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VIA ELECTRONIC MAIL

April 17, 2017

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

Re: Examination of Fiduciary Rule (RIN 1210-AB79)

Vanguard[1] welcomes the opportunity to comment on the Department of Labor's (the "Department") examination of the revised definition of the term "fiduciary" and related exemptions (the "Rule").[2] Vanguard supports the Department's efforts to adopt an updated definition of fiduciary advice that reflects the modern retirement landscape. Vanguard strongly believes that investors should always receive investment advice that is in their best interest, and those who provide investment advice should be held to a fiduciary standard. However, Vanguard urges the Department to modify the scope of its definition of investment advice and certain operational aspects of the Rule to protect investors in an efficient and cost-effective way while promoting access to high-quality investment advice, information and education. By adopting an updated Rule – one that provides streamlined, consistent requirements that protect investors – the Department will better promote investor access to quality investment advice while preserving the availability of critically important investment information and education.

I. Executive Summary

As noted above, Vanguard strongly believes that investors should always receive investment advice that is in their best interest, and those who provide investment advice should be held to a

[1] Vanguard is one of the world's leading asset managers, managing over $4 trillion for institutional and retail investors. Vanguard manages over $1 trillion in defined contribution ("DC") and defined benefit ("DB") plan assets and provides recordkeeping and administrative services for over 4 million participants in over 6,700 DC and DB plans. We also manage over $600 billion for over 6 million individual retirement account ("IRA") investors. We provide fiduciary investment advice to IRAs and other clients through Vanguard Personal Advisor Services, which currently has approximately $77 billion in assets under advisement across all client types. We also provide fiduciary investment management to retirement plan clients through the Vanguard Managed Account Program ("VMAP"), an investment management service based on systems and methodology developed and maintained by Financial Engines Advisors LLC. VMAP manages over $20 billion on a discretionary basis.

[2] 81 Fed. Reg. 20946 (Apr. 8, 2016).

fiduciary standard. As a result, Vanguard supports the Department's efforts to require those who provide investment advice to retirement accounts to do so in the investors' best interests. As such, we do not believe that the Rule should be revoked. Revoking the Rule in its entirety would allow some providers to continue to operate under a lower standard of care, different from the fiduciary duty their clients may believe they enjoy – ultimately sowing confusion and undermining investors' retirement security.

While the Rule is necessary to protect retirement investors' interests, the Department must revise the Rule to achieve its objectives. Specifically, the Department should redefine investment advice in a way that better reflects investor expectations. The Department should also revise its requirements to remove conditions that promote litigation while working to better harmonize requirements for all advice, regardless of method of delivery, nature of recommendation or client size. These changes will more effectively promote investor interests efficiently and without excessive cost.

In this regard, the Department has been directed by the President's Memorandum to consider whether the Rule "empower[s] Americans to make their own financial decisions" and "facilitate[s] their ability to save for retirement."[3] As discussed in more detail in this letter, we believe that the Rule as drafted harms investors through reduced access to products, information and advice and is likely to unnecessarily increase litigation and cost to investors seeking retirement services.

Moreover, the Department's decision to move forward with implementation of the Rule's updated definition of investment advice and the Best Interest Contract ("BIC") Exemption's Impartial Conduct Standards will likely further increase the cost of compliance and reduce access to investment advice, information and education for retirement plan participants and individual retirement account ("IRA") investors (together "Retirement Investors"). As discussed in this letter, there are some modest but important clarifications that are required for the definition of investment advice to preserve access to investment education and information. In particular, the arbitrary distinction between small and large retirement plans is an element of the definition that will harm Retirement Investors if it is not amended in tandem with the Department's reevaluation of the BIC Exemption.

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[3] Specifically, the President's Memorandum directs the Department to prepare an updated economic and legal analysis considering whether, among other things:

(1) the Rule harms investors due to reduced access to retirement savings products, information or advice;

(2) the Rule has resulted in dislocation or disruptions within the retirement services industry that may adversely affect investors and retirees; and

(3) the Rule is likely to cause increased litigation and cost to investors to access retirement services.

If the record demonstrates that the Rule has caused any of these effects, the Department must issue a new proposal to revise or rescind the Rule. 82 Fed. Reg. 9675 (Feb. 7, 2017).

Additionally, it will be difficult for the Department to fully evaluate the effect of the Rule on access to investment education, information and advice without considering the effects of its overly broad definition in concert with the exemptions the Rule provides. The Department has justified its decision to move forward with the Rule in piecemeal form because it believes that Retirement Investors will benefit more quickly from the Rule's protections if at least part of the Rule is in effect. In our view, it is unlikely that these benefits will materialize. Advisors and service providers, like many investors, do not operate well in an environment of uncertainty. It is unlikely that Retirement Investors will have access to greater protections of the definition of fiduciary investment advice because providers are unlikely to develop services to comply with a Rule when only half of the conditions are settled, and likely will choose to avoid fiduciary status instead. If the Department applies the expanded definition before it clarifies the remaining conditions of the exemptions, many providers may limit their provision of investment education and information, rather than expand or maintain it, to avoid being covered by a legal standard that has not been through the complete review ordered by the Administration. We strongly encourage the Department to reconsider its decision to implement the Rule in part in the absence of the full review required by the President's Memorandum.

