The COMMITTEE of ANNUITY INSURERS

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August 6, 2020

FILED ELECTRONICALLY

Office of Exemption Determinations
Employee Benefits Security Administration
Attention: Application No. D-12011
U.S. Department of Labor
200 Constitution Avenue, N.W.
Washington, DC 20210

Re: Proposed Rule, "Improving Investment Advice for Workers & Retirees"
Application No. D-12011, Docket EBSA-2020-0003

On behalf of the Committee of Annuity Insurers (the "Committee"), we are filing this letter in response to the above-referenced proposed prohibited transaction exemption ("Proposed Exemption") published by the Department of Labor ("the Department") on July 7, 2020. As explained in more detail in this letter, we have very serious concerns about the statements made by the Department in the preamble to the Proposed Exemption ("the Preamble") which purport to reinterpret the five-part test for investment advice fiduciary status. The Department's purported interpretations in the Preamble, if not corrected as part of the final rulemaking, will lead to uncertainty and inconsistent application, will reduce access to critical products that protect Americans' retirement security, and are inconsistent with *Chamber of Commerce of the United States v. U.S. Department of Labor*, 885 F.3d 360 (5th Cir. 2018) ("*Chamber of Commerce*"). Moreover, the Proposed Exemption does not provide an adequate solution to the problems caused by the interpretations in the Preamble.

The Committee is a coalition of life insurance companies formed in 1981 to participate in the development of federal policy with respect to tax, securities, ERISA, and banking law issues affecting annuities. The Committee's current 32 member companies represent over 80% of the annuity business in the United States and are among the largest issuers of annuity contracts to IRAs and employer-sponsored retirement plans. A list of the Committee's member companies is attached as Exhibit A.

The Committee is not requesting a hearing. However, if the Department holds a hearing, the Committee requests the opportunity to testify. The issues that would be addressed in the Committee's testimony are set forth in the Summary immediately below.

I. Summary

Our letter makes the following points:

- We are very concerned that a number of statements in the Preamble suggest that fiduciary status might attach in exactly the situations that the Fifth Circuit rejected, because no relationship of trust and confidence exists.

- We disagree that a recommendation to take a distribution from a plan is always equivalent to a securities recommendation with respect to the plan.

- The Preamble contains statements that improperly undermine the regular basis prong of the five-part test by asserting it is satisfied if, in the context of a rollover recommendation, the financial professional either has any prior relationship or might have a subsequent relationship with the customer.

- The Preamble improperly suggests that any recommendation will result in a mutual understanding that a recommendation will be "a" primary basis for decision making.

- The Preamble further incorrectly implies that simply providing a recommendation in an individual's "best interest" automatically satisfies the primary basis prong.

- The Preamble improperly suggests that trailing commissions imply the existence of an ongoing fiduciary relationship.

- The Proposed Exemption is not a solution to an overly broad rewriting of the five-part test.

- The Proposed Exemption should correct the Preamble's erroneous implication that the best interest standard establishes a monitoring obligation.

- The Proposed Exemption could be improved to adequately recognize different annuity distribution models and state insurance law.

- The Department should remove the fiduciary acknowledgement.

- The Department should make the Proposed Exemption available for in-house plans of financial institutions, as long as the fees and compensation are equivalent to advice offered to other plans, reconsider the need for retrospective review and certain disclosure requirements, and further evaluate the adequacy of the administrative procedures regarding ineligibility notices.

II. The Preamble Contains Statements Significantly Undermining the Five-Part Test in Contravention of the Fifth Circuit Decision

A. Introduction

In the *Chamber of Commerce* case, the U.S. Court of Appeals for the Fifth Circuit ("Fifth Circuit") vacated, *in toto*, the regulatory amendments and new and amended exemptions published in April 2016 and collectively referred to as the "Fiduciary Rule." The Fifth Circuit unambiguously held that the Fiduciary Rule, essentially an interpretation of the definition of "fiduciary" in section 3(21) of the Employee Retirement Income Security Act of 1974 ("ERISA") and the parallel provision in section 4975 of the Internal Revenue Code of 1986 (the "Code"), in fact conflicts with the unambiguous text of ERISA and the Code. The Fifth Circuit made clear that "all relevant sources indicate that Congress codified the touchstone of common law fiduciary status—the parties' underlying relationship of trust and confidence—and nothing in the statute 'requires' departing from the touchstone."[1] Further, as explained by the Fifth Circuit, the Fiduciary Rule "expressly include[d] one-time IRA rollover or annuity transactions where it is ordinarily inconceivable that financial salespeople or insurance agents will have an intimate relationship of trust and confidence with prospective purchasers."[2] The Fifth Circuit pointed out that the Department "contradict[ed] its own longstanding, contemporary interpretation of an 'investment advice fiduciary' and cannot point to a single contemporary source that interprets the term to include stockbrokers and insurance agents[, which] indicates that the [Fiduciary] Rule is far afield from its enabling legislation."[3]

At the same time as the Department published the Proposed Exemption, the Department also reinstated the five-part test for investment advice fiduciary status in Regulation § 2510.3-21.[4] Under the reinstated five-part test, for advice to constitute fiduciary investment advice, a person must:

(1) render advice as to the value of securities or other property, or make recommendations as to the advisability of investing in, purchasing, or selling securities or other property ("*the recommendation prong*")
(2) on a regular basis (the "*regular basis prong*")
(3) pursuant to a mutual agreement, arrangement, or understanding with the plan or individual (the "*mutual understanding prong*")
(4) that the advice will serve as a primary basis for investment decisions with respect to the plan or IRA (the "*primary basis prong*") and
(5) that the advice will be individualized based on the particular needs of the plan or IRA (the "*individualized prong*").

