

May 5, 2010

*Sent via Electronic Mail*

Office of Regulations and Interpretations  
Employee Benefits Security Administration  
Room N-5669  
U.S. Department of Labor  
200 Constitution Avenue, N.W.  
Washington, DC 20210

Re: 2010 Investment Advice Proposed Rule

To Whom It May Concern:

The Financial Planning Association<sup>1</sup> ("FPA®") is pleased to submit comments regarding the rules governing the delivery of personalized investment advice to plan participants under Section 601 of the Pension Protection Act of 2006 (the "PPA") and similar provisions governing individual retirement accounts ("IRAs").

Retirement planning is a core area of practice for financial planners. In addition to providing advice on a broad array of personal finance issues, many offer investment advice to plan participants, their beneficiaries and IRA account holders regarding the assets held in the 401(k) accounts and IRAs. Some financial planners may also serve as investment managers who advise plan sponsors on the selection of investment options to be offered under 401(k) plans. Most are subject to broad fiduciary duties as affiliates of registered investment advisers, and FPA members are also subject to a fiduciary duty for their financial planning activities under ethical rules incorporated by FPA in its bylaws<sup>2</sup>.

FPA supports the goals of the PPA to expand the pool of advisers eligible to help participants and beneficiaries owning assets in qualified plans and IRAs make wise investment decisions. We agree with the Department of Labor's (the "Department")

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<sup>1</sup> The Financial Planning Association is the largest organization in the United States representing financial planners and affiliated firms, with approximately 24,000 individual members. FPA members directly manage more than \$1.5 trillion in assets with a combined client base of 2.75 million individuals. Approximately 50 percent of FPA members are affiliated with SEC-registered investment adviser firms and 22 percent with firms registered on the state level. Half of its individual members are also affiliated with broker-dealers. FPA is incorporated in Washington, D.C., where it maintains an advocacy office, with headquarters in Denver, Colorado.

<sup>2</sup> See FPA Standard of Care, at <http://www.fpanet.org/AboutFPA/Organization/CoreBeliefs/>.

view that participants and beneficiaries often make costly investment errors which could be avoided if they receive quality investment advice.

FPA offers comments on the following issues:

- withdrawal of the individual class exemption;
- continuation of pre-existing guidance issued by the Department that applies to the provision of investment advice;
- the Department's request for comments on what constitutes generally accepted investment theories and appropriate and objective criteria to serve as basis for asset allocation;
- qualifications and scope of responsibilities of independent auditor;
- the Department's addition of a new requirement on factors that must be avoided in computer model-driven advice; and
- the Department's prohibition on a fiduciary adviser's receipt of any fee or other compensation that is based on a participant's or beneficiary's selection of investment options.

### **WITHDRAWAL OF THE INDIVIDUAL CLASS EXEMPTION**

The class exemption allowed varying fees to be provided to the fiduciary advisers' employer (not just affiliates of the fiduciary adviser) for individualized off-model advice. FPA has concerns that participants and beneficiaries could receive conflicted investment advice, regardless of what disclosures may be made. FPA feels the withdrawal of the class exemption is appropriate since the PPA statutory exemption does not provide prohibited transaction relief for individualized advice following the furnishing of investment recommendations generated by a computer model. While FPA understands that there will be situations whereby participants or beneficiaries may request advice outside of that provided by the computer, such advice would not be precluded so long as the advice is rendered under a fee-leveling arrangement.

### **EXISTING GUIDANCE ISSUED BY THE DOL OUTSIDE OF THE EXEMPTION WOULD STILL APPLY TO THE PROVISION OF INVESTMENT ADVICE**

FPA is pleased that the proposed regulations continue to expressly provide that neither the PPA nor the regulations invalidates or otherwise affects prior regulations, exemptions, interpretative or other guidance issued by the Department. Many of our members are currently providing participant education and advice under the current rules and will continue to do so. The PPA exemption was enacted to provide additional methods to allow investment advice to be provided to participants and beneficiaries.

## **THE REQUEST FOR COMMENTS ON GENERALLY ACCEPTED INVESTMENT THEORY AND OTHER MATTERS**

The Department requested comments on the conditions applicable to computer-driven model investment advice, including:

- (i) which investment theories are generally accepted and which ones are not;
- (ii) whether the regulations should specify certain investment theories that are acceptable or proscribe the application of those not deemed to be generally acceptable;
- (iii) what historical data should be considered in determining a computer model's expectation for future performance of asset classes and specific investment alternatives;
- (iv) whether the regulations should specify what criteria are appropriate and objective and what criteria are not for asset allocation purposes;
- (v) whether a fund's past performance relative to the average for its asset class is an appropriate criterion for allocating assets to the funds;
- (vi) whether a fund's superior past performance can be demonstrated to derive not from chance, but from factors likely to persist in the future; and
- (vi) how the computer model should take into account investment management style.

Even though the questions are limited to computer models, FPA is very concerned that the Department may prescribe specific guidelines for what constitutes generally accepted investment theories. Potentially, if such rules are promulgated, they would also affect the investment advice programs under the Sun America Advisory Opinion and education and asset allocation tools made available by plan sponsors to participants under Interpretative Bulletin 96-1.

