

July 21, 2015

Submitted Electronically – e-ORI@dol.gov and e-OED@dol.gov

Office of Regulations and Interpretations
Office of Exemption Determinations
Employee Benefits Security Administration
U.S. Department of Labor
200 Constitution Ave., NW
Washington, DC 20210

**Re: Definition of the Term “Fiduciary” (RIN 1210-AB32);
Best Interest Contract Exemption (ZRIN 1210-ZA25)**

Ladies and Gentlemen:

NorthStar Asset Management Group Inc. submits the following comments regarding the rule proposed by the U.S. Department of Labor (the “Department”) which would redefine who is a “fiduciary” by reason of providing investment advice for a fee or other compensation (the “Proposed Rule”) and the related proposed Best Interest Contract Exemption (the “BIC Exemption”).¹

NorthStar Asset Management Group Inc., including its predecessor (“NSAM”), through its global network of subsidiaries and branch offices, provides asset management and other services to both traded and non-traded public companies. As a proven institutional manager with approximately \$24 billion of real estate assets under management and a long-term track record of creating value for shareholders, NSAM has always supported actions that enhance transparency and protections for investors. As such, NSAM supports the Department’s goal of ensuring that financial advisors put the best interests of retirement plans, plan participants and IRA owners first. NSAM has consistently supported practices that provide investor protections and transparency, and favors promoting these goals through appropriate updates to regulations governing retirement plans (including IRAs). However, NSAM has a number of specific concerns about the negative effect the Proposed Rule and the BIC Exemption would have on the availability of quality investments, like publicly registered, non-listed real estate investment trusts (“Non-Listed REITs”) and publicly registered, non-listed business development companies (“Non-Listed BDCs”), used by IRA owners and participants to diversify their retirement portfolios and achieve their investment objectives.

NSAM is a member of the Investment Program Association (“IPA”) and the National Association of Real Estate Investment Trusts (“NAREIT”) and concurs with (i) the comment letter submitted to the Department by the IPA with respect to Non-Listed REITs and Non-Listed BDCs (the “IPA Letter”), and (ii) the comment letter submitted to the Department by NAREIT’s Public Non-Listed REIT Council.

¹ See Proposed Conflict of Interest Rule, 80 Fed. Reg. 21960 (proposed Apr. 20, 2015 (to be codified at 29 C.F.R. pt. 2550); and Proposed Best Interest Contract Exemption, 80 Fed. Reg. 21960 (proposed Apr. 20, 2015 (to be codified at 29 C.F.R. pt. 2550).

NSAM writes separately to highlight particular concerns with the scope of the Proposed Rule and the proposed BIC Exemption as they relate specifically to NSAM's businesses.

I. About NorthStar Asset Management Group Inc.

NSAM (NYSE: NSAM) is a publicly traded leading global asset management firm focused on strategically managing real estate and alternative investment platforms in the United States and internationally. NSAM has been an active participant in the retail marketplace since 2009 and its affiliates currently manage four Non-Listed REITs, which own portfolios of debt and equity investments in the commercial real estate industry. NSAM has also submitted a registration statement to the U.S. Securities and Exchange Commission ("SEC") to co-manage a Non-Listed BDC. NSAM's Non-Listed REITs and its Non-Listed BDC are or will be distributed by NSAM's captive broker-dealer subsidiary, NorthStar Securities, LLC. Collectively, the Non-Listed REITs and Non-Listed BDC currently sponsored by NSAM, are targeting approximately \$8 billion of equity capital raise, which is anticipated to be invested in approximately \$15 billion of assets. NSAM is actively developing new products for the retail and institutional markets, and expects to launch these sponsored companies in the near future.

NSAM was founded in 2004 and currently has approximately 240 employees located domestically and internationally. The members of NSAM's management team average over 20 years of investment and capital markets experience and have demonstrated a track record of generating positive returns to stockholders. As of May 2015, stockholders in NorthStar Realty Finance Corp. (NYSE: NRF) (which has approximately \$19 billion of assets), have received compounded annual returns of over 20% since its initial public offering in 2004. Additionally, NSAM's senior executive team has a significant amount of experience operating publicly registered companies, including expertise in initial and secondary offerings, public company reporting, internal controls and risk management, legal and regulatory compliance, stock exchange requirements, fund management and operations.

