The COMMITTEE of ANNUITY INSURERS

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Office of Regulations and Interpretations
Employee Benefits Security Administration
Attn: Definition of Fiduciary, RIN 1210-AC02
U.S. Department of Labor
200 Constitution Avenue, NW
Washington, DC 20210

Office of Exemption Determinations
Employee Benefits Security Administration
Attn: ZRIN 1210–ZA33; ZRIN 1210-ZA32
U.S. Department of Labor
200 Constitution Avenue, NW
Washington, DC 20210

Re: Comments on Proposed Retirement Security Rule: Definition of an Investment Advice Fiduciary (RIN 1210-AC02); Proposed Amendment to PTE 84-24 (ZRIN 1210-ZA33, Application No. D-12060); and Proposed Amendment to PTE 2020-02 (ZRIN 1210-ZA32, Application No. D-12057)

We are writing on behalf of the Committee of Annuity Insurers (the "Committee") to comment on the proposed regulation and proposed amendments to the prohibited transaction exemptions referenced above (collectively, the "Proposal"). The Committee urges the Department of Labor (the "Department") to withdraw the Proposal in full.

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

The Proposal suffers from the same fatal flaws that led the Fifth Circuit to vacate the Department's attempt in 2016 to expand the definition of an "investment advice fiduciary" beyond the scope of ERISA and congressional intent.[1] Even more troubling, the Proposal would significantly harm retirement savers, particularly those with lower incomes, by reducing their access to important services and annuity products – an outcome that was well-documented in the aftermath of the 2016 fiduciary rule.

Annuities are uniquely situated to protect American workers from numerous risks imperiling their retirement security, including the risk that a market downturn will erode their

[1] Chamber of Com. of the U.S. of Am. v. U.S. Dep't of Labor, 885 F.3d 360 (5th Cir. 2018).

savings and the risk of outliving those savings. As a result, federal policies should facilitate *better* access to annuities and *encourage* their use, not make it harder for individuals to understand how and when an annuity might be right for their retirement planning, which is what the Proposal would do. We have been especially disappointed by the rhetoric the Administration has deployed as part of the Proposal to unfairly and inaccurately disparage annuity products and the entire annuity industry. We are proud of our products, our services, our people, and our important contributions to the retirement security of millions of Americans. Unfortunately, the Administration's anti-annuity rhetoric has already endangered that security, regardless of whether or how the Department proceeds with the Proposal.

The Department has further damaged retirement security by crafting a Proposal that seems poised to suffer the same judicial fate as the 2016 fiduciary rule, given their similarity in substance and effect. Those similarities practically beg for new lawsuits, which will cost millions of dollars in legal fees to literally re-relitigate the same issues from 2016. Until such litigation is resolved, financial institutions and professionals will be forced to expend tremendous resources on compliance for a rule that the courts will likely strike down. Retirement savers ultimately will bear some of these costs. The Department also will be forced to use its own limited resources to defend the Proposal from the same valid criticisms that already won in court, rather than devoting those resources to other projects that have broad bipartisan support and will enhance retirement security.

All of these costs arising from the Proposal, along with the similarly extensive costs of the vacated 2016 rule and its 2010 predecessor, are what we would consider junk fees that the Department is imposing on the American retirement system. We think it is wrong, and it is time for the Department to end this 14-year campaign to impermissibly expand the law.

To make matters worse, the Department has short-changed stakeholders by imposing an unrealistically short timeframe for submitting written comments on the Proposal (39 working days spread over the biggest holiday season of the year) and by taking the unprecedented step of scheduling the public hearing well before written comments are due. The reason the Department took this unreasonable approach to public input is widely understood to be political. In our view, the Department's approach has violated not only fundamental principles of fairness, but also the requirements of the Administrative Procedure Act ("APA").

For these reasons, we urge the Department to withdraw the Proposal in full. If the Department nonetheless proceeds with the Proposal, we urge the Department to modify certain aspects, including PTEs 84-24 and 2020-02, to at least address some of its biggest shortcomings. While addressing those shortcomings could help blunt some of the Proposal's negative effects and bring some clarity to its long list of ambiguities, doing so would not cure the Proposal's fundamental defect: turning salespeople into ERISA fiduciaries in violation of the statute, congressional intent, and the Department's regulatory authority. That is why full withdrawal is the only real solution. The remainder of this letter expands upon these points.

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I. <u>The Department Should Withdraw the Proposal Regulation</u>

We urge the Department to withdraw the proposed regulation re-defining "investment advice fiduciary" because (A) the proposed regulation is in direct conflict with the Fifth Circuit's decision in *Chamber of Commerce*, (B) the proposed regulation would significantly harm retirement savers, particularly those with smaller account balances, (C) the Department's "Regulatory Impact Analysis" is flawed and incomplete, and (D) the Department's approach to public input likely violates the APA. These points are discussed below.

A. <u>The proposed regulation is in direct conflict with the Fifth Circuit</u>

In *Chamber of Commerce*, the U.S. Court of Appeals for the Fifth Circuit vacated, *in toto*, the regulatory amendments and new and amended PTEs published in April 2016 (collectively, the "2016 Fiduciary Rule"). The Fifth Circuit unambiguously held that the 2016 Fiduciary Rule conflicted with the text of ERISA and the Internal Revenue Code ("Code"). The Fifth Circuit focused on aspects of the 2016 Fiduciary Rule that, in effect, turned all salespeople into fiduciaries and that turned any one-time rollover recommendation into fiduciary advice. The court concluded that both of these aspects of the 2016 Fiduciary Rule violated ERISA based on the common law meaning of "fiduciary" and Congress's contemporary understanding of that meaning when enacting the statute:

> Had Congress intended to abrogate both the cornerstone of fiduciary status–the relationship of trust and confidence–and the widely shared understanding that *financial salespeople are not fiduciaries absent that special relationship*, one would reasonably expect Congress to say so. This is particularly true where such abrogation portends consequences that "are undeniably significant." Accordingly, the [2016] Fiduciary Rule's interpretation of "investment advice fiduciary" fatally conflicts with the statutory text and contemporary understandings…. The 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….*

> *Transforming sales pitches into the recommendations of a trusted adviser mixes apples and oranges*.[2]

In addition to these conclusions, the Fifth Circuit also expressly approved the Department's longstanding 5-part regulatory test for determining fiduciary status as an appropriate test for that purpose under the statute,[3] stating that:

> Congress is presumed to have acted against a background of shared understanding of the terms it uses in statutes…. And the phrase "investment advice for a fee" and similar phrases generally referenced a fiduciary relationship of trust and confidence between the adviser and client…. To begin with, DOL itself reflected this understanding in its 1975 definition of an "investment advice fiduciary"…. *DOL's 1975 regulation flowed directly from contemporary understanding of "investment advice for a fee," which contemplated an intimate relationship between adviser and client beyond ordinary buyer-seller interactions. The [2016] Fiduciary Rule is at odds with that understanding*…. That DOL contradicts 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 indicates that the Rule is far afield from its enabling legislation.[4]

The foregoing quotations from the Fifth Circuit's opinion are only samples of the numerous relevant statements from the opinion regarding why the court vacated the 2016 Fiduciary Rule as inconsistent with the statute and congressional intent. Overall, the undeniable conclusion from the Fifth Circuit decision, as well as from prior case law the Fifth Circuit cited,[5] is that when Congress used the word "fiduciary" in ERISA, it incorporated the common law meaning of that term, which requires the existence of a special relationship of trust and confidence between the parties, and that a mere buyer-seller transaction involving a salesperson and purchaser does not meet that standard and therefore does not give rise to fiduciary status.

Rather than accept or appeal the Fifth Circuit's decision, the Department chose to largely ignore it, stating in the preamble that the Department "rejects the purported dichotomy between a mere 'sales' recommendation to a counterparty, on the one hand, and advice, on the other, in the

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[2] *Id.* at 376, 380, 382 (emphasis added).

[3] Briefly, that test for fiduciary status requires that (1) there be an investment-related recommendation, (2) the person providing the advice provides investment advice on a regular basis (3) pursuant to a mutual understanding that (4) the advice will serve as a primary basis for decision-making and that (5) the advice will be individualized. 29 C.F.R. § 2510.3-21(c)

[4] *Chamber*, 885 F.3d at 373, 376 (emphasis added).

[5] *See id.* at 374 ("Substantial case law has followed and adopted DOL's original dichotomy between mere sales conduct, which does not usually create a fiduciary relationship under ERISA, and investment advice for a fee, which does.").

context of the retail market for investment products…. [S]ales and advice typically go hand in hand in the retail market."[6] The Fifth Circuit fully endorsed and embraced the concept that sales recommendations are not advice.[7] If the Department disagreed with the Fifth Circuit's explicit affirmation of this dichotomy, the Department should have appealed the court's decision, not publish a "new" proposal that is really a window-dressed version of the same proposal the Fifth Circuit already struck down.

In that regard, the new proposed regulation re-defining "investment advice fiduciary" suffers from the same flaws that the Fifth Circuit found fatal to the 2016 Fiduciary Rule. For example:

- ***The Proposal eliminates the same critical components of the 5-part test.***

  - *2016 Fiduciary Rule:* In the 2016 Fiduciary Rule, the Department eliminated the regular basis, mutual understanding, and primary basis prongs of the 5-part regulatory test for determining "investment advice fiduciary" status. The Fifth Circuit found that these prongs – particularly the regular basis and primary basis prongs – are critical to ensuring consistency with the common law meaning of "fiduciary" and therefore the meaning of that term in ERISA.[8]

  - *The Proposal:* The proposed regulation would eliminate these same three prongs of the 5-part test, thereby deviating from the common law meaning of "fiduciary" in the same manner that led the Fifth Circuit to vacate the 2016 Fiduciary Rule. The proposed regulation would expand the definition to include anyone who is in the business of selling annuities to plans and IRAs, including sales to retail customers and to plan fiduciaries. The Fifth Circuit found such effects of the 2016 Fiduciary Rule to be a fatal flaw. A sales pitch is not a fiduciary act, and making it so is a clear violation of current law and the Department's authority.

- ***The Proposal impermissibly attempts to regulate IRAs under Title II of ERISA.***

  - *2016 Fiduciary Rule:* The Fifth Circuit also found that the Department had exceeded its authority by attempting to regulate IRAs as part of the 2016 Fiduciary Rule. The court observed that "ERISA Titles I and II distinguish between DOL's authority over

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[6] 88 Fed. Reg. at 75907. The Department made an almost identical statement in the preamble to the 2016 Fiduciary Rule. *See* 81 Fed. Reg. at 20981 (April 8, 2016).

[7] *See*, *e.g.*, *Chamber*, 885 F.3d at 373 ("DOL's interpretation conjoins 'advice' with a 'fee or other compensation, direct or indirect,' but it ignores the preposition 'for,' which indicates that the purpose of the fee is not 'sales' but 'advice.' Therefore, taken at face value, the provision rejects 'any advice' in favor of the activity of 'render[ing] investment advice for a fee.' Stockbrokers and insurance agents are compensated only for completed sales ('directly or indirectly'), not on the basis of their pitch to the client. Investment advisers, on the other hand, are paid fees because they 'render advice.' The statutory language preserves this important distinction.").

[8] *See*, *e.g.*, *Chamber*, 885 F.3d at 366 ("Critically, the new definition dispenses with the "regular basis" and "primary basis" criteria used in the regulation for the past forty years. Consequently, it encompasses virtually all financial and insurance professionals who do business with ERISA plans and IRA holders. Stockbrokers and insurance salespeople, for instance, are exposed to regulations including the prohibited transaction rules.").

ERISA employer-sponsored plans and individual IRA accounts,"[9] and that while Title I requires plan fiduciaries to adhere to statutory duties of loyalty and prudence, "Title II did not authorize DOL to supervise financial service providers to IRAs in parallel with its power over ERISA plans."[10] The court went on to conclude that the 2016 Fiduciary Rule "impermissibly conflates the basic division drawn by ERISA,"[11] and that the PTEs the Department included with the 2016 Fiduciary Rule impermissibly had the effect of "actually subject[ing] most of these newly regulated actors and transactions to a raft of affirmative obligations," including by requiring "brokers and insurance salespeople [to] assume obligations of loyalty and prudence only statutorily required of ERISA plan fiduciaries."[12]

- *The Proposal:* The Proposal, including the proposed modifications to PTEs 2020-02 and 84-24, would have these same effects on IRA transactions that the Fifth Circuit found violative of the Department's regulatory authority. The Proposal broadly treats all financial professionals as fiduciaries and then requires any IRA salesperson wishing protection under the modified PTE to acknowledge and accept liability as a fiduciary who is subject to the duties of loyalty and prudence under Title I of ERISA.

- ***The Proposal impermissibly creates a private right of action for IRA owners.***

  - *2016 Fiduciary Rule:* The Fifth Circuit found that the 2016 Fiduciary Rule, and particularly the Best Interest Contract (BIC) Exemption, impermissibly created a private right of action in connection with IRAs that Congress did not intend to create under ERISA.

  - *The Proposal:* The Proposal would have a very similar effect by requiring financial professionals to acknowledge and accept fiduciary status as a condition of any relief in the modified PTEs, and in doing so to describe the Best Interest standard of care owed to them. As discussed further below, such statements could open the door to lawsuits under state law in circumstances where such laws ordinarily would not apply, in the absence of the Department requiring the financial professional's acknowledgement and acceptance of fiduciary status under ERISA. Likewise, the requirement to describe the Best Interest standard of care appears to be a back-door attempt to replicate the BIC from the vacated 2016 Fiduciary Rule.

- ***The Department's policy concern does not empower it to overstep its authority and has already been addressed by the appropriate regulators.***

  - *2016 Fiduciary Rule:* The Fifth Circuit also held that the Department's principal policy concern for promulgating the 2016 Fiduciary Rule did not justify it. The Department had pointed to "the lack of fiduciary safeguards in Title II" as its primary

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[9] *Id.* at 381.

