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July 21, 2017

Filed Electronically

Office of Exemption Determinations
Employee Benefits Security Administration
Attention: D-11933
U.S. Department of Labor
200 Constitution Avenue N.W., Suite 400
Washington, DC 20210

Re: RIN 1210-AB82; Request for Information Regarding the Fiduciary Rule and
Prohibited Transaction Exemptions; Delay of January 1, 2018 Applicability Date

Dear Sir or Madam:

The Investment Company Institute¹ is writing to urge the Department of Labor (the “Department”) to delay the January 1, 2018 applicability date² associated with its fiduciary rulemaking.³

¹ The Investment Company Institute (ICI) is the leading association representing regulated funds globally, including mutual funds, exchange-traded funds (ETFs), closed-end funds, and unit investment trusts (UITs) in the United States, and similar funds offered to investors in jurisdictions worldwide. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. ICI’s members manage total assets of US\$19.9 trillion in the United States, serving more than 95 million US shareholders, and US\$5.6 trillion in assets in other jurisdictions. ICI carries out its international work through ICI Global, with offices in London, Hong Kong, and Washington, DC.

² We are writing in response to the Department’s request for information (“RFI”), which was published at 82 Fed. Reg. 31278 (July 6, 2017). ICI will submit a separate letter responding to the RFI questions other than the delay of the January 1, 2018 compliance date.

³ The Department issued a final regulation defining who is a fiduciary of an employee benefit plan under the Employee Retirement Income Security Act of 1974 (“ERISA”) or an individual retirement account (IRA) under section 4975 of the Internal Revenue Code (“Code”), as a result of giving investment advice to a plan or its participants or beneficiaries, or an IRA or IRA owner. 81 Fed. Reg. 20946 (April 8, 2016). The rulemaking also includes two new related prohibited transaction exemptions and amendments to a number of existing prohibited transaction exemptions, described in footnotes 4 and 5, *infra*.

All conditions of the Best Interest Contract Exemption (“BICE”)⁴ and other related exemptions associated with the fiduciary rulemaking⁵ currently are scheduled to become applicable on January 1, 2018. This will occur despite the Department’s clear indications that it will modify the fiduciary rulemaking. To provide needed certainty, reduce harm to investors, and limit unnecessary “sunk” costs associated with implementing requirements that the Department ultimately eliminates or modifies, the Department should immediately—by August 15, 2017—issue an interim final rule delaying the January 1, 2018 applicability date to January 1, 2019. In conjunction with this, the Department also should announce its intent to finalize amendments to the rulemaking prior to the end of the one-year delay period. We further recommend that the applicability date of any modified rule and exemptions become effective no sooner than one year after finalization—approximately January 1, 2020.

We set forth below our responses to the RFI’s questions relating to the potential delay. Following an introduction and summary of key points in Section I, the letter in Section II discusses the multiple, overlapping reexaminations of the fiduciary rulemaking that portend significant changes. In Section III, we discuss why the benefits of delaying the January 1, 2018 applicability date outweigh any illusory costs, and explain that the delay is necessary to decelerate market disruptions that are harming retirement savers. Finally, Section IV discusses why the delay should be immediate and correspond to a proposed time line of rulemaking modifying the fiduciary rule and exemptions. It also explains why the Department should not have other conditions of the exemptions go into effect during any delay.

I. Introduction and Summary of Key Points

In April, the Department announced a phased implementation for the BICE and other related exemptions.⁶ During the transition period between June 9, 2017 and January 1, 2018 (the “Transition Period”), fiduciary advisers can use the BICE and related exemptions as long as they meet the Impartial Conduct Standards described in the exemptions. The other conditions of those exemptions—including the widely criticized contractual private right of action and warranties—are not applicable prior to January 1, 2018. The Department now seeks comments on whether to delay the January 1, 2018 applicability date while it evaluates the rule generally and the responses to issues identified in the RFI.

⁴ The BICE, published at 81 Fed. Reg. 21002 (April 8, 2016), was issued at the same time as the final rule with the stated intent—subject to its many conditions—of permitting the payment of commissions and other compensation that would otherwise be prohibited under ERISA and the Internal Revenue Code.

⁵ Related exemptions include the Principal Transaction Exemption, published at 81 Fed. Reg. 21089 (April 8 2016), and amendments to prohibited transaction exemption 84-24 (PTE 84-24), which were issued at the same time as the final rule.

⁶ 82 Fed. Reg. 16902 (April 7, 2017).

ICI has established research capabilities⁷ and therefore is well-positioned to evaluate the effects of a delay in the January 1, 2018 applicability date. As discussed in detail below, there is ample justification for such a delay. Simply put, the rule substantially harms investors and imposes undue costs on service providers. These negative implications far outweigh any negligible benefit from not delaying. Indeed, the Department in effect already concluded that delaying the January 1, 2018 applicability date will not negatively affect investors. Delaying the January 1, 2018 applicability date creates benefits—not losses—for investors, and is necessary to allow for the Department to thoughtfully and appropriately review the rulemaking.