Since NSAM's commencement of capital raising for its first sponsored Non-Listed REIT in July 2010 through March 31, 2015, the companies sponsored by NSAM have raised approximately \$3 billion in equity capital from over 59,000 individual accounts which has been invested in approximately \$6 billion of assets. Approximately 43% of the invested capital has come from individual retirement accounts ("IRAs") subject to the Employee Retirement Income Security Act of 1974 ("ERISA") and/or the Internal Revenue Code ("Code"). Since inception, the NSAM-sponsored Non-Listed REITs have made regular monthly distributions to investors aggregating approximately \$340 million, at an average rate of 7.5% based on the \$10.00 gross purchase price per share of the common stock. To date, 100% of the redemption requests made by investors in all NSAM-sponsored Non-Listed REITs have been satisfied.

In addition to providing consistent distributions on a monthly basis to investors and fully satisfying redemption requests, NSAM's sponsored REITs have demonstrated strong performance through their respective investment portfolios. As an example, NorthStar Real Estate Income Trust, Inc. ("NorthStar Income"), the first Non-Listed REIT sponsored by NSAM, established and publicly disclosed an estimated value per share of its common stock after the termination of its continuous public offering pursuant to a valuation conducted by a third-party independent valuation and consulting firm of \$10.02 as of October 31, 2014. NorthStar Income provided this estimated value per share to assist broker-dealers that participated in NorthStar Income's offering in meeting their customer account statement reporting obligations as required by the Financial Industry Regulatory Authority, Inc. ("FINRA").

II. The Scope and Potential Impact of the Proposed Rule Requires Further Consideration and/or Clarification.

As noted above, NSAM has consistently supported practices that provide investor protections and transparency. However, NSAM is concerned that, given its broad (and largely undefined) scope, the Proposed Rule may potentially create significant regulatory compliance concerns and uncertainty where none has existed before. NSAM maintains that there has been no specific demonstration that the existing regulation, coupled with extensive regulation of investment advisors under the securities laws, does not provide ample protection to retirement investors. The comment letter recently submitted to the Department by FINRA well underscores this point. Moreover, such a broad redefinition of fiduciary investment advice under ERISA and the Code will have a massive, and largely unpredictable, impact on economic expectations that have settled over the past 40 years under the existing regulation. At a minimum, such sweeping changes require a much longer time period to consider the interrelation with existing regulations under the securities laws and the likely impact on investors as well as other constituencies related to this industry.

III. The BIC Exemption Should Be Modified.

NSAM supports updates to regulations relating to retirement plans, including IRAs, to provide adequate investor protections and promote transparency. NSAM, however, believes that the Department's goal of protecting the interests of retirement investors will only be hindered by the creation of a "legal list" of "Assets" eligible for the BIC Exemption and such list is inconsistent with ERISA's previously stated goals and the current language in the Proposed Rule. Nevertheless, if the Department determines that maintaining a "legal list" is appropriate, NSAM respectfully requests that the Department include Non-Listed REITs and Non-Listed BDCs on that list given their common use, investor demand, performance and structure.

A. The Department Should Reject the Concept of a Legal List.

As discussed in the IPA letter, given the dynamics of the investment marketplace, it is unwise to attempt to capture at a specific point in time a list of investment products eligible for prohibited transaction exemptions. Attempts to require trustees to select investments from a statutory list of investments ("legal lists") have not been successful. Prior to the Great Depression, many states had such requirements, but experience has highlighted the advantages of a more flexible approach. Indeed, this history led the drafters of Restatement (Third) of Trusts to conclude that "[k]nowledge, practices, and experience in the modern investment world have demonstrated that arbitrary restrictions on trust investments are unwarranted and often counterproductive."²

