

## COMMENT LETTER

March 6, 2009

# ICI Comment Letter on DOL Investment Advice Final Rule

March 6, 2009 Submitted electronically Office of Regulations and Interpretations Employee Benefits Security Administration Room N-5655 U.S. Department of Labor 200 Constitution Avenue, N.W. Washington, DC 20210 Attn: Investment Advice Final Rule Ladies and Gentlemen: The Investment Company Institute<sup>1</sup> commends the Department of Labor's efforts to seek public comment and review its final rules on the provision of investment advice to participants and beneficiaries of self-directed individual account plans and individual retirement accounts, published on January 21, 2009, 74 Fed Reg. 3822 (the "Final Rules"). The Institute appreciates the need for the new Administration to review the Final Rules to assure itself that they are appropriate and in the public interest. The Final Rules arise from the investment advice provisions included by Congress in a bipartisan piece of legislation—the Pension Protection Act of 2006—with the goal of increasing opportunities for plan participants and IRA holders to have professional investment advice. The Institute strongly supports this goal and the Department's effort to ensure that the Final Rules implement Congressional intent and resolve any ambiguity or inconsistency in the statutory language while providing meaningful protection for plan participants and IRA holders. 1 The Investment Company Institute is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. Members of ICI manage total assets of \$9.88 trillion and serve over 93 million shareholders. Office of Regulations and Interpretations Investment Advice Final Rules Page 2 of 4 Although the Institute unsuccessfully urged certain changes or additions to the rules when proposed which we believe would have further improved the Final Rules,<sup>2</sup> we strongly support the Final Rules. The Final Rules thoughtfully implement the PPA provision in a manner that will encourage plans and providers to offer investment advice programs to assist participants and beneficiaries of ERISA plans and IRA holders in managing their accounts—exactly the outcome Congress intended in adopting the provision. As the Department noted in the preamble to the Final Rules, there has been an increasing recognition of the importance of investment advice for participants in defined contribution plans and IRA account holders.<sup>3</sup> A 2007 GAO report concluded that only 47% of ERISA plans offered some form of investment education to participants.<sup>4</sup> In contrast, 80 percent of households owning mutual funds outside of defined contribution plans purchased their funds using a professional financial adviser.<sup>5</sup> These data suggest that investment advice is much less widely available for retirement plans, and the Institute believes implementation of the PPA provision will remove obstacles that currently contribute to this disparity. As the Department recognized when promulgating the Final

Rules, extending quality, expert advice to a greater number of participants will improve investment decisions and results, reduce unnecessary investment expenses and improve the welfare of participants by better aligning investments and risk tolerances.<sup>6</sup> The need for investment advice programs is clear, particularly given the recent economic uncertainty and market turmoil. During recent months, as markets fell, participants have reached out 2

If the Department decides, nevertheless, to reconsider the substance of the Final Rules, it should as part of that process also reevaluate issues raised in the Institute's comment letters and testimony. For example, the Final Rule requires, under the fee level option, that fees do not vary depending on the basis of any investment option selected. The Institute had asked that the Department clarify that this condition would not be violated by certain bonus programs, such as a bonus program based upon the overall profitability of an adviser, or that of its business unit or parent entity, over a specified period of time, or based on total assets under management, that are not tied materially to a participant's investment decisions. The only guidance the Department provided was in the preamble, and that guidance states that "almost every form of compensation" that takes into account the investments selected by participants would violate the condition, but that this will depend on the details of the program. We are concerned that this provides insufficient guidance which may dissuade providers from using the exemption. In addition, the withdrawal of exemptive relief for any advice transaction that occurs during a period in which the adviser had a "pattern or practice" of noncompliance with the conditions of the Final Rules is unprecedented and unwarranted. Nothing in the PPA suggests such a condition. 3 74 Fed. Reg. 3822, 3822 (Jan. 21, 2009). 4 U.S. Government Accountability Office, GAO-07-355, Employer-Sponsored Health and Retirement Plans: Efforts to Control Employer Costs and the Implications for Workers, at 36 (Mar. 2007), available at <http://www.gao.gov/new.items/d07355.pdf>. 5 Investment Company Institute, Ownership of Mutual Funds Through Professional Financial Advisors, 2007 (Sept. 2008), available at <http://www.ici.org/statements/res/fm-v17n4.pdf>. 6 74 Fed. Reg. at 3838. Office of Regulations and Interpretations Investment Advice Final Rules Page 3 of 4 in record numbers to their plan providers for assistance.<sup>7</sup> Providers need to be able to respond and to develop new advice products to address market developments and participant needs. Prior to the PPA, the provision of investment advice by an entity that already provides services to the plan would have been, in many circumstances, a prohibited transaction. In the PPA, Congress permitted qualified "fiduciary advisers" to provide investment advice, so long as the adviser's compensation does not vary depending on the participant's investment choices, or the advice is rendered through an unbiased computer model, and all other requirements prescribed by the Department are met. In so doing, the PPA allowed participants easier access to advice from companies with which they are already familiar—those providing services or investments to the plan—but imposed strong fiduciary protections and other safeguards. These conditions include: • the fiduciary adviser must agree to be subject to ERISA's strict fiduciary duty and must acknowledge fiduciary status in writing; • the advice program must be audited annually by an independent auditor for compliance with all of the conditions of the exemption; • computer model advice must be pursuant to a model certified by an independent expert; • the fiduciary adviser must provide robust disclosure of fees, material affiliations and conflicts of interest, past performance, use of participant information, and more; and • the fiduciary adviser must maintain records demonstrating compliance with the exemption for six years. The Department's efforts to implement these PPA provisions extended over thirteen months, and include two requests for information, a Field Assistance Bulletin, two public hearings, and the development of proposed and final guidance. In the Final Rules, the Department balanced the need for increased advice and appropriate safeguards and reconciled textual ambiguities in the statutory language to achieve Congress' intent. Both aspects of the Final

