Davis & Harman LLP

September 9, 2015

Office of Regulations and Interpretations
Employee Benefits Security Administration
Attn: Conflict of Interest Rule
Room N-5655
U.S. Department of Labor
200 Constitution Avenue NW
Washington, DC 20210

RE: RIN 1210-AB32 – Conflict of Interest Rule

Dear Sir or Madam:

On behalf of a group of firm clients, I am writing today to provide additional comments on the Department of Labor's ("DOL") proposed new definition of a fiduciary, the proposed new prohibited transaction exemptions, and the proposed modifications of existing exemptions (together referred to as the "proposal"). As set forth in detail in our prior letter, while we share the belief that firms should act in their clients' best interest, the DOL's proposal, as currently drafted, is unworkable.

I plan to submit two comment letters during this second comment period. This letter focuses exclusively on one process issue: ***our concern that the decision not to re-propose appears to have been made by DOL before the hearing even started and before the second comment period began, thus indicating that the decision was made without considering public input, contrary to the law***. The second letter will address substantive issues that were raised at the hearing or arose after the close of the first comment period on July 21, 2015.

DOL should re-propose. We urge the DOL to re-propose the regulation. The current proposal would have the very serious adverse effects that were described in our original comment letter, such as widely depriving small businesses and small accounts of access to investment and distribution assistance and reducing retirement savings by as much as $80 billion annually.

Reading the comment letters and listening to the hearing only further underscored our view that the DOL needs to re-propose. The range of important issues raised in the comment letters and at the hearing was staggering, far greater than I can recall with respect to any regulatory project since I began working in this area over 30 years ago. And even more concerning, DOL needs to address substantially all of the issues raised to make the proposal workable. For example, there is a long list of reasons why no financial firm that I have spoken to is planning to use the "best interest contract exemption" ("BICE"). If most of those reasons are addressed but some are not, financial firms will still not be able to use the BICE. So there is enormous pressure to get this regulation right, not just mostly right.

In short, there are a staggering number of issues, and it is critical that they are resolved correctly. In this context, the chances that the next version of the proposal gets the issues exactly right seem very low. The emphasis should be on getting this right, not on getting this done on a particular schedule.

Concern that the decision not to re-propose was apparently made before the DOL hearing had even started. In light of this situation, we were very concerned about the letter that Secretary Perez sent to Congresswoman Ann Wagner dated August 7, 2015. The August 7th letter was in response to a bipartisan letter sent to Secretary Perez dated July 29, 2015. The bipartisan letter made one core request – for DOL to re-propose the regulation due to the problems with the proposal, the extensive comments, and the importance of the issues being addressed. In response, Secretary Perez pointed to the work that has been done on the proposal and the importance of the proposal and concluded: "For these reasons, we will move forward towards issuing a Final Rule that balances the input we received."

In context, there seemed to be very little doubt that the Secretary was saying no to the request that DOL re-propose. The bipartisan letter had one request: please re-propose. The response said that DOL will move forward with a final rule.

As discussed further below, under the Administrative Procedure Act, any decision regarding whether to re-propose is required by law to be made based on the record and the public input received and the rule changes needed to reflect that input. The Secretary's letter was dated August 7th, which was (1) before the hearing started, (2) before the second comment period started, and (3) before the DOL could possibly have read and analyzed the thousands of pages of comment letters from the first comment period.

Under the law, when is a re-proposal required? In determining whether finalization of a rule is appropriate, the long-standing test that courts have applied is whether the final rule is a "logical outgrowth" of the proposed rule. This is sometimes discussed in terms of whether the proposed rule "sufficiently foreshadowed" the final rule. The idea is that if the final rule includes materially different rules that interested parties did not have a chance to comment on, then finalization of the rule is not appropriate; rather, if the agency wants to move forward with the rule, the agency must re-propose. Set forth in the Appendix to this letter are examples of cases on this issue.

Analysis. The DOL has stated publicly that the next version of the rule will be "materially" different from the proposal. If it is indeed materially different, then it is possible that under the case law, it should be re-proposed. It is also possible that under the case law that the next version is a "logical outgrowth" of the proposal, despite the material changes. But until all the comments are received and considered, how can DOL possibly figure out the extent of the changes that will be made and thus whether the next version of the rule is a logical outgrowth of the proposal?[1]

Even a DOL official at the hearing acknowledged that it was too early to decide whether DOL needs to re-propose. But this was five days after Secretary Perez sent a letter stating that the DOL would move towards a final rule; in other words, the decision had already been made.