The Department itself has previously recognized that it is not appropriate "to include in the regulation any list of investments, classes of investment, or investment techniques that might be permissive under the 'prudence' rule. No such list could be complete; moreover, the Department does not intend to create or suggest a 'legal list' of investments for plan fiduciaries."³ In the preamble to the proposed BIC Exemption, the Department emphasized that it intended to adopt a "principles-based" or "standards-based" approach that "would flexibly accommodate a wide range of current business

² Restatement (Third) of Trusts, Ch. 17, Investment of Trust Funds (Introductory Note, Edward C. Halbach, Jr., Reporter); *See, also*, Jeffrey N. Gordon, *The Puzzling Persistence of the Constrained Prudent Man Rule*, 62 N.Y.U.L. REV. 52 (1987).

³ 44 Fed.Reg. 31639 (June 1, 1976).

practices” while minimizing conflicts of interest.⁴ Maintaining a “legal list” will restrict access to current and future products that have been, or may be, beneficial for ERISA accountholders. As discussed in the IPA letter, Non-Listed REIT and Non-Listed BDC programs have become “common” retail securities for IRA investments; for instance, of the \$21.1 billion invested in direct participation programs including Non-Listed REITs and Non-Listed BDCs in 2014 alone, 43% was invested by IRA accounts. Moreover, such products provided over \$5.9 billion of income distributions to investors in 2014, of which over \$2.5 billion went to IRA accounts.

The BIC Exemption has ample disclosure requirements and investor protections to allow for an open-ended number of investments. For example, the BIC Exemption explicitly requires disclosure of information relating to fees, compensation and material conflicts of interest. The BIC Exemption also requires a contractual agreement to adhere to impartial conduct standards, and the adoption of policies and procedures designed to mitigate material conflicts of interest. BIC contracts would be subject to judicial enforcement. It does not make sense to preclude certain investment products from such additional robust investor protections and disclosure requirements.

B. The Set of Assets Eligible for the BIC Exemption Should Include Non-Listed REITs and Non-Listed BDCs.

If the Department determines to proceed with a “legal list” of investments eligible for the BIC Exemption, the definition of “Assets” in such exemption should be expanded to include Non-Listed REITs and Non-Listed BDCs. First, as discussed extensively in the IPA letter, Non-Listed REITs and Non-Listed BDCs are already subject to extensive federal and state regulations that are sufficiently protective of investor interests as to warrant inclusion as Assets eligible for the BIC Exemption. Moreover, Non-Listed REITs and Non-Listed BDCs have a number of favorable attributes, including strong current income and low correlations to capital markets, which make them appropriate for inclusion in a well-diversified retirement portfolio. In addition, Non-Listed REITs and Non-Listed BDCs provide investors with best-in-class sponsors and asset managers, like NSAM, that might normally only be available to institutional and high net worth investors.

1. Non-Listed REITs and Non-Listed BDCs Are Subject to Even More Robust Regulation than Exchange-Listed Securities.

Non-Listed REITs are subject to the same IRS requirements as exchange-listed REITs, including the requirement that they distribute at least 90% of taxable income to shareholders annually. Also, like exchange-listed REITs, offers and sales of interests in Non-Listed REITs are registered with the SEC under the U.S. Securities Act of 1933, as amended (the “1933 Act”). In addition, like exchange-listed REITs, Non-Listed REITs must file with the SEC (and make publicly available) periodic and current reports, such as Forms 10-Q, 10-K and 8-K, as well as proxy statements, filed pursuant to the U.S. Securities Exchange Act of 1934, as amended (the “1934 Act”). The primary difference between the regulation of exchange-listed and Non-Listed REITs is that exchange-listed REITs are subject to the corporate governance and other requirements of the stock exchanges whereas Non-Listed REITs are subject to the corporate governance and other requirements imposed by state securities regulators, which generally follow the North American Securities Administrators Association (“NASAA”)’s Statement of Policy Regarding Real Estate Investment Trusts (the “NASAA REIT Guidelines”).⁵ In order to offer and sell their interests to the public, Non-Listed REITs must register and be approved for sale by the

⁴ Proposed BIC Exemption, at 21961.

