



March 17, 2017

Office of Regulations and Interpretations  
Office of Exemption Determinations  
Employee Benefits Security Administration  
U.S. Department of Labor  
200 Constitution Avenue, N.W.  
Washington, D.C. 20210

Re: Definition of the Term "Fiduciary" - Delay of Applicability Date, RIN 1210-AB79

To Whom It May Concern:

On behalf of Americans for Financial Reform (AFR) we are writing to express our strong opposition to the proposal to delay the applicability date of the Department of Labor's (DOL) fiduciary rule.<sup>1</sup> The fiduciary rule strengthens protections for retirement savers by requiring brokers and advisors to provide retirement investment advice that is in their clients' best interests. Delaying these protections would allow the sellers of financial products to retirement savers to continue to put their own profit interests above the needs of their clients, perpetuating harmful and exploitative practices that drain funds from retirement savers for the benefit of the seller.

Like many public interest, investor, and industry organizations, AFR has commented extensively regarding the fiduciary rule and has participated in numerous meetings with DOL and other agencies over the multi-year process of study and consultation that led to the final fiduciary rule. The final rule and the process that led to it has now been upheld by three federal district courts.<sup>2</sup> In contrast to the extensive and time-consuming analytic and consultative work leading up to the rule, this proposal would delay the rule's established implementation date with seemingly no clear basis beyond the new Administration's desire to reverse the final rule.

The proposal makes a speculative appeal to unspecified "frictional costs" of implementing the rule and then having it reversed in the future, a step which would lead to "two major changes in the regulatory environment" rather than one. This is a bit of circular reasoning thinly disguised as

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<sup>1</sup> Americans for Financial Reform is an unprecedented coalition of more than 200 national, state and local groups who have come together to reform the financial industry. Members of our coalition include consumer, civil rights, investor, retiree, community, labor, faith based and business groups. A list of AFR members is available at <http://ourfinancialsecurity.org/about/our-coalition/>

<sup>2</sup> *Chamber of Commerce of the United States v. Hugler*, Nos. 3:16-cv-1476-M, 3:16-cv-1530-C, 3:16-cv-1537-N (N.D. Tex. Feb. 8, 2017); *Market Synergy Group, Inc. v. Dep't of Labor*, No. 5:16-cv-04083-DDC-KGS (D. Kan. Nov. 28, 2016); *Nat'l Ass'n for Fixed Annuities v. Perez*, No. 1:16-cv-01035-RDM (D.D.C. Nov. 4, 2016). A fourth challenge, which seeks to invalidate only the arbitration provisions of the rule, is pending in federal district court in Minnesota. The arbitration provisions were upheld in the decision of the district court in Texas. See *Chamber of Commerce of the United States v. Hugler*, slip op. at 79-81.

an analytic justification. The Administration's desire to overturn the rule cannot itself serve as the justification for delaying the rule. The promulgation of this rule, including its implementation date, under the protocols of the Administrative Procedure Act involved thousands of hours of work by both DOL employees and by outside organizations such as AFR, which invested extensive effort in commenting on the details of rule proposals. It makes a mockery of these requirements to simply postpone the rule's implementation date without a clear policy justification.

As the DOL itself admits in this proposal, the extensive analysis done to support the fiduciary rule clearly demonstrates that a delay would create costs to investors many times higher than the benefits accrued to industry from delaying their compliance with the rule. Based on savings in only one market segment and making highly conservative assumptions about the rule's impacts, the proposal states that a sixty day delay would have present value costs to investors of at least \$890 million over a ten year horizon. Examining a broader market segment and a thirty year time horizon, the Economic Policy Institute has calculated costs to investors of \$3.7 billion for a sixty day delay. Both of these estimates dwarf the estimated reduction in compliance costs of \$42 million over a sixty day delay.

Unless it believes that gains in industry profits should be valued at a far higher level than costs to ordinary families saving for retirement, the DOL must reject any delay of this rule.

