

April 17, 2017

Office of Regulations and Interpretations
Employee Benefits Security Administration,
Room N-5655
U.S. Department of Labor
200 Constitution Avenue, NW
Suite 400
Washington, DC 20210

By Email: EBSA.FiduciaryRuleExamination@dol.gov

Attention: Fiduciary Rule Examination

Re: **Comments Regarding the Definition of the Term "Fiduciary;"
Conflict of Interest Rule – Retirement Investment Advice RIN 1210-AB79**

Dear Sir or Madam:

Allianz Life Insurance Company of North America ("Allianz Life")¹ appreciates the opportunity to provide comments on the questions of law and policy raised by

- President Donald Trump in a memorandum dated February 3, 2017; and
- the Department of Labor (the "DOL") in Release RIN 1210-AB79 and RIN 1210-AB32,

regarding the DOL's above-referenced, recently promulgated fiduciary rule (the "Fiduciary Rule"), in which the DOL defines who is a "fiduciary" under the Employee Retirement Income Security Act of 1974, the Internal Revenue Code of 1986, and related prohibited transaction exemptions.

Summary of Comments

- Allianz strongly supports the concept of a "best interest standard" across the financial services industry, applicable both to non-tax qualified retirement assets and to IRA accounts.
- However, the overall approach of the Fiduciary Rule is misguided and the Rule needs to be substantially revised.
- The DOL is not the best suited party to promulgate a rule with the breadth and significance of the Fiduciary Rule.
- Any rules establishing a best interest standard across the financial services industry should be promulgated by the SEC (and, with regard to insurance products, the NAIC).
- The Fiduciary Rule's emphasis on fee-based financial services may actually harm, not benefit, many consumers.
- The Fiduciary Rule has already resulted in potentially unintended negative consequences for consumers.
- The Fiduciary Rule suffers from a "one size fits all" approach.

¹ Allianz Life is a life insurance company that offers a portfolio of individual annuities and life insurance products. Allianz Life is a subsidiary of Allianz SE.

- Even more fundamentally, we do not believe that the Fiduciary Rule adequately addresses the most important retirement security issues over the next ten years, i.e., retirement plan payout and annuitization.
- We also believe that the Fiduciary Rule should provide for standardized, template risk and conflict of interest disclosures.
- Finally, private litigation should be removed as the main enforcement mechanism of the Fiduciary Rule.

Comments

Allianz strongly supports the concept of a "best interest standard" across the financial services industry, applicable both to non-tax qualified retirement assets and to IRA accounts. Such a rule has the potential to play an important part in both the long-term retirement planning of millions of Americans and the overall economic health of the United States.

However, the overall approach of the Fiduciary Rule is misguided and the Rule needs to be substantially revised. For this reason, we believe that the Fiduciary Rule should be rescinded and replaced. Among other things, we believe that the DOL did not obtain adequate input from other regulatory agencies with substantial experience and expertise in the financial services and retirement planning areas. For this and other reasons, the Fiduciary Rule in its current form is fundamentally structurally flawed. Implementation of the Rule will result in substantial dislocation of the financial services industry, and will subject consumers to significant and unclear risk, including a risk of increased costs; reduced availability of financial advice; and limited product choice.

The DOL is not the best suited party to promulgate a rule with the breadth and significance of the Fiduciary Rule. The Fiduciary Rule as currently framed affects IRA accounts, registered investment advisers, registered broker-dealers, licensed insurance agents, individual stocks and bonds, mutual fund products, and insurance products such as fixed annuities, variable annuities, and index annuities, among other things. While the DOL has expertise in certain aspects of financial management and retirement planning, we believe that, overall, other regulatory bodies are better suited to develop and enforce a Fiduciary Rule that touches so many aspects of the financial services industry.

Any rules establishing a best interest standard across the financial services industry should be promulgated by the SEC (and, with regard to insurance products, the NAIC). Among other things, the SEC has 80 years of experience in regulating fiduciary financial services professionals, through the Federal Investment Advisers Act of 1940. Rulemaking by the SEC should extend generally to securities products and services. With regard to insurance products, the NAIC should also be actively involved in the design of any new model regulations impacting these types of products. The state insurance regulators represented by the NAIC have over a century of experience regulating insurance products, those that are securities and those that are fixed products.

The Fiduciary Rule's emphasis on fee-based financial services may actually harm, not benefit, many consumers. The Fiduciary Rule appears to favor fee-based financial service arrangements over commission-based arrangements. While fee-based arrangements may be in the best interests of consumers in a number of situations, we believe that other consumers may be better served by

commission-based arrangements. Specifically, commission-based arrangements may better serve consumers who seek transactional assistance regarding a specific investment, but who are not looking for significant ongoing advice, and want to adopt a “buy and hold” strategy. In contrast, fee-based arrangements may better serve consumers who want significant ongoing advice from a fiduciary, and also want advice and assistance in integrating all of the consumer’s assets.

