

July 20, 2015

VIA ELECTRONIC MAIL

Office of Regulation 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”; Conflict of Interest Rule—Retirement  
Investment Advice (RIN 1210-AB32);  
Proposed Best Interest Contract Exemption (ZRIN 1210-ZA25)

To the Office of Regulation and Interpretations:

I write to comment on the rules proposed by the Employee Benefits Security Administration to broaden the definition of “fiduciary” under ERISA and the Internal Revenue Code, and to institute “best interest contract” requirements for financial representatives falling within this new definition. The purpose of this comment is to address certain legal flaws in the rulemakings and proposed rules.

The Department states that “changes in the marketplace” and its “experience” with the current definition of fiduciary have caused it to propose a new regulatory framework for broker-dealers and IRAs. Definition of the Term “Fiduciary”; Conflict of Interest Rule—Retirement Investment Advice, 80 Fed. Reg. 21,928, 21,932 (Apr. 20, 2015) (to be codified at 29 C.F.R. pts. 2509, 2510). The DOL also asserts that broker-dealers labor under conflicts of interest that cause them to act contrary to their client’s interests, which warrants a regulatory response by the Department. *Id.* at 21,934.

The Department’s assertion that “conflicted investment advice” by broker-dealers has resulted in substantial investment underperformance might—if accurate—be reason to call on Congress to enact corrective legislation. Indeed, Congress has already acted in the area by authorizing the Securities and Exchange Commission to establish a fiduciary standard of conduct for brokers and dealers consistent with the standard applicable to investment advisers under the Investment Advisers Act of 1940 (“IAA” or the “Advisers Act”). Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Pub. L. No. 111-203, § 913(g), 124 Stat. 1376, 1828 (2010). But the Department’s perceptions of broker-dealers

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and investment performance do not empower it to radically rewrite its long-standing definition of “fiduciary investment advice” in a manner that conflicts with ERISA’s plain statutory language, its common law roots, and the framework established by Congress for the regulation of broker-dealers and investment advisers. Nor do the Department’s policy views authorize it to deploy its exemptive authority to construct a whole new regulatory and enforcement regime for IRAs and broker-dealers.

For at least two overarching reasons, therefore, the Department’s expansive new regulatory program is legally flawed.

*First*, the Department’s proposed interpretation of “fiduciary” is vastly overbroad and impermissible. In enacting ERISA’s fiduciary definition, Congress drew upon principles of trust law and the law governing investment advisers and broker-dealers that must be considered in interpreting the statute today. *See Corning Glass Works v. Brennan*, 417 U.S. 188, 201 (1974); *Blitz v. Donovan*, 740 F.2d 1241, 1245 (D.C. Cir. 1984). Under trust law, a fiduciary relationship arises in the context of a relationship of special “trust and confidence” between the parties. The DOL proposal, however, would deem persons to be fiduciaries where those hallmarks of a fiduciary relationship are absent, for example, when making a recommendation regarding a single transaction. *See* 80 Fed. Reg. at 21,934. Further, ERISA’s reference to “render[ing] investment advice for a fee or other compensation” incorporates terminology in the IAA, which—in accordance with the industry understanding and practice when the IAA was enacted—excludes broker-dealers executing sales from the definition of “investment adviser.” That is because the payment to broker-dealers is principally for the product acquired or sold, not the advice. That limitation is incorporated in ERISA: The phrase “render[ing] investment advice for a fee” by its terms means that the payment is principally made for the investment advice provided, and not for execution of a financial transaction or the sale of a financial product.

*Second*, the Department lacks the authority to establish new standards and a regulatory and enforcement program for broker-dealers. In the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank”), Congress committed the authority to establish uniform fiduciary duty standards for broker-dealers and investment advisers to the SEC—the agency that has long held principal regulatory responsibility in that area—and only after the Commission completed a study on the effects of any such standards. DOL may not front-run the Commission by crafting its own new standards and enforcement program, and certainly may not do so by bootstrapping its authority to interpret “fiduciary” into a sweeping new regulatory program replete with private rights of action and mandatory class actions.

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## DISCUSSION

### I. The Department's Definition Of "Fiduciary" Is Vastly Overbroad And Impermissible.

The Department has proposed a definition of "fiduciary" so broad that it must be accompanied by seven carve-outs and six prohibited transaction exemptions to limit the scope of even a small portion of the vast new regulatory regime it would establish over broker-dealers and the IRA market. A regulatory definition that cannot function or be harmonized with generations of practice unless it is re-worked through a dizzying array of carve-outs and exemptions is, axiomatically, a definition that does not faithfully interpret the words Congress wrote.

ERISA does not allow for this expansive new definition. Indeed, as discussed below, its plain text precludes it.<sup>1</sup>

#### A. The Proposed Definition Conflicts With ERISA's Plain Text.

ERISA is a "comprehensive and reticulated statute," *Nachman Corp. v. PBGC*, 446 U.S. 359, 361 (1980), and its definition of "fiduciary" is no different. Under ERISA,

[A] person is a fiduciary with respect to a plan *to the extent* (i) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets, (ii) *he renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so*, or (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan.