### **The Fiduciary Rule Brings Extensive Benefits**

Without the implementation of the final rule, many financial advisers that retirement savers turn to for retirement investment advice would continue to be permitted to make recommendations that serve their own self-interest at their client's expense. This is due to the narrow construction of the original 1975 rules defining fiduciary status under the Employee Retirement and Income Security Act (ERISA). These rules, created before the widespread adoption of self-directed retirement plans, defined the term "fiduciary" narrowly to include only those advice providers who met each separate element of a non-statutory five part test.<sup>3</sup> The test effectively excludes many who provide important retirement advice to investors managing self-directed retirement plans such as 401(k) plans. To take one critical example, under the 1975 rules, brokers providing advice to retirement investors concerning the rollover of assets from an employer 401(k) plan to an IRA investment plan are not be covered as fiduciaries.

This narrow construction of fiduciary duty has permitted sellers in many areas of the market to provide retirement investment advice in the presence of extensive conflicts of interest, and to act on those conflicts of interests in ways that harm their clients. In its Regulatory Impact Analysis (RIA), the DOL extensively chronicled both the extent of these conflicts of interest and the harm

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<sup>3</sup> The five part test requires that to qualify as a fiduciary a person or entity (1) make recommendations on investing in, purchasing or selling securities or other property, or give advice as to the investments' value; (2) on a regular basis; (3) pursuant to a mutual understanding that the advice; (4) would serve as a primary basis for investment decisions; and (5) would be individualized to the particular needs of the plan.

they can cause.<sup>4</sup> The main body of the RIA is 395 pages long, and the appendices include hundreds of additional pages of report documents, so it is not easily summarized here. But the RIA gathered and surveyed a wide body of economic evidence which demonstrated that conflicted advice is widespread and causes serious harm to plan and IRA investors. It also found that advisers' compensation arrangements are often calibrated to align the firms', advisers', and product manufacturers' interests, over the interests of investors. Advisors or brokers are often paid more by the seller if they recommend products or transactions that are highly profitable to the financial industry, but produce losses for the investor compared to other alternatives. Investors can be harmed by conflicted advice in a variety of ways, including being steered into high-fee products, being steered into investments that perform poorly, or being encouraged to trade excessively, chase returns, and attempt to time the market in order to generate commissions for the broker.

After a careful review of the evidence, including extensive academic research using a range of methodologies and an original study based on data gathered by DOL researchers, the DOL estimated that IRA holders receiving conflicted investment advice can expect their investments to underperform by an average of 50 to 100 basis points per year over the next 20 years. Based on this careful review of the evidence, the DOL estimated that the underperformance associated with conflicts of interest in just one major market segment, mutual funds held by IRA owners, could cost IRA investors between \$95 billion and \$189 billion over the next 10 years and between \$202 billion and \$404 billion over the next 20 years. An ERISA plan investor who rolls her retirement savings into an IRA could lose 6 to 12 percent and in some cases as much as 23 percent of the value of her savings over 30 years of retirement by accepting advice from a conflicted financial adviser who does not qualify as a fiduciary under current rules.

This quantitative estimate is based only on losses to IRA investors due to excessive fees and underperformance in mutual fund products. The harm to retirement savers is far greater when one considers other potential impacts of conflicts of interest that were not included in the estimate, such as timing errors and excessive trading, and other products beyond mutual funds, most notably annuity products. The RIA also extensively documented evidence of investor losses in these areas.

In addition to the harm that can befall IRA investors from conflicts of interest, plan investors can also experience losses as a result of conflicts of interest. For example, the RIA pointed to a GAO study, which found that defined benefit pension plans using consultants with undisclosed conflicts of interest earned 1.3 percentage points per year less than other plans. Other recent research supports this finding. For example, a recent study by the Center for Retirement Research at Boston College found that mutual fund companies involved in plan management often act in ways that appear to advance their interests at the expense of plan participants.<sup>5</sup> The

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<sup>4</sup> Department of Labor, "Regulating Advice Markets: Regulatory Impact Analysis For Final Rule and Exemptions", United States Department of Labor, April 2016. 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>

<sup>5</sup> Veronika K. Pool, Clemens Sialm, and Irina Stefanescu, Are 401(k) Investment Menus Set Solely for Plan Participants?, Center for Retirement Research Boston College, August 2015, [http://crr.bc.edu/wp-content/uploads/2015/08/IB\\_15-13.pdf](http://crr.bc.edu/wp-content/uploads/2015/08/IB_15-13.pdf)

authors found that this bias is especially pronounced in favor of affiliated funds that delivered sub-par returns over the preceding three years. And participants do not shift their savings to undo this favoritism, especially the favoritism shown to sub-par affiliated funds, according to the study. The study also found that the lackluster performance of these sub-par funds usually persists.

