July 20, 2015

By U.S. Mail and Email: e-OED@dol.gov

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

Re: ZRIN: 1210-ZA25; PTE Application D-11712

Ladies and Gentlemen:

The Securities Industry and Financial Markets Association ("SIFMA")[1] is pleased to provide comments regarding the Department of Labor's ("Department") Proposed Best Interest Contract Exemption[2] ("BIC Exemption") under the Employee Retirement Income Security Act of 1974, as amended ("ERISA"). We appreciate the opportunity to comment and hope that our comments are helpful to the Department as it assesses whether the exemption, as written, can be accommodated into the broker-dealer model that exists today, or whether, as written, it will result in the loss of professional investment advice for small retirement accounts.[3] We respectfully request an opportunity to testify at the hearing on the proposed exemption.

[1] SIFMA is the voice of the U.S. securities industry, representing the broker-dealers, banks and asset managers whose 889,000 employees provide access to the capital markets, raising over $2.4 trillion for businesses and municipalities in the U.S., serving clients with over $16 trillion in assets and managing more than $62 trillion in assets for individual and institutional clients including mutual funds and retirement plans. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit http://www.sifma.org.

[2] Proposed Best Interest Contract Exemption, 80 Fed. Reg. 21960 (April 20, 2015).

[3] 80 Fed. Reg. at 21961.

Attached hereto are SIFMA's submissions for the related rulemakings being undertaken by the Department. These attachments are an integral part of this submission.[4]

Although the preamble states that the proposed BIC Exemption "seeks to preserve beneficial business models by taking a standards-based approach that will broadly permit firms to continue to rely on common fee practices," the exemption as currently proposed raises significant and in many respects insurmountable obstacles for broker-dealers, including the ability to offer commission-based advice. For example, the contract requirements of the proposed exemption do not comport with the manner in which financial professionals enter into relationships with retail customers. SIFMA further believes that the written disclosures required under the proposed exemption will not only overwhelm customers with more information than they can possibly digest, but also seriously impede customer transactions and cause timing and opportunity losses for smaller retirement accounts.

Moreover, complying with the terms and conditions of the proposed exemption will impose significant additional costs on broker-dealers and other providers of financial services. That will make it extremely difficult, if not impossible, for smaller retirement accounts to receive financial advice from the professionals who currently serve them. As a result, many of these smaller retirement accounts may be terminated or maintained such that the investor receives no assistance and the broker is no more than an order taker. To the extent that the investment education currently provided by financial professionals ceases to be available, the result will be accelerated leakage of retirement savings out of tax-advantaged accounts, less people saving for retirement and widespread confusion on the part of retirement investors, none of which is in the best interest of these investors.

[4] See Appendices numbered 1-8.

SIFMA shares the Department's interest in ensuring that investors receive appropriate, informed assistance with decisions concerning retirement. However, SIFMA respectfully believes that this proposed exemption, and the package of proposals accompanying it, are not the proper way of proceeding. SIFMA also does not believe that the Department may use a new definition of "fiduciary," in combination with its exemptive authority, as a means of establishing a new regulatory and enforcement program for financial professionals, ERISA plans, and non-ERISA plans such as IRAs. SIFMA expresses this objection with regard to the BIC Exemption, and the other, related exemptive rules that have been proposed.

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Section I: Scope of the Proposed Best Interest Contract Exemption

SIFMA respectfully believes that the Department's new "fiduciary" definition, and this proposed exemption, exceed the Department's statutory authority. SIFMA offers the comments and recommended changes in this letter to assist the Department in improving this exemptive rule in the event the Department resolves to adopt this package of proposals in final form, despite the deep concerns they present. Nothing in these comments should be understood to mean that SIFMA concurs with the construction of ERISA and the Code underlying the Department's proposals, or with the policy views regarding the financial services industry that the Department has articulated in presenting its proposals.

Advice Recipients Covered by the BIC Exemption.

The proposed BIC Exemption permits an adviser to receive compensation for services provided to a "Retirement Investor" in connection with a purchase, sale or holding of an "Asset" by a plan, a plan participant or an IRA. "Retirement Investor" is defined to include a plan participant or beneficiary with the ability to self-direct his or her account or take a distribution, an IRA owner, or a plan sponsor of a plan with fewer than 100 participants that is not participant-directed. We urge the Department to include advice to sponsors of participant directed plans with fewer than 100 participants on the composition of the menu of investment options available under such plans. Without such relief, sponsors of such plans would have to enter into a fixed fee arrangement with an adviser to obtain advice regarding menu selection, which many small employers would be unwilling to do. We also note that the Department has omitted Keogh plans from the list of retirement investors, which we assume was inadvertent.

As a result of the Department's decision to limit the availability of the BIC exemption to the "retail" retirement marketplace, no financial professional can receive any third party fees on behalf of any plan with more than 100 participants. We urge the Department to permit receipt of mutual fund third party payments in connection with plans with more than 100 participants under PTE 86-128 (amended consistent with SIFMA's comment letter addressing the Department's proposed amendments to PTE 86-128), with full disclosure in the manner that has worked successfully under that exemption for the last 30 years.

We also believe that the 100 participant ceiling in the BIC exemption will be operationally unworkable from a compliance perspective. For example, how often would the financial professional need to confirm that the number of participants in the plan is at or below 100? It would not be possible to confirm the number of participants prior to every transaction or every recommendation. If the 100 participant cap is intended to protect less sophisticated plan sponsors, we suggest as an alternative that the Department use an asset based test in Section (b)(1)(i)(B) of the proposed regulation[5] that aggregates the assets of all plans sponsored by the employer and its affiliates. Many large employers sponsor multiple plans, some of which may be quite small. In such cases, the plan sponsor is not likely unsophisticated or in need of the protection of the BIC Exemption. Such employers can take advantage of other exemptions for any small plans that they sponsor and should not be forced into the BIC Exemption. If the Department determines to keep the 100 participant test, we urge the Department to amend the proposed exemption to provide that the test must be met as of the latest Form 5500 filed by the plan sponsor and publicly available from the Department at the time the account is opened.

Transactions Covered by the BIC Exemption.

The exemption covers only the receipt of compensation in connection with the *purchase, holding or sale* of a specified list of "Assets." We believe it also needs to cover the receipt of

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[5] *See Definition of the Term "Fiduciary": Conflict of Interest Rule—Retirement Investment Advice*, 80 Fed. Reg. 21928, 21957 (Apr. 20, 2015).

compensation in connection with extensions of credit, since by its terms, the exemption covers debt instruments, bank deposits and certificates of deposit.[6]

We are troubled by the narrow scope of the permitted "Assets" and urge the Department to reconsider its approach to this concept. The term "Asset" is defined to include ***only***: bank deposits; certificates of deposit; shares or interests in registered investment companies, bank collective funds, insurance company separate accounts, exchange-traded REITs, or exchange-traded funds; corporate bonds offered pursuant to a registration statement under the Securities Act of 1933; agency debt securities as defined in FINRA Rule 6710(l) or its successor; US Treasury securities as defined in FINRA Rule 6710(p) or its successor; insurance and annuity contracts; guaranteed investment contracts; and equity securities within the meaning of 17 C.F.R. § 230.405 that are exchange-traded securities within the meaning of 17 C.F.R. § 242.600.[7] The term "Asset" is expressly defined to exclude "any equity security that is a security future or a put, call, straddle, or other option or privilege of buying an equity security from or selling an equity security to another without being bound to do so."

The investments excluded from the Department's proposed list of permissible "Assets" include such transparent and liquid securities as municipal bonds, federal agency and government sponsored enterprise guaranteed mortgage-backed securities, foreign bonds, foreign equities, and foreign currency. It also omits other common investments such as over the counter equities, structured products (other than U.S. corporate bonds), hedge funds, private equity and other

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[6] The BIC Exemption also provides no relief for principal transactions, which effectively denies relief under the exemption for the acquisition of shares of unit investments trusts. Although unit investment trusts are organized as registered investment companies, they are typically sold out of inventory. In a separate comment letter, SIFMA is recommending that the proposed exemption for principal transactions in debt securities be expanded in such a way that it would provide relief for the acquisition of unit investment trust shares.

[7] These "exchange" definitions make clear that only equities traded on a US exchange are covered under the exemption.

alternative investments, options, and futures contracts. In enacting ERISA, Congress chose not to prohibit these types of investments, and the Department has historically declined to create a "legal list" of investments for plan fiduciaries.[8]

The creation of an enumerated list of permissible asset types for small plans and IRAs is a marked departure from the Department's practice over the last 40 years. For the first time, the Department is proposing to create a "legal list" that substitutes its judgment for that of the plan fiduciary, IRA owner or plan participant. We question whether the Department has the legal authority to specify what retirement accounts can invest in. Had Congress wanted to place investment restrictions, it could have done so, as it did in IRC § 408(m) for IRA accounts. Because there are no such prohibitions in ERISA, we do not believe that the Department has the requisite authority to impose them now. We also question the Department's ability to expand the list of prohibited investments for IRAs given the language in IRC § 408(m) which does not include any of the securities prohibited under this proposed exemption.

