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Fiduciary Responsibility

DOL Fiduciary Re-Proposal Fires Up Foes, Supporters, as They Brace for Battle

Opponents and supporters of the Department of Labor's fiduciary rule began gearing up for battle as soon as President Barack Obama said that he was throwing his support behind it.

Without actual text of the re-proposed rule (RIN 1210-AB32), analysts descended on Obama's comments made when he announced at the AARP headquarters on Feb. 23 that the guidance was moving forward and gleaned his remarks for any information that could hint as to what the actual proposal might say.

"The proposed rule may have the unintended consequence of reducing middle class savings," Peter W. Schneider, chief administrative officer and incoming president of Primerica Inc., told Bloomberg BNA in an e-mail, adding that this is what he has heard so far, since the rule isn't public yet. "The rule is likely to make it harder or more expensive for working-class families to meet with financial representatives to learn about the importance of saving."

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"Cutting off access to financial education and savings options could dramatically reduce the preparedness of middle class Americans for retirement," said Schneider, of the Duluth, Ga.-based investment advice firm.

On the other side of the divide, Karen Friedman, executive vice president and policy director at the Pension Rights Center, told Bloomberg BNA that the proposal is a "common sense rule" that is "long overdue."

The proposal will "close a loophole" in the law so that investors will know that the advice they receive will be in their own best interest, Friedman said.

The Pension Rights Center and the AARP are both members Save Our Retirement coalition, which supports the administration's efforts.

At the heart of the battle is a retirement investment market in which more than 40 million American families have assets of more than \$7 trillion in individual retirement accounts, the majority of which comes from rollovers from employer-sponsored retirement plans, according to a new report from the president's Council of Economic Advisers.

Rollovers to IRAs exceeded \$300 billion in 2012 and are expected to increase steadily in the coming years, the report said.

The proposed rule, also called the conflict-of-interest rule, has been gestating for five years since it was initially issued in 2010 and then withdrawn a year later after receiving strong and sustained criticism (38 BPR 1693, 9/20/11).

The rule has been the subject of a long and fierce lobbying campaign that isn't likely to cool in the wake of the president's remarks.

"We've got to make sure Americans who are doing the responsible thing by preparing for retirement are getting a fair share of the returns of those savings," President Obama said.

He said that those saving for retirement "should have the peace of knowing the advice you're getting for investing those dollars is sound" and "that you're not being taken advantage of."

Obama said there are "a lot of very fine financial advisers out there, but there are also financial advisers who receive backdoor payments or hidden fees for steering people into bad retirement investments that have high fees and low returns."

"The re-proposal gets to the heart of what happens without fiduciary duties—widespread and harmful conflicts of interest. The re-proposal will reduce these conflicts."

—KNUT A. ROSTAD,
INSTITUTE FOR THE FIDUCIARY STANDARD

'Misleading.' "The White House message on the re-proposed rule is misleading," Judy Miller, director of retirement policy for the American Society of Pension Professionals & Actuaries, told Bloomberg BNA in an e-mail.

"Talk about 'hidden fees' and 'backdoor payments' makes it sound like a disclosure rule instead of a rule

that could prevent Americans from working with their financial advisor.”

The president called for a set of uniform rules to ensure financial advisers always act with their clients’ best interest in mind and don’t steer clients to particular products for their financial gain. Bad advice can wear away as much as 25 percent over 35 years of saving for retirement, he said.

Labor Secretary Thomas E. Perez said in a White House press statement, “Under the President’s direction, the Labor Department will publish a rule in the coming weeks that will require retirement advisers to put the best interests of their client above their own financial interests.”

Reviews by the Office of Management and Budget’s Office of Information and Regulatory Affairs are limited to 90 days, though the OMB director can extend it once for up to 30 days and the head of a rulemaking agency can extend it indefinitely.

Later in the week, a DOL official said at a Baltimore conference that opponents of the proposal should wait until it comes out to criticize it, as exemptions in the regulation could address concerns that the rule will harm the access of lower- and middle-income Americans to investment advice (see related article in this issue).