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[1] *Chamber of Commerce*, 885 F.3d at 369.

[2] *Id*. at 380.

[3] *Id*. at 376.

[4] 85 Fed. Reg. 40589, 40593-94 (July 7, 2020).

The preamble to that "final rule," described as a "technical amendment," simply explained that this action was needed "to reflect the mandate of the Fifth Circuit's decision, which vacated the Department's 2016 rulemaking *in toto*."[5] The preamble to the technical amendment contained no interpretation or explanation of the meaning of the five-part test, nor sought comments in any way on its application.

For that reason, we were very concerned and disappointed to see a number of statements in the Preamble to the Proposed Exemption that, in our view, introduce uncertainty in the longstanding understanding of the meaning of ERISA and the Department's 1975 regulation passed shortly after the enactment of ERISA. These statements, taken together, suggest that fiduciary status might attach in exactly the situations that the Fifth Circuit rejected, because no relationship of trust and confidence exists. Moreover, while many of these statements are articulated in the context of rollovers, the same principles would appear to apply more broadly to the application of the five-part test in other contexts, including sales activities, similar to the approach taken by the Department in the Fiduciary Rule.

In effect, while purporting to reinstate the five-part test without change and without notice and comment, the DOL has, through preamble commentary, significantly revised the five-part test, resulting in a restatement of the five-part test that has the effect of driving providers to rely on an exemption, including the new Proposed Exemption.

As the Fifth Circuit stated: "Transforming sales pitches into the recommendations of a trusted adviser mixes apples and oranges."[6] We explain our specific objections in the following sections.

B. Distribution Recommendations as an Automatic Securities Recommendation

In Advisory Opinion 2005-23A (the "Deseret Letter") the Department concluded that a recommendation to take a distribution is not advice or a recommendation concerning a particular investment. The Deseret Letter then states that, of course, any investment recommendation "regarding the proceeds of a distribution would be advice with respect to funds that are no longer assets of the plan."

In the Preamble, the Department states that it now believes that "the analysis in the Deseret Letter was incorrect and that advice to take a distribution of assets from an ERISA-covered Plan is actually advice to sell, withdraw, or transfer investment assets currently held in the Plan."[7] The Department argues that a recommendation to roll over assets from the plan "is necessarily a recommendation to liquidate or transfer the Plan's property interest in the affected assets, the participant's associated property interest in the Plan investments, and the fiduciary

[5] *Id*. at 40589-90.

[6] *Chamber of Commerce*, 885 F.3d at 382.

[7] 85 Fed. Reg. at 40839.

oversight structure that applies to the assets."[8] In connection with these statements the Department has placed the legend "WITHDRAWN AS OF 6/29/2020" on the Department's website on the page for the Deseret Letter.

We have both process and substantive concerns with this discussion in the Preamble. With respect to process, the Department has, in the preamble to an exemption, attempted to regulate on an issue specifically addressed in the Fiduciary Rule overturned by the Fifth Circuit. The Fiduciary Rule made a rollover recommendation equivalent to a securities recommendation, and this was an issue of significant discussion in the *Chamber of Commerce* litigation. The decision pointed out that the Fiduciary Rule "expressly includes one-time IRA rollover or annuity transactions where it is ordinarily inconceivable that financial salespeople or insurance agents will have an intimate relationship of trust and confidence with prospective purchasers."[9] Further, this pronouncement and withdrawal of the Deseret Letter has, unlike a regulation, no effective date, meaning rollover recommendations are subject, and have always been subject, to fiduciary status.

Substatively, we also disagree with the Department's conclusion. With respect to the *plan*, the only recommendation is a distribution recommendation. That distribution is not a securities recommendation and typically involves no advice about the investments under the plan. The Department even goes so far as to argue that a distribution recommendation is a securities recommendation because it is a recommendation about the "fiduciary oversight structure that applies to the assets." The Department cites no evidence that Congress intended such a result.

By asserting that a rollover recommendation is automatically a recommendation regarding securities with respect to the plan, the primary implication is to create a cause of action under ERISA by treating a financial professional as a fiduciary *with respect to that ERISA plan.* This is the case even if the financial professional's connection to a particular plan is no more than fleeting, because of this one rollover recommendation.