We also believe that the "legal list" is fundamentally inconsistent with a fiduciary standard. An adviser may in good faith believe that an investment not on the list of "Assets" is in the best interest of the plan, plan participant or IRA owner. If an adviser so believes and fails to act on his or her belief, will adherence to the list be a defense? Limiting the ability of advisers to take action that they truly believe would be in the best interest of IRA owners, plans and their participants would substitute the Department's judgment for that of advisers, IRA owners, plans and their participants, and seems counter to the Department's stated goals.

[8] *See* Investment of Plan Assets under the "Prudence" Rule, 44 Fed. Reg. 31369 (June 1, 1979) ("the Department does not consider it appropriate to include in the regulation any list of investments, classes of investment, or investment techniques that might be permissible under the prudence rule"). We note that exchange traded funds did not exist in 1979 and thus could not have made any such list at the time.

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Furthermore, limiting the types of permissible assets would create major operational challenges. As outlined in the Deloitte report submitted with this comment letter, SIFMA member firms would have to bifurcate accounts to accommodate products that would not be permissible under the exemption. Significant oversight would be required to ensure that advised retirement accounts are holding only permissible assets and that retirement investors are being advised only with respect to such assets. For pre-existing retirement accounts, SIFMA member firms will be barred from providing much needed advice to the account owners concerning the holding or sale of any assets that are not on the Department's proposed list. These negative consequences are discussed in greater detail below in SIFMA's comments regarding Section VII of the proposed exemption.

Although the Department suggests plans and IRAs can obtain exposure to impermissible assets through mutual funds, mutual funds does not have the risk, reward or fee structure of those assets (*e.g.*, sovereign bonds or foreign securities). It is not reasonable to suggest that a mutual fund is a substitute for an asset that the Department has excluded. We urge the Department to replace the term "Asset" in Section I(a) with the phrase "securities or other property." Given the impartial conduct standard required by the BIC Exemption, there should be no limit on the types of assets covered by the exemption. As proposed, the BIC Exemption purports to require brokers to act in the client's best interest, but then trumps the broker's judgment on what is or is not a suitable investment. Moreover, as the investment world constantly evolves, the sort of static list proposed in the BIC Exemption could impede investments in new vehicles that have the same level of transparency and liquidity cited by the Department as primary criteria in selecting "Assets." We believe that any such limitation is inappropriate.

The BIC Exemption also makes no provision for the receipt of compensation for two specific activities that the Department has included in the proposed definition of fiduciary investment advice: rollover advice and manager advice. Under the proposal, one becomes a fiduciary by recommending that a plan participant roll his or her account balance over to an IRA or by recommending a manager, but BIC Exemption provides no relief for the receipt of fees in connection with the rollover or the manager selection process.

In addition to substituting the phrase "securities or other property" for the term "Asset," SIFMA urges the Department to provide explicit relief for compensation received in connection with a recommendation to take a distribution of benefits or rollover into a plan or an IRA, as well as in connection with a recommendation concerning the selection of investment managers or advisers. We believe that these omissions must have been inadvertent, since it does not seem reasonable to make a person a fiduciary for a particular type of advice but provide no exemption for any compensation that may flow from that recommendation.

Because the proposed BIC Exemption is tailored to the recommendation of an "Asset," it is unworkable for recommendations of investment managers or advisers, including recommendations of separate managed account strategies or wrap fee programs (collectively, "advice programs"). These advice programs are for discretionary management services that, when provided for retirement accounts, are already subject to the full protections of ERISA today. A separate, modified BIC Exemption must be adopted that is more tailored and relevant to the recommendations of these advice programs. To address potential conflicts, such an exemption could incorporate the same impartial conduct standards and other requirements as contained in the BIC Exemption (subject to the necessary clarifications and modifications discussed below in this letter). To avoid encumbering unnecessarily the pre-investment conversation, and to leverage existing requirements and practices under the Advisers Act for discretionary management services, the exemption should allow the contractual requirements to be incorporated into an advice program agreement. It should be possible for that agreement to be executed after the adviser recommends the advice program, but prior to any actual investment through the advice program. For example, a required clause could state that an advice program recommendation was made in the best interest of the client. In lieu of the BIC Exemption disclosures, which are asset-based and therefore inapposite to the recommendation of advice programs, the Department should require 29 C.F.R. § 2550.408b-2 disclosures that could be incorporated into the advisory program's ADV Part 2 disclosure brochure that is already delivered to clients under the Advisers Act. The concept of leveraging § 2550.408b-2 disclosures is discussed in more detail below.

Section II: Contracts, Impartial Conduct and Other Requirements

Contract Requirement

The BIC Exemption requires that a contract be entered into *before* any recommendation is made to a retirement investor. There are several reasons why this requirement is simply incompatible with the markets and relationships it is intended to regulate. As a threshold matter, it is completely at odds with the manner in which brokers typically enter into relationships with retail customers. Given the uncertain scope of the term "recommendation" and the risk of non-compliance with the exemption, this proposed condition may leave brokers no choice but to ask retirement investors to enter into written contracts before any meaningful conversations have taken place. That could make retirement investors so uncomfortable that they simply decide not to proceed any further. Requiring a contract *before* any recommendation is made would also preclude reliance on the BIC Exemption for certain types of advice (such as rollover recommendations), because participants are not likely enter into a contract until they have considered the advice and made a decision.

There are other operational incompatibilities as well. The practical reality of the marketplace is that contracts are generally entered into between the financial institution and the IRA owner, plan fiduciary or participant acting on behalf of the IRA, plan or participant account. Advisers do not sign these contracts, and it would not be feasible for them to do so. Advisers are merely agents of the financial institution and they may leave that institution at any time. Having advisers sign the agreements would require the execution of a new contract whenever an adviser leaves the firm or an account is reassigned to another adviser. Likewise, if the adviser is not available, a recommendation could not be made by anyone else since the contract would be non-transferrable between advisers. Similarly, where an IRA or small plan account is serviced by a team of advisers, all of the advisers would have to sign the agreement, and a new contract would be required whenever an adviser leaves the team, or a new adviser joins the team.

Requiring advisers to sign a written contract would also create problems for financial institutions that have call centers and a rotating team of employees who may be permitted to provide advice. The Department declined to provide a "carve out" for call centers in the proposed definition of fiduciary advice. Can IRAs be allowed to use the call center if *no one* in the call center has signed the contract? If call center staff are fiduciaries, does each staff person in the call center have to sign the contract if an IRA owner could get a different person every time the IRA owner calls? These are just two examples of why this requirement is impractical.

Furthermore, there are close to fifty million IRAs and plans with *current* brokerage contracts. To amend, reprice, and resign all of those current contracts in the eight month period between the effective date and the applicability date would be an impossible undertaking. The Department has noted the impracticality of obtaining signatures on revised contracts in more than twenty prohibited transaction exemptions permitting deemed consent or negative consent. We respectfully request that any contract requirement be replaced by a written undertaking on the part of the financial institution; if the plan fiduciary, participant or IRA owner continues the relationship after being provided with the written undertaking, he or she will be deemed to have consented to it. At a minimum, the BIC Exemption should be revised to make clear that either negative consent or an electronic signature is sufficient, and that the written undertaking can be delivered either by mail or by electronic means.

Finally, we note that the proposed exemption for principal transactions targets the plan or IRA account as the counterparty to the agreement by requiring that the retirement investor enter into the contract "acting on behalf of the Plan, participant or beneficiary account, or IRA." This language makes clear that any advice provided by the adviser is being provided only with respect to the retirement account covered by the agreement. Although we have commented separately that the contract requirement of the proposed principal transaction exemption should likewise be replaced by an undertaking, we think treating the retirement account as the counterparty is more workable than the approach taken in the proposed BIC Exemption, which views the retirement investor as the counterparty.

Voluntary Assumption of Fiduciary Status

The BIC Exemption requires the adviser and the financial institution to affirmatively state that they are "fiduciaries under ERISA or the Code, or both, with respect to any investment recommendations to the Retirement Investor." The "Retirement Investor," as that term is defined in the exemption, will be a person or entity who may have more than one account with the adviser or the financial institution or both. At the very least, this language should be revised to clarify that the affirmative statement applies only with respect to recommendations provided with respect to the specific retirement account covered by the undertaking.

The required acknowledgement of fiduciary status creates other complications as well. For example, the preamble states that the requirement to adhere to a best interest standard "does not mandate an ongoing or long-term advisory relationship."[9] Section (c) of the proposed regulation[10] appears to limit the scope of any fiduciary duty to those assets for which a person exercises discretionary authority or renders investment advice. However, the Department should

[9] 80 Fed. Reg. at 21969.