⁵ See <http://www.nasaa.org/wp-content/uploads/2011/07/g-REITS.pdf>.

respective securities divisions of each state and U.S. territory in which offers and sales of the interests will be made and become subject to the NASAA REIT Guidelines.

The state specific regulations to which Non-Listed REITs are subject provide significant additional protection to investors that are not applicable to securities offerings of exchange-listed companies. For example, like exchange-listed REITs, Non-Listed REITs must have boards of directors that are comprised of a majority of independent directors and those boards act in a fiduciary capacity with respect to stockholders.⁶ Non-Listed REITs are subject to additional fiduciary requirements including an express fiduciary duty of the external manager to the REIT and its stockholders, and an additional fiduciary duty of the independent directors to stockholders to supervise the relationship of the Non-Listed REIT with its external manager. Further, the NASAA REIT Guidelines impose significant limitations on the types of investments a REIT can make, the fees and expenses it can pay, the level of its borrowings and the indemnification it can provide its directors and external manager, among others.⁷ Moreover, like exchange-listed REITs, Non-Listed REITs and Non-Listed BDCs, and their boards of directors, are also subject to strict corporate governance and conflict of interest requirements aimed at ensuring transparency and fairness in operations and communications with investors.

As an additional layer of investor protection, approximately 40 states apply a “merit review” approach to the registration of Non-Listed REIT securities offerings, wherein such states may review a registration statement for a securities offering, and make a determination regarding its fairness to investors. If a state securities regulator is not satisfied with the “fairness” of an offering, the regulator can refuse to declare the registration statement effective in that state. There are varying degrees of merit regulation, with some states applying stricter standards than other states.

Non-Listed BDCs are subject to certain provisions of the U.S. Investment Company Act of 1940, as amended (the “1940 Act”). Non-Listed BDCs are also subject to certain provisions of the 1933 Act,⁸ and 1934 Act.⁹ Investment advisers to Non-Listed BDCs are subject to the U.S. Investment Advisers Act of 1940 (the “Advisers Act”), which includes a statutory fiduciary duty. Under the 1940 Act, Non-Listed BDCs are subject to regulations governing, among other things, portfolio composition, director qualifications and independence, limitations on transactions with affiliates, bonding, capital structure, the approval of underwriting and advisory agreements and distributions to investors.¹⁰ In addition to federal regulations, Non-Listed BDCs are required to register with the state securities commissions or divisions of each of the states and U.S. territories in which the Non-Listed BDC publicly offers its shares. Although regulations may vary from state-to-state, many states have modeled their regulations after guidelines adopted by NASAA. NASAA’s Omnibus Guidelines¹¹ address, among other things: Non-Listed BDC sponsor financial condition,¹² the reasonableness of fees to the Non-Listed BDC’s external

⁶ See e.g., NASAA’s Statement of Policy Regarding Real Estate Investment Trusts at Section I.B.14; available at: <http://www.nasaa.org/wp-content/uploads/2011/07/g-REITS.pdf>. NASAA defines an independent director (or, in the context of a Non-Listed REIT that is in the form of a trust, an independent trustee) as: persons “who are not associated and have not been associated within the last two years, directly or indirectly, with the sponsor or advisor of the [Non-Listed] REIT.”

⁷ *Id.* at Section II.D and E.

⁸ See, e.g., the 1933 Act, available at: <http://www.sec.gov/about/laws/sa33.pdf>.

⁹ See, e.g., the 1934 Act, available at: <http://www.sec.gov/about/laws/sea34.pdf>.

¹⁰ See, e.g., Section 57 of the 1940 Act.

¹¹ NASAA has not yet developed specific guidelines for Non-Listed BDCs. However, Non-Listed BDCs are subject to NASAA’s Omnibus Guidelines, available at: http://www.nasaa.org/wp-content/uploads/2011/07/f-Omnibus_Guidelines.pdf.