[10] *Id.* at 364.

[11] *Id.* at 381.

[12] *Id.* at 382.

policy concern, but the court observed that such concern "was present when the statute was enacted, but Congress chose not to require advisers to individual retirement plans to bear the duties of loyalty and prudence required of Title I ERISA plan fiduciaries."[13] The court went on to conclude that the fact "[t]hat times have changed, the financial market has become more complex, and IRA accounts have assumed enormous importance are *arguments for Congress to make adjustments in the law, or for other appropriate federal or state regulators to act within their authority*. A perceived 'need' does not empower DOL to craft de facto statutory amendments or to act beyond its expressly defined authority."[14]

- *The Proposal:* In its new Proposal, the Department cites the same primary policy concern that the Fifth Circuit concluded was insufficient to empower the Department to act beyond its regulatory authority. If that policy concern was insufficient then, it remains so now. Furthermore, as the Fifth Circuit suggested, "other appropriate federal or state regulators" – the SEC and state regulators – have since acted within their authority to address the same underlying policy concern. This further detracts from the Department's stated policy concern and, therefore, the need for the Proposal. It also means the Department was successful in prompting changes that it has lauded as responsive to the policy concern it raised. In these circumstances, one wonders why the Department is resurrecting the same proposal that lost in the Fifth Circuit and is losing in pending litigation involving the preamble to PTE 2020-02.

Based on the foregoing, it is clear that the new proposed regulation contains the same failings that led the Fifth Circuit to strike down the 2016 Fiduciary Rule. In fact, the proposed regulation in many respects is *worse* than the 2016 Fiduciary Rule because it relies exclusively on a facts and circumstances test, using terms and phrases that are brand new, and for which the Department has provided insufficient time for the industry to digest and react.

B. The Proposal would significantly harm retirement savers, particularly those with smaller account balances

The Committee fully supports a regulatory regime that requires financial professionals, whether providing services through an investment advisory relationship or a brokerage or sales relationship, to make annuity purchase recommendations that are in the best interest of their clients, as they are required to do under SEC and state insurance laws. However, in order to ensure that Americans can obtain the financial protections that are right for their own situations, it is vital that they have access not only to a wide array of annuity products, but also to different models for obtaining those products.

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[13] *Id.* at 378-79.

[14] *Id.* (emphasis added). We also observe that the Proposal would appear to violate the McCarran-Ferguson Act by impermissibly regulating the conduct of agents compensated solely for the sale of insurance products. The American Council of Life Insurers ("ACLI") and Insured Retirement Institute ("IRI") include this point in their comment letters, which we fully endorse.

The "advisory" model, where the individual periodically pays a percentage of their retirement savings balance to an adviser in return for ongoing investment advice, is not right for everyone. It tends to work better for those fortunate savers who have higher account balances. Indeed, fee-based advisers often set minimum account balance thresholds, such as savings of at least $100,000, and charge percentage-based fees where the percentage decreases as the individual's account balance increases. Thus, financial professionals who use the advisory model typically serve wealthier clients.

For many other Americans, the brokerage model, where the financial professional is paid by a financial institution and the individual does not need to commit to paying ongoing annual fees for fiduciary investment advice, is more appropriate, cost-effective, and beneficial for the individual. The vast majority of annuities today are sold under the brokerage model, with the selling agent receiving commission-based compensation from the annuity provider. All annuities are inherently long-term products with a variety of protection features, as generally described below (see Part II of this letter). This requires sales agents to spend a considerable amount of time learning about the particular products they offer for sale and explaining the features (and alternatives) to customers. The insurer must compensate the sales agent for these efforts. Fee-based advisers typically are less willing to learn about annuity product features and details, and they may be reluctant to recommend purchasing some types of annuities because doing so would reduce their assets under management ("AUM") and therefore their own compensation (which itself is a conflict of interest for the advisory model that the Proposal ignores). As a result of these factors, annuities are available primarily through the brokerage model.

Maintaining retirement savers' access to both the advisory model and to the brokerage model is incredibly important to helping them achieve financial security in retirement based on their own personal circumstances. The Proposal, however, would significantly curb Americans' access to the brokerage model, and therefore to annuities. As described in Part II of this letter (below), annuities are critical to Americans' retirement security. They are the only product available to many Americans that can protect them from a wide range of risks endangering their retirement security, including longevity risk, mortality risk, morbidity risk, adverse selection risk, investment risk, timing risk, interest rate risk, disintermediation risk, and expense risk. Because the Proposal would cause Americans to lose access to the brokerage model, and because that model is the primary means of acquiring an annuity, Americans will lose access to the important protections from risk that only an annuity can provide.

The harm that the Proposal will cause is well-documented by various studies that measured the negative impact of the 2016 Fiduciary Rule, which, for the reasons discussed herein, is virtually identical to the Proposal in substance and effect. To summarize just a few of those studies:

- The national accounting firm Deloitte studied 21 financial institutions that represented 43% of U.S. financial advisors and 27% of the retirement savings assets in the market. The study found that as of the 2016 Fiduciary Rule's first applicability date, 53% of study participants reported limiting or eliminating access to brokerage advice for retirement

accounts, which the firms estimated as impacting 10.2 million accounts and $900 billion AUM.[15]

- In a Harper Polling survey of 600 financial professionals, 68% reported that they or their institutions would take on fewer small accounts.[16]

- A survey by the National Association of Insurance & Financial Advisors (NAIFA) of 1,093 members found that nearly 75% of financial professionals experienced or expected to experience an increase in the minimum account balances for the clients they serve.[17]

- A survey of Insured Retirement Institute (IRI) members found that "more than 60 percent of the distribution firms that participated in the Survey have, are planning to, or are considering exiting or de-emphasizing target markets such as small IRA holders and small retirement plan sponsors."[18]

- A 2021 study by the Hispanic Leadership Fund found that reinstating the 2016 Fiduciary Rule, which the current Proposal would largely do, would have the following effects:

    - "reduce the projected accumulated retirement savings of 2.7 million individuals with incomes below $100,000 by approximately $140 billion over 10 years," and

    - "have the most adverse effects on Blacks and Hispanics – reducing their projected accumulated IRA savings by approximately 20 percent over 10 years – contributing to an approximately 20 percent increase in the wealth gap attributable to IRAs for these individuals."[19]

In short, it is well-established that the 2016 Fiduciary Rule significantly curbed access to brokerage services through which annuities are primarily available. Given the similarities to the

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[15] Deloitte, *The DOL Fiduciary Rule: A study on how financial institutions have responded and the resulting impacts on retirement investors* (August 9, 2017), *available at* https://www.sifma.org/wp-content/uploads/2017/08/Deloitte-White-Paper-on-the-DOL-Fiduciary-Rule-August-2017.pdf.

[16] Harper Polling, *National Survey of Financial Professionals* (July 17, 2017), *available at* https://www.dol.gov/sites/dolgov/files/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB82/00601.pdf.

[17] *See* NAIFA letter to EBSA regarding RIN-1210-AB82 (August 4, 2017), *available at* https://www.dol.gov/sites/dolgov/files/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB82/00469.pdf. *See also* NAIFA, *Impact of the Proposed DOL Fiduciary-Only Rule on NAIFA Members* (Dec. 2023), *available at* https://advocacy.naifa.org/naifa-responds-to-the-dol (concluding, among other things, that the Proposal will cause an additional 42% of NAIFA advisors to institute minimum asset requirements for providing services).

[18] Insured Retirement Institute, Letter to Office of Exemption Determinations (Aug. 7, 2017), *available at* https://www.dol.gov/sites/dolgov/files/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB82/00541.pdf.

[19] Hispanic Leadership Fund, *Analysis of the Effects of the 2016 Department of Labor Fiduciary Regulation on Retirement Savings and Estimate of the Effects of Reinstatement* (Nov. 8, 2021) (emphasis in original), *available at* https://hispanicleadershipfund.org/wp-content/uploads/2021/11/FINAL_HLF-Quantria_FiduciaryRule_08Nov21.pdf.

2016 Fiduciary Rule, the new Proposal can be expected to have a similar negative impact on Americans' access to the many financial protections that only annuities can provide. This will only endanger their retirement security, which is the opposite of the Proposal's intended goal.

C. The Department's "Regulatory Impact Analysis" is flawed and incomplete

The Department's regulatory impact analysis (the "Impact Analysis") is flawed and fails to justify the Proposal. The ACLI has included a detailed discussion of this point in its written comments on the Proposal, which we strongly endorse. To summarize just a few of the many compelling points from the ACLI's analysis:

- ***The Impact Analysis does not adequately assess the Proposal's benefits and costs.*** The Impact Analysis acknowledges that the Proposal will change the market for advice and annuities, but it does not adequately examine, specify, or quantify those changes or their associated costs. The Impact Analysis naively assumes that the Proposal will universally benefit "retirement investors" but only speculates what those benefits might be, using vague concepts such as "'transfers' of social welfare to retirement investors from other entities in society."[20] Even though such "transfers" are "a primary objective" of the Proposal, the Impact Analysis acknowledges that there is insufficient data to "allow the Department to quantify the gains to investors or the components social welfare 'benefits' and 'transfers.'" A rule that will disrupt the advice and annuity markets and that will adversely affect lower- and middle-income Americans needs to be based on more than unspecified "social welfare benefits and transfers."

- ***The Impact Analysis does not adequately evaluate the effect of the 2016 Fiduciary Rule.*** The Impact Analysis does not reflect an adequate evaluation of how the 2016 Fiduciary Rule or the SEC's Regulation Best Interest rule affected different demographic and income groups or retiree and retirement savers. Worse, the Department casually attempts to discredit studies that actually evaluated such effects, many of which are described above, so that the Department could then ignore those studies.

- ***The Proposal should have been proceeded by an official RFI.*** The Impact Analysis seeks answers to *over 180 questions*, many of which require extensive analysis and research for which there is insufficient time and the answers to which will purportedly affect the Department's final rule. The Department should have addressed such a large-scale need for information by publishing an official "request for information," so that stakeholders would have time to respond and the Department could consider those responses before releasing the Proposal. The number and varied nature of questions the Department has posed, and the extremely short and ill-timed period the Department has provided for public response, strongly suggest that the Department released the Proposal prematurely and has pre-determined the outcome.

- ***The Proposal fails to properly address the value and utility of annuities.*** As discussed in more detail in Part III of this letter, annuities are critical to Americans' retirement

[20] 88 Fed. Reg. at 75937.

security. Unlike other types of investments or products, annuities do more than simply provide an investment return. They protect retirement savers from numerous risks they face when saving for and living in retirement, including longevity risk, mortality risk, morbidity risk, adverse selection risk, investment risk, interest rate risk, withdrawal timing risk, disintermediation risk, and expense risk. These important protections typically persist for long durations, such as 30 years or more for any given policyholder. Consequently, an adequate analysis of the Proposal should include a long-term focus and a careful examination of all annuity features available and their costs and benefits, not just returns to the investment component of some types of annuities. The Impact Analysis does not do this. Where the Impact Analysis does address annuities, it does not offer an honest, complete description, but rather offers half descriptions, emphasizing what the Department sees as limitations but neglecting to mention the benefits. This subtle bias by omission permeates the Proposal.

- ***The Proposal fails to adequately address consumer choice and consumer differences.*** The Proposal ignores consumer differences and the importance of consumer choice when planning for retirement. Because preferences, objectives, and risk tolerance differ, it is entirely feasible that some individuals would prefer an annuity that does not generate the highest return, but that offers other appealing features. The Department simply assumes that such an annuity is inferior without any basis in fact. Before concluding that potentially lower returns are an indication of conflicts of interest and an inferior product, it is necessary to clearly examine the purpose and objective of the product in question and the features offered, which neither the Proposal nor Impact Analysis do.

- ***The Proposal fails to address the impact on savings.*** The Proposal and Impact Analysis contend that retirement savers benefited from the 2016 Fiduciary Rule and will continue to benefit from the 2023 version. But other than speculating about investment returns and the timing of trades, the Department does not specify exactly *who* benefited, *how* they benefited, or *how much* they benefited. Concerningly, the Department does not know how the rule would impact the most important building-block of retirement security – savings. Indeed, "the Department acknowledges that there is significant uncertainty about the magnitude of savings that would result for retirement investors as a result of the proposed rulemaking."[21] This is a striking deficiency in the Impact Analysis.

- ***The Proposal cites studies that are narrowly or mis-focused and/or dated.*** Most of the studies referred to in the Impact Analysis are either narrowly focused or mis-focused for the DOL's intended purposes, and/or are recycled from the 2016 effort. For example, justification for the rule relies heavily on Egan et al, (2022).[22] However, this study focuses on fees and shorter-term investment returns, and it ignores the benefit of lifetime retirement income and risk management.

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[21] 88 Fed. Reg. at 75942.

[22] Egan, Mark; Ge, Shan; Tang, Johnny, "Conflicting Interests and the Effect of Fiduciary Duty – Evidence from Variable Annuities", *Review of Financial Studies*, vol. 35, no. 12, pp. 5334-5386.

D. <u>The Department's approach to public input likely violates the Administrative Procedure Act</u>

As mentioned at the outset of this letter, the Department has short-changed stakeholders by imposing an unrealistically short timeframe for submitting written comments on the Proposal and by taking the unusual step of scheduling the public hearing well before written comments are due. The reason the Department took this unfair approach to public input is widely understood to be political: if the Department does not finalize the Proposal by May 2024, the Proposal risks being overturned by a Congressional Review Act challenge in 2025.[23] These facts strongly suggest that the Department's procedural approach to the Proposal has violated the APA.