We urge the Department to address the issues raised by the President's Memorandum while continuing to protect investors by revising the Rule with these core principles in mind:

- ***The definition of investment advice should reflect reasonable investor expectations.*** An overly broad definition of investment advice that subjects educational and sales information to fiduciary obligations is not in investors' interest because it will undermine access to important retirement information and education. The Department should revise the definition of investment advice to better reflect reasonable investor expectations.
- ***Exemptions for fiduciary investment advice should apply consistently to all advice, regardless of method of delivery, nature of recommendation or client size.*** As finalized, the Rule applies unnecessary distinctions between the method institutions may use to deliver investment advice (digital vs. hybrid or in-person), the subject matter covered by a fiduciary recommendation (rollovers vs. investments) and different types of clients (small vs. large plans). These distinctions unduly complicate compliance and innovation in the delivery of investment advice – increasing cost and reducing access to services – and do not materially promote investors' interests or meet their expectations. Indeed, it is in investors' overall interest to have consistent fiduciary standards requiring advisors to act in their best interest regardless of these distinctions. The Department's review should harmonize the requirements for investment advice delivered to different clients, in different forms, covering different topics.
- ***The Department should significantly simplify the BIC Exemption by limiting it to the Impartial Conduct Standards and removing the Exemption's provisions encouraging class action litigation in state courts.*** The Department can effectively address conflicts of interest and promote broader availability of fiduciary advisory services by substantially simplifying the conditions of the BIC Exemption. Specifically, the Department should limit its

requirements to an enforceable commitment to the Impartial Conduct Standards. Additionally, the BIC Exemption should not be enforceable through class-action lawsuits in state courts with no experience in applying the complex fiduciary or prohibited transaction provisions of the Employee Retirement Income Security Act of 1974, as amended ("ERISA"). An enforcement system that substitutes class-action litigation for direct oversight by the Department and Internal Revenue Service threatens the critical uniformity in administration that ERISA was designed to promote and will drive up costs, thus lowering investors' returns.

- ***The Department should not delay the Rule to wait for other regulators to act first, but the Department should closely align with other regulators to harmonize investor experience across different types of accounts.*** Investors in different kinds of accounts – retirement and non-retirement – should all receive investment advice that is in their best interest. As the Department moves forward with its examination of the Rule, it should actively engage with other regulators to better harmonize the compliance requirements and investor experience in retirement and non-retirement accounts.

II. Retirement Investors Benefit from Investment Advice and Education

Access to quality investment advice promotes the objectives articulated in the President's Memorandum, and the Department should review the Rule with a careful eye toward protecting and improving that access for Retirement Investors. Professional investment advice and management are essential components of retirement planning for many Retirement Investors. Our research demonstrates that all types of investors benefit from investment advice that helps them appropriately diversify investments, select cost-effective investments, rebalance, contribute amounts that maximize employer match dollars and provide the best chance for long-term retirement success, hold and spend assets in a tax-efficient way, and spend down retirement assets at a sustainable rate.

A. The benefit of investment advice and investment management

Vanguard has found that fiduciary investment advice and management services are important ways for Retirement Investors to improve their savings rates, better diversify their investments, avoid reacting to short-term market swings, and can ultimately increase retirement wealth. As the Department evaluates the impact of the Rule on investor access to products, information and services, we encourage the Department to recognize the value of investment management and advice, and consider our examples of the ways the Rule will limit that access.

Relationship-oriented investment advisory services, which take a more holistic view of an investor's circumstances, can add meaningful value to investors' bottom line compared to the average investor experience. This value is illustrated through the Vanguard Advisor's Alpha concept.[4] Advisor's Alpha describes how fiduciary investment advisors can add more consistent value through wealth management in the form of services such as financial planning, behavioral coaching and guidance, rather than a more singular focus on outperforming a particular benchmark. More specifically, the Vanguard Advisor's Alpha framework demonstrates that advisors are capable of adding net returns in excess of standard advisory fees by delivering investment advice on a broader range of financial issues than just asset allocation. For example, advisors can improve outcomes by providing discipline and reason to investors who can be emotional or chase past performance in their investments without regard to diversification, overall cost or their long-term goals. While the actual amount of value added may vary significantly depending on clients' circumstances, we have found that relationship-oriented advisory services employing the Advisor's Alpha framework can potentially add about 3% in net returns to the portfolios of advised clients compared to investors who are not advised (or who are advised based on a different framework).[5]

Similarly, we have found that Retirement Investors benefit in a variety of ways from fiduciary investment management services where the investor turns over decision making to a professional who is acting on their behalf.[6] Our research indicates that participants who used fiduciary investment management services increased their retirement wealth over a decade by an average of 15% – and 60% of participants increased their retirement wealth by an average of 30%, net of investment and advice fees. Those increases were attributable to two key factors: increased returns to due greater equity exposure and, for some participants, increased retirement savings rates. In particular, we found that one-third of participants chose to increase savings rates by an average of 3 percentage points. Other factors contributed to increased retirement wealth, including reductions in average fund fees due to reallocation to lower-priced funds through a professionally managed portfolio, reduced allocations to company stock, and increased allocations to international equities. Participants who used investment management services invested more appropriately for their goals and saved more toward those goals than those who did not, and those factors materially increased their overall retirement wealth.

The benefits of fiduciary investment management and advice are clear. As drafted, however, the complexity of the Rule may reduce access to advice and management, creating an advice gap for some period of time where these valuable services are not available to all segments of the

[4] *See, e.g., Vanguard advisor's alpha*, Bennyhoff, Donald G. and Francis M. Kinniry, Jr. (June 2016), available at https://advisors.vanguard.com/VGApp/iip/site/advisor/researchcommentary/article/IWE_ResAdvisorsAlpha; *Putting a value on your value: Quantifying advisor's alpha*, Kinniry, Francis M., Jr., Colleen M. Jaconetti, Michael A. DiJoseph, Yan Zilberinga and Donald G. Bennyhoff (Sept. 2016), available at https://advisors.vanguard.com/VGApp/iip/site/advisor/researchcommentary/article/IWE_ResPuttingAValueOnValue; and *Reframing investor choices: Right mindset, wrong market*, Kinniry, Francis M., Jr., Colleen M. Jaconetti, Donald G. Bennyhoff and Michael A. DiJoseph (Apr. 2016), available at https://advisors.vanguard.com/VGApp/iip/site/advisor/researchcommentary/article/IWE_InvResRightMindSet.

