Congress of the United States
Washington, DC 20510

February 3, 2011

Assistant Secretary Phyllis Borzi
Employee Benefits Security Administration
U.S. Department of Labor
200 Constitution Avenue, NW
Washington, DC 20210

Re: <u>Definition of the Term Fiduciary (RIN 1210-AB32)</u>

Dear Assistant Secretary Borzi:

We write regarding the regulation proposed by the Department of Labor (the "Department") defining "fiduciary" (75 Fed. Reg. 65263 (Oct. 22, 2010), the "Proposed Regulation") under the Employee Retirement Income Security Act of 1974 ("ERISA"). We offer the following comments on the Proposed Rule:

- We strongly support the Department's decision to re-examine the types of advisory relationships that give rise to fiduciary status;

- Fiduciary status for advisers should not be conditioned on the advice (i) being provided on a "regular basis" or (ii) serving as the "primary basis" for investment decisions;

- Any limitations on fiduciary status should be narrowly tailored to address specific situations, and parties relying on the limitations should be required to fully disclose that information being provided is not fiduciary investment advice;

- "Investment advice" should be construed broadly to include recommendations regarding plan distributions, the management of securities, investment manager selection, and asset allocation.

We discuss these comments in more detail below, but as a preliminary matter, we commend the Department for scheduling a public hearing on the Proposed Regulation. 76 Fed. Reg. 2142 (Jan. 12, 2011). The retirement system is complex, and the changes proposed by the Department will undoubtedly have a significant impact on the relationship between those who make investment decisions on behalf of plans ("plan officials"), participants, and service providers. The Department's active approach to exploring the effects of the Proposed Rule and its efforts to work with stakeholders are commendable. We are encouraged by the process and hopeful that, at the end of the day, the final rule will provide significantly increased protections while, at the same time, being both practical and administrable.

I. Background

Congress passed ERISA to ensure that employers make good on the promises they make to employees. Central to that purpose are the fiduciary duties in Title I of ERISA. Those duties – which are "the highest known to the law" – compel parties who "render investment advice for a fee" to do so prudently, in the best interest of participants and beneficiaries, and free from certain conflicts and self-dealing. ERISA §§ 3(21)(A)(ii), 404, 406; *Donovan v. Bierwirth*, 680 F.2d 263, 272 n. 8 (2d Cir. 1982).

In 1975, the Department issued a regulation (the "'75 Regulation") to clarify who is a fiduciary under ERISA by virtue of providing investment advice. 29 C.F.R. § 2410.3-21. The '75 Regulation took what is a two-part test under ERISA and added additional conditions. In particular, the '75 Regulation provides that an adviser will be a fiduciary if the advice is –

- rendered on a "regular basis";
- rendered for a fee, direct or indirect;
- provided pursuant to a mutual agreement, arrangement, or understanding;
- individualized to the plan's particular needs; and
- a "primary basis" for the investment decision.

29 C.F.R. § 2510.3-21(c). Courts have generally required that each of the criteria in the '75 Regulation be satisfied in order to confer fiduciary status. Therefore, the '75 Regulation materially limits the scope of ERISA's fiduciary protections and, in many cases, has resulted in plan advisers not being held to the standards Congress originally intended.

The Proposed Regulation would replace substantial portions of the '75 Regulation and, among other things, eliminate the requirements that advice be provided on a "regular basis" and serve as the "primary basis" for investment decisions. It would also clarify that a person will not be an investment advice fiduciary merely because he or she sells a product to a plan or provides marketing materials, investor education, or general financial data. The Department believes that changes in the Proposed Regulation will "better ensure that persons… [p]roviding investment advice to plan fiduciaries and/or plan participants and beneficiaries are subject to ERISA's standards of fiduciary conduct." 75 Fed. Reg. 65275.

II. Comments on the Proposed Rule

We offer the following comments on the Proposed Rule:

A. We strongly support the Department's decision to re-examine the types of advisory relationships that give rise to fiduciary status.