[10] *See Definition of the Term "Fiduciary": Conflict of Interest Rule—Retirement Investment Advice*, 80 Fed. Reg. at 21959.

make clear in the BIC Exemption that advisers and financial institutions can limit any acknowledgment of fiduciary status and the requirements of the exemption to the *specific* assets for which investment advice has in fact been rendered, and if the investment advice is non-discretionary, that they can also limit the scope of any fiduciary obligation so that it does not extend to ongoing monitoring of that asset position. To do otherwise would require a financial institution to provide an additional investment advisory service (account monitoring) that neither the financial institution nor the plan, participant, or IRA owner may want or be willing to pay for. The Department should not imply that the adviser and/or financial institution will be acting in a fiduciary capacity *any* time they discuss investments for an account that holds an asset that was subject to non-discretionary investment advice. To do so would in fact preclude the adviser and financial institution from relying on the carve-outs to fiduciary status, including the ability to provide investment education, for any trade executed in the account.

In conjunction with the BIC Exemption's narrow definition of "Asset," the acknowledgement of fiduciary status must not result in self-directed IRA owners and plan participants being denied the ability to invest in assets of their choice. If a client with an advised IRA instructs the custodian to acquire a non-recommended investment that is excluded from the list of permissible "Assets," the broker should be able to execute the trade for a commission because the broker did not provide investment advice on that asset. The Department should make this clear. Otherwise, broker-dealers may be unwilling to risk dual-role accounts, where recommendations are made as to some but not all investments. This is a very common model for some broker-dealers whose advisers may provide occasional advice but not all the time and not with respect to all assets in the account, and it is consistent with Section (c) of the proposed regulation. If broker-dealers are instead forced to restrict advisory accounts to the acquisition, holding or sales of "Assets" as defined in the BIC Exemption, the result will be to deny clients the ability to invest their accounts in the assets of their choice. This does not seem to be the Department's intent, and in the final adoption the Department should make this clear.

Even if the above situation is addressed, dividing IRAs into advised and non-advised IRAs will create its own set of problems, not unlike the situation where a client has both a personal brokerage account and a plan or an IRA account. Assume that the broker recommends an investment for the client's personal account that would not be on the BIC Exemption's list of permitted "Assets," and that the client then instructs the broker to purchase the same investment for the IRA. The broker has not made a recommendation for the IRA and should be permitted to execute the transaction in the non-advised IRA as a non-fiduciary broker. However, the broker may risk being sued for a prohibited transaction by following the client's instruction with respect to the IRA. If the broker does not follow the client's instruction, the broker risks losing the client's business.

These types of risks are likely to drive many broker-dealers away from commission-based compensation arrangements entirely, contrary to the Department's stated goal of "flexibly accommodate[ing] a wide variety of business practices" through use of the BIC Exemption. [11] The broad undertaking of fiduciary responsibility, the prevalence of individuals having multiple accounts with the same financial institution and broker, and the severely constrained list of permitted "Assets" make the BIC Exemption an ineffective solution for the modern investment marketplace.

Impartial Conduct Standards

The BIC Exemption requires that the adviser and the financial institution affirmatively agree to comply with, and then in fact comply with, impartial conduct standards. The impartial conduct standards require the adviser to provide advice that is "in the Best Interest of the Retirement Investor (*i.e.*, advice that reflects the care, skill, prudence and diligence under the circumstances

[11] 80 Fed. Reg. at 21961.

then prevailing that a prudent person would exercise based on the investment objectives, risk tolerance, financial circumstances, and needs of the Retirement Investor, without regard to the interests of the Adviser, Financial Institution or any Affiliate, Related Entity, or other party)." The Department has thus taken ERISA's prudence standard and turned it into a prohibited transaction applicable to both plans and IRAs.

Congress saw no reason to impose a prudence standard for IRAs and believed that a violation of the prudence standard for ERISA plans should be remedied through litigation in federal court. Nonetheless, the proposal purports to condition relief under Section 4975 of the Code on the *contractual* assumption of a prudence standard that would be enforceable by IRA owners in state court through class action litigation or in arbitration on an individual claim basis. We do not believe that Congress intended a breach of the duty of prudence to violate the prohibited transaction provisions of ERISA and the Code.

We also do not believe the Department has a basis to apply its best interest standard to ERISA plans. The Department acknowledges in the preamble that the best interest standard "is based on longstanding concepts derived from ERISA and the law of trusts"; in particular, the duties of prudence and loyalty imposed by ERISA § 404(a). Requiring advisers to ERISA plans or plan participants to agree to, and comply with, a best interest standard separate and apart from their existing ERISA fiduciary duty is redundant and unnecessary to achieve the Department's stated goals. For ERISA plans, requiring advisers and financial institutions to adhere to a best interest standard as a condition for relief under the BIC Exemption ramps up the consequences of any fiduciary breach by imposing an excise tax on a prudence violation. We believe that is both inappropriate and contrary to the statutory framework and Congress's intent.

In our view, the Department lacks statutory authority to require compliance with a prudence rule as a condition of a prohibited transaction exemption. Congress has issued more than 20 statutory exemptions. Not one of those exemptions has imposed a vague "reasonable person" standard or a subjective "misleading disclosure" standard as a condition punishable by transaction reversal and an excise tax, regardless of whether there is a loss on the trade and regardless of whether the disclosure is entirely correct but simply unclear. Nor has any exemption previously issued by the Department contained such vague and subjective conditions. These conditions simply are not administrable and therefore do not meet the standards for issuance of an exemption under ERISA § 408(a). If the Department insists on retaining compliance with a non-misleading disclosure condition in the exemption, we suggest instead that the Department explicitly adopt FINRA guidance relating to Rule 2210 regarding the term "misleading."[12] In addition, we ask that the provision be clarified to require only that the financial institution and any adviser acting for the financial institution reasonably believe that the statements are not misleading. Because the failure to comply with a prohibited transaction exemption has such dire consequences, we do not believe that an inadvertent, immaterial statement taken in the wrong way by a client should result in reversal of the transaction, a guarantee of losses and the imposition of an excise tax.

We also question the language purporting to require advisers and financial institutions to prove that advice was given "without regard to the financial *or other interests of* the … Related Entity or *any other party*." We have several concerns with respect to this formulation. First, we believe the requirement that advice be "without regard" for the financial interests of the adviser sets up a standard that an adviser will fail any time a plaintiff can prove that the adviser did not recommend the investment that paid him the least. In guidance regarding the suitability rule, FINRA uses a much more common sense approach that does not contain this flaw: that the adviser provide recommendations that are in the best interest of his client and put his client's interest before his own.[13] We urge the Department to use this formulation.

[12] *See, e.g.*, FINRA Frequently Asked Questions regarding Rule 2210, *currently available at* www.finra.org/industry/finra-rule-2210-questions-and-answers.

[13] *See, e.g,* FINRA Regulatory Notice 12-25, Q1 at p.3 (May 2012) (citing FINRA rules that adhere to this formulation).

In addition, the proposed exemption in the language quoted above refers to "other interests" of "any other party," with no apparent limitation. We do not know what these "other interests" and "other parties" are intended to address; nor does the preamble explain them. We request that this language be deleted from the definition of "best interests" in the exemption.

The impartial conduct standards also prohibit the adviser, financial institution and their affiliates and related parties from receiving unreasonable compensation "in relation to the total services they provide to the Retirement Investor." This new formulation of reasonable compensation is unexplained. Nor does the Department attempt to justify the differences between this formulation and Congress's view of reasonable compensation, which does not require all compensation received by a financial institution to be justified by a particular set of services to a particular account. We believe that this language is troublesome and we urge the Department to use the language it has used since the enactment of ERISA and as recently as 2012, when it entirely revised its regulations under ERISA § 408(b)(2).[14]

The impartial conduct standards also prohibit misleading statements about the recommended asset, fees, material conflicts of interest and other matters pertinent to the retirement investor's investment decisions. While SIFMA generally agrees that misleading statements about such matters should be prohibited, we do not believe that such statements should be remedied by a prohibited transaction excise tax and rescission of related trades. We also note that the definition of "Material Conflicts of Interest" in Section VIII(h) of the proposed exemption provides no

[14] *See* 29 C.F.R. § 2550.408b-2(d) ("Section 2550.408c-2 of these regulations contains provisions relating to what constitutes reasonable compensation for the provision of services."); 29 C.F.R. § 2550.408c-2(b)(1) ("In general, whether compensation is 'reasonable' under sections 408(b)(2) and (c)(2) depends on the particular facts and circumstances of each case.").

explanation of the term “Material.”[15] The proposed definition in Section VIII(h) is so broad that it will be virtually impossible for financial institutions to enumerate every conceivable existing or potential conflict of interest. A materiality standard should be added to the proposed exemption by amending the definition of “Material Conflict of Interest” to state as follows: “A ‘Material Conflict of Interest’ exists when an Adviser or Financial Institution has a financial interest that, from the perspective of a reasonable person, could affect the exercise of its best judgment as a fiduciary in rendering advice to a Retirement Investor regarding an Asset.”