[5] *Putting a value on your value: Quantifying advisor's alpha*, at p. 4, Fig. 1.

[6] *See The value of managed account advice*, Pagliaro, Cynthia A. and Stephen P. Utkus (Aug. 2015), available at https://institutional.vanguard.com/VGApp/iip/site/institutional/researchcommentary/article/InvResManagedAccountAdvice.

market. In this regard, the experience in the United Kingdom with Retail Distribution Review ("RDR"), which reformed the market for investment advice (by, among other things, prohibiting commissions), is instructive.[7] Following implementation, a report from the Financial Advice Market Review ("FAMR") launched by HM Treasury and the Financial Conduct Authority on RDR included responses indicating that firms focused their efforts on clients with a certain minimum amount to invest. In particular, a survey of advice firms suggested that, between 2013 and 2015, the proportion of firms who asked for a minimum portfolio of more than £100,000 more than doubled, from around 13% in 2013 to 32% in 2015. A survey of advisors by the UK Financial Conduct Authority also supports this, suggesting that 45% of firms very rarely advise customers on retirement income options, if those customers have small funds (*i.e.*, less than £30,000) to invest.[8]

Ultimately, we believe that any advice gap created by the Rule can be narrowed as advisors develop more innovative ways to deliver advice. The UK experience with respect to RDR is instructive on this point, as well. In its report, the FAMR concluded that the advice gap created by RDR with respect to some investors could be narrowed by fostering access to affordable advice through robo-advisory services, encouraging the development of nudges and making other investment information more available to investors, and clarifying the potential liability advisors may face with respect to their services.[9] The suggested changes we describe in this letter are intended to address similar concerns. In our view, the Department must revise the Rule to reduce complexity and remove unnecessary conditions that deter advisors from filling the advice gap in order to encourage and protect the innovation that is necessary to address the advice gap. In particular, as described below, we urge the Department to revise the Rule to remove arbitrary distinctions in the conditions applicable to different types of advice, provided to different clients, through different methods. Without these changes, the Rule will reduce investor access to investment advice.

B. The majority of Retirement Investors still depend on investment education

Despite the demonstrated benefits that professional investment management and advice can provide, we have found that relatively few participants take advantage of these services. For example, although 75% of participants in plans that are recordkept by Vanguard have access to investment advice or investment management, only 16% of participants have used investment advice or investment management services.[10] We encourage the Department to consider how the Rule may be amended to encourage a greater number of Retirement Investors to seek assistance in light of the benefits of fiduciary investment management and advice. For those who will continue to make investment and distribution decisions on their own, however, it is critical for

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[7] These reforms were adopted by the UK Financial Services Authority on December 31, 2012.
[8] *See Financial Advice Market Review Final Report* (Mar. 2016) at p. 19, available at https://www.fca.org.uk/publication/corporate/famr-final-report.pdf.
[9] *Id.* at 4.
[10] *How America Saves 2016* at p.75, Fig. 81 (June 2016), available at https://institutional.vanguard.com/VGApp/iip/site/institutional/researchcommentary/article/HowAmericaSaves2016.

the Department to revise the Rule to better protect Retirement Investors' continued access to investment education and information. The majority of Retirement Investors depend upon it.

Automatic enrollment, automatic increases in savings rates and default investments have been powerful forces to increase retirement plan participation rates and improve investment allocations. While those features continue to gain popularity and increase retirement wealth, we have found that meaningful numbers of participants still lack automated plan features, or are not affected by those provisions because plan design only applies automatic features to newly enrolled participants.[11] For those participants who are not covered by default provisions and who do not use or have access to investment advice, simple and actionable educational messages to save more for retirement or modify extreme asset allocations are important tools to improve retirement outcomes.

For example, we have found that a simple "one step" enrollment process that allows participants to quickly enroll using a pre-filled deferral rate, automatic annual increase rate and investment in the plan's qualified default investment alternative ("QDIA")[12] has been 80% more effective than the lengthier traditional enrollment process. Specifically, while traditional enrollment materials tend to generate a 29% action rate, our "enroll now" approach has achieved a 53% enrollment completion rate. While interpreting and implementing the Rule, however, Vanguard became concerned that these simple messages could be considered fiduciary investment advice by identifying a single investment and encouraging participants to save more in the plan. Under the Rule's broad definition, these simple, effective messages could constitute investment advice either because they are "directed" to Retirement Investors or could be interpreted as a suggestion to take action with respect to a particular investment. As a result, the Rule caused us to question whether we should continue to deliver these messages, particularly in light of the Department's interpretive guidance issued after the Rule.[13] As described below, without modification, the overly broad definition of investment advice under the Rule could limit investors' access to this type of investment information and actionable education, ultimately reducing retirement wealth.[14]

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[11] *Id.* at 22-27.
[12] Each of the selections in the "enroll now" approach can be easily changed by participants if they choose to elect a different deferral or increase rate or investment option, and this feature is clearly explained.
[13] *See* Section III.A.1 below for discussion of the Department's Frequently Asked Questions ("FAQs").
[14] If the Department does not modify the definition of investment advice as we have suggested, we urge the Department to provide interpretive guidance that would permit simple, actionable messages promoting and simplifying investment in the plan's QDIA. Participants may be defaulted into a QDIA without making an affirmative election; it should be permissible to include those investments in actionable communications to participants.