The key points supporting this conclusion are as follows:

- **The Department undoubtedly will propose modifications to the fiduciary rule and related exemptions.** The President’s directive, Labor Secretary Acosta’s and SEC Chairman Clayton’s express efforts to coordinate fiduciary rulemaking, and recent Department acknowledgements that it exceeded its authority by issuing the BICE’s prohibition on contractual class action waivers all indicate that the Department will modify the fiduciary rulemaking.⁸ Moreover, the Department’s queries in the RFI itself about potential changes to the rule and BICE, potential new exemptions or streamlined exemptions, show that potential modifications are already being considered. A delay is needed urgently to allow for the Department to reexamine the final rulemaking and prepare an updated economic and legal analysis as directed by the President. A delay also will permit the Department to benefit from the SEC’s input in that review. Failing to delay the January 1, 2018 applicability date while this review is ongoing will only perpetuate the harms the rulemaking has caused.
- **The benefits of delaying the January 1, 2018 applicability date outweigh the speculative and illusory costs of such a delay.** Our analysis demonstrates that the tangible benefits of delaying the January 1, 2018 applicability date, both for retirement savers and for providers of retirement services, far outweigh any speculative costs of delay. As widely reported, intermediaries have announced a variety of changes to service offerings, including no longer offering mutual funds in brokerage IRA accounts and raising account minimums or discontinuing advisory services and commission-based arrangements for lower balance

⁷ The Institute serves as a source for statistical data on the investment company industry and conducts public policy research on fund industry trends, shareholder characteristics, the industry’s role in U.S. and international financial markets, and the retirement market. For example, the Institute publishes reports focusing on the overall U.S. retirement market, fees and expenses, and the behavior of defined contribution plan participants and IRA investors. In its research on mutual fund investors, IRA owners, and 401(k) plan participants, the Institute conducts periodic household surveys that connect directly with investors.

⁸ See text accompanying footnotes 18 through 24, *infra*.

accounts.⁹ Our estimates, as detailed in comment letters to the Department, indicate that investors could lose \$109 billion over 10 years due to the effects of these changes. This would amount to \$780 million *per month* in losses to investors.¹⁰ For this reason, the impact calculation weighs heavily in favor of delaying implementation so that the Department can further study the data and more fully consider how the fiduciary rulemaking will affect retirement savers' access to guidance, products, and services—particularly lower- and middle-income savers with smaller account balances.

- **The Department already effectively concluded that delaying the January 1, 2018 applicability date will not negatively affect investors.** The fiduciary rule and Impartial Conduct Standards currently are applicable, and the Department acknowledged their effectiveness in ensuring investor protections. Indeed, it noted in its prior rulemaking concerning the delay of the April 10, 2017 applicability date that “[i]f advisers fully adhere to these requirements [the Impartial Conduct Standards], affected investors generally will receive the full gains due to the fiduciary rulemaking.”¹¹ The Department also acknowledged its expectation that advisers will substantially comply with the Impartial Conduct Standards.¹²
- **Speculation that some lapses in compliance may result is not sufficient to draw conclusions about potential investor harm from a delay.** The Department speculates that some compliance lapses could possibly occur during the Transition Period. Despite that, any losses for retirement investors from the delay due to compliance lapses are not only highly speculative, but illusory. The Department used its analysis in the 2016 regulatory impact analysis (“RIA”) to support its claims of potential investor losses if the rule does not go into effect, and thus potential harm to investors (in the form of “foregone gains”).¹³ That analysis does not account for the fact that the Impartial Conduct Standards are now applicable. But, even if it had, the 2016 RIA is fundamentally flawed and woefully incomplete. In fact, because the 2016 RIA’s benefit calculation is not supported by the very studies on which it is based,

⁹ See “A Complete List of Brokers and Their Approach to ‘The Fiduciary Rule’”, Wall Street Journal, February 6, 2017, available at <https://www.wsj.com/articles/a-complete-list-of-brokers-and-their-approach-to-the-fiduciary-rule-1486413491>. See also letter from Brian Reid and David Blass, to Office of Regulations and Interpretations, Employee Benefits Security Administration, US Department of Labor (April 17, 2017), available at https://www.ici.org/pdf/17_ici_dol_fiduciary_reexamination_ltr.pdf (“ICI’s April 17 Letter”), footnotes 50 through 52.

¹⁰ This is calculated as the monthly payment required over a 10-year period at a discount rate of 3 percent to achieve a future value of \$109 billion at the end of 10 years.

¹¹ See footnotes 25 through 29 and accompanying text, *infra*.

¹² See footnote 27, *infra*.

¹³ See 82 Fed. Reg. 16902, at 16907-8.

estimates based on the 2016 RIA also are unreliable and of little relevance to assessing the potential impact of the delay of the January 1, 2018 applicability date on retirement investors. In fact, the Institute has shown that, even if one accepts the 2016 RIA's methodology, its misapplication of academic research means that the 2016 RIA overstated the estimated benefits of the final rule by 15 to 50 times.¹⁴ The Administrative Procedure Act ("APA") does not "lock" the Department into its flawed impact analysis, but, rather, obligates it to depart from it.

- **The lack of investor harm from a delay of the applicability date stands in stark contrast to the burdens of ongoing implementation costs.** No evidence exists for concluding that investors would be harmed by a delay of the January 1, 2018 applicability date. What is certain, however, is that service providers are spending very significant amounts preparing for January 1, 2018. The Department's own estimates of the fiduciary rule's implementation costs show that implementing the rule will cost \$5 billion in the first year of the final rule's application.¹⁵ Although a portion of those costs will necessarily be incurred in connection with efforts to comply with the fiduciary rule and Impartial Contract Standards, advice providers are incurring the vast majority of the costs in implementing the more cumbersome and technically complicated aspects of the BICE conditions. These include developing the policies and procedures to comply with the contractual warranties and technologically challenging website requirements. Thus, any speculative and illusory foregone gains do not outweigh providers' real first-year implementation costs, which are far in excess of \$5 billion.

