Allianz
For all that's ahead.℠

August 7, 2017

Email: EBSA.FiduciaryRuleExamination@dol.gov

Office of Exemption Determinations
Employee Benefits Security Administration (Attention: D-11933)
U.S. Department of Labor
200 Constitution Avenue, NW
Suite 400
Washington, DC 20210

Re: Request for Information, RIN 1210-AB82

Dear Sir or Madam:

Allianz Life Insurance Company of North America ("Allianz Life")[1] appreciates the opportunity to provide these comments in response to the Request for Information (the "RFI"),[2] in connection with the Department of Labor's (the "Department") examination of the final Fiduciary Rule, which seeks public input that could form the basis of new exemptions or changes/revisions to the Fiduciary Rule, the Best Interest Contract Exemption (the "BIC Exemption"), the Class Exemption for Principal Transactions in Certain Assets Between Investment Advice Fiduciaries and Employee Benefit Plans and IRAs, and Prohibited Transaction Exemption 84-24 ("PTE 84-24").

EXECUTIVE SUMMARY

We strongly support the concept of a "best interest standard" across the financial services industry, applicable both to non-tax qualified and tax qualified retirement assets, as we have stated in our prior comment letters. However, the overall approach of the Fiduciary Rule is misguided, and the Fiduciary Rule needs to be substantially revised to avoid subjecting retirement savers and financial institutions to significant and unclear risk, including: a risk of increased costs; reduced availability of financial advice; increased litigation costs; and limited product choice.

The following is a summary of our comments and recommendations in response to select questions contained in the RFI.

1) Incorporation of Securities Regulation.
The Department should coordinate with the Securities and Exchange Commission ("SEC"), the Financial Industry Regulatory Authority ("FINRA") and state insurance and securities regulators, through the National Association of Insurance Commissioners ("NAIC")[3] and the North American

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[1] Allianz Life is a life insurance company that offers a portfolio of individual annuities and insurance products. Allianz SE is the ultimate parent company of Allianz Life.
[2] Any capitalized terms not defined herein will have the meaning set forth in the RFI.
[3] The NAIC is the standard-setting and regulatory support organization created and governed by the chief insurance regulators from the 50 states, the District of Columbia and five U.S. territories.

Securities Administrators Association ("NASAA"),[4] respectively, to adopt a uniform best interest standard applicable to both qualified and non-qualified retirement assets.

2) Contract Requirement in BIC Exemption.
The contract requirement and warranties in the BIC Exemption are not necessary to motivate compliance with the Impartial Conduct Standards, and should be eliminated.

3) Alternative Streamlined Exemption and PTE 84-24.
The 2006 version of PTE 84-24, as amended to add the Impartial Conduct Standards ("Amended PTE 84-24"), should remain available for all annuities, including fixed index annuities and variable annuities.

4) Disclosure Requirements.
The Department should work with the financial services industry's regulators to simplify the disclosure requirements under the BIC Exemption and PTE 84-24.

RESPONSES TO SELECT QUESTIONS

Incorporation of Securities Regulation

> *If the SEC or other regulators were to adopt updated standards of conduct applicable to the provision of investment advice to retail investors, could a streamlined exemption or other change be developed for advisers that comply with or are subject to those standards? To what extent does the existing regulatory regime for IRAs by the SEC, self-regulatory bodies (SROs) or other regulators provide consumer protections that could be incorporated into the Department's exemptions or that could serve as a basis for additional relief from the prohibited transaction rules?*[5]

We support a uniform best interest standard applicable to all account types and insurance products. Regulatory coordination could help avoid unintended and inconsistent treatment between federal and state regulators, both in terms of defining a uniform best interest standard and enforcing it. We urge the Department to work together with the financial services industry's regulators to create consistency. These regulators include the SEC, FINRA, and state insurance and securities departments. We do not believe the Department adequately consulted with all of these regulators before adopting the Fiduciary Rule.

Even before the Fiduciary Rule took effect, the Government Accountability Office ("GAO") found the regulatory structure in place to be fragmented among multiple agencies that have overlapping authorities. According to a GAO report[6] released last year, fragmentation, overlap and duplication in the financial regulatory structure introduce significant challenges for efficient and effective oversight.

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[4] NASAA is the association of state and provincial securities regulators. NASAA membership consists of 67 state, provincial, and territorial securities administrators in the 50 states, the District of Columbia, the U.S. Virgin Islands, Puerto Rico, Canada and Mexico.

[5] RFI Question 11

[6] U.S. Governmental Accountability Office. (2106, February). Financial Regulation: Complex and Fragmented Structure Could Be Streamlined to Improve Effectiveness. (Publication No. GAO-16-175).

Efficient and effective oversight includes eliminating overlapping federal regulatory missions where appropriate and minimizing regulatory burden without sacrificing effective oversight. We believe consumer protections work best when consumers receive consistent, useful information and legal protections for similar financial products and services.

