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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, DC 20210

Re: Improving Investment Advice for Workers and Retirees (ZRIN 1210-ZA29)

Dear Sir or Madam:

CFA Institute appreciates the opportunity to respond to the U.S. Department of Labor (the "Department") in response to its recently proposed prohibited transaction class exemption[1] (the "Proposal") and final regulation implementing the vacatur of the Department's 2016 "Fiduciary Rule" under the Employee Retirement Income Security Act of 1974 (ERISA).[2] This letter follows our 22 July letter to the Department requesting an extension of the comment period to, at minimum, 60 days, from 30 days provided, and a request for the scheduling of a public hearing.[3] We further respectfully requested the opportunity to present our views at a public hearing on the Proposal.

CFA Institute is a global, not-for-profit professional association with more than 80,000 U.S.-based investment analysts, advisers, portfolio managers, and other investment professionals affiliated with our 67 CFA local societies in the United States.[4] CFA Institute represents the views of those investment professionals who are its members before standard setters, regulatory authorities, and legislative bodies worldwide on issues that affect the practice of financial analysis and investment management, education and licensing requirements for investment professionals, and on issues that affect the efficiency, integrity and accountability of financial markets.

EXECUTIVE SUMMARY

CFA Institute supports the goal of the Department, which we see as ensuring that the interests of Retirement Investors are placed prior to the interests of those who advise them on their retirement investments and strategies ("Agents"), and the firms that employ those Agents. We

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[1] Department of Labor, "Improving Investment Advice for Workers and Retirees," 85 FR 40834 (July 7, 2020) (https://www.govinfo.gov/content/pkg/FR-2020-07-07/pdf/2020-14261.pdf). Also see Fact Sheet at (https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/fact-sheets/improving-investment-advice-for-workers-and-retirees).

[2] Department of Labor, "Conflict of Interest Rule—Retirement Investment Advice: Notice of Court Vacatur," 85 FR 40590 (July 7, 2020) (https://www.govinfo.gov/content/pkg/FR-2020-07-07/pdf/2020-14260.pdf).

[3] *See* CFA Institute comment letter on the "Proposed Exemption" (June 22, 2020)

[4] CFA Institute membership includes more than 185,400 investment analysts, advisers, portfolio managers, and other investment professionals in 163 countries, of whom more than 178,500 hold the Chartered Financial Analyst® (CFA®) designation. CFA Institute membership also includes 160 member societies in 77 countries and territories.

also support enhancing the investment options available to Retirement Investors without placing undue burdens on retirement Agents.

At the same time, we believe many of the Proposal's provisions will weaken the fiduciary regime that is the foundation of ERISA and the investor protections this regime affords to millions of Retirement Investors. In particular, we are concerned the Proposal's broad-based exemptive relief to investment advice fiduciaries will allow financial institutions and their professionals to receive commissions and other payments, provided they meet certain conditions – namely, that they adhere to a standard of care modeled after the Securities and Exchange Commission's ("SEC") Regulation Best Interest ("Reg BI").

While we do not categorically oppose fiduciaries receiving compensation for investment advice in potentially conflicted situations, we see the Proposal too heavily relying on the SEC's Regulation Best Interest which the SEC did not define. Consequently, we are concerned that investors will not understand the distinction between fiduciary and best interest advice, nor fully comprehend what the difference may mean for the quality and independence of the advice they receive. Moreover, Reg BI took effect as the Department published the Proposal, and therefore has not had sufficient time to determine whether its approach is worthy of replacing ERISA's existing fiduciary standards. The regulatory harmonization, therefore, appears premature, at best.

Further, we do not support the Department's official reinstatement of the so-called Five-Part Test defining what constitutes investment advice and, therefore, an investment advice fiduciary. As we explain more fully below, we believe the Five-Part Test is inadequate, outdated, and does not adhere to the statutory intent of an ERISA fiduciary.

We are concerned about the combined effects of the Five-Part Test and the broad-based exemptive framework. The Five-Part Test is susceptible to regulatory circumvention, allowing Agents as well as investment advice fiduciaries to circumvent ERISA's fiduciary obligations. The Proposal then allows those who qualify as investment advice fiduciaries to apply for exemptive relief and, if successful, become eligible to receive a wide variety of payments from brokers and investment product providers whose interests conflict with those of the fiduciary's beneficiaries. In effect, the Test and the proposed exemption act as a double-layer regulatory sifter, allowing Agents to twice avoid fiduciary obligations intended under ERISA.

