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SUBMITTED ELECTRONICALLY

April 17, 2017

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

Attention: Fiduciary Rule Examination

Re: *Definition of the Term Fiduciary – Retirement Investment Advice (RIN 1210-AB79)*

Ladies and Gentlemen:

Fidelity Investments[1] ("Fidelity") appreciates the opportunity to comment on the examination of the regulation and related prohibited transaction exemptions (the "Rule") published by the Department of Labor ("Department") concerning the definition of investment advice under section 3(21)(A)(ii) of the Employee Retirement Income Security Act of 1974 ("ERISA") and section 4975(e)(3)(B) of the Internal Revenue Code ("Code").[2] As one of the nation's leading retirement services providers, Fidelity has a deep and long-standing commitment to working with the Department on its rulemaking in the area of investment education and advice.

While we support an appropriate expansion of the range of advice activities subject to a best interest standard, the Rule adopted by the Department has fundamental flaws that must be addressed. These flaws include an overly broad definition of advice accompanied by exemptive relief that is unnecessarily burdened by onerous and complex limitations and conditions. The Rule is designed to be enforced primarily through litigation and imposes significantly greater

[1] Fidelity was founded in 1946 and is one of the world's largest providers of financial services. Fidelity provides recordkeeping, investment management, brokerage and custodial/trustee services to thousands of Code section 401(k), 403(b) and other retirement plans covering approximately 25 million participants and beneficiaries. Fidelity is the nation's largest provider of services to individual retirement accounts ("IRA") with more than 7 million accounts under administration. Fidelity also provides brokerage, operational and administrative support, and investment products and services to thousands of third-party, unaffiliated financial services firms (including investment advisors, broker-dealers, banks, insurance companies and third party administrators) that may in turn provide investment advice to plans, participants and IRA owners.

[2] *Definition of the Term "Fiduciary"; Conflict of Interest Rule – Retirement Investment Advice*, 81 FR 20946 (April 8, 2016). Capitalized terms not otherwise defined have the meaning ascribed to them in the Rule or proposed exemptions.

requirements on commission-based business models than on fee-based business models. As a result, the Rule would restrict access to the type of investment assistance that many plans, participants and IRA owners need and want to invest successfully for retirement, disrupt the retirement industry to the detriment of retirement investors, and increase litigation and costs. As outlined briefly below, all of the questions the Department has been asked to address by President Trump's Memorandum to the Secretary of Labor dated February 3, 2017, must be answered in the affirmative and therefore require the Rule to be revised or rescinded.

Given the clear need to revise or rescind the Rule, we feel compelled to comment on the manner in which the Department has approached the applicability date of the Rule.[3] We have deep concerns with the Department's decision to make the Rule applicable while it conducts the examination ordered by the February 3, 2017 memorandum. When it originally proposed the 60-day delay, the Department stated:

> Additionally, absent an extension of the applicability date, if the examination prompts the Department to propose rescinding or revising the rule, affected advisers, retirement investors and other stakeholders might face two major changes in the regulatory environment rather than one. This could unnecessarily disrupt the marketplace, producing frictional costs that are not offset by commensurate benefits. This proposed 60-day extension of the applicability date aims to guard against this risk. The extension would make it possible for the Department to take additional steps (such as completing its examination, implementing any necessary additional extension(s), and proposing and implementing a revocation or revision of the rule) without the rule becoming applicable beforehand. In this way, advisers, investors and other stakeholders would be spared the risk and expenses of facing two major changes in the regulatory environment.

By making the Rule applicable on June 9, 2017, before it has considered comments on the examination, the Department has effectively ensured the very disruption and frictional costs to retirement investors and the marketplace that the delay was designed to avoid. Plans, participants and IRA investors now run a significant risk that they will be subject to multiple changes in the investment-related services they receive over the next several months. This will result in confusion and dissatisfaction, as well as potentially increase costs to retirement investors.

