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Office of Regulations and Interpretations
Employee Benefits Security Administration
Room N-5655
U.S. Department of Labor
200 Constitution Avenue, NW
Washington, D.C. 20210
ATTN: Brokerage Windows RFI

Re: Brokerage Windows RFI

Ladies and Gentlemen:

This letter responds to the Request for Information Regarding Standards for Brokerage Windows in Participant-Directed Individual Account Plans (the "RFI") published by the Department of Labor (the "Department") in the Federal Register on August 21, 2014. The RFI notice states that it will assist the Department in determining whether and to what extent regulatory standards or other guidance concerning the use of brokerage windows by plans are necessary to protect participants' retirement savings.

These comments are submitted on behalf of the group of financial service companies for which FMR LLC is the parent corporation (collectively, "Fidelity"). Fidelity provides investment management, recordkeeping, brokerage, and directed trustee and custodial services to thousands of participant-directed individual account plans covering millions of participants. As discussed in detail below, some of these plans offer a brokerage window or similar arrangement to plan participants, in most cases alongside a menu of designated investment alternatives.

We appreciate the Department's decision to follow an information gathering process in order to determine whether the Department should undertake any rule-making project that would change the existing legal framework for brokerage windows. We think that it is important to understand the 20 year history of the current regulatory framework under the Employee Retirement Income Security Act of 1974 ("ERISA") to provide the proper context for the Department's inquiry. Brokerage windows and similar arrangements have been offered in 401(k) and other individual account plans for two decades based on this guidance.

Given the substantial guidance already provided on this topic in recent years, we do not believe further rulemaking in this area is warranted. However, in the interest of assisting the Department in its deliberations, we are providing the information and comments below. The responses that follow are organized according to the general categories of questions set forth in

the RFI, and discussed in the order followed in the RFI. Unless otherwise noted, all data is as of June 30, 2014.

Defining "Brokerage Windows" – Scope *(RFI questions 1 through 3)*

The disclosure regulations recently issued by the Department under ERISA Section 408(b)(2) and ERISA Section 404(a)(1)(A) and (B) exclude "brokerage windows, self-directed brokerage accounts or similar plan arrangements" from the detailed disclosure requirements applicable to designated investment alternatives. However, the regulations do not define the term "brokerage window or similar plan arrangements". If the Department decides to develop further regulations in this area, it would be necessary to provide a more specific definition of the types of arrangements that are treated as brokerage windows.

In common practice, brokerage windows are implemented through a brokerage account opened by the plan's trustee or custodian on behalf of the plan and over which the participant has limited trading authority. The brokerage window allows participants to purchase a wide range of mutual funds and individual securities. In some plans, the plan sponsor may decide to limit the available investments to mutual funds, an arrangement which is often referred to as a "mutual fund window". This limitation may be imposed to comply with restrictions on investments under Internal Revenue Code Section 403(b)(7) or perhaps to ensure that investments made through the brokerage window are more diversified than investments in individual securities. Even in those instances, however, the participant may usually choose from among hundreds or thousands of investment options.

From a regulatory perspective, the defining characteristic of a brokerage window is that specific investments available through the window are not treated as "designated investment alternatives". Accordingly, any definition of what constitutes a brokerage window should focus on the range and breadth of the investments offered and not the particular account structure of the arrangement. As an example, prior to the availability of brokerage accounts on Fidelity's recordkeeping platforms, certain small business plans were offered access to more than 250 Fidelity mutual funds through mutual-fund-only accounts. The same mutual-fund-only account approach has been utilized for over 20 years for 403(b) plans, which may invest only in annuities or mutual funds purchased through a custodial account. In more recent years, these 403(b) offerings have expanded to include a wide range of non-Fidelity mutual funds.

In these types of plans, the plan sponsor did not designate any specific investments as available investment options under the plan; rather, the plan sponsor only made a decision to offer Fidelity's platform. This platform in turn made available hundreds of mutual funds representing a broad range of investment opportunities for participants. In practice, plan sponsors have not historically considered these arrangements as involving designated investment alternatives that are selected and monitored by the plan sponsor as a fiduciary because of the

large number and broad range of funds available. We believe this position is correct under current law.