CFA Institute has long advocated for a fiduciary duty standard that applies to all who provide personalized investment advice to retail investors. Our Code of Ethics and Standards of Professional Conduct[5], to which all members must annually attest to adhering, require members and candidates to "act for the benefit of their clients and place their clients' interests before their employer's or their own interests." We believe it is more important than ever to provide retirement savers with appropriately tailored investment advice protections while preserving myriad investment options and encouraging greater financial literacy and education.

Finally, we encourage the Department to hold a public hearing and engage with stakeholders to improve the Proposal and better align the Proposal with congressional intent under ERISA.

[5] CFA Institute Code of Ethics and Standards of Professional Conduct: https://www.cfainstitute.org/en/ethics-standards/ethics/code-of-ethics-standards-of-conduct-guidance

The "Five-Part Test"

Along with the Proposal, the Department has issued as a final rule a "technical amendment" to restore the Department's 1975 regulation defining under ERISA and the Code what constitutes investment advice. This is the so-called "Five-Part Test." Under the test, a financial institution or investment professional becomes a fiduciary by reason of providing investment advice and satisfying each of the test's five elements[6]:

(1) render advice to a plan based on the value of securities or other property, or make recommendations regarding advisability of investing in/purchasing/selling;
(2) do so on a regular basis;
(3) would provide the advice pursuant to a mutual agreement with the plan;
(4) in which the advice would serve as primary basis for investment decisions with respect to plan assets; and
(5) in which the advice would be individualized.

By comparison, ERISA Section 3(21) describes a fiduciary as someone who has discretion over how plan assets are invested for a fee based on assets under management, or "with respect to a plan," as someone who "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." Duties owed to beneficiaries stemming from this designation are commonly recognized as the "highest known to the law,"[7] requiring that fiduciaries act with "an eye single to the interests of the participants and beneficiaries."

CFA Institute has long advocated a fiduciary duty standard that would apply uniformly to all who provide personalized investment advice to retail investors. Under our Standards of Professional Conduct (the "Standards"), CFA Institute members owe their clients a duty of prudence, loyalty and care and must annually attest to adhering to this and other provisions of the Standards and our Code of Conduct, including acting "for the benefit of their clients" and placing "their clients' interests before their employer's or their own interests."

Consistent with our testimony during the Department's 2015 hearing on "Conflicts of Interest – Definition of Fiduciary Investment Advice,"[8] CFA Institute believes the five-part test is "inadequate" in serving beneficiaries' interests. In part, this is because the test was established at a time when retirement investing was uniformly outsourced to defined-benefit pension funds utilizing professional investment managers required by ERISA to act in the interests of fund beneficiaries. As such, the test is outdated for application in today's complex and increasingly participant-driven, defined-contribution retirement structures, which were legislated into existence three years after the Department first adopted the test.

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[6] "A financial institution or investment professional that meets this five-part test, and receives a fee or other compensation, direct or indirect, is an investment advice fiduciary under ERISA and under the Code."

[7] Donovan v. Bierwirth, 680 F.2d 263, 272 n.8 (2d Cir. 1982) (Friendly, J.).

[8] Linda L. Rittenhouse. Department of Labor, "Public Hearing Agenda: Conflict of Interest –Definition of Fiduciary Investment Advice," *available at* https://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/public-comments/1210-AB32-2/written-testimony-33.pdf.

Responsibility for managing retirement savings these days has largely shifted to individual plan beneficiaries, most of whom depend on self-directed plans and the periodic education plan sponsors choose to provide. Over this same period, the legal and retirement investment landscape has also become more complex even as defined-contribution plans are seen driving "the future growth in retirement plan assets."[9] The financial stability of employee benefit plans and the retirement benefits of American workers, therefore, require consistent protections for participants and beneficiaries. Re-adoption of the Five-Part Test would create too many opportunities for Agents to circumvent ERISA's fiduciary obligations, and to provide conflicted advice relating to these irreplaceable (for retirees and near-retirees) investments.

For instance, under the Five-Part Test, an Agent or Financial Institution may escape fiduciary status by disclaiming in "fine print," an otherwise "mutual agreement" that an investment decision is of "primary basis." Likewise, the "regular basis" requirement is inappropriate because the frequency of advice does not relate to either its quality or importance. Moreover, neither an Agent nor a Financial Institution should have a green light to provide to substandard or self-dealing advice merely because the advice is provided on a one-time or intermittent basis.