Another recent study published in the Yale Law Journal found that a significant portion of 401(k) plans establish investment menus that predictably lead investors to hold high-cost portfolios. Using data from more than 3,500 401(k) plans with more than \$120 billion in assets, the authors found that fees and menu restrictions in an average plan lead to a cost of seventy-eight basis points (0.78%) in excess of index funds. The authors also documented a wide array of “dominated” menu options -- funds that make no substantial contribution to menu diversity but charge fees significantly higher than those of comparable funds in the marketplace.<sup>6</sup>

Incorporating the benefits reducing conflicted advice to employer plan investors would increase the expected benefits of the fiduciary rule significantly beyond the hundreds of billions of dollars of benefits expected to accrue to IRA mutual fund investors. The DOL rule would directly address the problem of conflicted retirement investment advice in both the plan and IRA contexts by requiring all financial advisers who provide retirement investment advice to serve their clients’ best interest, not their own self-interest. Importantly, the rule applies this protection not only to individual investors, but also to employers operating small company plans and relying on financial institutions for advice on investment selection. While the rule clearly allows firms to charge commissions for this advice, firms would be required to ensure that charging in this way is consistent with the client’s best interest. The rule would require firms and advisers to charge no more than reasonable compensation based on the value of products and services provided. And, it would require firms to rein in their often toxic web of conflicts of interest that encourage and reward advice that is not in their clients’ best interest. As a result, the rule would better align advisers’ and their clients’ incentives and, ultimately, produce better outcomes for both.

### **The DOL’s Own Analysis Shows That Benefits Justify The Rule’s Implementation Costs**

The fiduciary rule will produce both transfers, in the form of transfers of profits from large Wall Street financial companies and other sellers of financial products to the savings of ordinary retirement investors, and market efficiency gains due to improved transparency and reductions in agency costs. Because of this its many benefits cannot be simply netted against implementation costs. However, the DOL analysis clearly shows that the rule’s implementation costs are far lower than its benefits. The estimated implementation costs of the rule are between \$10 billion and \$31 billion, with a preferred estimate of \$16.5 billion over ten years.

The current proposal also acknowledges that these implementation costs are significantly lower than the expected benefits of the rule. The proposal cites only one quantified estimate of the benefits of the rule. This estimate is derived from examining just one segment of the IRA market,

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<sup>6</sup> Ian Ayres & Quinn Curtis, Beyond Diversification: The Pervasive Problem of Excessive Fees and “Dominated Funds” in 401(k) Plans, Yale Law Journal, March 2015, <http://www.yalelawjournal.org/article/excessive-fees-and-dominated-funds-in-401k-plans>.

namely front-end-load mutual funds, a market segment where the academic evidence on the costs of conflicted advice is particularly extensive. The estimate is also based on conservative assumptions, including the assumption that the rule will have only 50% effectiveness in its first year of implementation, and also that even independently of the rule there will be a trend toward improved practices in this segment of the market.

Even given these conservative assumptions and the examination of only a single market segment, this analysis produces investor benefits of between \$33 billion and \$36 billion over the first ten years of the rule. As detailed in the current delay proposal, this estimate implies that the present value costs of a 60-day delay in the rule will be \$890 million in lost investor benefits over a ten year time horizon. This compares to a total reduction in start-up compliance costs of \$42 million. Even looking at the conservative estimate of benefits in this single market segment, the costs to investors of delay will far exceed the benefits to industry of delaying compliance.

Of course, reductions in returns to IRA investors in front-end load funds are only a small fraction of the overall benefits of this rule. Evidence on the broader IRA mutual fund market implies much greater savings, such as for example the DOL's estimate cited above of \$202 to \$404 billion in 20-year savings to investors from the rule. The President's Council of Economic Advisors used evidence on the entire IRA market to estimate that the rule would boost returns to investors receiving advice on IRA rollovers by approximately \$17 billion per year.<sup>7</sup> Using the CEA report, as well as current data on the rate of IRA rollovers and withdrawals into mutual funds and variable rate annuities, the Economic Policy Institute has estimated that a 60-day delay would cost IRA investors in mutual funds and variable rate annuities \$3.7 billion in the present value of lost returns over a 30-year period.<sup>8</sup>

This EPI estimate still excludes additional potential losses to plan investors and losses to IRA investors in certain types of products not included in the EPI data sources, such as non-traded REITs and certain kinds of fixed annuities. In short, investor losses from this delay would dwarf the estimated \$42 million compliance cost savings to industry over the 60-day delay period.