Moreover, the Department's implementation cost estimate does not include any estimate for the amount that asset providers, including mutual funds, will incur to change product offerings to ease intermediary compliance burdens.¹⁶ Such costs will be significant and unrecoverable. For example, as we previously informed the Department, sunk costs relating to only one segment of product changes—the creation of T-shares—could reach \$94 million during the first year.¹⁷

¹⁴ While the Department disputes the significance of this analysis in the 2016 RIA, that criteria is based on a clear misunderstanding and misapplication of the Institute's arguments. *See* text accompanying footnotes 36 through 38, *infra*.

¹⁵ *See* U.S. Department of Labor, Employee Benefits Security Administration, Regulating Advice Markets, Definition of the Term "Fiduciary" Conflicts of Interest—Retirement Investment Advice Regulatory Impact Analysis for Final Rule and Exemptions (April 2016), ("2016 RIA"), available at <https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/completed-rulemaking/1210-AB32-2/conflict-of-interest-ria.pdf>, at p. 10. *See also* 82 Fed. Reg. 12319 at 12320 (March 2, 2017).

¹⁶ *See* 2016 RIA at p. 244.

¹⁷ *See* ICI's April 17 Letter.

II. The Department Must Propose Modifications to the Fiduciary Rule and Related Exemptions, Following its Multiple, Overlapping Reexaminations of the Rule.

The Department is engaged in multiple, overlapping reexaminations of its rulemaking. First, the Department currently is reviewing the rule in response to the President's directive to determine whether significant changes are needed to the rulemaking.¹⁸ It is clear that the Department must issue a proposal to revise or rescind the rulemaking to honor the directive in the President's Memorandum.¹⁹

Second, the Department is working with the SEC to coordinate efforts on fiduciary standards of conduct. Secretary of Labor Acosta²⁰ and SEC Chairman Clayton²¹ both recently publicly commented that they intend to work together, as a coordinated effort, to make the fiduciary rule a more consistent and unified rulemaking. This coordinated effort will take time to achieve—clearly more time is needed than the five and a half months that remain until January 1, 2018. SEC Chairman Clayton already is gathering input that would be helpful in creating a harmonized standard of care.²²

¹⁸ 82 Fed. Reg. 31279, at 31279.

¹⁹ See White House memorandum to the Secretary of Labor, dated February 3, 2017 and published at 82 Fed. Reg. 9675 (February 7, 2017), available at <https://www.gpo.gov/fdsys/pkg/FR-2017-02-07/pdf/2017-02656.pdf>. As described in detail in ICI's April 17 Letter, the rulemaking runs afoul of *all* the criteria in the President's Memorandum dictating the issuance of a proposal to rescind or revise the rule, and is clearly inconsistent with the Administration's priorities of ensuring that Americans have access to retirement information and financial advice and empowering Americans to make their own financial decisions.

²⁰ Secretary Acosta stressed the Department's need for SEC's expertise in this area in both his May 22, 2017 op-ed in the Wall Street Journal and in the June 27, 2017 hearing of the Senate Subcommittee on Labor, Health and Human Services, Education, and Related Agencies ("Previously the SEC did not work jointly with the Department of Labor; as I indicated quite publicly, I think that the SEC has important expertise and that they need to be part of the conversation. And I asked the chairman of the SEC if the SEC would be willing to work with us. The chairman indicated his willingness to do so. It is my hope as the SEC also receives a full complement of commissioners, that the SEC will continue to work with the Department of Labor on this issue.").

²¹ At the June 27, 2017 hearing of the Senate Subcommittee on Financial Services and General Government, Chairman Clayton said "Look, it's not separate; what's happening at the Department of Labor is going to affect the markets we [the SEC] regulate and vice versa. It's my intent as chairman to try and move forward and effectively deal with that, in a way that is coordinated so that our Main Street investors have access to investment advice and access to investment products. I don't want to see any of these actions that we would take reduce the access to investment advice or the access to investment products, at the same time very much fulfilling our investor protection mission." "I am confident that we're going to have cooperation in this regard. It's a very complicated issue. I don't think it would have been here this long if it weren't complex, but I'm confident that we're going to cooperate." <http://www.thinkadvisor.com/2017/06/27/sec-moving-forward-on-fiduciary-rule-clayton-says>.

²² Chairman Jay Clayton, Public Comments from Retail Investors and Other Interested Parties on Standards of Conduct for Investment Advisers and Broker-Dealers (June 1, 2017), available at <https://www.sec.gov/news/public-statement/statement-chairman-clayton-2017-05-31>.

Likewise, the Department already is seeking input regarding how an updated SEC standard of conduct could fit with the Department's rulemaking (*see* RFI question 11).

We applaud Secretary Acosta's efforts to coordinate the Department's fiduciary rulemaking with the SEC. Such a coordinated approach should allow the Department to abandon creating a private right of action and relying on the plaintiffs' bar as a means of enforcement. The Department used this bootstrap approach solely because it did not have enforcement authority over IRAs. Promoting litigation as an enforcement strategy brings significant risk, expense and uncertainty. Secretary Acosta appears to recognize that a much better approach is to work with the SEC and other agencies with enforcement authority over the various market segments that serve the retirement industry to develop a consistent enforceable best interest standard.

A coordinated SEC/DOL approach would be more consistent with other Administrative directives²³ and would reflect the reality that individuals who seek financial guidance often have both retirement accounts and retail accounts. It would permit these individuals to receive guidance that reflects consistent and compatible regulatory requirements. To permit adequate SEC/DOL coordination, a delay of the January 1, 2018 compliance date is necessary.