III. The Department should modify the Rule to better reflect investor expectations, simplify compliance, promote innovation and harmonize investor experience

As drafted, the Rule harms Retirement Investors by reducing access to retirement savings products, information and advice and by increasing the cost of obtaining those products and services where they are available. To prevent these effects, the Department must amend the Rule to tailor the scope of the definition of investment advice to better reflect investor expectations while preserving access to investment education and information. The Department must also remove the Rule's arbitrary limitations on advice to different clients, on different topics, and through different channels, which increases the complexity of compliance and creates confusion for Retirement Investors. Finally, the Department must amend the exemptions under the Rule to remove unnecessary conditions and enforcement provisions that promote class-action litigation. These provisions increase the risk and uncertainty of complying with the exemption, ultimately discouraging advisors from providing services within the BIC Exemption's protective framework. As explained below, these changes will help the Department more effectively regulate fiduciary investment advice while ensuring that Retirement Investors still have access to the investment education and advice that is critical to their investment success.

A. The definition of investment advice should reflect reasonable investor expectations

The Department should revise the Rule to define investment advice in a way that is more consistent with Retirement Investors' expectations. The Rule's current definition sweeps in elements of investor education, sales and investment information in ways that do not promote Retirement Investors' interests, and is likely to reduce access to investment information and education, jeopardizing the majority of investors who rely on access to investment education to develop their own investment strategies and plan lineups without fiduciary help.

Vanguard agrees that investors should always receive investment advice that is in their best interest. The Department must recognize, however, that advisors must meet a high bar to ensure that a recommendation is in the investor's best interest. A fiduciary standard requires significant data regarding an investor's goals, risk tolerance, investment horizon, other assets and potential accounts or investments that may be used to satisfy the investor's needs. Advisors must assist Retirement Investors in collecting and analyzing that information. Importantly, the Department has suggested that advisors cannot provide recommendations at all unless Retirement Investors provide them with sufficient information.[15]

These efforts are warranted where advisors provide individualized recommendations about a course of action, such as statements that the Retirement Investor should roll over a plan account to an IRA or invest in a particular fund. Such detailed conversations are not warranted, however,

[15] *See, e.g.*, Conflict of Interest FAQs (Part I – Exemptions), Q&A 14 (Oct. 27, 2016), available at https://www.dol.gov/sites/default/files/ebsa/about-ebsa/our-activities/resource-center/faqs/coi-rules-and-exemptions-part-1.pdf.

where service providers are simply encouraging Retirement Investors to contribute more to their retirement accounts, consider the benefits of a more streamlined plan lineup or consider diversifying out of concentrated allocations to company stock. Without further clarification from the Department, each of these messages could be considered fiduciary investment advice under the Rule. If that is the case, many of these communications will become more complex to avoid the risk of being considered advice or will be simply abandoned.

1. *Investor education and clear sales communications should not be considered fiduciary advice*

As described above, Retirement Investors benefit from clear communications that simplify enrollment in the retirement plan and boost retirement savings. The Rule's overly broad definition of investment advice has called into question whether beneficial communications that promote retirement savings and improve retirement outcomes may continue. For example, the Department addressed messages intended to encourage greater retirement savings in a recent set of FAQs.[16] The Department's analysis suggested that those messages would be permissible as non-fiduciary activity when delivered by employer representatives, provided that their compensation was not affected by the overall amount of assets in the retirement plan. By adopting that rationale, the Department implied that the same message to increase contributions to a retirement plan could be considered investment advice if it were delivered by a service provider (whose compensation for recordkeeping services may be based on plan assets).[17] The Department's reasoning could also apply a fiduciary standard to communications designed to encourage participants with extreme asset allocations, such as a high concentration in employer stock, to consider diversifying their investments by using the plan's QDIA. Most Retirement Investors would benefit from greater retirement contributions and improved diversification, but if service providers must demonstrate that in every case such a message is in each investor's individual best interest, fewer service providers will deliver that education. For those attempting it, fewer Retirement Investors will provide the detailed information necessary for a service provider to confirm that the suggestion is in the investor's best interest.

Similarly, the Rule must provide clearer standards permitting call center representatives to provide information about their firms' products and services without triggering fiduciary status. Service providers often receive unsolicited investment inquiries by plan fiduciaries and individual Retirement Investors seeking information about the firm's products and services. In those cases, Retirement Investors do not reasonably expect the firm to provide information about other firm's products or advice about the universe of potential services available to the Retirement Investor. As long as those representatives do not make recommendations through a call to action that a reasonable investor would consider investment advice, that conduct should not be considered investment advice.

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[16] Conflict of Interest FAQs (Part II – Rule), Q&A 10 (Jan. 2017), available at https://www.dol.gov/sites/default/files/ebsa/about-ebsa/our-activities/resource-center/faqs/coi-rules-and-exemptions-part-2.pdf.