It is not even clear that this conclusion is contemplated by the reinstated five-part test. On page 40834 of the Preamble, the Department states that the "recommendation prong" of the five-part test is involved when a person "render[s] advice as to the value of securities or other property, or make[s] recommendations as to the advisability of investing in, purchasing, or selling securities or other property." But the Department has misquoted the text of the 1975 regulation by omitting a key phrase. The five-part test requires a person to "render[] advice **to the plan** as to the value of securities or other property, or makes recommendation as to the advisability of investing in, purchasing, or selling securities or other property" (emphasis added).[10] In the context of a rollover recommendation, no advice is given "to the plan."

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[8] *Id*.

[9] *Chamber of Commerce*, 885 F.3d at 380.

[10] 29 C.F.R. § 2510.3-21(c)(1)(i).

Moreover, the Department's position proves too much, as was explored in detail in many comments to the vacated Fiduciary Rule. If the Department's analysis is correct, then recommendations to *contribute to a plan or to contribute to an IRA* are securities recommendations, as are recommendations *not* to take a distribution or loan.

C. Rollover Recommendations and the "Regular Basis" Prong

The Preamble contains two statements that, taken together, make the "regular basis prong" satisfied in almost any case where a rollover recommendation is made. First, the Department states that the regular basis prong of the five-part test would be satisfied when "an entity with a pre-existing advice relationship with the Retirement Investor advises the Retirement Investor to roll over assets from a Plan to an IRA."[11] Second, the Department states that in the case of "an investment advice provider who establishes a new relationship with a Plan participant and advises a rollover of assets from the Plan to an IRA, the rollover recommendation may be seen as the first step in an ongoing advice relationship that could satisfy the regular basis prong of the five-part test depending on the facts and circumstances."[12]

These statements are troubling with respect to exactly the scenarios for which the Fifth Circuit determined Congress did not intend to consider fiduciary in nature. The first statement *might* be simply presupposing its own conclusion, namely that the parties have entered into a relationship of trust and confidence, meeting the five-part test, under which there is a mutual understanding that rollover recommendations will be part of that advice. If that is what is intended, the statement is not saying anything meaningful, other than a rollover recommendation is fiduciary in nature when the five-part test is satisfied.

But the first statement does not actually suppose that a *fiduciary* relationship has been previously established. It assumes only that a "pre-existing advice relationship" exists. If that is the case, the Department has introduced significant uncertainty to, and significantly undermined, the five-part test. Rarely do individuals seek out a financial professional randomly; rather, when they have a job change they will often reach out to someone with whom they have previously received recommendations on financial products. The simple fact that the individual and financial professional have a pre-existing relationship, even one that involved recommendations, does not mean that there was a mutual understanding that advice would be provided on a regular basis and that this would include rollover recommendations. In fact, the Department's statement appears to suggest that a rollover recommendation is being made on a "regular basis" solely because a financial professional knows a particular individual.

The second statement quoted above is even more troubling. It concludes that the rollover recommendation "may be seen as" the first step in a relationship that "could" satisfy the regular basis prong. We have serious concerns with this statement. It provides no workable guidance for a financial professional to be able to reach a mutual understanding that no fiduciary

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[11] 85 Fed. Reg. at 40840.

[12] *Id*.

relationship exists. And it suggests that a sales conversation will be retroactively transformed into a fiduciary recommendation, if the individual is happy with the sale and returns for additional recommendations. The fact is, financial professionals that sell annuities and other products must *know* at the moment a rollover recommendation is made whether or not they are a fiduciary. Unless the client has specifically requested and is paying for ongoing investment advice, and the financial professional has agreed to provide those services, the existence of a later relationship cannot transform the understanding of the parties that recommendations are being provided on a "regular basis."

D. More than One Primary Basis for Decisions

The Preamble asserts that "the five-part test does not look at whether the advice serves as 'the' primary basis of investment decisions, but whether it serves as 'a' primary basis."[13] While it is true that the 1975 regulation does use the word "a" and not "the," this is, as far as we know, the first time the Department has placed this surprising gloss on the primary basis prong.[14]

The Department's position suggests that any recommendation that might be considered by an individual is automatically a primary basis for investment decisions. Such a statement undermines the fundamental difference between a sales conversation, which always involves some sort of recommendation, and a relationship of trust and confidence under which the individual will expect fiduciary investment advice. We disagree that the regulation is this broad. As the Fifth Circuit emphasized, the Fiduciary Rule improperly captured anyone who makes "a suggestion" and thus "it comprises nearly any broker or insurance salesperson who deals with IRA clients."[15]

The primary basis prong, more than any other part of the five-part test, captures the essence of a relationship of trust and confidence. Thus, it should only capture those situations where the parties have come to a mutual understanding that the individual will be relying on the recommendation above all other considerations.

E. Primary Basis Prong Automatically Satisfied When a Recommendation is Made

Most surprisingly, the Preamble suggests any recommendation made by a financial professional would satisfy the primary basis prong: "When financial service professionals make recommendations to a Retirement Investor, particularly pursuant to a best interest standard such as the one in the SEC's Regulation Best Interest, or another requirement to provide advice based

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[13] *Id*.

[14] To the contrary, in Advisory Opinion 83-60A, which discusses certain duties of broker-dealers, the Department used the phrase "the primary basis" in summarizing the five-part test.