Finally, the recently issued RFI identifies a number of possible changes to the BICE, a number of potential new exemptions or streamlined exemptions, and questions that imply likely changes to the rule itself. The fact that the Department has requested this input through the RFI arguably suggests that it agrees that changes to the rulemaking are needed. In fact, in its recently filed brief in the 5th Circuit relating to litigation over the fiduciary rule, the Department now acknowledges that one provision in the BICE (the prohibition on contract terms that waive or qualify an investor's right to bring or participate in a class action) should be invalidated because it violates existing law (the Federal Arbitration Act).²⁴

In light of these multiple reexamination tracks and recognizing the importance of coordination with the SEC, it is clear that the Department will make at least some changes to the fiduciary rulemaking. Given that the Department has not yet decided the scope of the changes to the fiduciary rule and BICE nor whether any one of the individual conditions of the BICE will ultimately remain intact, delaying the January 1, 2018 applicability date is critical.

²³ *See* Presidential Executive Order on Enforcing the Regulatory Reform Agenda, issued on February 24, 2017 (stating that "[i]t is the policy of the United States to alleviate unnecessary regulatory burdens placed on the American people" and encourages Agencies to eliminate regulations that "create a serious inconsistency or otherwise interfere with regulatory reform initiatives and policies"), available at <https://www.whitehouse.gov/the-press-office/2017/02/24/presidential-executive-order-enforcing-regulatory-reform-agenda>; and Presidential Executive Order on Reducing Regulation and Controlling Regulatory Costs, issued on January 30, 2017 (directing agencies to identify at least two existing regulations to be repealed for every new regulation proposed), available at <https://www.whitehouse.gov/the-press-office/2017/01/30/presidential-executive-order-reducing-regulation-and-controlling>.

²⁴ *See* Chamber of Commerce v. U.S. Department of Labor, 5th Cir., No. 17-10238, brief for appellees at pp. 59-60 (7/3/17).

III. The Benefits of Delaying the January 1, 2018 Compliance Date Outweigh the Speculative and Illusory Costs of Such a Delay.

The Department poses questions regarding the costs and benefits associated with a delay of the January 1, 2018 applicability date, including whether a delay carries any potential risks or would be advantageous to advisers or investors. It is clear that the benefits of delaying the January 1, 2018 applicability date outweigh any hypothetical and illusory costs.

As described below, the current application of the fiduciary rule and Impartial Conduct Standards negate any argument—however specious—of potential risk to investors. Moreover, the Department’s previous claims of potential investor losses if the rule does not go into effect are not relevant here and are based on flawed analysis. Significantly, a delay would result in substantial cost-savings for financial institutions by allowing them to avoid the significant and burdensome costs of implementation that will likely ultimately prove unnecessary. More time also will allow for a more efficient transition because it will allow the market to develop new products and services in response to the rulemaking. In contrast, the abbreviated timeline required by the January 1, 2018 applicability date will simply accelerate the harm to small investors—depriving them of access to investment advice in many cases and pricing them out of the advice market in others.

A. The Department already concluded that delaying the January 1, 2018 compliance date will not negatively affect investors.

No evidence exists that deferring the January 1, 2018 compliance date will have any negative impact on investors. To the contrary, the Department recognizes that delaying the January 1, 2018 compliance date would have a negligible cost to investors. This is because the gains to investors that the Department asserts will result from the rule come almost entirely from the expanded fiduciary definition and the imposition of the Impartial Conduct Standards. As the Department explains, the current bifurcated approach, without imposing the additional BICE requirements, does not give “short shrift to the competing interest of retirement investors in receiving advice that adheres to basic fiduciary norms. Because the Impartial Conduct Standards apply [as of June 9, 2017], retirement investors will benefit from higher advice standards, while the Department takes the additional time necessary to perform the examination required by the President’s Memorandum.”²⁵

²⁵ 82 Fed. Reg. 16902, at 16906 (April 7, 2017).

While the Department suggests that it is possible that “some lapses in compliance may result in investor losses,”²⁶ it also clarifies that such a possibility is clearly negligible and unsubstantiated.²⁷ The Department previously reasoned that a delay in the original April 10, 2017 applicability date could result in investors receiving conflicted advice resulting in foregone gains.²⁸ However, that possibility was expressed prior to the fiduciary rule and Impartial Conduct Standards becoming applicable. Additionally, although both the Department and the Internal Revenue Service have issued enforcement relief through temporary enforcement policies, that relief is available only for those “working diligently and in good faith to comply with the fiduciary duty rule and exemptions.”²⁹

Because the imposition of additional BICE conditions will result in additional and likely unnecessary costs to the industry, with little to no additional benefits to retirement investors, the Department must further delay all of the conditions of the BICE.

Not only would a delay *not harm* retirement investors, but the risks to investors if the January 1, 2018 compliance date is *not delayed* are substantial. As described in ICI’s April 17 Letter, the rule already is negatively affecting many investors. Intermediaries are orphaning accounts and intermediaries are changing business models in a manner that is causing some investors to either pay more for advice or lose access to advice altogether.³⁰ The final rule also threatens to severely reduce the commonplace exchanges of information—currently provided at no cost to millions of retirement savers through call

²⁶ The Department states: “If advisers fully adhere to these requirements [the Impartial Conduct Standards], affected investors will generally receive the full gains due to the fiduciary rulemaking. However, the temporary absence (until January 1, 2018) of exemption conditions intended to support and provide accountability mechanisms for such adherence (e.g., conditions requiring advisers to provide a written acknowledgement of their fiduciary status and adherence to the Impartial Conduct Standards) obliges the Department to consider the possibility that some lapses in compliance may result in investor losses.” 82 Fed. Reg. 16902, at 16909.