Given the lack of regulatory guidance on what constitutes a "designated investment alternative", however, there remains some confusion over the number and range of investment alternatives that must be made available to participants in order to avoid having any specific investment alternative treated as designated by the plan sponsor. While we do not believe it is necessary, if the Department decides to engage in further rulemaking in this area, any new guidance should confirm that the concepts applicable to brokerage windows encompass any arrangement where the specific investment alternatives are not treated as designated investment alternatives. Accordingly, developing rules for brokerage windows will necessarily entail a more specific definition of the types of plan investment structures that involve designated investment alternatives.

In developing this definition, we believe it is appropriate to take into account the number of investments offered as well as the manner in which they are communicated to participants. For example, in cases where a plan sponsor has clearly delineated and communicated a fund line-up, it is appropriate to view those funds in the line-up as designated investment alternatives even though participants may also have unlimited choice available through a brokerage window. We suggest that the Department consider some type of safe harbor approach based on a minimum number of funds necessary to avoid designated investment alternative status in situations where the investments are not identified as part of a designated line-up.

Plan Investment Offerings – Brokerage Windows and Designated Investment Alternatives *(RFI questions 4 though 8)*

As noted above, Fidelity has for many years serviced arrangements that make available a large number of mutual funds to participants in a manner that we believe should be treated as brokerage windows. In addition, Fidelity also services IRA-based and qualified plans for small employers that are record kept solely on our brokerage platform where the available investments include virtually any security that is appropriate for investment by a tax-favored retirement plan. This business continues to grow and, accordingly, the number of plans that we view as using a brokerage window structure continues to increase. However, for the remainder of this section, we will focus on plans that are record kept on our institutional defined contribution plan recordkeeping system. In these plans, brokerage windows are typically offered through a service called "BrokerageLink®" as a supplement to a line-up of designated investment alternatives.

BrokerageLink provides participants and beneficiaries the opportunity to invest in a broad range of options beyond the plan's designated investment alternatives, including mutual funds, ETFs and individual stocks, bonds and other securities. Although the majority of plan sponsors offer BrokerageLink with the broadest range of investment options (including

individual securities), some sponsors choose a brokerage window offering that includes only mutual funds (which may include ETFs). This more limited form of BrokerageLink still permits a participant to choose among thousands of mutual funds from more than 600 mutual fund families.

While we have seen a substantial increase in the number of plans that offer BrokerageLink over the last five years, these plans still represent less than 15 percent of the total plans record kept by Fidelity on its institutional defined contribution plan recordkeeping system. BrokerageLink is more prevalent in the large plan market with approximately 42 percent of plans with 10, 000 or more participants offering this feature. For plans with less than 1,000 participants, approximately 12 percent of those plans offer BrokerageLink.

We are not aware of any correlation between plans that offer BrokerageLink and the number of designated investment alternatives available in the plan's fund line-up. That is, the average number of designated investment options in a plan that offers BrokerageLink is substantially the same as for plans that do not. In some cases, plan sponsors have used BrokerageLink as a way to allow participants to retain investments that are being eliminated from the plan's designated fund line-up. More commonly, though, it appears that plan sponsors decide to offer BrokerageLink as a way to offer a very broad universe of investment choices to those participants who are interested in and comfortable with such choices and willing to do more research on their own

Participation in Brokerage Windows *(RFI questions 9 through 14)*

Approximately 40 percent of all participants whose accounts are recordkept on the traditional defined contribution platform have access to BrokerageLink. This high percentage of participants results from the fact that BrokerageLink adoption is highest among large employers. Of the total number of participants in plans with BrokerageLink, only 2.6 percent actually utilize the feature. This utilization percentage has only increased by a .04 percent over the past five years, even as the percentage of record kept plans offering BrokerageLink has more than doubled during the same period.

Participants utilizing BrokerageLink have invested 56.7 percent of their aggregate account balances in the brokerage window. Of the amount invested in these plan brokerage accounts, a little more than two-thirds are invested in mutual funds, primarily equity funds (65 percent) but with fairly substantial holdings in both bond funds (21 percent) and money market funds (14 percent). The remaining one-third of BrokerageLink balances are invested almost entirely in individual equity securities.

