Institute for Portfolio Alternatives

January 2, 2024

Office of Regulations and Interpretations,
Employee Benefits Security Administration, Room N–5655,
U.S. Department of Labor,
200 Constitution Ave. NW,
Washington, DC 20210

Re: Definition of an Investment Advice Fiduciary—RIN 1210–AC02, Proposed Amendment to Prohibited Transaction Exemption 2020-020—ZRIN 1210.

Dear Assistant Secretary Gomez:

The Institute for Portfolio Alternatives (the "Institute") appreciates the opportunity to comment on the Department of Labor's (the "Department") proposed rule titled "Retirement Security Rule: Definition of an Investment Advice Fiduciary" ("Proposed Rule") and "Proposed Amendment to Prohibited Transaction Exemption 2020-02 ("Proposed PTE 2020-02") published on November 3, 2023. For the reasons stated below, the Institute urges the Department to withdraw the Proposed Rule and Proposed PTE 2020-02. If the Department does not withdraw the Proposed Rule, we ask that the Department reconsider the Proposed Rule for the reasons described below.

This letter provides the Department a brief background of the Institute, a summary of our concerns regarding the Proposed Rule and Proposed PTE 2020-02, and provides the Institute's suggestions regarding the requirements of both.

I. Background of the Institute

For over 35 years, the Institute has raised awareness of alternative investment products among stakeholders and market participants, including investment professionals, policymakers, and the investing public. The Institute regularly provides substantive input to regulators such as the Department, the U.S. Securities and Exchange Commission ("SEC"), the Financial Industry Regulatory Authority ("FINRA"), and state regulators. The Institute is pleased to have provided meaningful input to the Department's previous rule proposal.[1] Furthermore, the Institute is committed to ensuring that all investors have access to real assets and the opportunity to diversify their investment portfolios with alternative products, based on appropriate standards of financial and personal suitability and consistent with the investment goals of the investors.

[1] Letter from Kevin Shields, Chairman of Investment Program Association to Office of Regulations and Interpretations Office of Exemption Determinations Employee Benefits Security Administration (July 21, 2015).

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The Institute's membership[2] consists of product sponsors of private real estate, private credit and other real assets, financial intermediaries such as registered investment advisers and broker-dealers, and industry services providers including major law firms, accouting firms, technology providers and consultants. The Institute's mission is to promote portfolio diversifying products among the investing public, conduct research and provide industry-leading data, and advocate for our members' interests to policymakers. The Institute is pleased to provide you with its thoughts regarding the Proposed Rule and Proposed PTE 2020-02.

II. Summary

The Institute supports the objective of the Department to protect investors by requiring that those financial professionals who provide fiduciary advice to retail retirement savers comply with a fiduciary standard of care. However, we believe that the standard of care must and can be adopted in a way that preserves investor choice and access to different business models and investment products. We appreciate the Department's efforts to consider and reflect on the concerns stated in our and others' comment letters on the 2016 Final Regulation.[3] Additionally, in light of the questions raised in connection with litigation of the 2016 Final Regulation and exemptions, we respectfully provide the following comments.

The Institute is concerned that conflicting regulatory requirements could create confusion and uncertainty among firms, advisors, and clients, and therefore, do not further the goal of investor protection. Significantly increased compliance and operational costs in providing quality services to retirement savers will have a direct impact on the availability and cost of financial services and products for American retirement savers, particularly those with small dollar accounts.

We focus on seven areas where the Proposed Rule and Proposed PTE 2020-02 would particularly benefit from additional consideration:

- The Department should comply with the Administrative Procedures Act.
- Investors benefit from diversification and the Proposed Rule will lead to less diversification.
- The Proposed Rule is unneeded considering the SEC's Regulation Best Interest.
- The Proposed Rule should be reevaluated based on the Fifth Circuit's 2018 decision vacating the Department's previous fiduciary rule and the text of Employee Retirement Income Security Act ("ERISA").

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[2]Collectively, the Institute's members service financial and direct investment assets in virtually all investment categories. Investment strategies are structured through investment vehicles such as non-listed real estate investment trusts, non-listed business development companies, unlisted closed-end funds including interval and tender offer funds, and private placements. With nearly $300 billion in capital investments, these diversifying investments are a critical component of an effectively balanced investment portfolio.

[3] 81 Fed. Reg. 20946 (Apr. 8, 2016).

- The Department should clarify that communications with intermediaries and "hire me" conversations do not create a fiduciary relationship.
- The Department should not change PTE 2020-02.
- The Proposed Rule's effective date is unreasonable.

III. The Department should comply with the Administrative Procedures Act.

The Department has not complied with the Administrative Procedure Act's requirement that agencies provide the public with a meaningful opportunity to participate in the public rulemaking process and provide thoughtful input.