²⁷ The Department explains: “[T]he Department expects that advisers’ compliance with the Impartial Conduct Standards during the [Transition Period] will be substantial, even if there is some reduction in compliance relative to the baseline.” 82 Fed. Reg. 16902, at 16910.

²⁸ In its determination of whether to further delay the April 10, 2017 applicability date, the Department concluded that a 60-day delay in the applicability date and the accompanying delayed “commencement of the potential investor gains estimated in the RIA published on April 8, 2016, and referenced above, could lead to a reduction in those estimated gains of \$147 million in the first year and \$890 million over 10 years using a three percent discount rate.” 82 Fed. Reg. 12319, at 12320 (March 2, 2017).

²⁹ Department of Labor Field Assistance Bulletin No. 2017-02, issued on May 22, 2017; IRS Announcement 2017-4.

³⁰ See pages 11 through 12 of ICI’s April 17 Letter for a discussion of orphaned accounts. See also pages 31 through 34 of ICI’s April 17 Letter for a description of the dislocations that will adversely affect retirement investors. As we explain, investors who no longer have access to advice are likely to experience lower returns because of poor asset allocation and market timing, or because they incur tax penalties by taking early withdrawals. We calculate that the 10-year cost of lower returns caused by such errors would be \$62 billion. Indeed, the Institute estimates that retirement investors’ returns could be reduced, conservatively, by \$10.9 billion a year—or \$109 billion over 10 years—as a result of the additional fees and lost returns they will incur.

centers, walk-in centers, and websites. The implementation of the fiduciary rule already is limiting investment education to retirement savers, due to the risk of inadvertently triggering fiduciary status.³¹

The Department's announcement of the phased implementation approach, including the Conflict of Interest FAQs regarding the Transition Period, slowed/postponed some of this intermediary activity.³² Consequently, investors have not yet faced the full impact of the rule. If the Department does not delay the January 1, 2018 compliance date, we expect to see additional orphaned accounts and business model changes that will further reduce investors' access to advice.³³

B. The Department cannot properly rely upon its flawed prior claims of investor harm.

The Department's prior speculative estimate of foregone gains does not weigh against delay. In its recent consideration of whether to postpone the applicability dates associated with the fiduciary rulemaking, the Department put significant weight on its estimation of forgone gains described in its 2016 RIA and turned a blind eye to arguments showing that the Department's misapplication of the academic studies on which it relied led it to overstate by a factor of 15 to 50 times any potential benefits of the rule.³⁴ The flaws in the Department's RIA are not based on mere disagreements. Rather, they reflect clear errors in the application of a key coefficient crucial to its findings. In effect, the Department simply got the math wrong. The APA does not handcuff the Department from acknowledging its error and adjusting its analysis accordingly.

³¹ Even the most basic information could trigger ERISA fiduciary status and prohibited transactions.

³² Under the phased implementation, the BICE is available as long as the Impartial Conduct Standards are met. In the Transition period FAQs, issued May 2017, the Department clarified that an adviser will be able to use the BICE during the Transition Period even if compensation structures that create conflicts of interest persist. Significantly, the FAQs clarify, among other things, that the policies and procedures requirement that commissions vary only based on "neutral factors" is not required during the Transition Period.

³³ An informal survey of our members supports this prediction. As described in our prior comment letters, many accounts already have been orphaned. However, as intermediaries gain clarity on their business models in light of the current (or modified) final rule, our members expect orphaned accounts to increase. This expectation is based on the fact that the vast majority of intermediaries with retail accounts where account orphaning in response to the final rule is possible have not yet contacted our members. Members also indicated that some intermediaries are orphaning accounts in batches, which means that mutual funds cannot assume an intermediary has completed its orphaned account activity with just one contact. Given that changes to the final rule could alter intermediary business decisions that could, in turn, reduce or eliminate the number of orphaned investors, a delay in the January 1, 2018 compliance date is likely to prevent some intermediaries from orphaning a number of accounts.

³⁴ See pages 18 through 28 of ICI's April 17 Letter. The Department's impact analysis supporting the rule was flawed, exaggerating potential harm to investors if the rule was not made effective. ICI has repeatedly provided clear explanation showing that there simply is no basis for the Department's conclusion. These speculative benefits described by the Department will not offset the harm to investors caused by the rule.

1. The Department's prior findings are based on bad math.

The Department's 2015 and 2016 RIAs lean heavily on results from an academic study by Christoffersen, Evans, and Musto (2013) ("CEM"). Using a key coefficient in the CEM study, the 2015 and 2016 RIAs concluded that the benefits of the fiduciary rule could reach approximately \$33 billion to \$36 billion over a 10-year period. As we have previously indicated, however, the Department's estimated benefits calculation (*i.e.*, \$33 billion to \$36 billion over a 10-year period) embodies a mathematical error, which causes the Department's benefits estimates to be overstated by about 15 to 50 times.

The Department's mistake is best illustrated by a simple analogy. A researcher studies the relationship between life expectancy and excess weight. Controlling for height, age, and gender, the researcher plots predicted weights for the adult population. The researcher finds that for every 10 pounds of "excess" weight—weight above the predicted normal weight given height, age, and gender—an individual's life expectancy falls by 0.5 years. Thus, if the predicted normal weight for a 50-year-old man who is 6 feet, 3 inches tall is 195 pounds, a 50-year-old man of that height who weighs 205 pounds could lose an estimated six months (0.5 year) of life due to "excess" weight.