Rules were within the Department's authority under ERISA and the PPA. For example, ERISA section 408(g)(3), as added by the PPA, addresses investment advice using a computer model and requires that only advice generated by the certified computer program be given. The statute clarifies, however, "Nothing in the preceding sentence shall preclude the participant or beneficiary from requesting investment advice [other than from the computer model] but only if such request has not been solicited" by the investment advisor. While this provision clearly contemplates that the statutory prohibited transaction exemption should apply to advice given in response to such a participant request, the language inexplicably seems to exempt only the question, and not the answer. 7 See, e.g., [http://content.members.fidelity.com/Inside\\_Fidelity/fullStory/1,7669,00.html](http://content.members.fidelity.com/Inside_Fidelity/fullStory/1,7669,00.html) (reporting that the volume of calls during the most volatile period, late September and early October 2008, spiked to over 100,000 calls per day, with a record number on October 10, 2008, the day after the Dow Jones Industrial Average closed below 9,000 for the first time in five years). Office of Regulations and Interpretations Investment Advice Final Rules Page 4 of 4 The Final Rules implement Congress' intent by permitting fiduciary advisers to respond to participant inquiries (so-called "off-model advice"), if the requirements of the Final Rules are met. Similarly, the PPA's exemption for advice that does not affect the adviser's compensation (the "fee leveling condition") must be reconciled with the well-established position of the Department, first articulated in 1997, that no prohibited transaction occurs if an advice arrangement involved fee leveling at every level in the provider's organization.<sup>8</sup> If the fee leveling condition in the statutory exemption was not intended to expand the Department's pre-PPA guidance, it would be meaningless. The PPA provision is unclear on precisely how the fee leveling condition should apply. The Final Rules apply fee leveling in the place it makes the most sense: to the party with discretion to provide advice to a participant. This makes the exemption applicable in a variety of business models (both where advice is generated by an individual representative of an advisory firm and where advice is generated by the advisory firm itself) and accomplishes Congress' goal of increasing the availability of investment advice to participants. If the Department determines that changes to the Final Rules are needed, the Department should issue a new proposal for notice and comment pursuant to the Administrative Procedure Act, explaining the reasons why the rule raises issues of law or policy and explaining why its analysis, after a lengthy regulatory process, has changed. \* \* \* The Institute appreciates this opportunity to express its views, and looks forward to continuing to work with the Department to implement the PPA's goal of expanding opportunities for investment assistance. If you have any questions, please contact the undersigned at 202.326.5826 or Michael Hadley at 202.326.5810. Sincerely, /s/ Mary S. Podesta Mary S. Podesta Senior Counsel – Pension Regulation 8 See DOL Adv. Op. 2005-10A (May 11, 2005); DOL Adv. Op. 97-15A (May 22, 1997).