Looking at the demographics of participants who utilize a brokerage window in their plan, the average compensation of participants utilizing a brokerage window is much higher than

the average compensation of other plan participants. Not surprisingly, those participants also have an average account balance that is much larger than the average of other participants. Although we do not have precise figures, available information suggests that a number of participants utilizing a brokerage window employ the services of a third-party adviser to help them manage their account investments.

Only a handful of plans restrict the percentage of a participant's account balance that may be invested through a brokerage window offered by the plan. Some plans require that a minimum amount be invested through the brokerage window, but in our experience the minimum investment, if any, is usually no more than $1,000. In addition, participants utilizing mutual funds offered via BrokerageLink are subject to the frequent trading restrictions imposed by those mutual funds.

Plans which include a stable value fund usually impose an "equity wash" restriction on transfers (exchanges) to a plan brokerage window. The wash restriction requires a participant exchanging funds from a stable value option to invest in an equity investment option for a period of time before he or she can transfer those funds to BrokerageLink. These restrictions are imposed to satisfy contractual obligations imposed by insurers of stable value arrangements which are designed to prevent participants from moving funds to competing investment funds in rising interest rate environments.

Selecting and Monitoring Brokerage Windows and Service Providers *(RFI questions 15 through 21)*

If a plan fiduciary wishes to offer a brokerage window to plan participants that is fully integrated with Fidelity's defined contribution plan recordkeeping services, then BrokerageLink must be utilized to meet operational, reporting and customer experience priorities. Fidelity developed BrokerageLink in the late 1990's based on demand from existing plan recordkeeping clients. Over the years, clients have added BrokerageLink to their plan for a variety of reasons including the desire to offer expanded choice, to respond to employee demand and to maintain a competitive benefits offering.

In our experience, clients consider both the fiduciary implications of the offering as well as the participant disclosure requirements if BrokerageLink is made available. Plan fiduciaries review how BrokerageLink works operationally as well as the fees associated with the service, which Fidelity discloses to plan fiduciaries as required under the 408(b)(2) regulation. In addition, Fidelity provides disclosure related to the shareholder servicing payments it receives from certain non-Fidelity mutual funds purchased through BrokerageLink to allow the plan fiduciary to assess the compensation received by Fidelity from the offering.

If the plan fiduciary wishes to offer BrokerageLink to its plan participants and beneficiaries, this arrangement is reflected in the recordkeeping contract between Fidelity and the plan sponsor or other hiring fiduciary. Participants or beneficiaries who wish to utilize the service receive additional materials beyond those required under the participant-level disclosure regulation, as discussed further below, and complete an authorization form with Fidelity.

Fiduciary Access to Information about Brokerage Window Investments *(RFI questions 22 through 24)*

As outlined above, under the current regulatory framework, fiduciaries are not required to monitor the investments made in their plan's brokerage window. Fiduciaries are provided data related to the type and value of investments in BrokerageLink in the Form 5500 reporting plan package Fidelity provides annually to plan sponsors. Data reflecting the specific holdings (e.g. individual mutual funds, securities) is also available upon request.

Plan sponsor utilization of information about BrokerageLink investments varies. Some plan fiduciaries request the specific holdings, although such data is not necessary as a component of their review of Fidelity's brokerage window services, which typically focuses on internet and rep-assisted transaction processing, any trading or other service issues as well a review of related fees. Rather, the focus is on utilization and experience of their plan participants with BrokerageLink rather than any fiduciary concern regarding specific investments made by participants.

Brokerage Window Costs *(RFI questions 25 though 28)*

The vast majority of plans offering BrokerageLink do not charge participants a separate fee for participating in the brokerage window. Accordingly, almost all of the fees charged in connection with BrokerageLink are generated in connection with the specific transactions and investments that the participant chooses to make.