Now, the researcher wants to show how much a government program encouraging people to lose "excess" weight could expect to add to individuals' lives. To form this estimate, the researcher multiplies the man's full weight (205 pounds) times the variable for the impact of "excess" weight on life expectancy (0.5 year per 10 pounds). This is inappropriate because the life-expectancy variable was calculated as the impact of "excess" weight—not total weight. The researcher erroneously concludes that the government program could add 10.25 years (*i.e.*, $(0.5/10) \times 205$) to the individual's life, overstating the true effect (0.5 years) by more than 20 times. This error, which is eminently clear, is entirely analogous to how the 2015 and 2016 RIAs misapplied the CEM results, leading the RIAs to massively overstate any potential benefits from the rule. Had the Department corrected for this mistake, it would have concluded that the net benefits from the rule are approximately zero.

What is new is that in the 2016 RIA the Department indicated that it had not corrected this mathematical error,³⁵ and in fact, implicitly admitted that it did not understand its mistake.³⁶

³⁵ See 2016 RIA at 149-150 stating that "Comments on the 2015 NPRM Regulatory Impact Analysis suggest that DOL inappropriately interpreted results presented in some of the academic papers referenced in this section and other sections of the Regulatory Impact Analysis. Of course, data can be interpreted in a multitude of ways, and reasonable minds can disagree. However, DOL continues to strongly believe that readings contained in the 2015 NPRM Regulatory Impact Analysis and carried over into the current Regulatory Impact Analysis are the most appropriate interpretations of the studies given the available data."

³⁶ The 2016 RIA responded briefly to ICI's analysis of this math error (see 2016 RIA at 348). In footnote 641 on page 348, the Department states "For additional discussion of ICI's critique of the Department's use of CEM results, see Padmanabhan, Panis and Tardiff (2016)," a consultant study commissioned by the Department. See Padmanabhan, Karthik, Constantijn Panis, and Timothy J. Tardiff. "Review of Comments on the Department of Labor's Conflict of

2. The APA does not lock the Department into a flawed impact analysis.

In considering whether to extend the January 1, 2018 applicability date, the Department is not obligated under the APA to adhere to, or accept as a given, the factual findings and cost-benefit conclusions that accompanied the final rule as adopted in April 2016. Indeed, not only is the Department permitted to depart from its earlier analysis for appropriate reasons, it is *obligated* to do so when new evidence or further analysis shows those conclusions to be wrong. Persistence in what is shown to be erroneous is neither a virtue, nor legally required—it is prohibited.³⁷

It is well understood in this regard that the APA “makes no distinction...between initial agency action and subsequent agency action undoing or revising that action.”³⁸ Thus, when an agency changes course, it need only “adequately explain ... the reasons for a reversal of policy.”³⁹ While an agency cannot “ignore ... or countermand ... its earlier factual findings without reasoned explanation for doing so,” by the same token, those earlier findings are not forever binding, and may be revisited and revised with an appropriate “reasoned explanation.”⁴⁰ Accordingly, it is sufficient under the APA if the Department identifies weaknesses in the factual analysis underlying the rule and details those weaknesses and its reasons for a new assessment.

Interest Proposed Rule,” Advanced Analytical Consulting Group, 2016. This consultant study on page 35, footnote 39 spells out precisely this mathematical error in mathematical symbols. That footnote argues that the benefits calculation the Department used, based on the CEM study, measures changes in fund returns owing to the rule as $\Delta return = \beta \Delta Load$, where β is taken from the CEM study. As ICI’s April 14, 2017 comment letter to the Department proved, this formula is incorrect. The correct formula, is $\Delta return = \beta \Delta Load \times .071$, or more precisely still $\Delta return = \beta \Delta Load \times .071 \times 0.5$. This mistake causes the Department to overstate its benefits calculations by 14 to 28 times. When ICI applied the correct formula to actual data for 2013, we found that the Department had likely overstated its benefits calculations by approximately 15 to 50 times.

³⁷ “An initial agency interpretation is not instantly carved in stone. On the contrary, the agency . . . must consider varying interpretations and the wisdom of its policy on a continuing basis.” *Nat’l Cable & Telecomms. Ass’n v. Brand X Internet Servs.*, 545 U.S. 967, 981 (2005) (citations omitted). An agency is therefore always free to reconsider “the wisdom of its policy” and to respond “to changed factual circumstances, or a change in administrations.” *Id.* An agency, “faced with new developments or in light of reconsideration of the relevant facts and its mandate, may alter its past interpretation and overturn past administrative rulings and practice.” *Am. Trucking Associations v. Atchison, T. & S. F. Ry. Co.*, 387 U.S. 397, 416 (1967). This is “especially” true when an agency’s “prior determination is based on error.” *Phoenix Hydro Corp. v. FERC*, 775 F.2d 1187, 1191 (D.C. Cir. 1985); see *Clark-Cowlitz Joint Operating Agency v. FERC*, 826 F.2d 1074, 1083 (D.C. Cir. 1987) (en banc) (allowing FERC to change its policy and apply it retroactively when it concluded that “its prior interpretation thwarted Congressional intent” and was “erroneous,” because an “agency’s discretion to change its course is broader when [the] agency believes its prior course is contrary to statutory design”).

³⁸ *FCC v. Fox Television Stations Inc.*, 556 U.S. 502, 514–15 (2009).

³⁹ *Brand X*, 545 U.S. at 981.

⁴⁰ *Fox Television*, 556 U.S. at 537.

