

U.S. Department of Labor

Assistant Secretary for
Congressional and Intergovernmental Affairs
Washington, D.C. 20210



December 13, 2011

The Honorable John Kline
Chairman
Committee on Education and the Workforce

The Honorable Phil Roe, M.D.
Chairman
Subcommittee on Health,
Employment, Labor and Pensions

U.S. House of Representatives
2181 Rayburn House Office Building
Washington, D.C. 20515-6100

Dear Chairman Kline and Chairman Roe:

I am writing in response to your letter dated November 18, 2011, to Assistant Secretary Phyllis C. Borzi in which you inquired about continuing regulatory activity undertaken by the Employee Benefits Security Administration (EBSA) with regard to the definition of a "fiduciary" under the Employee Retirement Income Security Act of 1974 (ERISA). As noted in your letter, on September 19 the Department announced that it would repropose its rule defining the term fiduciary. You requested additional information regarding the Department's ongoing rulemaking on this issue.

The Department submitted the original proposed regulation (RIN: 1210-AB32) to amend the definition of the term fiduciary to the Office of Management and Budget's Office of Information and Regulatory Affairs (OIRA) on July 6, 2010. The fact of this submission was made available to the public on an OIRA website, REGINFO.GOV. See <<http://s.dol.gov/KQ>>. On October 22, 2010, the Department published the proposed rule in the Federal Register (75 FR 65263). The Notice of Public Rulemaking (NPRM) and information related to the Department's OMB submission is available online at <<http://s.dol.gov/KR>>.

In response to the NPRM, the Department received more than 300 written public comments and held two days of open hearings and more than three dozen individual meetings with interested parties. The original proposed rule, the transcripts of the two-day public hearings and written testimony, 39 requests to testify at the public hearings, 316 public comments, interviews and other information on the original proposed rule are available online at <<http://s.dol.gov/KP>>.

The Department decided to repropose the rule in part as a response to requests from the public and members of Congress for the Department to allow an opportunity for more input on the rule. The Department agrees that this important consumer protection initiative will benefit from additional input, review and consideration. More public input and additional analysis will strengthen the rule and supplement the existing record.

The Department's decision to repropose the regulation is consistent with the goals of Executive Order 13563, *Improving Regulation and Regulatory Review*. The reproposal process is designed to inform judgments, ensure an open exchange of views while protecting consumers and avoiding unjustified costs and burdens. The extended rulemaking process will ensure that the public receives a full opportunity to review and comment on EBSA's updated economic and regulatory analysis and revisions of the rule, including any new or amended prohibited transactions exemptions that would also be part of the proposal. EBSA is reviewing a wide range of academic studies and information submitted by commenters and will make public, as part of the revised NPRM, any new relevant material not already in the administrative record. I am enclosing a list of studies EBSA used in the regulatory analysis for the original proposed regulation.

The Department's decision to repropose will ensure that the revised rule provides the strongest possible protections to participants and beneficiaries, business owners, and retirement savers in pension plans and IRAs. As Assistant Secretary Borzi testified before your Committee, the regulation issued by the Department in 1975 must be re-examined so that plan fiduciaries, participants and IRA holders receive the impartiality they expect when they rely on their adviser's expertise in providing investment advice. Since the mid-1970s, there have been significant changes in the retirement plan community and marketplace, with more complex investment products, transactions and services available to plans and IRA investors. The shift from defined benefit plans to defined contribution plans has also made investment advice increasingly important to employers, particularly small and medium-sized employers, when choosing appropriate plan investments for their workers, and for workers when selecting among investments for their individual accounts. IRA holders also shoulder a greater amount of investment responsibility and are even more vulnerable than 401(k) plan participants since no other plan fiduciary protects the IRA investments. The reproposed rule will adapt the 1975 rule to the current retirement marketplace. The review of this regulation is itself consistent with Executive Order 13563, which requires agencies to periodically review and modify or expand existing regulations that are outmoded to make an agency's regulatory program more effective.