We believe that the DOL’s “one size fits all” approach favoring fee-based arrangements is short-sighted and substantially understates the costs to consumers of fee-based arrangements over the long term (e.g., 10 or 20 years). For example, assuming a consumer purchases a commission-based variable annuity, and holds it for 20 years, the Financial Professional would receive a commission of approximately 6-7% (or would receive a lower commission plus a trail commission). However, if the consumer purchases a fee-based annuity and pays his/her investment adviser an annual fee of 1%, assuming a 5% discount rate the consumer would over 20 years pay fees with a present value of 12.5 to 13%. Put simply, fee-based arrangements work better for some consumers while commission-based arrangements work better for other consumers, and individual consumers should be given the choice of selecting the arrangement that works best for them.

The Fiduciary Rule has already resulted in potentially unintended negative consequences for consumers. We believe that further study and input is essential for any best interest standard rule that has the range and significance of potential effects of the Fiduciary Rule. The potential ramifications of the Fiduciary Rule have already begun to be felt in the market place and include, among other things, the following:

- It is highly likely that consumer choice in financial products and services will be reduced, and access to financial professionals will be reduced particularly for consumers with lower net worth. Many fee based advisers have significant account minimums, and if access to commission-based products and Financial Professionals is reduced, this will preclude many consumers from receiving essential retirement advice. In addition, as a result of increased compliance costs caused by the Fiduciary Rule, costs for financial services will increase² which likely also will put retirement planning services out of reach for less affluent customers.
- We note that the Fiduciary Rule has already begun to have market effects, which may or may not be in the best interest of consumers. For example, certain broker-dealers have announced they will discontinue sales of commission-based products.³ As noted above, we believe there is a strong argument that, in certain situations, fee-based products may be contrary to the best interest of some consumers over the long term.
- Further, we note that the Fiduciary Rule has resulted in the proliferation of different, new types of product share classes, such as “T shares” and “clean shares.” Notably, this wholesale restructuring of product design and pricing is being driven largely by the Fiduciary Rule rather

² See, *Batkins, Fiduciary Rule Has Already Taken Its Toll: \$100 Million in Costs, Fewer Options*, Insight, February 22, 2017.

³ Morningstar, *Cost of Fiduciary Rule Underestimated*, Feb. 9, 2017 at <http://news.morningstar.com/articlenet/article.aspx?id=793268>.

than by consumer demand -- a consequence that may result in increased industry confusion, both on the part of Financial Professionals and on the part of consumers.

The Fiduciary Rule suffers from a "one size fits all" approach. Further, because the DOL lacks expertise in areas such as, for example, the annuity industry, the Fiduciary Rule appears to be based in part on unwarranted concerns with established insurance industry concepts. The DOL may not fully realize the reasons for these long-established practices.

For example:

- In discussing the Fiduciary Rule, the DOL repeatedly expresses concerns about "excessive trading" to generate commissions. This concept is largely inapplicable to annuity products. For example, transfers of assets between allocation options available within an annuity are typically done in a no-tax, no-charge manner to the consumer and do not generate commissions to the Financial Professional.
- The DOL appears to be concerned that certain types of annuities permit credited rates and "caps" to be changed annually during the surrender charge period. We believe this concern is misplaced. Adjustment of credited rates and caps is a fundamental component of annuity issuance, risk management, and pricing. This sort of risk management has gone on in the annuity industry, with the concurrence of state insurance regulators, for approximately a century, and has proven to be an effective mechanism to define risk and product pricing. The insurance industry and insurance regulators do not view this widespread and accepted practice as inherently problematic.
- Because of the Fiduciary Rule's one-size-fits-all approach, the Rule is not a good "fit" for certain parts of the financial services industry, and has the potential to lead to significant negative effects on both Financial Professionals and consumers. Specifically, we believe the Fiduciary Rule will create substantial dislocations in the fixed (i.e., non-securities) part of the annuity industry, and will negatively affect many of the smaller insurance producers who sell these products. This portion of the financial services industry is heavily populated by small businesses and relatively less affluent consumers. The DOL's attempt to address this problem in its proposed Best Interest Contract Exemption for Insurance Intermediaries, created such onerous requirements that by the DOL's own estimate, only 19 large insurance intermediaries would qualify for the exemption.⁴ Thus, many consumers who depend on this segment of the financial services industry will be deprived of the products and retirement services furnished by these Financial Professionals.

