



FINANCIAL
SERVICES
ROUNDTABLE

SUBMITTED ELECTRONICALLY

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Office of Regulations and Interpretations
Employee Benefits Security Administration
Room N-5655
U.S. Department of Labor
200 Constitution Avenue, N.W.
Washington, DC 20210

**Re: Request for Information Regarding Standards for Brokerage
Windows in Participant-Directed Individual Account Plans [RIN:
1210-AB59] 79 FEDERAL REGISTER 49469 (August 21, 2014) (the
“RFI”)**

Ladies and Gentlemen:

The Financial Services Roundtable¹ (“FSR”) welcomes the opportunity to provide the Department of Labor (the “Department”) with a response to its RFI with respect to

¹ As *advocates for a strong financial future*TM, FSR represents the largest integrated financial services companies providing banking, insurance, payment, and investment products and services to the American consumer. Member companies participate through the Chief Executive Officer and other senior executives nominated by the CEO. FSR member companies provide fuel for America’s economic engine, accounting directly for \$92.7 trillion in managed assets, \$1.2 trillion in revenue, and 2.3 million jobs.

so-called “brokerage windows” in defined contribution plans (“DCPs”), including plans containing a cash or deferred feature under Section 401(k) of the Internal Revenue Code of 1986, as amended (the “Code”). In our response, we offer our view that such brokerage windows further the intent and purpose of Section 404(c) of the Employee Retirement Income Security Act of 1974, as amended (“ERISA”), and that no further guidance or incremental disclosure is required with regard to the operation and utilization of such brokerage windows by participants in DCPs.

I. General Comment on Brokerage Windows

While the term brokerage window broadly refers to a program or procedure whereby the participants in a DCP are afforded access to investment options that are not “designated investment alternatives” – that is, core investment funds offered under a DCP to afford participants investment choices that offer a mix of alternatives with divergent risk profiles, there is no standard program or process associated with such term. In some cases, the brokerage window may be a mutual fund window that offers access to an incremental number of publicly available registered investment companies. In other cases, such a window affords participants access to a broader group of publicly available pooled investment funds and alternatives; in yet other cases, it allows participants to select from a wide array of such collective investment vehicles and to make investments in individual publicly traded securities. A recent study on defined contribution/401(k) fees shows that only the participants that use a brokerage window bear the related recordkeeping and administrative fees.²

Larger plans, which have greater numbers of participants and assets available for investment, generally offer participants a larger number of designated investment

² Deloitte and Investment Company Institute, “Inside the Structure of Defined Contribution/401(k) Plan Fees, 2013: A study assessing the mechanics of the ‘all-in’ fee,” (Aug. 2014) at 7, available at http://www.ici.org/pdf/rpt_14_dc_401k_fee_study.pdf (noting that activity-related fees for self-directed brokerage “are not part of the core expense of administering a plan”). *See*, RFI Questions 25-26.

alternatives from which to choose, as the per participant administrative expense associated with offering such alternatives within the applicable legal requirements is more manageable. In such larger plans, the brokerage window serves as a means to afford participants access to more specific investments (such as individual stocks) or a manager or a management style that is not available within the designated investment alternatives. This allows a participant to choose to diversify the participant's account balance by adding investments with risk profiles that may not be considered appropriate for a designated investment alternative. In smaller plans, where the assets available for investment and the associated cost constraints will generally make offering a larger number of designated investment alternatives impossible or prohibitive, brokerage windows may afford access to a wider array of registered investment fund alternatives among which the participants may choose to diversify their portfolios. Indeed, with respect to plans that have a very modest number of participants, the expenses associated with establishing and maintaining designated investment alternatives may be simply prohibitive for the employer or the participants. Brokerage windows can eliminate the need for elaborate recordkeeping programs that have significant expenses that can not be amortized rationally across a handful of participants. Given these applicable constraints, such brokerage windows may be an important element in allowing the sponsor to offer a plan to its employees that is cost sustainable, has sufficient investment opportunity to make the plan attractive to employees and to operate within the parameters of applicable law.