Limiting Advice. David Hirschmann, president and chief executive officer of the U.S. Chamber of Commerce’s Center for Capital Markets Competitiveness, said in a news release that we “should always seek ways to better inform and serve investors, but one size-fits-all rigid rules is a step in the wrong direction. We will judge any proposed rule by the Department of Labor by one simple test: will it help ensure investors have access to more advice and well-disclosed choices to plan and save for their retirement.”

The DOL has promised to revise old prohibited transaction exemptions and issue new ones to help financial advisers continue to do business without worrying about tripping the Employee Retirement Income Security Act’s penalties on prohibited transactions. On Feb. 20, the Chamber of Commerce released a white paper, “Using PTEs to Define a Fiduciary Under ERISA: Threading the Needle with a Piece of Rope,” in which it sought to lay out the difficulties involved in defining the limits of a fiduciary’s responsibilities by using PTEs.

Obama may have indicated in his remarks that the proposal will address the PTE problem, said Bradford P. Campbell, counsel at Drinker, Biddle & Reath LLP in Washington.

“The most interesting statement from the Administration is that there will be a ‘principles-based’ exemption regarding conflicts in the re-proposal. While it is not clear what this means, one may hope that it is an exemption with reasonable conditions permitting fiduciary advisors to plans to help plan participants with IRA rollovers, rather than a prohibition of such advice,” said Campbell, who previously served as the assistant secretary of the DOL’s Employee Benefits Security Administration from 2007 to 2009.

“I think it is interesting because it could be a new exemption governing the rollover process, something that is currently a legal grey area (the applicable DOL advisory opinion currently says only that a rollover done by a fiduciary advisor to the plan ‘may’ be a prohibited

transaction) and that an overly restrictive proposal would make worse,” Campbell said.

The applicable opinion is Advisory Opinion 2005-23A, in which the DOL said that an individual who advises a plan participant on how to invest assets or manages the assets in exchange for a fee is a fiduciary with respect to the plan, within the meaning of ERISA Section 3(21)(A) (33 BPR 232, 1/24/06).

The DOL also said in that guidance that a recommendation that a participant roll over an account balance to an IRA to take advantage of investment options that aren’t available under the plan doesn’t necessarily constitute investment advice with respect to plan assets. However, this applies only to advice provided by a person who is not a plan fiduciary on some other basis, the guidance said.

At a Chamber of Commerce panel discussion on the fiduciary proposal held Feb. 20, ASPPA’s Miller said that her organization would like to see the exemption in the rule itself, not in a PTE, that would allow 401(k) plan advisers, with appropriate disclosures, to talk to plan participants about their rollovers without being considered a fiduciary and therefore subject to ERISA’s fiduciary standards (42 BPR 351, 2/24/15).

Expanded Definition. The Certified Financial Planner Board of Standards Inc. (CFP Board) supports the DOL’s proposal.

“As a fervent advocate for strong fiduciary standards in the provision of investment advice, CFP Board is pleased to see the White House and Department of Labor take a critical step toward protecting American investors and their retirement savings through a fiduciary rule under ERISA,” the group said in a news release.

The CFP Board sets and enforces standards for certified financial planners, and according to the new release, has certified more than 71,000 financial planners.

“We remain steadfast in our belief that it is appropriate for every advisor who provides financial planning advice—including professionals providing retirement investment advice—to do so under a fiduciary duty to their clients. We believe that, based on our experience with the application of CFP Board’s fiduciary standard across business models, that the fiduciary standard can be applied without reducing the availability of services,” the group said.

Knut A. Rostad, president of the Institute for the Fiduciary Standard, said that ERISA’s concept of fiduciary responsibility is based on “centuries-old fiduciary law, English common law, that has governed ‘advisors’ for ages. The relevance is this is not new or just hatched up by the government regulators; it’s long-established as essential to the markets and economy. The re-proposal gets to the heart of what happens without fiduciary duties—widespread and harmful conflicts of interest. The re-proposal will reduce these conflicts.”