Warranties

The proposed BIC Exemption requires that the adviser and the financial institution warrant that: (i) they and their affiliates will comply with all applicable federal and state laws regarding investment advice and securities transactions; (ii) the financial institution has adopted written policies and procedures reasonably designed to mitigate the impact of material conflicts of interest and “ensure” that its advisers adhere to the impartial conduct standards; (iii) in formulating its policies and procedures, the financial institution specifically identified material conflicts of interest and has adopted measures to prevent material conflicts from causing violations of the impartial conduct standards; and (iv) the financial institution and its affiliates and related entities do not use “quotas, appraisals, performance or personnel actions, bonuses, contests, special awards, differential compensation or other actions or incentives to the extent that they would tend to encourage individual Advisers to make recommendations that are not in the Best Interest of the Retirement Investor.” Although differential compensation encouraging the adviser to act in a manner that is not in the client’s best interest would breach that warranty, differential compensation received by the financial institution itself would be permitted.

[15] The term “Material Conflicts of Interest” appears throughout the proposed exemption, and our comment on that term should be deemed restated each time the term appears. The repeated use of the term makes it even more important that the definition in Section VIII(h) be clarified.

These warranties are extremely troublesome, particularly in light of the resulting exposure to class action litigation. SIFMA requests that the first warranty be modified to warrant that the advisor, the financial institution and their affiliates have adopted policies that are *reasonably designed* to achieve compliance with all applicable law, not that they "will comply" with all applicable law. This is the regulatory standard that FINRA uses, and which the SEC approved.[16] We hope that the Department will recognize that this warranty would be provided in the context of the safeguards established by the SEC and FINRA and not require an absolute, strict liability declaration.

SIFMA also requests clarification regarding the second and third warranties. The Department should make clear that the second warranty requires the financial institution to warrant that it has adopted written policies and procedure that are *reasonably designed* to ensure that its advisers adhere to the impartial conduct standards, not that policies and procedures "ensure" such adherence. Similarly, the third warranty should be modified to warrant that the financial institution has adopted measures that are *reasonably designed to mitigate* material conflicts of interest, not that the financial institution has adopted measures "to prevent" such conflicts from causing violations of the impartial conduct standards. The financial institution cannot possibly adopt measures that will "prevent" material conflicts of interest.

SIFMA urges the Department to eliminate the fourth warranty regarding compensation practices entirely. Contrary to the Department's statement that the BIC Exemption "will broadly permit firms to continue to rely on common fee practices,"[17] we believe that this warranty will require a

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[16] Rule 3110(a) provides that: "Each member shall establish and maintain a system to supervise the activities of each associated person that is reasonably designed to achieve compliance with the applicable securities laws and regulations, and with applicable FINRA rules."

[17] 80 Fed. Reg. at 21961.

substantial, if not a complete, overhaul of broker compensation arrangements. Indeed, as far as we can tell, it will require the elimination of commission-based advice. Although the preamble indicates that the failure to comply with the mandated warranties would not result in a loss of the exemption, any breach of these warranties in the IRA setting, including the warranty regarding compensation policies and procedures, would be actionable under state contract law.[18] Thus, any warranty that differentiated commissions, sales loads, trail commissions,12b-1 fees and other payments from third parties do not "tend to encourage" violations of the best interest standard would expose financial institutions to the risk of class action litigation. To avoid that risk, financial institutions would be forced to eliminate differential and third party compensation arrangements with advisers (including attendance at training or other seminars to which advisers may be invited), as well as any bonus or incentive programs for advisers, in the provision of investment products and services to small plans and IRAs.

The preamble suggests several methods of satisfying the "policies and procedures" warranty, including the use of computer models to generate advice delivered by advisers, asset-based compensation, fee offsets, compensation systems based on the financial institution's determination of what products take more time or effort to sell, and compensation arrangements that are designed to align the interests of the adviser with the interests of the investor. None of these examples would reasonably permit the continuation of commission-based advice. Thus, contrary to what the Department says in the preamble, commission-based advice would be eliminated in brokerage accounts for IRAs, and an important choice for retirement investors about how to pay for advice would be gone.

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[18] *See* 80 Fed. Reg. at 21970 ("Failure to comply with the [policies and procedures] warranty could result in contractual liability for breach of warranty."); *id*. at 21972 ("The Department intends that all the contractual obligations (the Impartial Conduct Standards *and the warranties*) will be actionable by IRA owners.") (emphasis added).

Given their resulting exposure to class actions for breach of warranty, SIFMA believes that its members will either terminate their relationships with smaller plans and IRAs or offer only fee-based compensation arrangements. As the head of FINRA noted quite recently:

> … I have practical concerns with the Labor proposal in a number of areas. First, the warranty and contractual mechanism employed by Labor used to address their limited IRA enforcement jurisdiction, appears to me to be problematic. In one sweeping step, this moves enforcement of these provisions to civil class action lawsuits or arbitrations where the legal focus must be on a contractual interpretation. I am not certain how a judicial arbiter would analyze whether a recommendation was in the best interests of the customer "without regard to the financial or other interests" of the service provider. I'm not sure, but I suspect, a judicial arbiter might draw a sharp line prohibiting most products with higher financial incentives no matter how sound the recommendation might be. Similarly, I'm not sure how a judicial arbiter would evaluate which compensation practices "tend to encourage" violations of the exemption. It would appear likely, however, that firms would be required to demonstrate, at least, that any higher compensation was directly related to the time and expertise necessary to provide advice on the product, as specifically suggested by DOL. To say the least, making that case is not a simple proof standard.
>
> This all leads to my second concern that there is insufficient workable guidance provided either to the firm or the judicial arbiter on how to manage conflicts in most firms' present business models other than moving to pure asset-based fees, or a completely fee-neutral environment...I fear that the uncertainties stemming from contractual analysis and the shortage of useful guidance will lead many firms to close their IRA business entirely or substantially constrain the clients that they will serve. Put another way, the subjective language of the PTE, coupled

with a shortage of realistic guidance, may lead to few providers of these critical investor services.[19]

We believe that these concerns are well founded. Full and prominent disclosure, brought to the client's attention with some frequency, will do far more to shed light on fee differences, and educate clients regarding these differences, than arbitrarily banning fee differences in a business model that treats agency transaction compensation, principal transaction spreads, mutual fund fees and insurance company commissions differently. It is a not a "principles based" change to require this kind of massive overhaul in the way all brokers are compensated. In 2010, the Department suggested that it wanted a change in the law to make its enforcement program easier. We are very concerned that this exemption has the same aim, but at a huge cost to the financial services industry and those saving for retirement. We strongly urge the Department to reconsider this requirement.

If the Department determines to proceed with this approach, we ask the Department to delay the differential compensation rules for thirty six months. As the Department is well aware, the compensation paid to brokers differs *within asset types* and *across asset types*. It is simply unrealistic to require a change of this magnitude in eight months. Financial professionals with IRA or other plan clients would have to be excluded from firm-wide bonus pools that reflect the profitability of the entire firm, including retirement clients. Financial professionals also would have to be excluded from training programs if such programs are sponsored or supported by a mutual fund complex or similar provider of investment offerings. Changes like this will take years to plan and implement. Financial institutions cannot renegotiate the contractual arrangements with third parties and venders to alter the pay practices of every adviser within the eight month period provided in the proposed exemption. Delaying the differential compensation

[19] http://www.finra.org/newsroom/speeches/052715-remarks-2015-finra-annual-conference

rules by thirty six months should give financial institutions the time to redesign their programs, review all bonus and incentive programs, set new policies and procedures, retrain all necessary compliance, audit and risk teams, and put in new systems to accommodate these rules.

Contract Disclosures

Under the proposed BIC Exemption, the written contract must disclose all material conflicts of interest, and inform the investor of the right to obtain complete information about all fees associated with the assets in which the plan or IRA is invested, including “all of the direct and indirect fees paid [sic] *payable to* the Adviser, Financial Institution, and any Affiliates.” (Emphasis added). It must also disclose the existence of proprietary investment products, any fees that the adviser will receive from third parties in connection with the purchase, holding or sale of any asset, and the address of the website required by the exemption. Failure to include any of these disclosures would preclude reliance on the exemption, and advisers and financial institutions will be exposed class action lawsuits challenging the completeness of any such disclosures.

Again, the use of the prohibited transaction framework here is troublesome. For example, many indirect fees cannot be attributed to specific transactions or customers due to the nature of the compensation arrangements utilized by investment providers and do not affect the customer’s bottom line. For example, a mutual fund company may agree to pay a broker a flat fee that is unaffected by sales volume. The payment would be made regardless of whether the broker provides services to retirement investors and the payment may be insignificant when attributed to individual investors. Yet the smallest omission would require reversal of the transaction and payment of an excise tax, even where the omission had no effect on the transaction.