[15] *Chamber of Commerce*, 885 F.3d at 382.

on the individualized needs of the Retirement Investor, the parties typically should reasonably understand that the advice will serve as at least a primary basis for the investment decision."[16]

While part of this sentence references a best interest standard (addressed below), the statement is not limited to that circumstance. The Preamble is saying that all that is needed for the primary basis prong to be satisfied is that a financial professional has made a recommendation. The Department concludes that in that case the parties will understand that the advice will serve as a primary basis for the investment decision. In other words, satisfaction of the recommendation prong automatically triggers the primary basis prong, or at least it "typically" would do so. Even if this were the case, and we do not agree that satisfying one prong automatically satisfies the other, the Department gives no guidance as to when a recommendation by a financial professional would *not* trigger the primary basis prong. In any event, the primary basis prong requires a *mutual* understanding; financial professionals that make recommendations in connection with annuity sales decidedly do not understand themselves to be taking on fiduciary status merely because they make a recommendation.

And it is not clear the Department's position is limited to the primary basis prong. The language quoted above references individualized recommendations. If the parties would "typically" understand a recommendation to satisfy the primary basis prong, then presumably they would "typically" understand a recommendation to satisfy the individualized prong.

As noted above, the Department states that the primary basis prong is triggered "particularly" when a recommendation is being made "pursuant to a best interest standard such as the one in the SEC's Regulation Best Interest." This places financial professionals in a "Catch-22": by complying with a best interest standard, which the SEC already requires and many states will be requiring for any annuity recommendation, even in a non-fiduciary sales context,[17] the financial professional is triggering multiple elements of the five-part test. And once a financial professional believes that he or she "might" have met the five-part test, the Proposed Exemption, if that will be relied upon, prevents the financial professional from taking a different position *because it requires affirmative acknowledgement of fiduciary status prior to engaging in a transaction covered by the Proposed Exemption*.

The Department attempts to contrast this situation with "a one-time sales transaction, such as the one-time sale of an insurance product," which the Department states "does not by itself confer fiduciary status under ERISA or the Code, even if accompanied by a recommendation that the product is well-suited to the investor and would be a valuable purchase." While we appreciate this statement, unfortunately we are left scratching our heads as to how to reconcile this with the Department's statement that a rollover recommendation satisfies the regular basis prong if there is an existing advice relationship or there are further recommendations and that the recommendation, made in the individual's best interest, satisfies the primary basis prong (and perhaps the individualized prong).

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[16] 85 Fed. Reg. at 40840.

[17] *See* National Association of Insurance Commissioners ("NAIC") Suitability in Annuity Transactions Model Regulation 275, sections 1.A. and 6.A.

F. Trailing Commissions as Evidence of a Fiduciary Relationship

The Preamble contains a very troubling footnote (number 41) which strongly implies that the existence of trailing commissions on insurance products is evidence of a fiduciary relationship. The footnote states: "Like other Investment Professionals, however, insurance agents may have or contemplate an ongoing advice relationship with a customer. For example, agents who receive trailing commissions on annuity transactions may continue to provide ongoing recommendations or service with respect to the annuity."[18] This footnote is apparently intended as a caveat to a sentence in the text which states that "a one-time sales transaction, such as the one-time sale of an insurance product, does not by itself confer fiduciary status under ERISA or the Code, even if accompanied by a recommendation that the product is well-suited to the investor and would be a valuable purchase." And this sentence is contained in a paragraph discussing the primary basis prong.

It is unclear exactly what the Department intends to achieve with this footnote, but we strongly disagree that trailing commissions imply anything at all about the relationship between the purchaser of the insurance product and the salesperson. Insurance companies that issue annuities and other products pay commissions to intermediaries and financial professionals over time for a variety of economic reasons. A trailing commission can, for example, align the financial interests of the insurance company, intermediary, and the selling agent. It is true that a trailing commission may be intended to incentivize a financial professional to reach out to the individual from time to time to confirm the product still meets their needs, answer any questions, and provide administrative services in connection with the product. But trailing commissions are still commissions, paid in connection with a sale.

More to the point, this sentence suggests that whenever (a) there is a recommendation and (b) *some* kind of compensation is being provided, then there must be "investment advice for a fee." In the case of trailing commissions, the Department seems to take it further to imply that the primary basis prong, and presumably the regular basis prong, will be satisfied. The Fifth Circuit's decision was, rightly so, extremely skeptical about this interpretation of what it means to provide investment advice "for a fee" because Congress intended "an intimate relationship between adviser and client beyond ordinary buyer-seller interactions."[19]

We urge the Department to clarify that the existence of trailing commissions, like commissions paid immediately upon the sale of a product, do not imply the existence of a fiduciary relationship, which depends on a *mutual* understanding of the parties.

III. <u>Comments on Proposed Exemption</u>

We support the Department's goal of offering an exemption that will allow parties who affirmatively wish to act as fiduciaries to provide investment advice and be paid for that advice, including in connection with rollovers. We appreciate that a number of the conditions in the

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[18] 85 Fed. Reg. at 40840 n.41.

[19] *Chamber of Commerce*, 885 F.3d at 374.