### **The Rule Is Already Created Investor Benefits, and Delay Would Disrupt These Benefits**

Recent developments have shown how the DOL rule is transforming the way commission-based advice is offered, with enormous potential benefits for all investors, not just those saving for retirement. For example, the Securities and Exchange Commission recently approved a proposal from Capital Group to create a new class of mutual fund shares for its American Funds that will greatly ease compliance with the DOL rule while preserving investors' ability to get commission-based advice.<sup>9</sup> The approved "clean shares" will allow the broker, rather than the

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<sup>7</sup> Council of Economic Advisers, "The Effects of Conflicted Investment Advice on Retirement Savings", Executive Office of the President, February 2015. 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>

<sup>8</sup> Economic Policy Institute, "Comment on Fiduciary Rule Examination", March 17, 2017.

<sup>9</sup> John Waggoner, "American Funds gets SEC approval for clean shares," Jan. 13, 2017, <http://www.investmentnews.com/article/20170113/FREE/170119955/american-funds-gets-sec-approval-for-clean-shares>.

fund, to determine how much to charge for their services. By allowing brokers to separately price commissions, just as they do when recommending ETFs and individual securities, these shares make it easier for firms to adopt compensation policies that pay standardized amounts across different funds and different investments, eliminating the conflicts that are the target of the DOL rule without eliminating commission-based advice. They also allow advisers to succeed and prosper based on the cost and quality of their services and products rather than on how much they are being paid by third parties to recommend particularly investments.

In addition, many other fund firms are responding to the DOL rule by issuing T shares that both dramatically reduce the commissions for broker-sold funds and reduce the compensation-related conflicts associated with those funds. With T shares carrying a maximum sales load of 2.5 percent, compared with an industry standard for A shares of 4.75 percent (and as high as 5.75 percent), and 12b-1 fees of just 25 basis points, investors will also benefit from the dramatic reduction in cost. Indeed, Morningstar's John Rekenhaller notes, these shares have the potential to exert downward pressure on investment advisers' asset-based fees as well, as advisers seek to remain cost competitive.<sup>10</sup>

In addition, a number of major firms, including Schwab, Blackrock, Fidelity and Prudential, among others, have announced plans to reduce costs on certain investment products, such as ETFs and mutual funds, at least in part to be more competitive under the DOL rule.<sup>11</sup> And, large firms have announced that they are reducing advisory account minimums and costs as a result of the rule. For example, Edward Jones and LPL announced shortly after the DOL rule was finalized that they would lower the minimums on their fee accounts, to \$5,000 and \$10,000 respectively.<sup>12</sup> Schwab just announced a new advisory program with a minimum initial investment of \$25,000, all-in-costs between 0.36% and 0.52%, and comprehensive financial and investment planning from a CFP professional.<sup>13</sup> Vanguard's Personal Advisor Services offers fee-based advisory and financial planning services, charging only 0.30% for accounts with \$50,000. This platform has gathered almost \$40 billion in less than two years.<sup>14</sup>

The financial industry has spent a considerable amount of time and money preparing for implementation of the rule, and firms have made some very impressive improvements to their business models in order to comply. In response to a letter sent by United States Senator Elizabeth Warren, a number of firms, including Charles Schwab, BBVA Compass, Capital One, John Hancock, U.S. Bancorp, Fidelity, RBC, Principal Financial Group, Prudential Financial,

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<sup>10</sup> John Rekenhaller, Lower-Cost T Shares Coming to a Fund Near You, Morningstar, January 6, 2017, <http://beta.morningstar.com/articles/787395/lower-cost-t-shares-coming-to-a-fund-near-you.html>

<sup>11</sup> Consumer Federation of America, "The Department of Labor Conflict of Interest Rule is Already Delivering Benefits to Workers and Retirees: Delay Puts Those Benefits at Risk," Jan. 31, 2017, [http://consumerfed.org/wp-content/uploads/2017/01/1-31-17-DOL-Rule-Delivering-Benefits\\_Fact-Sheet.pdf](http://consumerfed.org/wp-content/uploads/2017/01/1-31-17-DOL-Rule-Delivering-Benefits_Fact-Sheet.pdf).

