

# American Federation of Labor and Congress of Industrial Organizations



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March 6, 2009

Sent by E-Mail to [e-ORI@dol.gov](mailto:e-ORI@dol.gov)

Office of Regulations and Interpretations  
Employee Benefits Security Administration  
Attn: Investment Advice Final Rule  
Room N-5655  
U.S. Department of Labor  
200 Constitution Avenue, NW  
Washington DC 20210

Re: Investment Advice Provided to Participants in  
Self-Directed Individual Account Plans—Final Rule  
Docket ID EBSA-2008-0011 (RIN 1210-AB13)

Ladies and Gentlemen:

On behalf of the more than 10 million working men and women of the AFL-CIO, we offer our comments on the final rule implementing the statutory exemption on investment advice under Sections 408(b)(14) and 408(g) of the Employee Retirement Income Security Act of 1974, as amended (ERISA)<sup>1</sup> and the related class exemption embedded in the final regulation.<sup>2</sup>

In the notice published on February 4, 2009 (74 Fed. Reg. 6007), the Department proposed to extend the effective date of the final investment advice rule from March 23, 2009 to May 22, 2009 and requested "... comments on issues of law and policy concerning all the provisions of these rules ..." to assist in its review.

<sup>1</sup> The statutory exemption was added by Section 601 of the Pension Protection Act of 2006, Public Law 109-280, 120 Stat. 780 (Aug. 17, 2006).

<sup>2</sup> The final rule was published in the Federal Register on January 21, 2009 (74 Fed. Reg. 3822).

We believe it is appropriate for the Department to review the final regulation and embedded class exemption to avoid eliminating even the modest protections included in Sections 408(b)(14) and 408(g) of ERISA and expanding the provision of investment advice by financial institutions with conflicts of interest.

The importance of strong, meaningful regulatory safeguards to avoid conflicts of interest is of the utmost importance at this time as participants grapple with significant declines in the value of their retirement savings. As a result of the collapse in our financial markets last year, there have been enormous losses in participant account balances in Section 401(k) and other individual account plans, as well as IRAs. Defined contribution plans of all types lost \$2 trillion between October 2007 and October 2008 and the market value of assets in Section 401(k) plans and IRAs fell by 30 percent, according to the Center for Retirement Research at Boston College.<sup>3</sup> At this point, the wrong advice could permanently damage retirement savings if the decline in the value of equity investments were realized. Participants could also be harmed even more by self-interested investment advice as financial service providers face pressure to attract business and assets for investment.

For the reasons we explain below, the Department should withdraw the final rule, including the class exemption, with this action taken at the earliest date that satisfies the Administrative Procedure Act, 5 U.S.C. § 551 *et seq.* In our view, the final rule, particularly the terms of the class exemption, undermine the modest protections included in Section 408(g) of ERISA.<sup>4</sup> Any amendments the Department may propose should not include a class exemption expanding the scope of the statutory exemption.

### Fiduciary Adviser Compensation

The final regulation and the class exemption undermine the statutory fee-leveling exemption in ERISA Section 408(g)(2)(A)(i) in two different ways. The final regulation excludes affiliates of the fiduciary adviser from the fee-leveling requirement while the class exemption limits it to the particular employee, agent or registered representative providing the investment advice.<sup>5</sup> These provisions, both restricting the scope of the statutory exemption, raise significant questions of law and policy, particularly because it is apparent from the administrative

<sup>3</sup> Alicia Munnell, Francesca Golub-Sass, and Dan Muldoon, *An Update on 401(k) Plans: Insights from the 2007 SCF*, Center for Retirement Research at Boston College, Brief Number 9-5 (March 2009) available at [http://crr.bc.edu/images/stories/Briefs/ib\\_9\\_5.pdf](http://crr.bc.edu/images/stories/Briefs/ib_9_5.pdf).

<sup>4</sup> We also note that the Department has not provided any explanation for merging the class exemption with the final regulation, something never done before now.

<sup>5</sup> Section 2550.408g-1(b)(3)(i)(D) requires that the fees and compensation paid to employees, agents and registered representatives of the fiduciary adviser not vary based on the investment options selected. Section 2550.408g-1(b)(3)(i)(E) applies the same restriction to the fees, commissions and other compensation due the fiduciary adviser. Section 2550.408g-1(d)(4) explicitly excludes the fiduciary adviser from the restriction.

record that Congress does not agree with the approach taken in the final regulation and class exemption.<sup>6</sup>

In their comments on the proposed investment advice regulation and class exemption, members of the Senate and the House of Representatives reviewed the development of the statutory investment advice exemption, emphasizing that it was narrowly drawn and the result of a bipartisan compromise.<sup>7</sup> Each set of comments expressed concern about excluding affiliates from the reach of the fee-leveling exemption and the Senators disagreed with the exclusion of the fiduciary adviser in the proposed class exemption. Each set of comments was clear that these provisions of the proposed regulation and class exemption, as well as the modification of the statutory computer model exemption, were contrary to the statutory language and the intent of Congress.

The interpretation of the statute advanced by the Department excluding “affiliates” from the fee-leveling exemption, however, ignores the statutory definition of a fiduciary adviser set forth in Section 408(g)(11)(A) of ERISA. That section explicitly includes “an affiliate” of any of the persons and entities that can serve as a fiduciary adviser.<sup>8</sup> By restricting the scope of the statutory exemption, the final regulation leaves the incentive to recommend investment options that provide greater benefit to an affiliate of the fiduciary adviser—one source of the conflicts of interest the statutory exemption sought to limit—in place.

The restriction of the level fee requirement in the class exemption also disregards the explicit terms of the statute. While the Department has the authority under Section 408 of ERISA to issue prohibited transaction exemptions, its authority cannot include the ability to effectively amend ERISA by disregarding its terms.

