million baby boomers will turn 65 today -- that's about 7,500 per day -- and they'll begin their transition into retirement, which must account for longer lifespans, stockmarket volatility, a low interest environment, rising health care costs, and a potentially changing tax landscape. We recently did a study, which found that 62 percent of our pre-retirees heading towards retirement feel anxious or stressed about making that transition from saving for retirement to living off those savings in retirement. Despite that concern, 75 percent of those pre-retirees do not have a formal retirement income plan in place that could help alleviate some of that anxiety. Several years ago we launched Retirement Income planner to help customers answer the question, how much will I need to live in retirement? By helping customers understand concepts like inflation, rising health care costs and longevity, we began a dialogue with our customers that helped them understand some of the risks they faced when they entered retirement. But, today's retirement environment is facing -- forcing even more questions for America's workers; interest rates are low, corporations have cut the dividends they pay their investors, pensions are under pressure, and retirees are being asked to shoulder a larger portion of their health care expenses.

Last month we expanded our education and guidance to pre-retirees by unveiling an innovative new program to help investors and workplace participants close to retirement explore vehicles that provide income in retirement. We know that lifetime income is an important priority for the Department and view the tools that we have developed is an important step in helping to educate investors on how to shift their portfolios from the accumulation mode towards portfolios that will provide income streams throughout retirement. The program's highlights include an intensive 30-day coast-to-coast education, an investor education initiative that includes 200 free live educational seminars and events, one-on-one guidance sessions with Fidelity professionals, and the introduction of a Fidelity income strategy evaluator, an on-line tool designed to help participants understand how different investment products can help generate income throughout retirement. This program is already available to more than 10 million workplace plan participants and to non-Fidelity customers as well.

We appreciate the Department's desire to thoughtfully re-examine what constitutes fiduciary investment advice. What we cannot stress enough is that the new rules must encourage, not restrict, the ability of financial services providers to provide educational support. Over 11 million participants invested in Fidelity through a workplace-sponsored 401-K plan. Most of these participants also have IRAs and other savings vehicles, either at Fidelity or at other firms. We know that most Americans will be required to use a combination of their workplace retirement accounts, their IRAs, as well as taxable accounts to supplement social security and any pension that might be available to provide income in their retirement.

At Fidelity our experience has been that investors do not treat these accounts differently when considering questions such as: am I prepared for retirement; am I meeting my savings goals; and how can I transform my savings into retirement income. Similarly, regardless of whether an investor is deciding between 30 investment option in his or her 401(k) or broad universal investment choices when dealing with his or her IRA, the deliberations are the same; investors do not and cannot be expected to believe that the legal framework governing these investment decisions is different based solely on the vehicle they have chosen to make their investment.

Given the importance of proper oversight on behalf of investors and the services they receive, we appreciate that the Department is working with the SEC to ensure that these investor services are protected and not restricted under a new regulatory regime.

Any changes to the current ERISA definition of fiduciary investment advice should not threaten access to the guidance that all the investors receive every day by placing a phone call, going on-line, attending an investor workshop, or visiting a branch for one-on-one assistance. Investors do not understand the underlying regulatory complexity that allows for the valuable services they receive; however, they have a growing awareness that they need to save and invest in their workplace plans, their IRAs, and other accounts, as the saving and retirement tools for most Americans. We ask for your assistance in providing a framework in which we continue to respond to the thousands of American investors who ask us every day, how do I save and invest to meet the many goals I have in life?

Thank you for the opportunity to testify today. I am happy to respond to any questions you have at this time.

MR. DAVIS: Thanks so much, Mr. Sweeney. I'll turn to Virginia for the first question.

MS. SMITH: Mr. Stevens, in the previous panel Mr. Ferrigno talked about his experience with rollover distributions and why people involved with that should be considered fiduciaries, and you indicated that that should not be considered investment advice, and the way you provided the example is really what I want to hone in on. Your example was, when a participant approaches somebody about rollover advice then that shouldn't be considered fiduciary advice. Did you really mean to narrow it just in situations where the participant instituted the discussion, or are you looking as both ways?

