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August 7, 2017

Via Email

Office of Exemption Determinations
Employee Benefits Security Administration
Attn: D-11933 (RIN 1210-AB82)
U.S. Department of Labor
200 Constitution Avenue, NW
Washington, DC 20210

Dear Sir or Madam:

Re: Schulte Roth & Zabel LLP Comments on Request for Information Regarding the Fiduciary Rule and Prohibited Transaction Exemptions (RIN 1210-AB82)

Schulte Roth & Zabel LLP is a multidisciplinary law firm with offices in New York, Washington, D.C. and London, England. Founded in 1969, the Firm has, since its beginning, represented numerous private funds, including hedge funds, private equity funds and real estate funds; currently in the hundreds. This experience has enabled us to develop a deep understanding both with respect to how private funds operate and with respect to the needs and desires of the investors who invest in private funds. As discussed below, that understanding has made clear the adverse effect that the Fiduciary Duty Rule (the "Rule") and its related Best Interest Contract Exemption (the "BIC Exemption") has already had on the ability of sophisticated individual investors who desire to invest in private funds through their individual retirement accounts ("IRAs") and individual accounts in self-directed defined contribution plans ("Individual Accounts"), typically alongside their personal investment in such funds, to make such investments. For many such investors, access to such investments closed on June 9. For the reasons discussed below and in furtherance of both President Trump's February 3 Presidential Memorandum on the Fiduciary Duty Rule (the "President's Memorandum") and the Secretary of Labor's Op-Ed piece regarding the Rule, we believe that the Rule should be revised with respect to such sophisticated IRA and Individual Account Investors and, while such a process is occurring, the effective date of the BIC Exemption should be postponed and the non-enforcement period should be extended.

1. <u>The Rule is adversely effecting sophisticated individual investors who desire to invest in private funds through IRAs and Individual Accounts.</u> The Rule, as currently drafted, denies sophisticated individual investors the freedom of choice given them by Congress to invest in

private funds without the need to seek and pay for outside advice. Congress has specifically and repeatedly chosen to treat an IRA and its IRA holder, and an Individual Account and its Individual Account holder, as one for investment sophistication purposes (both in the definition of "accredited investor" and the definition of "qualified purchaser"). Congress thus enabled the typically smaller IRAs and Individual Accounts to make investments that are only available to sophisticated investors and accordingly enabled such sophisticated investors to take a holistic approach to investing their personal, IRA and Individual Account portfolio. Yet, in commentary issued by the Department in connection with the Rule, the Department has specifically rejected this treatment of IRAs and Individual Accounts as one and the same. Accordingly, sophisticated individual investors are now face the unappealing and unnecessary choice of giving up the ability to make investments in a manner that is most advantageous to them, while they adopt a holistic view of their investment portfolio, or paying an outside person a fee to tell them how to invest their IRA and/or Individual Account, a decision they are fully capable of making on their own. As mentioned above, forcing such sophisticated individual investors into a framework best designed for retail investors is antithetical both to the directives set forth in the President's Memorandum and Secretary Acosta's Op-Ed piece, both of which emphasize expanding investment freedom of choice where it has been unnecessarily limited.

2. The BIC Exemption provides no relief to private funds nor their IRA and Individual Account Investors

The fundamental approach of the BIC Exemption is to require the advice fiduciary to view its client and their investment portfolio on a holistic basis. While this may make sense in the retail setting, private funds are not designed in this manner and private fund investors do not look to the manager of the private fund to provide such advice. Moreover, such investors and potential investors do not even want to receive such advice from the private fund manager because that would entail giving the private fund manager access to the potential investor's entire portfolio. Private fund managers typically offer a very limited menu of investments (often just one fund) and may have expertise only in the particular investment strategy they pursue. Typically, they do not have staff to analyze the overall investment portfolio of existing and, often times the existing and potential investors do not and will not give the private fund manager access to such information. Of course, some individual investors hire do outside investment advisory consultants. That is their choice. Many other sophisticated investors make their own investment choices without advice or input from outside advisers, much less from the private fund manager, although they may have a discussion with the private fund manager solely with respect to the fund's investment strategy and philosophy. The sophisticated IRA and Individual Account Investor is looking to the private fund manager for one thing only, execution of the investment strategy laid out in the fund's private placement memorandum. Thus, as drafted, the BIC Exemption provides no relief because it requires an analysis of the IRA Investor's or Individual Account Investor's portfolio in a way that those investors are not seeking.

Further, because neither the BIC Exemption nor the so-called seller's exemption provide relief from fiduciary status in connection with the marketing of private funds, we have found that large numbers of private funds have been forced by necessity to simply close their private funds to investments from unrepresented IRAs and Individual Accounts. This is the antithesis of the directives set forth in the President's Memorandum and Secretary Acosta's statement in the Op-

Ed piece which emphasize expanding freedom of investment choice, rather than narrowing it, as has been accomplished by the Rule.