Under the Fiduciary Rule, the Department would further fragment the existing regulatory structure by adding new compliance requirements, as well as extending oversight to the Department and Internal Revenue Service ("IRS"). This fragmentation will cause further regulatory overlap. For example, the Fiduciary Rule would require additional, and in many cases, overlapping disclosures on top of existing disclosures under other regulatory requirements. Department and IRS oversight would also be duplicative in terms of regulating market conduct that is already overseen by the SEC, FINRA, state insurance and securities departments.

We urge the Department to work together with all of the financial services industry's regulators to assure regulatory consistency and to adopt regulations that are as workable as possible. We note that the SEC and the NAIC are currently and separately engaged in efforts to establish a best interest standard of care. The SEC's Chairman, Jay Clayton, recently issued a public statement[7] in which he asked for public comments to help the SEC "evaluate the range of potential regulatory actions" as authorized by the Dodd Frank Wall Street Reform and Consumer Protection Act. The NAIC has also formed the Annuity Suitability Working Group (the "Suitability Work Group") to consider revisions to the NAIC Suitability in Annuity Transactions Model Regulation (the "Suitability Model") to possibly include a best interest standard of care. We were pleased to hear Employee Benefits Security Administration Assistant Secretary Timothy Hauser's comments on the NAIC Suitability Working Group's July 26, 2017 call, in particular, that the "door is open" and the Department is "happy to work with [the NAIC]." We encourage the Department to continue its outreach to the NAIC as it reevaluates the Fiduciary Rule and its exemptions. Unlike the Fiduciary Rule, which applies only to recommendations made with respect to qualified retirement assets, NAIC involvement in the Department's coordination efforts would promote the establishment of a consistent conduct standard for all insurance products and account types, including non-qualified accounts and insurance products that are not securities.

Finally, the Department should coordinate with state securities departments by engaging NASAA. NASAA would offer valuable perspective from its work with state securities regulators to protect investors and help maintain the integrity of the securities industry under state securities laws. NASAA has communicated its commitment to establishing a best interest standard governing the conduct of broker-dealers that is consistent with the best interest standard applicable to investment advisers.

Contract Requirement in BIC Exemption

> *What is the likely impact on Advisers' and firms' compliance incentives if the Department eliminated or substantially altered the contract requirement for IRAs? What should be changed? Does compliance with the Impartial Conduct Standards need to be otherwise incentivized in the absence of the contract requirement and, if so, how?*[8]

[7] Available at https://www.sec.gov/news/public-statement-chairman-clayton-2017-05-31.
[8] RFI Question 5

> *What is the likely impact on Advisers' and firms' compliance incentives if the Department eliminated or substantially altered the warranty requirements? What should be changed? Does compliance with the Impartial Conduct Standards need to be otherwise incentivized in the absence of the warranty requirement and, if so, how?*[9]

We do not believe the contract requirement and warranties in the BIC Exemption are necessary to motivate compliance with the Impartial Conduct Standards and recommend that they be eliminated. The Impartial Conduct Standards alone provide significant protections to retirement savers. Additionally, there are already robust and effective enforcement mechanisms in place with the SEC, FINRA and the state insurance and securities departments to protect retirement savers. We have consistently urged the Department to work with all the financial services industry's regulators to adopt a uniform best interest standard applicable to all account types and insurance products. Doing so would help ensure regulatory consistency. With a uniform best interest standard that is enforced by the SEC, FINRA and state insurance and securities departments there is no need for the BIC contract and warranties.

The enforcement tools currently available to these regulators include the authority to commence investigations of violations, pursue administrative proceedings, bring civil actions in court in appropriate circumstances, impose fines, and suspend or revoke the licenses of violators. They include customer tip lines and complaint programs that are relied on as an early warning system to detect compliance problems and violations. These regulators may also have the authority to refer complaints to the Department of Justice or law enforcement for criminal prosecution, as appropriate. Institutions that are subject to these regulations must comply with their existing duties and responsibilities and remediate failures to comply in order to avoid punitive measures being imposed.

The contract and warranty requirements are widely believed to be magnets for litigation, both legitimate and non-legitimate. This problem is exacerbated by the fact that the Fiduciary Rule and related exemptions are replete with standards and terms that are unclear and prone to differing interpretations, such as "reasonable compensation" and "material conflicts." As a result of this lack of clarity, the number of customer disputes would likely rise, leading to an increase in litigation. In February 2017, Morningstar estimated the long-term annual costs associated with class action lawsuits stemming from the Fiduciary Rule to be between $70 and $150 million.[10] These costs would undoubtedly be passed on to retirement savers in the form of higher priced financial products and services -- clearly, an undesirable result for retirement savers.

Based on the foregoing, we respectfully request that the Department eliminate these requirements from the BIC Exemption.

