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July 21, 2015

By E-Mail to e-ORI@dol.gov

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: **Proposed Definition of Fiduciary Rule RIN 1210-AB32**

Dear Sir or Madam:

We submit this letter in response to the request of the U.S. Department of Labor (the "DOL") for comments on proposed regulations published in the Federal Register on April 20, 2015 (the "Proposal"). The Proposal is designed to implement a new definition of the term "investment advice" under Section 3(21) of Title I of the Employee Retirement Income Security Act of 1974, as amended ("ERISA").

Seward & Kissel LLP has a substantial number of clients who would be affected by the adoption of the Proposal. We respectfully submit the following comments and request that the DOL consider them before adopting any final regulation. Our comments fall into three categories:

(i) the plain language of the statutory provision does not authorize the DOL's expansive definition of "investment advice", and the legislative history of ERISA confirms that this definition is not in line with the intent of Congress;

(ii) the stated purpose of the Proposal and the narrowness of the "seller's carve-out" are not aligned; and

(iii) an additional carve-out should be provided for advice given to qualified professional asset managers ("QPAM"s).

The views we express in this letter are our own and do not necessarily reflect those of our clients.

ERISA's Definition of a Fiduciary

In relevant part, Section 3(21)(A) of ERISA provides that a person is a fiduciary with respect to a plan to the extent he or she: (i) 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) 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) has any discretionary authority or discretionary responsibility in the administration of such plan.

As noted in the Proposal, "the statutory definition contained in section 3(21)(A) deliberately casts a wide net in assigning fiduciary responsibility with respect to plan assets. Thus, . . .any person who renders 'investment advice for a fee or other compensation, direct or indirect is an investment advice fiduciary, regardless of whether they have direct control over the plan's assets, and regardless of their status as an investment adviser and/or broker under the federal securities laws." This is axiomatic; however, the Proposal then states that "[w]hen Congress enacted ERISA in 1974, it made a judgment that plan advisers should be subject to ERISA's fiduciary regime and that plan participants, beneficiaries and IRA owners should be protected from conflicted transactions by the prohibited transaction rules. More fundamentally, however, the statutory language was designed to cover a much broader category of persons who provide fiduciary investment advice based on their functions and to limit their ability to engage in self-dealing and other conflicts of interest than is currently reflected in the five-part test."

While the Proposal makes these and numerous other references to and statements of Congress's intent, it does not provide any citations for these statements; nowhere in the Proposal is a reference or citation to the legislative history of Section 3(21). We note that the Conference Committee Joint Explanation to ERISA specifically provides the following explanation of the definition of a fiduciary under ERISA.

> While the ordinary functions of consultants and advisers to employee benefit plans (other than investment advisers) may not be considered as fiduciary functions, it must be recognized that there will be situations where such consultants and advisers may because of their special expertise, in effect, be exercising discretionary authority or control with respect to the management or administration of such plan or some authority or control regarding its assets. In such cases, they are to be regarded as having assumed fiduciary obligations within the meaning of the applicable definition.

The DOL should address the legislative history of Section 3(21) quoted above and describe how the Proposal's definition of investment advice meets the plain meaning of the statutory language and captures those situations where consultants and advisers are "in effect... exercising discretionary authority or control... regarding [plan] assets". The Proposal defines "investment advice" as:

> (i) A recommendation as to the advisability of acquiring, holding, disposing or exchanging securities or other property, including a recommendation to take a distribution of benefits or a recommendation as to the investment of securities or other property to be rolled over or otherwise distributed from the plan or IRA;
>
> (ii) A recommendation as to the management of securities or other property, including recommendations as to the management of securities or other property to be rolled over or otherwise distributed from the plan or IRA;
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> (iii) An appraisal, fairness opinion, or similar statement whether verbal or written concerning the value of securities or other property if provided in connection with a specific transaction or transactions involving the acquisition, disposition, or exchange, of such securities or other property by the plan or IRA;
>
> (iv) A recommendation of a person who is also going to receive a fee or other compensation for providing any of the types of advice described in paragraphs (i) through (iii); [if]
>
> [The] person, either directly or indirectly (e.g., through or together with any affiliate),— [providing such advice]
>
> > (i) Represents or acknowledges that it is acting as a fiduciary within the meaning of [ERISA] with respect to the advice described in paragraph (a)(1) of [the Proposal]; or
> >
> > (ii) Renders the advice pursuant to a written or verbal agreement, arrangement or understanding that the advice is individualized to, or that such advice is specifically directed to, the advice recipient for consideration in making investment or management decisions with respect to securities or other property of the plan or IRA.