II. Executive Summary

We believe that the information reported in the Plan Sponsor Council of America's "56th Annual Survey of Profit Sharing and 401(k) Plans" (the "PSCA Study") and referenced herein demonstrates that brokerage windows primarily are used by the participants in DCPs to afford them access to additional types of investment opportunities that are not otherwise available to them. Brokerage windows allow the participants the opportunity to invest in a wide array of investments available generally in the

marketplace on a basis that is substantially comparable to how the participants could invest their own non-plan assets. FSR believes that such opportunities are not only allowed, but encouraged, by the statutory provisions of Section 404(c) of ERISA. We also believe that any guidance that would limit their use, attempt to establish greater responsibility or liability for plan fiduciaries or impose additional disclosure requirements would likely impede the cost-effective utilization would of such brokerage windows in direct conflict with the Congressional intent reflected in Section 404(c) of ERISA.

III. Purpose and Intent of Section 404 of ERISA

As is illustrated below by reference to the statute itself and the accompanying legislative history, Section 404(c) of ERISA demonstrates a strong Congressional intent to allow participants in DCPs to direct and control their own investments without imposing fiduciary duties and obligations on other persons, so long as those participants have access to a broad range of investments.

Section 404(c)(1)(A) of ERISA provides that:

In the case of a pension plan which provides for individual accounts and permits a participant or beneficiary to exercise control over assets in his account, if a participant or beneficiary exercises control over the assets in his account (as determined under regulations of the Secretary)—

- (i) such participant or beneficiary shall not be deemed to be a fiduciary by reason of such exercise, and
- (ii) no person who is otherwise a fiduciary shall be liable under this part for any loss, or by reason of any breach, which results from such participant's or beneficiary's exercise of control, except that this clause shall not apply in connection with such participant or beneficiary for any blackout period during which the ability of such participant or beneficiary to direct the investment of the assets in his or her account is suspended by a plan sponsor or fiduciary.

That this provision of ERISA is intended to allow participants the opportunity to invest their account balances at their discretion among investments that they personally

select is expressly illustrated in the Conference Committee Explanation of Section 404 of ERISA:

Under the substitute, a special rule is provided for individual account plans where the participant is permitted to, and in fact does, exercise independent control over the assets in his individual account. In this case, the individual is not to be regarded as a fiduciary and other persons who are fiduciaries with respect to the plan are not to be liable for any loss that results from the exercise and control by the participant or beneficiary. Therefore, if the participant instructs the plan trustee to invest the full balance of his account in, *e.g.*, a single stock, the trustee is not to be liable for any loss because of a failure to diversify or because the investment does not meet the prudent man standards. However, the investment must not contradict the terms of the plan, and if the plan on its face prohibits such investments, the trustee could not follow the instructions and avoid liability.

Indeed, the Congressional intent in affording the Department authority to adopt regulations in regard to such participant directed investments is to address whether the participant has exercised “independent control” over the investment of his or her account balance; and not to limit the circumstances under which, or the investments as to which, a participant could provide direction regarding the investment of his or her account.

The conferees recognize that there may be difficulties in determining whether the participant in fact exercises independent control over his account. Consequently, whether participants and beneficiaries exercise independent control is to be determined pursuant to regulations prescribed by the Secretary of Labor. The conferees expect that the regulations will provide more stringent standards with respect to determining whether there is an independent exercise of control where the investments may inure to the direct or indirect benefit of the plan sponsor since, in this case participants might be subject to pressure with respect to investment decisions. (Because of the difficulty of ensuring that there is independence of choice in an employer established individual retirement account, it is expected that the regulations will generally provide that sufficient independent control will not exist with respect to the acquisition of employer securities by participants and beneficiaries under this type of plan.) In addition, the conferees expect that the regulations generally will require that for there to be independent control by participants, a broad range of investments must be available to the individual participants and beneficiaries.