[17] *Id.*

The Rule's overreaching definition of investment advice in the plan sponsor context is also illustrated in the context of sales to retirement plan sponsors. Specifically, the Rule allows a provider to provide a sample investment lineup in response to an initial Request for Proposal ("RFP") – a welcome provision intended by the Department to address plan sponsor expectations and common sales practices. However, an RFP is typically only the initial entry point to a multi-round bidding process. Because the Department's exception is so narrow, if an institution provides the same information in a later round of the bidding process that it did at the RFP stage, those recommendations may become fiduciary investment advice even though the counterparty relationship remains the same. That complicates plan fiduciaries' ability to select providers and providers' ability to describe products and services that should be considered to meet participants' needs. The Rule's definition of investment advice should exclude a broader range of sales communications to permit a more robust exchange of information.[18]

2. *Rollover recommendations should continue to be considered fiduciary investment advice*

What to do with a retirement account balance – whether to roll it over, keep it in a plan or take the money in a lump sum – is one of the most important financial decisions a Retirement Investor will ever make. Those who provide rollover recommendations should be required to act in their clients' best interest when identifying the best option for Retirement Investors. Accordingly, we agree with the Rule's treatment of rollover recommendations as fiduciary investment advice and believe that any revised Rule should continue to classify rollover advice as investment advice.

An individualized call to action to take specific action with respect to investments is treated as investment advice in other contexts.[19] Similarly, an individualized call to action move money from one retirement account to another merits the protection of a fiduciary standard and should be considered fiduciary investment advice. Retirement Investors who are encouraged to roll plan balances over to an IRA based on their individual circumstances would likely reasonably consider that call to action to be an investment recommendation or investment advice. Retirement Investors should have confidence that rollover recommendations will be provided in their best interest. As described in detail below, however, the conditions that apply to those recommendations must be streamlined and harmonized to ensure that Retirement Investors will retain access to these services.

Rollover communications that do not contain a call to action, however, should remain available to Retirement Investors as non-fiduciary investment education. Many Retirement Investors do

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[18] Small plan sponsors are also disadvantaged due to the definition's overly restrictive carve outs for sales and ongoing communications regarding possible criteria for selection of investments. *See* Section III.B.3 below for additional discussion of the arbitrary $50 million distinction in the definition of investment advice and the BIC Exemption.

[19] *See, e.g.*, FINRA Regulatory Notice 11-02, *Know Your Customer and Suitability* (Jan. 2011), available at http://finra.complinet.com/net_file_store/new_rulebooks/f/i/finra_11-02.pdf; NASD Notice to Members 01-23, *Online Suitability* (Apr. 2001), available at http://www.complinet.com/file_store/pdf/rulebooks/nasd_0123.pdf.

not ask for a recommendation when deciding whether to take a distribution from a retirement account – they just want information about the potential consequences of different choices. These Retirement Investors should still be able to access important rollover education to better inform their decisions.

Rollover communications that are balanced under the circumstances should be clearly considered education under the Rule. Generally, this means presenting all distribution options when helping Retirement Investors making a decision on whether and how to take a distribution. If a Retirement Investor has already decided on a particular course of action – for example, a participant decides to cash out early despite negative income tax consequences – providers should be able to explain the consequences of that decision and identify alternatives that would not result in income taxes and penalties. In this example, the call center representative should be permitted to provide balanced guidance by explaining not only the tax benefits of a rollover but also the benefits of leaving account balances in the plan.

B. Exemptions for fiduciary investment advice should apply consistently to all advice, regardless of method of delivery, subject of recommendation or client size

One of the most challenging aspects of the Rule is its inconsistent and inefficient approach to different types of clients and services. By creating arbitrary distinctions among the conditions that must be satisfied to provide investment advice depending on the method used to deliver investment advice, subject of the recommendation and client size, the Rule prevents a consistent approach to compliance, hampers innovation as advisory services continue to evolve and promotes investor confusion. Consistent exemptions for different client types, recommendations and methods of delivery can significantly reduce the complexity and cost of implementation while preserving the benefits of the Rule for Retirement Investors.

Vanguard serves a wide spectrum of Retirement Investors with a wide range of preferences, from traditional in-person advice to online tools and recommendations, and naturally offers a range of investment advice programs to cater to these different preferences. Exemptions with consistent conditions would simplify compliance efforts and benefit Retirement Investors through lower costs and a more consistent experience. Client characteristics (such as assets under their control), needs and preferences (such as eligibility for or desire to use robo or in-person aspects of an advice service) do not remain static, and the conditions that apply to define and permit investment advice to meet those changing characteristics and needs should be flexible enough to apply to a broad range of circumstances. These changes can help prevent the Rule from harming Retirement Investors by reducing access to retirement savings products, information and advice and by increasing the cost of those products and services when they are available.

1. *Investment advice should be covered by similar conditions, whether provided through a robo-advisor or in-person*

As described above, investment advice can significantly improve outcomes for investors, and "robo" advisors provide perhaps the most – and in many cases, only – cost-effective method of making such advice available to Retirement Investors with smaller balances. The BIC Exemption, however, explicitly excluded robo-advice from its scope, apart from a limited carve-out for level-fee arrangements, concluding that "[i]ncluding such relief in this exemption could adversely affect the incentives currently shaping the market for robo-advice."[20] This restriction does not make sense. It is the content of the advice itself – for example, to invest in investment products affiliated with the advisor – that requires advisors to mitigate conflicts of interest through an exemption in the first place. The method by which the investor receives advice (in-person vs. robo vs. hybrid) is irrelevant to determining what conditions should apply to the advice. Perversely, by excluding robo-advice from the BIC Exemption, the Department may actually increase costs for investors by causing more investors to receive higher-cost in-person investment advice that can be provided under the BIC Exemption.