MR. STEVENS: Well, first of all, my focus on the rollover issue, as such. Presumably you could then get into a whole range of issues. Well having decided to rollover, I recommend this, that and the other thing. That may very well constitute investment advice.

MS. SMITH: Mmm-hmm (in the affirmative).

MR. STEVENS: That may very well be subject to all sorts of regulatory issues, but it's not investment advice of the sort that we are talking about here, I don't think. The rollover decision --

MS. SMITH: Which is whether to rollover?

MR. STEVENS: -- the rollover decision itself, I could say it's advice about tax planning; I could say it's advice about structuring one's financial assets. I personally have had five 401(k) plans in my career, and frankly I would have been very ill-advised to keep my assets in five different places. So I would look at that as advice not with respect to the investments in the old plan, but advice with respect to how you are going to maintain your investments going forward and the tax advantages or disadvantages there might be of one or the other, and the flexibility in terms of the investment options in one as opposed to the other.

MS. SMITH: Okay. I listened to your description of what you think the regulation should be that started out with the caveat that you think standard business practices should not be disrupted, and I am not sure I followed you, but is there any part of the five-part rule that you would agree is unnecessary?

MR. STEVENS: I appreciate, Ms. Smith, the opportunity to address that. We think it's quite reasonable that the Department would, for a variety of reasons. One, to address this notion that it's not investment advice and let's just provide it on an ongoing or regular basis. We certainly would acknowledge that you can have investment advice, which is a one-off event, which could be quite significant.

MS. SMITH: Okay.

MR. STEVENS: We also think that it's reasonable to say that there shouldn't be a requirement to prove that it was the primary basis for investment decision-making. It could simply be a basis or a factor, or something of that nature, and that would make sense to us as well.

MS. SMITH: Okay.

MR. STEVENS: There are other things the Department can do to as it thinks about this going forward. You have identified for yourselves an issue we don't really have any position on with respect to valuation, for example, which is predicated on experience the Department has. So, we would say there are certainly things that you could do that, from our perspective at least would not be terribly controversial, but it's some of the other aspects of the rule and the lack of clarity that they entail that causes us the concern.

MS. SMITH: Okay. One last question, if I may, of Mr. Graff, if I can find my question? When you were talking about -- putting aside the IRA issues please for me --

MR. GRAFF: Sure.

MS. SMITH: -- I mean --

MR. GRAFF: Oh, come on, Virginia? Okay.

MS. SMITH: But, the other information that you provided, one of the things that you did not address that several people today have addressed is this idea that a regulation is going to cause a lot of increased cost; how does ASPPA view that?

MR. GRAFF: We don't agree with that

assertion at all.

MS. SMITH: You don't? And, why not?

MR. GRAFF: Because the -- what we believe is that if we can fashion a seller's exemption that is somewhat more -- is written in a way that people are more comfortable with, we believe frankly the marketplace will settle out such that those people that want to be ERISA fiduciaries, who currently are right now, will continue to do so. Those costs are already baked into their fees. And, those that don't want to will take advantage the seller's exemption. So that's what's important, is that the marketplace clearly understands what's going on with the person that they are working with. If they are a commission-based adviser, the customer should know that they are dealing with someone who is a commission-based adviser and decide to work with that person and move on. So we don't believe, in the end, if this is fashioned correctly, that it would have any significant marketplace disruption.

MS. SMITH: Thanks.

MR. DAVIS: Mr. Stevens and Mr. Graff, I

think you both in your testimonies talked about the use of the word adverse, and we have heard testimony on that word in previous panels. Do you guys have thoughts that you would share on what you would use in place of the word adverse?

