

July 21, 2015

Filed Electronically

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

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

Re: Conflict of Interest Rule – Retirement Investment Advice      RIN 1210-AB32

Ladies and Gentlemen:

Financial Engines respectfully submits the following comments in response to the Department of Labor's proposed regulation entitled *Definition of the Term "Fiduciary; Conflict of Interest Rule – Retirement Investment Advice,"* published in the April 20, 2015 Federal Register.<sup>1</sup> We applaud the Department's proposal to update the definition of fiduciary under 29 CFR 2510.3-21(c), and support the objective of improving protections for retirement investors by seeking to ensure that persons providing investment advice are subject to ERISA's standards of fiduciary conduct. We share the concern that the current regulation may not adequately protect the interests of retirement investors and may limit unnecessarily the scope of ERISA's fiduciary protections. ERISA's fiduciary standards provide important protections against conflicts of interest and self-dealing and, particularly in light of changes in the financial industry, it is crucial now more than ever to re-examine the types of relationships that should give rise to fiduciary duties under ERISA and to apply these protections broadly.

We thank the Department for encouraging input on the proposed regulation. The Department's public comments have provided additional helpful clarification as to the intended objectives and interpretation of the proposed regulation. We are respectfully submitting these comments to provide responses to several of the questions posed by the Department, and to offer specific proposals to address a few potential ambiguities and areas where there may be unintended consequences. We have provided marked changes to the proposed regulation, in the hopes of making our suggestions somewhat easier to follow.

## **Financial Engines**

Financial Engines Advisors L.L.C., a wholly owned subsidiary of Financial Engines, Inc., is a registered investment adviser that provides personalized investment advice and management services to retirement investors. Financial Engines provides such services as a fiduciary under the Employee Retirement Income Security Act of 1974, as amended ("ERISA") and the parallel prohibited transaction restrictions of the Internal Revenue Code.<sup>2</sup> Financial Engines is the leading provider of independent advisory services to large plan sponsors, working with many of the nation's largest employers and retirement service providers to provide access to advisory services to over 9 million participants in 401(k) and similar plans. Notably, while Financial Engines may be best known for providing discretionary investment management through our Professional Management service (managed accounts program) since September 2004, the company was founded to provide non-discretionary investment advice, and continues to do so today.

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<sup>1</sup> 80 Fed. Reg. 21928 (Apr. 20, 2015).

<sup>2</sup> Except as expressly noted, references in this letter to ERISA should be read to include the corresponding provisions of the Internal Revenue Code.

Established in 1996 by Nobel Laureate William Sharpe, former SEC Commissioner Joseph Grundfest, and the late Craig Johnson, then-chairman of the Venture Law Group, Financial Engines offers personalized, independent, and high-quality investment advice to individuals, regardless of their wealth or investment experience. We assist individuals with developing a personalized and comprehensive savings, investing, and retirement income plan. We use sophisticated technology to deliver services that help individuals set an appropriate risk level for their goals and situation, and create a diversified investment portfolio from among the investment choices available in their employer's 401(k) plan.

We can either professionally manage an employee's 401(k) account on a discretionary basis or provide online advice through expert recommendations, interactive tools and certified advisors. For employees who decide to rollover their 401(k) when retiring or leaving their employer, we can also manage the employee's, or their spouse's, individual retirement accounts ("IRA") assets. Annually, Financial Engines provides a retirement readiness assessment, including estimated annual retirement income from Social Security, 401(k)s, IRAs, and pensions, if applicable, to all employees in the plans we serve. For employees selecting the Income+ feature of Financial Engines® Professional Management service, we will manage the portfolio to be ready to generate retirement income, and can generate steady payouts that are designed to last for life with the purchase of an optional out-of-plan fixed annuity. Financial Engines is not affiliated with any other financial services entity, does not manufacture or sell investment products, and does not accept commissions or product-based revenue sharing.