The Department justifies its decision make the Rule applicable on June 9, 2017 by temporarily delaying certain conditions under applicable exemptions and by asserting that there is widespread agreement about the Impartial Conduct Standards so there is no reason to delay further the imposition of those standards. Temporary modifications to the exemptions' conditions will not avoid the disruption, confusion and cost to retirement investors that will result from serial changes to the Rule. Moreover, the issue is not with the imposition of the standards themselves but rather the overly-broad definition of investment advice that defines the conduct which is subject to the Impartial Conduct Standards. The fact is there is no widespread agreement about the scope of the definition of investment advice in the Rule and the Department offers no justification for making that definition applicable prior to conducting any of the analysis required by the February 3, 2017 memorandum.

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[3] *Definition of the Term "Fiduciary"; Conflict of Interest Rule – Retirement Investment Advice,* 82 FR 16902 (April 7, 2017).

As discussed in more detail below, the Rule is fundamentally flawed in its failure to distinguish between sales activity and advice. This flaw was the primary focus of our July 21, 2015 comment letter and we reiterate those comments today. Allowing the Rule to go into effect without addressing this flaw will create the adverse consequences that the examination is designed to address.

We suggest that the Department further delay applicability of the Rule until January 1, 2018 which is the date the Department targets for completion of its examination. If the Department decides to leave the Rule unchanged following the examination, it should then provide a period of at least 90 days following announcement of its decision to allow time for providers to comply with the Transition Period provisions of the BIC exemption and an additional nine months to comply with the full conditions of the BIC exemption. If the Rule is revised, we would expect the rulemaking process to contemplate delay of the Rule pending revision with appropriate time to comply with any modified Rule.

The Rule Should Be Revised or Rescinded

The three questions the Department has been asked to address by the February 3, 2017 memorandum require the Rule to be revised or rescinded. We keep our comments on these questions brief because affirmative responses to the questions are largely self-evident.

Whether the anticipated applicability of the final rule has harmed or is likely to harm investors due to a reduction of Americans' access to certain retirement savings offerings, retirement product structures, retirement savings information, or related financial advice

The Rule defines advice to include a communication that "would reasonably be viewed as a suggestion that the advice recipient engage in or refrain from taking a particular course of action" related to investment matters. With this overly broad definition of advice, virtually any interaction with a retirement investor runs the risk of being treated as fiduciary level advice, including both casual communications and communications in connection with the sale of investment products and services. For retirement services providers, this means that most interactions with customers must be limited to ensure that fiduciary level investment advice is only provided in situations where fiduciary due diligence requirements and conflict of interest rules, including prohibited transaction exemptions, can be met. Necessarily, this means providing investment assistance only to customers or prospective customers and only in circumstances where the economic relationship justifies the additional risk.

Fidelity believes all investors should have access to the skill and knowledge that financial services providers can provide. In anticipation of the Rule, we attempted to structure our customer interactions to preserve to the extent possible the level of investment assistance that we currently provide. However, if the Rule is not revised, there will be many situations where we could have provided valuable assistance in a non-fiduciary framework but would be unable to do so under the Rule. Reduced access to this valuable assistance will be harmful to retirement investors and negatively affect their ability to meet their retirement and other financial goals.

Whether the anticipated applicability of the final rule has resulted in dislocations or disruptions within the retirement services industry that may adversely affect investors or retirees

As noted above, Fidelity approached its Rule compliance efforts attempting to preserve to the extent possible the level of investment assistance that we currently provide. However, this has and will continue to cause very significant disruption to both Fidelity and its customers with no discernible benefit. Fidelity has dedicated thousands of hours and millions of dollars to efforts to comply with the Rule. The dedication of these resources for the purpose of preserving current services under the Rule has disrupted business plans and affected the development of additional product and service enhancements for our customers. This disruption and unwarranted expense will continue if the Rule goes into effect. In connection with our intermediary businesses, we also note that many of our clients and competitors have restructured their product and service offerings in anticipation of the Rule in ways that clearly deprive customers of choice in the way they pay for investment services.