<sup>12</sup> Michael Wursthorn, Brokerages Adapt to Pending Labor Rule, Wall Street Journal, March 16, 2016, <https://www.wsj.com/articles/brokerages-adapt-to-pending-labor-rule-1458151260>

<sup>13</sup> Press Release, Schwab, "Schwab Announces Schwab Intelligent Advisory™", December 13, 2016, <http://pressroom.aboutschwab.com/press-release/schwab-investor-services-news/schwab-announces-schwab-intelligent-advisory>

<sup>14</sup> Vanguard, Personal Advisor Services, <https://investor.vanguard.com/advice/personal-advisor>

LPL Financial, Symetra Life Insurance, TIAA, Transamerica and Wells Fargo, responded they had devoted time and resources to meeting the April 10, 2017 implementation date and all expressed confidence that they would indeed be ready to comply on that date.<sup>15</sup>

This extensive progress toward compliance shows the error in the proposal's unsubstantiated claim that unspecified additional cost savings to industry will result from a last-minute delay of the rule. Delaying the rule at the eleventh hour will only disrupt the progress that has been made. Worse, such a delay would permit firms to roll back their pro-investor changes in order to once again profit by steering investors into higher-cost options. As a result, all of the benefits from firms' efforts that would flow to retirement savers would be in jeopardy if a delay goes through. Simply put, a delay in implementation of the DOL rule will immediately harm retirement savers.

### **Any Delay Will Not Be Limited To Sixty Days**

The 45-day comment period to address the issues outlined in the Presidential Memorandum as well as the many complex questions raised in the proposal will end on April 17<sup>th</sup>. This would provide less than eight weeks for the Department to consider and respond to comments, and make a final decision before the delay runs out on June 9<sup>th</sup> regarding whether to engage in further rulemaking. That's far too short a period to engage in the type of careful and rigorous analysis that is appropriate for an issue of this importance, and it is totally inconsistent with the careful and deliberative process the DOL undertook in promulgating the rule. The proposal itself anticipates that it may take more time to complete the full examination of the rule, further delaying protections for retirement savers.

Assuming the Department reasonably anticipates that a longer delay will be needed, it must evaluate the delay proposal based on the economic impact of the reasonably anticipated delay, not an arbitrary and misleading timeframe chosen in the apparent hope that the delay will survive legal review. If the DOL does evaluate the delay proposal based on the economic impact of a reasonably anticipated delay, it will find that the longer the rule is delayed, the more harm will befall retirement savers and the more obvious it will become that a delay is wholly unjustified.

The DOL should seriously rethink its apparent position that industry opponents' interests in avoiding having to comply with the rule should win out over retirement savers' interests in receiving the critical protections from the rule. Retirement savers, particularly small savers, cannot afford to wait any longer for those protections to be in place. Small savers are disproportionately served by non-fiduciaries today and therefore most susceptible to being given conflicted, harmful advice. As a result, small savers have the most to gain from having this rule be implemented as scheduled because it will ensure that every dollar that they save for retirement counts—that investment returns are maximized and unnecessary and hidden costs are minimized.

Retirement savers need and deserve to receive the protections of the rule without delay. The DOL should conclude that the proposed delay is unjustified and that the rule's April 10<sup>th</sup> implementation date should remain in force.

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<sup>15</sup> Letter from United State Senator Elizabeth Warren to Acting Department of Labor Secretary Edward Hugler, Feb. 7, 2017, [http://www.warren.senate.gov/files/documents/2017-2-7\\_Warren\\_Ltr\\_to\\_DOL.pdf](http://www.warren.senate.gov/files/documents/2017-2-7_Warren_Ltr_to_DOL.pdf).

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Thank you for your attention to this comment. If you have any questions, contact AFR's Policy Director, Marcus Stanley, at [marcus@ourfinancialsecurity.org](mailto:marcus@ourfinancialsecurity.org) or 202-466-3672.

Respectfully submitted,

Americans for Financial Reform