First, by publishing the proposed regulatory package and significant changes to exemptions on November 3, 2023, and requesting comments by January 2, 2024, the Department offered only 35 business days[4] for stakeholders to assess the package and draft meaningful input. This period includes four federal holidays, and, for some of them, individuals have significant religious and familial obligations. The Proposed Rule redefines "investment advice," and is accompanied by the elimination or substantial rewrite of five longstanding class exemptions and modifications to PTE 2020-02 (collectively, the "Amended PTEs").

Second, the Department scheduled a hearing as required by ERISA Section 408(a) on December 12th and 13th, several weeks before the comment period ended, and comments were posted and publicly available. Before granting an exemption from ERISA Section 406(b), the Department is required to "afford an opportunity" for a hearing. For all other proposed class exemptions from ERISA Section 406(b), the Department has held the hearing after the comment period. Holding the hearing after the comment period importantly affords members of the public the opportunity to meaningfully participate because it allows them to respond to issues that are raised by other commenters. The Department's failure to hold the hearing after the comment period was unprecedented and compounded by the Department's failure to publish comments as they were submitted. The Department has received 18,368 comments (or form letters) on the proposed regulatory package, but as of the date comments were due, fewer than 100 comments (including the requests to testify) were publicly available.

Third, the Institute and seventeen other trade associations requested that the Department extend the comment deadline.[5] On November 14, 2023, the Department rejected this request. While the Institute recognizes the Department's desire to move the rulemaking process forward, there is no policy justification for a rulemaking process that hinders the ability of the industry to provide input to the Department and raise legitimate concerns. In fact, the Department's response to the request suggests that the Department would prefer for the public to not submit comments as the Department

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[4] This timeframe excludes the publication date, the comment due date, the two days that the hearings are scheduled, observed holidays, and weekends.
[5] *See* https://ipa.com/wp-content/uploads/2023/11/Trades-Request-Additional-Comment-Time.pdf

believes the Proposed Rule and Amended PTEs (the "Proposal") already "reflect[] significant input it has received from public engagement with this project since 2010."

To the contrary, a short 60-day comment period, with a virtual public hearing held before comments were due and publicly available, is unreasonable and insufficient for a vigorous public debate and thoughtful comments on a proposal that significantly revises the definition of fiduciary and amends multiple exemptions. As a result, this abbreviated process is contrary to the intent of the Administrative Procedure Act which is to "provide for public participation in the rulemaking process."

IV. Investors benefit from portfolio diversification and the Proposed Rule and Amended PTEs will lead to less diversification.

Millions of Americans benefit from diversification both inside their retirement plan and in their individual retirement accounts ("IRAs"). Diversification is enhanced when retirement savers have access, learn about, and have the opportunity to invest in asset classes with a variety of different correlations. The Department has underestimated the costs of the Proposed Rule and the Amended PTEs. The Proposal would change the market for providing investment advice and impact retirement savings by significantly increasing the compliance costs of firms, and in particular of firms offering products other than publicly traded equities. It would do this by subjecting most interactions by financial professionals with American savers to ERISA's fiduciary rules and forcing them to comply with the conditions of PTE 2020-02.

The Institute's members offer several alternative products that help generate successful retirement outcomes. The Institute believes these products possess attributes that complement retirement investment objectives. In moderation, these portfolio additions can provide asset class diversification and incremental portfolio diversity beyond traded securities. For example, they offer the potential to hedge inflation through ownership of real and inflation indexed assets, while also providing a limited level of liquidity and avoiding exposure to the volatility of the traded markets. Investors benefit from access to these products because they provide a way for investors to have some liquidity, while also offering prices and valuation tied to the value of underlying assets, rather than daily market fluctuations.

Based on the Department's 2016 rulemaking, we expect financial institutions to pull back from the retail market if the Proposed Rule is finalized. On August 9, 2017, Deloitte issued a white paper "The DOL Fiduciary Rule: A study on how financial institutions have responded and the resulting impacts on retirement investors" (the "Deloitte Study").[6] Under the Deloitte Study, 53% of participants eliminated or limited access to brokerage advice services. 95% of participants limited or made changes to the products that were available to retirement savers. And ultimately, this reduced access contributed to investors moving to self-directed accounts. The reduction in available products impacted 21.7 million

[6] https://www.sifma.org/wp-content/uploads/2017/08/Deloitte-White-Paper-on-the-DOL-Fiduciary-Rule-August-2017.pdf

accounts and more than $2 trillion in assets under management—with the impact disproportionately affecting smaller accounts.

Harper Polling found a similar result when it surveyed 600 financial professionals in 2017.[7] There, 50% of those polled said that the 2016 Fiduciary Rule was restricting them from serving their client's best interests. They found that the 2016 Final Rule led to "fewer investment options," "additional fees," "fewer smaller accounts," "more paperwork," and "less client time."