It would appear that, notwithstanding the DOL's claim that the statutory language was designed to cover a much broader category of persons who provide investment advice than is currently reflected in the five-part test, the existing regulation was a reasonable attempt to define the

circumstances when a person providing advice is effectively exercising discretionary authority or control over plan assets. The DOL should explain how a recommendation as to the advisability of acquiring, holding, disposing or exchanging securities or other property provided to a plan or IRA fiduciary for consideration in making his or her investment or management decisions is a situation where an adviser is providing the type of investment advice described in the legislative history – that is, where the consultant or adviser is, in effect, exercising discretionary authority or control with respect to the management or administration of such plan or exercising some authority or control regarding its assets.

The marketplace for financial services and pension plan investments has developed in the years since 1975, and it may be true that the five-part test may now allow advisers, brokers, consultants and valuation firms that exercise effective control or authority over plan assets to avoid fiduciary status and ERISA's fiduciary obligations of care and prohibitions on disloyal and conflicted transactions. The Proposal, however, significantly exceeds the plain meaning of the term "investment advice" and the Congressional intent as stated in the legislative history of ERISA. Rather than deeming every recommendation as to the advisability of acquiring, holding, disposing or exchanging securities or other property, directed to a plan or IRA fiduciary for his or her consideration a fiduciary act subject to ERISA's duties, restrictions and liabilities, the DOL's proposal should focus on defining those situations where in the existing environment advisers, brokers, consultants or valuation firms are in effect exercising some authority or control over plan assets. To do otherwise is to legislate rather than regulate.

Seller's Carve-out

The Proposal provides a carve-out from the general definition of investment advice for recommendations provided in connection with an arm's length sale, purchase, loan, or bilateral contract between an expert plan investor and an adviser.

The DOL stated that the "overall purpose of this carve-out is to avoid imposing ERISA fiduciary obligations on sales pitches that are part of arm's length transactions where neither side assumes that the counterparty to the plan is acting as an impartial trusted adviser, but the seller is making representations about the value and benefits of proposed deals. Under appropriate circumstances, reflected in the conditions to this carve-out, these counterparties to the plan do not suggest that they are an impartial fiduciary and plans do not expect a relationship of undivided loyalty or trust. Both sides of such transactions understand that they are acting at arm's length, and neither party expects that recommendations will necessarily be based on the buyer's best interests. In such a sales transaction, the buyer understands that it is buying an investment product, not advice about whether it is a good product, from a seller who has opposing financial interests. The seller's invitation to buy the product is understood as a sales pitch, not a recommendation."

In the preamble to the Proposal, the DOL noted that it "does not believe such a carve-out can or should be crafted to cover recommendations to retail investors, including small plans, IRA owners and plan participants and beneficiaries. As a rule, investment recommendations to such retail customers do not fit the 'arm's length' characteristics that the seller's carve-out is designed to preserve. Recommendations to retail investors and small plan providers are routinely presented as advice, consulting, or financial planning services. In the securities markets, brokers' suitability obligations generally require a significant degree of individualization. Research has shown that disclaimers are ineffective in alerting retail investors to the potential costs imposed by conflicts of interest, or the fact that advice is not necessarily in their best interest, and may even exacerbate these costs." The DOL went on to state that "[m]ost retail investors and many small plan sponsors are not financial experts, are unaware of the magnitude and impact of conflicts of interest, and are unable effectively to assess the quality of the advice they receive" and that "[i]n this retail market, a seller's carve-out would run the risk of creating a loophole that would result in the rule failing to improve consumer protections by permitting the same type of boilerplate disclaimers that some advisers now use to avoid fiduciary status under the current 'five-part test' regulation."