We also note that there have been instances since June 9 where private fund managers, including private fund managers that manage plan asset look-through funds, have been denied access to private funds managed by others because they saw no need to hire outside consultants to advise them how to invest their IRAs. In addition, some private funds have already begun to compulsorily redeem existing IRA and Individual Account Investors. During this non-enforcement period and in light of the President's Memorandum and Secretary Acosta's Op-Ed piece, other funds have taken a more wait and see approach in the hope that the Department will revise the Rule and/or the BIC Exemption so that they are not in contravention of the directives set forth in the President's Memorandum and Secretary Acosta's Op-Ed piece.

3. The marketing of private funds does not constitute investment advice. The marketing of private funds is not intended to be and is not in the nature of investment recommendations to potential investors. Rather, such marketing activities are in the nature of an explanation of how the private fund works, its investment aims and strategies, and the risk surrounding such investments. This is true both with respect to a fund's offering memorandum and subsequent investor letters. They speak to a particular product, but not the role of that product in an investor's overall investment portfolio. Yet the lack of clarity in the Rule with respect to investment education could cause these materials to render the private fund manager a fiduciary to the unrepresented IRA and Individual Account Investor, adding to the reason that many private funds are denying access to sophisticated IRA and Individual Account Investors. This, in turn, results in a situation that limits the ability of sophisticated investors to invest their combined assets in an optimal manner. This too is inconsistent with the directives set forth in the Presidential Memorandum and Secretary Acosta's emphasis in his Op-Ed piece with respect to investment freedom of choice.

4. The lack of a Realistic Hire Me Exception inhibits investment of unrepresented IRAs and Individual Accounts in Private Funds. In formulating ERISA's Plan Asset regulation and Section 3(42) of ERISA, both the Department and Congress viewed the investment in a private investment vehicle as tantamount to the hiring of the investment manager. Even though both regulation and the law provide an exception for a fund in which benefit plan investors hold less than under 25% of the equity interests in such vehicle, the fundamental underpinning of the Plan Asset regulation is quite clear. The Rule allegedly provides a hire me exception from fiduciary status in marketing the services of an investment manager, but the Rule has defined that exception so narrowly as to itself bring about the potential for a violation of section 404 of ERISA by the hiring plan fiduciary. Although the Rule is particularly unclear in this area, if a manager seeking to comply with the hire me exception is unable to discuss his or her investment strategy and philosophy with potential clients, then the plan fiduciary is arguably in violation of his or her fiduciary duty under ERISA to understand how the manager it selects will manage the money entrusted to the manager. Given the Department's over 30-year view that the investment in an over 25%-plan asset fund is tantamount to an investing plan hiring the pooled vehicle manager as a direct fiduciary of that plan, investing in a pooled investment vehicle should be subject to a realistically revised hire me exception. Such a revision both as to the scope of the hire me exception and its application to private funds would be consistent with the fundamental underpinnings of the Plan Asset regulation that an investment in a private pooled vehicle is akin

to hiring the pool's investment manager as a direct investment manager of each investing plan and would also be consistent with the directives in the President's Memorandum and Secretary Acosta's Op-Ed piece regarding the restoration of the freedom of investment choices unnecessarily removed by the Rule as applied to sophisticated IRA and Individual Account Investors.

5. The lack of recognition of co-investing. The Rule ignores the reality that many sophisticated investors invest both their personal assets and their IRA or Individual Account together in the same private funds. When private funds communicate with investors they rarely, if ever, differentiate those communications between different types of investors other than to explain the tax ramifications of investing taxable and tax exempt monies. Yet the Rule as written would require the unrepresented sophisticated IRA and Individual Account Investor to ignore his or her personal investments and pay an outside consultant in order to be able to invest in the very same private fund. Here too, this limitation contravenes the directives on expanding freedom of investment choice set forth in the President's memorandum and Secretary Acosta's Op-Ed piece.

Each of the points raised in this letter are capable of appropriate resolution by modifying the Rule and the BIC Exemption to provide an exemption for investment by sophisticated unrepresented IRAs and Individual Accounts to avoid this class of investors from being shut out from investing in private funds where a sophisticated investor has determined that such an investment is appropriate. We encourage the Department to follow the clear guidance from Congress in treating such sophisticated investors as different from retail investors and recognize that the protections necessary for such investors have been clearly set by Congress and the SEC, rather than subjecting them to rules that will close off private funds as an investment option, no matter how appropriate. We also encourage the Department to clarify the rules surrounding the marketing of private funds and recognize the investment education rather than investment recommendation nature of those marketing materials. In addition we encourage the Department to adopt a realistic hire me exception that will apply to the marketing of private funds, both Plan Asset and non-Plan Asset. Finally, we encourage the Department to carve out from coverage under the Rule the situation where a sophisticated investor has invested both his or her personal assets and his or her IRA or Individual Account in the same fund.

Schulte Roth & Zabel LLP would like to reiterate its thanks to the Department for the opportunity to provide comments in response to the Request for Information and we would welcome the opportunity to discuss our views in greater detail. Please do not hesitate to contact David M. Cohen at (212) 756-2141 with any questions that the Department or its staff have regarding this letter.

Schulte Roth & Zabel LLP