29 U.S.C. § 1002(21)(A) (emphasis added).

Congress did not develop this provision in a vacuum, but drew from existing law. *See, e.g., Firestone Tire & Rubber Co. v. Bruch*, 489 U.S. 101, 110-11 (1989). That included the law of trusts and the law embodied in, and developed under, the IAA. *See infra* pp. 4-6.

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<sup>1</sup> For simplicity, this comment refers to the proposed rule's interpretation of ERISA's definition of "fiduciary," but the discussion applies equally to the Code's definition of "fiduciary," which is identical as relevant here.



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In interpreting the definition of “fiduciary,” therefore, both the common law of trusts and the IAA must be consulted, since it is presumed that “Congress is knowledgeable about existing law pertinent to the legislation it enacts.” *Goodyear Atomic Corp. v. Miller*, 486 U.S. 174, 185 (1988).

1. A fundamental principle of trust law is that a “fiduciary” relationship arises only under certain circumstances, specifically, where “special intimacy or . . . trust and confidence” exists between the parties. *Bogert’s Trusts & Trustees* § 481; *see also Black’s Law Dictionary* 753 (rev. 4th ed. 1951) (defining “fiduciary” based on the “trust and confidence involved” in the relationship). For example, at the time of ERISA’s enactment, courts had held relationships such as physician-patient or director-corporation/stockholder to be fiduciary based on the particularly close and trusting relationship between the parties. *See, e.g., Twin-Lick Oil Co. v. Marbury*, 91 U.S. 587, 588 (1876) (recognizing that “a director of a joint-stock corporation occupies [a] fiduciary relation[ship] [and] his dealings with the subject-matter of his trust or agency, and with the beneficiary or party whose interest is confided to his care” are protected by courts); *Hammonds v. Aetna Cas. & Sur. Co.*, 237 F. Supp. 96, 102 (N.D. Ohio 1965) (deeming physician a “fiduciary” to his patient where patient “entrusted” information to the doctor).

Relationships lacking that special degree of “trust and confidence”—such as everyday business interactions—are not fiduciary. The court in *In re Codman*, 284 F. 273, 274 (D. Mass. 1922), for example, rejected the contention that “the relation of the broker to his margin customers is a fiduciary or trust relation,” describing it instead as a “debtor and creditor” relationship. And in *Robinson v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 337 F. Supp. 107, 113-14 (N.D. Ala. 1971), the court concluded that a broker “had no fiduciary relationship to the plaintiff” where he was merely “executing the plaintiff’s orders on an open market.”

These principles were well established by the time of ERISA’s enactment and were incorporated into ERISA. *See Bruch*, 489 U.S. at 110-11. As the report of the House of Representatives stated in setting out ERISA’s definition of the term, “[a] fiduciary is one who occupies a position of confidence or trust.” H.R. Rep. No. 93-533, at 11 (1973); *see also id.* (“The fiduciary responsibility section, in essence, codifies and makes applicable to these fiduciaries certain principles developed in the evolution of the law of trusts.”). One who does not occupy that position of heightened trust and confidence cannot be considered a fiduciary under ERISA.

2. The law of trusts is not the only body of law that informs the meaning of “fiduciary” in ERISA. So, too, does the law embodied in, and developed under, the IAA. In the investment-advice prong of ERISA’s definition of fiduciary, Congress used the phrase

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“renders investment advice for a fee or other compensation.” That language reflects terminology in the IAA, which for decades had held a central place in the regulation of investment advisers, and which defines “investment adviser” as a person who “*for compensation . . . advis[es] others . . . as to the value of securities or as to the advisability of investing in, purchasing, or selling securities.*” 15 U.S.C. § 80b-2(a)(11) (emphasis added).

The language and history of the Advisers Act is informative of ERISA’s meaning in two ways. First, by the time of ERISA’s enactment, investment advisers were widely understood to be fiduciaries—and the *reason* they were fiduciaries was that they had a closer, deeper relationship with their clients than did other financial professionals. Thus, the Supreme Court wrote in 1963 that the Advisers Act “reflects a congressional recognition of the delicate fiduciary nature of an investment advisory relationship”; therefore, “Congress recognized the investment adviser to be” “a fiduciary.” *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 191, 194-95 (1963). In reaching this conclusion, the Court relied on legislative history that recognized the “personalized character of the services of investment advisers,” *id.* at 191, and cited congressional testimony that characterized investment advisers as having relationships of “trust and confidence with their clients,” *id.* at 190 (internal quotation marks omitted). The Court cited this legislative history two decades later in reiterating the fiduciary “character” of the investment-adviser relationship. *Lowe v. SEC*, 472 U.S. 181, 190 (1985). Being an investment adviser, the Court said, is a “personal-service profession [which] depends for its success upon a *close personal and confidential relationship* between the investment-counsel firm and its client. It requires *frequent and personal contact* of a professional nature between [the advisers] and [their] clients.” *Id.* at 195 (emphases altered and internal quotation marks omitted).

Second and related, when investment advisers were being described by the Court as having the sort of “close and personal” relationship with clients—characterized by “frequent and personal contact”—that rose to the level of a fiduciary relationship, the Court was not considering investment advisers in isolation, but rather *in contrast with* other financial professionals whose relationships did not rise to the same level, namely, broker-dealers. Thus, the Advisers Act included a carve-out which clarified that “investment adviser” did not include “any broker or dealer” who provided advice that was “solely incidental to the conduct of his business as a broker or dealer and who receives no special compensation therefor.” 15 U.S.C. § 80b-2(a)(11)(C).