We urge the Department to incorporate the materiality standard described above in the definition of “Material Conflicts of Interest.” Otherwise, even the most inconsequential omission would require reversal of the transaction and payment of an excise tax and expose advisers and financial institutions to class action litigation. For purposes of assessing the disclosures, we recommend, and assume that the Department intends, that the terms “direct” and “indirect” have the same meanings ascribed to them in the recent amendments to the regulation under ERISA § 408(b)(2).

Prohibited Contract Provisions

As an initial matter, we note that the Department does not have the authority to create a new private right of action, which is what is done with the BIC requirement. Beyond this, SIFMA has concerns with a number of the contractual prohibitions in the BIC Exemption. The Exemption provides that the written contract may not limit the liability of the adviser or the financial institution for violations of the contract, nor may it waive or limit the retirement investor’s right to participate in class actions against the adviser and the financial institution. The Department states in the preamble that “[t]he right of a Retirement Investor to bring a class-action claim in court (and the corresponding limitation on fiduciaries’ ability to mandate class-action arbitration) is consistent with FINRA’s position that its arbitral forum is not the correct venue for class-action claims.” The Department also states, however, that “this section would not affect the ability of a Financial Institution or Adviser, and a Retirement Investor, to enter into a pre-dispute binding arbitration agreement with respect to individual contract claims.”

We believe that the BIC Exemption should allow advisers and financial institutions to exclude liability for actions and omissions outside of their control. If an adviser recommends a transaction, the investor approves it, but the transaction fails or is cancelled for lack of funding by the client, then the *client* should be responsible for the failure to settle the trade and any compensation received by the adviser should not be at risk under the BIC Exemption. Similarly, the acts or omissions of a third party, such as a custodial error in recording assets or trades, or impossibility due to an occurrence outside the control of the financial institution (a force majeure) should not cause liability on the part of a broker.

We also ask the Department to confirm in any final rule that, consistent with existing law, the contract with the retirement investor may exclude liability for punitive and consequential damages. In addition, we ask the Department to clarify that the contract may require the use of FINRA's securities dispute resolution forum as the venue for arbitrating claims under the contract. Finally, we urge the Department to eliminate the proposed prohibition of provisions waiving the right to bring a class or other representative action in court. The Department has no authority to prohibit such agreements under the Federal Arbitration Act.

Section III: Disclosure Requirements

As a general matter, SIFMA agrees that appropriate cost disclosure may enhance a retirement investor's ability to assess prospective transactions, whether in a plan or in an IRA. However, SIFMA is very disappointed that the Department chose not to rely on the detailed disclosures required by the 2012 amendments to its regulation under ERISA § 408(b)(2).[20] SIFMA's members opposed many of the requirements of that disclosure regime, largely on the ground that the costs of implementing the new requirements would greatly outweigh any benefits to be gained from them. But the entire industry complied with those requirements just three years ago. Now, after SIFMA's members have spent millions of dollars building the systems necessary to implement that disclosure regime, the Department is proposing to require a new disclosure framework, different from the first, which would be far more costly to design and implement.

Rather than continue down this path, SIFMA suggests that the Department incorporate the fee disclosure requirements of 29 C.F.R. § 2550.408b-2(c) into the BIC Exemption. Following

[20] *See* Reasonable Contract or Arrangement Under Section 408(b)(2)—Fee Disclosure, 77 Fed. Reg. 6632 (Feb. 3, 2012).

adoption, the Department could take the appropriate time to judge whether those disclosures provide plan fiduciaries, participants and IRA owners with sufficient information to assess conflicts of interest, and then determine based on actual experience with those disclosures whether it is still necessary to mandate the additional disclosures set forth in the proposal. This would allow SIFMA's members to rely on the systems already in place to make disclosures to IRA owners. With this approach the Department should make clear that it is permissible for financial institutions that are operating under the Advisers Act (*e.g.*, when recommending discretionary investment management services or advice programs as discussed above) to include the 408b-2 disclosures in their Form ADV disclosure brochures, as this will be more manageable for both advisers and their clients.

SIFMA offers the following additional comments with respect to the disclosure requirements of Section III of the proposed BIC Exemption:

Cost Disclosure at Time of Purchase

Under the proposed BIC Exemption, whenever an adviser executes a purchase of an asset for a retirement investor, the investor must be given a chart showing the "total cost" of the acquired asset over periods of one, five, and ten years. "Total cost" includes the acquisition cost (*e.g.*, loads, commissions, mark-ups on assets bought from dealers, and account opening fees), ongoing fees and expenses of pooled investment funds (*e.g.*, annualized mutual fund expenses), and costs of disposition (*e.g.*, surrender fees and back-end loads). The Department states that its proposal is designed to direct attention to fee information "in a time frame that would enable the Retirement Investor to discuss other (possibly less costly) alternatives with the Adviser prior to executing the transaction" and invites comment on all aspects of the provision of data both at the time of the transaction and annually.

We believe that this chart is unworkable. Providing an investment's "total cost" over one, five and ten year periods will require return assumptions, which no financial professional will be prepared to speculate about. The SEC and FINRA have for years taken the position that projected return information is unreliable and misleading to investors. Indeed, a communication to a retirement investor that purports to predict or project performance would violate FINRA Rule 2210(d)(1)(F). The Department lacks any special expertise in this area and should not attempt to override the judgment of the agencies that have that expertise,

We firmly believe that this disclosure requirement should be eliminated. Differing assumptions across firms to calculate future performance of products could mislead retirement investors. Forward-looking cost estimates, based on future performance speculation, is simply unsubstantiated speculation. Will the 1-, 5- and 10-year data be deemed to satisfy the requirement if they are calculated using FINRA rules? To the extent that an investment is not subject to FINRA's oversight (*e.g.*, GIPS standards or state insurance regulations), what assumptions would advisers be required to make in order to comply? Do the 1, 5 and 10 year calculations apply to stocks and bonds and bank deposits, and if so, how? No financial professional could operationalize these requirements and they should be dropped.

The chart would also slow trading to the disadvantage of retirement investors alone. While the financial professional creates the chart, provides it by mail or electronically, and waits for the retirement investor to see and approve it, the market moves, pricing changes, and valuable opportunities are lost. By focusing on cost to the exclusion of other investment characteristics such as historical performance, the chart also provides a distorted picture of the relative merits of a particular investment. In short, we believe that the chart envisioned by the Department would help no one, and at worst, would seriously undermine the financial institution's duty of best execution.

Practical issues surrounding the timing and mode of delivery of this chart provide yet another reason why it should be eliminated. How long would the adviser have to wait after mailing, emailing or other means of delivery to the investor before the adviser could reasonably assume the investor has reviewed the information? If the disclosure is provided in a compliant form, will the investor be precluded from later claiming that the adviser failed to explain the information sufficiently or that the investor did not find the disclosure to be adequate to assess a course of action? In all cases, an investor must instruct the adviser to make a trade only after having the full disclosure in hand. Will the adviser be required to furnish the disclosure, even if by postal mail, before the transaction can be placed? If so, the disclosure requirement might actually impede best execution or affect the advisability of the particular transaction.

Furthermore, many substantive elements of the disclosure make no sense given the narrow definition of permissible "Assets." We are confused by the reference to mark-ups in the costs of acquisition. Mark-ups are charged only on principal transactions, which are not covered by the exemption. Even if a fixed income security is sold on an agency basis, the adviser would have no way of knowing what the mark-up is, since it is charged by an unrelated dealer that has no legal duty to disclose the mark-up. If mark-up includes spread revenue on annuities, then the proposed disclosure requirement is inconsistent with the disclosures required by 29 C.F.R. § 2550.404a-5. The reference to account opening fees is also puzzling. Accounts do not seem to be covered as an Asset. What is contemplated by the required disclosure of mark-downs on assets sold to dealers? That information will not be available to the financial professional or the financial institution; if required, the third party dealer will not engage in the trade.

Various types of accounts impose fees at the time of opening, and some may have fees if the account is materially changed – such as transitioning an account from a pure investment vehicle to an annuitized account without liquidating any investments. Unless the definition of "Asset" under the BIC Exemption is revised to include a rollover account, the fees associated with opening a rollover account are not costs of acquiring an "Asset." More importantly, while we recognize that the Department's goal is to provide the investor with a sound basis to assess costs, we do not believe that including this type of account fee in the disclosure makes sense in the overall context of the regulation. Similarly, fees imposed to close an account do not have a connection to any "Asset." In our view, these disclosure items need to be rethought and better tailored to reflect the narrow list of assets permitted under this exemption.

Annual Fee and Compensation Disclosure

Under the BIC Exemption, within 45 days after the end of each year, the adviser must give the retirement investor a list of each asset purchased, sold, or held for his account during the preceding year, as well as a statement of all fees and expenses paid by the investor, directly or indirectly, during the year with respect to each asset. A statement of the total compensation received by the adviser and financial institution directly or indirectly from any party, as a result of each asset purchased, sold or held for the investor's account during the year also must be included.