CFA Institute strongly supports any attempts by the Department to realign the provisions of the Five-Part Test with the original statutory context or eliminating the Test entirely. Either approach would mark an important step in providing retirement investors with the protection intended by ERISA.

Aligning with Regulation BI

Under the Proposal, investment advice fiduciaries could, under certain conditions, receive a wide variety of payments in return for advice they would give to clients promoting products and services of the financial institutions providing those payments. These payments include:

- commissions,
- 12b–1 fees,
- trailing commissions,
- sales loads,
- revenue-sharing payments from investment providers or third parties,
- mark-ups and mark-downs.

The Proposal's exemption would extend to prohibited transactions resulting from investment advice on rollovers from a Plan to an IRA. It also would apply to Plans and IRAs in which a financial institution engages in principal transactions to buy or sell investment instruments to clients from its own account. As the Department notes, this exemptive relief is "broader and more flexible" than the Department's pre-existing prohibited transaction class exemptions for investment advice fiduciaries.

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[9] Retirement Savings 2.0: Updating Savings Policy for the Modern Economy: Hearing before the Senate Finance Committee, 113th Cong. (2014) (testimony of Jack Bogle). Retrieved from https://www.finance.senate.gov/imo/media/doc/Testimony%20-%20John%20Bogle.pdf

The exemption's relief is available to SEC- and state-registered investment advisers, registered broker-dealers, banks, insurance companies, and the employees, agents, and representatives of each. The Department notes that other institutions, specifically field marketing organizations and brokerage general agencies, can also apply for relief.

Under the Proposal's potential exemptions, investment advice fiduciaries could become exempt from ERISA coverage if they satisfy the following conditions:

- Compliance with "Impartial Conduct Standards," which have three components: a best-interest standard; a reasonable compensation standard; and a requirement to make no misleading statements about investment transactions and other relevant matters. The best-interest standard is aligned with the conduct standards in Reg BI and the fiduciary duties of registered investment advisers under the Investment Adviser Act of 1940.
- Provide disclosure to retirement investors of their status as investment advice fiduciaries under ERISA and the Code, as applicable, and a written description of services being offered and material conflicts of interest.
- Establish, maintain, and enforce policies and procedures requiring mitigation of conflicts of interest and prudently designed incentive practices.
- Conduct retrospective (annual) written compliance reviews; reports to be certified by the CEO (or equivalent officer) of the financial institution.

The Proposal requires IRA advice fiduciaries to satisfy the duties of prudence and loyalty as a condition for relief. At the same time, however, the Department makes it clear that it does not intend the exemption to provide IRA investors with a private right of action. Nor does it intend for the fiduciary's acknowledgment or any of the disclosure obligations to create a private right of action between a financial institution or investment professional and a retirement investor. We disagree with this approach. Retirement Investors should have the option to seek redress for wrongdoing related to their investment accounts. ERISA has always provided a private right of action in other retirement account areas. We believe this option to address breaches of duty should similarly extend to IRA investors. Put simply, without the option to recover their losses, Retirement Investors may find their retirement investment potentially entirely irreplaceable.

While the Department takes notable steps in the Proposal to bolster the new regime with additional disclosure and compliance obligations, its operation hinges on the recently implemented and untested Reg BI. CFA Institute believes Reg BI falls short of adequately protecting investors, in part because it does not define what constitutes a "best interest" standard.[10] Moreover, its application in the context of ERISA plans is particularly problematic as Reg BI's standard of care requires brokers only not put their own interests ahead of those of their clients. In other words, it is acceptable that they put their own interests and those of their clients on the same level. This conflicts with the traditional fiduciary standards of care applicable in the ERISA context, where investors' interests were placed prior to those of their Agents' and those of their Agents' firms. We remain concerned that investors will not understand the distinction between fiduciary and best interest advice, nor fully comprehend what the difference may mean for the quality and independence of the advice they receive.

[10] *See* CFA Institute comment letter on "Regulation Best Interest" (August 7, 2018): https://www.cfainstitute.org/-/media/documents/comment-letter/2015-2019/20180807-3.ashx

Given its only-recent implementation, it remains uncertain as to whether Reg BI will improve the advice investors receive or further muddy the distinctions between brokers and fiduciary-bound investment advisers. Nor is it clear how Reg BI will affect mis-selling of financial products. These uncertainties have been heightened by monumental recent changes in the brokerage industry.