Proposed Exemption follow other statutory provisions (such as the requirement for no more than reasonable compensation) and align with requirements of the Securities and Exchange Commission's Regulation Best Interest ("Reg BI"), although we note some concerns below with respect to annuity sales not governed by Reg BI.

Indeed, annuities are commonly used as part of a portfolio put together by registered investment advisers who may be providing fiduciary services that meet the five-part test. Fiduciary consultants to plan committees routinely recommend the addition of annuities. The recently enacted Setting Every Community Up for Retirement Enhancement ("SECURE") Act contains a number of provisions that evidence Congress's desire to facilitate the use of annuities and other lifetime income vehicles in plans. Thus, to the extent that a financial professional and his or her firm enters into a mutual agreement to provide investment advice meeting the five-part test, we think an exemption which supports the adviser recommending a variety of products, compensation, and services, is a worthwhile goal.

In particular, we support that the Proposed Exemption allows for recommendations of a variety of types of annuities and does not favor one kind of annuity over another, as the Fiduciary Rule had done.[20]

That said, we do have some concerns and suggestions with respect to the Proposed Exemption, as detailed below.

A. The Proposed Exemption is Not a Solution to an Overly Broad Interpretation of the Five-Part Test

As detailed above in Part II of our comment letter, we are very concerned that the variety of statements in the Preamble to the Proposed Exemption, taken together, eviscerate the five-part test by introducing uncertainty to every prong of that test. At a minimum, because the consequences of a prohibited transaction are so severe, we fear that the variety of statements will result in some financial professionals who sell annuities concluding they have no choice but to rely on an exemption, such as the Proposed Exemption.

The Proposed Exemption is not, nor should it be, a solution to the problem of financial professionals feeling *forced* into fiduciary status when they do not intend to enter into a position of trust and confidence that is the hallmark of a fiduciary relationship. If that is the intent, then the Proposed Exemption will repeat the mistakes of the Fiduciary Rule. As the Fifth Circuit described the Fiduciary Rule:

> To begin with, DOL knew, and continues to concede, its new definition encompassed actors and transactions that the Department "does not believe Congress intended to cover as fiduciary." DOL had to create exemptions not

[20] We agree that the sale of an annuity, even when sold directly by an insurance company's employees, is not a "principal transaction" and thus does not need to be subject to the rules in the Proposed Regulation for principal transactions. *See* 85 Fed. Reg. at 40840.

> exclusively for the statutory purposes, ***but to blunt the overinclusiveness of the new definition***. Were it not for DOL's ahistorical and strained interpretation of "fiduciary," there would be no rationale for the BICE exemptions. Thus, when DOL argues that any exemptions would be more lenient on IRA financial services providers than deeming their ordinary activities to fall within the ERISA Title II prohibited transactions provision, DOL proves too much.[21] (Emphasis added.)

The various statements we describe in Part II of this letter could, if not corrected, result in "inadvertent" fiduciaries – parties that become fiduciaries despite making clear to a customer that no fiduciary relationship is intended. And the Proposed Exemption, insofar as it contains expensive conditions and requires detailed policies and procedures, is not a workable solution to the problem of inadvertent fiduciaries. Instead, the best solution to avoid inadvertent fiduciaries is for the Department to acknowledge that the parties can agree on the capacity in which a financial services professional will be providing services and the nature of the services to be provided.

The Proposed Exemption should be designed for those who wish to act a fiduciary and enter into a deliberate mutual understanding that fiduciary-level advice is intended.

B. The Department Should Correct the Preamble's Implication that the Best Interest Standard or Some Other Condition of the Proposed Exemption Establishes a Monitoring Requirement

Nowhere in the text of the Proposed Exemption is a requirement of ongoing monitoring set out. Indeed, the Preamble expressly acknowledges that the Proposed Exemption does not establish such a condition.[22] The Preamble also acknowledges that the parties can choose to establish a monitoring obligation by agreement should they wish to do so.[23] In other statements in the Preamble, however, the Department proceeds to cast a large shadow of doubt over those acknowledgements.

Specifically, the Preamble states that an investment that has "unusual complexity and risk . . . may *require* ongoing monitoring to protect the investor's interests."[24] (Emphasis added.) It then comments that an "Investment Professional may be unable to satisfy the exemption's best interest standard with respect to such investments without a mechanism in place for monitoring." A requirement to monitor certain investments cannot be squared with the clear lack of any monitoring requirement in the Proposed Exemption. In any event, there is no clear or direct connection between complexity or risk and the need for monitoring.

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[21] *Chamber of Commerce*, 885 F.3d at 381-82.

[22] 85 Fed. Reg. at 40843

[23] *Id.*

[24] *Id.*

To the extent that an investment is complex and/or risky, the duty of care incorporated into the best interest standard adequately addresses this. As the SEC observed in its release accompanying Reg BI, and quoted by the Department in the Preamble, the greater the risk and the complexity of an investment, the greater the need for an adviser to be able to explain the product's features and risks.[25] But this does not lead to a requirement to monitor, which is apparent from the fact that Reg BI does not impose such a requirement.[26]

Moreover, the Department's assertions undermine the ability of parties to set out the scope of services that will and will not be provided. As the Department recognizes, monitoring brings added costs, which some investors are willing to bear for the benefits that can accompany monitoring. However, other investors may be capable of and willing to purchase a complex investment with greater risk and not wish to incur those additional costs. Presumably the Department does not intend to suggest that sales to such investors cannot satisfy the Proposed Exemption. Yet, that is the clear implication of its commentary.