The conditions of the seller's carve-out, however, are more restrictive than these goals, more burdensome than is required to achieve them and will effectively remove entire classes of investment choices from IRAs, self-directed plan participants and small plans. As proposed, the seller's carve-out is subject to the following conditions:

> First, the person must provide advice to an ERISA plan fiduciary who is independent of such person and who exercises authority or control respecting the management or disposition of the plan's assets, with respect to an arm's length sale, purchase, loan or bilateral contract between the plan and the counterparty, or with respect to a proposal to enter into such a sale, purchase, loan or bilateral contract.
>
> Second, either of two alternative sets of conditions must be met. Under the first alternative, prior to providing any recommendation with respect to the transaction, such person must:
>
> > (1) obtain a written representation from the independent plan fiduciary that the independent plan fiduciary exercises authority or control with respect to the management or disposition of the employee benefit plan's assets (as described in section 3(21)(A)(i) of ERISA), that the employee benefit plan has 100 or more participants covered under the plan, and that the independent plan fiduciary will not rely on the person to act in the best interests of the plan, to provide impartial investment advice, or to give advice in a fiduciary capacity;

(2) fairly inform the plan fiduciary of the existence and nature of the person's financial interests in the transaction;

(3) not receive a fee or other compensation directly from the plan, or plan fiduciary for the provision of investment advice in connection with the transaction (this does not preclude a person from receiving a fee or compensation for other services);

(4) know or reasonably believe that the independent plan fiduciary has sufficient expertise to evaluate the transaction and to determine whether the transaction is prudent and in the best interest of the plan participants (such person may rely on written representations from the plan or the plan fiduciary to satisfy this condition).

The second alternative applies if the person knows or reasonably believes that the independent plan fiduciary has responsibility for managing at least $100 million in employee benefit plan assets. For purposes of this condition, when dealing with an individual employee benefit plan, a person may rely on the information on the most recent Form 5500 filed by the plan to determine the value of plan assets, and, in the case of an independent fiduciary acting as an asset manager for multiple employee benefit plans, a person may rely on representations from the independent plan fiduciary regarding the value of employee benefit plan assets under management. In that circumstance, the adviser need not obtain written representations from its counterparty to avail itself of the carve-out, but must comply with conditions (2) and (3) above. There is no requirement that the person relying on the second prong of the seller's carve-out believe that the independent plan fiduciary has sufficient expertise to prudently evaluate the transaction.

With regard to this carve-out, it is unclear that the size of a plan (i.e., the fact that a plan has 100 participants) is in any way indicative of the ability of the plan fiduciary to appreciate the magnitude and impact of conflicts of interest, or their ability to effectively to assess the quality of the advice they receive, or that a fiduciary needs to manage $100 million of plan assets to be a sophisticated investor. In this regard, under the Securities Act of 1933, as amended (the "1933 Act"), a company that offers or sells its securities must register the securities with the SEC or find an exemption from the registration requirements. The 1933 Act provides companies with a number of exemptions. Certain exemptions permit a company to sell its securities to what are known as "accredited investors." The term "accredited investor" is defined in Rule 501 of Regulation D and includes a "plan" within the meaning of ERISA if the investment decision is made by a plan fiduciary which is either a bank, savings and loan association, insurance company, or registered investment adviser, or if the employee benefit plan has total assets in excess of $5,000,000, or, if a self-directed plan, has investment decisions made solely by persons that are accredited investors. The term also includes a natural person who had an individual income in excess of $200,000 in each of the two most recent years or joint income with that person's spouse in excess of $300,000 in each of those years and has a reasonable expectation of reaching the

same income level in the current year, or has a net worth over $1 million, either alone or together with a spouse (excluding the value of the person's primary residence).

Congress enacted the Small Business Investment Incentive Act of 1980 (the "Incentive Act") which, among other things, authorized "the development of a uniform exemption from registration for small issuers which can be agreed upon among several States or between the States and the Federal Government." The Incentive Act also added Section 2(15) to the 1933 Act, which defined "accredited investor" as one of five enumerated institutional entities or persons who, on the basis of such factors as financial sophistication, net worth, knowledge, and experiences in financial matters, or amount of assets under management qualifies as an accredited investor under rules and regulations which the Commission shall prescribe. As a result of the Congressional mandate in the Incentive Act, the SEC undertook a general examination of the exemptive scheme under the Securities Act. In March of 1982, it adopted Rule 501, the current form of selected parts of which are described above, which provides quantifiable metrics to create bright-line rules for determining whether investors are sophisticated and capable of fending for themselves.