Since the Department issued the '75 Regulation, the private retirement system has undergone a number of changes that have profoundly reshaped the relationship between plan officials, service providers, and participants. The most obvious change has been the shift from defined benefit pension plans to defined contribution plans, but there also has been a veritable explosion in the number and complexity of the financial products and services on the market. Now more than ever, plan officials and participants rely on consultants and other service providers for advice and recommendations regarding investment decisions. However, there is widespread confusion over what constitutes "investment advice" under ERISA and when a service provider is acting as a fiduciary.

In our judgment, it is entirely reasonable for the Department to take whatever steps are necessary to address changes in the retirement system and ensure that the people providing investment advice are subject to ERISA's rigorous fiduciary standards. Therefore, we strongly support the Department's efforts to update and strengthen the regulation clarifying who is an investment advice fiduciary under ERISA.

B. We support the elimination of the "regular basis" and "primary basis" conditions from the test to determine an adviser's fiduciary status.

The five-part test applied under the '75 Regulation is overly narrow and yields results that are contrary to Congressional intent. The language of ERISA section 3(21) is clear on its face. A person is a fiduciary if he or she provides investment advice and receives a fee. Congress did not condition fiduciary status on the frequency with which the person provides advice or on whether the advice is a primary factor contributing to an investment decision.

Therefore, we support the Department's proposed elimination of the "regular basis" requirement. As noted by the Department, "the significance of the advice on a plan fiduciary's decisions [does not diminish] merely because it is rendered only once." 75 Fed. Reg. 65267. Plan fiduciaries often hire consultants for advice on one-time investments, particularly for transactions that could have enormous consequences for plans. In such cases (*i.e.*, cases where an adviser is retained specifically to provide advice with respect to a transaction), we think that ERISA, by its plain language, makes the adviser a fiduciary.

We also support the Department's proposed elimination of the "primary basis" requirement. In our judgment, "when a service provider is retained to render advice, the plan should generally be able to rely on the advice without regard to whether the parties intend it be a primary or lesser basis in the fiduciary's decision-making." 75 Fed. Reg. 65267. In practice, the "primary basis" requirement can mean that an adviser specifically retained to provide advice to a plan owes no fiduciary duty if a plan official will also consult or consider other sources regarding the investment decision.

In place of the "regular basis" and "primary basis" conditions, we urge the Department to take steps to clarify what actions are fiduciary in nature. The Department should include as part of the final rule specific hypothetical examples of fiduciary advice and non-fiduciary conduct.

We recognize and accept that expansion of fiduciary liability will require certain plan service providers to modify their business practices.[1] For the first time, many will have a direct obligation to disclose their direct and indirect fees. They also will have to avoid conflicts of interest and refrain from engaging in self-dealing. However, that is what Congress intended, and the costs associated with the expansion of the scope of fiduciary liability will be more than offset by the protections afforded to plans and participants that will be achieved by bringing more service providers within ERISA's regulatory regime.

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[1] Many service providers have extensive affiliations with other entities, so an expansion of fiduciary status could result in certain beneficial practices being prohibited under ERISA section 406. Therefore, we encourage the Department to work with the plan community to determine whether there are particular circumstances in which it is appropriate to grant additional or modified exemptive relief to select individuals or classes.

C. Any limitations on fiduciary status should be narrowly tailored to address specific situations, and parties relying on the limitations should be required to fully disclose that information being provided is not fiduciary investment advice.

The Proposed Regulation broadens the definition of fiduciary and creates several limitations for specific activities that are generally not considered fiduciary in nature. Specifically, the Proposed Regulation states that a person will not be considered an investment advice fiduciary if he or she provides (i) recommendations or advice as a seller, (ii) investment education, (iii) non-individualized marketing materials, or (iv) general financial information and data.

We believe that the Department should ensure that the language of the limitations is carefully tailored to address specific, limited situations. The limitations should not create an exception that allows those actually providing investment advice to escape fiduciary liability.