C. The Exemption Should be Improved to Adequately Recognize Different Distribution Models and State Insurance Law

Annuities are distributed through a variety of models. Annuities that are securities are sold through broker-dealers. Annuities that are not securities may be sold by employees of the insurance company or by independent agents. Many Committee members permit agents to sell their annuity products, as well as products issued by unrelated insurance companies ("independent distribution").

A fundamental problem with the "Best Interest Contract Exemption" was that an insurance company using an independent distribution model was forced to monitor and control agents that the insurance company was in no position to monitor or control. This is because these agents have business relationships with multiple insurance companies and are also selling the products of multiple companies. Insurance companies would not have access to the information and agreements related to annuity products offered by independent agents from unaffiliated insurance companies, and thus would not be in a position to provide meaningful oversight of recommendations other than from a "siloed" view of their own products.

The Proposed Exemption, while it attempts to address some aspects of this problem, unfortunately does not provide a complete solution. By requiring the participation of a "Financial Institution," which is limited to certain types of entities including insurance companies and broker-dealers, the Proposed Exemption does not adequately recognize the structure of an independent distribution model for annuities. It presumes that an insurance company which is no position to monitor or control an independent agent is in fact acting as a fiduciary simply because the independent agent is providing fiduciary investment advice. We

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[25] *Id.* note 51, quoting Regulation Best Interest Release, 84 FR at 33376 & n. 598.

[26] *See, e.g.,* 84 Fed. Reg. at 33334 (stating "We confirm that . . . Regulation Best Interest *would not* (1) Extend beyond a particular recommendation or generally require a broker-dealer to have a continuous duty to a retail customer or impose a duty to monitor. . . ."). (Emphasis in original.)

believe that the participation of an insurance company is appropriate and necessary only if the insurance company is, in fact, acting as a fiduciary.

While the Preamble does seem to recognize certain of the challenges for an insurance company acting as a Financial Institution, it cannot overcome all the structural issues that exist in asking an insurance company to provide review and oversight of an independent agent. The insurance company simply does not have control over the agent's selling activities and the agent's annuity product offerings (i.e., their "product shelf") the way that a broker-dealer can control those aspects of one of its registered representatives. As a result, the insurance company as Financial Institution has certain inherent limitations in attempting to conduct its duties under the Proposed Exemption. The Preamble recognizes this limitation to some degree by stating:

> In this regard, insurance company Financial Institutions would be responsible only for an Investment Professional's recommendation and sale of products offered to Retirement Investors by the insurance company in conjunction with fiduciary investment advice, and not unrelated and unaffiliated insurers.[27]

We would note, however, that because of the lack of control the insurance company has with respect to the independent agents, it will be difficult for the insurance company to "implement procedures to review annuity sales to Retirement Investors to ensure that they were made in satisfaction of the Impartial Conduct Standards,"[28] which is a higher standard than that required of the insurer to ensure that such sales are suitable. In addition, while the Preamble indicates that an insurance company as Financial Institution has limited duties with respect to an Investment Professional's recommendation of products of unrelated or unaffiliated insurers, we believe an insurer should have additional protections related to the compensation that may be paid to independent agents. As an example, we note that the National Association of Insurance Commissioners ("NAIC") Suitability in Annuity Transactions Model Regulation (#275) ("NAIC #275"), as revised in March 2020, addresses this point. Section 6(C)(4)(b) of NAIC #275 indicates expressly that an insurer is *not required* to include in its system of supervision:

> Consideration of or comparison to options available to the producer or compensation relating to those options other than annuities or other products offered by the insurer.

The Proposed Exemption should at least recognize this limitation faced by an insurance company attempting to supervise the activities of agents in an independent distribution channel.

We would also point out that the Proposed Exemption is reasonably well integrated with Reg BI (which would cover the sale of SEC-registered annuities that are sold through broker-dealers) but does not, except in an offhand way, recognize the differing standards that apply to annuities sold under state insurance law. For example, there are only passing references to NAIC #275. We strongly recommend that the Department review NAIC #275 and state

[27] 85 Fed. Reg. at 40846

[28] Id.

insurance laws governing the duties of agents and determine if further changes are appropriate to ensure that compliance with state insurance law is harmonized with the final exemption. As a general matter, the Proposed Exemption should look to the supervisory mandates imposed on insurers under NAIC #275 as a basis for determining the fitness of the supervisory mandates under the Proposed Exemption for an insurance company acting as a Financial Institution. The development of those mandates by the NAIC involved more than two years of work, and multiple drafts, that resulted in a set of obligations on insurers that accurately reflects the supervisory limitations that exist for an insurer with respect to its independent agents.