Financial Engines believes that our history and growth support the conclusion that it is neither onerous nor impossible for service providers to provide high quality services in a fiduciary capacity to large numbers of plans and participants. We have a proven track record of providing high-quality independent investment advice. Financial Engines is America's largest independent registered investment advisor.<sup>3</sup> Financial Engines works with more than 600 large employers (including 146 of the FORTUNE 500) and 8 of the largest retirement plan providers serving the defined contribution market. As a result, over three million people have used Financial Engines Online Advice<sup>4</sup>, and approximately 900,000 have their retirement account professionally managed by the company<sup>5</sup>. Nearly 240,000 of our discretionary managed account service clients have less than \$20,000 in their 401(k) portfolio, and the median balance is \$57,000.<sup>6</sup> Over 77% of the professionally managed portfolios are unique to the individual. The median balance for the more than 9 million plan participants with access to our services is \$32,000, and approximately 43% of those participants have less than \$25,000 in their 401(k) portfolio.<sup>7</sup>

**I. The preamble to the proposed regulation and proposed exemptions provide useful clarification and context relative to existing advisory opinions and other guidance.**

With a regulatory regime as complex as ERISA, it is often difficult to interpret the impact of proposed new regulation on existing interpretations and guidance. We appreciate the Department's specific confirmation, in the preamble to the Proposed Best Interest Contract Exemption,<sup>8</sup> that the Department is not retracting the views expressed in Advisory Opinion 2001-09A (the "SunAmerica Letter"). We also appreciate the Department's clarification that the proposed regulation is directed to

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<sup>3</sup> For independence methodology and ranking, see InvestmentNews RIA Data Center. (<http://data.investmentnews.com/ria/>).

<sup>4</sup> As of December 31, 2014, the number of people who have accepted our online services agreement.

<sup>5</sup> As of March 31, 2015.

<sup>6</sup> As of March 31, 2015.

<sup>7</sup> As of March 31, 2015.

<sup>8</sup> 80 Fed. Reg. 21960 (Apr. 20, 2015).

the provision of investment advice, and does not change the responsibilities of advisers who have full investment discretion with respect to plan or IRA assets, which is consistent given that in these instances fiduciary status has been affirmatively accepted.<sup>9</sup>

**II. While we agree that providing advice regarding the selection of an adviser should generally be subject to a fiduciary standard, the proposed regulation could unduly restrict the ability of investment advisers to present their services to an individual retirement investor.**

**A. Concern: An investment adviser's conversation with a retirement investor about the fiduciary advisory services it makes available could be construed as a "recommendation" of such advisory services, triggering fiduciary status with respect to that initial conversation and, potentially causing a prohibited transaction if the retirement investor uses such services and the adviser then receives fees, even when those fees are reasonable, fully disclosed, and free of potential conflicts of interest. Unless clarified, this could make it difficult for an investment adviser to present its fiduciary services to a retirement investor.**

The Department has long recognized the need for investment advice directed to retirement investors. Further, Congress and the Department have also recognized that retirement investors do not always use the help that is available to them. To reach retirement investors who need help, it is essential that advisers be able to provide information to retirement investors about their services. These communications may take the form of in-person presentations, printed mailings, electronic communications, social media, and phone or email contacts. We believe it is beneficial to retirement investors to receive information in a form that suits their particular needs, and through a wide variety of channels or approaches to engage retirement investors with different communications preferences. In the case of registered advisers, any such communications would be delivered in compliance with applicable securities laws.

We understand the Department's intent with the proposed regulation is to increase the access a retirement investor has to obtaining investment advice within a fiduciary relationship. However, unless clarified, the proposed regulation may block the initial contacts with retirement investors necessary for an investment adviser to engage such individuals in a fiduciary relationship. Under the proposal, some of these communications, especially one-on-one conversations with an adviser's representatives, in person, or by phone, email, or "chat", could be characterized as providing a recommendation of a fiduciary adviser, and thus could be characterized as fiduciary investment advice at the time of such discussions and presentation of services. Under such an interpretation of the proposed regulation, fiduciary status is immediately triggered, and, unless an exemption is available, a prohibited transaction may result if the adviser then receives fees, even when those fees are reasonable, fully disclosed, and free of potential conflicts of interest. We are not aware of an existing exemption that would serve in the circumstances described. The proposed "Best Interest Contract Exemption", which is primarily designed to permit the receipt of conflicted fees for recommending certain investment products, if certain conditions are met, would also not be applicable.