Abbreviated comment periods have been grounds for APA violations in the past, when combined with clear evidence of a predetermined political agenda.[24] Not only has the Department provided a mere 39 working days over the year-end holidays to digest all the details of the lengthy Proposal then develop and draft their written comments, the unusual (at best) move of scheduling the public hearing 21 total days before written comments are due means that many stakeholders will need to have their comments largely finished well before the actual deadline. And in denying a request for an extension of the comment period from several trade associations, EBSA Assistant Secretary Lisa Gomez justified the denial in large part based on the view that EBSA already got most of the input they need *before the Proposal was even released*:

> EBSA believes that its current proposal reflects significant input it has received from public engagement with this project since 2010, and looks forward to another robust comment period, public hearing, vigorous public debate, and stakeholder meetings. In addition, since the beginning of this Administration, EBSA has engaged informally with numerous stakeholders representing multiple viewpoints on issues related to the proposed rulemaking package. Therefore, at this point, EBSA does not intend to extend the comment period or delay the hearing.

In other words, EBSA generally has all the information it needs and is comfortable with the Proposal, so a normal comment period is not needed. Chairwoman Virginia Foxx of the House Education and the Workforce Committee drew this same conclusion from Assistant

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[23] *See*, *e.g.*, Bloomberg, *Punching In: Congressional Review Act Threat Looms for DOL Rules*, by Rebecca Rainey and Diego Areas Munhoz (November 20, 2023).

[24] *See*, *e.g.*, *Int'l Snowmobile Mfrs. Ass'n v. Norton*, 340 F.Supp. 2d 1249 (D. Wyo. 2004) (setting aside National Park Service ("NPS") final rule banning snowmobiles in national parks for violating both the APA and a federal environmental law in part because evidence showed that the agency had already made a prejudged decision with respect to the rule; in addition, finding that the NPS failed to adequately provide for public participation because it provided abbreviated comment timelines and "did not seriously consider public comments…. Based on the agency's failure to provide for public participation in the rule, including an abbreviated comment period of 30 days, the court concluded that "The NPS and/or the Clinton administration higher-ups had made a predetermined political decision, did not seriously consider public comments and performed mere pro forma compliance with [the National Environmental Policy Act ("NEPA")]. During this entire time the NPS ignored the purposes and procedures of NEPA and the APA in order to get this legislation approved before the end of the Clinton Administration.").

Secretary Gomez's dismissal of the need to extend the comment period, saying that "this statement seems to confirm that the public is being served a regurgitation of the same old rule and that EBSA has predetermined the outcome in violation of the APA."[25]

II. If the Department Does Not Withdraw the Proposed Regulation, Certain Changes will be Critical to Blunt its Fundamental Flaws

We are hopeful that the Department will take seriously the risk that, unless the Proposal is withdrawn and reproposed, it will not survive a court challenge and the Department will find itself right back where it was in 2018 – forcing the industry to spend many millions of dollars to get ready to comply with a rule that never went into effect (or did so only briefly). We also hope that the Department will prepare a reproposal that is balanced and thus could gain support from all sides and survive political changes in the future. That would be the best outcome.

But Committee members are realistic that the Department likely will move quickly to a final rule. If that occurs, ***the fundamental flaws in the test must be addressed***. The test for fiduciary status that the Department has proposed is so broad that it encompasses many interactions that are not fiduciary in nature. As noted earlier, the proposed test for fiduciary status is *worse* than the 2016 Fiduciary Rule because it not only covers the same non-fiduciary conduct and individuals, but relies exclusively on a facts and circumstances test and uses terms and phrases that are brand new.

Many of the recommendations that we make below will sound familiar because commenters, including the Committee, have been making them in some form throughout the 14-year life of this project. But those recommendations remain as vital as ever, perhaps more, to ensure that the test for fiduciary investment advice status properly captures true relationships of fiduciary trust and confidence and does not unnecessarily and inappropriately cause retirement investors to lose access to broad choice in investment and financial products, services, or financial assistance.

A. The proposed test does not properly distinguish fiduciary and non-fiduciary communications

Although Department officials have described the Proposal as more "targeted" to reflect the Fifth Circuit decision, the truth is that the test covers the same non-fiduciary conduct, the same products and services, and the same individuals and firms as the 2106 Fiduciary Rule. In this section we explain why the new proposed test does not meaningfully distinguish fiduciary and non-fiduciary conduct. The discussion that immediately follows focuses first on the part of the test that involves individualized recommendations, *i.e.*, paragraph (c)(1)(ii) of the proposed regulation, and at the end of this section we address concerns regarding the part of the test that

[25] The Chairwoman's letter is available at https://edworkforce.house.gov/uploadedfiles/11.17.23_final_fiduciary_rule_comment_period_letter_to_dol.pdf.

incorporates the activities of affiliates when determining fiduciary status, *i.e.*, paragraph (c)(1)(i) of the proposed regulation.

1. "Recommendation" is undefined and unclear

The term "recommendation" is not defined in the text of the Proposal, but in the preamble the Department takes the same position it took in the 2016 Fiduciary Rule: a recommendation is "a communication that, based on its content, context, and presentation, would reasonably be viewed as a *suggestion* that the retirement investor engage in or refrain from taking a particular course of action."[26] A mere "suggestion" is enough. This is too low of a bar to establish a fiduciary relationship of trust and confidence. The Department explains that it intends to view the meaning of recommendation similar to the SEC and FINRA, even though those regulators do not turn mere suggestions into *fiduciary* obligations. The Department must clarify and confirm that "recommendation" has the same meaning as in existing SEC and FINRA guidance, and this clarity should be provided in a form that stakeholders can rely on, not just in a preamble that bears no precedential weight.

In that regard, the SEC and FINRA have developed well-articulated and comprehensive guidance on how to determine if a recommendation has taken place, and in general it focuses on whether the applicable financial professional (or other source) has set forth a "call to action" for the customer.[27] There is voluminous authority indicating that the determination of whether a recommendation has been made is fact specific and turns on the context and content of the information provided to the customer.[28] Notice to Members (NTM) 01-23 goes on to clarify that a call to action should be viewed in terms of the overall context, and that an important factor in determining whether a call to action took place is whether it was directed to a large, un-targeted group (like a general advertisement), or a more tailored audience.[29] The concept of a recommendation being deemed to be a "call to action" has also been recently identified by SEC

[26] 88 Fed. Reg. at 75904 (emphasis added).

[27] *See Regulation Best Interest: The Broker-Dealer Standard of Conduct,* 84 Fed. Reg. 33318, 33335 (July 12, 2019) ("Reg BI Adopting Release") ("Factors considered in determining whether a recommendation has taken place include whether a communication 'reasonably could be viewed as a "call to action"' and 'reasonably would influence an investor to trade a particular security or group of securities.' The more individually tailored the communication to a specific customer or a targeted group of customers about a security or group of securities, the greater the likelihood that the communication may be viewed as a 'recommendation.'"); NASD Notice to Member 01-23: *Online Suitability: Suitability Rule and Online Communications* (April 2001) at p. 2 ("NTM 01-23") ("An important factor in this regard is whether—given its content, context, and manner of presentation— a particular communication from a broker/dealer to a customer reasonably would be viewed as a "call to action," or suggestion that the customer engage in a securities transaction.").

[28] *See* Reg BI Adopting Release at 33337; NTM 01-23 at p. 2 ("First, as NASD Regulation has often emphasized, "[w]hether a particular transaction is in fact recommended depends on an analysis of all the relevant facts and circumstances." (footnote omitted)).

[29] NTM 01-23 at p. 4 ("Members should analyze any communication about a security that reasonably could be viewed as a "call to action" and that they direct, or appear to direct, to a particular individual or targeted group of individuals—as opposed to statements that are generally made available to all customers or the public at large—to determine whether a "recommendation" is being made.").

staff in the "Digital Engagement Release."[30] The Department should clarify and confirm that "recommendation" has the same meaning as in the existing SEC and FINRA guidance.

2. "Regular basis" is now meaningless

The proposed test requires that the person "makes investment recommendations to investors on a regular basis as part of their business." To be frank, in the very limited time that the Committee's members and counsel have had to think about this brand-new phrase, we are not entirely sure what it means. One thing that does appear clear, however, is that this part of the test does not meaningfully exclude any interactions with anyone who works in the financial services industry.

If someone has a job that involves making suggestions (including sales suggestions) to IRA customers, plan participants, or plan fiduciaries, this will be done "on a regular basis as part of their business." Because the term "recommendation" is so broadly defined, this phrase captures regular non-fiduciary *sales* recommendations, *i.e.*, suggestions. In fact, any non-fiduciary interaction that involves a "suggestion" and that is regularly made as part of one's job is covered.

For example, imagine an insurance wholesaler who has regular sales calls with financial advisers. Those sales calls naturally involve suggestions that financial advisers should take a particular course of action, but none of them involve regular *fiduciary investment advice.* Yet, the Proposal seems to treat such sales interactions as fiduciary in nature, and the existence of PTE 84-24 is of no comfort because, among many other reasons, the wholesaler is in a position to provide impartial advice and is not in front of the retirement investor to make the required disclosures.

3. "Particular needs or individual circumstances" is meaningless

The test simply requires that "the recommendation is provided under circumstances indicating that the recommendation is based on the particular needs or individual circumstances of the retirement investor." Again, this phrase has little meaningful substantive content for any interaction between a plan participant, IRA owner, or plan sponsor, as nearly every interaction that involves a suggestion will be based in *some way* on the particular needs or individual circumstances.

For example, imagine that an individual who is age 58 and approximately seven years from retirement approaches an insurance salesperson about buying an annuity. If the salesperson takes the individual's age into account when identifying an appropriate annuity product, for example to ensure that surrender charges will not affect their retirement planning, the salesperson would be making a suggestion based on individual circumstances.

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[30] SEC Release No. 34-92766: *Request for Information and Comments on Broker-Dealer and Investment Adviser Digital Engagement Practices, Related Tools and Methods, and Regulatory Considerations and Potential Approaches; Information and Comments on Investment Adviser Use of Technology to Develop and Provide Investment Advice* (Aug. 27, 2021).

Or imagine that a defined benefit plan consultant contacts an insurance company to ask them to meet with the consultant and the plan committee to discuss pension de-risking, or to discuss annuities that will be used to terminate the plan. A salesperson from the insurance company then gives a presentation explaining why the plan should choose their products. This will clearly be a sales conversation, but the suggestions being made are clearly based on the particular needs or individual circumstances of the plan—namely the plan wishes to de-risk or terminate.

For similar reasons, merely responding to any request for proposal (RFP) from a plan regarding any aspect of the plan's investments or benefits could be a fiduciary act under the Proposal. In fact, we submit that, other than generic pamphlets, newspaper articles, and other communications aimed at no one in particular, nearly every "suggestion" could be said to be, in some way, based on particular needs or individual circumstances.

4. "Relied upon" is ubiquitous

The test requires that "the recommendation is provided under circumstances indicating that the recommendation … may be relied upon by the retirement investor as a basis for investment decisions that are in the retirement investor's best interest." We understand the point of this language is to remove the "primary basis" part of the current 5-part test. But we urge you to read that language a few times over and think about how people communicate with each other when a "suggestion" is involved. The whole point of a "suggestion" is to provide information that may be relied upon in making decisions. No "suggestion" that one human being makes to another is made with the idea that the other person might use it to make a decision that is *not* in their best interest.

5. The proposed test covers virtually everything

Based on the foregoing, it is clear that none of the various elements of the new test the Department has proposed in fact distinguishes non-fiduciary suggestions from fiduciary recommendations. All suggestions involving investments, investment strategies, or retirement income solutions create fiduciary status, unless this is being done for free.

In the preamble, the Department provides two examples of circumstances that the new test of fiduciary status would not cover. These two examples are largely strawmen, since they simply prove the test does not cover circumstances that are not even remotely investment advice. One example is a car dealer who regularly suggests that a consumer finance a purchase by tapping into retirement funds. The second example is a human resources employee of a plan sponsor who regularly meets with participants and makes suggestions that they take a particular investment action with respect to their retirement plan (such as routinely suggesting employees not take hardship distributions).

The Department says in the non-precedential preamble that these interactions do not create fiduciary status, but the truth is that the Department's regulation could cover them. These individuals are regularly making suggestions that involve retirement funds, and this is part of their job. The interactions are based on the individual's circumstances, and in each case the

suggestions are given with the idea that they may be relied upon in making a decision. The car dealer stands to receive compensation if the suggestion is taken, and the human resources employee is paid explicitly to have these meetings with employees.

The real point is that because the Department's test is both overly broad and based on facts and circumstances, the car dealer and human resources employee *cannot do their job and be confident that they will not need to defend a fiduciary lawsuit*. And this illustrates the same concern that Committee members have with the Department's approach: the test is so broad that nearly every interaction could end up in court with a plausible allegation of fiduciary status.

To summarize, for financial services firms and investment professionals who regularly interact with plan and IRA investors, the new test can be described as having only two requirements: (1) a "suggestion" is made and (2) that "suggestion" is based on some knowledge of the individual or plan. All the other elements of the test are largely irrelevant.

B. The proposed test improperly attributes affiliate services

The proposed test also creates fiduciary status when there is not even a personalized recommendation, if the firm is otherwise providing *unrelated* investment management services. Under subparagraph (c)(1)(i) of the test, a person is a fiduciary if they make a recommendation and "directly or indirectly (e.g., through or together with any affiliate) [have] discretionary authority or control, whether or not pursuant to an agreement, arrangement, or understanding, with respect to purchasing or selling securities or other investment property for the retirement investor." We assume the purpose of this is to capture circumstances in which a fee-based investment adviser is recommending a participant roll over assets to the adviser's investment account. But this also captures non-individualized sales recommendations simply because the firm is providing unrelated investment management services.