D. The Department Should Remove the Acknowledgement of Fiduciary Status

The Proposed Exemption would require a "written acknowledgment that the Financial Institution and its Investment Professionals are fiduciaries under ERISA and the Code, as applicable, with respect to any fiduciary investment advice provided by the Financial Institution or Investment Professional to the Retirement Investor."[29] We recommend that this condition be removed.

As explained in Part II of this letter, the Department has introduced considerable uncertainty as to when a sales conversation might turn out to have created a fiduciary relationship, despite the intention and efforts of a financial professional and his or her firm not to take on that status. We hope the Department will correct these statements in the final Exemption, but even if the Department clarifies what it means, the damage is done—there will continue to be uncertainty about fiduciary status.

The fiduciary acknowledgement prevents the exemption from being used as a protective measure in case a prohibited transaction has been committed. As the Department knows, since the enactment of ERISA, whether a prohibited transaction has occurred, and whether an existing statutory or administrative exemption is available, is often uncertain. The Department routinely refuses to issue guidance on the contours of the existing statutory and class exemptions. It is perfectly appropriate for a party to rely on an exemption even when it is not clear one is needed.

But the fiduciary acknowledgement makes it impossible to use the Proposed Exemption as a protective measure. If a Financial Institution believes that for *some* relationships its employees, representatives or agents might meet the five-part test, it has no choice under the Proposed Exemption but to transform all of these into fiduciary in nature by affirmatively stating the Financial Institution and its Investment Professional are acting as fiduciaries.

This condition is not needed. There are a long line of class exemptions allowing fiduciaries to receive relief from violations of ERISA section 406(b) without the need to acknowledge fiduciary status, including all the exemptions that the Department sought to amend in the Fiduciary Rule.

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[29] 85 Fed. Reg. at 40863.

We also believe that the acknowledgement of fiduciary status can cause confusion because of other regulatory regimes. For example, Reg BI does not require brokers to act as fiduciaries and stating that they are could cause confusion with the Form CRS. Similarly, insurance agents regulated by state law generally do not act as fiduciaries, and the new model disclosure form under NAIC #275 does not require a disclosure of fiduciary status. In fact, such a disclosure in another document could be materially misleading given the obligations that NAIC #275 imposes, and does not impose, on insurance agents.

We have a broader and more fundamental objection to the use of this disclosure with respect to IRAs. Code section 4975, which imposes an excise tax on fiduciaries as defined in Code section 4975(e)(3), has no role in regulating the duties and obligations of fiduciaries other than to require that they pay a tax if they engage in certain prohibited transactions. The Proposed Exemption would require a disclosure that the Financial Institution and its Investment Professional are acting as fiduciaries "under the Internal Revenue Code." But that is nearly meaningless, in terms of regulating conduct, other than that prohibited transactions must be avoided.

In the Preamble, the Department states that it "does not intend the fiduciary acknowledgment or any of the disclosure obligations to create a private right of action as between a Financial Institution or Investment Professional and a Retirement Investor and it does not believe the exemption would do so."[30] In the context of an IRA, we think that this acknowledgement absolutely could create a private right of action where one does not exist. State law governs the duties and obligations of fiduciaries—in fact, the concept in ERISA was taken from the duties required of trustees under state law. A reasonable person would understand that someone calling themselves a "fiduciary" would act in the same way that a trustee would act, i.e., with an expectation of trust and confidence and with a duty of undivided loyalty. It is for this reason that some states, such as New York, are imposing a fiduciary duty on insurance agents, and other states, such as Iowa and Arizona, are not, because the word "fiduciary" has meaning and content.[31] And that meaning and content may be enforced by private rights of action under a variety of state law theories.

We submit that the Department has failed to provide sufficient justification for why this fiduciary acknowledgement is needed. The justification in the Preamble is limited to a single sentence: "The proposed disclosures are designed to ensure that the fiduciary nature of the relationship is clear to the Financial Institution and Investment Professional, as well as the Retirement Investor, at the time of the investment transaction." If the five-part test is satisfied, however, the nature of the relationship is already clear, because the five-part test requires a *mutual understanding* of that relationship.

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[30] 85 Fed. Reg. at 40844.

[31] New York Department of Financial Services Insurance Regulation 187 (11 NYCRR 224); IAC 191-15.72(507B); Ariz. Rev. Stat. § 20-1243.

E. Other Issues that Should be Addressed

There are several other aspects of the Proposed Exemption that the Committee urges the Department to consider modifying.

1. Retrospective Review

We recommend that the Department reconsider the need for the retrospective review. We are concerned that this is simply the audit requirement from the Best Interest Contract Exemption in another form. Further, the requirement seems unnecessary. The entities involved in the Proposed Exemption are all heavily regulated financial institutions that are subject to various audit and other compliance procedures appropriate for their businesses. That's the reason the Department chose those types of institutions. If the Department decides to retain the retrospective review, we recommend that the chief compliance officer (or equivalent position) be the person to receive the review. This is the person with the expertise to evaluate it.