MR. STEVENS: Well, I guess my point is fairly simple. If you think about economic transactions -- I took a cab over here just now -- I got in the cab. I knew I was going to have to pay the taxicab driver and I paid the taxicab driver, and he did a fine job of getting me here to the Labor Department. But, I didn't consider the fact that he was going to be compensated for what he did, to create a conflict of interest, because if it does, then we have conflicts of interest virtually everywhere in our economic society. It proves too much. The compensation is a subject for disclosure, and the Department has worked long and hard on making sure that plans and plan participants and others are well-informed, and we have supported that idea. But, the fact that a service has provided for compensation or an investment product for compensation doesn't necessarily mean that's a conflict of interest. I doubt that my colleague here, Brian, would say that the unregulated advisers that he -- the providers that he represents, who are providing recordkeeping services, necessarily are adverse to the plans that -- by the recordkeeping services just simply because they expect to be paid for them. So I think it's gratuitous. It's not necessary to the rule to put that in. And frankly, in our frame of reference, we don't accept it as a characterization.

MR. GRAFF: Yeah. And, as I said, I certainly think it's unduly harsh. We -- you know, again, what does the customer need to know, the plan sponsor need to know so they can approach this in a transparent way and understand who they are dealing with and what the financial arrangements are. So, as I said before, I think, one, they need to know that the person that they are dealing with is not an ERISA fiduciary, okay; two, that the advice may not be impartial because they are being compensated by the individual, the investment providers, and that the amount of that compensation could be affected by the investments selected; and three, what -- as 408(b)(2) is going to require, what's the amount that's reasonably expected to be received as compensation from those investment providers? We think -- you know we can dither over the word impartial, if that's the right word. I think there is a word somewhere along the lines -- I think their principles frankly are more important than words, and we believe if that, the essence of those points of information are conveyed, then the plan sponsor, with open eyes, will be making a choice. And, we absolutely believe, particularly in the small business market, that many small business sponsors will continue to work with an adviser, who is commission-based, and there is nothing wrong with that, and I think it's important that everyone recognize that. We just want to make sure that, in our world, there is this -- sometimes it's referred to as the blind squirrel -- you may have heard that expression -- and our basic concern, from a policy standpoint, is we want to make sure that, to the extent there is behavior out there that is concerning, that this information is clearly disclosed.

MR. STEVENS: May I supplement my comment, because the disclosure issue seems to be taking such a front and center attention here? I worry about disclosure for two reasons as a way of approaching this issue.

One, it celebrates form over function. You can essentially get a boilerplate disclaimer, and I don't know what lengths you'll have to go to get it, but a boilerplate disclaimer that then basically says, well, I can now invite all the trust and confidence I want because you have said that I am not your fiduciary, and I think that invites lots of mischief potentially.

The second thing about a disclosure regime is that it will burden the system with paperwork, because you will have to get it into each interaction. There is not a once and forever way of doing that, and you will even only -- as a provider of a service, you think about an interaction about a mutual fund call center, perhaps discover long into the conversation that the context that the individual is calling you about is one where you need to give a disclosure. And then some have suggested that it be written. And so you'll have to stop the world and say, you'll have to send this form back to me before I can talk to you about anything here just to acknowledge that I am not your fiduciary. The Department ought to be looking at the course of dealing between the parties and ask itself whether it is reasonable for the individual to expect that the person on the other side of the table has undertaken to provide impartial investment advice to them. And, irrespective of whatever paperwork -- if that's the case, then that's fine -- I also don't believe that you can simply ask people, do you think this person is a fiduciary, and that solves it. The fiduciary concept is a legal concept. Most people don't understand it, but I think, looking at the course of dealing, the Department ought to be able to tell when the line has been crossed or not.

MR. GRAFF: You know just to add to what Paul is saying, I think there is a concern, and this goes to the issue of whether or not there should be a postponement of these -- of considering these rules, waiting for the SEC to act. There are plenty of folks in our industry, who are regulated by the SEC by FINRA, but there are also plenty of folks who are not, and you need to be mindful of that. They may be subject to some state regulation; they may be subject to no regulation, and they are out there. And, it's important that you guys address this because of that gap. So there are going to be situations where there will be customers, in our view, that will not appreciate who they are dealing with, and so it's important that they understand that.

MR. DAVIS: Thank you.