The fact that alternative exemptions are available to cover pure robo-advice (for example, the statutory exemption for computer-based advice under ERISA section 408(b)(14) (the "PPA Exemption")) should not bar providers from relying on the BIC Exemption for different methods to deliver investment advice. As investment advisory services continue to evolve, it is likely that some arrangements will include robo-advice for some investors and in-person or hybrid advice for others, depending on the type of account and the investor's preferences. As the Rule is drafted, advisors must design those programs to meet different conditions under different exemptions, requiring different disclosures at different points of engagement with the client, different contracts, and different oversight by internal or external parties.[21] These arbitrary differences do not provide additional protections to Retirement Investors, and are likely to limit ongoing innovation in investment advisory services, ultimately limiting access to investment advice for some investors and increasing cost for others.

2. *The same conditions should apply to investment advice regarding rollovers and investment decisions*

Similarly, the Rule has limited advisors' ability to use existing exemptions to cover investment advice regarding both rollover and investment decisions. To harmonize its regulatory framework, the Department should amend its regulations under the PPA Exemption to include rollover advice. In light of the Department's broader interpretation of fiduciary investment advice and the extensive protective conditions imposed by the PPA Exemption, the Department should clarify that the PPA Exemption may be used to provide distribution advice and other recommendations

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[20] *See* Preamble to the BIC Exemption, 81 Fed. Reg. at 21058.

[21] On a related note, we again urge the Department to issue guidance confirming that the audit requirement of the PPA Exemption is satisfied through an annual independent review of the advisor's controls and systems in place to comply with the PPA Exemption.

newly defined as investment advice. Congress has already determined that the PPA Exemption's conditions sufficiently protect investors receiving specific investment recommendations.[22]

Without this harmonization, an advisor that generally provides investment advice under the PPA Exemption is required to add policies and procedures to comply with the BIC Exemption with respect to distribution or rollover advice. Requiring a provider to combine two exemptions for a single investment advisory service does not serve the interests of investors. As noted above with respect to robo- and in-person advice, advisors must design investment advisory programs designed to satisfy the PPA Exemption to also meet the standards of the BIC Exemption in order to discuss rollovers or retirement distributions with clients. These exemptions require different disclosures at different points of engagement with the client, different contracts, and different oversight by internal or external parties. Comprehensive exemptions that permit an advisor to choose whether to structure all of its advice under the BIC or PPA Exemption will improve investor experience.

3. ***Plan sponsors of large and small plans should be eligible for the same services subject to the same conditions***

The Department should encourage investment advice for plans of all sizes by allowing advisors to rely on the BIC Exemption to provide fiduciary investment advice to sponsors of any size plan. Conversely, the Department should revise the definition of investment advice to allow the sponsor of any size plan to determine whether it can forego fiduciary advice because it can evaluate investment recommendations as a "sophisticated" counterparty. These changes will allow plan sponsors of all sizes to determine whether or not they need fiduciary investment advice based on their own expertise, rather than solely the assets under their control.

Generally, advisors may rely on the BIC Exemption only when providing investment advice to sponsors of plans with less than $50 million in assets. The Department excluded large plans from the BIC Exemption in an attempt to avoid weakening "the protections provided under existing law, without offsetting benefits."[23] Yet, in the very same paragraph the Department noted that investment recommendations to large plans generally would not even constitute fiduciary investment advice.[24] While we agree that large plan sponsors are generally very capable of independently evaluating investment recommendations, a large plan sponsor should be able to obtain fiduciary investment advice on equal footing with smaller plans if it determines that it needs that advice. Moreover, for large plans seeking fiduciary investment advice, there are no other exemptions designed to cover investment advice to a plan sponsor.[25]

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[22] At the time the PPA Exemption was passed, however, neither Congress nor the Department interpreted fiduciary investment advice to include rollover advice. *See e.g.*, DOL Adv. Op. 2005-23A (Dec. 7, 2005), available at https://www.dol.gov/agencies/ebsa/employers-and-advisers/guidance/advisory-opinions/2005-23a.

[23] See Preamble to the BIC Exemption, 81 Fed. Reg. at 21014.

[24] *Id.* at 21014.

[25] Prohibited Transaction Exemption 77-4, which could be used for investment advice, was designed to cover discretionary investment management services and includes conditions that do not easily carry over to an advisory service covering a participant-directed plan.

It is unlikely that expanding the BIC Exemption would weaken protections for larger plans when actual investment recommendations to large plans who do not seek fiduciary services will not require an exemption at all. Notably, the BIC Exemption includes more conditions than any other administrative exemption for investment advice or investment management. The Department has already determined under ERISA section 408(a) that the conditions of the BIC Exemption are sufficient to protect smaller plans and individual investors. There is no compelling reason why the BIC Exemption should not also be available to cover transactions with larger plans, which the Department typically views as more capable of protecting their own interests in dealing with investment and service providers. Moreover, Congress determined that all plan sponsors, regardless of plan size, have a fiduciary obligation to either possess the requisite expertise to evaluate potential plan investments and services or obtain such expertise based on their evaluation of their capabilities and needs, which do not conform to plan size. The Department should rely on this statutory construct and not attempt to create different standards based on size.

Without these changes, the Rule will either limit the information that is available to small plans or will force those plans to engage a fiduciary investment advisor at increased cost. Removing size constraints will also benefit smaller plans by allowing them to retain their advisors as their assets grow. For large plans, the Rule will limit access to fiduciary investment advice from any advisor who needs to rely on an exemption, because without the BIC Exemption, there is no exemption that is designed to permit fiduciary investment advice to large retirement plan sponsors. For plans that change from small to large or vice versa, the Rule will complicate compliance and confuse plan sponsors seeking services any time the plan moves across the arbitrary line between small and large status. Ultimately, this aspect of the Rule harms Retirement Investors in retirement plans of any size. A BIC Exemption that is available consistently across a plan's life cycle would better serve plan sponsors.

