

PUBLIC SUBMISSION

As of: September 28, 2015
Received: September 24, 2015
Status: Pending_Post
Tracking No. 1jz-8lba-42bt
Comments Due: September 24, 2015
Submission Type: Web

Docket: EBSA-2010-0050

Definition of the Term ‘Fiduciary’; Conflict of Interest Rule—Retirement Investment Advice; Notice of proposed rulemaking and withdrawal of previous proposed rule.

Comment On: EBSA-2010-0050-0204

Definition of the Term Fiduciary; Conflict of Interest Rule- Retirement Investment Advice

Document: EBSA-2010-0050-DRAFT-7955

Comment on FR Doc # 2015-08831

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General Comment

I have commented briefly already on this proposed rule but would like to add a copy of an outside interpretation that explains the basis for my concerns:

But the portion that really worries us falls under the provision titled the "Best Interest Contract Exemption," or "BICE." In particular, the provision's executive summary states the following (emphasis added):

The exemption proposed in this notice ("the Best Interest Contract Exemption") was developed to promote the provision of investment advice that is in the best interest of retail investors such as plan participants and beneficiaries, IRA owners, and small plans. [Employee Retirement Income Security Act of 1974 (ERISA)] and the Code generally prohibit fiduciaries from receiving payments from third parties and from acting on conflicts of interest, including using their authority to affect or increase their own compensation, in connection with transactions involving a plan or IRA. Certain types of fees and compensation common in the retail market, such as brokerage or insurance commissions, 12b-1 fees, and revenue-sharing payments, fall within these prohibitions when received by fiduciaries as a result of transactions involving advice to the plan participants and beneficiaries, IRA owners, and small-plan sponsors. To facilitate continued provision of advice to such retail investors and under conditions designed to safeguard the interests of these investors, the exemption would allow certain investment advice fiduciaries, including broker dealers and insurance agents, to receive these various forms of compensation that, in the absence of an exemption, would not be permitted under ERISA and the Code. The provision later defines "fiduciaries" and "advice" quite broadly (again, emphasis added):

Under the statutory framework, the determination of who is a "fiduciary" is of central importance. Many of ERISA's and the Code's protections, duties, and liabilities hinge on fiduciary status. In relevant part, ERISA

section 3(21)(A) and Code section 4975(e)(3) provide that a person is a fiduciary with respect to a plan or IRA to the extent he or she (i) exercises any discretionary authority or discretionary control with respect to management of such plan or IRA, or exercises any authority or control with respect to management or disposition of its assets; (ii) renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan or IRA, or has any authority or responsibility to do so; or, (iii) has any discretionary authority or discretionary responsibility in the administration of such plan or IRA.

The statutory definition deliberately casts a wide net in assigning fiduciary responsibility with respect to plan and IRA assets. Thus, "any authority or control" over plan or IRA assets is sufficient to confer fiduciary status, and any persons who render "investment advice for a fee or other compensation, direct or indirect" are fiduciaries, regardless of whether they have direct control over the plan's or IRA's assets and regardless of their status as an investment adviser or broker under the federal securities laws.

Finally, the provision defines which assets would be "exempt" from the new rule (once again, emphasis added):

(c) An "Asset," for purposes of this exemption, includes only the following investment products: Bank deposits, certificates of deposit (CDs), shares or interests in registered investment companies, bank collective funds, insurance company separate accounts, exchange-traded REITs, exchange-traded funds, corporate bonds offered pursuant to a registration statement under the Securities Act of 1933, agency debt securities as defined in [Financial Industry Regulatory Authority (FINRA)] Rule 6710(l) or its successor, U.S. Treasury securities as defined in FINRA Rule 6710(p) or its successor, insurance and annuity contracts, guaranteed investment contracts, and equity securities within the meaning of 17 CFR 230.405 that are exchange-traded securities within the meaning of 17 CFR 242.600. Excluded from this definition is any equity security that is a security future or a put, call, straddle, or other option or privilege of buying an equity security from or selling an equity security to another without being bound to do so.

Under the proposal, brokerages (including discount online brokerages) that administer IRA or other retirement plans could be considered "fiduciaries" with regard to any asset NOT on the list above... even if they provide no actual investment "advice" and simply collect a commission or transaction fee for trades like most online brokerages do. And options are clearly excluded from this list.

So unless you believe your online brokerage is likely to allow you to trade for free, your ability to buy or sell options in your IRA could disappear under this proposal.