This interpretation is based on the current language of section 2510.3-21(a)(1)(ii), which provides that investment advice includes "[a] recommendation as to the management of securities or other

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<sup>9</sup> These advisory relationships may be established by an agreement between a plan sponsor or other authorized plan fiduciary on behalf of a plan participant, as reflected in the Department's regulation on qualified default investment alternatives. Default Investment Alternatives Under Participant Directed Individual Account, 72 Fed. Reg. 60452 (Oct. 24, 2007).

property”, and section 2510.3-21(a)(1)(iv), which provides that “[a] recommendation of a person who is also going to receive a fee or other compensation for providing any of the types of advice described in paragraphs (i) through (iii).” The proposed definition of “recommendation” under the proposal (when communications are “specifically directed to the advice recipient” as provided under section 2510.3-21(a)(2)(ii)) further contributes to this interpretation.

It also is important to address the situation of advisers who are already acting in a fiduciary capacity relative to a particular retirement investor. This arises when an adviser offers different types of advisory services. For example, Financial Engines may act as a fiduciary for an individual who is using one of our services, such as our non-discretionary online advice service, who wishes to explore using our discretionary managed accounts service. Changing to a different service can be appropriate for an advice recipient whose circumstances have changed over time: perhaps he or she is now closer to retirement and wishes to have additional help, or no longer has the time to manage investments themselves. ERISA has long been understood to permit service providers to act as a fiduciary for some, but not all of the services provided, and we believe that the Department should continue to recognize this important distinction.<sup>10</sup>

**B. Proposal: Clarify that only recommendations of “another” constitute investment advice and that “recommendation” excludes an entity’s presentation of its own services**

As stated in the proposing release, “the proposal is intended to ensure that small plan fiduciaries, plan participants, beneficiaries and IRA owners would be able to obtain essential information regarding important decisions they make regarding their investments without the providers of that information crossing the line into fiduciary status.”<sup>11</sup> We believe that the Department’s intent with paragraph (iv) is to ensure fiduciary protections for retirement plans and retirement investors where advice regarding the selection of an investment advisor is being made by a third party that will receive compensation for such recommendation. Given the Department’s comment that call center employees, “and possibly their employers”<sup>12</sup> should be treated as fiduciaries unless they meet the conditions of one of the carve-outs, it would be useful to use language permitting an employee to present or explain the available services, as the agent of his or her employer. Thus, paragraph (iv) could be amended to clarify that the “person” referred to in paragraph (iv) is a person other than the one referred to in the first instance in 2510.3-21(a):

“(iv) A recommendation of a third party, other than such person’s employer, who is also going to receive a fee or other compensation ~~for providing~~ if any of the types of advice described in paragraphs (i) through (iii) are provided; and”

Further clarity would be achieved by also including within the definition of “recommendation” a specific exclusion for a “presentation of services” by the provider of such potential services. As the Department recognized, it can be faithful to the overall purpose of ERISA to exclude specific types of communications that would not be treated as investment advice, where the activities do not “implicate relationships of trust and expectations of impartiality,” rather than adding additional elements that must be met in all instances. Retirement investors would still have the

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<sup>10</sup> The Department has long recognized that a person may act as a fiduciary with respect to a plan and still offer to perform additional services to the plan in a non-fiduciary capacity. See 29 CFR 2550.408b-2(f), *Examples 1 and 2*.

<sup>11</sup> 80 Fed. Reg. 21928, 29142 (April 20, 2015).