C. The Department should significantly simplify the BIC Exemption by limiting it to the Impartial Conduct Standards and removing the Exemption's provisions encouraging litigation

The Department can effectively address conflicts of interest and promote broader availability of fiduciary advisory services by substantially simplifying the conditions of the BIC Exemption. Specifically, the Department should limit its requirements to an enforceable commitment to the Impartial Conduct Standards and remove provisions encouraging enforcement through litigation in state courts. The conditions of the BIC Exemption are complex and unnecessary, provided that it continues to apply the Impartial Conduct Standards. This complexity, combined with the threat of litigation in state courts that are unfamiliar with ERISA, can serve to limit advisors' willingness to provide advice and is likely to increase costs for those who do obtain advice.

The BIC Exemption could promote greater access to fiduciary investment advice if it limited its requirements to the core requirements reflected in the Impartial Conduct Standards, as follows:

- When providing investment advice to a Retirement Investor, the advisor must provide investment advice that is in the best interest of the Retirement Investor;

- The terms of the arrangement, including compensation, may not be unreasonable under the circumstances; and
- The advisor's statements about any matters relevant to a Retirement Investor's investment decision may not be misleading.

This simplified approach would better reflect the Department's stated objective of adopting a principles-based exemption.[26] A principles-based approach can better adapt to new business models and advances in retirement products and services, and improves harmonization with other exemptions the Department has amended to include the Impartial Conduct Standards.[27]

Further, this approach would eliminate the Department's reliance on litigation as a primary means of enforcement by removing the contract and warranty requirements. The BIC Exemption's unprecedented requirement that any person seeking to rely on it agree to class-action litigation in state court to enforce the requirements of the Exemption is a significant deterrent to its use. This condition is not found in any other prohibited transaction exemption, and the Department's rationale for its approach in the BIC Exemption is unconvincing. Under a revised BIC Exemption that is focused on the Impartial Conduct Standards, advisors would be required to act in the best interests of the Retirement Investor and refrain from providing any investment advice that would lead to the advisor, its affiliates and the financial institution receiving more than reasonable compensation. These conditions are more than sufficient to protect Retirement Investors. By turning over enforcement to the state courts, the Department would threaten the long-standing principle of ERISA preemption, which fosters the stability and uniformity upon which the voluntary employee benefit plan system depends. Using state courts as an enforcement mechanism would encourage frivolous lawsuits, driving costs up and turning interpretation of the exemption's complex conditions and the definition of fiduciary investment advice over to the uncertainty of a patchwork of litigation pursued through state courts.

In our experience, financial institutions already expend significant resources on compliance with the Department's existing exemptions to avoid these consequences, and consistency in the interpretation and enforcement of the prohibited transaction rules is critical to their efforts. In doing so, financial institutions need the certainty that can come only from dealing with a single expert regulator on questions of interpretation and compliance that applies on a national basis. The prohibited transaction rules under ERISA, the severe tax penalties imposed under the Internal Revenue Code for violations and the reputational consequences of prohibited transaction failures have long served as powerful incentives for financial institutions and their representatives to comply with the substantive conditions of any exemption.

Our own experience is relevant to this point. Vanguard offers investment advice to IRA investors through Vanguard Personal Advisory Services ("PAS"). PAS is currently designed to operate in accordance with the PPA Exemption. Notably, Vanguard's PAS offer is not available to ERISA plans or participants at this time. Nevertheless, Vanguard has expended considerable resources to

[26] *See, e.g.*, Preamble to the BIC Exemption, 81 Fed. Reg. at 21002-3.
[27] 81 Fed. Reg. at 21139 et seq.

operate PAS in accordance with the PPA Exemption, despite the absence of litigation as a means of enforcement.

D. The Rule should closely align with other regulatory frameworks to harmonize investor experience across different types of accounts and rationalize compliance

Vanguard continues to support the creation of a consistent fiduciary standard for individualized investment advice provided with respect to specific investments to any Retirement Investor, regardless of account type. Vanguard appreciates the Department's efforts to reflect existing guidance from FINRA and the SEC in its development of the Rule. As the Department reviews the Rule, we encourage coordination between and among the Department, the SEC and FINRA as each moves forward with fiduciary guidance. Because investors benefit from a consistent experience regardless of account type, each agency should strive to apply consistent principles wherever possible. Adopting the principles-based approach we outlined above would make harmonization possible.

At the same time, we agree that the benefits of the Rule should not be delayed by the lack of consensus among other regulators about fiduciary status or who should act first, for which accounts, through what mechanism. The Department should move forward with the Rule, taking care to remove unnecessary obstacles that complicate compliance and access to investment advice, education and information, as we have outlined in this letter. The authority of other regulators is generally tied to the type of investment products a provider offers, rather than the type of investor served. As a result, no other single regulator can "act first" in a way that comprehensively protects Retirement Investors. Throughout the Department's consideration of the Rule, some have suggested that the Department should wait for the SEC to adopt a fiduciary standard for broker-dealers, but the SEC does not regulate all investments that may be held by Retirement Investors (such as traditional annuity contracts or bank products that may be regulated by other state and federal authorities). Waiting for a consensus to develop among all interested regulators will threaten development of any standard. The Department, as the single regulator that can govern all Retirement Investors, should move forward with the Rule. It must do so, however, by adopting the modifications we have outlined. Without these changes, Retirement Investors will have less access to retirement products and services, and those that remain available will be costlier, more complex and more fragmented.