We believe that this requirement should be eliminated. Requiring annual disclosure of all fees and expenses paid by the investor during the year would be duplicative of disclosures made at the time of sale (*e.g.*, through prospectuses and trade confirmations) and would only impose unnecessary costs on financial institutions that would ultimately be passed on to retirement investors. It would also be extremely difficult for advisers and financial institutions to identify all of the indirect compensation that they may receive. As stated previously, many indirect fees cannot be attributed to specific transactions or customers due to the nature of the compensation arrangements utilized by investment providers. By the same token, the amount of any indirect compensation attributable to a specific transaction or customer may be insignificant, and the failure to disclose even an immaterial amount of indirect compensation could result in a complete loss of the exemption.

If the Department insists on retaining this annual disclosure requirement, it should be expressly limited to assets *for which investment advice was provided* during the preceding year. We assume that is the Department's intent, and request that the Department make that limitation clear. We also respectfully request that the timing of the annual disclosure be revised to match the timing requirements for the annual Form 5500. We do not believe any meaningful purpose is served by requiring the disclosure within forty-five days after each year end. Further, our members believe that this time frame is not reasonable and should, at the very least, be extended to ninety days. Also, for fees and expenses paid by the investor, estimates should permitted, as they are in the Department's current regulation under ERISA § 408(b)(2) – for example, fees for pooled investment vehicles are estimated based on the average annual fee rates of those vehicles. The Department should also permit estimates for indirect compensation and require only that material amounts be disclosed.

Web Disclosure

The BIC Exemption requires the financial institution to maintain a web page that lists all "direct or indirect material compensation" payable to the adviser for services in connection with each asset (or, if uniform across a class of assets, the class of assets) that an investor is able to purchase, hold or sell through the adviser and that has been purchased, held or sold in the last 365 days, along with the source of the compensation and how it varies within and among assets. The information also must be accessible in a machine readable format. This presumably requires the detailing of every insurance company separate account, every collective trust by unit class, every mutual fund by share class, every annuity contract and every GIC.

SIFMA views the web page disclosure requirement as overly broad, very impractical, and extremely costly and cumbersome to build, administer and maintain. SIFMA's members have had the experience of modeling disclosure for plans and participants in the last five years. They do not believe that such an undertaking would achieve the Department's stated goal of providing "a broad base of information about the various pricing and compensation structures adopted by Financial Institutions and Advisers."[21] In addition, although the Department states that a related goal is to provide information that enables "financial information companies" to analyze and compare fee and compensation practices of advisers and financial institutions, this is a massive undertaking, requiring daily review for product and fee changes, and would cost millions of dollars for every single financial institution. We simply do not see how establishing a publicly available web page would serve the interests of the public and it certainly could not be cost justified. Even if the Department's goal is to condense information that would then be aggregated and disseminated by "financial service companies," the varying degrees of payments that could be attributed across the many types of institutions would be meaningless. In addition to these steep challenges, the information would not have any use for members of the public, even for participants of plans that invest in privately managed accounts.

We urge the Department to abandon the proposed web page disclosure requirement as a condition for relief under the BIC Exemption. This requirement, coming so close on the heels of the massive section 408(b)(2) project, is simply impossible to justify. On its own, it will result in brokers refusing to use the exemption, which in turn will result in more leakage of retirement savings from tax-advantaged accounts and widespread confusion on the part of retirement investors, neither of which is in their interest.

Section IV: Range of Investment Options

Under the BIC Exemption, the financial institution must offer and the adviser must make available a range of assets that is broad enough for the adviser to make recommendations with respect to every asset class necessary to serve the retirement investor's best interests. The

[21] 80 Fed. Reg. at 21973.

exemption permits the financial institution to offer only proprietary products, only those that generate third party fees or only those of a particular asset class or product type, if it makes a written finding that the limitations do not prevent the adviser from providing advice that is in the investor's best interest, if the compensation received for the services provided to the investor is reasonable, and if the investor is given written notice of the limitations placed on assets that may be offered to the investor. The adviser must notify the investor if the adviser does not in fact recommend a sufficiently broad range of assets to meet the investor's needs.

The precise language in Section IV(a) of the exemption states that the financial institution and adviser must offer "a range of Assets that is broad enough to enable the Adviser to make recommendations with respect to all of the asset classes reasonably necessary to serve the Best Interests of the Retirement Investor in light of its investment objectives, risk tolerance, and specific financial circumstances." The Department should make clear that the term "asset classes" refers to the broad categories of equity, debt and cash instruments, rather than subcategories or other classifications that are less easily categorized. Any other intended meaning would be unworkable and lead to confusion.

The Department's use of the phrase "range of Assets" in Section IV(a) is also confusing. Could a financial institution that offers only mutual funds have a "range of Assets" that is broad enough to satisfy the requirements of Section IV(a)? What about a financial institution that offers bank deposits, CDs and money market funds? How would the requirement of a "broad enough" array of "Assets" apply in cases where a financial institution specializes in a limited range of asset classes? Could a specialist in fixed income satisfy the broad "range of Assets" requirement of Section IV(a) if the specialist recommends a broad range of corporate bonds, agency debt and U.S. Treasury securities that meet the definition of an "Asset" under the BIC Exemption, or would the specialist have to advise on an entire range of asset classes? Could such a fixed income specialist satisfy the broad "range of Assets" requirement in Section IV(a) with respect to some retirement investors but not others? The Department acknowledges that some firms "specialize in particular asset classes or product types" and suggests that such firms may still be able to use the exemption;[22] however, it is unclear how the "range of Assets" requirement could be satisfied outside the context of mutual funds. We urge the Department to limit this requirement to recommendations to purchase, hold or sell mutual funds.

Section IV(b) focuses on financial firms that exclusively offer specialized and/or proprietary products, which may or may not cross an array of asset classes. Many of the above questions about Section IV(a) reflect confusion about the interplay between Sections IV(a) and (b). We believe that Section IV(b)'s "Section (a) notwithstanding" language should be clarified to delineate the scope of the general rule and the exceptions and conditions.

We are also unclear about how the conditions of Section IV(b) would be applied in operation. The conditions of Section IV(b) specify that the firm and adviser must satisfy the best interest, impartial conduct and reasonable compensation standards contemplated by the proposal and notify the retirement investor of the limitations placed on the Assets offered to the investor. These requirements of Section IV(b) raise a number of questions.

- To the extent that a financial institution offers a limited range of investment options, does Section IV(b)(1) require the financial institution to make a separate written finding for each retirement investor that the limitations on Assets available for purchase do not prevent the advisor from acting in the best interest of the retirement investor or otherwise adhering to the impartial conduct standards? Can this requirement be satisfied by a written finding that applies to all of the financial institution's retirement investor clients?

[22] *See* 80 Fed. Reg. at 21975.

- How would the adviser address questions from a client in a case where Section IV(b)(4) requires the adviser to provide notice that it is not recommending a sufficiently broad range of investment options to meet that client's needs? For example, assume a financial institution's business model is to sell only funds with agreements for compensation, and it and the adviser make the finding required under (b)(1). Further narrowing the range of investments, the individual adviser advises only on bond funds regardless of whether other advisers may recommend a broader range. Does Section IV(b)(4) require the adviser to provide the investor with a notice stating literally that "the Adviser does not recommend a sufficiently broad range of Assets to meet the Retirement Investor's needs"? Section IV(b)(4) should be revised to make clear that the notice can be phrased in less pejorative terms that are more tailored to fit the circumstances – *e.g.*, "Please understand that the adviser provides recommendations only on bond funds and that the adviser's recommendations are not intended to encompass the entire range of assets that might be necessary to meet your needs."

In addition to the questions noted above, it is unclear whether the notice required by Sections IV(b)(3) must be repeated every time a recommendation is made, updated or changed. Similarly, under what circumstances would a change in the limitations on Assets offered to retirement investors render a notice provided under IV(b)(3) insufficiently specific? For example, what if the financial institution changes the amount or percentage of revenue sharing it expects to receive? Would it be sufficient in all such cases to state in a notice that the firm expects to receive payment from the investment providers whose products are being offered, or is more specific disclosure required as to the relative amounts of such compensation?

The requirements of Section IV(b)(1), (3) and (4) are vague and confusing. We urge the Department to eliminate these sections, or repropose them with more clarity and objective requirements. Failure to meet this exemption requires reversal of the transactions done under it, and payment of a significant excise tax. It is quite unfair to impose a vague, internally inconsistent, and ill-defined requirement with these severe penalties.

Finally, we request that Section IV(b)(2) be deleted. That condition requires that any compensation be "reasonable in relation to the value of the specific services provided to the Retirement Investor in exchange for the payments and not in excess of the services' fair market value." Because the impartial conduct standards already prohibit the receipt of compensation in excess of what is reasonable, Section IV(b)(2) should be unnecessary.