2. Availability of Proposed Exemption for In-House Plans

The Proposed Exemption is not available if the plan is covered by ERISA and "the Investment Professional, Financial Institution or any affiliate is (A) the employer of employees covered by the Plan, or (B) a named fiduciary or plan administrator with respect to the Plan that was selected to provide advice to the Plan by a fiduciary who is not independent of the Financial Institution, Investment Professional, and their affiliates."[32] In other words, the exemption is not available for in-house plans of financial institutions.

We urge the Department to reconsider this exclusion. If the Department determines that the Proposed Exemption is otherwise in the interest of participants and protective of their rights, as required by ERISA section 408(a), then excluding participation in an advice program by employees of a financial institution will result in their losing access to a valuable service. We appreciate the Department's concern that "employers generally should not be in a position to use their employees' retirement benefits as potential revenue or profit sources, without additional safeguards."[33] The Department could require that the compensation and fees paid to the Financial Institution are no more than would be charged or paid in connection with a plan that is not the in-house plan. If that were the case, participants would be adequately protected.

3. Ineligibility Notice Procedures

The Proposed Exemption provides that an Investment Professional or Financial Institution will not be eligible to use the exemption in two circumstances, one of which is receipt of a written ineligibility notice issued by the Office of Exemption Determinations. The bases for a notice of ineligibility identified in the Proposed Exemption involve allegations of extremely egregious conduct, and the period of ineligibility would be 10 years. The Proposed Exemption

[32] 85 Fed. Reg. at 40862.

[33] 85 Fed. Reg. at 40841.

provides an opportunity to be heard, but in recognition of the seriousness of the conduct that would underlie the notice and the severity of the sanction, we ask the Department to consider a more objective process, such as the use of an administrative law judge before a written eligibility notice is issued.[34]

4. Compliance Disclosure Requirements

The Proposed Exemption imposes certain recordkeeping requirements, which is not unusual for an exemption. It is also not unusual that the Department or the Internal Revenue Service would expect to be able to review these records in an enforcement request. What is unusual is a broad requirement to make available to *any* participant or IRA owner *all* of the records of a Financial Institution demonstrating compliance with the exemption (other than records specifically relating to another participant or IRA owner). The Department offers no rationale or support for extending disclosure requests beyond agencies with enforcement authority. We are very concerned that this extension is an invitation for class action lawsuits and does not provide any meaningful protection to participants and IRA owners. The requirement is particularly troubling in the context of IRAs, because the excise tax rules in the Code do not provide for a private right of action. To the extent any records of a Financial Institution are relevant to a claim by a participant or IRA owner, subpoena procedures overseen by a judge are more than adequate.

In addition, we note that the Proposed Exemption requires the Financial Institution to make records available to "any authorized employee of the Department." In that regard, we recommend that this be limited to requests related to plans governed by ERISA. The Department does not have enforcement jurisdiction with respect to the prohibited transaction rules of the Code that apply to IRAs.

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If you have any questions, or if we can be of any assistance in your consideration of the issues summarized above, please do not hesitate to contact either of the undersigned at 202-347-2230.

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Attachment (List of Committee Members)

[34] For example, the Department's regulations have procedures involving administrative judges in the case of civil penalties. *See generally* 29 C.F.R. Part 2570. Such a procedure would allow someone independent of the Office of Exemption Determinations to review the matter.

Exhibit A

The COMMITTEE of ANNUITY INSURERS

AIG Life & Retirement, Los Angeles, CA
Allianz Life Insurance Company, Minneapolis, MN
Allstate Financial, Northbrook, IL
Ameriprise Financial, Minneapolis, MN
Athene USA, Des Moines, IA
Brighthouse Financial, Inc., Charlotte, NC
Equitable, New York, NY
Fidelity Investments Life Insurance Company, Boston, MA
Genworth Financial, Richmond, VA
Global Atlantic Financial Group, Southborough, MA
Great American Life Insurance Co., Cincinnati, OH
Guardian Insurance & Annuity Co., Inc., New York, NY
Jackson National Life Insurance Company, Lansing, MI
John Hancock Life Insurance Company, Boston, MA
Lincoln Financial Group, Fort Wayne, IN
Massachusetts Mutual Life Insurance Company, Springfield, MA
Metropolitan Life Insurance Company, New York, NY
National Life Group®, Montpelier, VT
Nationwide Life Insurance Companies, Columbus, OH
New York Life Insurance Company, New York, NY
Northwestern Mutual Life Insurance Company, Milwaukee, WI
Ohio National Financial Services, Cincinnati, OH
Pacific Life Insurance Company, Newport Beach, CA
Protective Life Insurance Company, Birmingham, AL
Prudential Insurance Company of America, Newark, NJ
Sammons Financial Group, Chicago, IL
Security Benefit Life Insurance Company, Topeka, KS
Symetra Financial, Bellevue, WA
Talcott Resolution, Windsor, CT
TIAA, New York, NY
The Transamerica companies, Cedar Rapids, IA
USAA Life Insurance Company, San Antonio, TX

The Committee of Annuity Insurers was formed in 1981 to participate in the development of federal policies with respect to annuities. The member companies of the Committee represent more than 80% of the annuity business in the United States.