The Proposed Rule unnecessarily harms savers and investors based on the substantial challenges, costs and legal risks of implementing business and compliance solutions. If adopted without modifications and additional consideration given to costs, greater consolidation in the financial services industry may result. This will ultimately hurt retail investors, and in particular small dollar savers. Because the data suggests that the Proposed Rule will lead to more limited investment menus and less financial services available for American savers, the Department should withdraw the Proposal.

V. The Proposed Rule is unnecessary in light of the SEC's Regulation Best Interest.

The Institute is concerned because the SEC's Regulation Best Interest ("Reg BI") already provides a comprehensive framework and established rules surrounding rollover recommendations. Moreover, Reg BI and the Proposed Rule conflict in certain areas.

a. Regulation Best Interest already regulates rollover recommendations.

The Department states that the Proposed Rule generates benefits by "reducing conflicts related to one-time advice concerning rollovers."[8] The Department notes that rollover recommendations are generally not subject to ERISA's fiduciary standard today and that the Proposed Rule would subject rollover recommendations to conflict mitigation requirements. The benefit is illusory because Reg BI already protects recipients of rollover recommendations. Under Reg BI,

> [a] recommendation that a retail customer roll over or transfer assets to an IRA held at the broker-dealer, or open an IRA or another securities account with a broker-dealer, presumes that the recommendation would involve transactions in securities, even if the rollover or account recommendation does not result in transactions or transaction-based compensation.[9]

[7] https://www.dol.gov/sites/dolgov/files/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB82/00601.pdf

[8] 88 Fed. Reg. 75890, 75938 (Nov. 3, 2023).

[9] 84 Fed. Reg. 33318, 33339 n.194 (July 12, 2019).

When recommending a rollover, the SEC stated that "a broker-dealer should discuss the basis of such recommendations with the retail customer."[10] In fact, the SEC explicitly listed several factors that a broker should consider when recommending a rollover:

- fees and expenses;
- level of service available;
- available investment options;
- ability to take penalty-free withdrawals;
- application of required minimum distributions;
- protection from creditors and legal judgments;
- holdings of employer stock; and
- any special features of the existing account.

There is no need for the Department to also regulate rollovers. Adding another federal regulatory framework for rollover recommendations will not enhance investor protection and instead will increase costs, confusion, and uncertainty among firms, advisors, and clients.

b. The Proposed Rule conflicts with Reg BI.

The Department states that the Proposed Rule is "consistent with the requirements of SEC's Regulation Best Interest" and that "broker-dealers . . . that have already adopted meaningful compliance mechanisms for Regulation Best Interest . . . should be able to adapt easily to comply."[11] There are, however, significant ways where Reg BI and the Proposed Rule differ and conflict.

The Department's limitation on compensation is directly in contrast with Reg BI. In proposed amendments to PTE 2020-02, the Department states that a financial institution's policies and procedures must mitigate conflicts of interest, including incentive compensation.[12] The Department also broadly states that financial institutions "may not use quotas, appraisals, performance or personnel actions, bonuses, contests, special awards, differential compensation, or other similar actions or incentives that are intended, or that a reasonable person would conclude are likely, to result in recommendations that are not in the retirement investors' Best Interest" and expressly bans "if a reasonable person would conclude they are likely to impact a financial professional's recommendation."[13]

[10] 84 Fed. Reg. 33318, 33360 (July 12, 2019).
[11] 88 Fed. Reg. 75890, 75899 (Nov. 3, 2023).
[12] *See* Proposed Amendments to PTE 2020-02, Section II(c)(2). Conflicts of Interest must be mitigated "to the extent that a reasonable person reviewing the policies and procedures and incentive practices as a whole would conclude that they do not create an incentive for a Financial Institution or Investment Professional to place their interests ahead of the interests of the retirement investor."
[13] 88 Fed. Reg. 75979, 75987 (Nov. 3, 2023).

The Department, by delineating specific compensation practices, implies that these practices, in and of themselves, may lead to recommendations that are not in the best interest of retirement investors, and are therefore prohibited. These restrictions also appear to hinder firms from rewarding individuals based on performance or offering promotions tied to performance metrics. In sum, the Institute is concerned about the uncertainty surrounding the Department's subjective determination of conflicted compensation structures. This lack of clarity can create situations where firms are unable to operate confidently, because the Department may deem a particular compensation structure conflicting.

The Proposed Rule's broad list of compensation practices contradicts Reg BI. The SEC regulation explicitly allows "sales contests, quotas, bonuses, and non-cash compensation that are based on sales of specific securities and specific types of securities within a limited period of time." [14] There is no mandate to eliminate additional sales practices beyond those specified in Reg BI. Instead, the emphasis is on disclosure and mitigation of such practices.

This is just one example of certain conflicts with the Proposal and Reg BI. We encourage the Department to withdraw the Proposed Rule to better conform the Department's rules with the SEC's rules.