To the extent that Section IV(b)(2) purports to establish a different standard of "reasonable compensation," we believe that it is too prescriptive and narrow to be workable. A standard requiring that compensation be no more than "fair market value" for the specific services provided to plan investors and individual investors alike would be extremely difficult to apply. How would a financial institution prove reasonableness in relation to the specific services provided to the retirement investor if the firm has only omnibus expenses that are based on services and profitability across a large retirement plan book of business? Would it be reasonable to allow an adviser to recommend one mutual fund over another where the adviser knows that the recommended fund's investment manager pays the adviser's firm more than another fund manager? Would the firm be prepared to show that the adviser's only economic benefit would be greater fees paid to his firm, or would the firm be better advised to recommend only funds with the lowest third party payments? Third party fees vary widely. If a financial institution accepts a low fee from one fund, would all other fund fees in excess of that level be unreasonable on the ground that the benefit to the firm is indirectly compensating the individual adviser?

In short, the "reasonable compensation" standard articulated in Section IV(b)(2) is unreasonable, and appears to be drafted as an impossibility: unless a financial professional can trace every dollar to a particular service to a particular account in connection with a particular transaction and demonstrate that others charge the same way, he is destined to fail. We suggest that this has never been the law, nor even the Department's position with respect to the reasonable compensation requirements of the statutory exemption for services.

Sections V and IX: Disclosure to the Department, Recordkeeping and Data Requests

Section IX of the BIC Exemption requires financial institutions to maintain information at the financial institution level by quarter, concerning investment inflows, outflows and holdings for each asset purchased, sold or held under the exemption, including: the identity and quantity of each asset purchased, held or sold; the aggregate dollar amount invested or received and the cost to the investor for each asset purchased or sold; the cost incurred by the investor for each asset held; all revenue received by the financial institution or its affiliate in connection with the purchase, holding or sale of each asset, disaggregated by source; the identify of each revenue source and the reason for the payment. In addition, financial institutions must maintain information at the investor level concerning the identity of the adviser, the beginning- and end-of-quarter value of each investor's portfolio, and each external cash flow to or from the investor's portfolio during the quarter.

Section V(b) of the BIC Exemption further requires that this data be maintained for a period of six years from the date of the transaction for which relief is sought under the exemption and that it be made available to the Department upon request *within six months from the date of the request*. In addition, Section V(c) requires the financial institution to maintain for a period of six years records demonstrating that the conditions of the exemption have been satisfied. Such records must be made available to the Department, the Internal Revenue Service (IRS), any retirement investor and any contributing employer or employee organization whose members are covered by a plan that engaged in a transaction under the exemption.

The preamble states that the purpose of the Section V(b) data request requirement is to "assist the

Department in evaluating the effectiveness of the exemption." The effect of that requirement, however, would be to invalidate past and future compensation covered under the exemption if the Department's data request cannot be met within the six month period. Creating a system that would be able to respond to such a data request will be extremely costly and time consuming. The cost implications of these data request requirements are described in greater detail in the Deloitte report submitted with this comment letter. We do not believe that these costs are justified by the benefit the Department suggests would be obtained. We urge the Department to eliminate the data request requirements of Sections V(b) and IX entirely.

If the Department decides to move forward with the data request requirements of Sections V(b) and IX, it should extend the effective date of these requirements by at least thirty-six months to give the industry adequate time to develop the systems necessary to capture the data and perform the calculations contemplated by the requirements. We also ask the Department to eliminate the Section IX(e) public disclosure provision. We believe it is entirely inappropriate to disclose portfolio return information alongside the identity of the individual advisor in a public filing. It appears that the entire purpose of this disclosure is to embarrass or otherwise call out advisors whose clients have lower returns, regardless of whether the clients' returns are determined by their own choice of strategies, and not by their advisor's skill or expertise. It is a blunt instrument, without any differentiation between asset classes, age or risk tolerance of the investor, or any other parameter that would actually be relevant to a comparison.

In addition, we ask that the data request requirement in Section V(b) be modified to parallel the exception in the proposed recordkeeping requirement of Section V(c) for records that are lost or destroyed due to circumstances beyond the control of the financial institution. We also request clarification that, to the extent a financial institution cannot rely on the exemption due to a failure to maintain or provide information that complies with a data request under Section V(b), that the inability to rely on the exemption will apply only prospectively from the date the BIC Exemption becomes unavailable to that institution, and that there will be no retroactive consequences.

In contrast, we believe that the comprehensive disclosure framework administered by the SEC and FINRA is far more targeted and nuanced in an appropriate manner. Particularly in light of the privacy risks highlighted by the widely-publicized hacking of confidential personal information concerning millions of federal employees, we believe that sensitive information about individual investors should either be excluded from the data request requirements of Sections V(b) and IX, or at the very least subject to a right on the part of the investor to "opt out" of having their sensitive financial information scrutinized, or even inadvertently disclosed, by federal regulators. At the very least, we believe this section should require all retirement investors to be warned that every transaction they engage in will be reported to the federal government.

Section VII: Exemption for Pre-Existing Transactions

The supplemental relief for pre-existing transactions would provide relief from the prohibitions of ERISA §§ 406(a)(1)(D) and 406(b) and Code §§ 4975(c)(1)(D), (E) and (F) for the receipt by advisers of prohibited compensation in connection with transactions that were entered into prior to the applicability date of the proposed regulation. The supplemental relief for pre-existing transactions applies to the receipt of compensation for services in connection with the purchase, holding or sale of an "Asset" by IRAs, participant accounts and *all* ERISA plans, regardless of size and whether or not the plan is participant-directed. The supplemental relief would cover advisers who did not consider themselves fiduciaries prior to the applicability date, as well as advisers who considered themselves fiduciaries but relied on an exemption that has since been amended. The proposed conditions for supplemental relief would require that the compensation be received under an arrangement that was entered into prior to the applicability date. The proposed conditions also would require that the adviser not provide any "additional advice" regarding the purchase, holding or sale of the asset after the applicability date. The proposed conditions would also exclude transition relief for any compensation received in connection with a purchase or sale that was a non-exempt prohibited transaction when it occurred.

SIFMA does not believe that it would be in the best interests of retirement investors to deny transition relief for advice to hold or sell or otherwise dispose of assets already held in such accounts. Not providing advice to a retirement investor on assets that the advisor previously recommended will only confuse the investor. Advisers should be able to continue to receive compensation for any asset in the retirement investor's account prior to the effective date of the rule as long as the adviser does in fact continue to give advice to the investor. That is a common sense approach and is in the retirement investor's best interest.

We also would ask that any acquisitions or dispositions that are effected after the applicability date of the regulation pursuant to any standing or automatic investment instructions effected before the applicability date (*e.g.*, investment instructions to rebalance back to the original investment allocation) be afforded protection under the BIC Exemption. These modifications would allow investors and advisers to continue on previously agreed courses of action, with the relief to end immediately upon any new recommendation or transaction that otherwise would trigger the contractual and other requirements of the BIC Exemption.

We believe that investors are best served by transition guidance that enables them to dispose of assets that they or their advisers no longer wish to own. The adoption of a new set of rules should not make it more cumbersome to advise, recommend or process an order to liquidate a pre-existing position, particularly given the time it will undoubtedly take to bring pre-existing accounts into compliance with the new rules. Rather, the disposition of a pre-existing position for cash should be grandfathered under existing rules, although any recommendation to re-invest that cash would, appropriately, be subject to the new fiduciary definition. Any other approach would be, at best, confusing to explain and apply, and at worst, inhibit communications between advisers and clients about poorly performing assets. In the event there is no relief for advice regarding pre-existing holdings, however, we recommend that prohibited transaction relief for such advice be conditioned only on compliance with the "best interests" standard proposed by FINRA. In this way, firms will be able to limit sales or other dispositions of assets that may generate extra compensation for the adviser, such as a back-end load or surrender charge.

We believe that it is equally important to extend transition relief to acquisitions of investments that are part of an automatic savings and investment program. For example, if a plan participant elects automatic salary deferrals into the plan after receiving advice from an adviser prior to the applicability date, we do not believe it serves the interests of anyone involved to require that such advice be revisited and, most likely, given again subject to the fiduciary standard, with or without the BIC Exemption. It would create an enormous burden for financial firms, and it is difficult to understand how it would benefit the participant. If, of course, the adviser recommends any increase in the investment amount, or changes the recommended asset mix after the applicability date, the new fiduciary framework would apply. Similarly, standing asset allocation (and rebalancing) instructions and automatic dividend reinvestment should not be an inadvertent compliance trap, so long as it is not changed or advised to be changed. Mutual fund and annuity "dollar-cost averaging," where an individual purchases a highly liquid interest, usually a money market fund, and has the money fund account automatically fund other investments at pre-set intervals, also should be unaffected if the dollar-cost averaging advice and investment program were set before the applicability date.