Whether the final rule is likely to cause an increase in litigation and an increase in the prices that investors and retirees must pay to gain access to retirement services

The primary enforcement mechanism of the Rule in the IRA context is private litigation, particularly class action lawsuits. In the preamble to the Best Interest Contract Exemption, the Department explained:

> The contract between the IRA or non-ERISA plan, and the Financial Institution, forms the basis of the IRA's or non-ERISA plan's enforcement rights. The Department intends that all the contractual obligations imposed on the Financial Institution (the Impartial Conduct Standards and warranties) will be actionable by the IRAs and non-ERISA plans. Because these standards are contractually imposed, an IRA or non-ERISA plan has a contract claim if, for example, its Adviser recommends an investment product that is not in the Best Interest of the IRA or other non-ERISA plan.[4]

Similarly, the Department intended that ERISA plans and participants would help enforce the Rule through litigation:

> An Advisor's failure to comply with the exemption would result in a non-exempt prohibited transaction under ERISA section 406 and would likely constitute a fiduciary breach under ERISA section 404. As a result, a plan, a plan participant or beneficiary would be able to sue under ERISA section 502(a)(2) or (3) to recover any loss in value to the plan (including the loss in value to an individual account), or to obtain disgorgement of any wrongful profits or unjust enrichment…. The Department expects claims of Retirement Investors regarding investments in ERISA plans to be brought under ERISA's enforcement provisions, discussed above.[5]

Therefore, the Rule by design is intended to increase litigation which will result in either an increase in costs or avoidance of litigation through reduction in assistance provided to retirement

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[4] *Best Interest Contract Exemption*, 81 FR 21020 (April 8, 2016).
[5] *Best Interest Contract Exemption*, 81 FR 21021 (April 8, 2016).

investors. In a market-based system, we believe that some or all of these costs will ultimately be borne by retirement investors in the form of increased fees or reduction in services.

Fixing the Fundamental Problems with the Rule

We believe that the investment activities of firms like Fidelity are more appropriately regulated through the primary financial services regulators and that the Department's effort to create an entirely new regulatory framework for investment advice services under ERISA and the prohibited transaction provisions of the Code is misguided. However, if, following the examination of the Rule, the Department remains committed to regulatory action in this area, we believe there is a workable alternative that would better accomplish the Department's objectives. We outlined that alternative in our original comment letter on the Rule proposal submitted on July 21, 2015 (https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB32-2/00658.pdf). We will summarize the key elements of this approach in this comment letter but refer the Department to our earlier letter for additional details.

Assuming the Department decides to modify rather than simply rescind the Rule, there is a workable way to ensure that advice is provided in the investor's best interest while preserving existing business models that provide valuable assistance to retirement investors. In our earlier comment letter, we proposed a "new best interest paradigm" that addresses the two foundational problems with the Rule – the overly broad definition of investment advice under the Rule and the limitations and conditions of the BIC Exemption which make it ineffective in addressing the prohibited transaction problems created by the overly broad advice definition. Having spent more than two years closely analyzing, interpreting and applying first the proposal and then the final Rule, we continue to believe that our new best interest paradigm would yield greater benefits to retirement savers and providers at less cost and would be a superior approach to rulemaking if the Department remains committed to regulatory action in this area.

The fundamental problem with the overly broad definition of investment advice under the Rule is that it conflates two separate acts – an investor's engagement of an advisor[6] to provide advice and the advisor's recommendation of investment products and services pursuant to such engagement – and treats both as a single "recommendation" subject to fiduciary conduct standards. By so doing, the rule proposal makes an advisor a fiduciary with respect to establishment of its own services and compensation. This is both unprecedented in fiduciary law and not commercially viable, potentially requiring an advisor to recommend its competitors over itself even in cases where its own services are wholly appropriate for the investor.

The Rule attempts to deal with this problem in part through a limited seller's exclusion for sophisticated fiduciaries, including certain large plans. While we believe the exclusion approach makes sense for true sales activity and should be applied to all investors in that context, the exclusion is an "all or nothing" approach. When it applies, neither the sale of the advisor's

[6] We generally use the term "advisor" to refer to both the regulated financial institution and/or its individual representative, but provide greater specificity where the context requires.

own services nor the advisor's actual investment recommendations would be held to a fiduciary standard. Because the best interest standard does not apply to the actual investment recommendation when the exclusion applies, the exclusion defeats the purpose of the Rule. Thus, the Department's proposal either imposes a fiduciary duty on the sale of an advisor's own services (where it does not belong) or removes a fiduciary standard with respect to an investment recommendation (where it does belong). We refer to this as the "sales dilemma" that is created by the Rule. Notably, the Rule creates this dilemma not only with respect to advisors with transaction-based compensation but also for advisors selling fee-based advisory services with an extremely limited exception for "hire me" discussions.