Even more fundamentally, we do not believe that the Fiduciary Rule adequately addresses the most important retirement security issues over the next ten years, i.e., retirement plan payout and annuitization. This is a significant structural flaw that we believe makes the Fiduciary Rule in its current form materially deficient. As stated in our earlier comment letter regarding the DOL's

⁴ Proposed Best Interest Contract Exemption for Insurance Intermediaries, 82 Fed. Reg. 7,336 at 7,361 (Proposed January 19, 2017).

proposed rule, dated July 21, 2015 (“Allianz Life Comment Letter”):

“It is generally acknowledged that there is a significant need to make lifetime income options available to plan participants and IRA owners. The United States Government Accountability Office (the GAO) has gone so far as to encourage the purchase of annuities for retirement planning....

In its June 2011 report on Retirement Income, submitted to the Chair of the U.S. Senate Special Committee on Aging, the GAO warned that “holding stocks and bonds leaves households exposed to the financial uncertainty in financial markets over an unknown number of retirement years” and noted the adverse impact for retirees if they need to begin taking income after the value of their investments has declined. The report further noted that experts recommended that retirees draw down their reserves at a systematic rate and that this process “should be a part of a larger strategy that includes a certain amount of lifetime retirement income (such as Social Security, defined benefit, and annuity income).” The report went on to say that experts generally recommended “income annuities, in conjunction with systematic drawdown of other savings, to provide a greater level of retirement income security.”

Allianz Life Comment Letter at pages 6 and 10.

The retirement plan payout and annuitization issue could be addressed, for example, through regulatory changes that provide standardized disclosure as to payout options. Additionally, revisions should be made to the current form of the Fiduciary Rule that give consumers greater, not less, access to insurance producers who specialize in providing retirement services and payout type products, such as fixed annuities and fixed index annuities.

We also believe that the Fiduciary Rule should provide for standardized, template risk and conflict of interest disclosures. The original proposal for the Fiduciary Rule took the approach of relying heavily on personalized, highly complex, and largely unworkable risk and conflict of interest disclosures. This approach defeats the purpose of comparability of disclosures, and would be confusing to consumers. We believe that outlines for consumer disclosure templates that facilitate comparability of disclosure should be prepared and authorized by applicable regulators. As an example of this sort of regulation, the investment advisory industry, which is regulated primarily by the SEC, is regulated in large part by standardized conflict of interest disclosure in the adviser’s Form ADV. Again, with its expertise in the financial services industry, including responsibility for investment risk disclosure, conflict of interest disclosure, and fiduciary regulation, the SEC is the best situated agency to prepare these templates for securities products and services, while state insurance regulators, working in alignment with the SEC, would be best suited to create disclosure templates for the insurance industry.

Finally, private litigation should be removed as the main enforcement mechanism of the Fiduciary Rule. In President Trump’s February 3, 2017 memorandum, the Secretary of Labor is directed to

“publish for notice and comment a proposed regulation rescinding or revising” the Fiduciary Rule if the DOL makes an affirmative determination that:

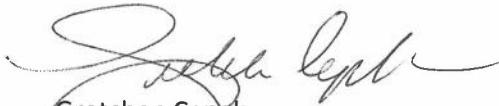
“... the Fiduciary Regulation is likely to cause an increase in litigation, and an increase in the prices that investors and retirees must pay to gain access to retirement services. “

The Fiduciary Rule is widely believed to be a magnet for litigation, both legitimate and non-legitimate. This problem is exacerbated by the fact that the Fiduciary Rule is replete with standards and terms that are unclear and prone to subjective interpretation, such as “reasonable compensation,” “material conflicts,” and “best interest standard.” As a result of this lack of clarity, the number of customer disputes will likely rise, leading to an increase in litigation. In fact, because the Fiduciary Rule by its very design relies on private litigation as its primary enforcement mechanism, it is virtually certain that litigation will increase under the Rule. Morningstar has estimated that the long-term annual costs associated with class action lawsuits stemming from the Fiduciary Rule is between \$70 and \$150 million. These costs will undoubtedly be passed on to consumers in the form of higher priced financial products and services -- clearly, an undesirable result for consumers, particularly less affluent consumers.

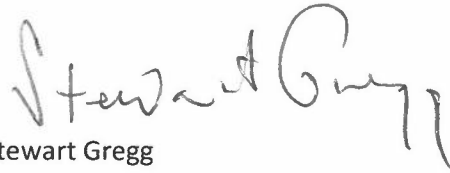
In view of the foregoing, the Fiduciary Rule must be rescinded and replaced by a new rule that does not rely on private litigation as its primary means of enforcement. As noted in an earlier Allianz Life submission on the proposed Fiduciary Rule, we do not believe the Fiduciary Rule should be a “trap for the unwary” that foments unnecessary consumer disputes.

Allianz Life appreciates the opportunity to provide comments on the Fiduciary Rule. Should the DOL have any questions, please contact us.

Sincerely,



Gretchen Cepek
Sr. Vice President, General Counsel
gretchen.cepek@allianzlife.com
763-765-5311



Stewart Gregg
Sr. Counsel
stewart.gregg@allianzlife.com
763-765-2913