This exemption from the definition of investment adviser was not introduced by the IAA, the D.C. Circuit has explained, but “reflected [a] distinction” then existing between the “two general forms of compensation” that financial professionals received in connection with offering investment assistance. *Fin. Planning Ass’n v. SEC*, 482 F.3d 481, 485 (D.C. Cir. 2007). “Some [representatives] charged only . . . commissions (earning a certain amount for



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each securities transaction completed). Others charged a separate advice fee (often a certain percentage of the customer's assets under advisement or supervision)." *Id.* This difference in compensation structures—and the notion that a fee for *advice* was suggestive of a fiduciary relationship, whereas a commission on a sale was not—was captured by the IAA in the broker-dealer exemption. A financial representative became an "investment adviser" when "[a]t least part [of] the charge to customers receiving advice [was] attributable to such advice," but not where the payment was principally for the sale of the product. SEC Op., 1940 SEC LEXIS 1466, at \*7 (1940); *see also Thomas v. Metro. Life Ins. Co.*, 631 F.3d 1153, 1166 (10th Cir. 2011) ("[T]he IAA excludes a broker-dealer who provides advice that is attendant to, or given in connection with, the broker-dealer's conduct as a broker or dealer, so long as he does not receive compensation that is (1) received in exchange for the investment advice, as opposed to . . . the sale of the product, and (2) distinct from a commission or analogous transaction-based form of compensation for the sale of a product."). As explained in the Senate and House reports, the broker-dealer exemption was "so defined as specifically to exclude . . . brokers (insofar as their advice is merely incidental to brokerage transactions for which they receive only brokerage commissions)." S. Rep. No. 76-1775, at 22 (1940); H.R. Rep. No. 76-2639, at 28 (1940).

Following the IAA's enactment, this limitation on "investment advice" was repeatedly recognized and enforced. In *Robinson*, for example, the district court concluded that the broker was not an investment adviser and "had no fiduciary relationship to the plaintiff" where "any investment advice was incidental to brokerage services." 337 F. Supp. at 113-14. The SEC emphasized that "render[ing] investment advice merely as an incident to . . . broker-dealer activities" does not by itself place broker-dealers "in a position of trust and confidence as to their customers." Broker-Dealer Registration, Exchange Act Release No. 4048, 1948 WL 29537, at \*7 (Feb. 18, 1948), *aff'd*, *Hughes v. SEC*, 174 F.2d 969 (D.C. Cir. 1949). *See also Kaufman v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 464 F. Supp. 528, 538 (D. Md. 1978) (broker not an investment adviser where "[t]here is no indication that [defendant] received any fees specifically for his advising [plaintiff]; rather it appears that the commissions received were for his services in effecting the transactions, not for his rendering of advice").

3. This understanding of what made investment advisers' relationship fiduciary in character—as well as the form of compensation associated with it, and the difference from a simple broker-dealer relationship—was well established when ERISA was enacted in 1974. Accordingly, when Congress used the phrase "renders investment advice for a fee or other compensation" in ERISA's fiduciary definition, it "is deemed to [have] know[n] the . . . judicial gloss given to [that] language and thus [to have] adopt[ed] the existing interpretation unless it affirmatively act[ed] to change the meaning," *Blitz v. Donovan*, 740 F.2d 1241, 1245 (D.C. Cir. 1984) (internal quotation marks omitted). *See also United States v. Wells*,

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519 U.S. 482, 491 (1997) (it is presumed “that Congress incorporates the common-law meaning of the terms it uses if those terms have accumulated settled meaning under the common law and the statute does not otherwise dictate” (alterations and internal quotation marks omitted)); *Corning Glass Works v. Brennan*, 417 U.S. 188, 201 (1974) (“[W]here Congress has used technical words or terms of art, ‘it [is] proper to explain them by reference to the art or science to which they [are] appropriate.’” (alterations in original) (quoting *Greenleaf v. Goodrich*, 101 U.S. 278, 284 (1880))). Any interpretation of the investment-advice prong must therefore be consistent with (1) the recognition under the law of trusts that only relationships marked by a heightened degree of trust and confidence are fiduciary, and (2) the common law recognition—embodied in the IAA—that broker-dealers providing advice incidental to the sale of a product are not providing *investment advice* in a *fiduciary* capacity. That meaning cannot be altered by Department of Labor regulation. See *Chevron U.S.A. Inc. v. Nat’l Res. Def. Council, Inc.*, 467 U.S. 837, 842-43 (1984); *Thiess v. Witt*, 100 F.3d 915, 918 (Fed. Cir. 1996) (agency interpretation of “compensation” impermissible because it conflicted with the term’s established meaning in the employment context).