To determine a fiduciary's sophistication based on the number of participants in a plan not only fails to promote the purpose of the carve-out (namely, to assure that transactions are entered into by plan fiduciaries that can appreciate the magnitude and impact of conflicts of interest and effectively assess the quality of the advice they receive), but effectively eliminates any IRA, self-directed plan or small plan from investments in a private placement. Under the private placement regime of the 1933 Act, a general solicitation is forbidden in connection with private offerings under Rule 506. While new rules under the JOBS Act change this absolute prohibition, "quiet" 506 offerings will remain the norm and avoiding general solicitations will remain relevant to a majority of private placements. The SEC has never drawn a sharp line separating communications that qualify as general solicitations from those that do not. However, in a line of no-action letters, the SEC has explained that, if a substantive relationship exists between the offeror and the offeree at the time the offer is made, it will not find that the offer is a general solicitation. The SEC has emphasized the temporal element of this analysis: the relationship must be pre-existing. Questionnaires are frequently used to qualify investors to participate in private placements under Rule 506. These questionnaires allow prospective investors to speak to their sophistication and financial wherewithal, and their purpose is to establish a substantive relationship between the prospective offeror and offeree. Upon receipt of a private offing memorandum, it is common for potential investors, including plan and IRA fiduciaries, to conduct their own due diligence and ask questions regarding the investment and the investment manager. Finally, it is customary for the manager of private investment funds to provide their investors with periodic letters describing the current state of the private investment fund and their thoughts regarding the general investment environment.

The Proposal defines "investment advice" broadly as a recommendation as to the advisability of acquiring, holding, disposing or exchanging securities specifically directed to the advice recipient for consideration in making investment decisions with respect to securities. Although the Proposal has provided the seller's carve-out to exempt arm's length transactions between sophisticated parties from the definition of investment advice, as proposed this carve-out would not cover the private offering to an IRA, a self-directed plan or a small plan. Because private placements require direct communications between the offeror and offeree, the effect of the Proposal will be to preclude IRAs, a self-directed plans and small plans from investing in private placements, including private investment funds and private equity funds. If the DOL does not wish to abandon modern portfolio theory and retreat to the pre-ERISA days of "legal lists", it must adopt the standard developed by the SEC in Rule 501 and either (i) replace the 100 participant and $100 million requirements with an accredited investor requirement or (ii) at a minimum, include a separate carve-out for plans or IRAs that meet the accreditor investor standard when investing and holding private placements. As stated above, the accredited investor determination is currently required by the SEC in private offerings and provides bright-line rules for determining whether investors are sophisticated and capable of fending for themselves; this standard is more indicative of a plan fiduciary's ability to appreciate the magnitude and impact of conflicts of interest and to effectively to assess the quality of the advice they receive and meets the purpose of the Proposal without adding administrative burdens, additional investor representations or eliminating investment choices currently available to professionally managed plans and sophisticated self-directing plan participants and IRA owners.

QPAM Carve-out

Registered investment advisers currently receive information, research and market data from a plethora of sources. The scope of this information is as varied as the investment strategies investment advisers employ and can include proprietary research on companies that the investment adviser is considering acquiring, due diligence on a prospective acquisition or a valuation of a portfolio an investment manager is considering purchasing or selling. If the investment adviser is acting as a fiduciary to a pension plan, under the Proposal, this type of market research could be considered a recommendation as to the advisability of acquiring, holding, disposing or exchanging securities specifically directed to the investment adviser for its consideration in making investment decisions, thereby imposing ERISA fiduciary status on the provider of the research. The effect of ERISA fiduciary status and liability will be to increase the cost of such market research and/or limit the availability of such research provided to professional investment managers serving ERISA clients.

For example, if a market researcher provides a registered investment adviser with a report as to the value and advisability of buying a municipal bond and the investment adviser purchases those municipal bonds for one or more of its pension plan clients, assuming the purchase of a tax-

exempt bond is inappropriate for the pension accounts, did the market researcher breach the ERISA standard of care? Under the Proposal, would the researcher be required to know the clients for which the research would be used or specifically indicate the appropriateness of the research for ERISA clients in order to meet the prudent man standard of care imposed on fiduciaries by ERISA? Similarly, if a researcher provides an investment adviser with shoddy research and the investment manager purchases a security in part based on that research is the researcher liable to the ERISA client for the losses the plan suffered due to its failure to act in accordance with ERISA's prudent man standard of care? Additionally, if an affiliate of an investment adviser provided an investment adviser with a report regarding CLOs available in the market, including CLOs that are managed by another affiliate of the investment adviser, would the delivery of the report be a prohibited transaction?