VI. The Proposed Rule should be reevaluated based on the Fifth Circuit's 2018 decision on the Department's 2016 Fiduciary Rule and the text of ERISA.

The Proposed Rule attempts to convert brokers who make recommendations to retirement investors, including IRA holders, into ERISA fiduciaries. Under the Proposed Rule, brokers who "make[] investment recommendations to investors on a regular basis as part of their business" based on the "individual circumstances" where those recommendations can be relied upon to be in the best interest of the investor would be ERISA fiduciaries.[15] The Proposed Rule's text conflicts with the Fifth Circuit's decision in *Chamber of Commerce v. United States Department of Labor* ("*Chamber of Commerce*") and with the text of ERISA.[16]

a. *Chamber of Commerce*

In *Chamber of Commerce*, the Fifth Circuit described a relationship of "trust and confidence" as "the cornerstone of fiduciary status" and reiterated that absent the special fiduciary relationship, it is

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[14] 84 Fed. Reg. 33318, 33321 (July 12, 2019).
[15] 88 Fed. Reg. 75890, 75977 (Nov. 3, 2023).
[16] *Chamber of Com. of United States of Am. v. United States Dep't of Lab.*, 885 F.3d 360, 365 (5th Cir. 2018), *judgment entered sub nom. Chamber of Com. of Am. v. United States Dep't of Lab.*, No. 17-10238 (5th Cir. June 21, 2018) (hereinafter referred to as *Chamber*).

widely recognized that “financial salespeople are not fiduciaries.”[17] The Proposed Rule not only redefines “investment advice” to create a fiduciary relationship where there is no relationship of trust and confidence, but also it expressly conflicts with the decision in three specific ways.

First, the Department should not seek to reject the five-part test that the Fifth Circuit expressly endorsed. The Court held that the Department’s 1975 five-part test that defines an investment advice fiduciary “captured the essence” of the common law fiduciary relationship Congress incorporated in ERISA.[18] Nevertheless, in the Proposed Rule, the Department asserts that this five-part test “diverges from . . . the language . . . and purposes” of ERISA.[19] The Proposed rule creates a broad presumption that all investment interactions by firms (and their representatives) relating to ERISA/IRA assets trigger fiduciary status, requiring reliance on an exemption. This expressly contradicts the Fifth Circuit’s holding.

Second, the Department should not seek to disregard the Fifth Circuit’s decision that sales activity is different from advice and is not fiduciary advice. The Department states that it “rejects the purported dichotomy between a mere ‘sales’ recommendation to a counterparty, on the one hand, and advice, on the other, in the context of the retail market for investment products.”[20] This rejection is incompatible with the Fifth Circuit’s opinion, which clarified that investment advice fiduciary status means there is a “special relationship beyond that of an ordinary buyer and seller.”[21] It is also incompatible with the Fifth Circuit’s clarification of the distinction between “[s]tockbrokers and insurance agents [who] are compensated only for completed sales” and investment advisers who are “paid fees because they ‘render advice.’”[22] While an investment adviser typically receives fees because of their ongoing advice, brokers are paid a commission for executing a trade.[23] In other words, the Fifth Circuit made clear that brokers who receive transaction-based compensation and investment advisers who are compensated based on the total value of the investments under management are subject to different legal standards and obligations.

Third, the Department should reverse its conclusion that a relationship of “trust and confidence” can exist at the time that a broker makes a recommendation to a potential client. Although the Proposed Rule is designed to cover one-time advice,[24] this too is inconsistent with the Fifth Circuit’s description that “it is ordinarily inconceivable that financial salespeople or insurance agents will have an

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[17] *Chamber* at 376.
[18] *Chamber* at 365.
[19] 88 Fed. Reg. 75890, 75915 (Nov. 3, 2023).
[20] 88 Fed. Reg. 75890, 75907 (Nov. 3, 2023).
[21] *Chamber* at 377.
[22] *Chamber at* 373.
[23] The amount of a brokerage commission for the execution of a securities transaction does not change based on whether a trade is recommended, and brokers are not paid for recommendations that do not lead to executed trades. This compensation structure suggests that contrary to Advisory Opinion 83-60A, no part of a brokerage commission is a fee for “advice.”
[24] 88 Fed. Reg. 75890, 75938 (Nov. 3, 2023).

intimate relationship of trust and confidence with prospective purchasers" for "one-time IRA rollover" transactions.

b. ERISA

The text and history of ERISA also conflict with the Proposed Rule. ERISA endorsed the common law meaning of the word "fiduciary" and the Proposed Rule's definition of investment advice is inconsistent with that meaning. The Department should follow the text of the statute and Congress's direction and retain the common law definition of fiduciary.

i. Congressional intent when ERISA was enacted

ERISA is a comprehensive federal statute regulating employer-sponsored retirement and benefit plans. When Congress passed ERISA, it included explicit language that one is a fiduciary to the extent that he or she renders "investment advice" for a fee or other compensation (direct or indirect), with respect to a plan's money or property, or has any responsibility to do so.[25]

Under the Investment Advisers Act of 1940, an "investment adviser" "means any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities."[26] A "broker" as defined in the Securities Exchange Act of 1934 is excluded from this definition of "investment adviser" so long as the broker's "performance of such [advisory-type] services is solely incidental to the conduct of his business as a broker or dealer and who receives no special compensation therefor[e]."[27] Under these statutes, investment advisers give investment advice, and brokers, at most, recommend products for purchase.