<sup>12</sup> 80 Fed. Reg. 21946 (April 20, 2015).

benefit of the intended fiduciary protections around specific recommendations to take, or not take, specific actions:

“(1) “Recommendation” means a communication, other than a Service Offering, that, based on its content, context, and presentation, would reasonably be viewed objectively as a suggestion that the advice recipient engage in or refrain from taking a particular course of action. “Service Offering” means those written and/or oral communications between an advice recipient and a provider of services, which is intended to convey information that the advice recipient in the ordinary course would deem relevant in the evaluation of such service(s), including without limitation scope of services, proposed fees, termination rights, fiduciary status of service provider if selected, and other attributes of the services that enable informed decision making by an advice recipient.”

**III. The proposed rule may create confusion over what content will be deemed to constitute representing or acknowledging that a person is a fiduciary within the meaning of the Act.**

- A. Concern: Certain comments in the proposing release imply that use of certain phrases by an adviser when communicating with retirement investors about the advisory services it makes available, could immediately trigger fiduciary status and potentially result in a prohibited transaction if the adviser receives fees for its advisory services, even when those fees are reasonable, fully disclosed, and free of potential conflicts of interest.**

Similar to our comments under Part II above, advisers who fully intend to become fiduciaries and to manage investments as a fiduciary may trigger such status prematurely if Section (2)(i) is interpreted broadly, to encompass not just the adviser’s actual use of the word “fiduciary”, but also the adviser’s use of words such as “personalized,” or indications that the adviser will act in the individual’s “best interests.” We are basing this interpretation on the proposing release, which notes that: “Thus, at the same time that marketing materials may characterize the financial adviser’s relationship with the customer as one-on-one, personalized, and based on the client’s best interest, footnotes and legal boilerplate disclaim the requisite mutual agreement, arrangement, or understanding that the advice is individualized or should serve as a primary basis for investment decisions.”<sup>13</sup> Further, the use of the word “indirect” implies that the provision could be construed broadly. We believe that the Department intends that such phrases and positioning should not be used where the adviser simultaneously, or later, disclaims fiduciary responsibility, but that the intent is not to prevent an adviser from describing the relationship that will result once the adviser begins to provide investment management services.

- B. Proposal: Clarify that advisers that intend to offer fiduciary advisory services will not become fiduciaries prematurely merely by virtue of using phrases that attempt to convey the meaning of fiduciary duty and responsibility.**

Paragraph (2) can be amended to remove the reference to “indirectly”:

“(2) Such person, either directly or ~~indirectly~~ (e.g., through or together with any affiliate),

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(i) Represents or acknowledges that it is acting as a fiduciary within the meaning of the Act with respect to the advice described in paragraph (a)(1) of this section; or”

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<sup>13</sup> 80 Fed. Reg. 21951 (April 20, 2015).

Further clarity is achieved with the same suggestion made above:

“(1) “Recommendation” means a communication, other than a Service Offering, that, based on its content, context, and presentation, would reasonably be viewed objectively as a suggestion that the advice recipient engage in or refrain from taking a particular course of action. “Service Offering” means those written and/or oral communications between an advice recipient and a provider of services; intended to convey information that the advice recipient in the ordinary course would deem relevant in the evaluation of such service(s), including without limitation scope of services, proposed fees, termination rights, fiduciary status of service provider if selected, and other attributes of the services that enable informed decision making by an advice recipient.”

#### IV. Additional Comments

- A. **The Department has requested comment on whether it is appropriate to omit the provisions of IB 96-1 relating to specific investment products and alternatives available under the plan. We believe that the educational carve-out is appropriate and will help retirement investors get needed information and assistance, without including specific investment products and alternatives in the carve-out.**

We agree with the Department’s definition of educational materials. It is especially important, and appreciated, that the Department specified that educational material may continue to be provided without triggering fiduciary status irrespective of whether such educational materials are provided by the plan sponsor or by service providers. In addition, it is especially useful that the Department specified that materials could be provided in any form including individually or on a group basis, in writing or orally, or via call center, video or computer software. We believe it is appropriate that the Department excluded asset allocation models that identify specific investment products available under the plan or IRA from the description of educational materials. However, there may be circumstances in which the identification of specific investment products does not create a conflict of interest. We suggest that the language be modified to allow presentation of specific investment products, if either one of two additional criteria are met<sup>14</sup>, perhaps with appropriate caveat language to make it clear that the examples may not be the only choice for a particular investor: (1) all of the investment products or alternatives available under the plan or IRA applicable to a specific asset class are presented, or (2) only investment products or alternatives with respect to which the education provider has no conflicts from differential compensation arrangements are shown.