For example, assume an insurance company's investment management affiliate is managing funds for a plan in a group annuity contract separate account. The plan committee asks the insurance company to discuss whether it can offer annuities as distribution options for the plan. If the insurance company's representative makes *any* suggestion as to what the plan committee should do with respect to these annuities, fiduciary status is triggered. It is not necessary that the sales conversation is based on the needs of the plan, or even that the plan committee might use that sales pitch to assist it in making decisions for the plan. In other words, *any* suggestion, whether individualized or not, and even potentially including communications like general marketing materials, conceivably could be treated as fiduciary advice under the Proposal if an affiliate of the salesperson's company is separately providing unrelated investment management services.

C. The need for a true exception for sales conversations

Because of the extremely broad reach of the test for fiduciary status, as explained in the prior section, it is critical, as the Department recognized in 2015, that the Proposal "appropriately distinguishes incidental advice as part of an arm's length transaction with no expectation of trust or acting in the customer's best interest, from those instances of advice where customers may be

expecting unbiased investment advice that is in their best interest."[31] The Fifth Circuit agrees, as it concluded that having a "single sales transaction" create fiduciary status is "[e]xpanding the scope of DOL regulation in vast and novel ways."[32]

The Department thought about this problem correctly 14 years ago. In its 2010 proposal, the Department included a provision to clarify that a person is not a fiduciary if they can demonstrate:

> that the recipient of the advice knows or, under the circumstances, reasonably should know, that the person is providing the advice or making the recommendation in its capacity as a purchaser or seller of a security or other property, or as an agent of, or appraiser for, such a purchaser or seller, whose interests are adverse to the interests of the plan or its participants or beneficiaries, and that the person is not undertaking to provide impartial investment advice.[33]

The Department previously agreed on this principle, as reflected by the 2015 proposal and the 2016 Fiduciary Rule retaining a version of the seller's carve-out. That version, however, applied only to an arbitrary subset of investors who the Department had determined were smart or sophisticated enough to know what it means for someone to be selling a product. We fundamentally disagree that, as a rule, IRA owners and plan participants are wholly and always incapable of looking out for their own interests and understanding that people in the world do not work for free. If these individuals are given sufficient information and disclosures about the retirement products, including IRA rollovers, and there are rules against making misleading statements, then informed decisions can be made.

If insurance companies and their distribution partners become ERISA fiduciaries just by selling products to IRA customers and plan participants, insurers may have to limit and restrict these types of sales, either because they are unwilling to take on fiduciary status or are unwilling or unable to comply with a prohibited transaction exemption. That only means less choice, not more retirement security.

It is no answer to say that prohibited transactions exemptions are available to narrow the Proposal's overreach. When a person agrees to take on a fiduciary advice relationship, that decision is done willingly and with due consideration of the additional responsibilities, costs, and risks, including litigation risks. It is entirely inappropriate to *force* someone into fiduciary status simply because they wish to suggest that someone purchase a product (and do so by suggesting that this product is right for these individual circumstances), and explain that this can be treated as a fiduciary act because the existence of an exemption means the sale is not *per se* illegal.[34]

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[31] 80 Fed. Reg. 21,928, 21,941 (April 20, 2015).

[32] *Chamber*, 885 F.3d at 369.

[33] 75 Fed. Reg. 65267 (Oct. 22, 2010).

[34] Another example of this from a Committee member company involves the requirement in the proposed amendments to PTE 84-24 for an insurer to review the recommendations of an independent producer prior to issuing an annuity contract. If the insurer believes that the recommendation of the independent producer should be

D. At a minimum, communications with sophisticated fiduciaries, including licensed financial professionals who are fiduciaries to their plan clients, should be carved out from the rule

The truth is, this proposal is *unworkable* without some clear ability to have a conversation to sell a product without triggering fiduciary status in circumstances where it is understood that no fiduciary status is intended. Otherwise, the Department is making salespeople illegal. The Proposal's broad test of fiduciary status eliminates the ability of one party to act as a mere counterparty to the other.

The preamble to the proposed regulation includes a discussion of the need for a special provision to allow for recommendations to sophisticated advice recipients without improperly being treated as fiduciary advice. The Department, however, rejected such a provision in the Proposal, for what is a very strange reason:

> The Department acknowledges that some commenters in previous rulemakings have asserted that a specific "counterparty" provision is necessary to avoid limiting plan and IRA investors' choices in investment transactions. Commenters have suggested that the Department should adopt certain metrics, such as wealth or income, as conclusively establishing that the retirement investor has sufficient expertise and sophistication to foreclose fiduciary status of an advice provider. The Department is unaware, however, of compelling evidence that wealth and income are strong proxies for financial sophistication or inconsistent with a relationship of trust and confidence.[35]

It was the *Department* that included thresholds in the 2015 proposal and 2016 Fiduciary Rule based on the number of participants or assets under management. Industry commenters, including the Committee, believe that clear sales conversations should not be treated as fiduciary recommendations at all, but we all generally accepted that if the Department was going to have a test that treated them as such, we needed *some* rule where we could be sure that the conversation was safe to have, with a carve-out covering clearly sophisticated counterparties.

The Department's response to this concern is to say "[t]o the extent counterparties wish to avoid fiduciary status, they can avoid structuring their relationships to fall within the circumstances described in" the new regulatory test for fiduciary investment advice status.[36] As

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modified, how is the insurer supposed to respond without becoming a fiduciary? For example, the independent producer has recommended an annuity for an inherited IRA, but the inherited IRA is subject to required minimum distribution rules that will require a complete distribution from the inherited IRA before the end of the annuity's surrender charge period. Any suggestion of an alternate product with a shorter surrender charge period would seem to be a "recommendation" that would make the insurer a fiduciary.

[35] 88 Fed. Reg. at 75907.

[36] *Id.*

explained above, that is not really possible, or at least not possible to do with any certainty, because the test sets the threshold for fiduciary status so low. ***We cannot stress strongly enough that those who deal with ERISA plans and IRAs must be able to know with certainty that they are not going to be treated as fiduciaries.*** Class action plaintiff attorneys will not be deterred from bringing lawsuits solely because the Department said in a preamble that parties can arrange their affairs.

The Department explains in the preamble that in the context of "wholesaling" activity, namely communications by product manufacturers or other financial service providers to financial intermediaries who then directly advise plans, participants, beneficiaries, and IRA owners and beneficiaries, no carve-out is needed, because those communications "would not involve recommendations based on the particular needs or individual circumstances of the plan or IRA serviced by the intermediary." ***That is not correct.*** In fact, financial professionals value the conversations with insurance wholesalers precisely because the wholesaler can discuss individual needs of the professional's client and how they might be served by the wholesaler firm's products. For example, a financial adviser, acting as a fiduciary, might determine that providing guaranteed income that also includes some possibility of market growth is right for their client, and meet with a wholesaler to discuss that situation and learn about the insurance company's products. That conversation cannot happen under this new rule, even though the financial professional – they are a called a "professional" for a reason – understands that this wholesaler is only going to recommend their own products and is not acting impartially.

While we have never believed that a counterparty or seller's rule should be limited to sophisticated fiduciaries, the truth is that we *must* have some safe set of clearly defined circumstances under which insurance company representatives can meet with licensed financial professionals, plan consultants, or plan fiduciaries and discuss their products without risking inadvertently triggering fiduciary status under ERISA.

As we have said in the past, the lack of a carve-out for sales conversations has many adverse impacts that the Department continues to ignore. For example, annuities are commonly used by defined benefit plans to reduce the volatility and risk of the plan's portfolio, and in the case of the termination of a DB plan, annuities *must* be purchased to fund the termination. Suppose a plan fiduciary contacts an insurance agent to inquire about the possibility of the agent effecting the sale of a group annuity in connection with the de-risking or the termination of the plan. Under the Department's overly-broad test, the agent cannot make any communication suggesting the fiduciary should purchase the annuity for the plan; otherwise the agent is a fiduciary, triggering fiduciary status and requiring the agent/fiduciary to act for the "exclusive purpose" of the plan and its participants. It is not sufficient that PTE 2020-02 or 84-24 may be available to avoid the inherent prohibited transaction. Whether or not a prohibited transaction has occurred, the agent is now a fiduciary. This means the agent can no longer do her job – explaining the attributes of the annuity and its issuer – and now must take on a role entirely inappropriate for the agent, namely acting on behalf of that plan with the highest duty known to the law. This is the case even though everyone involved understands that the agent is not undertaking to provide impartial investment advice.

The lack of appropriate consideration for wholesaling and sales conversations, where both parties understand that one is trying to sell another a product, could have unintended consequences for the functioning of the capital markets. Besides offering critical guaranteed income, insurance companies and their products also serve critical roles in allocating capital and purchasing fixed income securities to fund their guarantees. Particularly in sales to sophisticated counterparties, the capital markets depend on robust competition—that counterparties will represent their interests and thereby properly allocate capital and provide for free enterprise to work. By forcing those who sell insurance products to sophisticated counterparties to either take on the role of *representing* their counterparty, or otherwise shy away from promoting their own products, the proposal will distort a critical part of the capital markets.

E. Offering a menu of investments in connection with an insurance product is not a fiduciary recommendation

The 2016 Fiduciary Rule included an exception commonly known as the "platform carve-out." This platform carve-out, at its heart, was a common sense expression of the idea that it cannot be "investment advice" for a service provider to put together a product – in this case a menu of available investments – which is offered generally to the market or segments of the market.

This was an important clarification for Committee members that offer variable annuities which include a preset list of investments available through a separate account. It cannot be a fiduciary recommendation to simply offer a variable annuity to the marketplace, including to 403(b) plan participants, but under the Department's Proposal that appears to be the case. In the preamble, the Department suggests that offering a preset list of investments would not trigger fiduciary status, but states that:

> whether a recommendation exists under the proposal will turn on the degree to which a communication is 'individually tailored' to the retirement investor or investors, and providing a selective list of securities to a particular retirement investor as appropriate for the investor would be a recommendation as to the advisability of acquiring securities even if no recommendation is made with respect to any one security. Therefore, the inquiry may turn on whether the provider presents the investments on the platform as having been selected for and appropriate for the investor (i.e., the plan and its participants and beneficiaries).[37]

As we have said elsewhere in this letter, a discussion in the preamble that the Department's overly-broad test does not need a carve-out is unsatisfactory. We believe this platform exception should be explicit in the text of the rule and be available regardless of the legal structure of a particular investment platform.

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[37] 88 Fed. Reg. at 75908.

F. A reasonable implementation period is needed and existing products should be grandfathered

The Department has proposed to make the Proposal effective 60 days after publication of the final rule and PTEs in the Federal Register. We have difficulty believing that the Department views this as an appropriate implementation timeframe. The Proposal's impact on the insurance industry is breathtaking. It is hard to imagine a regulation that affects more aspects of the retirement industry or crosses more business lines for service providers. We said in 2015 that there is no regulation in recent memory with this breadth, and it is true again with this largely similar Proposal.

Often when we provide comments to a regulator about a proposed change in regulatory requirements, we base our comments on estimates learned from experience implementing similar rules. This time, we know how disruptive this rule will be because the industry went through this once before – spending millions of dollars to examine the impact and prepare for implementation – before the federal courts struck down the 2016 Fiduciary Rule. Our firm worked with a number of individual Committee members to identify the changes needed to the 2016 Fiduciary Rule, and even with the effective date extension the Department provided for that rule, complete implementation was difficult. In short, since this Proposal is simply a resurrection of the 2016 Fiduciary Rule, at least the same amount of time is needed to implement it.

We also strongly urge the Department to provide that the Proposal does not apply to annuities sold and arrangements entered into prior to the effective date of the regulation, including with respect to commissions and other compensation on premiums paid for contracts sold prior to the effective date. This new regulation imposes significant costs that were not priced into products sold before the Proposal will become effective.

III. The Administration's Rhetoric Unfairly and Inaccurately Disparages Annuities

We are extremely disappointed by the caustic anti-annuity rhetoric the Administration has deployed as part of its strategy for the Proposal. The Administration unfairly and inaccurately disparaged annuity products and the entire annuity industry in the preambles to the Proposal, the related press releases and blog posts, and the President's remarks at the unveiling ceremony. These incendiary attacks are misleading, unwarranted, and unhelpful.[38] As we stated at the outset of this letter, ***we are proud of our products, our services, our people, and our important contributions to the retirement security of millions of Americans***. Our products protect real people who value an insured solution to their retirement needs, and the Department's rhetoric insults them all by suggesting they were somehow duped into choosing a path of personal responsibility by protecting themselves from risk.

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[38] Some Department officials have responded to criticism of the President's remarks at the unveiling by pointing to his statement to the effect that "most financial advisers give their clients good advice at a good price and are honest with them, but that is not always the case." While we appreciate this, a single five-second snippet during a prolonged, inaccurate attack on annuities did little to blunt the damage.

Annuities are critical to Americans' retirement security. Other than Social Security and defined benefit plans, annuities are the only means that Americans have to *guarantee* they will not outlive their retirement income.[39] With fewer employers offering defined benefit plans and the continuing strain that an aging population places on Social Security, it will be even more important to ensure that Americans have ready access to annuities in the decades to come – a fact that the Treasury Department and Congress have repeatedly recognized,[40] despite the Administration's bombast surrounding the Proposal.

In addition to protecting individuals from the risk of outliving their savings (longevity risk), annuities often provide other guarantees that are critical to assuring a secure retirement. Such guarantees typically cover multiple risks and persist for long durations, such as 30 years or more for any given policyholder. These risks include mortality risk, morbidity risk, adverse selection risk, investment risk, interest rate risk, withdrawal timing risk, disintermediation risk, and expense risk. Annuity insurers take on these substantial and long-duration risks so that individuals do not have to bear them alone.