In 1984, the DOL developed and granted a class exemption for qualified professional asset managers, PTE 84-14. The essential premise of the DOL for providing broad exemptive relief from the prohibitions of section 406(a) of ERISA for all types of transactions in which a plan engages was that investments of plan assets, and the negotiations leading thereto, are the sole responsibility of an independent professional investment manager. The DOL noted that the conditions of the exemption for a professional asset manager to be qualified "ensure that entities serving as QPAMs are established financial institutions which are large enough to discourage the exercise of undue influence upon their decision making processes." (See: Application for Class Transaction Exemption D-11047) Specifically, to be a "qualified professional asset manager" (a "QPAM") an entity must be registered with the SEC as an investment adviser, have $85 million in total client assets as of its most recently completed fiscal year, have shareholder equity in excess of $1 million and acknowledge in writing it is acting as a fiduciary.

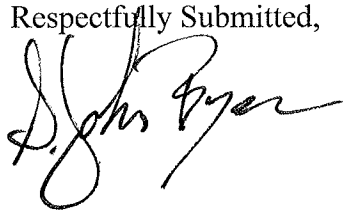
As a fiduciary, a QPAM is responsible for the investments it makes on behalf of its plan and IRA clients. If a QPAM blindly relies on shoddy research or conflicted information, it will be liable to make their plan clients whole for any losses the plan suffers on that investment. There seems little or no benefit to the plans, or their participants and beneficiaries, to impose a second level of fiduciary responsibility and liability on persons providing advice to a QPAM retained by the plan; in fact, the likely increase in the cost of such research or reduction in providers of such research will be detrimental to the plans. As noted by the DOL in issuing PTE 84-14, QPAMs are established financial institutions which are large enough to discourage the exercise of undue influence upon their decision making processes. It seems self-evident that an established financial institution that is large enough to discourage the exercise of undue influence upon its decision making processes, should also be able to discern the magnitude and impact of any conflicts of interest, and be able to assess the quality of the advice it receives. Therefore, we suggest that an additional carve-out for any recommendations given to a QPAM be included in any final regulation. A QPAM carve-out would permit professional asset managers to continue to receive information, research and recommendations from their current providers of such information and

research will be detrimental to the plans. As noted by the DOL in issuing PTE 84-14, QPAMs are established financial institutions which are large enough to discourage the exercise of undue influence upon their decision making processes. It seems self-evident that an established financial institution that is large enough to discourage the exercise of undue influence upon its decision making processes, should also be able to discern the magnitude and impact of any conflicts of interest, and be able to assess the quality of the advice it receives. Therefore, we suggest that an additional carve-out for any recommendations given to a QPAM be included in any final regulation. A QPAM carve-out would permit professional asset managers to continue to receive information, research and recommendations from their current providers of such information and would meet the DOL's stated goal of the Proposal -- to ensure that any advice recipient is aware of the magnitude and impact of conflicts of interest, and is able to assess the quality of the advice they receive.

We note that the information and research provided to QPAMs often does not relate to the purchase, sale or holding of specific assets and therefore may fall outside of the relief provided by the "seller's carve-out" or the BIC Exemption[1].

We thank the DOL for the opportunity to comment on the Proposal, and hope that these comments are helpful in the DOLs efforts to craft a final regulation that comports to the intent of Congress, does not impose unintended limitations on the investment choices available to plans and IRAs and does not impede the free flow of investment research and information to professional investment managers.

Respectfully Submitted,



[1] The proposed BIC Exemption is a new class exemption from the "prohibited transaction" rules that would allow certain "investment advice" fiduciaries to receive compensation for services rendered in connection with a retail retirement investor's purchase, holding or sale of certain investment products in accordance with the fiduciary's advice, if certain protective conditions are met. The BIC Exemption requires contractual acknowledgment of fiduciary status, commitment to basic standards of impartial conduct, including providing advice only if it is in the "best interest" of the plan or IRA, and clear and prominent disclosure of conflicts of interest.