Moreover, when an agency is presented with record evidence demonstrating that its prior analysis and conclusions were wrong in relevant part, it is *obligated* to reconsider that earlier work and *prohibited* from relying on it.

Thus, as the Department considers whether to delay the January 1, 2018 applicability date, it cannot ignore ICI's detailed demonstration of flaws in the Department's prior analysis. This is because an agency is obligated to consider all "relevant matter[s] presented" during notice and comment,⁴¹ and may not "fail to respond to substantial problems raised by commenters,"⁴² nor "offer ... an explanation for its decision that runs counter to the evidence before the agency."⁴³ ICI has offered irrefutable analysis showing that the Department's previous assessment of the rule's benefits was flawed; it was based on a mathematical error—easily noted and easily fixed. To the extent the Department considers the rule's benefits in deciding whether to extend the January 1, 2018 date, the Department may not rely on demonstrably flawed conclusions, since that would "run counter to the evidence before the agency,"⁴⁴ and would improperly "fail to respond to substantial problems raised by commenters."⁴⁵ Therefore, the Department now must reconsider its flawed earlier conclusions regarding the rule's purported benefits for retirement investors.

C. Delaying the January 1, 2018 applicability date would reduce burdens on service providers and benefit retirement investors by allowing for a more efficient implementation of the fiduciary rulemaking.

A delay would result in substantial cost-savings for financial institutions by allowing them to avoid the significant and burdensome costs of implementation that likely ultimately will prove unnecessary.⁴⁶ More time also will allow for a more efficient transition because it will allow the market to develop new products and services in response to the rulemaking. In contrast, the abbreviated timeline required by the January 1, 2018 applicability date simply will accelerate the need for sub-

⁴¹ 5 U.S.C. § 553(c).

⁴² *Bus. Roundtable v. SEC*, 647 F.3d 1144, 1149 (D.C. Cir. 2011).

⁴³ *Motor Vehicle Mfys. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983).

⁴⁴ *Id.*

⁴⁵ *Bus. Roundtable*, 647 F.3d at 1149.

⁴⁶ The Department estimates that implementation of the fiduciary rule will cost \$5 billion in the first year of the final rule's application. 2016 RIA at p. 10. The Department's estimate, however, does not include any estimate for the amount that asset providers, including mutual funds, will spend to change product offerings requested by intermediaries to ease compliance burdens. *Id.* at p. 244. As noted above, the vast majority of the costs will be incurred in implementing the more cumbersome and technically complicated aspects of the BICE conditions, including the policies and procedures required by the contractual warranties and technologically challenging website requirements. Further, as we stated in ICI's March 17 Letter, we believe that compliance costs will far exceed the Department's estimate in the 2016 RIA. *See* letter from Brian Reid and David Blass to Office of Regulations and Interpretations, Employee Benefits Security Administration, US Department of Labor (March 17, 2017), available at https://www.ici.org/pdf/17_ici_dol_fiduciary_applicability_ltr.pdf ("ICI's March 17 Letter").

optimal decision making that already is doing great harm to small investors—depriving them of access to investment advice in many cases and pricing them out of the advice market in others.

All conditions of the BICE and other related exemptions are scheduled to become applicable as of January 1, 2018—less than six months from the date of this letter. Undertaking the systems, website design, personnel training and product development changes necessitated by these conditions present costly and time consuming challenges. Each week that passes without a delay represents additional “sunk costs.” If the January 1, 2018 applicability date is not delayed, firms will continue to incur these costs—costs incurred solely to comply with conditions that ultimately may not be included in the BICE or related exemptions. The Department can prevent additional wasted implementation costs by delaying the January 1, 2018 compliance date.

Many funds do not plan to use the exemptions associated with the fiduciary rulemaking because they do not plan to become fiduciaries by providing advice. Even for these firms, failing to delay the compliance requirement for BICE conditions will be costly. This is because funds must respond to the needs of intermediaries who are relying on the exemptions. The “sunk costs” that will be caused by a failure to delay if the rule is ultimately modified would be “significant and unrecoverable.”⁴⁷

The move toward T shares is a primary example for why a delay is needed. Many funds have been developing T shares, which in most cases are only expected to be a temporary solution, until a better solution (*e.g.*, clean shares) can be made available. The Department’s bifurcated approach allowed many intermediaries to postpone the decision of whether T shares are needed, because the neutral factors provisions of the warranty/policies and procedures conditions of the BICE are not yet applicable. A sampling of our members⁴⁸ reports intermediaries’ declining interest in T shares, and confirms that this development is due in part to a growing perception that clean shares offer a better long-term solution under the framework of the current rule. ICI members also report that many of their key intermediary partners are strongly considering the use of mutual fund clean share classes in both fee-based and commissionable account arrangements but that certain obstacles⁴⁹ prevent rapid

⁴⁷ This is described in detail in ICI’s March 17 Letter. *See* page 19 through 22 of ICI’s March 17 Letter.

⁴⁸ ICI informally surveyed its members regarding their adoption of T shares. Two-thirds of respondents to ICI’s member survey indicate they requested SEC approval to introduce T shares to the market, yet only 17% of respondents have actually launched T shares, and another 11% plan to launch later this year. The majority of respondents (approximately 72%) indicate there is not sufficient intermediary demand to warrant the launch of T shares.

