Submitted Electronically

June 25, 2012

The Honorable Phyllis C. Borzi
Assistant Secretary
Employee Benefits Security Administration
U.S. Department of Labor
200 Constitution Avenue, NW
Washington, DC 20210

Re: **Field Assistance Bulletin 2012-02 Question and Answer 30**

Dear Ms. Borzi:

This letter is a follow-up to the meeting among you and your staff and a group of trade associations concerning positions set forth in the Department of Labor's (the "Department") Field Assistance Bulletin No. 2012-02 (the "FAB").[1] We believe the positions set forth in Question and Answer 30 ("Q&A-30") have potentially enormous costs and adverse effects on the retirement plan system - costs and impacts that we believe need to be further developed and considered as part of a public notice and comment process.

By its terms, the FAB "supplements" the plan participant disclosure regulation (the "regulation").[2] We are troubled by the fact that the Department has changed well-established law and policy regarding plan fiduciaries' duties and imposed new requirements with respect to investment selection and monitoring through a FAB intended to clarify participant disclosure compliance issues.[3] Neither the preambles, nor the text of the Department's regulation, originally proposed in July 2008 and finalized in October 2010, suggest in any way the substantive rules newly promulgated in Q&A-30. Indeed, we believe the regulation as promulgated, and current law, clearly require the opposite result. Accordingly, we urge you to withdraw the answer in Q&A-30. If, instead, the Department determines that the unprecedented approach set forth in Q&A-30 is appropriate, the Department should propose these new requirements for notice and comment in accordance with the Administrative Procedure Act[4] and the President's Executive Orders regarding regulatory burdens.[5]

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[1] The organizations that have signed this letter represent the interests of a significant and broad part of the retirement plan community, including employers and service providers. More organizations have signed this letter than attended the meeting on May 31, 2012.

[2] 29 C.F.R. § 2550.404a-5.

[3] We note that the participant disclosure regulation becomes effective in approximately two months. We are also troubled by the potential consequences that this sudden change in the fiduciary rules and policy will have on plan sponsors' ability to comply with the regulation, as well as their service providers' ability to facilitate compliance.

[4] 5 U.S.C. Sections 511-599 (2012).

[5] Executive Order 12866, "Regulatory Planning and Review," 58 F.R. 51735 (September 30, 1993); Executive Order 13610, "Identifying and Reducing Regulatory Burdens," 77 F.R. 28469 (May 14, 2012).

1. New Fiduciary Requirement to Designate a *Manageable Number* of Plan Investment Options - In Q&A-30, the Department expresses a number of troubling views. First, the Department indicates that "the failure to designate a manageable number of investment alternatives raises questions as to whether the plan fiduciary has satisfied its obligations under [section 404 of the Employee Retirement Income Security Act ("ERISA")]." That phrase is followed by a citation to Hecker v. Deere, which appears to have no direct relationship to the principle for which it is cited, since the Court specifically refused to rule on the issue that the Department raised in its request for rehearing. The Department has never heretofore set forth such a fiduciary principle in any rulemaking. The Department has never suggested in any rulemaking that a plan sponsor's decision to comply with Section 404(c) by making available the broadest range of investment alternatives through a brokerage account or window[6] somehow could be viewed as violating ERISA Section 404(a).

2. Failure to Provide Adequate Guidance or Seek Public Comments - Also troubling is the Department's failure to provide guidance as to when or how any fiduciary would comply with this newly created fiduciary principle. By articulating a new fiduciary principle in the form of an answer to a question in the FAB without any of the public input that accompanies an appropriate rulemaking process, the Department exposes plan sponsors to the substantial risk of litigation over the number of investment options offered by a plan (brought either by the Department or by private plaintiffs). In addition, Q&A-30 creates fiduciary consequences for plan sponsors through the challenge they will face in identifying or not identifying securities in brokerage windows as designated investment alternatives. In this regard, we would note that, heretofore, the fiduciary obligations associated with the construction of an investment menu for a 401(k) plan have been viewed by most as limited to ensuring that designated investment options are prudent, not whether they include too many or too few choices. All of these issues, and undoubtedly more, would have been raised and analyzed, both by the Department and the public, had this novel idea been published for notice and comment as a new regulation.