The current regulatory interpretation, which was adopted shortly after enactment of ERISA, reflected these established limitations on the meaning of “fiduciary.” See 29 C.F.R. § 2510.3-21(c). The 1975 regulation appropriately clarifies that investment advice will trigger fiduciary duties only when rendered “on a regular basis to the plan,” “pursuant to a mutual agreement” that the services will be a “primary basis” on which the plan makes investment decisions. *Id.* Providing advice “on a regular basis,” for example, reflects the Supreme Court’s recognition in *Lowe*, 472 U.S. at 191-95, that a fiduciary typically renders advice in a close relationship characterized by “frequent” contact. This helps ensure presence of the heightened “trust and confidence” associated with fiduciary status, and that the advice is not merely “incidental” to the sale of a product.

The Department’s proposal, by contrast, radically departs from these settled limitations. The proposed rule conflicts with trust-law principles because it would deem persons not in special relationships of “trust and confidence”—e.g., broker-dealers executing sales—to be fiduciaries. To make a person a “fiduciary” for providing a “one-time . . . recommendation or valuation” (80 Fed. Reg. at 21,934), for example, cannot reasonably be viewed as consistent with the special relationship of trust and confidence envisioned under the law of trusts—a relationship, the Supreme Court has said, characterized by “frequent and personal contact.” *Lowe*, 472 U.S. at 195 (emphasis omitted). The proposal reflects no consideration of this trust-law principle (or others)—even though the DOL acknowledges that the law of trusts must inform its interpretation of ERISA, 80 Fed. Reg. at 21,932, 21,938.



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The method applied by the Department in its proposal is instead to identify acts that in its opinion *should be* performed by fiduciaries, and then to dub those actors fiduciaries even when under the accepted meaning of that term and as a matter of historical fact, they are not. In doing so, the Department departs not only from the accepted understanding of what relationships are fiduciary in character, but also from the statutory requirement that an investment fiduciary “render[ ] investment advice for a fee.” Under this language, it is the “advice” that must be the thing paid for, not the product that the purchaser selects, or the transaction she conducts.<sup>2</sup> Because a commissioned broker-dealer is only paid if a product is purchased, the client’s payment is plainly for the product, not for advice that might have accompanied the sale.

The very definition of a broker is a “person engaged in the business of effecting transactions in securities for the account of others,” 15 U.S.C. § 78c(a)(4)(A); by definition, he does not provide investment advice for a fee. Congress recognized this in the IAA by excluding ordinary broker services from the “investment adviser” definition, as discussed above. The Department’s proposed definition ignores that exclusion, and instead encompasses many activities customarily performed by broker-dealers that are not properly considered “advice.” For example, under the proposal, a broker’s sales pitch is transformed into advice when provided to a retail investor, but the same pitch is not advice when made to an “expert plan investor.” The Department’s reasoning that an expert buyer will understand “that it is buying an investment product, not advice,” but that a retail buyer will not (80 Fed. Reg. at 21,941-42), has no basis in principle or the long-standing financial regulatory framework established by Congress. Sales pitches are a common experience, whether for cars, electronics, or a range of financial products, and no ground exists for concluding that a broker’s offer is transformed into “advice” when tendered to a potentially less sophisticated buyer.

The extent to which the Department’s proposal captures activities ordinarily conducted by broker-dealers is, in fact, powerful evidence of the over-breadth of its “fiduciary” definition. At law, fiduciaries and broker-dealers are distinct, and broker-dealers are paid by commission. But with its proposal, the Department first mis-defines “fiduciary”

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<sup>2</sup> The Department’s proposed interpretation is also inconsistent with the term “render.” To “render” is “to pronounce or declare (a judgment, verdict, etc.), as in court,” *Webster’s New World Dictionary* 1136 (3d ed. 1988), or “to furnish for consideration, approval, or information: as (1) to hand down (a legal judgment) (2) to agree on and report (a verdict),” *Merriam-Webster’s Collegiate Dictionary* 1054 (11th ed. 2003). That means something more than merely making investment suggestions in the context of a sales transaction.



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so broadly that it sweeps in hundreds of thousands of broker-dealers, and then locates a supposed conflict of interest in broker-dealers being paid in exactly the manner they by definition *are* paid. *See Fin. Planning Ass'n*, 482 F.3d at 485 (“Some [representatives] charged only commissions (earning a certain amount for each securities transaction completed). Others [which the Advisers Act treats as fiduciaries] charged a separate advice fee (often a certain percentage of the customer’s assets under advisement or supervision).”). It is not broker-dealers’ compensation structure that is flawed, it is the Department’s attempt to define broker-dealers as fiduciaries.

**B. The Department’s Interpretation Also Conflicts With The Statutory Definition Of “Fiduciary” As A Whole.**

Section 3(21) of ERISA identifies three ways that a person or entity becomes a fiduciary: by (i) “exercis[ing] any discretionary authority or discretionary control” over the “management” of a plan or its assets; (ii) “render[ing] investment advice for a fee or other compensation, direct or indirect”; and (iii) exercising “discretionary authority or discretionary responsibility in” the plan’s “administration.” 29 U.S.C. § 1002(21)(A). The management and administration of a plan are central functions, involving a meaningful, substantial, and ongoing relationship to the plan. Subsection (ii) must be read in a manner consistent with these provisions. Congress would not, for two of the provisions, have required a substantial and direct connection to the essentials of plan operation, and for the provision lying in-between have required only a short-term relationship whose essence was sales rather than significant investment advice provided on a regular basis. *See Pollard v. E.I. du Pont de Nemours & Co.*, 532 U.S. 843, 852 (2001) (“[W]e must not be guided by a single sentence or member of a sentence, but look to the provisions of the whole law.” (alteration in original and internal quotation marks omitted)); *Garcia v. Vanguard Car Rental USA, Inc.*, 540 F.3d 1242, 1247 (11th Cir. 2008) (“By construing proximate statutory terms in light of one another, courts avoid giving ‘unintended breadth to the acts of Congress.’” (quoting *Gustafson v. Alloyd Co.*, 513 U.S. 561, 575 (1995))). This further demonstrates that the definition in the proposed regulation is overbroad.