This dilemma can be avoided by separating the advisor's establishment of its own services and compensation – which are always conflicted components of the relationship – from the actual recommendations about investment products and services. These are inherently distinct activities subject to fundamentally different duties. Following appropriate disclosure, an investor would agree to the scope of the advice to be provided, the amount of compensation payable to the advisor in connection with an investment recommendation or over a range of recommendations, restrictions on the advice (such as limitations to proprietary products or products that generate revenue sharing), and other terms and conditions of the engagement. The investor's agreement with respect to the service and compensation terms would be established at arm's length outside of the fiduciary relationship, as it historically has been in every comparable fiduciary context. Once the terms of the engagement are established, all investment recommendations within that framework must be in the investor's best interest.

It is important to note that this approach of separating the terms of the engagement from the actual investment recommendation would not apply solely at the initiation of the advisory relationship. It would also apply whenever the terms of the engagement were later renegotiated by the parties, or if even they were established on a transaction-by-transaction basis.

This approach of separating the terms of the engagement from the actual investment advice is conceptually identical to a long-standing regulation of the Department addressing application of the prohibited transaction exemption under ERISA section 408(b)(2) for payment of service providers. This regulation provides that if a person who is already providing investment advice to a plan "persuades" a plan fiduciary to extend his contract at a higher fee, the advisor has not engaged in a prohibited transaction because the advisor has not used any of the authority, control or responsibility which makes it a fiduciary to cause the plan to pay an additional fee. There is no reason why this concept should not apply where the advisor's compensation varies based on the transactions and services recommended by the advisor, or to other limitations and conditions on the scope of the advisor's services.

The second foundational problem with the proposal is that its proposed exemption structure is laden with complex limitations and unnecessary conditions which narrow both the scope and practicality of the exemptions and make them unworkable. Most of this problem can be solved by implementing a broad, principles-based approach to exemptions for regulated financial institutions that act in the investor's best interest. Notably, the Department follows this approach through the "Impartial Conduct Standards" that are proposed as amendments to several existing exemptions in other parts of the rule proposal. For example, the Department has proposed this approach in the amendments to PTE 77-4 which allows a discretionary manager to invest in its own proprietary mutual funds – often cited as one of the most conflicted transactions for an advisor. If this simple, straightforward approach is sufficiently protective of the interests of plans, participants and IRA owners in the context of a discretionary investment manager, it is certainly sufficient in the context of nondiscretionary advice.

In fact, the Department has already acknowledged the sufficiency of this approach in its final rule adopting a 60-day extension of the Rule's applicability date. In connection with the adoption of the delay, the Department indicated that while the Rule will become applicable on June 9, 2017, all conditions of the BIC exemption other than the Impartial Conduct Standards will be deferred until January 1, 2018. The stated reason for this approach is that the imposition of the Impartial Conduct Standards alone will avoid the losses that retirement investors would have otherwise incurred by a longer delay. If that is the case, then the additional costs involved in complying with the requirements that are scheduled to take effect on January 1, 2018 are unnecessary because they are not required to obtain the benefits that the Rule purports to achieve. In other words, the Department's approach to the examination of the Rule undercuts any prior justification it had for the additional requirements of the BIC exemption beyond the Impartial Conduct Standards. If the Impartial Conduct Standards alone effectively avoid investor losses and preserve their investment gains between June 9, 2017 and January 1, 2018, then the significant additional disclosure and other requirements that are scheduled to become effective on January 1, 2018 cannot be justified.

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We would be pleased to respond to any questions or comments regarding this letter.

Sincerely,

Ralph C Derbyshire

Ralph C. Derbyshire

cc: **United States Securities and Exchange Commission**
The Honorable Michael S. Piwowar, Acting Chair
The Honorable Kara M. Stein, Commissioner

Financial Industry Regulatory Authority
Robert Cook, Chairman and Chief Executive Officer, FINRA
Robert Colby, Chief Legal Officer, FINRA