For these reasons, we encourage the Department to more thoughtfully weigh whether adopting the broad-based Proposal, with its heavy reliance on another agency's determinations, is appropriate. We also urge careful consideration as to what extent this interagency regulatory harmonization aligns with existing statutes and congressional intent under ERISA. Finally, we encourage the Department to further engage with stakeholders to better understand their views and concerns before finalizing the Proposal. A good way to achieve this is by hosting a public hearing with testimony from a variety of interested parties.

Plan rollovers require uniform fiduciary protection

In the preamble to the Proposal, the Department states its belief that advice relating to a distribution of assets from an ERISA plan will constitute investment advice in the future. This position overrides DOL Advisory Opinion 2005-23A – also known as the "Deseret Letter" – which has been interpreted to suggest that advice to roll over Plan assets to an individual retirement account ("IRA") "does not generally constitute investment advice." We commend the Department for taking this step to protect retirement investors.

In making this determination, the Department recognized, correctly in our view, that the decision to roll assets into an IRA is "potentially a very consequential financial decision for a Retirement Investor." The amounts accrued in ERISA-covered Plans, the Department stated, "often comprise the largest sum of money a worker has at retirement." Moreover, it noted that rollovers represent a significant source of funds for the industry and therefore account for a significant percentage of revenue for investment advice providers.

While we support the Department's decision to classify rollovers as investment advice, we object to its requirement that rollover advice satisfy "all prongs" of the Five-Part Test to be considered fiduciary investment advice. We interpret the Proposal's preamble to mean the Department intends to interpret the Five-Part Test sufficiently broadly such that rollover advice would generally be considered fiduciary investment advice. In particular, the Department states, "the rollover recommendation may be seen as the first step in an ongoing advice relationship," thereby satisfying the "regular basis" prong of the five-part test. The Department also notes that statements disclaiming a mutual understanding or forbidding reliance on advice as primary basis for investment decisions "are not determinative." Finally, the Department states that advice pursuant to a best interest standard (for example, Reg BI) or based on individualized needs may satisfy the "primary basis" part of the test.

Rollovers often represent critical junctures in a person's retirement roadmap and therefore require uniform fiduciary standards of care. To reiterate an earlier point, the Five-Part Test is inadequate, insufficient, and outdated, thereby making the consequences of failing to adhere to fiduciary standards of care more significant in the case of rollovers. We recommend that the Department define all rollover advice as fiduciary investment advice, subject to a limited number of narrowly defined exemptions. This approach would be consistent with congressional intent under ERISA of protecting retirement investments and investors.

Finally, we urge the Department to mandate special precautions to rollovers directed into annuity products. The ongoing and high costs to investors who invest in these products, together with the significant illiquidity they will face when trying to liquidate their interests, can significantly impair investor returns. Consequently, the Department should impose strict oversight and enforcement on firms that market such instruments for retirement rollovers to prevent undue dilution and diminution of retirees' retirement earnings.

Provision of General Education Material

The Department has also reinstated its 1996 Investment Education Bulletin, which states that the provision of investment education materials does not constitute the provision of fiduciary investment advice.

CFA Institute supports the clarification that retirement advisers and others may provide *general* education on retirement savings or employment-based plans and IRAs without being seen as fiduciaries. Neither the frequency nor the form of these materials or information matters as long as they do not include advice or recommendations as to specific investment managers, investment products, or the value of particular securities or property. In allowing a range of educational information to easily flow to investors, the reinstatement provides investors with more tools to make meaningful investment decisions and prepare for a retirement future.

Conclusion

As described above, we support the Department's proposed provisions to reinstate the 1996 Investment Education Bulletin, and to classify rollover advice as investment advice. At the same time, the Five-Part Test is, in our view, outdated in an environment where retirees rather than investment professionals are increasingly responsible for investment decisions. We recommend either a revision of the Test to prevent easy provision of conflicted advice or elimination of the Test in its entirety. And we urge the Department to consider deferring any linkage of ERISA plans' approach to conflicted advice with the SEC's untested Regulation Best Interest at least until it is clear how Reg BI is affecting investor advice and investor outcomes.

In conclusion, we believe the Proposed Exemption and the Five-Part Test, taken together, do not achieve the Department's intended goal of "Improving Investment Advice for Workers & Retirees." We consequently urge the Department to delay a final decision on the Proposal until at least after it convenes a hearing to gather and better understand stakeholder input.

Thank you for considering our views. Should you have any questions, please do not hesitate to contact James C. Allen, CFA, at james.allen@cfainstitute.org, or Karina Karakulova, at karina.karakulova@cfainstitute.org.

Sincerely,

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