**C. The Department Errs By Inexplicably Departing From Its 2005 Advisory Opinion To Treat Actions In Connection With Rollovers As Fiduciary.**

A significant consequence of the errors by the Department described above is that the proposed rule would make *any* advice regarding investments of distributions from an ERISA plan or IRA “fiduciary advice,” regardless whether the advice is merely incidental to a sale (or proposed sale), or whether it is specifically paid for, or even related to assets no longer held by the plan. Thus, the proposed rule appears so broad that it might cover advice

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regarding investment of a distribution from an ERISA plan into an equity or debt security rendered on a one-time basis.

That is improper, and directly contradicts the DOL's conclusion just ten years ago that a recommendation regarding a rollover of plan assets to an IRA does not constitute fiduciary advice. *See* Advisory Opinion 2005-23A. For an act to be fiduciary in character, ERISA (and the Code) require, first, there be "advice" related to an "investment." 29 U.S.C. § 1002(21)(A)(ii). A distribution is not an investment; it follows that a recommendation to rollover plan assets is outside the scope of the statute because it does not "concern[ ] a particular investment."<sup>3</sup> Advisory Opinion 2005-23A. Second, advice provided with respect to the *proceeds* of a distribution does not fall within ERISA because the statute requires that the advice relate to "any moneys or other property of [the ERISA] plan." 29 U.S.C. § 1002(21)(A)(ii). Upon distribution, the proceeds are no longer "moneys or other property" of the plan and therefore do not fall within the scope of the statute. *See* Advisory Opinion 2005-23A; *see also, e.g., Beeson v. Fireman's Fund Ins. Co.*, 2009 WL 2761469, at \*6 (N.D. Cal. Aug. 31, 2009) (stating that "providing financial advice as to the investment of non-plan assets is generally not a fiduciary duty under ERISA" and noting that a DOL publication "[did] not state that providing investment advice (or hiring advisors to do so) will be considered a fiduciary act simply because the advice may cause participants to remove money from a plan").

ERISA's plain language, accordingly, permits only one conclusion about whether actions in connection with rollovers are fiduciary: They are not. Unlike the 2005 Advisory Opinion, the DOL's current position regarding rollovers cannot be reconciled with the statutory text. For that reason, it is precluded. *See Chevron*, 467 U.S. at 842-43.

## **II. The Department Lacks Statutory Authority To Adopt Its New Proposed Regulatory Framework.**

Together, the Department's "fiduciary" rule and "BIC" Exemption would impermissibly expand the Department's authority outside its jurisdiction. As the Department admits, the principal goal of the rulemaking is to regulate IRAs and the broker-dealers who offer them (*see* 80 Fed. Reg. at 21,928, 21,932)—even though the DOL has no enforcement authority over IRAs. Congress, moreover, recently made clear that the SEC, not the DOL, should be the arbiter of what fiduciary standards of conduct should govern broker-dealers,

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<sup>3</sup> Similarly, providing a valuation opinion or appraisal is not equivalent to "render[ing] investment advice." The valuation provides information regarding the market value of a security or other property, but does not itself recommend its purchase.

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and what regulatory action should be taken, if any. In addition, the DOL's proposed BIC Exemption, which would affect most of the IRA market, purports to create a private right of action for plans and participants to sue broker-dealers who offer IRAs for breach of contract. But only Congress may create private rights of action, *Alexander v. Sandoval*, 532 U.S. 275, 286 (2001), and nothing in ERISA or the Internal Revenue Code permits the cause of action proposed in the BIC Exemption. In fact, section 4975 of the Code, which prohibits certain transactions involving IRAs, does not provide for any civil enforcement. The BIC is also flawed because the DOL lacks authority to ban class action waivers in arbitration agreements, *cf.* 15 U.S.C. § 78o(o) (permitting SEC to regulate arbitration agreements of "customers or clients of" broker-dealers for disputes arising under the securities laws and regulations), and its attempt to enact such a ban conflicts with the mandate of the Federal Arbitration Act ("FAA") that arbitration agreements be enforced according to their terms, *CompuCredit Corp. v. Greenwood*, 132 S. Ct. 665, 669 (2012).

In short, DOL is the regulator of neither the IRA market in particular nor the financial industry in general, and it cannot regulate through "exemption" matters that are beyond its authority to regulate affirmatively. In a word, it cannot create "backdoor regulation" by "manipulat[ing] the safe harbor criterion [of a regulation] to compel different or broader compliance" by actors in that field. *Hearth, Patio & Barbecue Ass'n v. U.S. Dep't of Energy*, 706 F.3d 499, 507-08 (D.C. Cir. 2013).