EBSA's enforcement experience also provides evidence of the need to update this rule. The requirement under the 1975 rule that the plan consult the adviser "on a regular basis" presents one of the greatest obstacles to holding most investment advisers to fiduciary standards. This is because plans often hire consultants for advice on one-time transactions. Examples are numerous, such as the purchase of employer stock upon establishment of an employee stock ownership plan (ESOP), or a large multiemployer plan retaining an investment adviser to evaluate real estate investment development opportunities for the plan, or a firm's representatives having infrequent contact with plans after the selections of mutual funds. Faulty valuations in connection with ESOPs also show the scope of the problem. The Department provided examples from EBSA's investigations and litigation to Chairman Kline in responses to Questions for the Record submitted following Secretary Solis' February 16, 2011, testimony before the Committee. See H. Comm. on Ed. & the Workforce, *Policies and Priorities at the U.S. Department of Labor*, Hearing, Feb. 16, 2011 (Serial 112-6), 76-77, 103-106 (available

The Honorable John Kline
The Honorable Phil Roe, M.D.
December 13, 2011
Page 3

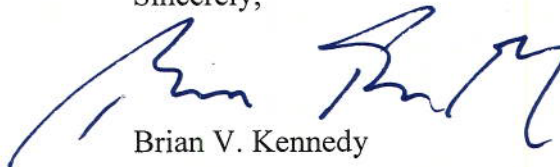
online at <<http://s.dol.gov/J5>>). The Department believes that these numerous enforcement examples further support the need to revise the types of advisory relationships that should give rise to fiduciary status on the part of those providing investment advice services.

As the Department works to repropose the regulation, we have said publicly that we anticipate revising the rule to address concerns about the application of the regulation to routine appraisals and to clarify the limits of the rule's application to arm's length commercial transactions, such as swap transactions. The Department is also considering issuing at least one additional exemption from ERISA's prohibited transaction rules to address concerns about the impact of the new regulation on the current fee practices of brokers and advisers and revenue-sharing arrangements. In addition, we are considering possible amendments clarifying the continued applicability of existing exemptions. Should the Department include additional exemptions in the reproposal, it will carefully craft any such new or amended exemptions to best preserve beneficial fee practices, while at the same time protecting plan participants and individual retirement account owners from abusive practices and conflicted advice.

The Department anticipates that the new proposed rule will be issued in 2012. The timing will be addressed with greater specificity in the forthcoming Fall 2011 Semiannual Regulatory Agenda. Consistent with the principles set forth in Executive Order 13563, the reproposal will ensure that the public is provided with a meaningful opportunity to participate in the rulemaking process through an open exchange of information and perspectives that will lead to an effective rule that does not impose unjustified burdens and costs.

If you or your staff have any questions about this response, please contact Patrick Findlay in the Department's Office of Congressional and Intergovernmental Affairs. He may be reached at (202) 693-4600.

Sincerely,



Brian V. Kennedy

Enclosure

cc: The Honorable George Miller
Senior Democratic Member, Committee on Education and the Workforce

The Honorable Robert Andrews
Senior Democratic Member, Subcommittee on Health, Employment, Labor and Pensions

Materials Cited in the Regulatory Impact Analysis for the Original Proposed Regulation Issued on October 22, 2010

U.S. Securities and Exchange Commission, Office Compliance Inspections and Examinations, Staff Report Concerning Examination of Select Pension Consultants (Washington, DC: May 16, 2005), available online at <http://www.sec.gov/news/studies/pensionexamstudy.pdf>

GAO, Conflicts of Interest Can Affect Defined Benefit and Defined Contribution Plans, GAO-09-503T, Testimony Before the Subcommittee on Health, Employment, Labor and Pensions, Education and Labor Committee, House of Representatives (March 24, 2009), available online at <http://www.gao.gov/new.items/d09503t.pdf>

Bergstresser, Daniel B., John Chalmers, and Peter Trufano. "Assessing the Costs and Benefits of Brokers in the Mutual Fund Industry," Social Science Research Network Abstract 616981 (Sept. 2007), available online at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=616981

Bullard, Mercer, Geoffrey C. Friesen, and Travis Sapp. "Investor Timing and Fund Distribution Channels" SSRN Working Paper, Dec. 2007, available online at <http://ssrn.com/abstract=1070545>

Zhao, Xinge. "The Role of Brokers and Financial Advisors Behind Investments into Load Funds," December 2005, available online at <http://www.ceibs.edu/knowledge/papers/images/20060317/2845.pdf>