“(iii) Asset allocation models ...

(C) Such models do not include or identify any specific investment product or specific alternative available under the plan or IRA, unless including or identifying all of the investment products or specific alternatives available under the plan or IRA for an identified asset class, or including or identifying only one or more investment products or specific alternatives available under the plan or IRA for an identified asset class with respect to which such person and its affiliates will not receive any differential compensation; and

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<sup>14</sup> While cost is an important factor in the selection of investments, we would not recommend allowing identification of specific products or investment alternatives based on cost alone. A provider acting as a fiduciary could make a fiduciary determination as to which products or investment alternatives to identify based on consideration of all of the product’s attributes, but cost alone might not be a sufficient indicator of quality and potential benefit.

(D) The asset allocation models are accompanied by a statement indicating that, in applying particular asset allocation models to their individual situations, participants, beneficiaries, or IRA owners should consider their other assets, income, and investments (e.g., equity in a home, Social Security benefits, individual retirement plan investments, savings accounts and interests in other qualified and non-qualified plans) in addition to their interests in the plan or IRA, to the extent those items are not taken into account in the model or estimate, and if some, but not all, specific investment products or specific alternatives available under the plan or IRA are identified pursuant to clause (C), that other products or alternatives with similar risk and return characteristics may be available and identifying where information about those alternatives can be obtained.”

We suggest a few additions to the language in (i) “Plan information” and (ii) “General financial, investment and retirement information” to convey additional types of information that would not constitute investment advice under the proposed regulation.

“(i) Plan information. Information and materials that, without reference to the appropriateness of any individual investment alternative or any individual benefit distribution option of the plan or IRA, or a particular participant or beneficiary or IRA owner, describe the terms of operation of the plan or IRA, inform a plan fiduciary, participant, beneficiary, or IRA owner about the benefits of plan or IRA participation, the benefits of increasing plan or IRA contributions, the impact of preretirement withdrawals on retirement income, retirement income needs, varying forms of distributions available from the plan or IRA, including rollovers, annuitization and other forms of lifetime income payment options (e.g., immediate annuity, deferred annuity, or incremental purchase of deferred annuity or other strategy for systemic withdrawals), advantages, disadvantages and risks of different forms of distributions (such as required minimum distributions and relative costs of investments associated with the different forms of distributions) or describe investment objectives and philosophies, risk and return characteristics, historical return information or related prospectuses of investment alternatives under the plan or IRA.

(ii) General financial, investment and retirement information. ....

(H) General methods and strategies for managing assets in retirement (e.g., systematic withdrawal payments, annuitization, guaranteed minimum withdrawal benefits), including those offered outside the plan or IRA and including the impact of other retirement benefits such as Social Security or defined benefit payments.”

Educational materials and models are by their nature often designed for general information, without offering individualized information. Clearly, educational materials or a model would be less helpful to retirement investors without information about the underlying assumptions, such as whether inflation is taken into account, or whether estimates of future income streams assume continued contributions to the plan or IRA. However, it would be helpful if the Department could provide additional clarity on how advisers should assess what is “material” in the context of facts and assumptions relating to educational materials, as it could be difficult for service providers to know if sufficient information had been provided. We also believe it would be useful to clarify that service providers can use alternate means of providing access to these material facts and assumptions. We are hopeful that the Department is intending that the material facts and assumptions cover information that is material to the intended recipients overall, rather than assessing and describing every circumstance in which an individual’s outcome might vary. Individuals who require advice tailored to and taking into consideration their own personal