## **A. The SEC, Not The DOL, Has Authority To Establish Standards Of Conduct For Broker-Dealers.**

The DOL seeks to apply fiduciary standards of conduct to broker-dealers. Congress, however, recently considered the process for a possible extension of fiduciary duties to broker-dealers, and in Dodd-Frank gave the SEC, which has nearly eighty years' experience regulating financial markets, the authority to adopt a uniform fiduciary standard following a study of the effects of such a regulatory change, and subject to certain express limitations. This recent demonstration of congressional intent confirms that the Department lacks the power to promulgate the proposed rules.

Section 913 of Dodd-Frank directs the SEC to evaluate the standards of care that currently govern broker-dealers and investment advisers. Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Pub. L. No. 111-203, § 913, 124 Stat. 1376, 1824 (2010). Specifically, it instructs the SEC to consider "the potential impact of eliminating the broker and dealer exclusion from the definition of 'investment adviser' under section 202(a)(11)(C) of the Investment Advisers Act of 1940[.]" *Id.* § 913(c)(10). Dodd-Frank also empowers the SEC to "promulgate rules to provide that, with respect to a broker or dealer, when providing personalized investment advice about securities to a retail customer . . . the



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standard of conduct . . . shall be the same as the standard of conduct applicable to an investment adviser.” *Id.* § 913(g)(1).

The DOL’s attempt to establish a new standard of care for broker-dealers disregards Congress’s expressed directive that such a decision is for the SEC. The Supreme Court recently instructed that, where “a question of deep economic and political significance that is central to [a] statutory scheme” exists, “had Congress wished to assign that question to an agency, it surely would have done so expressly.” *King v. Burwell*, No. 14-114, 2015 WL 2473448, at \*8 (U.S. June 25, 2015) (internal quotation marks omitted). Further, “[i]t is especially unlikely that Congress would have delegated this decision to [an agency] [with] no expertise” in the matter. *Id.* Congress gave DOL no such authority here, but *did* expressly assign the question of further broker-dealer regulation—which would have broad effects on financial professionals and their clients—to an agency with expertise in the industry: the SEC. In doing so, Congress did not leave the door open for DOL to use the Tax Code to craft and impose its own fiduciary duties for more than half the assets in broker-dealer retail customer accounts.

The Department’s encroachment on the SEC (and FINRA) is also foreclosed by *FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 143, 161 (2000). There, the Supreme Court held that the Food and Drug Administration lacked authority to regulate tobacco because of the “tobacco-specific legislation that Congress ha[d] enacted over the [previous] 35 years.” *Id.* at 143. At the time a statute is enacted, the Court explained, it may have “a range of plausible meanings” that could seem to permit agency regulation, but “[o]ver time . . . subsequent acts can shape or focus those meanings.” *Id.* In particular, later-enacted statutes that “more specifically address the topic at hand” may occupy the field in a manner that forecloses agency action, even if that subsequent legislation does not explicitly block the agency’s jurisdiction. *See id.* at 127, 143, 157. So, here, even if DOL once possessed authority to promulgate regulations of the nature proposed (it did not), Dodd-Frank “more specifically address[es]” procedures for evaluating the standard of care for broker-dealers, committing it to SEC review and, possibly, SEC regulation. Action on the subject is foreclosed to the Department.

The specific terms of the Department’s proposed rules are barred as well. Dodd-Frank requires that any new standard of conduct for broker-dealers be “the same” as “applicable to an investment adviser under section 211” of the Advisers Act. Dodd-Frank § 913(g). The standards imposed by the new rules are far more onerous than under the IAA. In Dodd-Frank Congress also provided that “[t]he receipt of compensation based on commission or other standard compensation for the sale of securities shall not, in and of itself, be considered a violation of such standard applied to a broker or dealer.” *Id.* DOL’s

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“fiduciary” rule makes broker-dealers’ “standard compensation” a prohibited transaction, with only partial relief (supposedly) available through the unadministrable BIC Exemption.

The Dodd-Frank provisions regarding a potential uniform fiduciary standard show the analysis underlying the Department’s rules to be flawed as well. Congress instructed the SEC to conduct a study and report to Congress before adopting a new standard for broker-dealers, enumerating in detail the potential effects on customers that the SEC study “shall” consider, including “the potential impact on access of retail customers to the range of products and services offered by brokers and dealers,” and loss of access to “personalized investment advice.” Dodd-Frank §§ 913(c)(9)-(10), 913(d). Commenters in the current rulemaking will show that these (and other) effects of the Department’s rules will be severe, yet the Department makes no attempt to consider these effects in its “regulatory impact analysis.” That is clear error: The proposals’ effect on access to professional financial assistance was an “important aspect of the problem” that the Department was obligated to consider under any circumstance, *Motor Vehicle Mfrs. Ass’n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983), and certainly the Department could not fail to address the issue when Congress directed the SEC to consider that very thing before imposing fiduciary standards on broker-dealers. The Department must conduct that assessment and make it available for public review and comment. See *Chamber of Commerce v. SEC*, 443 F.3d 890, 894, 900 (D.C. Cir. 2006).