IV. Brokerage Windows Effect the Congressional Intent of Allowing Participants Independent Investment Control Over Their Account Balances

Brokerage windows are perhaps the best illustration of the independent control of investments that Congress expressly authorized for participants in Section 404(c). The presence of such brokerage windows within a DCP affords the participants access to a wider array of investment alternatives for the investment of their account balances than would otherwise be available to such participants under the DCP's designated investment alternatives.

Indeed, as a practical matter, the Department's guidance on the duties and responsibilities of fiduciaries with regard to investment opportunities that are designated investment alternatives has the effect of creating a limit on the number of alternatives that can reasonably be made available to participants. It would be unreasonable to expect that plan fiduciaries could (or would) undertake to evaluate and approve an unlimited number of designated investment alternatives, and for the sponsor to provide the required disclosure in respect of each such designated investment alternatives. These burdens essentially assure that the number of designated investment alternatives in any DCP will be constrained, and particularly so in respect of DCPs sponsored by smaller employers, where the plan has a modest number of participants and a correspondingly smaller cumulative amount of assets available for investment at the direction of participants. Such small employers do not have extensive human resources or finance departments with the capabilities to assist the internal plan fiduciaries in evaluating a large number of designated investment alternatives. Accordingly, the investment choices that can be reasonably made available to participants in DCPs, and especially those of smaller employers, will be finite.

Brokerage windows operate to allow participants in DCPs reasonable latitude to direct the investment of their own account balances in a manner that is substantially comparable to how they would invest their own personal, non-plan assets. The

participants would do their own investigation of the available investment options, and would bring to bear the same judgment as to whether they have sufficient information to make an informed investment determination as they would in investing assets in a non-plan account. Consistent with the purpose and intent of Congress in enacting Section 404(c), plan fiduciaries should have no added responsibility or liability, or duty to provide disclosure about the specific alternatives available, when allowing the participants to exercise their personal judgment among a wide array of market-based investment alternatives.

Participants can utilize brokerage windows to access managers and investment strategies that would not be available to them under the otherwise available designated investment alternatives. Through these windows, participants can elect to diversify their portfolios or access investment opportunities beyond those that would otherwise be available. The legislative history cited above states that Congress would allow a participant to direct the investment of his or her entire account balance into a single stock, and that no other person should have any liability for that decision. Thus, Congress established the framework that allows for such brokerage windows, and determined that it was appropriate to allow each participant to make his or her own investment judgments, and his or her investment errors, without having ERISA impose added burdens on fiduciaries or plan sponsors.

The data available under the PSCA Study suggests that, consistent with the Congressional intent, such windows are generally used as a means of supplementing the core investment funds that are available to participants under their DCPs. The PSCA Study shows that, based on data assembled with regard to 2012, brokerage windows were utilized modestly by plan participants. That study included a total of 686 DCPs, covering an aggregate of 10.3 million participants, having collectively \$769 billion in assets. As to all plans in the study, only 2.4% of the assets in such plans were allocated to what was

described in the PSCA Study as “self-directed brokerage windows.”³ An additional 1.3% of the assets under such plans were allocated to what the PSCA Study described as “mutual fund windows.”⁴ If these two categories of self-directed options were combined, less than 4% (*i.e.*, 3.7%) of the assets of the 686 plans in the PSCA Study were allocated to brokerage windows. While in the aggregate, this represents that in 2012, the 686 DCPs in the PSCA study had collectively just under 28.5 billion invested through brokerage windows, this amount represents only \$2,765 per participant.

A similar result derived from a study conducted by Deloitte Consulting LLP, entitled, “Inside the Structure of Defined Contribution/401(k) Plan Fees, 2013 (the “Deloitte Study”). 361 plans participated in the Deloitte Study, providing information with respect to over 200 data elements covering plan design, investment options and plan, participant and investment fee information.⁵ Over 90% of the assets in respondent plans were allocated to investment options that included equity investment options (41%), fixed income or stable value funds (collectively 22%), target date funds (16%) and company stock funds. Of the respondents, 47% indicated that they had investment options that were collapsed into a category of other options, including self-directed brokerage and plan loans, that represented only 2% of the assets of the plan. While over 95% of the respondents indicated that they offered equity investment options and fixed income investment options, and over two-thirds stated they had stable value and target funds, only 47% of the respondents indicated that they had options (including self-directed brokerage) included in the sparsely utilized “other” category.⁶

³ PSCA Study, Table 74 – Average Asset Allocation of Plans, “Average Asset Allocation for All Plans.”