In its review of the final rule, including the class exemption, the interpretation of the statutory fee-leveling exemption should be reconsidered, giving due regard to the comments submitted by Congress and the Department’s longstanding concerns about exposing participants to investment advisers with conflicts of interest. Exempting affiliates from the fee-leveling provision undermines the statutory protections. Exempting the fiduciary adviser itself from this same provision, as the class exemption does, creates an exception that could swallow the rule.

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<sup>6</sup> The AFL-CIO, as well as others, raised similar objections to the treatment of the fee-leveling exemption in both the proposed regulation and proposed class exemption.

<sup>7</sup> See Comments from Senators Bingaman, Kennedy and Grassley and comments from Representatives Miller and Andrews, available at <http://www.dol.gov/ebsa/regs/cmt-investment-advice.html>.

<sup>8</sup> Section 408(g)(11)(A) (i) through (iv) describe four different individuals or entities that may qualify as fiduciary advisers, including registered investment advisers, banks and registered brokers and dealers. Section 408(g)(11)(A)(v), in turn, provides that “an affiliate of a person described in ... (i) through (iv) ...” is included as a “fiduciary adviser.” The final paragraph of Section 408(g)(11)(A) covers employees, agents and registered representatives of the other five defined categories.

These expansions of the statutory exemption are contrary to the policy goal of making good investment advice available to participants who want it.

### Expansion of the Computer Model Exemption

In addition to restricting the scope of the statutory fee-leveling exemption, the final class exemption creates an alternative for the computer model exemption not sanctioned by Section 408(g)(3) of ERISA.

The final exemption permits individualized advice to be given after computer model recommendations are generated with virtually no restrictions to avoid potential conflicts of interest. The computer model recommendations are relegated to providing "... a context for assessing and evaluating the individualized investment advice ...." 74 Fed. Reg. at 3834.

The Department viewed the relaxed requirements in the class exemption for the computer model exemption, as well as the restriction on fee-leveling discussed earlier, as "... necessary to provide more comprehensive relief for fiduciary investment advice and to address certain aspects of the statutory exemption that were unclear or that did not extend relief to certain arrangements." 74 Fed. Reg. 3833. In addition, the Department took "... into account the intent of the Congress and the administration to dramatically expand the availability of affordable, quality investment advice for millions of America's workers ...." 74 Fed. Reg. 3834.

Congress determined the scope of the investment advice exemption, and once that policy decision was enacted, we do not believe it appropriate for the Department to expand the relief. While the statutory exemption did expand the availability of investment advice, Congress chose to do so in specific ways and that action should not be treated lightly. In light of the national financial crisis, now is not the time to propose an exemption that goes well beyond the statutory compromise reached just two years ago in the Pension Protection Act.<sup>9</sup>

### Disclosure to Participants

The Appendix to the final rule includes a model notice to use in order to comply with the disclosure requirements in Sections 2550.408g-1(b)(7) and (d)(8). The required notice "... must be written in a clear and conspicuous manner and in a manner calculated to be understood by the average plan participant ...." Sections 2550.408g-1(b)(7)(ii)(A) and (d)(8)(ii)(A).

The final model notice, like the proposed notice, fails to meet the regulatory standard and should be rewritten. Revisions to the notice should be informed by the results of any focus group review of the model notice, a suggestion made by the Pension Rights Center that we support.<sup>10</sup>

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<sup>9</sup> For other reasons, the Department itself considered, but rejected, deferring the issuance of the class exemption. 73 Fed. Reg. at 49911-49912.

<sup>10</sup> See p. 3 of the Pension Rights Center's Comments on Proposed Regulations and Class Exemption on Investment Advice, dated October 6, 2008 available at <http://www.dol.gov/ebsa/regs/cmt-investment-advice.html>.

At a minimum, as we noted in our comments on the proposed regulation, the notification that a participant can arrange for advice from an independent adviser should be clearly and separately stated, not buried in the middle of the notice.

We also suggest that any revised regulation and accompanying model notice include information about the profitability of the various investment options under the plan. As we noted in our previous comments, providing this information will give participants some ability to protect themselves from the possibility of being steered into higher margin products.<sup>11</sup>

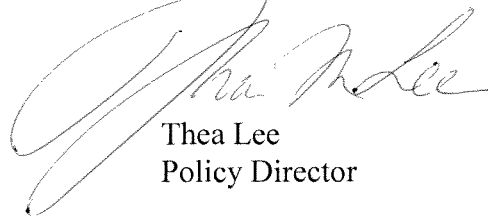
### Audit

The audits required by the regulation and class exemption do not adequately protect participants from the results of conflicted investment advice, particularly because any audit will be performed after action on the investment advice is taken. In addition, no minimum criteria for either the scope of the audit or the qualifications of the auditor were included.<sup>12</sup> Nor is there any requirement that participants be informed of the audit results, including the potential affect of the failure of an investment advice arrangement to meet the requirements of the exemption.

Any modifications to the final regulation should address these matters to assure that the audit provides the intended protection to participants.

We hope our comments are helpful to the Department during its review of the final rule on the provision of investment advice. Should there be any questions about them or if we can provide any additional information, please do not hesitate to contact me at (202) 637-3907.

Sincerely,

A handwritten signature in cursive script, appearing to read 'Thea Lee', is written over a light blue horizontal line.

Thea Lee  
Policy Director

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<sup>11</sup> The Department acknowledged our comments in the preamble to the final rule, although it did "... not believe it would be appropriate, as part of this final rule, without further notice and comment, to include such a disclosure obligation." 74 Fed. Reg. at 3832. That concern would be addressed by incorporating our suggestion in any proposed amendments to the final rule.