circumstances can seek a relationship with an advice provider. Although we agree with the Department's assumption that much disclosure will be distributed electronically, this is not always the case, and postage and materials costs from inserting the disclosure can be significant. In addition, some of these electronic channels do not support extensive disclosure (e.g., a brief educational "teaser" on a webpage), but can easily refer to a website or other means by which the retirement investors can gain additional information. We would suggest conforming the provisions relating to asset allocation models and interactive investment materials. The language in the latter is useful to convey that the required disclosure should be viewed from the perspective of facts and assumptions that are likely to affect a participant's perspective, as opposed to all of the underpinnings of the model or interactive materials. For example, it should not be necessary to include macroeconomic or capital market assumptions, such as the estimated volatilities for various assets or asset classes used in the model or materials. We would suggest the following revisions:

"(iii) Asset allocation models. Information and materials (e.g., pie charts, graphs, or case studies) that provide a plan fiduciary, participant or beneficiary, or IRA owner with models of asset allocation portfolios of hypothetical individuals with different time horizons (which may extend beyond an individual's retirement date) and risk profiles, where --

...

(B) ~~All~~ The material facts and assumptions on which such models are based (e.g., retirement ages, life expectancies, income levels, financial resources, replacement income ratios, inflation rates, rates of return, expected future contributions) that typically affect a participant's, beneficiary's or IRA owner's assessment of such model are provided, or are specified by the participant, beneficiary or IRA owner;

...

(iv) Interactive investment materials. Questionnaires, worksheets, software, and similar materials which provide a plan fiduciary, participant or beneficiary, or IRA owners the means to estimate future retirement income needs and assess the impact of different asset allocations on retirement income; questionnaires, worksheets, software and similar materials which allow a plan fiduciary, participant or beneficiary, or IRA owners to evaluate distribution options, products or vehicles by providing information under paragraphs (b)(6)(i) and (ii) of this section; questionnaires, worksheets, software, and similar materials that provide a plan fiduciary, participant or beneficiary, or IRA owner the means to estimate a retirement income stream that could be generated by an actual or hypothetical account balance, where --

...

(D) ~~All~~ The material facts and assumptions (e.g., retirement ages, life expectancies, income levels, financial resources, replacement income ratios, inflation rates, rates of return, expected future contributions and other features and rates specific to income annuities or systematic withdrawal plan) that ~~may~~ typically affect a participant's, beneficiary's or IRA owner's assessment of the different asset allocations or different income streams ~~accompany the materials are provided,~~ or are specified by the participant, beneficiary or IRA owner;"

#### **V. Department Requests for Comment**

The Department has requested comment on whether it should adopt some or all of the standards developed by FINRA in defining communications that rise to the level of a recommendation for purposes of distinguishing between investment education and investment advice under ERISA, including comment on the discussion in FINRA's "Frequently Asked Questions, FINRA Rule 2111 (Suitability)" of the term "recommendation" in the context of asset allocation models and general investment strategies.

As shown in our suggested revisions above, we believe it would be useful to clarify that the determination of whether a suggestion is fiduciary advice should be made objectively rather than subjectively, consistent with FINRA Regulatory Notice 11-02. However, we suggest it could be source of confusion if the Department were to adopt FINRA standards, or to imply that they are incorporated by reference into the proposed regulation, since many of the advisers subject to the proposed regulation are not regulated by FINRA. It may be difficult for such advisers to anticipate and interpret any future changes to FINRA's standards.

#### **Conclusion**

Financial Engines supports the Department's actions in seeking to better protect retirement investors and beneficiaries. We appreciate the opportunity to comment on the proposed regulation and welcome the opportunity to work with the Department and to provide any further assistance that may be required. Please contact us should you have any questions.

Very truly yours,

A handwritten signature in black ink, appearing to read "Chris Jones", with a long horizontal flourish extending to the right.

Christopher Jones  
Executive Vice President of Investment Management and Chief Investment Officer