For individual securities, fees associated with BrokerageLink generally come in the form of brokerage commissions. Commission amounts vary depending what type of security is being purchased and the channel in which the participant requests the transaction (e.g. via the web versus through a phone representative). These costs are typically born by the participant's account. These fees are typically based on a standard fee schedule for BrokerageLink and are not negotiated by the plan fiduciary. All transaction fees associated with BrokerageLink accounts as well as any account maintenance fees are disclosed to both plan sponsors and participants.

Fidelity's BrokerageLink platform is separate from the recordkeeping platform used for the plan's designated investment alternatives. Fidelity views the revenue generated through

BrokerageLink accounts as sufficient to support the servicing of the brokerage window. Accordingly, there is no direct subsidy of BrokerageLink activity by participants in the plan who do not use BrokerageLink.

It is difficult to compare the costs of investing through BrokerageLink with the costs of investing through the plan's designated investment alternatives as it depends in large part on what the plan offers and what investments the participant chooses. BrokerageLink includes thousands of mutual funds with expense ratios that vary from less than 10 basis points to more than 150 basis points. If a participant decides to invest in individual securities, the participant may incur a one-time commission cost on the purchase but then pay no additional costs until the position is sold many years later. The plan's designated investment options may include share classes or institutional products with lower asset based fees that are not available through BrokerageLink. On the other hand, the plan may not include low cost options that may be available through BrokerageLink.

The costs of investing in funds or purchasing individual securities under BrokerageLink are essentially the same as an individual would pay for the same investments in a retail brokerage IRA at Fidelity.

In our experience, plan fiduciaries review and monitor the fees and compensation related to BrokerageLink as a component of the overall pricing of their defined contribution plan. While utilizing another brokerage provider is not feasible if the plan is record kept by Fidelity, our fees are benchmarked with other service providers to assess reasonableness. As it is a highly competitive market, brokerage commissions and other costs have historically decreased over time.

Disclosure Concerning Brokerage Windows and Underlying Investments *(RFI questions 29 through 32)*

As acknowledged by the Department in developing the fiduciary (408(b)(2)) and participant-level (405(a)(1)(A) and (B)) disclosure regulations, it is not practical and certainly not helpful to try to provide detailed information about every investment that may be purchased in a brokerage window. The participant-level regulation preamble stated that "it is important that participants and beneficiaries understand how brokerage windows operate and the expenses attendant thereto... For this reason, the Regulation includes more specific requirements than the proposal concerning the information that must be disclosed about brokerage windows or similar arrangements." [75 FR 64923]

As noted in the RFI, on May 7, 2012, the Department issued Field Assistance Bulletin 2012-02 ("FAB 2012-02"), a set of questions and answers providing additional guidance regarding the participant-level disclosure regulation. Questions 13 and 14 specifically address

the information that the Department would expect to be included related to brokerage windows and to whom it should be provided. Substantively, this information does not differ from what Fidelity previously provided to participants and beneficiaries related to our brokerage offering. We believe that this information is sufficient for the general participant population, particularly in light of the fact that only a small percentage of participants who have a brokerage window available to them actually utilize it. As described above, if a participant or beneficiary wishes to utilize BrokerageLink, they must complete an authorization form and are provided additional information about the brokerage account, including brokerage commissions, the pass-through of shareholder rights such as proxy voting, the availability of electronic services, dividend reinvestment programs and regulatory disclosures.

The description of BrokerageLink in the participant disclosure notice does state that the plan's fiduciaries do not monitor the investments available in the brokerage window.

The RFI asks whether plan disclosures typically include a description of the different risks and costs of investing through a brokerage window compared to investing in a designated investment alternative. The brokerage window would generally include options that (1) may be similar to options included in the designated menu (e.g. same asset class) and (2) provide a greater range of choice among asset classes. Fees charged are disclosed to participants and beneficiaries in advance, and the expense ratio of mutual funds or other investment pools are also available to those who utilize the brokerage window. Regarding the risks of investing in the brokerage window, the participant disclosure notice states that the offering may be most appropriate for those that have more time to review investment materials and manage their account. A brokerage window provides access to many low-cost options.

It is also worth noting that participant account statements already include a diversification notice, as required by ERISA Section 105(a) as amended by the Pension Protection Act of 2006 ("PPA"). The notice reminds participants of the benefits of diversification and the risks of committing more than 20 percent of retirement savings to a single company or industry.