FPA believes that "generally accepted investment theory" is not one that is susceptible to specific guidelines. Rather, it is a fluid theory which has evolved over the years and will continue to evolve in the future. Investment professionals have sufficient knowledge and expertise to determine what theories are appropriate to be used in computer models and what data should be considered in developing computer models. Under the proposed rules, an eligible investment expert must certify that the computer model meets the requirements of the regulations, including that it applied generally accepted investment theories. Additionally, an annual audit must be performed by an independent auditor who has appropriate technical training and experience and

efficiency. The audit requirement applies to both level fee advice and computer-driven advice.

FPA believes that prescribing methodology to determine whether the generally accepted investment theory requirement was satisfied would be beyond the Department's purview and would substitute its judgment for that of the experts required to be retained by the fiduciary adviser. Moreover, it would not be practicable since any requirements published today would not take into account changing financial markets and conditions in the future.

### **ADDITIONAL GUIDANCE NEEDED ON QUALIFICATIONS OF INDEPENDENT AUDITOR AND THE SCOPE OF THE AUDIT**

The regulations require annual audits for both level fee advice and computer model-driven advice. The audits are to be conducted by an independent auditor who has appropriate training or experience and proficiency. The auditor is required to "review sufficient relevant information to formulate an opinion as to whether the investment advice arrangements, *and the advice provided pursuant thereto*, offered by the fiduciary adviser during the audit period were in compliance with [the regulations]."

FPA believes that additional guidance should be provided on the qualifications for an independent auditor based on satisfaction of enumerated requirements as to experience, education, professional certification and/or licensing. The regulations impose a fiduciary duty on the fiduciary adviser for the selection of the auditor, but do not provide any tangible guidance to them on what qualifications would constitute "appropriate technical training or expertise."

FPA also believes that additional guidance should be provided on the scope of the auditor's engagement. Under the regulations, the auditor is tasked with determining the appropriate scope of the audit and the extent to which it can rely on representative samples. However, this reliance upon the auditor without any guidance as to what the Department would consider a reasonable scope does not assist the fiduciary adviser in selecting and monitoring the independent auditor. This is a new requirement and persons who will fulfill the responsibilities of an independent auditor (as well as fiduciary advisers who retain them) will need guidance on the scope of the engagement in auditing both the level fee arrangement and the computer model arrangement.

### **ADDITIONAL REQUIREMENT ON FACTORS TO AVOID IN COMPUTER MODEL-DRIVEN ADVICE**

The regulations added a new requirement that computer model advice must satisfy—the investment recommendations must not "inappropriately favor investment options within a single asset class on the basis of a factor that cannot confidently be expected to persist in the future." In the Preamble, the Department, in explaining this language, opined that:

*While some differences between investment options within a single asset class, such as differences in fees and expenses or management style, are likely to persist in the future and therefore to constitute appropriate criteria for asset allocation, other differences, such as differences in historical performances, are less likely to persist and therefore less likely to constitute appropriate criteria for asset allocation.*  
[Emphasis added.]

FPA is very concerned by this comment. Historical rates of returns, even within a single asset class, have always been considered under generally accepted investment theories. Obviously, historic rates of returns are not the only criterion and must be carefully analyzed along with many factors, but they should not be ignored.

FPA is also concerned that the Department is favoring passively managed or index investment funds over actively-managed funds for 401(k) plans and IRA accounts. Again, we believe that this decision is outside the scope of the Department's role in promulgating these regulations and also not within its expertise. The Department would be substituting its judgment for that of the experts required to be retained by the fiduciary adviser. The investment experts will use their expertise and professional judgment in providing investment advice and developing, certifying and auditing eligible investment advice arrangements. One final comment is that there are many changes that occur in funds—managers leave, others are retained; fees and expense ratios increase and decrease over time; new participants may be precluded from investing in funds; or different terms of investments may apply from time to time. Nothing is immutable and any major event at the fund level may render criteria used "less likely to persist."

#### **PROHIBITION ON THE FIDUCIARY ADVISER'S RECEIPT OF COMPENSATION BASED IN WHOLE OR IN PART BASED ON THE PARTICIPANT'S SELECTION OF INVESTMENT OPTIONS**

FPA supports the Department's objective to clarify that a fiduciary adviser (including any employee, agent or registered representative) may not receive any fees or other compensation (other than its disclosed level fee) from any party that is based (in whole or in part) on a participant's selection of an investment option. FPA understands that, in order to assure that the level-fee requirement is rigorously enforced on financial advisers, it is important that the rules are not breached through "backdoor" arrangements. However, we believe that the rule as written is overly broad and ambiguous. For example, it includes "awards," "promotions" and "other things of value." This encompasses more, we believe, than is necessary to ensure unbiased advice through level-fee arrangements.

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## **SUMMARY**

We thank you for the opportunity to comment on the proposed rules that are critical to helping Americans reach financial independence at retirement and with standards that allow for the delivery of competent, objective investment advice. We are available to discuss these matters further at the Department's request. Please do not hesitate to contact us at (202) 449-6340.

Very truly yours,

A handwritten signature in black ink, appearing to read "Phillips Hinch". The signature is written in a cursive style with a long horizontal stroke at the end.

Phillips Hinch  
Assistant Director, Government Relations