   The circumstances surrounding the issuance of Q&A-30 through the FAB are strikingly similar to actions taken by the Department and struck down in Christopher v. Smithkline Beecham, 567 U.S. ____ (2012). In Christopher, the Supreme Court accorded no deference to a DOL position that departed from published regulations, had not been subject to notice and public comment, and had been, at best, articulated in amicus briefs.[7] In particular, the

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[6] The FAB references "brokerage windows" and "brokerage platforms." These arrangements are referred to as brokerage windows herein for convenience.

[7] As the Court noted in Christopher, while ordinarily an agency's interpretation is entitled to deference by the courts:

> …this general rule does not apply in all cases. Deference is undoubtedly inappropriate, for example, when the agency's interpretation is "'plainly erroneous or inconsistent with the regulation.'. And deference is likewise unwarranted when there is reason to suspect that the agency's interpretation "does not reflect the agency's fair and considered judgment on the matter

Court was concerned with cases where the Department's novel interpretation of ambiguous regulations could impose "potentially massive liability" for conduct occurring before such a new interpretation. The Court stated that "[t]o defer to the agency's interpretation in this circumstance would seriously undermine the principle that agencies should provide regulated parties 'fair warning of the conduct [a regulation] prohibits or requires' …. [and] would result in precisely the kind of "unfair surprise" against which our cases have long warned." (Citations omitted).

3. <u>New Fiduciary Requirement to Monitor and Evaluate Non-Designated Investment Alternatives</u> - Q&A-30's suggestion that plan sponsors may need to look through brokerage windows to determine whether any particular investment is popular enough with participants to be considered a "designated investment alternative" is surprising and even more concerning. Specifically, Q&A-30 provides:

> 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 this section.**[8] (Emphasis added).

Since 1992, when the Department adopted its regulation under ERISA Section 404(c), plan fiduciaries have understood that they have certain duties regarding the prudent selection and monitoring of "designated investment alternatives." The Section 404(c) regulation defined the term "designated investment alternative" to mean "a specific investment identified by a plan fiduciary as an available investment under the plan,"[9] which would not include investments selected and made by individual participants through a brokerage window. The Section 404a-5 regulation similarly applies to "designated investment alternatives," which are defined in a manner that is similar to the Section 404(c) regulation as:

> any investment alternative designated by the plan into which participants and beneficiaries may direct the investment of assets held in, or contributed to, their individual account. The term 'designated investment alternative' **shall not include 'brokerage windows**,' 'self-directed brokerage accounts,' or similar plan

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in question." This might occur when the agency's interpretation conflicts with a prior interpretation, or when it appears that the interpretation is nothing more than a "convenient litigating position," or a "'post hoc rationalizatio[n]'advanced by an agency seeking to defend past agency action against attack". (Citations omitted)

[8] Indirectly, through what is characterized as an enforcement policy, the Department suggests that a "significant number" of participants and beneficiaries would be at least five participants in the case of a plan with 500 or fewer participants or 1 percent in the case of a larger plan.

[9] 29 C.F.R. § 2550.404c-1(e)(4).

> arrangements that enable participants and beneficiaries to select investments **beyond those designated by the plan.**[10] (Emphasis added).

Even the recently adopted amendment to the Section 404(c) regulation to provide that Section 404(c) "does not serve to relieve a fiduciary from its duty to prudently select and monitor any service provider **or designated investment alternative offered under the plan**" (emphasis added) is clear on its face that it does not apply to brokerage windows. Further, until this FAB, at no time following the adoption of the Section 404(c) regulation in 1992 did the Department ever express, or even suggest, that plan fiduciaries may have a duty to monitor non-designated investments, that is, investments selected by participants through a brokerage window.[11] Brokerage windows have long been understood as mechanisms by which plan participants may invest in a wide range of stocks, mutual funds and other investments not otherwise specifically designated by the plan as available for investment. The participant disclosure regulation and the FAB specifically say that brokerage windows are not designated. It is then quite surprising that what the Department now says it means is that any securities within the brokerage window, if held by as few as five participants, must be treated as designated alternatives.

In this regard, the Department at no time following the adoption of the ERISA Section 404(c) regulation or during the promulgation of the ERISA Section 404a-5 or 408(b)(2) regulations ever suggested the position taken in Q&A-30 of the FAB, despite having had ample opportunity to present its view for public consideration. It is striking that during the promulgation of these regulations (i.e., the notice and comment process), although certain other brokerage window issues were specifically reviewed, the Department did not identify or suggest it was considering the position it articulated in Q&A-30.