Finally, with respect to questions regarding standardized performance and benchmarking information for managed accounts, we did participate in the Government Accountability Office ("GAO") research for the recent GAO report on managed accounts. As we explained to the GAO staff, it is difficult to create such benchmarks for managed accounts because the adviser generally constructs the managed account portfolios from the plan's menu of designated investment options, which may differ completely from plan to plan. The creation of benchmarks is also challenging because the service is designed to invest among the different asset classes, rendering broad market-based benchmarks of limited usefulness. Finally, the glide path used by each manager will also differ, which changes asset allocation at different rates over time, complicating any determination of performance measurement.

The Role of Advisers *(RFI questions 33 through 36)*

We do not have specific information regarding how many plan sponsors retain the services of an adviser to help them with the selection of a brokerage window for their plan. Given the increasing use of consultants by plan sponsors in recent years to select plan service providers, we assume that consultants are advising many plan sponsors on the selection of brokerage windows as part of the consulting engagement.

Fidelity's managed account service is not currently offered for investments made through BrokerageLink. However, we believe that some participants retain the services of an outside investment adviser to manage or advise the participant on their brokerage window investments. In general, the plan sponsor or other fiduciary would not be in a position to select or monitor the activities of such advisers. Of course, this is also the case for advisers hired to assist with the allocation of account balances among the plan's designated investment alternatives.

Fiduciary Duties (RFI question 37)

The RFI asks whether additional guidance is needed with respect to the requirements for brokerage windows under ERISA's fiduciary provisions. We do not believe such guidance is necessary.

The final 404(c) regulation issued in 1992 provided a framework for fiduciary liability premised on the notion of imposing responsibility only with respect to "designated investment alternatives" of a plan. The final regulation defines a designated investment alternative as "a specific investment identified by a plan fiduciary as an available investment alternative under the plan." In clarifying the import of this rule, the preamble to the final regulation states:

> In this regard, the Department points out that the act of limiting or designating investment options which are intended to constitute all or part of the investment universe of an ERISA plan is a fiduciary function which, whether achieved through fiduciary designation or express plan language, is not a direct or necessary result of any participant direction of such plan. Thus, for example, in the case of look-through investment vehicles, the plan fiduciary has a fiduciary obligation to prudently select such vehicles, as well as a residual fiduciary obligation to periodically evaluate the performance of such vehicles to determine, based on that evaluation, whether the vehicles should continue to be available as participant investment options. Similar fiduciary obligations would exist in the case of an investment universe consisting of investment alternatives which are not look-through investment vehicles but which are specifically designated by plan fiduciaries. *(Emphasis added)* [57 FR 46906, footnote 27].

In offering a brokerage window, plan sponsors are seeking to remove the limitations associated with a designated investment line-up and the investments available through brokerage windows are clearly not designated in a way contemplated by the 404(c) regulation. Accordingly, the existing regulatory framework for brokerage windows is well-established and does not require further clarification.

The response from both plan sponsors and service providers to the Department's attempt to change the rules in this area is evidence of the extent to which these rules are understood and accepted in the benefit plan community. In Field Assistance Bulletin ("FAB") 2012-02, the Department provided additional guidance regarding the participant-level regulation. Although much of the FAB 2012-02 guidance was helpful, the response in Q&A-30 contradicted the position taken in the participant-level regulation and other regulatory guidance by asserting:

> If, through a brokerage window or similar arrangement, non-designated investment alternatives available under a plan are selected by significant numbers of participants and beneficiaries, an affirmative obligation arises on the part of the plan fiduciary to examine these alternatives and determine whether one or more such alternatives should be treated as designated for purposes of the [participant disclosure] regulation.

This statement and other language in Q&A-30 triggered serious concerns among plan sponsors and service providers alike, with respect to both the substance of this new position and the lack of a procedural process required for changes in regulations or other forms of legislative guidance. The response included a number of industry meetings with the Department and OMB and the submission of comment letters on behalf of numerous industry groups and even members of Congress from both parties. This ultimately resulted in the withdrawal of this aspect of the guidance in FAB 2012-02R and reaffirmation of the accepted treatment of brokerage windows from a fiduciary perspective.

