

## COMMENT LETTER

December 12, 2007

# Institute Letter to DOL on Investment Advice (pdf)

December 12, 2007 The Honorable Bradford Campbell Assistant Secretary Employee Benefits Security Administration U.S. Department of Labor Washington, D.C. Dear Assistant Secretary Campbell: We understand that the Department of Labor is considering providing regulatory guidance on the new investment advice exemption under section 408(b)(14) of ERISA or, alternatively, issuing a class exemption covering similar investment advice related transactions. We welcome this initiative and are submitting this letter to provide the views of the Investment Company Institute on the types of conditions that may be appropriate to include in developing regulations or an exemption. As our prior submissions and recent testimony make clear, the Institute recommends that the Department issue regulations or an exemption that applies the level fees requirement only to the entity that determines what investment advice is given to participants. This would be an individual financial adviser (FA) where the FA exercises discretion to determine what investment recommendations are provided to participants. If no individual has this authority, the level fees condition would apply to a corporate entity that determines what investment recommendations are made. The Department also should clarify that when a proprietary computer model is used to provide advice, after a portfolio generated by the model has been presented, an FA may provide specific investment recommendations that deviate from the model at the request of the participant without engaging in a prohibited transaction. We believe that the Department can provide guidance to improve the application of many aspects of the computer modeling and fee leveling provisions interpretively and without pursuing a separate class exemption. If the Department also pursues a class exemption on its own initiative or under section 601(b)(3)(C)(ii) of the Pension Protection Act,<sup>1</sup> the exemption should cover all transactions and relief provided in section 408(b)(14). The Department also should consider 1 As we stated in our testimony on July 31, 2007 in connection with the Department's required determination under section 601(b)(3)(C) of the PPA, the Institute believes that computer models that cover the full range of investments available to IRAs are not feasible. The Honorable Bradford Campbell December 12, 2007 Page 2 of 3 expanding the scope of any exemption to cover advice to plan sponsors in addition to advice to plan participants. Plan sponsors routinely request advice on the selection and monitoring of plan investment options and having access to this advice would be helpful. We recognize that in taking action along the lines we suggest, the Department will want to include conditions to address concerns that advisors may have a financial conflict of interest in providing advice. The Institute believes that the following types of conditions would ensure that any permitted advice will be objective and unbiased while affording financial institutions flexibility in designing and delivering advice programs:

- Require upfront and ongoing disclosure of fees received directly and indirectly by the

advisor and its affiliates in connection with the advice that is given. • Require disclosure of which investment options are affiliated with the advisor and what other entities involved in the advisory program are affiliated with the advisor. • Require an acknowledgement of fiduciary status by both the financial institution and, if applicable, the individual FA. • Require that the advisory program include the preparation of an asset allocation that is based on an objective assessment of the risk tolerance of the individual receiving advice. This asset allocation must be based on generally accepted investment principles and any specific investment recommendations of investment options must be consistent with the individual's asset allocation and risk tolerance. This condition could be met where an FA or computer model: o Determines an individual's risk tolerance, and proposes an asset allocation, either by (1) taking into account specific information provided by the individual (e.g., via responses to a questionnaire administered by an FA or a computer) or (2) by disclosing to the individual the key variable or variables used to determine the individual's risk tolerance (e.g., this risk tolerance is appropriate for someone who expects to retire in the year 2020). It is expected that, with appropriate disclosure, risk tolerances and asset allocations could be established solely with reference to age or expected retirement date. o Makes specific recommendations of investment options in a manner that is consistent with an individual's asset allocation and risk tolerance and based on generally accepted investment principles and objective selection criteria. • To the extent an advisory program limits the ability of the FA to recommend investment products, or a computer model has a limited universe of investments from which it will make recommendations, the limitations would have to be clearly disclosed to the individual. The Honorable Bradford Campbell December 12, 2007 Page 3 of 3 Advisory programs should be able to expressly limit investment recommendations to subsets of investments available under a plan or IRA, such as mutual funds or a single family of proprietary mutual funds. Because any specific investment recommendation would have to be consistent with an overall asset allocation appropriate to the individual (see recommended condition above), individuals would be assured that any limitations on investments would not affect portfolio diversification and the application of other generally accepted investment principles. • Entities that seek to rely on the exemption would have to maintain reasonable, written procedures for compliance with the exemption. Provided that the conditions of the exemption (or regulation) are met, the Department should make clear that an FA or a computer based advisory program would not be prohibited from recommending products that increase the compensation of the firm sponsoring the program. \* \* \* We hope that the Institute's suggestions are helpful to the Department in developing further guidance for advisory programs. We would be pleased to discuss our ideas in more detail as the Department works on this important issue. Sincerely, /s/ Mary S. Podesta Mary S. Podesta Senior Counsel – Pension Regulation cc: Robert Doyle Ivan Strasfeld