When "Congress uses terms that have accumulated settled meaning under . . . the common law, a court must infer, unless the statute otherwise dictates, that Congress means to incorporate the established meaning of these terms."[28] Under this canon of statutory interpretation, "investment advice" in ERISA Section 3(21) has the same meaning its long-established meaning under the Investment Advisers Act. A broker or salesperson is excluded from this definition.

ii. Text of ERISA conflicts with the Proposed Rule

Beyond being contrary to the plain meaning of "investment advice," the text of ERISA's core statutory provisions also shows that Congress did not include brokers or salespeople within the

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[25] 29 C.F.R. § 2510.3-21(c).
[26] 15 U.S.C. § 80b-2(a)(11).
[27] 15 U.S.C. § 80b-2(a)(11)(c).
[28] *Nationwide Mut. Ins. Co. v. Darden*, 503 U.S. 318, 322 (1992) (citation omitted).

meaning of "fiduciary" in ERISA. ERISA Section 404(a)(1) requires that fiduciaries discharge their duties "solely in the interest of participants and beneficiaries."

Under the federal securities laws, brokers are not fiduciaries. While they must act in their customers' best interest when they make recommendations to retail customers (but not to institutional customers), they are not required to act "solely" in their retail customer's interest. The federal securities laws recognize that brokers may have conflicts of interest that they are permitted to resolve through mitigation or disclosure.

Moreover, ERISA Section 406(b)(3) prohibits fiduciaries from earning commissions. Securities brokers typically are paid commission for the execution of trades, even when they have recommended the trade to the investor. A broker could not simultaneously satisfy ERISA Sections 404 and 406(b)(3), while also meeting the broker-dealer exclusion from investment adviser status. An investment adviser, on the other hand, can satisfy those requirements because once hired, an investment adviser can receive an asset-based fee instead of a commission.

There is no policy basis or legal authority to justify the Department deviating from the text of ERISA to redefine "fiduciary" to include securities brokers or salespersons. When working with a financial intermediary who provides access to investment products, individuals typically have, and should continue to have, two options (i) pay a commission or (ii) pay an annual management fee. These two standards are important distinct choices that should be preserved for investors.

The Department should withdraw the Proposed Rule to comport with Congress's intent that savers have access to different advice models and options.

VII. Wholesaling and "hire me"

a. Wholesaling to intermediaries

The Institute agrees with the Department that wholesaling activity "would not involve recommendations based on the particular needs or individual circumstances of the plan or IRA serviced by the intermediary" and therefore, should not trigger fiduciary status.[29] Nevertheless, in the same passage the Department states, "communications to financial intermediaries *would typically* fall outside the scope of the proposed paragraph (c)(1)(ii)." The phrase "would typically fall outside the scope" of triggering fiduciary status undermines the Department's otherwise potentially helpful language by encouraging expensive and counterproductive litigation over the facts and circumstances of each wholesaling conversation. The Department's conflicting statements will cause confusion.

Moreover, the Proposed Rule's operative text would seem to apply to intermediaries if those intermediaries are plan fiduciaries. Under the Proposed Rule, recommendations to "plan fiduciaries"

[29] 88 Fed. Reg. 75890, 75907 (Nov. 3, 2023) (emphasis added).

trigger fiduciary status. "Plan fiduciary" means "a person described in [S]ection 3(21)(A) . . . with respect to a plan."[30] Using this definition, any entity that is itself an "investment advice" fiduciary will be a "plan fiduciary" so it could create a "daisy-chain" problem[31] where any wholesaler, no matter how far upstream from a plan, could fall within the Proposed Rule's definition if the entities that are downstream of it are connected by recommendations to a plan or IRA.

This would lead to the creation of fiduciary status for both intermediaries and even potentially product sponsors, even if they do not know who the end plan is or what the plan's needs are. This possibility cannot be the Department's intent, given the preamble language, and as a recommender is clearly not in a relationship of trust and confidence with an entity that it does not know exists.[32] Further, creating a fiduciary relationship between entities that may not have any direct contact or information would create significant challenges for compliance.