⁴ *Id.*

⁵ Deloitte Study, *supra note 2* at p. 2.

⁶ *Id.* at p.15

FSR believes that such data demonstrates that participants find that such brokerage windows offer them a not immaterial benefit to diversify and manage the investment of their account balances among investment options that are not designated investment alternatives, but that the vast majority of the assets invested under such plan are still invested through the DCPs' designated investment alternatives. Applying this data in the same way, in 2012, over 96% of the assets in the covered DCPs (representing over \$740 billion and approximately \$72,000 per participant) were being invested through investment alternatives other than brokerage windows.

The PSCA Study demonstrates that this conclusion is true even in respect of the smallest plans participating in the Study—that is, plans covering between 1 and 49 participants (a “Small Plan”). The utilization of brokerage windows does increase for these Smaller Plans, likely reflecting the practical reality that such Smaller Plans are not able to cost-effectively offer their participants as many and as diverse designated investment alternatives as those generally made available under plans with significantly larger numbers of participants. Yet, the PSCA Study shows that these brokerage windows nonetheless generally supplement the designated investment funds even in these smaller plans.

Approximately 17.4% of the Smaller Plans reported having available self-directed brokerage windows and another 7.6% reported offering mutual fund windows.⁷ By way of contrast, 75% or more of these Smaller Plans indicated that they offered within the DCP a domestic equity fund, an international equity fund and a domestic bond fund.⁸ Approximately 50% of these Smaller Plans also indicated that they offered plan participants the choice of one or more target date retirement funds.⁹ With regard to asset

⁷ PSCA Study, Table 67 – Investment funds available in the plan by plan size, “Plans with 1-49 participants.”

⁸ *Id.*

⁹ *Id.*

allocation, the PSCA Study reported that 7.7% of the assets of these Smaller Plans were allocated to the self-directed brokerage windows, with an additional 5.1% reported as being allocated to the mutual fund windows.¹⁰ Thus, on a combined basis these self-directed brokerage windows represented fewer than 13% (that is, 12.8%) of the assets invested through these Smaller Plans. Thus, approximately 5/6ths of the assets in such Smaller Plans were invested through investment options other than the brokerage windows. Interestingly, these Smaller Plans reported that the largest single concentration of assets reported was the 25.1% allocated to the domestic equity fund¹¹ alternative made available under such plans. Thus, the allocation under these Smaller Plans to just the single most commonly used designated investment alternative was almost twice as large as the allocations to both the self-directed brokerage window and the mutual funds windows combined.

V. Data with Regard to the Allocation of Costs Related to Brokerage Windows

A study of the expenses incurred in connection with the administration of defined contribution plans indicates that the expenses related to such self-directed brokerage accounts are borne by the participants who use that option, and not by participants generally.

The Deloitte Study concluded that participants bear the majority of the fees incurred in the administration of 401(k) plans, determining that, on average, participants bear 87% of the of the total plan fees.¹² The median “all-in” fee for plans in the survey was 0.67% or approximately \$267 per participant. However, the study clearly indicated that the percentage of assets payable to cover plan expenses varied inversely to plan size, with participants in respondent plans with less \$1 million in assets paying a median of

¹⁰ PSCA Study, Table 74 – Average Asset Allocation of Plans, “Plans with 1-49 participants.”

¹¹ *Id.*

¹² Deloitte Study, at p.17; *see also* Exhibit 14 on p.17.