We further note that during the 18 month period since the publication of the regulation (October 2010), the period during which employers and their service providers, at significant cost in time and dollars, have had to develop compliance tools, the Department provided no indication of its intention to dramatically change the understood principles of the final rule.

4. <u>Additional Consequences and Costs</u> - The Department's policies and positions in Q&A-30 raise the following additional issues and concerns.

    a. <u>Lack of Evaluation or Explanation of Problem and Approach</u> - Whether or to what extent the problem perceived by the Department is real and whether the position set forth by the

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[10] 29 C.F.R. § 2550.404a-5(h)(4).

[11] Indeed, the Department's own Section 404(c) regulation is entirely to the contrary. It provides as follows:

> A participant, P, independently exercises control over assets in his individual account plan by directing a plan fiduciary, F, to invest 100% of his account balance in a single stock. P is not a fiduciary with respect to the plan by reason of his exercise of control and F will not be liable for any losses that necessarily result from P's investment instruction.

See 29 C.F.R. 2550.404c-1(f)(5). It is noteworthy that the Department <u>did not condition its conclusion by saying</u> "if F prudently monitors P's investment decisions."

Department in Q&A-30 is the best, most cost-effective means by which to address that problem has not been evaluated. Q&A-30 provides no insight into what may have prompted the Department to set forth such a dramatic change, nor does it provide any insight into whether the Department considered the benefits, costs or burdens attendant to its position.

b. Impact on Retirement Plan Establishment and Retention - The extent to which employers will reconsider establishing or maintaining a plan in the absence of being able to offer a brokerage window has not been considered. We note that brokerage windows tend to be very common and attractive features for small employers. Many other employers offer brokerage windows to accommodate participant requests for a broader array of investment options. The new requirements and substantive uncertainty noted throughout this letter create significant additional risk that many employers and plan sponsors will be unwilling to accept.

c. Impact of Potential Brokerage Window Elimination and Liquidation of Participants' Current Holdings - The extent to which participants will be adversely impacted by the elimination of brokerage windows due to employer concerns about fiduciary liability under the Department's interpretation has not been evaluated. As noted above, the new requirements and substantive uncertainty noted throughout this letter create significant additional risk that many employers and plan sponsors will be unwilling to accept. For employers that offer a brokerage window, even deciding to eliminate the window subjects them to significant risk because of the potential reactions from participants who would be forced to liquidate their investments. These plan sponsors have suddenly been put in an untenable position of having to choose between two unacceptable alternatives; maintain brokerage account investments and accept the risk of participant claims about improper fiduciary oversight, or eliminate the accounts and bear the risk of claims from participants who did not want their investments liquidated.

d. Lack of Evaluation of Financial Impact and Potential Compliance Costs - The financial impact of the new requirements and costs associated with setting up mechanisms to monitor participant investments in brokerage windows will be significant but have not been quantified or evaluated. We are unaware of any service provider whose record keeping system can gather and disclose the required information for brokerage window investments. Unlike plan sponsor-selected designated investment alternatives, brokerage window investments are maintained on separate systems that are not linked to those that have been built for making the participant disclosures. Thus, the disclosures required for the first time by Q&A-30 will involve significant and costly manual processes pending development of the needed systems and linkages. These costs are likely to be borne by plan participants and beneficiaries. Neither the costs to develop, build and maintain systems, nor the costs to comply on a manual basis, have been quantified or evaluated.

e. Substantive Complexity and Uncertainty - There is considerable complexity surrounding how and under what circumstances a plan fiduciary determines, at any given point in time, whether a brokerage window investment has a "significant number" of participants or beneficiaries invested and, if so, the actions required as a result of such determinations.[12, 13]

f. Impact on SEPs and SIMPLE IRAs - It appears that, while the 404a-5 regulation does not apply to SEPs and SIMPLE IRAs, two of the most popular forms of small business plans, the Department's interpretive position set forth in Q&A-30 would apply to such arrangements, without a clarification otherwise. Almost by definition, SEPs and SIMPLE IRAs offer all participants the right to invest through a brokerage account – they are, in fact, brokerage arrangements. It does not appear that the Department has attempted any analysis of these plans, and whether the limited plan sponsor responsibilities set forth by Congress in establishing these arrangements are not overruled by the Department's FAQ.