If the Department does not withdraw the Proposed Rule, it should provide clear language in the operative text of any final regulation that wholesaling conversations, including wholesaling conversations with intermediary fiduciaries, do not trigger a fiduciary relationship with any ERISA plan or IRA. The Department should make clear that a plan or IRA fiduciary is only considered a "Retirement Investor" when receiving advice that is based on the individual needs of a plan or IRA holder. This clarity could be accomplished by defining a "plan fiduciary" as the "named fiduciary" of a plan, and defining an IRA fiduciary as an individual or entity that is in a fiduciary relationship to a particular IRA or IRA holder and who is receiving the recommendation on behalf of a specific IRA or IRA holder. We strongly encourage the Department to provide this clarity.

b. "Hire Me" Conversations

The preamble of the Proposed Rule states, "when a recommendation to 'hire me' effectively includes a recommendation on how to invest or manage plan or IRA assets . . . that recommendation would need to be evaluated separately."[33] This principle could mean that all sales discussions of a fund manager could be fiduciary advice.

[30] 88 Fed. Reg. 75890, 75978 (Nov. 3, 2023).
[31] In its comment letter submitted in response to the Department's "Definition of the Term 'Fiduciary'; Conflict of Interest Rule" 2015 proposed rule, the Investment Company Institute explained the "daisy-chain" problem. Specifically, the Investment Company Institute noted that the 2015 proposed rule's "ambiguous language defining who is a fiduciary could be construed to make . . . [product sponsors and securities wholesalers] fiduciary advice providers under ERISA simply by providing needed product sponsor and wholesaler services to those financial intermediaries who would be fiduciaries by virtue of the application of the expanded fiduciary definition." *See* https://www.ici.org/system/files/attachments/15_ici_dol_rule_comment.pdf
[32] 88 Fed. Reg. 75890, 75907 (Nov. 3, 2023).
[33] 88 Fed. Reg. 75890, 75906 (Nov. 3, 2023).

Fund managers engage with fund investors[34] as part of their sales process. Before being hired, managers meet with retirement plan sponsors to introduce their capabilities and team, discuss industry trends, and describe their investment strategy. After a plan invests in one of a manager's funds, the manager may subsequently meet with a plan sponsor or its investment representative so that the plan can perform diligence on the investment team, ask the team questions, and discuss market trends.

Retirement savers would suffer if "hire me" conversations trigger fiduciary status or if final regulations are ambiguous on this topic. Plan fiduciaries and retirement savers expect and benefit from candor when they interview financial professionals, diligence funds, and submit requests for proposals. If final regulations are issued that do not clearly exclude such interactions from triggering fiduciary status, financial professionals will be forced to fall back on legalese and opaque responses if they want to be able to present their services to plan fiduciaries. If any final regulation is issued, the Department should clarify that these conversations are non-fiduciary. Without clarification, this aspect of the Proposed Rule would (i) materially interfere with the efficient operation of the alternative investment distribution market and (ii) make it harder for retirement plan fiduciaries to perform due diligence on private fund managers.

The Department's view that one can be an advice fiduciary before being "hired" conflicts with caselaw that has been issued since the Proposed Rule was published. In *D.L. Markham v. VALIC*, the Fifth Circuit affirmed the lower court's decision, which provided that ERISA's text is clear—service providers are not "parties in interest" before the service provider "has started providing services or has at least agreed to do so."[35] The court concluded there must be a contract in place before a service provider qualifies as a party in interest. On that same logic, one can only "render investment advice" "for a fee or other compensation" *after* being hired (and as a result, being paid) to provide the advice.

Even if the Department continues to believe that some "hire me" conversations can trigger fiduciary status, the Department should exclude "hire me" conversations with sophisticated plan fiduciaries. The Department claims that it is "unaware . . . of compelling evidence that wealth and income are strong proxies for financial sophistication or inconsistent with a relationship of trust and confidence." However, the SEC has created definitions of accredited investors, qualified purchasers, and qualified institutional buyers that turn on their sophistication, qualification, wealth, and/or income. Individuals qualify as accredited investors based on their net worth exceeding $1,000,000 or income or joint income being greater than $200,000 or $300,000 respectively in the past two years with a reasonable expectation of continuing to earn that same level of income.[36] Congress also understands

[34] The following are provided as examples: defined benefit plans regularly ask private fund managers to attend finalist presentations, and mutual fund families regularly send defined contribution plan fiduciaries and consultants materials touting their funds.

[35] *Markham v. Variable Annuity Life Ins. Co.*, No. CV H-22-0974, 2022 WL 5213229 at *9 (S.D. Tex. Oct. 5, 2022), *aff'd sub nom. D.L. Markham DDS, MSD, Inc. 401(K) Plan v. Variable Annuity Life Ins. Co.*, No. 22-20540, 2023 WL 8642231 (5th Cir. Dec. 14, 2023).