IV. The Market Continues to Evolve, and the Department's Cost-Benefit Analysis Must be Updated

As the Department evaluates the potential costs and benefits of a delay in the Rule, we ask the Department to recognize the extent to which the industry has changed over the past year and continues to evolve to deliver better solutions to investors. These changes suggest that – as directed in the Presidential Memorandum – the Rule's economic analysis must be updated, and likely overstates the potential costs of a delay in the applicability date.

The Department's implementation of the Rule in the absence of an updated economic analysis fails to accurately reflect the current costs and benefits of the Rule. For more than a decade, investors have favored low-cost funds. Over the past 15 years, equity funds with expense ratios in the lowest quartile have attracted $611 billion in assets, while funds with higher expense ratios have experienced net asset outflows. Similarly, over the past 15 years, taxable bond funds with expense ratios in the lowest quartile have attracted $871 billion in assets.[28] Asset-weighted expense ratios have dramatically declined as a result, as shown in Appendix A. Investors have been moving toward lower-cost funds for years, and the Department's economic analysis, relying on dated academic studies, does not fully reflect these effects. These reductions in cost began before the Rule was proposed, and have accelerated in the time since the Department completed its economic analysis to support the Rule, overstating the economic benefits of the Rule.

At the same time, we believe the Department underestimated the cost of interpretation, implementation and ongoing compliance with the Rule. Vanguard's business model simplified our compliance with the Rule in two respects. First, Vanguard does not compensate its employees on the basis of investments they may sell or otherwise pay commissions for investment advice. Second, Vanguard's funds do not carry loads or 12b-1 fees to pay for distribution. Those two factors removed some of the most complex interpretive and business issues from our own analysis and compliance planning in connection with the Rule. Nevertheless, Vanguard was impacted by the Rule in three divisions – those serving advisors, retirement plan sponsors and participants, and IRA investors – and collectively devoted thousands of hours to interpreting, analyzing and developing compliance plans in connection with the Rule. The magnitude of the effort required and expected in the future, if the Rule is not amended, is a signal that it is overly complex. By adopting the modifications to the Rule that we have suggested in this letter, we believe the Department could dramatically reduce these costs.

* * *

Vanguard appreciates the opportunity to submit these comments and would welcome further discussion with the Department. If there you have any questions or wish to discuss in greater detail, please do not hesitate to contact Ann Combs at 610-503-6305, John Schadl at 610-669-4011 or Stephanie Napier at 610-503-1377.

Sincerely,

F. William McNabb

F. William McNabb III
Chairman and Chief Executive Officer
The Vanguard Group, Inc.

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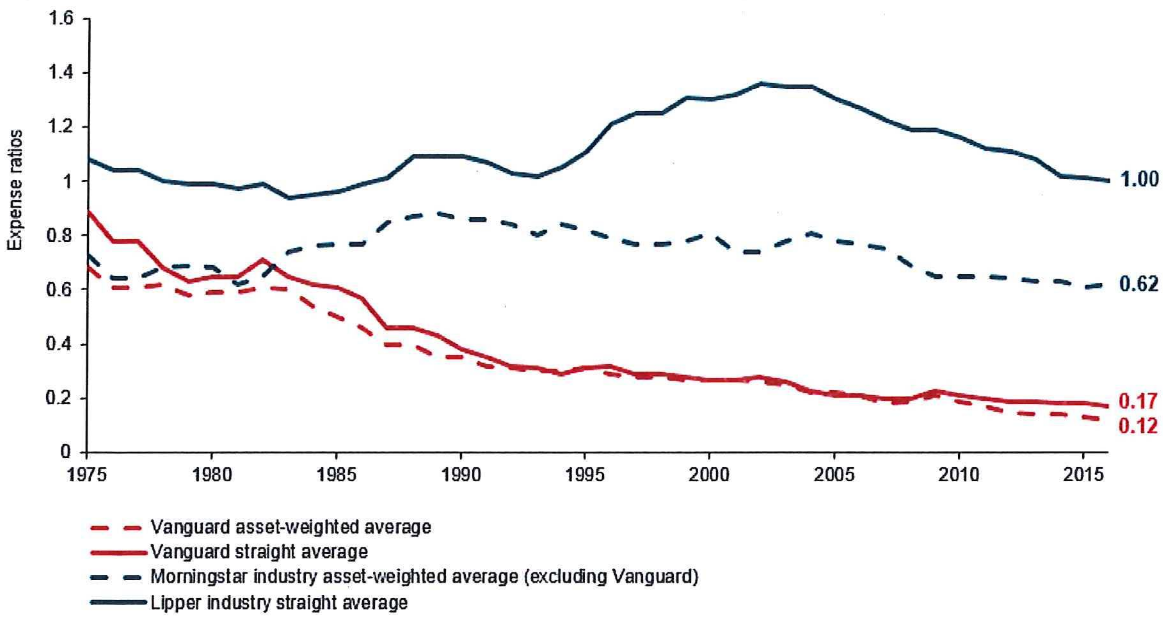
[28] *See Investors are "voting with their feet" on costs*, Vanguard Research Insight (June 2016), available at https://personal.vanguard.com/pdf/ISGIVF.pdf.

Vanguard Comment Letter
Examination of Fiduciary Rule (RIN 1210-AB79)
April 17, 2017

Appendix A: Asset-Weighted Expense Ratios

Average expense ratios (%)



Sources: Vanguard, Morningstar, Inc., and Lipper, a Thomson Reuters Company.
Note: As of 12/31/2016.