SIFMA is also concerned that the narrow definition of the term "Asset" could have serious adverse consequences if the exemption for pre-existing transactions is adopted in its proposed form. As we understand the proposed transition relief in Section VII, if a pre-existing holding is not an "Asset" within the meaning of the BIC Exemption, Section VII will provide no relief for any compensation received with respect to that holding going forward, and Section I likewise will provide no relief for any advice or recommendations with respect to that holding going forward. Denying transition relief for compensation received with respect to pre-existing holdings that are not "Assets" not only defeats legitimate expectations of the contracting parties, but will create a huge compliance burden from the instant the rules become applicable. Advisers and financial institutions will have to determine promptly which pre-existing accounts hold investments that meet the definition of an "Asset," which hold investments that do not meet that definition, and which hold both types of investments. For any pre-existing accounts that hold investments that are *not* "Assets," advisers and financial institutions will have to immediately suspend the receipt of any compensation attributable to such assets and cease to provide any advice or recommendations with respect to such non-"Assets" going forward. For accounts that hold both "Assets" and non-"Assets," segregating any ongoing compensation associated with "Assets" covered by the transition rule will present its own technical challenges, and advisers and financial institutions may have no choice from a compliance perspective but to split the "Assets" and non-"Assets" into separate accounts. Such splitting into separate accounts would not only increase recordkeeping and other costs, but also make it more difficult for the account owner to monitor his accounts with the financial institution.

Furthermore, because of the time it would take to identify every account holding non-"Assets," advisers and financial institutions may have to place all of their retirement accounts into a "no advice" category until all of these issues can be sorted out. The process of identifying all pre-existing account holdings that are not "Assets" will be extremely costly and time consuming, and the account owners themselves are likely to be bewildered and upset by the entire experience. We do not believe this is workable and we urge the Department to broaden the scope of transition relief.

The transition relief also suffers from the concerns we have previously raised regarding multiple accounts, such as an IRA and a non-retirement account, and the limited scope of the "Asset" definition. We will not reiterate all of those concerns in this section of our comments, but we wish to point out that, apart from the fiduciary requirements and proposed exemptions, there is no history in account construction or composition that differentiated among assets as the Department now proposes. Therefore, while the issues we raised above certainly apply in the context of future accounts, assets and recommended transactions, the complications are multiplied where financial firms are maintaining multiple pre-existing accounts for clients. It will be next to impossible to succinctly explain to clients or advisers how the rule regarding "Assets" is to be applied, particularly with long-standing investment accounts.

The Request for Comment on a Low Fee Streamlined Exemption

The preamble to the proposed exemption seeks comments on whether the Department should issue a separate class exemption, with fewer conditions, for advice concerning low-fee index funds. Examples mentioned in the preamble are "a long-term recommendation to buy and hold a low-priced (often passively managed) target date fund that is consistent with the investor's future risk appetite trajectory" and "a medium-term recommendation to buy and hold (for 5 or perhaps 10 years) an inexpensive, risk-matched balanced fund or combination of funds, and afterward to review the investor's circumstances and formulate a new recommendation."

This contemplated exemption appears, similar to the "Asset" definition, to indicate a policy preference by the Department for passively managed target date funds. Neither ERISA nor the Code authorizes the Department to implement such policy changes. Further, we disagree with this approach because there is no good evidence that passively managed investments are "safer" than actively managed investments. An investment in an S&P 500 index fund reflects an affirmative decision to invest in large U.S. equities (and incidental futures used to smooth rebalancing transactions, or large inflows and outflows). The fund's investment strategy is quite simple to explain, but its underlying assets are subject to all of the market volatility and to some extent sector volatility that underlie all equity investing. We do not believe that any element of such vehicles, in and of itself, lends itself to a different fiduciary analysis, and we reiterate our view that the Department's desire to simplify the investment advice for retirement investors should not result in the Department lending favored status to any particular investment type. We recommend even-handed treatment of investments in the BIC Exemption and in the fiduciary regulation overall absent specific features that demand special precautions.

Section VIII: Definitions

Many of SIFMA's questions and comments regarding the proposed definitions in the BIC Exemption are addressed as they arise in the proposal itself. What follows is a list of additional comments and questions concerning the definitions, not specific to any particular functional part of the exemption.

Adviser – Under the proposed fiduciary regulation, there is no carve out for call centers or their personnel. SIFMA has separately commented on that proposal. For purposes of the BIC Exemption, call center employees may be compensated in a way that puts them in a position that requires relief. However, to meet the definition of an "Advisor" under Section VIII(a) of the BIC Exemption, call center employees would have to "[s]atisfy the applicable federal and state regulatory and licensing requirements of insurance, banking, and securities laws with respect to the transaction." We are concerned that this language may require call center employees to register with the SEC as "advisers" under the Investment Advisers Act of 1940 ("Advisers Act"). Unless the Department decides to include a specific carve out in the fiduciary regulation for call centers, we urge the Department to clarify that call center employees do not have to register as "advisers" under the Advisers Act to qualify for relief under the BIC Exemption.

The Department, in the proposed fiduciary regulation, has cited its extensive coordination with securities regulators. We are hopeful that the SEC and the Department are aligned on the "Adviser" definition, and that invoking the relief provided by the BIC Exemption will not, by itself, trigger a separate registration requirement with the SEC under the Advisers Act to the extent there was no other need to register under that statutory framework.

Affiliate – We urge the Department to revise this definition to provide greater consistency with the federal securities laws, particularly with respect to the individuals covered in paragraph VIII(b)(2). The ERISA and Code definitions cited in that section will introduce an additional compliance hurdle to the extent those definitions do not align with the common definitions applied in the securities law context.[23] We recommend using the existing framework of broker-dealers' compliance programs, which are predicated not only on an "affiliate" definition but also on an "associated person" definition.

Best Interest – The proposed best interest standard requires advisers and financial institutions to prove that their recommendation was made "without regard to the financial *or other interests* of the Adviser, Financial Institution or any Affiliate, Related Entity *or other party*." We recommend that this clause be replaced with the phrase "and place the interests of the Retirement Investor ahead of their own." At a minimum, for the reasons explained in our comments on the impartial conduct standards, we urge the Department to delete the phrases "other interests" and "or other party" from the current formulation of the standard.

Financial Institution – Section VIII(e)(2) defines the term "Financial Institution" to include a bank or similar financial institution supervised by the United States or a state, or a savings association, "but only if the advice resulting in the compensation is provided through a trust department of the bank or similar financial institution or savings association which is subject to periodic examination and review by federal or state banking authorities." We see no reason to

[23] Rule 12b-2 under the Securities Exchange Act of 1934 defines "Affiliate" as a "person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, the person specified." That Rule contains a separate definition for an "associate": "(1) any corporation or organization ...of which [a] person is an officer or partner or is, directly or indirectly, the beneficial owner of 10 percent or more of any class of equity securities, (2) any trust ..., and (3) any relative or spouse of such person, or any relative of such spouse, who has the same home as such person or who is a director or officer of the registrant or any of its parents or subsidiaries."

limit this definition to advice provided through a bank's trust department. Advice to IRA owners may emanate from any department of a bank and all areas are subject to federal or state supervision.[24] Accordingly, we request that the entire "but only if" clause be dropped.

Independent – As written, the definition of "independent" would disqualify any company that provides services to the financial institution, such as its accounting firm, lawyers, cleaning services, food services, security services, parking services, window washing services, etc. To the extent any of those companies sponsors a plan, the plan sponsor would not be "independent," regardless of how small the amount of income received from the financial institution. Historically, the Department has recognized this fact in virtually every exemption it has granted and we assume its failure to do so here was inadvertent. Accordingly, we suggest that subsection (2) of the definition of "independent" in Section VIII(f) should be replaced with the following: "Receives less than 5% of its gross income from the Adviser, Financial Institution or Affiliate." In addition, subsection (3) should be revised to make clear that an IRA owner will not be deemed to fail the independence requirement simply because he or she is an employee of the financial institution.

Individual Retirement Account – We believe that health savings accounts (HSAs) should not be included in the definition. HSAs by their terms are not intended for retirement income but rather health care expenses. To be clear, we argue the same is true for other tax favored savings vehicles that are not intended to provide retirement security, such as college or other educational savings accounts that may be offered through broker-dealers.

[24] The bank regulators at the federal level include the Office of the Comptroller of the Currency, the Consumer Financial Protection Board and the Securities and Exchange Commission.

Material Conflict of Interest – This definition should be revised to incorporate the standard of materiality described above in our comments concerning the impartial conduct standards. Without more, the Department's proposed definition could be interpreted to cover even the most remote financial interest that could possibly affect one's best judgment, regardless of whether the effect of the financial interest would be material.

Proprietary Product – Section VIII(j) defines a "proprietary product" as one that is "managed by" the financial institution or any of its affiliates. However, investment products are generally considered "proprietary" to a firm when they are issued or sponsored by the firm or an affiliate. We recommend a definition more in line with these concepts and believe that the term "managed by" is not a meaningful indicator of "proprietary" status.

SIFMA and its members appreciate the opportunity to comment and look forward to meeting with the Department to discuss our concerns. For further discussion, please contact the undersigned at 202-962-7329.

Sincerely,

Lisa J. Bleier

Lisa J. Bleier
Managing Director, Federal Government Relations
and Associate General Counsel