[36] 17 C.F.R. § 230.501(a)(5)-(6).

the consideration of similar factors when classifying an individual as an accredited investor.[37] Qualified purchasers include individuals who hold more than or equal to $5,000,000 in investments.[38] Qualified institutional buyers include certain entities that own and discretionarily invest at least $100,000,000 in the aggregate in securities of unaffiliated issuers.[39] Even the Department itself requires asset managers to have total client assets above a certain size before they can rely on PTE 84-14 (the "QPAM Exemption").[40] Apart from size thresholds, the Department should exclude "hire me" conversations with intermediaries that are SEC-registered broker-dealers, SEC or state-registered investment advisers, or exempt reporting advisers.

Given the overwhelming conclusion by financial service regulators (including the Department) that larger investors are in fact more sophisticated, we urge the Department to refine its understanding and consider a retirement investor's wealth, income, and qualifications when measuring its sophistication to avoid departing from a longstanding metric and disrupting the marketplace (both of which would result in tremendous cost).

In the plan space, the Department should offer guidance to plan fiduciaries instead of imposing conditions on fund managers and their distribution agents. ERISA requires plan fiduciaries to know the difference between sales conversations and advice. ERISA Section 404 requires all plan fiduciaries to act with "the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims."[41] Because the statute requires plan fiduciaries to be sophisticated, the Department's premise, that plan fiduciaries are not, should be revisited.

If the Department does not withdraw the Proposed Rule, it should revise the Proposed Rule to expressly state that a fund manager or other counterparty will not become a fiduciary when selling to a plan if the plan has engaged its own advisors or consultants to help the plan's fiduciaries evaluate the fund, product, or service being offered.

VIII. The Department should not change PTE 2020-02.

In Proposed PTE 2020-02, the Department would impose new requirements on financial institutions that rely on PTE 2020-02 as a method for curing ERISA Section 406(b) conflicts. The proposed text includes a requirement that financial institutions produce records to the Department and other federal and state regulators on request. In addition, the Department grants itself the authority to disallow financial institutions the ability to use PTE 2020-02 without requiring the Department to go

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[37] Congress authorized the SEC to refine the accredited investor definition based on the consideration of an individual's "financial sophistication, net worth, knowledge, and experience in financial matters, or amounts of assets under management." 15 U.S.C. § 77(b)(15)(ii).
[38] 15 U.S.C. § 80a-2(51)(A).
[39] 17 C.F.R. § 230.144A(a)(1)(i).
[40] 75 Fed. Reg. 38837, 38843 (July 6, 2010).
[41] 29 U.S.C. § 1104(a)(1)(B).

through the judicial process. We ask that the Department not include these changes in any final PTE 2020-02.

Rather than expanding the scope of fiduciary status and adding new compliance burdens on retirement service providers, the Department should instead consider amendments to PTE 2020-02 to streamline compliance where it would not lead to harm for retirement savers. For example, the Department could repropose amendments to PTE 2020-02 to incorporate a materiality threshold before entities relying on the exemption are required to file reports with the Department and remediate.

a. Disclosure or Records Requirements

The amendments to PTE 2020-02 would require financial institutions to provide reports, certifications, and supporting data demonstrating compliance with the exemption to the Department within ten business days of a request.[42] The Department should not require entities relying on PTE 2020-02 to provide their policies and procedures and records documenting compliance within ten business days of the Department's request.[43]

ERISA Section 504 sets out the Department's investigative authority when its investigations relate to plans subject to Title I of ERISA. While it allows the Department to request materials, the Department's authority is limited by its need to go to court to seek to enforce subpoenas. In Proposed PTE 2020-02, the Department has exceeded the scope of its authority to investigate by attempting to request more than what it can demand without judicial process.

This lack of authority is compounded in the IRA market. In Reorganization Plan No. 4 of 1978 (the "Reorganization Plan"), the Department was only granted interpretive authority in the IRA space.[44] The Reorganization Plan explicitly clarified that with respect to ERISA Title I, Subtitle B Parts 2 and 3 and anywhere else in which the authority of the Secretary of Labor was transferred to the Secretary of the Treasury in the Reorganization Plan, "the Secretary of Labor shall be bound by the regulations, rulings, opinions, variances, and waivers issued by the Secretary of the Treasury." Based on the text and impact of the Reorganization Plan, the Department does not have authority to demand documents under ERISA Section 504.

The Department should remove this change from Proposed PTE 2020-02, and if it believes it has a valid legal basis for requesting records pursuant to its enforcement authority, the Department should continue to use the subpoena process.

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[42] 88 Fed. Reg. 75979, 75986 (Nov. 3, 2023).
[43] 88 Fed. Reg. 75979, 76001 (Nov. 3, 2023).
[44] https://www.dol.gov/agencies/ebsa/laws-and-regulations/laws/executive-orders/4

b. Notices of Ineligibility

In Proposed PTE 2020-02, the Department proposes to grant itself the ability to deprive entities of their right to rely on prohibited transaction exemptions by issuing a notice of ineligibility due to a "systematic pattern or practice of violating the conditions of this exemption in connection with otherwise non-exempt prohibited transactions."[45] This power has a procedural due process flaw that renders it unconstitutional under Article III of the Constitution, the Due Process Clause of the Fifth Amendment, and the Seventh Amendment.