When these risks and guarantees are properly understood, it is readily apparent to any objective and reasonable person why the "cost" of an annuity contract can, in many instances, be materially greater than the "cost" of purchasing a simple and uninsured financial instrument, such as shares in a passively-managed index fund. Thus, the criticism that the Department and others have lodged at annuity products for higher relative fees overlooks the fact that the fees pay for not only the costs associated with selling the product (discussed below), but more importantly, the valuable insurance benefits that annuities offer by protecting retirement investors from a variety of risks they face in retirement – features that are not available with other investments.

A particularly egregious example of ignoring the insurance features of annuities while lambasting their "costs" is the Council of Economic Advisers' blog post that accompanied the Proposal's unveiling.[41] The CEA launched a misleading attack on a particular type of annuity product – the fixed-indexed annuity. Fixed-indexed annuities, or FIAs, fill a critical gap in retirement security by enabling individuals to reap the benefits of market-based investment gains while completely avoiding exposure to market losses, all at costs that are reasonable for the

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[39] *See generally,* J. BROWN, O. MITCHELL, J. POTERBA, AND M. WARSHAWSKY, THE ROLE OF ANNUITY MARKETS IN FINANCING RETIREMENT (MIT Press, 2001).

[40] *See*, *e.g.*, Department of the Treasury and Department of Labor, *Request for Information on Lifetime Income Options for Participants and Beneficiaries in Retirement Plans*, 75 Fed. Reg. 5253 (Feb. 2, 2010) ("the Agencies are considering whether it would be appropriate for them to take future steps to facilitate access to, and use of, lifetime income or other arrangements designed to provide a stream of income after retirement" in light of "the continuing trend away from traditional defined benefit plans to 401(k) defined contribution plans and hybrid plans, including the associated trend away from annuities …."); the Setting Every Community Up for Retirement Enhancement Act of 2019, enacted as Division O of the Further Consolidated Appropriations Act of 2019, Pub. L. No. 116-94 (enacting numerous provisions intended to encourage the availability and use of annuities in retirement arrangements); the SECURE 2.0 Act of 2022, enacted as Division T of the Consolidated Appropriations Act, 2023, Pub. L. No. 117-328 (enacting even more provisions intended to encourage the availability and use of annuities in retirement arrangements).

[41] https://www.whitehouse.gov/cea/written-materials/2023/10/31/retirement-rule/.

protections provided. This is particularly attractive to risk-averse retirement savers who are seeking returns that can outpace other fixed income asset classes, especially in times of low interest rates.

In providing the insurance guarantees under an FIA, the insurer uses complex investment hedging strategies that no ordinary investor could replicate on their own, and the insurer takes on the risk that its strategies will actually achieve the results it has promised. When FIAs are considered in this objective light, it is easy to see why many individuals and the financial professionals who assist them find FIAs to be an ideal option. Indeed, the Department observed in the preamble to the proposed regulation that "*[f]iduciary duty protections tend to shift sales towards fixed indexed annuities and away from variable annuities*," presumably because of the protections just described.[42]

Despite this acknowledgement that fiduciary investment advice results in *more* FIAs being purchased, the CEA, and by extension the Administration, chose to attack FIAs in a way that broadly impugned their suitability for retirement investors. The blog is a master class in internal inconsistency and misleading rhetoric. In one breath, it recognizes that FIAs "could be attractive to risk-averse investors" and that the complex hedging expertise needed to achieve the investment results of an FIA would be "difficult for a retail investor" to replicate on their own. In the next breath, it characterizes the costs of obtaining access to such investment expertise through an FIA as "junk fees" because of the "additional costs and fees when compared to investments in comparable mutual funds," including the caps that the hedging strategies dictate will be placed on participation in market gains. ***Mutual funds are not comparable to FIAs because mutual funds do not protect the investor from market losses.*** The preamble to the Proposal also suffers from this defect in its discussion of FIAs. The CEA, Administration, and Department are unfairly ignoring the insurance features of FIAs while deriding their "costs" in a comparison of apples to oranges.

Another example of critics ignoring the insurance protections of annuities while criticizing their "costs" occurs in connection with guaranteed lifetime benefits, *i.e.*, insurance that guarantees the retiree will always be able to withdraw at least a minimum amount from their account for life regardless of investment performance or longevity. Such benefits can provide critically important protections against sudden and severe market downturns occurring right when the retiree needs income the most. Because such benefits protect against catastrophic events that, while potentially devastating to the retirement security of millions of Americans, are relatively rare in occurrence, critics tend to focus on how the fees affect returns under the contract during the "good times" in which the catastrophic event has not occurred. As one well-respected textbook on insurance has observed:

> The fees associated with VAs in general and GLBs in particular have been characterized as excessive by some. Other criticisms are similar to those associated with index annuities; the amount of potential gain sacrificed in return for the guarantees is too great relative to their underlying value. *Guarantee performance during*

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[42] 88 Fed. Reg. at 75940 (emphasis added).

> *the global equity market declines of 2008-2009 do not support this view*.[43]

The same textbook observes that researchers who examined economic aspects of guaranteed minimum withdrawal benefits (GMWBs) found that the benefit of the guarantee is substantial in times of market distress. They examined the hypothetical performance of variable annuities with a GMWB during the generally rising market for equities from 1979 through 1999 and during the falling markets of 2000 through 2008. The account balance and benefit base (the guaranteed withdrawal amount) grew at the same pace during the years of rising markets, but during the years of falling markets the benefit base was more than twice the account value.[44] This highlights the substantial economic (and emotional) benefits that such guarantees provide in bad financial times.

In that regard, concern over such potentially catastrophic financial events is a driving motivation for many annuity owners. These individuals elect to purchase GMWBs and similar benefits like FIAs to eliminate such concerns and to give them confidence to invest in the equity markets throughout retirement, thereby improving their chances for higher returns that can help sustain their financial security for the rest of their lives. Of course, this requires a trade-off between paying the fees necessary for the insurance protection and keeping those fees invested in the account value. For many, this trade-off is more than worthwhile; it is critical to their willingness to *invest*, rather than simply *save*.

This is evident from the fact that individual annuity owners are overwhelmingly satisfied with the annuity contracts they purchased. According to a Gallup survey of individuals who actually own annuity contracts:[45]

- On average, owners purchased their first annuity at age 51 and are currently age 74. Over nine in ten (92%) still own the first annuity they purchased. These statistics evidence their satisfaction with a product they have owned, on average, for more than 20 years.

- Over eight in ten owners cite having "a good rate of return" and the ability to "get payments guaranteed to continue for as long as you live" as important reasons for their purchase of an annuity (86% and 84% respectively).

- 86% agree that "[o]wning an annuity makes them feel more secure in times of financial uncertainty, such as during declines in the stock market," and 80% agree that "[b]eing

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[43] Kenneth Black, Jr., Harold D. Skipper, Jr., and Kenneth Black III, LIFE INSURANCE, at 139 (14th ed. 2013) (emphasis added).

[44] *Id.* at 601 (citing Chen, Peng and Milevsky, *Merging Asset Allocation and Longevity Insurance: An Optimal Perspective on Payout Annuities*, JOURNAL OF FINANCIAL PLANNING (Feb. 2010)).

[45] The Committee of Annuity Insurers, *Survey of Owners of Individual Annuity Contracts* (The Gallup Organization and Mathew Greenwald & Associates 2022), *available at* https://www.annuity-insurers.org/wp-content/uploads/2023/07/Gallup-Survey-of-Owners-of-Individual-Annuity-Contracts-2022.pdf. This survey is of the owners of non-qualified (after-tax, non-Roth) annuity contracts. However, the same annuity products (variable, fixed indexed, *etc.*) are purchased in the qualified markets, and we are not aware of any reason to think that purchasers' views would differ by market type.

able to invest in the stock market through annuities and still get guaranteed income for life adds to the financial security of retirees."

- 89% cite "it was a safe purchase" as a very important or somewhat important reason for purchasing their annuity, and 87% agree that annuities are "secure and safe."

- 84% agree that "[a]nnuities are an important source of retirement security," and 88% agree that "[a]nnuities are a good way to ensure their surviving spouse has a continuing income."

These perceptions of annuity products from people who actually purchase and own them for long periods of time tell a very different story than the anti-annuity narrative the Department, CEA, President Biden, and other critics have advanced. We believe our customers.

Another criticism that the Department and others have directed at annuities, including as part of the Proposal, relates to surrender charges, *i.e.*, charges that the insurer assesses if the contract owner withdraws substantial funds from their contract too soon after having purchased it. Such charges relate to the fact that an insurance company incurs a variety of costs and financial risks when it issues an annuity, including commission costs and the costs and investment risks inherent in hedging insurance guarantees under the contract.

Annuities are intended to be long-term products with a variety of protection features, as described above. This requires sales agents to spend a considerable amount of time learning about the particular products they offer for sale and explaining the features (and alternatives) to customers. The insurer must compensate the sales agent for these efforts and recover the costs of doing so. This can be done in different ways, including by imposing a charge at the time the premium or premiums are paid. Indeed, for many years, this was exactly how distribution and other acquisition costs were recovered by life insurance companies. However, few consumers today are willing to pay an up-front charge. As a result, most insurers offer a class of annuity products with a surrender charge that will enable the carrier to recoup at least some of its up-front costs if the individual surrenders the contract soon after purchasing it.

Surrender charges also serve purposes other than allowing the carrier to recover its up-front costs. For example, a fixed indexed annuity might impose a surrender charge because the carrier faces interest rate disintermediation risk if the contract is surrendered prior to the duration of the assets held to support the carrier's obligations under the contract. In that regard, to the extent that carriers can invest the premiums they receive in longer-term fixed income assets, they generally can earn better returns, which translates into higher annuity benefits. If, however, the carrier must reflect the possibility of an early surrender when investing the premiums it receives, the carrier would need to invest in shorter-duration fixed income assets, which typically earn lower returns that would translate into smaller annuity benefits. Thus, surrender charges can help carriers provide higher benefits under the annuity contracts they issue.

The Proposal omits any discussion of the true economics of surrender charges. It also fails to mention that most annuities offer what is called a "free withdrawal provision" that allows a policyholder the ability to withdraw a designated portion of their funds, often 10% each year, without incurring a surrender charge. Thus, when surrender charges do apply, it typically is in a

situation where the individual is not using the contract for the long-term savings and income purposes for which the contract was intended.

Overall, the Proposal evidences a lack of understanding or an unwillingness by the Department to objectively consider the benefits of annuities when criticizing them. This has led the Department and Administration to deploy inaccurate and misleading anti-annuity rhetoric as part of its strategy to rush the Proposal to finalization. Not only is the rhetoric unfair and unnecessary, it will only harm retirement investors by inappropriately scaring them away from the only financial product that can protect them from a plethora of risks they face in retirement.

IV. Comments on the Proposed Amendments to PTE 84-24 and PTE 2020-02

A. The Department should withdraw the proposed amendments

Insurers and financial professionals who distribute annuity contracts have relied upon PTE 84-24 for nearly 40 years, and we believe that PTE 84-24 has worked well. PTE 84-24 and its predecessor PTE 77-9 have applied under eight different presidents, many dozens of sessions of Congress, and for many different assistant secretaries of EBSA (and its predecessor PWBA), without ever being questioned until the Department began this project 14 years ago. The existence of PTE 84-24, we believe, has helped increase the availability of lifetime income products in plans and IRAs. PTE 84-24 has served precisely the goals that Congress seeks for exemptions: it is in the interests of participants and IRA owners, protective of their rights, and administratively feasible.

The Department should withdraw the proposed amendments to PTE 84-24 and PTE 2020-02 along with the proposed regulation. At a high level, this is necessary for two reasons. The first, we explained earlier: the premise of this entire project is to turn non-fiduciary interactions into fiduciary acts, and this cannot be solved by offering exemptions for the prohibited transactions that result. The second is explained in more detail below: the proposed amendments to PTE 84-24 and PTE 2020-02 will limit choices, create market distortions, and impose unnecessary costs and burdens that ultimately will be borne by individual savers.

B. Increased burdens under, and inconsistency between, proposed PTE 84-24 and state insurance laws

The structure that the Department has established under the Proposal with respect to the sale of annuities is as follows:

- With one exception, all annuities must be sold under PTE 2020-02. This includes the sale of annuities (of whatever kind) by employees of an insurance company, the sale of annuities (of whatever kind) by an independent agent who is treated as a "statutory employee" for tax purposes, and the sale of all annuities (of whatever kind) that are considered securities.

- The premise of PTE 2020-02 is that there must be a "Financial Institution" that is willing to agree to and affirmatively state fiduciary status, agree to supervise the "Financial

Professional" as a fiduciary, and most importantly serve as a deep pocket for the inevitable litigation that this project will bring.

Industry stakeholders have repeatedly informed the Department that even if this structure makes sense in some cases (and it really does not), it is unworkable in the case of independent producers who sell non-security insurance products of multiple insurance companies. In connection with the 2016 Fiduciary Rule, the Department attempted to propose a special exemption that would allow Insurance Marketing Organizations (IMOs) and similar entities to serve as the "Financial Institution," but that effort was largely dropped as itself being unworkable.[46]

The Department's latest proposed solution is to allow PTE 84-24 to be used solely for "Independent Producers" but impose on the insurance companies whose products these Independent Producers sell the obligation to supervise the sales and compensation of the Independent Producers. Under revised PTE 84-24, insurers would need to perform the same actions and assume essentially the role that a supervising fiduciary would assume, just without the need to literally say in writing that the insurer is a fiduciary.