Further, we are concerned that plan officials and participants may not always have a clear understanding of when a service provider is offering fiduciary investment advice. When an adviser provides recommendations as a seller, the recommendations generally should carry less weight with decision-makers than recommendations coming from a fiduciary. Ambiguity regarding the status of the adviser providing the recommendations may lead people to overly rely on sales materials when making investment decisions.

Therefore, we believe that the rule should require service providers to make clear, upfront disclosures regarding their fiduciary status and the nature of the information being provided. In this regard, we support the Department's decision to require service providers relying on the limitations to "demonstrate that the recipient of the advice knows... [t]hat the [service provider] is providing the advice or making the recommendation in its capacity as a... [seller]" whose interests are not necessarily aligned with the interests of the plan or its participants. Prop. Reg. § 2510.3-21(c)(2). Merely disclosing that the recommendations are not impartial may not be sufficient to alert participants and plan officials to the existence of material conflicts. The rule also should be clear that plan officials are fully subject to the fiduciary rules on prudent selection and monitoring of non-fiduciary investment related services.

Additionally, we ask the Department to consider whether to require additional disclosure where service providers are dealing directly with participants and beneficiaries. For example, it may be appropriate to require the disclosure of material conflicts affecting any recommendations or "market color" being provided to participants. Similarly, participants do not select service providers and do not always have a clear understanding of the service providers' legal responsibilities. Therefore, plan officials may need to provide more information about the particular service providers' responsibilities.

D. "Investment advice" should be construed broadly to include recommendations regarding plan distributions, the management of securities, investment manager selection, and asset allocation.

The Department should broadly construe what constitutes "investment advice" under ERISA. Plan fiduciaries may retain advisers to provide recommendations regarding the management of securities or other property (*e.g.*, proxy voting), the selection of investment managers, and portfolio asset allocation. Fiduciaries rely on such advisers to maximize the value of their investments, and we see no reason that the advisers should not be held to the same standard as persons recommending the purchase or sale of a specific security.

Additionally, we strongly encourage the Department to include in the final rule a provision stating that recommendations regarding plan distributions constitute investment advice. In our judgment, distribution recommendations are inherently advice concerning plan investments because, when a participant takes a distribution, the participant generally liquidates a portion of his or her investments.[2] Therefore, those providing advice with respect to plan distributions should be fiduciaries subject to ERISA's more rigorous protections.[3]

This is particularly important in light of the growing 401(k) roll-over market. We are aware of many cases in which non-fiduciary plan service providers (*e.g.*, recordkeepers) use their access to plan participants to sell roll-over products, and in some cases, participants end up rolling over their account into share classes that carry higher management and/or administrative fees.

Finally, we believe that educating participants about their distribution options is critically important and that the provision of such educational information may not be a fiduciary function. Therefore, we ask that the Department consider whether it is appropriate to issue guidance to help plan sponsors distinguish fair and balanced education with respect to distribution options from fiduciary investment advice.

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The retirement security of working Americans, retirees, and their families will benefit greatly from your efforts. We appreciate all of your work and look forward to continuing to work with you to improve the fiduciary protections for workers and their families.

Sincerely,

Tom Harkin

TOM HARKIN
Chairman
Senate Committee on Health, Education Labor, and Pensions

George Miller

GEORGE MILLER
Ranking Member
House Committee on Education and Workforce

Herb Kohl

HERB KOHL
Chairman
Senate Special Committee on Aging

SANDER M. LEVIN
Ranking Member
House Committee on Ways and Means

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[2] We soundly reject the conclusion in Advisory Opinion 2005-23A (December 7, 2005) that a recommendation to take a permissible distribution is not investment advice under ERISA.

[3] We note that it should not matter whether there are other laws applying to distribution recommendations because ERISA does not condition fiduciary status on the existence (or inexistence) of overlapping legal regimes.