The Department's process only includes a written warning, a six-month opportunity to cure, and an opportunity to be heard by the Department itself that is "*limited to one conference* unless the Department determines *in its sole discretion* to allow additional conferences."[46] This means that the Department would be in complete control over the fate of the financial institutions' livelihoods—the Department writes the regulations, conducts the hearings, and makes the decisions. This outcome is incompatible with the separation of powers. The constitutional flaws are even greater when one considers that the procedural protections that defendants are entitled to in federal courts (*e.g.*, the Federal Rules of Evidence, the "two-way street"[47] of discovery, and a neutral factfinder) are *not* available to defendants before the Department. Notably, the Supreme Court has struck down the SEC's in-house judicial process, even though its procedural safeguards are greater than those of the Department.[48]

The sanction of depriving an entity of its ability to engage in its business is analogous to the penalties that courts have repeatedly found to be akin to a criminal penalty. For example, in *Nell v. United States*,[49] the Fourth Circuit held that due process requires an attorney's disbarment or suspension proceedings to be preceded by an opportunity to prepare a defense. In *Saad v. S.E.C.*,[50] the D.C. Circuit stated that a sanction imposing "a lifetime bar . . . is 'the securities industry equivalent of capital punishment.'" Although the notice of ineligibility does not include a lifetime bar, and instead lasts for ten years,[51] the impact of receiving a notice of ineligibility is functionally equivalent to a lifetime bar, as it will put many receivers out of business.

Only after sufficient due process can an individual be barred from engaging in a practice that they are legally entitled to do. In any final amendments to PTE 2020-02 (and the QPAM Exemption), the Department should not include provisions regarding the issuance of notices of ineligibility.

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[45] 88 Fed. Reg. 75979, 76001 (Nov. 3, 2023).
[46] 88 Fed. Reg. 75979, 76002 (Nov. 3, 2023) (emphasis added).
[47] *Wardius v. Oregon*, 412 U.S. 470, 475 (1973).
[48] *Lucia v. S.E.C.*, 138 S. Ct. 2044 (2018).
[49] 450 F.2d 1090, 1093 (4th Cir. 1971).
[50] 718 F.3d 904, 906 (D.C. Cir. 2013).
[51] 88 Fed. Reg. 75979, 76002 (Nov. 3, 2023).

IX. Even if the Department does not make substantive changes to the Proposed Rule, the effective date is unreasonable and inconsistent with past practice.

The Proposed Rule and Amended PTEs would be effective 60 days after the date any final rule is published in the Federal Register. The Proposed Rule is as expansive in scope as the 2016 Final Regulation. The timeline for implementation of the Proposed Rule significantly underestimates the amount of time that financial advisers, investment platform providers, and product sponsors will need to come into compliance. Even firms that have voluntarily implemented the current PTE 2020-02 will have to make extensive updates if the amendments to PTE 2020-02 are finalized.

The requirements and conditions included in the Proposed Rule are exceedingly complex and will require expensive information technology re-design. Without additional time, many institutions will simply not be able to meet the Proposed Rule's requirements and may be forced to suspend delivery of services to customers. A delay in the applicability date will help mitigate these unnecessary market disruptions.

The implementation timeline is also inconsistent with the Department's past practice in adopting new regulations. The 2016 Final Regulation had a one-year applicability date, and numerous extensions. The effectiveness and enforceability of PTE 2020-02 required almost two years to materialize. Consequently, it is impractical to anticipate adherence to both a comparably intricate Proposed Rule and significantly modified Amended PTEs within a mere 60-day timeframe. Further, the adjustments that will be required by the Proposed Rule are significant ERISA regulatory changes. The applicability date does not consider the complexity and enormity of the effort that the financial services industry will be required to undertake to comply with it. A delay in the applicability date will give the financial services industry a more manageable amount of time to develop, test, and implement the necessary new systems and processes.

While we encourage the Department to withdraw the Proposed Rule and Amended PTEs, if the Department does move forward, we encourage the Department to have, at least, a one-year effective date.

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For the reasons stated in this letter, the Institute urges the Department to withdraw the Proposed Rule and Proposed PTE 2020-02. If the Department does not withdraw the Proposed Rule, we ask that the Department reconsider the Proposed Rule considering the factors described above.

The Institute appreciates the opportunity to comment on the Proposal. Should you have any questions about our comments, please feel free to contact me or Gina Gombar at (202) 548-7185.

Sincerely,

Anya Coverman
President and CEO