FirstClearing

An affiliate of Wells Fargo & Company

February 3, 2011

Office of Regulations and Interpretations
Employee Benefits Securities Administration
Attn: Definition of Fiduciary Proposed Rule, Room N-5655
U. S. Department of Labor
200 Constitution Avenue, NW
Washington, DC 20210

Re: Definition of Fiduciary Proposed Rule

Ladies and Gentlemen,

First Clearing, LLC ("First Clearing") appreciates the opportunity to provide comments to the Department of Labor (the "Department") on the proposed regulation, published on October 22, 2010, which would substantially amend the current and longstanding regulatory interpretation of fiduciary status under the Employee Retirement Income Security Act of 1974, as amended ("ERISA"). First Clearing, an affiliate of Wells Fargo & Company, provides securities-execution and brokerage-clearance services to Wells Fargo Advisors, LLC, Wells Fargo Advisors Financial Network, LLC, H.D. Vest Investment Securities, Inc, and over 100 non-affiliated retail securities firms throughout the United States. Although First Clearing is included within the Wells Fargo & Company comment letter to the Department, we are forwarding this supplemental letter in order to provide greater specificity as to the unique attributes governing a clearing firm.

In the proposed rule, the Department expands the interpretation of fiduciary status under Section 3(21)(A) of ERISA by redefining the activities that constitute the provision of "investment advice for a fee or other compensation." We understand that the Department hopes thereby to reach individuals and entities that it believes should appropriately be held liable as fiduciaries, either for activities or guidance that reasonably appears to the client to be fiduciary in nature or for activities that are in and of themselves fiduciary in scope. However, the proposed regulation as it is currently drafted will significantly impact broker-dealers who act as clearing firms in ways that are not within the scope of the change's intent.

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First Clearing, LLC is a registered broker-dealer and a non-bank affiliate of Wells Fargo & Company, member NYSE/SIPC.

The proposed regulation includes in "investment advice" the provision of advice or an appraisal or fairness opinion concerning the value of securities or other property.[1] It goes on to exclude from these activities "the preparation of a general report or statement that merely reflects the value of an investment of a plan or a participant or beneficiary, provided for purposes of compliance with the reporting and disclosure requirements of the Act [ERISA], the Internal Revenue Code, and the regulations, forms and schedules issued thereunder, unless such report involves assets for which there is not a generally recognized market and serves as a basis on which a plan may make distributions to plan participants and beneficiaries."[2]

Unfortunately, the exclusion does not address the other legal and regulatory requirements that may cause a service provider to provide a general report or statement. As a clearing institution, First Clearing provides clearing services to retail and institutional accounts through an introducing broker. The introducing broker is the party who works directly with the retail client. Introducing brokers have a variety of responsibilities related to the opening and approving of brokerage accounts, including the responsibility for making recommendations and determining the suitability of specific investment strategies, as well as maintaining the client relationship. The clearing firm's responsibility is more limited, in that the clearing firm does not provide any advisory services to the client nor does it generally have direct contact with the client. However, the clearing firm is responsible for the safekeeping of money, funds, and securities and is tasked with the delivery of a confirmation for each transaction of an introduced account. Under NASD Rule 2430, it is also responsible for providing at least one quarterly summary of account status (an account statement). Such statements are subject to numerous format and content requirements. Since these required statements are not different in nature from statements that may be provided for ERISA or Internal Revenue Code, we request that the Department remove the limitation that only general reports or statements provided for purposes of compliance with ERISA or the Internal Revenue Code are exempt.

In addition to the expansion of the types of general reports and statements covered by the exclusion, we suggest that the limitations on the exclusion be removed. In many instances, clearing broker-dealers are required to provide valuations that are not derived from an exchange or an active market. As disclosed to the client, securities prices reflected on client statements may not reflect values derived from a "generally recognized market" when securities are thinly-traded or are illiquid. In those instances, clearing broker-dealers typically rely on outside quotation services, computerized pricing services, or on methodology based on the most recent "bid-price" or last reported transactions. As an example, certificate of deposits ("CD's") purchased by clients of broker-dealers are usually priced by a pricing service vendor. For other investments, the investment's value is determined by a third party. A hedge fund's values, for instance, are determined by the hedge fund manager and it is the hedge fund manager's valuation that is reported on the statement. In certain cases, such as for limited partnership holdings or other hard-to-value assets, the client may direct the clearing broker-dealer to accept valuations from a third party.

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[1] Proposed §2510.3-21(c)(1)(i)(A)(1)
[2] Proposed §2510.3-21(c)(2)(iii)

In non-market pricing situations, securities prices are provided as estimated valuations. Statement disclosures alert clients that they may not be able to buy or sell an investment based on the estimated statement value. For example, NASD Rule 2340 makes clear that if an account statement provides an estimated value for a Direct Participation Program (DPP) or Real Estate Investment Trust (REIT) security, it must include a brief description of the estimated value, its source, and the method by which it was developed, as well as a disclosure that DPP or REIT securities are generally illiquid, and that the estimated value may not be realized when the investor seeks to liquidate the security. Since the provision of estimated values or values received from a source other than an exchange is required but administrative in nature, we believe that the provision of non-market valuations on other statements and reports required through other regulation should not be considered fiduciary activity.

Absent greater clarity and a broader exclusion for general statements and reports required by other regulatory authority, we are concerned that IRA custodians and other parties who provide investment account services for IRAs and ERISA-covered plans may substantially limit the investments that IRAs and ERISA-covered plans may hold in their accounts. While certain investments may not be valued in a manner consistent with the Department's concept of a "generally recognized market", they can be valuable additions to a plan or IRA's investment portfolio, providing additional protections (in the case of CDs) or a means for balancing market exposure. We are also concerned about the, possibly unintended, impact of the proposed regulation on pricing and quotation services vendors, who may choose to cease certain pricing services or substantially change the cost in light of potential liability under the proposed regulation. We strongly urge the Department when drafting the new regulation to consider the full range of investments available and the way in which such investments are typically valued, and to broaden the exclusion for statements and reports.

We hope these comments have been helpful and we hope that the Department will consider them while determining the proposed regulation's scope and form.

Sincerely,

Atul Kamra
President
First Clearing Correspondent Services