In that regard, under section VII(c) of proposed PTE 84-24, reliance on the exemption is conditioned on Insurers' creating, maintaining, enforcing, and reviewing and updating certain policies and procedures related to supervision and oversight of the Independent Producers offering annuities to Retirement Investors.[47] The policies and procedures address: (1) review of Independent Producers recommendations ("Recommendation Review Procedures"); (2) Conflicts of Interest ("Conflict Procedures"); and (3) authorizing and retaining Independent Producers for the sale of an Insurer's products ("Producer Review Procedures"), including a requirement for an annual retrospective review of each producer's fitness. In the preamble, the Department asserts that:

- The proposed Recommendation Review Procedures are "consistent with the language in NAIC Model Regulation Section 6.C.(2)(d);"[48]

- the proposed Conflict Procedures are "consistent with although more protective than, the narrower NAIC Model Regulation section 6.C.(2)(h);"[49] and

[46] 82 Fed. Reg. 7336 (Jan. 19, 2017).

[47] Capitalized terms that we use but have not defined have the meanings ascribed to them in proposed PTEs 84-24 and 2020-02.

[48] 88 Fed. Reg. at 76011. The preamble to the proposed changes to PTE 84-24 refers to the NAIC Suitability in Annuity Transactions Model Regulation (#275) as the "NAIC Model Regulation," and this comment letter will maintain that terminology for simplicity.

[49] 88 Fed. Reg. at 76011.

- the proposed Independent Producer Review Procedures are "consistent with but more protective than, NAIC Model Regulation section 7.B.(11)."[50]

Despite the Department's contention that the proposed insurer policies and procedures required for Independent Producer oversight are "consistent" with the NAIC Model Regulation, they are inconsistent with certain provisions (*e.g.*, the Conflict Procedures), and will impose a significant increased burden on Insurers to create, maintain, and enforce new policies and procedures in addition to their procedures already in place to meet the NAIC Model Regulation supervisory requirements.

As indicated above, the Committee recommends that proposed PTE 84-24 be withdrawn. If the Department does not take that step, ***the policies and procedures requirements should be revised to provide a safe harbor for any Insurer who supervises its annuity sales in compliance with the NAIC Model Regulation***. The safe harbor should apply whether the Insurer conducts the reviews itself or outsources the duties of the supervisory system to third parties.

The NAIC took exactly this approach in the NAIC Model Regulation where it expressly permitted outsourcing and recognized the complexity of dueling regulatory structures imposed for the sale of annuities that are also regulated as securities products (*e.g.*, variable annuities) by adopting the so-called "Comparable Standards" safe harbor in Section 6.E of the NAIC Model Regulation ("Comparable Standards Safe Harbor"). The NAIC relied on the previously-considered and designed structure built through "sister" regulatory regimes to simplify the landscape for market participants and utilize a regulatory construct with an historical track record of accepted practices.

Set forth below is a more detailed review of the policies and procedures required under proposed PTE 84-24 and their departure from the current framework under the state insurance laws.

1. Recommendation Review Procedures

Section VII(c)(1) of proposed PTE 84-24 sets forth the following requirement related to an Insurer's Recommendation Review Procedures:

> The Insurer establishes, maintains, and enforces written policies and procedures for the review of each recommendation before an annuity is issued to a Retirement Investor pursuant to an Independent Producer's recommendation that are prudently designed to ensure compliance with the Impartial Conduct Standards and other exemption conditions. The Insurer's prudent review of the Independent Producer's specific recommendations must be made without regard to the Insurer's own interests. An Insurer is not required to supervise an Independent Producer's

[50] *Id*.

recommendations to Retirement Investors of products other than annuities offered by the Insurer.

While the preamble categorizes the Recommendation Review Procedures as "consistent" with the NAIC Model Regulation, that categorization overlooks a fundamental difference between the competing supervisory obligations. Under the NAIC Model Regulation, while the responsibility for meeting the supervisory obligations ultimately rests with the Insurer, there is an express provision that allows for Insurers to outsource the duties of the supervisory system to third parties.[51] In addition, the Insurer can rely on the Comparable Standards Safe Harbor to allow for significant assistance in its obligations to be performed by other regulated entities (such as a broker-dealer, investments adviser, or certain fiduciaries). As a result, proposed PTE 84-24 significantly increases the direct burdens on Insurers in their supervision of Independent Producers.[52]

In addition, the Insurer's responsibilities under proposed PTE 84-24 with respect to the procedures related to the standard of care of the recommendation (*e.g.*, meeting the NAIC Model Regulation's "best interest" standard versus proposed PTE 84-24's Impartial Conduct Standards) are significantly different than those under the NAIC Model Regulation. Under the NAIC Model Regulation, the applicable procedures must be "designed to ensure there is a reasonable basis to determine" the recommendation meets the standard. However, proposed PTE 84-24 requires the Recommendation Review Procedures to be "prudently designed to ensure compliance with the Impartial Conduct Standards." The proposed PTE 84-24 standards effectively require the Insurer to act as a guarantor of the Independent Producer's recommendations, rather than as a reasonable "back stop" for over-aggressive recommendations.

The Recommendation Review Procedures also add standards that are not required of Insurers under the NAIC Model Regulation. Under proposed Section VII(c)(1), the policies and procedures of the Insurer's review of recommendations "must be made without regard to the Insurer's own interests." This concept of reviewing of recommendations "without regard to" the Insurer's interest would be an additional requirement that Insurers would need to add to their procedures that does not exist under their procedures designed to comply with the NAIC Model Regulation. As has been stated on multiple occasions in the past, as well, the breadth of the language "without regard to" an Insurer's own interest causes significant concerns. Any time an Insurer reviews a recommendation, it is fundamentally acting in its own interest.

The Committee also notes that the preamble includes relatively comprehensive references to the NAIC Model Regulation's specific provisions related to recommendation review.[53] Given the somewhat sparse language included in proposed PTE 84-24 itself on recommendation review, the Committee believes it is extremely important to expressly clarify that the framework

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[51] *See* Section 6.C. of the NAIC Model Regulation ("Nothing in this subsection restricts an insurer from contracting for performance of a function (including maintenance of procedures) required under this subsection").

[52] Throughout the course of the Department's efforts to address the diverse nature of annuity distribution systems, the proposed PTEs have never managed to satisfactorily address the differences in annuity distribution channels such as through independent marketing organizations, broker-dealers, and investment advisers.

[53] *See* 88 Fed. Reg. at 76011, including in particular footnote 15.

for transaction review (including the explicit references to automated review) under the NAIC Model Regulation would be considered to meet the recommendation review requirements under proposed PTE 84-24 as well.

If the Department does not withdraw proposed PTE 84-24, the Committee urges the Department to make revisions as identified above to conform the Recommendation Review Procedures to the NAIC Model Regulation, or to provide that compliance with the NAIC Model Regulation requirements would be a safe harbor for compliance with proposed PTE 84-24.

2. Conflict Procedures

Section VII(c)(2) of proposed PTE 84-24 sets forth the following requirement related to an Insurer's Conflict Procedures:

> The Insurer's policies and procedures mitigate Conflicts of Interest to the extent that a reasonable person reviewing the policies and procedures and incentive practices as a whole would conclude that they do not create an incentive for the Independent Producer to place its interests, or those of the Insurer, or any Affiliate or Related Entity, ahead of the interests of the Retirement Investor. The Insurer's procedures identify and eliminate quotas, appraisals, performance or personnel actions, bonuses, contests, special awards, differential compensation, or other similar actions or incentives that are intended, or that a reasonable person would conclude are likely, to result in recommendations that are not in the Retirement Investor's Best Interest, or that subordinate the interests of the Retirement Investor to the Independent Producer's own interests, or those of the Insurer, or to make recommendations based on the Independent Producer's considerations of factors or interests other than the investment objectives, risk tolerance, financial circumstances, and needs of the Retirement Investor.

The preamble describes the Conflict Procedures as being "more protective than" the NAIC Model Regulation. The preamble indicates that an Insurer "could not offer incentive vacations, trips, or even educational conferences, if qualification for the vacation, trip or conference is based on sales volume or satisfaction of sales quotas." This fundamentally alters the manner in which certain types of compensation are paid, and *training is provided,* by Insurers, and is completely different than the manner in which the NAIC Model Regulation, and other regulators, have addressed conflicts created by such contests.

The NAIC, following the SEC's lead, focused on the more acute conflicts that take place when the sales incentives are designed with an element of time pressure, and thus restrict these types of compensation structures when they are designed to put a big reward, and heightened

pressure, on the salesperson.[54] By refusing to recognize the impact that time pressure has in creating a problematic sales practice, the Department has proposed a rule that will fundamentally reshapes incentive compensation and educational training provided by Insurers. The Committee notes that, in particular, eliminating the ability to provide educational conferences in any way conditioned on sales is short-sighted and fundamentally misunderstands the manner in which sales production levels are important factors in the design, budgeting, and content of such educational conferences.

The Committee believes that, if the Department does not withdraw the proposed PTE 84-24, it should revise the conflicts rules that prohibit sales incentive based on production to be more closely aligned with the NAIC Model Regulation and the SEC's Regulation Best Interest. If proposed PTE 84-24 is adopted with the existing Conflict Procedures requirements, every Insurer will need to fundamentally alter its compensation, education, and incentive programs. Setting up a structure that results in fewer training opportunities is bad for Insurers, Independent Producers, and Retirement Investors.

3. Producer Review Procedures

Section VII(c)(2) of proposed PTE 84-24 sets forth the following requirements related to an Insurer's Producer Review Procedures:

> The Insurer's policies and procedures include a prudent process for determining whether to authorize an Independent Producer to sell the Insurer's annuity contracts to Retirement Investors, and for taking action to protect Retirement Investors from Independent Producers who have failed or are likely to fail to adhere to the Impartial Conduct Standards, or who lack the necessary education, training, or skill. A prudent process includes careful review of customer complaints, disciplinary history, and regulatory actions concerning the Independent Producer, as well as the Insurer's review of the Independent Producer's training, education, and conduct with respect to the Insurer's own products. The Insurer must document the basis for its initial determination that it can rely on the Independent Producer to adhere to the Impartial Conduct Standards, and must review that determination at least annually as part of the retrospective review set forth in subsection (d) below.

The preamble indicates that the Producer Review Procedures are "consistent with but more protective than, NAIC Model Regulation section 7.B.(11)."[55] Section 7.B.11 of the NAIC Model Regulation focuses solely on the required annuity training and states that:

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[54] *See* Section 6.C.(2)(h) of the NAIC Model Regulation. *See also* the conflict of interest provisions of Regulation Best Interest (Section 240.15l-1(a)(iii)(D) ("Identify and eliminate any sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sales of specific securities or specific types of securities *within a limited period of time*" (emphasis added)).

[55] 88 Fed. Reg. at 76011.

> An insurer shall verify that a producer has completed the annuity training course required under this subsection before allowing the producer to sell an annuity product for that insurer. An insurer may satisfy its responsibility under this subsection by obtaining certificates of completion of the training course or obtaining reports provided by commissioner-sponsored database systems or vendors or from a reasonably reliable commercial database vendor that has a reporting arrangement with approved insurance education providers.

While the Producer Review Procedures under proposed PTE 84-24 may be generally consistent with the training requirements of the NAIC Model Regulation, such Procedures also call for sweeping new, and unclear, requirements with respect to the Insurer's vetting process of Independent Producers. Proposed PTE 84-24 effectively creates a new regulatory regime under which an Insurer's procedures require the Insurer to authorize (and re-authorize annually) an Independent Producer to sell an Insurer's annuities. The Insurer's Producer Review Procedures would be required to:

- Identify Independent Producers "who have failed or *are likely to fail* to adhere to the Impartial Conduct Standards;" and

- Identify producers who "lack the necessary education, training, or skill."

Failed or are Likely to Fail to Adhere to Impartial Conduct Standards: State insurance laws have clear requirements for the review of the qualifications of an Independent Producer before the producer is issued an individual insurance producer license. In addition, as part of an Insurer's onboarding process, and under state insurance appointment laws, there are clearly articulated guidelines and guardrails for authorizing an insurance producer to offer the Insurer's products.[56] As a general matter, it seems likely that the current standards and procedures in place under state insurance laws should routinely capture a prospective Independent Producer who has been formally found by a regulatory body, court, or the Insurer itself to have failed to adhere to the Impartial Conduct Standards.

It does not seem reasonable, however, to expect the Insurer's Producer Review Procedures to make accurate judgements about the *future* behavior of Independent Producers offering their products. A standard that requires the Insurer to identify an Independent Producer who is "likely to fail to adhere" to the Impartial Conduct Standards is a nebulous standard, and most likely impossible to rebut with hindsight. Certainly, a more reasonable crafting of the language could focus on the Insurer's actual knowledge about the proposed Independent Producer's disciplinary background and requiring the Insurer to assess that background prior to any decision to authorize the Independent Producer to offer products. The Committee believes the current language imposes a requirement on Insurers to effectively predict future behavior and

[56] *See also* 18 U.S.C. § 1033 that disqualifies certain individuals from associating with an insurance business and requires screening for such individuals.

it would serve solely to provide a strict liability trigger for a finding of a deficiency with the Insurer's Producer Review Procedures.

***Lacking the Necessary Education, Training or Skill*:** The NAIC Model Regulation has a very concrete requirement related to producer training: producers must complete the Insurer's general "producer product training" under Section 6.C.(2)(b) and also the "product-specific training and training materials which explains all the material features of its annuity product" under Section 6.C.(2)(c). While these provisions appear in the "supervisory" section, they are also addressed under the NAIC Model Regulation in Section 7. Proposed PTE 84-24 adds some new, and very unclear, concepts to the vetting process under the Producer Review Procedures: "education" and "skill." There is no description or amplification of those terms in the preamble.

The Committee notes that it is unclear whether "education" refers to insurance-specific education (like required pre-licensing education or continuing education under state insurance laws), general education requirements (like high school, college, graduate school), or even professional education (like certain insurance professional designations such as FLMI or others). The requirement that the Insurer's Producer Review Procedures vet the "skill" of an Independent Producer is unclear, subjective, and has no current analog under any licensing regime for financial professionals. The preamble includes no description of how "skill" should be analyzed under Producer Review Procedures. Is it how many clients have been served? How many years the Independent Producer has worked? What their "reviews" are like with their supervisors, if applicable?