MR. LEBOWITZ: I -- not to be argumentative, but I was intrigued by your cab driver story. It seems to me that the only reason that your interests were not adverse was because your ride was very tightly regulated; the cab driver was not free to set his own compensation, unless he went by Bethesda or something from wherever you were coming from. But for that regulation, if you got into the cab and there were no meters, no regulations at all, the cabbie says let's negotiate. In that circumstance your interests, it seems to me, were quite adverse to the driver's. So I think it proves the value of regulation.

MR. STEVENS: Can I respond? They were adverse, Alan, only because the cab driver had an interest in being paid more and I have an interest in paying less.

MR. GRAFF: Right.

MR. STEVENS: And that operates without a framework, you are right, but that's true within markets too.

MR. LEBOWITZ: Right.

MR. STEVENS: But it's always in the provision of any kind of service or sale of any product that those two interests are, or it seems to me, at odds with one another.

MR. LEBOWITZ: Yeah. And I think that's really all we are getting at in the use of the word. But, I just wanted to -- just one question for Brian. You described the IRA market as the Wild West, but you are opposed to our proposed approach to it, leaving it the way it is, I guess, --

MR. GRAFF: Mmm-hmm (in the affirmative). Yeah, that's right.

MR. LEBOWITZ: -- which you think is better than it would be?

MR. GRAFF: Correct.

MR. LEBOWITZ: So can you talk about that a little bit more?

MR. GRAFF: Explain why?

MR. LEBOWITZ: Yeah.

MR. GRAFF: Well, very much so, and we thought long and hard about this. I personally spent some time in dealing with some state issues. I personally spent some time in the state of Nevada, quite a bit of time, dealing with a situation with some vendors that were selling fractional shares of viatical settlements, interest in limited partnerships, and literally the enforcement regimen that was practically being employed to these providers was minimal, and that's probably overstating it. And so, your concern, as policy makers, your concern and our shared concern isn't about the fact that, on a marginal basis it might be that the retirement plan service provider is going to get five basis points more on an IRA investment versus the in-plan investment. The bigger concern frankly is elderly people losing their entire IRA and their entire retirement assets because they had been investing in limited partnerships interests and viatical -- stuff that they shouldn't be anywhere near. And, if the more regulated providers, the larger providers who have compliance departments, are hampered in any way, then they are going to be disadvantaged in that marketplace. And right now, given what's going on, our concern about where the money has been going in the first place is paramount relative to the issue of fees. And we think, frankly, the IRA market is generally very competitive. As you pointed out in your preamble, there are -- you know the IRA is under the control of the retiree; they can decide to move the money where they want to be and they have control over it, and given all those factors, until there is some basis where you can apply enforcement in a consistent way and meaningful way, we think you will do more harm than good in the short run.

MR. LEBOWITZ: Do you have a vision of a --

MR. GRAFF: Well, I mean, you know there has been some -- there has been -- it's interesting -- there are people in our industry who are scared to death about what I am about to say, but I'm going to say it anyway, because I think you guys know that I never am shy about these things -- I do think that, as more and more baby boomers are retiring, as my colleague to my left said, and they are choosing to move their money typically to an IRA, there is a larger universe of consumers who are prey to vendors who are selling products that, for most retirees, they shouldn't be anywhere near. And I think we are going to start hearing more and more of these stories. I do think we need some type of regime -- it may have to be disclosure only because, practically speaking, the idea of an army of -- of any agency having an army of employees, to imagine that right now in this fiscal situation is rather unlikely, but nonetheless, if there was some uniform disclosure rules, at least it would be somewhat easier to identify whether the enforcement is happening. And, where would that be placed? That's -- you know, that's an inter-agency issue and, as a general manner, I have learned that that's generally not something I should get myself in the middle of.

MR. LEBOWITZ: Mr. Sweeney, do you have any observations about that?

MR. SWEENEY: I think that in terms of IRAs, what you -- what I mentioned before is that people think of them as one of the stools of retirement income -- well, retirement savings first of all, and then ultimately retirement income; so we think that they are used in combination. Legislatures have given investors the option to save in a workplace sponsored retirement account plus an IRA, and most customers that we see have to use both of those to solve their retirement income. And we think it's important that people know about their options and be able to choose from them.