The inappropriateness of the DOL leaping out in front of the SEC is confirmed by the findings of SEC staff in the study they performed under Dodd-Frank. After examining the potential effect of eliminating the broker-dealer exclusion, SEC staff recommended against such an amendment, in view of the negative effect on consumers. SEC Study on Investment Advisers & Broker-Dealers 140, 152 (2011). As the staff explained: “If, in response to the elimination of the broker-dealer exclusion, broker-dealers elected to convert their brokerage accounts from commission-based accounts to fee-based accounts, certain retail customers might face increased costs, and consequently the profitability of their investment decisions could be eroded, especially accounts that are not actively traded[.]” *Id.* at 152 (footnote omitted). IRAs are just such accounts, yet the DOL fails to give appropriate consideration to those adverse effects.

Others with responsibility over broker-dealers have voiced similar concerns. The Chairman and CEO of FINRA, Richard Ketchum, has said the SEC “should lead” the drafting of a fiduciary standard applicable to broker-dealers, because it has the necessary expertise and is better positioned than DOL to design and implement the standard. *Oversight of the Financial Industry Regulatory Authority: Hearing Before the Subcomm. on Capital Mkts. & Gov’t Sponsored Enters. of the H. Comm. on Fin. Servs.*, 114th Cong. (2015) (statement of Richard G. Ketchum, Chairman and CEO of FINRA). In testimony before



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Congress, Chairman Ketchum expressed concern that the DOL's proposed rule would result in conflicting standards of care and stated that "the right way to move forward is for . . . the [SEC] to look [at] the possibility of a balanced fiduciary standard across all products." *Id.* These cautions from the self-regulatory organization with responsibility over broker-dealers should be given great weight, and further demonstrate why proceeding with these proposed rules is particularly inappropriate in light of the SEC's authority over the financial industry.

**B. The Department Cannot Leverage Its Interpretive Authority To Exercise Enforcement Authority Not Conferred By Congress.**

The DOL does not have regulatory authority over IRAs because IRAs—when sold to individual clients—are not "employee welfare benefit plans" or "employee pension benefit plans" that are "established or maintained by an employer or by an employee organization." *See* 29 U.S.C. § 1002(1) & (2). To be sure, the Department has authority to interpret the definition of "fiduciary" under ERISA and the Internal Revenue Code. Its *enforcement* authority, however, is limited to ERISA. *See* Reorganization Plan No. 4 of 1978, § 105. Only the Treasury Department has authority to enforce Section 4975 of the Code, an authority that is restricted to imposing excise taxes and conducting audits. *Id.* As the DOL acknowledges in the proposal, ERISA's duties of prudence and loyalty do not apply to IRA fiduciaries, and IRA fiduciaries are not liable under ERISA for losses arising from breaches of such duties: "Under the Code, advisers to IRAs are subject only to the prohibited transaction rules," and "no private right of action under ERISA is available to IRA owners." 80 Fed. Reg. at 21,938.

This admission is fatal to the DOL's attempt in the BIC Exemption to leverage its interpretive authority into enforcement power over matters outside the Department's jurisdiction. Among other things, DOL conditions the BIC Exemption—which is necessary for the rule's newly-discovered fiduciaries to continue long-standing compensation practices—on the fiduciary's consent to be sued by ERISA plans, IRAs, participants, and others for breach of contract related to the best interest standards created in the rule. Proposed Best Interest Contract Exemption, 80 Fed. Reg. 21,960, 21,962, 21,972 (Apr. 20, 2015) (to be codified at 29 C.F.R. pt. 2550). That is a new private right of action. It is axiomatic, however, that only Congress, not an agency, may create a cause of action. In *Sandoval*, for instance, the Supreme Court rejected the government's argument that "the regulations contain rights-creating language and so must be privately enforceable." 532 U.S. at 291. "Language in a regulation may invoke a private right of action that Congress through statutory text created, but it may not create a right that Congress has not. . . . [I]t is most certainly incorrect to say that language in a regulation can conjure up a private cause of action that has not been authorized by Congress." *Id.* (citation omitted).



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What *Sandoval* forbids is what the DOL attempts to do. Nothing in ERISA or the Code even hints that a state-law contract action can be brought against purported fiduciaries to enforce statutory provisions. ERISA's civil remedies are limited both in nature and scope, *Great-W. Life & Annuity Ins. Co. v. Knudson*, 534 U.S. 204, 209-10 (2002), and the statute broadly preempts most state law, including breach-of-contract actions, *Cromwell v. Equicor-Equitable HCA Corp.*, 944 F.2d 1272, 1275 (6th Cir. 1991). Further, ERISA's remedies have no application to non-ERISA plans such as IRAs. See 29 U.S.C. § 1002(1) & (2). The remedies under the Code are even more restricted than ERISA's, extending only to conducting audits and imposing taxes. 26 U.S.C. § 4975; see also Reorganization Plan No. 4 of 1978, § 105. Accordingly, ERISA, the Code, and basic principles of separation of powers preclude DOL's attempt to create its new "BIC" private rights of action. See also *Mertens v. Hewitt Assocs.*, 508 U.S. 248, 254 (1993) (stating Court's "unwillingness to infer causes of action in the ERISA context, since that statute's carefully crafted and detailed enforcement scheme provides strong evidence that Congress did *not* intend to authorize other remedies that it simply forgot to incorporate expressly" (internal quotation marks omitted)); *Transamerica Mortg. Advisors, Inc. v. Lewis*, 444 U.S. 11, 19 (1979) ("[I]t is an elemental canon of statutory construction that where a statute expressly provides a particular remedy or remedies, a court must be chary of reading others into it.").