<u>*Alternative Streamlined Exemption and PTE 84-24*</u>

> *Clean shares, T-shares, and fee-based annuities are all examples of market innovations that may mitigate or even eliminate some kinds of potential advisory conflicts otherwise associated with recommendations of affected financial products. These innovations might also increase transparency of advisory and other fees to retirement investors. Are there other innovations that*

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[9] RFI Question 6

[10] Morningstar, Cost of Fiduciary Rule Underestimated, Feb. 9, 2017 at http://news.morningstar.com/articlenet/article.aspx?id=793268

> *hold similar potential to mitigate conflicts and increase transparency for consumers? Do these or other innovations create an opportunity for a more streamlined exemption? To what extent would these innovations address the same conflicts of interest as the Department's original rulemaking?*[11]
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> *If the Department provided an exemption for insurance intermediaries to serve as Financial Institutions under the BIC Exemption, would this facilitate advice regarding all types of annuities? Would it facilitate advice to expand the scope of PTE 84-24 to cover all types of annuities after the end of the transition period on January 1, 2018? What are the relative advantages and disadvantages of these two exemption approaches (i.e., expanding the definition of Financial Institution or expanding the types of annuities covered under PTE 84-24)? To what extent would the ongoing availability of PTE 84-24 for specified annuity products, such as fixed indexed annuities, give these products a competitive advantage vis-à-vis other products covered only by the BIC Exemption, such as mutual fund shares?*[12]

The Department asks for comment on a special exemption for fee-based annuities. Creating additional exemptions tied to specific products is unnecessary and would be detrimental to retirement savers. Annuities are the only products offering guaranteed lifetime income and therefore should all be treated the same under Amended PTE 84-24. As we pointed out in our April 2017 letter to the Department, commission-based arrangements may better serve retirement savers 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 retirement savers who want significant ongoing advice from a fiduciary, and also want advice and assistance in integrating all of the retirement saver's assets.

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

Allowing Amended PTE 84-24 exemption to continue in its current form with respect to all annuities would avoid confusion for retirement savers and enable financial professionals to comply with the Fiduciary Rule and Amended PTE 84-24. The availability of alternative exemptions could cause the financial professional to steer retirement savers to fee-based annuities when they would be better off with a commission-based product. Or, the financial professional could cease selling certain insurance products to avoid the added compliance costs. Also, making Amended PTE 84-24 permanent for all annuities would alleviate the need for an exemption specific to insurance marketing intermediaries. The addition of the Impartial Conduct Standards to PTE 84-24 provides retirement savers with significant

[11] RFI Question 9
[12] RFI Question 17

protections to ensure that the advice they receive regarding their purchase of an annuity is in their best interest.

Disclosure Requirements

> *Are there ways to simplify the BIC Exemption disclosures or to focus the investor's attention on a few key issues, subject to more complete disclosure upon request? For example, would it be helpful for the Department to develop a simple up-front model disclosure that alerts the retirement investor to the fiduciary nature of the relationship, compensation structure, and potential sources of conflicts of interest, and invites the investor to obtain additional information from a designated source at the firm? The Department would welcome the submission of any model disclosures that could serve this purpose.*[13]

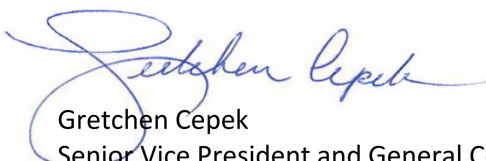
The Department should simplify the disclosure requirements. The point-of-sale, website, annual and ongoing information maintenance requirements of the BIC Exemption will lead to consumer confusion. In addition, these mandates impose exceedingly burdensome and expensive disclosure requirements on annuity product providers, distributors and financial institutions. The disclosure requirements of the BIC Exemption are duplicative in some respects with the disclosures required under federal securities laws and state insurance laws and regulations.

The Department should design a simplified disclosure for registered representatives, investment advisers, and insurance agents alike to use with retirement savers. This disclosure should explain to the retirement saver in what capacity the financial professional is acting, broadly describe how he/she is compensated, and set forth potential material conflicts of interest. We believe this disclosure should be modeled after the disclosure required under Amended PTE 84-24, which is currently in use until January 1, 2018. A simplified disclosure document would ensure that the retirement saver's attention is focused on the most important information in connection with the advice recommendation.

We understand that the NAIC may include a disclosure requirement in connection with its revisions to the Suitability Model. The SEC also is considering whether to adopt a uniform plain English disclosure document to be provided to customers of both broker-dealers and investment advisers at the start of the engagement. Retirement savers would receive more consistent, useful information if the Department would work with the financial services industry's regulators to simplify the disclosure requirement.

Allianz Life appreciates the opportunity to provide these comments and looks forward to constructive dialogue on these issues in the coming months.

Sincerely,



Gretchen Cepek
Senior Vice President and General Counsel

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[13] RFI Question 13