Adding the "education" and "skill" prong to the vetting process under the Producer Review Procedures is new and unclear, and should be eliminated. If the Department does not remove these terms as factors, each such factor should be explained in much greater detail.

4. Retrospective Review

Proposed PTE 84-24 requires a retrospective review of the fitness of each Independent Producer under Section VII(d):

> The Insurer conducts a retrospective review, at least annually, that is reasonably designed to detect and prevent violations of, and achieve compliance with the conditions of the exemption .... As part of this review, the Insurer must prudently determine whether to continue to permit individual Independent Producers to sell the Insurer's annuity contracts to Retirement Investors.

This requirement would force Insurers to expend the resources that are used to "on board" a new Independent Producer every year. This would be a substantial increase in burdens associated with ongoing monitoring obligations of such producers.[57]

[57] For example, an Insurer with 5,000 Independent Producers would need to conduct 5,000 retrospective reviews – as contrasted with a single retrospective review under PTE 2020-02. It is difficult to imagine how this volume of reviews could be conducted in such a short period of time.

The current insurance regulatory regime relies on the current system of (a) periodic licensing renewals for each agent under state insurance law, and (b) periodic updates of the appointment of the agent under state insurance laws by the insurer to provide a form of ongoing monitoring of each producer. This should be more than adequate supervision, especially considering that Insurers also must prudently review each Independent Producer's specific recommendations. The retrospective review requirement would offer little or no additional protections and would be extremely redundant of the multiple other layers of robust protections under the Proposal, federal securities laws, and state insurance laws. The Committee recommends that the annual retrospective review requirements be eliminated as it is a very significant burden and adds virtually nothing to the current insurance regulatory regime's required, ongoing oversight process.[58]

C. <u>If the Department does not withdraw the proposed amendments to PTE 84-24 and PTE 2020-02, additional changes should be made</u>

Although we are urging the Department to withdraw the Proposal in full, we are realistic that the Department is likely to move forward with the basic structure of changes to the fiduciary test, PTE 84-24, and PTE 2020-02 as proposed, especially given the Department's approach to public input after releasing the Proposal. Working with Committee members, we have tried to identify as best we can, in the limited time available during the truncated comment period, the changes to proposed PTE 84-24 and PTE 2020-02 that will be needed to make them at least somewhat more workable, somewhat limit the amount of damage they will do to the choices available to plans and individuals, somewhat limit the ability of class action plaintiff firms to exploit the rule to generate strike suits, and somewhat limit the amount of market distortion that will be created.

The following discussion describes the issues we have identified so far. If we had a reasonable timeframe to review and digest the Proposal, we are certain that we would identify more issues. That is one of the real dangers of the Proposal – its broad and vague standards could create problems that cannot reasonably be anticipated in the 39 working days that stakeholders have to comment, and the Department later could issue new sub-regulatory guidance interpreting the rule's broad and vague standards to inappropriately expose stakeholders to liabilities that ERISA was not intended to impose. That is why full withdrawal is the only real solution. That said, we offer the following specific comments on the proposed amendments to PTEs 84-24 and 2020-02.

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[58] We also observe that when an Insurer discovers facts that suggest an Independent Producer has engaged in a non-exempt prohibited transaction, PTE 84-24 requires the Insurer to file Form IRS 5330. The instructions to that form make it clear that the form is filed by a disqualified person who is *liable for tax* under Code section 4975 (emphasis added). There is no option to file Form 5330 as an information return to report a prohibited transaction engaged in by a third party (the Independent Producer). The Insurer should not be subject to a 15% excise tax per year on a prohibited transaction when it reasonably believed the transaction to be exempt, nor should the Insurer be subject to the 100% excise tax on a prohibited transaction when it cannot reverse the commission and state law does not allow it to rescind the annuity contract unilaterally.

1. PTE 84-24 should not be limited to narrowly-defined "Insurance Commissions"

Under proposed PTE 84-24, the only compensation that may be paid in connection with the sale of an annuity, if "investment advice" is provided, is an "Insurance Commission" paid directly by the insurance company. The Department proposes to define Insurance Commission as follows:

> a sales commission paid by the Insurance Company or an Affiliate to the Independent Producer for the service of recommending and/or effecting the purchase or sale of an insurance or annuity contract, including renewal fees and trailing fees, but excluding revenue sharing payments, administrative fees or marketing payments, payments from parties other than the Insurance Company or its Affiliates, or any other similar fees.[59]

We strongly urge the Department to revise PTE 84-24 so that it provides relief for the same types of compensation covered by PTE 2020-02, whether paid by an insurance company or another party. If this limitation on PTE 84-24 remains, it will create market distortions and put unnecessary burdens on one way that annuities are sold, but not others.

While the sale of an annuity is typically compensated through an "Insurance Commission" as the Department has proposed to define it, that is certainly not the only compensation that might need relief. Insurers often make payments to intermediaries such as IMOs (sometimes based on total sales, but sometimes not) and these intermediaries support the selling agent with training, marketing, and administration. Intermediaries might compensate agents based on sales without regard to which insurance company's products were sold – a compensation structure that encourages the independent agent to consider the product that is best suited for a customer.

This is not fundamentally different than the payments that investment manufacturers make to any other intermediary. Mutual fund companies make payments to broker-dealers which are used to support individual registered representatives not related to particular fund sales. Insurance companies make payments to captive general agents which support an insurance agency and which might be used to compensate individual agents. PTE 2020-02 allows all these compensation structures, subject of course to the numerous requirements that it otherwise imposes, including that they do not exceed reasonable compensation, that they are not intended to result in recommendations that are not in the customer's best interest, and that they are disclosed.

There is no conceivable reason to impose a different rule on independent producers, and the reason the Department offers in the preamble is brief and inadequate:

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[59] Section X(g) of proposed amendment to PTE 84-24, 88 Fed. Reg. at 76031.

> This is consistent with the Department's historical understanding and intent. The exemption was originally granted in 1977, and the conditions were crafted with simple commission payments in mind. In the interim, the exemption was not amended or formally interpreted to broadly permit additional types of compensation.[60]

This explanation is paper-thin, especially as the entire premise of this Proposal is to reflect changes in the retirement product marketplaces in recent years. The Department is upending the annuity marketplace, and what it had in mind in 1977 is completely irrelevant.

This limit has nothing to do with the *amount* of the compensation. Under both PTE 2020-02 and 84-24, compensation paid to the individual who recommends a product must be reasonable (along with other restrictions). This limit relates instead to the *kinds* of compensation that can be paid, as well as by whom and to whom. PTE 2020-02, appropriately so, is flexible on how an investment advice fiduciary might be compensated, subject always to that compensation being reasonable. There is no reason to impose on fixed annuities sold through independent producers a structural limit that does not apply to any other investment, whether a mutual fund, bond, variable annuity, or even real estate. The Department itself has indicated that a goal of the Proposal is to provide uniformity in treatment. Accordingly, the Department should modify PTE 84-24 so that it provides relief for any reasonable compensation paid in connection with the sale of an annuity.

2. The Department should remove or significantly modify the "Eligibility" conditions

Because the Proposal will make virtually all annuity sales involving an agent or broker into fiduciary action, the use of PTEs 84-24 or 2020-02 is no longer "optional." No insurance company can be in the annuity business without being able to have its products available in at least IRAs. Under the proposed amendments to PTE 84-24 and 2020-02, the Department has given itself unprecedented power to put an insurance company out of business by creating "Eligibility" conditions that immediately disqualify an insurance company from selling its products. Taken as a whole, the Department has turned itself into a "gatekeeper" regulator, supplementing (or even supplanting) state insurance regulators, and has given itself the sole power of life and death to say which insurance companies can exist and which cannot.[61]

Under PTEs 2020-02 and 84-24, if any "Affiliate" of the insurance company is convicted of virtually any crime, the insurer is immediately disqualified from relying on the exemption. This is true even if the conviction has nothing to do with the sale of annuities to qualified plans and IRAs, and it is true even for convictions in any foreign jurisdiction, whether or not that foreign jurisdiction has the kind of due process rights that are available in modern democracies.

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[60] 88 Fed. Reg. at 76007.

[61] This is another example of the Proposal appearing to violate the McCarran-Ferguson Act. *See supra* note 14.

An insurance company also is disqualified from relying on PTE 84-24 if a single regional office of EBSA determines that the insurance company is:

> (A) engaging in a systematic pattern or practice of violating the conditions of this exemption in connection with otherwise non-exempt prohibited transactions; (B) intentionally violating, or knowingly participating in violation of, the conditions of this exemption in connection with otherwise non-exempt prohibited transactions; or (C) providing materially misleading information to the Department in connection with the conditions of the exemption.[62]

It appears that the Department does not need to *prove* any of this in any court, it only needs to say so.[63] And if it does say so, the only due process that the Proposal offers is that, after six months, the Department will grant one opportunity to be heard, with no right to appeal. After that, the insurance company is effectively out of business because PTE 84-24 is not available.

It is frustrating that we have to explain how unacceptable this is. This is a complete end-run around the limits Congress placed on the Department under Titles I and II of ERISA. First, Title I of ERISA generally requires that the Department go to federal court to obtain equitable relief to disqualify someone from serving in a fiduciary or other capacity with respect to an ERISA plan.[64] In the case of an IRA, which pursuant to Title II is governed solely by Code section 4975, the Department's enforcement authority is extremely limited: the Department solely has the power to interpret certain terms and to grant PTEs. As the Fifth Circuit made clear, "ERISA provisions must have different ranges; they cannot mean that DOL may comparably regulate fiduciaries to ERISA plans and IRAs" and the court concluded that by using the power to grant exemptions from prohibited transactions to regulate substantive conduct with respect to IRAs, the Department "abused that power."[65]

We further observe that the circumstances that could lead to disqualification are surprisingly (or perhaps unsurprisingly) broad. For example, the conviction by an "Affiliate" of an insurance company results in disqualification. "Affiliate" is defined to include employees. In other words, if a single employee of an insurance company is convicted of tax evasion or embezzlement, the insurance company can no longer use PTE 2020-02 or 84-24 and the Department can effectively put them out of business with little or no due process. The Proposal also defines "Affiliate" to include an entity unrelated to an insurer if the insurer has the power to "control" that entity's "policies." Insurers routinely dictate "policies" that their service

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[62] Section VIII(a)(2) of proposed PTE 84-24, 88 Fed. Reg. at 76029.

[63] Our firm has had many interactions with regional offices of EBSA. Investigators routinely assert allegations of ERISA violations; very often our clients disagree with the findings. Sometimes these are simply foot faults in disclosure, or reasonable disagreements about whether something constitutes a fiduciary breach. If a resolution cannot be reached, a *federal court* must settle the matter. This is the nature of basic fairness and the right to a neutral arbiter. It would be terrifying if the right to a day in court was not available.

[64] *See* ERISA section 502(a).

[65] *Chamber*, 885 F.3d at 381.

providers, such as third-party administrators, must follow with respect to products the insurer issues. Under the Proposal, this could make the service provider an "Affiliate" of the insurer, so if the service provider is convicted of a crime described in the Proposal, the insurer is potentially out of business, even if the crime is completely unrelated to the insurer.

We assume – or at least hope – that such results were not intended, but we know that there are many *intended* circumstances under which an insurer will be at the mercy of the Department to stay in business. Accordingly, the Department needs to remove the bulk of the Eligibility provisions, so that it focuses on circumstances under which the insurer is convicted of a crime related to the sale of annuities to plans or IRAs. In addition, the Department should not have the ability to issue a "written ineligibility notice" that disqualifies an insurer from relying on PTE 2020-02 or 84-24, without having to go to federal court to seek equitable relief or provide some real due process with an arbitrator that is not the Department.

3. The exemptions should not require an evaluation of the prudence of a rollover if no rollover recommendation is being given

Both PTE 2020-02 and 84-24 should be amended so that the requirement to consider and document a rollover recommendation applies only if a rollover recommendation is being made. Although the Department largely glosses over this in the preambles, one requirement of PTE 2020-02 and 84-24 is that a Financial Professional or Independent Producer is *forced* to make a rollover recommendation and document that such a rollover recommendation is in the customer's best interest, *even if the customer is not requesting, and is not receiving, a rollover recommendation*. This is because under section II(b)(5) of PTE 2020-02 and section VII(b)(7) of PTE 84-24, the Financial Professional, Financial Institution, or Independent Producer must consider and document whether a rollover is in the retirement investor's best interest *even if the only recommendation being made is how assets will be invested after the rollover*.

In other words, if a customer comes to an agent, broker, or investment adviser, and states that the customer has decided to roll over assets from a plan or IRA, and is not seeking a recommendation about that, no recommendations about how to invest that rollover can be made until the agent, broker, or investment adviser (a) forces the customer to stop and gather a significant amount of detailed information about the prior plan or IRA, (b) goes through a comparison process, and (c) documents the comparison and provides that documentation to the customer. But this is a customer who is not seeking that recommendation, and certainly does not want to pay the cost of the work that is required. Many customers will simply decide *not* to roll over in this situation, and either decide to take the distribution in cash or go to a financial firm more willing to take the rollover without worrying much about compliance.

More generally, the proposed requirements related to rollover recommendations are divorced from reality. Unless the Independent Producer or Financial Institution advising the retirement investor on how to invest rollover funds also happens to be involved in the administration of the plan from which the funds are being distributed, there is no reasonable expectation that they have the capacity to (1) compare plan fees and expenses to annuity product fees and expenses (especially for fixed and fixed-indexed annuity products that do not have stated fees and expenses), (2) inform the retirement investor whether the employer or other party

pays for some or all administrative costs and expenses, and (3) compare the fiduciary protection, services, and investments available under the plan to the fiduciary protection, services, and investments available under the annuity product. The only way an Independent Producer or Financial Institution unrelated to the plan could obtain this information would be to ask the retirement investor for it or to ask the retirement investor to get it from their employer plan. In this sense, the Proposal seems intended to preclude any retirement investor from ever receiving a recommendation about how to invest their IRA rollover proceeds from any adviser other than a fiduciary of the employer retirement plan.