We would additionally note that in connection with the withdrawal of the guidance, FAB 2012-02R included language in Q&A-39 that introduced an entirely new fiduciary concept with respect to designated investment alternatives in stating that "a plan fiduciary's failure to designate investment alternatives, for example, to avoid investment disclosures under the regulation, raises questions under ERISA section 404(a)'s general statutory fiduciary duties of prudence and loyalty." If the Department intends to adhere to this position in enforcement actions, we respectfully suggest that more formal regulatory guidance should be provided giving interested parties the opportunity to comment.

Annual Reporting and Periodic Pension Benefit Statements *(RFI questions 38 and 39)*

The RFI asks whether Schedule H of the Form 5500 annual return should require more details of the various classes of investment held in a plan's brokerage window. Loans, partnership or joint venture interests, real property, employer securities or investments which generate losses in excess of the account balance must be reported on the lines on Schedule H specially listed for these types of investments. All other investments may reported as an aggregate balance on line 1c (15) of the schedule and gains or losses in the aggregate on line 2c of the schedule. While Fidelity does provide a plan specific breakdown of all types of investments (not just the types which are ineligible for aggregation) to assist in the completion of Schedule H for brokerage account assets, we do not believe that requiring the separate reporting of investments that are now aggregated would serve any meaningful purpose.

The RFI also asks how brokerage window investments are generally reflected on participant statements intended to satisfy the requirements imposed by Section 105 of ERISA. Investments made by participants through BrokerageLink are maintained on the brokerage platform which is different from the recordkeeping platform used for the plan's designated investment alternatives. While the aggregate holdings balance in BrokerageLink is reported on the participant's statement that includes the plan's designated investment alternatives, detailed individual holdings and transactions are reported on a separate BrokerageLink statement.

This approach is consistent with FAB 2006-03 which provides that, pending the issuance of final guidance, good faith compliance with the periodic statement requirements of ERISA Section 105 (as amended by PPA) would not preclude the use of multiple documents or sources for benefit statement information. The FAB provides an example of a plan administrator maintaining vesting information and a broker-dealer or record keeper maintaining investment information for the same plan.

We strongly recommend that the Department make this aspect of the guidance to be permanent. Investment information, which appears to be the main focus of Congress in enacting the PPA amendments, is often divided among several service providers. For example, Fidelity's brokerage platform tracks brokerage investments separately from the plan record keeping system that tracks "designated investment alternative" positions. We understand that the same approach applies in the case of brokerage features maintained by other plan service providers. For Code Section 403(b) plans, as another example, each mutual fund family generally serves as the custodian for its funds and record keeps those investment positions separately. Insurance products are also generally record kept separately by each issuing insurance company for a 403(b) program.

In each of these cases the information is stored on different reporting systems maintained by different organizations, whether the organizations are affiliated or not. The operational and

compliance challenges to combine the information on these different systems would be immense, without any real benefit to the recipient. In the absence of a maximum page requirement, for example, there would be nothing to prevent the plan administrator or a service provider from stapling various documents together to constitute "one" statement.

We understand that the Department may have concerns about whether the statutory use of the singular form of the word "statement" in the statutory provision requiring participant statements precludes the Department from continuing with the flexible approach embodied in the FAB. In further rulemaking on this issue, we urge the Department to consider the basic rule for statutory construction in dealing with Federal statutes in 1 U.S.C. §1:

> In determining the meaning of any Act of Congress, unless the context indicates otherwise - - words importing the singular include and apply to several persons, parties, or things; words importing the plural include the singular…

This rule of statutory construction has been applied in the context of an ERISA provision by at least one Federal appellate court. See In re: Kaiser Aluminum Corp., 456 F. 3d 328 (3rd Cir. 2006) (regarding the use of the term "plan" in the statute). We believe that Congressional intent in enacting a statement requirement was to provide minimum standards for the types and timeliness of account information, not to confine the medium or format of the information to be provided.

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We would be pleased to discuss or explain any of the comment provided above.

Respectfully,

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