[1] As noted, we strongly believe that the rule must be re-proposed. If the proposal is not ***very*** materially modified, the rule will be unworkable. If the rule is modified as materially as it needs to be, re-proposal is clearly required under the standard described above.

Respect for the openness of the process. We have great respect for the open manner in which DOL has sought input since the release of the proposal in April of this year. The DOL is to be commended on its dedication to meeting with and listening to interested parties. And Secretary Perez is to be specifically applauded for setting the tone for this open process in many ways, including meeting with many stakeholders himself on numerous occasions. But if decisions are being made by DOL without regard to the input being provided, that is not appropriate, nor is it consistent with the law.

In short, we urge the DOL to re-propose and not adhere to a decision made before hearing and the second comment period. Thank you for your consideration of the views expressed in this letter.

Sincerely,

Kent A. Mason

APPENDIX

CASE LAW REGARDING WHEN FINALIZATION OF A RULE IS NOT APPROPRIATE AND RE-PROPOSAL IS REQUIRED IF THE AGENCY WANTS TO MOVE FORWARD WITH THE RULE

- "While 'a final rule need not be identical to the original proposed rule,' when the final rule 'deviates too sharply from the proposal, affected parties will be deprived of notice and an opportunity to respond to the proposal.' ... The test is whether the final rule is a 'logical outgrowth' of the proposed rule. If 'a new round of notice and comment would provide the first opportunity for interested parties to offer comments that could persuade the agency to modify its rule,' then the final rule is not a 'logical outgrowth.'" Doe v. Rumsfeld, 341 F. Supp. 2d 1, 14 (D.D.C. 2004) (citations omitted).

- "The logical-outgrowth doctrine typically applies where an agency publishes a notice of proposed rulemaking ('NPRM'), receives comments, and issues a final rule whose contours differ substantially from those described in the NPRM…The 'key focus' of the logical-outgrowth inquiry remains whether the purposes of notice and comment have been served." AFL-CIO v. Chao, 496 F. Supp. 2d 76, 86 (D.D.C. 2007).

- *"The 'logical outgrowth' test is satisfied if interested parties 'should have anticipated' the agency's final course in light of the initial notice.'* … As the Supreme Court recently explained, the object of the logical outgrowth test 'is one of fair notice.' … It is certainly true that a notice can be 'too general to be adequate.' … '*Agency notice must describe the range of alternatives being considered with reasonable specificity*[;][o]therwise, interested parties will not know what to comment on.'" Owner-Operator Indep. Drivers Ass'n, Inc. v. Fed. Motor Carrier Safety Admin., 494 F.3d 188, 209 (D.C. Cir. 2007) (citations omitted) (emphasis added).

- "'A rule is deemed a logical outgrowth if interested parties 'should have anticipated' that the change was possible, and thus reasonably should have filed their comments on the subject during the notice-and-comment period.' ... Our Circuit has stated that '[t]his means that a final rule will be deemed the logical outgrowth of the proposed rule if a new round of notice and comment would not provide commentators with 'their first occasion to offer new and different criticisms which the agency might find convincing.'' ... If a 'final rule deviates too sharply from the proposal, affected parties will be deprived of notice and an opportunity to respond to the proposal.' ... A final rule is not necessarily invalid for lack of notice, however, simply because the position it adopts differs somewhat from the position in the proposed rule. ... [A] final rule is not the logical outgrowth of the proposed rule if the agency's final rule is the *opposite* of the proposed rule. ... '[i]f the APA's notice requirements mean anything, they require that a reasonable commenter must be able to trust an agency's representations about *which particular* aspects of its proposal are open for consideration.'" Nat'l Ass'n of Home Builders v. U.S. Army Corps of Engineers, 453 F. Supp. 2d 116, 124-25 (D.D.C. 2006) (citations omitted).

- "[A]gencies may not 'pull a surprise switcheroo on regulated entities.'" Allina Health Servs. v. Sebelius, 746 F.3d 1102, 1108 (D.C. Cir. 2014).

- "Courts have not allowed for agency's [sic] to write into the proposed rule language that the agency can later point in asserting that the rule provided adequate notice, otherwise known as 'catch-all notice.' ... Catch-all notice is problematic because it allows an agency to 'propose a rule and state that it might change that rule without alerting any of the affected parties to the scope of the contemplated change, or its potential impact and rationale, or any other alternatives under consideration.'" Pub. Citizen, Inc. v. Mineta, 427 F. Supp. 2d 7, 15 (D.D.C. 2006) (citations omitted).