¹² For a detailed discussion of the different factors related to the computation of the sponsor’s required net worth, see, for example, the NASAA Omnibus Guidelines, at Section II.B.

manager and Non-Listed BDC expenses, conflicts of interest, investment restrictions, and shareholder voting rights. Moreover, both a Non-Listed BDC and its external manager are subject to periodic SEC audits to determine compliance with the 1940 Act and Advisers Act, respectively, and under which the SEC is empowered to bring enforcement proceedings for any actions or omissions that it determines to be violations thereunder.¹³ Finally, the “merit review” utilized by approximately 40 states with regard to the registration of public offerings of Non-Listed REITs also applies to the registration of public offerings of Non-Listed BDCs, providing an additional layer of protection to investors.

Moreover, the primary channel used to distribute Non-Listed REITs and Non-Listed BDCs is through broker-dealers that are registered with the SEC, FINRA, and the relevant state securities regulatory authorities. Federal law and FINRA rules require brokers to “adhere to high standards of conduct in their interactions with investors.”¹⁴ The suitability requirements of FINRA Rule 2111 and the FINRA Rule 2310(b)(2)¹⁵ mandate that broker-dealers have a reasonable basis to believe that a recommended investment in Non-Listed REIT or Non-Listed BDC securities is suitable for each customer based on reasonable diligence¹⁶ into the investor’s investment profile. In addition, state securities laws impose their own suitability standards and income and net worth requirements. The sponsor of a Non-Listed REIT or Non-Listed BDC, and those selling shares on its behalf, including participating broker-dealers and registered investment advisers recommending the purchase of such shares, must make every reasonable effort to determine that the purchase of shares in a particular offering is a suitable and appropriate investment for each investor based on information provided by the investor regarding the investor’s financial situation and investment objectives.

Broker-dealers offering investments in Non-Listed REITs or Non-Listed BDCs are also subject to additional product-specific disclosure requirements pursuant to FINRA Rule 2310. Prior to investing, Section (b)(3) of the Rule requires “that all material facts are adequately and accurately disclosed [to offerees] and provide a basis for evaluating the program.”¹⁷ In determining the adequacy of disclosure, FINRA sets minimum guidelines for broker-dealers, such as: “(i) items of compensation; (ii) physical properties; (iii) tax aspects; (iv) financial stability and experience of the sponsor; (v) the program’s conflicts and risk factors; and (vi) appraisals and other pertinent reports.”¹⁸ Moreover, FINRA Rule 2310 stipulates that a broker-dealer may not sell a publicly registered direct participation program or Non-Listed REIT security unless the issuer agrees to provide a valuation in its annual report (or other public filing). Recent changes to FINRA Rule 2340 will impose additional transparency requirements for Non-Listed REITs and Non-Listed BDCs relating to the reporting of their values on customer account

¹³ See Section 42 of the 1940 Act and Section 209 of the Advisers Act.

¹⁴ See, e.g., Securities and Exchange Commission, Study on Investment Advisers and Broker-Dealers at 13 (Jan. 2011), available at: <http://sec.gov/news/studies/2011/913studyfinal.pdf>.

¹⁵ Investment advisers, whether or not they are registered, are subject to their own fiduciary duty standards. See, e.g., FINRA Rule 2111 and FINRA Regulatory Notice 11-02, available at: http://finra.complinet.com/en/display/display_viewall.html?rbid=2403&element_id=9859&print=1.

¹⁶ For example, broker-dealers have a duty to “to conduct reasonable investigation of securities, including those sold in a Regulation D offering. See, e.g., FINRA Regulatory Notice 10-22, available at: <http://www.finra.org/industry/notices/10-22>.

¹⁷ See, e.g., Disclosures for Direct Participation Programs, which includes REITs discussed herein, Section (b)(3)(A) of FINRA Rule 2310, available at: http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=8469.