To Mr. Stevens' point earlier around the choices, we think it's important to make sure that people understand their options, so whether they -- when they are leaving their jobs -- you said you had five 401(k)s at some point -- the average American will work for seven employers over their career, and so managing investments across seven different 401(k)s is very difficult. We talk about concepts not only around asset allocation, but asset location. You want to think about what accounts you hold different asset classes in. You want your high turnover or high tax accounts in the accounts that are tax deferred, and you want more efficient vehicles in the accounts that are taxable. So when you start thinking about a client's portfolio, you want to educate them on concepts when they are thinking about their portfolio in totality, because it's important that they see all of the options available to them when they are trying to accumulate savings and then ultimate generate income in retirement.

MR. HAUSER: For Mr. Stevens, I was intrigued by your suggestion that the focus ought to be on, you know, whether the person had a reasonable expectation that they were in a position of trust and confidence, vis-the adviser, as opposed to getting too into the weeds on various disclosure sorts of documents. But, with respect to the seller exception, I just wonder exactly how you go about accomplishing that purpose, because it seems to me one of the problems is that there is a lot of confusion, and especially in unsophisticated investors' minds, as to whether they are being sold a product or whether they are really being sold advisory services? And, even broker dealers, they may -- you know they are brokers when they are submitting comment letters to us, but they are financial advisers and financial planners, you know, when they are dealing with participants. And, the commercials, you know, suggest that they are there. They are in your corner. They are -- you know, they are going to be there for your retirement. And so I think for a lot of people there probably really is kind of an expectation that we are getting good faith, professional advice that's in no way steered by any conflicts we may have. And, I guess, what, short of disclosure, is where you draw the line and have a seller's exception that's going to get at that problem?

MR. STEVENS: Well, first of all, I would say that I am very sympathetic. I understand the challenge of drawing the line, but my point most basically is that there has to be a context in which it is in fact a sale and it's not been that relationship of trust and confidence that's been assumed. I think if you were to adopt a rule with that as the standard and make it clear that the Department will look at all the facts and circumstances for that purpose, that will encourage people, not necessarily in some sort of wooden, regulatory, mandated disclosure regime, but just as a matter of a course of dealing with participants or with plan sponsors to try to make sure that they are on the right side of that line when they want to be looked at as sellers. And, there are people, there are industries, certainly in our context included, where that would be the case. If you have a directly marketed fund firm, you know, they don't undertake -- and this is in the normal marketplace -- they do not undertake to have an advisory relationship with a customer. They offer a menu, they inform you about the menu, and you select from the menu, and it's s sale. So my point is that the rule needs to make room for both and draw the line as best you can. I wouldn't do it simply on the basis of some disclaimer document, but more in the context and all the circumstances, and thereby incentivize people to make sure that dealing honestly and conscientiously with people they don't leave a lot of room for doubt about which part of that -- which side of that line they are on.

MR. HAUSER: Thank you.

MR. DAVIS: I think that's it. Thanks so much.

MR. STEVENS: Thank you.

MR. DAVIS: We are adjourned for the day. Our panel number eight starts tomorrow at 9:15 in this room. Thank you.

(Whereupon, the meeting is adjourned).

CERTIFICATE OF NOTARY PUBLIC

I, NATALIA KORNILOVA, the officer before whom the foregoing meeting was taken, do hereby certify that the witness whose testimony appears in the foregoing pages was recorded by me and thereafter reduced to typewriting under my direction; that said hearing is a true record of the proceedings; that I am neither counsel for, related to, nor employed by any of the parties to the action in which this hearing was taken; and, further, that I am not a relative or employee of any counsel or attorney employed by the parties hereto, nor financially or otherwise interested in the outcome of this action.

____
Natalia Kornilova
Notary Public in and for the
District of Columbia

My commission expires: April 14, 2012

V

Y