4. The vague "on request" disclosure should be removed or significantly clarified

Under both PTE 84-24 and 2020-20, the Department has added the following new disclosure requirement:

> the Retirement Investor has the right to obtain specific information regarding costs, fees, and compensation, described in dollar amounts, percentages, formulas, or other means reasonably designed to present full and fair disclosure that is materially accurate in scope, magnitude, and nature, with sufficient detail to permit the Retirement Investor to make an informed judgment about the costs of the transaction and about the significance and severity of the Conflicts of Interest, and that describes how the Retirement Investor can get the information, free of charge.[66]

The new disclosure contains a number of uncertain terms, including the need for the disclosure to be accurate in "scope, magnitude, and nature" and regarding "the significance and severity" of conflicts of interest. This language is so vague as to be open to multiple interpretations, and a financial institution that is honestly trying to comply will simply open itself up to attack by class action plaintiffs—as those are the only people who will request this information.[67]

In the case of annuities, the SEC and state insurance regulators have specific disclosures which must be provided and which are designed with the particular product in mind to facilitate understanding by the customer. Is the prospectus for a variable annuity sufficient for purposes of the Department's new disclosure requirement? It would be surprising if not, and it would be difficult to know what is missing.

We recommend this disclosure be eliminated. It is not necessary for the exemption, which already imposes multiple requirements on costs, fees, and compensation, and it is duplicative of the disclosures that are provided to purchasers of variable and fixed annuities.

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[66] Section VII(b)(5) of proposed PTE 84-24; section II(b)(4) of proposed PTE 2020-02.

[67] The Department provides model language as to how to satisfy the disclosure to inform the customer that this additional information is available, but does not provide any model language about how to satisfy it if requested.

5. The fiduciary acknowledgement should not be modified as proposed

a. Creating a "Catch 22" for firms and professionals

Under PTE 2020-02 as proposed, the Financial Professional and Financial Institution must provide a written acknowledgement that they "are providing fiduciary investment advice to the Retirement Investor and are fiduciaries under Title I, the Code, or both when making an investment recommendation," and must also provide a "written statement of the Best Interest standard of care owed by the Investment Professional and Financial Institution to the Retirement Investor."[68] Proposed PTE 84-24 would impose these same requirements on Independent Producers.[69] These are important and subtle changes from the current fiduciary acknowledgement in PTE 2020-02. The effect is that firms and financial professionals would not be permitted to limit their acknowledgement of fiduciary status to those circumstances under which they are operating as investment advice fiduciaries.

The Department states that the current fiduciary acknowledgment rule in PTE 2020-02 is inadequate because the Department believes that parties will "claim to satisfy it through artful phrasing that does not, in fact, tell the Retirement Investor if the recommendation is made by a fiduciary (for example, by saying they 'may' be fiduciaries or that they are fiduciaries to the extent they meet the definition of fiduciary investment advice under the ERISA or the Code)."[70] But the new proposed requirement suffers from a serious flaw, because it requires a disclosure that implies *every* communication is fiduciary investment advice.

Financial institutions and professionals have many kinds of communications with customers. Some of these communications might be fiduciary in nature, others might not. For example, an insurance agent might suggest that an individual purchase an IRA annuity (generating a commission); this would trigger fiduciary status under the Proposal and require compliance with PTE 2020-02 or 84-24. The customer might call the insurance agent later for information or advice about the product, such as whether it would be appropriate to annuitize or not. The insurance agent does not wish to provide fiduciary investment advice, and certainly is not being compensated to do so. But the disclosure required by the Department clearly implies that the insurance agent has agreed to an ongoing relationship of trust and confidence.

This rule also puts financial professionals and firms in a "Catch-22." The new test places fiduciary status on them even if they do not claim to be a fiduciary, if they make a recommendation that is based on the individual's circumstances. But to avoid a prohibited transaction, they must state they are a fiduciary. And now the Department has trapped them, because under the Department's test, anyone who states that they are a fiduciary is automatically one for all communications that are recommendations, personalized or not.

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[68] Sections II(b)(1) and (2) of proposed PTE 2020-02, 88 Fed. Reg. at 76000.

[69] Sections VII(b)(1) and (2) of proposed PTE 84-24, 88 Fed. Reg. at 76027-28.

[70] 88 Fed. Reg. at 75984.

b. Creating a private right of action

Committee members have noted to us another problem with the proposed amendment to the fiduciary statement requirement: it likely creates a new private right of action that does not otherwise exist. It is true that neither PTE 2020-02 nor 84-24 requires a new contract like the BIC Exemption would have required if the Fifth Circuit had not shot it down, but it is hard to imagine how a state law claim is *not* being created by stating, in writing, that one is acting as a fiduciary and describing the Best Interest standard of care. The Department and ERISA do not possess exclusivity over what it means to be a fiduciary. The word and concept were borrowed from state trust law, where it meant something very specific. And saying you are a "fiduciary" will certainly catch the eye of class action lawyers under state law, and it will not matter that you said it only because the Department forced you to as a condition of relief from an overly-broad rule that applies even though you were not, in fact, a fiduciary. In other words, the proposed amendment to the acknowledgment requirement will surely create a cause of action that otherwise would not exist.

It is not reasonably questionable that the new Proposal is covering people who are not otherwise fiduciaries under federal or state law (if they were, the 5-part test already covers them); but if a professional states that they are a fiduciary and describes the Proposal's standard of care, they certainly must be ready to defend themselves from a claim under state law that would be applied to fiduciaries. Thus, this new rule suffers from the same fatal flaw that the Fifth Circuit noted: the Department is creating a new private right of action with respect to IRAs, even though Congress explicitly decided not to do that when devising Title II of ERISA. This back-door attempt to replicate the BIC Exemption should be abandoned.

6. PTE 84-24 should be available for statutory employees and for any employees who sell unrelated products

Proposed PTE 84-24 would not be available for any agent who sells products of multiple companies but who is also an employee of an insurance company, including a statutory employee under Code section 3121. This is an unnecessary limitation and should be removed. Instead, PTE 84-24 should be available for all sales by statutory employees of any Insurer's annuity products, as well as for any employees of an Insurer to the extent that they sell products of other, unrelated Insurers.

While employees and statutory employees often sell products only of their associated insurance company, that is not universally true. For example, while a full-time life insurance salesman who is a statutory employee under Code section 3121 must *primarily* sell products of one company, there is no requirement that they *only* sell products of one company.[71] And statutory employees often do sell products of other companies, for example if a customer has a need for a product that their primary insurance company does not meet. In that case, the insurance company is not going to be in a position to supervise, under PTE 2020-02, the sale of the other company's product. The same is true if the selling agent is a common law employee of

[71] Treas. Reg. § 31.3121(d)-1.

the Insurer and the sale involves another company's product. So, the sale must be made under PTE 84-24, but the Department has unnecessarily prevented this from occurring.

The Department's stated premise in limiting proposed PTE 82-24 to producers who are not common law or statutory employees is to recognize the fact that Insurers "cannot effectively exercise fiduciary authority over independent insurance agents who do not work for any one insurance company and are not obligated to recommend only one company's annuities."[72] We certainly agree with this premise. The Proposal, however, does not adhere to it.

In that regard, we observe that statutory employees are treated as "employees" of an Insurer only for certain limited purposes under the Code, such as for purposes of FICA taxes and for purposes of applying certain employee benefit provisions of the Code.[73] A statutory employee, by definition, is not a common law employee. If this were not the case, there would be no need for the Code to treat full-time life insurance salesmen as statutory employees; they would be employees already. If an individual is merely a *statutory* employee and not a *common law* employee, it means the Insurer does not have the requisite control over the individual to satisfy the common law definition of employee,[74] and therefore the individual is treated as an independent contractor other than for a few limited purposes prescribed in the Code. Given this lack of control over statutory employees, Insurers should not be expected to "exercise fiduciary authority" over them as PTE 2020-02 requires. The Department should not be able to arbitrarily exclude statutory employees from using PTE 84-24 because they receive health and welfare benefits from one of the insurance companies for which they sell annuities. Rather, PTE 84-24 should be available with respect to these individuals.

Similarly, in situations where a common law employee of one Insurer occasionally sells products of an unrelated Insurer, the employer Insurer should not be expected to review the sale of the unrelated Insurer's products. PTE 84-24 should be available in this situation, with the unrelated Insurer having the supervisory responsibilities set forth therein for the sale of that Insurer's products.

7. The Department must reevaluate its views on the kinds of incentive compensation that are prohibited by PTE 2020-02 and 84-24

Under PTE 2020-02 and 84-24 as proposed, the insurance company or other financial institution must have compensation policies that do not create an incentive for the Financial Professional or Independent Producer to place its interests, or those of the insurer, ahead of the interests of the Retirement Investor. The Department is also proposing to add to the text of the rule additional language that requires the elimination of any "quotas, appraisals, performance or personnel actions, bonuses, contests, special awards, differential compensation, or other similar actions or incentives that are intended, or that a reasonable person would conclude are likely, to

[72] 88 Fed. Reg. at 76005.

[73] *See*, *e.g.*, Code section 3121(d)(3) (FICA); Code section 7701(a)(20) (employee benefits).

[74] *See*, *e.g.*, Hathaway v. Comm'r, T.C. Memo. 1996-389.

result in recommendations that are not in the Retirement Investor's Best Interest."[75] In the preamble, the Department explains this requirement in a way that is breathtaking in its scope:

> [A]n Insurer could not offer incentive vacations, trips, or even educational conferences, if qualification for the vacation, trip or conference is based on sales volume or satisfaction of sales quotas. The Best Interest standard discussed above and defined in proposed Section X(b) clearly prohibits these types of incentives on the grounds they create undue conflicts of interest. Moreover, the Department believes that educational opportunities should be offered equally to all agents and not connected to sales volume, because training is a necessary component of providing Best Interest advice.[76]

These statements seem to suggest that an insurer cannot offer any educational conferences unless *every single person* who sold, or might sell, one of the insurer's products is included. If that is the intent, it is irrational and unworkable. More generally, we are very concerned that the theory underlying the statements quoted above, *i.e.*, that some forms of performance-based compensation can be *per se* banned, could call into question other forms of compensation that simply must be permitted for the insurance industry to function, such as bonuses and commissions, both of which necessarily increase with job performance. The Proposal cannot prohibit those who sell more from getting paid more.

There is no such limitation under SEC, FINRA, or state insurance rules, nor would such a restriction make any sense. In the past, the Department has focused on financial incentives that create specific improper motivations to sell a product, for example a sales contest which provides a bonus for someone who sells 10 of a particular type of annuity in a month.[77] A reasonable person might believe such an incentive is likely to result in recommendations that are not in the customer's best interest. But if the Department believes that *any* reward for success is going to create such incentives, then there is no limit to this theory. Even a commission would be prohibited.

The truth is that the most successful agents, brokers, and investment advisers got that way by delivering good recommendations, education, and advice. It is simply unrealistic to require financial institutions to treat the most successful and the least successful financial professionals equally.

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[75] Section VII(c)(2) of proposed PTE 84-24, 88 Fed. Reg. at 76028.

[76] 88 Fed. Reg. at 76011.

[77] See the further discussion of this point on page 31, *supra*.

8. PTE 2020-02 should be clarified to ensure that it covers annuity sales

In the short period that Committee members have had to evaluate the Proposal, we have discovered some drafting errors and unintended consequences. We mentioned one earlier—the definition of "Affiliate" includes employees and even unrelated parties for purposes of the Eligibility rule. We note an additional unintended consequence here that is even more significant. Given more time, we almost certainly would uncover other similar errors.

As described earlier, the Department intends that, with one narrow exception, sales of annuities must be made under PTE 2020-02. But it is not clear that PTE 2020-02 actually covers the transactions that need relief. PTE 2020-02 covers only two kinds of transactions: the receipt of "reasonable compensation" in connection with investment advice, and a "Principal Transaction."

The term "Principal Transaction" is defined to include only a limited set of securities, which does not include annuities or other life insurance products. And the sale of an annuity might involve a prohibited transaction other than the "reasonable compensation" that is received by the person who has made the recommendation. For example, PTE 84-24 has covered, for many years "[t]he purchase, with plan assets, of an insurance or annuity contract from an insurance company." This is necessary because the insurance company is not typically understood to be receiving "compensation" in connection with the sale of its products. Often the insurance company's profit comes from the spread between the guarantees in the contract and the amount the insurance company can earn from the investments it makes. These are not, for example, required to be disclosed under the 408(b)(2) disclosure as "compensation."

We believe that the Department intended PTE 2020-02 to cover all of the prohibited transactions that might result from, for example, an employee of an insurance company providing a recommendation to a customer to purchase a propriety product, but we ask the Department to confirm this.

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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 or at the email addresses listed below.

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Attachment (List of Committee Members)

The COMMITTEE of ANNUITY INSURERS

Allianz Life Insurance Company, Minneapolis, MN
Ameriprise Financial, Minneapolis, MN
Athene USA, Des Moines, IA
AuguStar Life Insurance Company, Cincinnati, OH
Brighthouse Financial, Inc., Charlotte, NC
Corebridge Financial, Houston, TX
Equitable, New York, NY
Fidelity & Guaranty Life Insurance Company, Des Moines, Iowa
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Global Atlantic Financial Group, Southborough, MA
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New York Life Insurance Company, New York, NY
Northwestern Mutual Life Insurance Company, Milwaukee, WI
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TruStage, Madison, WI
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 approximately 80% of the annuity business in the United States.