It is no answer that the DOL has interpretative authority with respect to the definition of "fiduciary" in both statutes. The courts will reject an agency's attempt to use interpretive authority to regulate beyond that authority. In *American Bankers Ass'n v. SEC*, 804 F.2d 739, 754-55 (D.C. Cir. 1986), for example, the D.C. Circuit explained that "[t]he [Commission] cannot use its definitional authority to expand its own jurisdiction and to invade the jurisdiction" of other agencies through rulemaking. In that case, the agency was authorized to regulate banks, not broker-dealers, but wrongly sought to "redefine" "bank" in a way that gave it authority over broker-dealers as well. *Id.* at 742-43. See also *Business Roundtable v. SEC*, 905 F.2d 406, 412-13 (D.C. Cir. 1990) (SEC had power to mandate listing standards, but exceeded its authority by attempting to leverage that power to regulate corporate governance). And in *Home Care Ass'n of America v. Weil*, 2014 U.S. Dist. LEXIS 176307, at \*14-15 (D.D.C. 2014), the court rejected the DOL's attempt to use "its definitional authority" in a way that eliminated part of a statutory exemption, explaining that "Congress surely did not delegate to the Department of Labor . . . the authority to issue a regulation that transforms defining statutory terms into drawing policy lines." So, here, the DOL seeks to define "fiduciary" in a way that gives it authority over plans and persons outside its reach, and then—having defined the term in an impossibly onerous manner—wields its exemptive authority to offer clemency to those who are willing to accede to new duties and private rights of action that have no basis in the statute DOL administers. But the Department may not conduct "backdoor regulation" through manipulation of "safe harbor criterion." *Hearth, Patio & Barbecue Ass'n*, 706 F.3d at 507-08. See also *Chamber of*

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*Commerce v. U.S. Dep't of Labor*, 174 F.3d 206, 210 (D.C. Cir. 1999) (concluding OSHA had authority to conduct inspections, but could not use that as “leverage” to impose obligations not required by law).

“[I]t is fundamental that an agency may not bootstrap itself into an area in which it has no jurisdiction.” *Adams Fruit Co. v. Barrett*, 494 U.S. 638, 650 (1990) (internal quotation marks omitted). That is what the DOL attempts to do through these proposals, and for this reason too, the proposals are impermissible.

**C. The Department Lacks Authority To Ban Class Action Waivers In Connection With Arbitration Agreements.**

The Department also exceeds its statutory authority by purporting, in the BIC Exemption, to bar all waivers of participation in class actions or other representative actions, without regard to whether those waivers are in connection with arbitration agreements. 80 Fed. Reg. at 21,973, 21,985.

Under the FAA, valid arbitration agreements must be enforced according to their terms unless the FAA “has been overridden by a contrary congressional command.” *CompuCredit*, 132 S. Ct. at 669 (internal quotation marks omitted); *see also, e.g., Am. Express Co. v. Italian Colors Rest.*, 133 S. Ct. 2304, 2309-11 (2013) (rule applies even to statutes that “expressly permit[] collective actions”). This includes arbitration provisions containing class waivers, which the Supreme Court has repeatedly upheld. *Italian Colors*, 133 S. Ct. at 2312; *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 1748 (2011). “When [Congress] has restricted the use of arbitration,” moreover, “it has done so with . . . clarity.” *CompuCredit*, 132 S. Ct. at 672.

Nothing in ERISA gives DOL clear authority—or any authority—to preclude financial institutions and their clients from entering into and enforcing arbitration agreements that include class waivers. *See Kramer v. Smith Barney*, 80 F.3d 1080, 1084 (5th Cir. 1996) (“Congress did not intend to exempt statutory ERISA claims from the dictates of the [FAA].”); *Bird v. Shearson Lehman/Am. Express, Inc.*, 926 F.2d 116, 120 (2d Cir. 1991) (concluding ERISA does not preclude waiver of a judicial forum for ERISA claims). As for Code Section 4975, it is not enforceable through a private right of action at all, *see supra*,

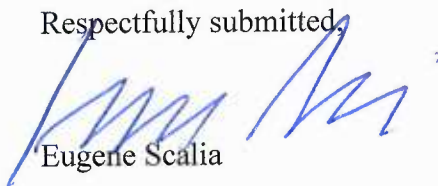
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and plainly furnishes DOL no authority to regulate parties' arbitration agreements. Simply, DOL's lack of authority to regulate arbitration agreements is dispositive of its attempt to bar class waivers in those agreements. *See CompuCredit*, 132 S. Ct. at 672.

In this respect, as in so many others in this bundle of proposed rules, the Department has overstepped its bounds.

Respectfully submitted,

A handwritten signature in blue ink, appearing to read "Eugene Scalia", is written over the typed name.

Eugene Scalia

ES/bmr

cc: Office of Exemption Determinations