¹⁸ See, e.g., Disclosures, Section (b)(3)(B)(i)-(vi) of FINRA Rule 2310.

statements and requiring the material involvement and confirmation of such reported values by valuation experts.¹⁹

Thus, Non-Listed REITs and Non-Listed BDCs are subject to extensive federal and state regulation, and the brokers-dealers and investment advisers who offer these products to their clients are also heavily regulated. These regulations are even more rigorous than those applicable to many of the products included in the current “legal list.” If the Department is going to add regulatory oversight under ERISA and the Code when these products are sold to retirement plans, it should include these products in the BIC Exemption. Doing so would provide investors the full panoply of protections available under the Proposed Rule and the BIC Exemption, as well as the robust securities law protections already in existence. Providing retirement plan investors effective access to Non-Listed REITs and Non-Listed BDCs will provide such investors with more diversification options, as well as adequate protections, disclosure and oversight.

2. Non-Listed REITs and Non-Listed BDCs are Appropriate Investments for Retirement Plans.

As accurately described in the IPA Letter, Non-Listed REITs and Non-Listed BDCs are transparent, widely held investments that have a strong performance history, relatively low volatility and significant diversification advantages. Also as described in the IPA Letter, Non-Listed REITs have shown a lower correlation to public equity markets than listed REITs, and, as a result, Non-Listed REITs provide even better diversification against market volatility. NSAM, a sponsor of both exchange-listed REITs and Non-Listed REITs, is in a unique position to understand these intrinsic benefits. The fact that a particular REIT is not listed on a securities exchange also provides a degree of protection against adverse market sentiment, insulating investors from equity market fluctuations, and as history has demonstrated, Non-Listed REITs are typically less volatile than exchange-listed REITs.

Exchange-listed REITs provide greater liquidity than Non-Listed REITs, but each can have its own role in a diversified portfolio, and a reasonable investor may choose to have exposure to both investments. Non-Listed REITs typically have provisions that permit redemptions subject to certain limitations prior to the date the Non-Listed REIT provides full liquidity to investors upon the consummation of a liquidity event (such as a stock exchange listing, sale or merger with an exchange-listed company). In fact, none of the NSAM-sponsored Non-Listed REITs has ever declined an investor’s request for redemption. In addition, retirement plan investments are typically long-term investments in which immediate liquidity needs are generally limited.

Non-Listed REITs and Non-Listed BDCs invest in a broad array of asset classes, including commercial office, industrial, retail, hotels, healthcare and the debt secured by such assets. Debt-focused Non-Listed REITs (for which NSAM is the leading market sponsor) and Non-Listed BDCs can act in certain respects like fixed income substitutes because they provide current income with more downside protection than equity-focused investments. Direct investments in real estate assets can also provide a superior hedge against inflation and rising interest rates compared to most fixed income investments which do not provide for any potential appreciation of the capital invested, and which also offer limited liquidity. Inflation is a significant risk to retirement income and the purchasing power of saving. Unlike bond and fixed income portfolios where the purchasing power of invested capital can be eroded by inflation, asset-based direct investments, like Non-Listed REITs, can provide capital protection through

¹⁹ See FINRA Regulatory Notice 15-02 (discussing how amended NASD Rule 2340 will provide two different options for calculating estimated per share values of products, such as Non-Listed REITs and Non-Listed BDCs, on customer account statements). Available at: http://www.finra.org/sites/default/files/notice_doc_file_ref/Notice_Regulatory_15-02.pdf.

appreciation of value of the assets induced by inflation. Accordingly, direct investments in real estate have been a fundamental component of the investment portfolios of institutional pension plans and endowments for years.

Excluding Non-Listed REITs and Non-Listed BDCs from the BIC Exemption altogether limits the diversification, inflation hedging, downside protection, lower volatility and income options available to retirement plan investors that research and analysis has proven enhances overall returns as well as reduces risk. The Department should include Non-Listed REITs and Non-Listed BDCs as Assets eligible for the BIC Exemption and thus retain these important investment strategies that are currently available and widely used by the public for prudent retirement investing.

IV. Conclusion.

For the reasons discussed above, if the Department determines to adopt the Proposed Rule, NSAM believes that the BIC Exemption should be modified to eliminate any legal list of investment options. If the Department determines to maintain such a list, NSAM believes that it is essential to modify the list to include Non-Listed REITs and Non-Listed BDCs.

Sincerely,



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