⁴⁹ These obstacles include: (1) intermediaries must significantly modify both brokerage and sub-account recordkeeping systems to apply the intermediary’s own commission, rather than apply the traditional fund sales charge, on account transactions and report this information on shareholder confirmations; (2) intermediaries must determine how clean shares fit within the intermediary’s ongoing business model for adviser compensation and coverage of account servicing costs; and (3) funds may require intermediaries to execute an addendum to selling agreements that clarify their role as broker when offering clean shares. The contract vetting and sign off process takes time to execute, especially considering the fact that funds responding to ICI’s survey reported an average of 864 retail intermediary arrangements. While not all intermediaries

adoption of clean shares.⁵⁰ As this demonstrates, even absent any changes to the rule, more time is needed to develop clean shares and other long-term solutions to mitigate conflicts of interest.

Similarly, some firms may be considering using the BICE, but may be better served by a yet-to-be-developed exemption. These firms will incur unnecessary implementation costs to develop compliance with the BICE conditions, only to find out months later that a more appropriate exemption strategy is available.

A delay also is needed for those funds who plan to use the exemptions. For example, the BICE requires that the adviser provide disclosures by providing the investor a link to the financial institution's website. It will take a significant effort for many advisers to make the changes necessary to develop a website that is compliant with the BICE.⁵¹ If the BICE is modified to remove the website requirement, or to modify the information that is required to be included in the website, or if a new exemption is created that is a better fit for that adviser, then the expensive effort to develop the website will be completely wasted.

IV. The Length of the Delay of the January 1, 2018 Compliance Date Should Correspond to Timing of the Department Ultimately Determining the Future of the Rule.

As we previously advised the Department, the regulated community is operating in an environment of great uncertainty, creating inefficiency and sub-optimal implementation decisions.⁵² While a delay of the January 1, 2018 applicability date is crucial, such a delay must be sufficient to provide real relief. It also must provide the Department time to progress through its multiple tracks of reexamining its rulemaking in coordination with the SEC and other agencies. A brief delay only would exacerbate the uncertainty currently plaguing the industry and harming investors.

To provide increased certainty and to limit the continued expenditure of unnecessary “sunk” implementation costs and harm to investors, the Department should immediately—by August 15, 2017—issue an interim final rule delaying the January 1, 2018 applicability date for one year. In

may choose to offer clean shares, the number of agreement updates to allow intermediaries to sell clean shares to retail investors could be significant.

⁵⁰ A number of our members also report that a large portion of their intermediary partners have not contacted them regarding their compliance plans. This concerns us for a number of reasons. It is important for funds to understand the intermediaries' business models and to be able to offer appropriate product such as clean shares.

⁵¹ Note that we do support electronic delivery and the Department's effort to harness the benefits of online delivery. *See* page 10 of letter from David M. Abbey and David W. Blass, to Office of Exemption Determinations, Employee Benefits Security Administration, U.S. Department of Labor (July 21, 2015), available at https://www.ici.org/pdf/15_ici_dol_fiduciary_best_interest_ltr.pdf.

⁵² *See* ICI's March 17 Letter at p. 24.

conjunction with the delay, the Department should announce that it expects to propose modifications to the rulemaking under a set timetable with an expectation of finalizing such modifications prior to the end of the one-year delay period. The Department further should note that the applicability date of the modified rule and exemptions will become effective no sooner than one year after finalization.

This would provide the Department with adequate time to complete its multi-track reexamination of the rule and determine what modifications it will propose to the BICE and other related exemptions, as well as propose any potential new exemptions. It also would give the financial services industry and other interested parties clarity as to how the Department intends to proceed.

Finally, the Department invites comments on whether additional conditions of the exemptions should go into effect. In delaying the January 1, 2018 applicability date, the Department should not require compliance with additional conditions of the BICE and other related exemptions. This will only further compound the problems created by its rulemaking.

Even if the Department acts quickly after submission of the responses to the RFI, the Department will not be able to determine the exact nature of modifications to the rulemaking until it completes the impact analysis required by the President's Memorandum. Indeed, the weaknesses in the fiduciary rulemaking to date stem from a flawed impact analysis. Rather than serving as a tool to understand a problem and determine the best solution, the Department started with a predetermined agenda of eliminating perceived "conflicts" in the retirement marketplace and used the 2016 RIA to justify that effort. The result is an impact analysis that focuses on claims that support the Department's narrative and that readily dismisses facts that raise contrary conclusions regarding that narrative. Most significantly, the 2016 RIA fails to address adequately the harms of the rule—a topic of primary importance in the President's Memorandum. These harms include the economic impact of investors losing access to commission-based arrangements, being pushed to fee-based accounts, and losing access to advice and guidance. In addition to accounting for the foregoing, the Department's impact analysis must include information derived from quantitative or qualitative data focused more clearly on showing the problem that the rule is intended to solve, as well as the anticipated costs and benefits of the rule as a solution. Among other things,⁵³ it must include analysis of the costs associated with the failure to coordinate with the SEC and implement a single consistent best interest standard.

We are certain that such an analysis will lead the Department to conclude that a more targeted and consistent best interest standard will better protect investors while ensuring the continuation of affordable access to financial guidance to help individuals prepare for their financial needs. Moving forward with additional conditions prematurely and without the benefit of a new impact analysis will only exacerbate the harm that the rulemaking is having on retirement investors.

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⁵³ See pages 30 through 31 of ICI's April 17 Letter for a discussion of other analyses that are missing from the Department's 2016 RIA that should be included in the impact analysis requested by the President.

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We appreciate the opportunity to comment in response to the RFI. If you have any questions regarding our comments, or would like additional information, please contact Dorothy Donohue at 202-218-3563 or ddonohue@ici.org or David Abbey at 202-326-5920 or david.abbey@ici.org.

Sincerely,

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