We believe that the consequences and costs described above represent only a few of those that should be considered in assessing the merits of the Department's position set forth in Q&A-30. While we understand that the Department is willing to consider further clarifications of its position on an issue-by-issue basis, such an approach leaves plan sponsors, participants, and service providers without guidance for extended periods of time while each issue is identified and resolved.

While the Department's guidance may have been well intended, it appears that the implications of that guidance were not fully appreciated or considered prior to issuance. In this regard, this Administration, as evidenced in Executive Order 13563 and other actions, has shown sensitivity to the need to comply with sound regulatory processes. Critical retirement security issues, like those raised herein, deserve that same sensitivity and benefit of adherence to the carefully constructed regulatory process administered by the Office of Management and Budget ("OMB").

Finally, the requirements set forth in Q&A-30 are effective immediately and will result in significant costs and adverse effects with respect to the retirement plan system.[14] The

[12] For example, if a fiduciary determines that more than five participants have invested in a single stock (e.g., Facebook) and the fiduciary has concerns about attesting to the prudence of such an investment, is the fiduciary required to direct the sale of such investment and limit all future investments in Facebook? Such decisions raise a number of issues in terms of the fiduciary's liability for such an act or potentially from a failure to act. There is no guidance, nor likely to be any guidance specifically addressing these issues, thus resulting in a litigation trap for plan sponsors and fiduciaries.

[13] We also note that the substantive issues and compliance complexities impact retirement plan service providers' ability to comply with the Department's service provider fee disclosure rules under Section 408(b)(2) of ERISA that are effective on July 1, 2012, approximately one week away. The FAB raises the possibility that certain brokerage window investments may have to be treated as designated investment alternatives. The Section 408(b(2) regulation requires certain record keepers and brokerage service providers to furnish disclosures for each of a plan's designated investment alternatives to the responsible plan fiduciary. The implications, including compliance costs for service providers, resulting from the new requirements in the FAB are potentially significant. These issues should be considered in evaluating concerns about the FAB.

[14] We believe the costs attendant to the Department's policy are almost certainly far in excess of $100 million nationally. In addition, Q&A-30 clearly raises "novel legal or policy issues", especially since there is no legal authority for the position taken in Q&A-30. Under the OMB's Good Guidance Practices Bulletin, either of the conclusions in the prior two sentences would make Q&A-30 an "economically significant guidance document."

transitional relief provided in Q&A-37 by its terms has no application with respect to the law applicable to participant claims. Accordingly, we believe that the Administrative Procedure Act, Executive Orders 12866 and 13610, as well as the guidance in OMB's Good Guidance Practices Bulletin, require that the Department withdraw the answer to Q&A-30. To the extent that the Department believes that the position set forth in Q&A-30 continues to deserve consideration, it should propose the guidance, in conjunction with a cost/benefit analysis, and invite public comment as is required for any "supplement" to a regulation. Such a process would ensure a comprehensive and complete analysis of the policy and issues by the Department and the public, without lingering questions regarding application, scope, and compliance.

We thank you for your consideration of our views and of our request.

Respectfully submitted,

AMERICAN BANKERS ASSOCIATION

AMERICAN BENEFITS COUNCIL

AMERICAN COUNCIL OF LIFE INSURERS

AMERICAN SOCIETY OF PENSION PROFESSIONALS & ACTUARIES

THE ERISA INDUSTRY COMMITTEE

FINANCIAL SERVICES INSTITUTE, INC.

THE FINANCIAL SERVICES ROUNDTABLE

INVESTMENT ADVISER ASSOCIATION

INVESTMENT COMPANY INSTITUTE

INSURED RETIREMENT INSTITUTE

NATIONAL ASSOCIATION OF INSURANCE AND FINANCIAL ADVISORS

PLAN SPONSOR COUNCIL OF AMERICA

SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION

SOCIETY FOR HUMAN RESOURCE MANAGEMENT

THE SPARK INSTITUTE

UNITED STATES CHAMBER OF COMMERCE

cc: The Honorable Hilda Solis, Secretary of Labor
Mr. Cass Sunstein, Office of Information and Regulatory Affairs, OMB

As such, the OMB Bulletin requires advance public notice and the opportunity for public comment with respect to Q&A-30. Since the Department did not follow this procedure, the answer in Q&A-30 must be withdrawn.