Real-Life Implications. Lisa Bleier, managing director and associate general counsel at the Securities Industry and Financial Markets Association, said that SIFMA has asked the DOL and the administration to consider the potential real-life implications of the proposal on middle income investors, but that “we believe those have not been taken into account up to now.”

If the rules aren’t crafted well, they will limit people’s access to the advice they need to get ready for retirement, Bleier said.

But if the rules are well-crafted, they will help lower the fees that investors pay, said Matthew Morey, finance professor at Pace University.

Based on his research, Morey said that “what makes sense to me” is that investors should have to pay only low fees, and that they need to know what fees they’re paying.

Unfortunately, investors “often are lured, or coerced into, funds with high fees, even index funds,” which can charge “insane fees,” Morey said.

However, mutual fund fees have already come down over the past 20 years, Paul S. Stevens, president and CEO of the Investment Company Institute, said in a Feb. 23 news release.

“America’s retirement savers need continued access to information and guidance to make sound investment decisions,” Stevens said. “The mutual fund industry provides a tremendous amount of support and information to retirement savers, including disclosure on the cost of investing. We are proud of the fact that mutual fund fees in retirement plans have fallen for two decades, even as the services provided to employers and plan participants have increased.”

They’ve fallen, but not enough, Morey said.

“Fees have kind of come down, but nowhere near what it should have. Fees are still way too high,” he said.

Whether the regulation will knock fees down further will depend on how well it is drafted to not let advisers and broker-dealers “get around the rules” and how well it is enforced, he said. And that’s “basically a big if,” he said.

SEC Coordination. SIFMA has also asked the DOL to work closely with the Securities and Exchange Commission and the Financial Industry Regulatory Authority (FINRA), both of which provide guidance on advisers and broker-dealers.

The SEC has also been working on fiduciary guidance, but hasn’t indicated when it will be released. Mary Jo White, SEC chairman, said Feb. 20 that among the SEC’s priorities this year is “consideration of whether to adopt a uniform fiduciary duty for broker-dealers.”

Daniel M. Gallagher, a Republican SEC commissioner and frequent critical of the DOL’s re-proposal, said in remarks at a conference Feb. 20 that “despite

public reports of close coordination between the DOL and SEC staff, I believe this coordination has been nothing more than a ‘check the box’ exercise by DOL designed to legitimize the runaway train that is their fiduciary rulemaking.”

Bleier, for her part, said that the SEC should move forward with its fiduciary guidance. “We do wish they were closer,” she said.

Bleier added that the issues that the DOL and SEC have been working on are complex, and that SIFMA wants to make sure that the proposed rules have in place “appropriate protections” for both advisers and broker-dealers, and for investors.

Regarding whether the DOL has been taking into account the many comments it has received from the financial industry, Friedman, of the Pension Rights Center, said, “My assumption is that the DOL has heard from every single person on this.” The concern that the DOL hasn’t listened to everyone is “absurd,” she said.

Long Road. Frank Cummings, a benefits attorney who helped draft ERISA with Jacob K. Javits, a Republican senator from New York who ushered the passage of the law, told Bloomberg BNA that there is a long road to go before the proposal becomes a rule.

“The proposal is not yet a regulation,” said Cummings, currently an adjunct lecturer at the University of Virginia School of Law, and adjunct professor at John Marshall Law School and Earle Mack Law School of Drexel University.

Once the DOL puts the proposal out, it “will then be subject to notice, comment, and hearings, as it was when previously proposed in 2010 (and later withdrawn). So it’s a long way from being a regulation. But it’s important, and it raises some important policy issues.”

Cummings also said that while the general thrust of the proposal is already known, he didn’t want to criticize it before seeing it.

“My own view is that the problem is important, but not all solutions make things better. In other words, it all depends.”

BY SEAN FORBES

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