1.27%, while participants in respondent plans with over \$500 million in assets paid a median of only 0.37% of assets to cover administrative and investment expenses. This disparity reflected the fixed costs required to establish and operate a defined contribution plan, which are mostly driven by legal and regulatory requirements. As a plan grows in size, “these fixed costs can be spread over more participants and/or a larger asset base.”¹³

In determining the applicable “all-in” fees, Deloitte excluded “those recordkeeping and administrative activity fees that only apply to particular participants who engage in the activity (*e.g.*, self-directed brokerage, managed accounts, loans, QDROs and distributions).”¹⁴ The study stated that “[w]hile these specific activity-related fees are an important consideration for participants engaging in the activity, they are not a part of the core expense of administering a plan.”¹⁵ Thus, the Deloitte Study concluded that among the respondent plans in its survey, the participants who use these self-directed accounts bore the expenses associated with using this investment alternative.

VI. No Need for Further Disclosure Regarding Brokerage Windows

FSR believes that the currently effective disclosure régime with regard to brokerage windows, as discussed and described in Questions 13 and 29 of Field Assistance Bulletin No. 2012-02R, adequately protects the interests of plan participants, provides them with the information that they need to determine whether to utilize any available brokerage window, and does not place an excessive burden on the sponsors of the DCPs that have a brokerage window opportunity. The current régime properly reflects the role such brokerage windows play within the applicable DCP. As is discussed above, these brokerage windows offer participants the opportunity to exercise their own independent control and judgment as to what investments to make from a broad

¹³ *Id.* at p.7.

¹⁴ *Id.*

¹⁵ *Id.* at p. 17.

array of choices, just as they would were they investing their own assets outside of the DCP. FSR believes that these brokerage windows further the purposes of Section 404(c), and that the current regime of reporting and disclosure reflected in Questions 13 and 29 of the Field Assistance Bulletin is not inconsistent with that intent. Added disclosure burdens could prove to discourage plan sponsors and plan fiduciaries from offering these incremental investment opportunities to plan participants. As is illustrated in the information cited from the PSCA Study, participants generally would appear to utilize these brokerage windows to enhance the diversification of their portfolios and undertake independent control of their investments, just as Congress has indicated that they could when enacting Section 404(c). FSR is concerned that an unnecessary expansion of the duty to disclose would have the unintended effect of minimizing the opportunities afforded to participants under such brokerage windows, actually diminishing their rights rather than protecting them.

VII. Conclusion

The focus of the RFI appears to suggest that the Department is seeking to explore whether brokerage windows may be operated in a manner that is detrimental to plan participants. FSR and its members support efforts to assure that these otherwise appropriate and permissible programs are not, in some cases, operated in a manner that is detrimental or unfair to the participants that such programs are designed to assist. Initiatives that further the interests of plan participants and that limit, minimize or eliminate the possibility that plan participants are subjected to improper or inappropriate risks, costs or other detriments are to be lauded. However, FSR hopes that, as it undertakes its review, the Department approaches the process of identifying perceived areas of abuse with a thorough understanding of, and an open mind as to, the value that such brokerage windows afford to participants by providing them broad access to incremental investment choices to be exercised (as Congress intended) under their independent control. We have some concern that the tenor and nature of the questions presented in the RFI may imply that the Department has assumed, or worse pre-

determined, that such windows are generally operated to benefit persons other than the participants themselves. Based on the experience of our members, this would be a severe misperception and an unjustified and unwarranted conclusion. We also hope that the Department recognizes and appreciates that additional regulation that imposes additional burdens and/or potential liabilities on plan fiduciaries or disclosure that makes the offering of brokerage windows cost prohibitive to the plan sponsors could have the perverse effect of causing the elimination or substantial curtailment of brokerage windows, causing an unnecessary reduction in the investment opportunities available to plan participants.

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FSR appreciates the opportunity to provide the Department with our views regarding the utilization and benefit of brokerage windows in DCPs. If it would be helpful to discuss FSR's specific comments or general views on this issue, please contact me at Richard.Foster@fsroundtable.org.

Sincerely yours,



Richard Foster
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for Legal and Regulatory Affairs
Financial Services Roundtable

With a copy to:

The Honorable Phyllis Borzi, Assistant Secretary
Judy Mares, Deputy Assistant Secretary

Employee Benefits Security Administration
Department of Labor