The Committee for the Fiduciary Standard

Via email to e-ORI@dol.gov re: RIN 1210-AB32

Office of Regulations and Interpretations July 20, 2015
Employee Benefits Security Administration
Attn: Conflict of Interest Rule
U.S. Department of Labor
200 Constitution Avenue NW
Washington, DC 20210.

Re: Definition of the Term "Fiduciary"; Conflict of Interest Rule - Retirement Investment Advice. Document No. 2015-08831, RIN 1210-AB32

Ladies and Gentlemen,

We write in support of the Department of Labor's Conflict of Interest Rule

Thank you for the opportunity to comment on the Department of Labor's Conflict of Interest proposal. We appreciate the thoughtful, substantive approach and the intellectual rigor that so many individuals have contributed to this effort. In particular, we would like to thank the White House and the DOL for making this rulemaking a priority. We appreciate the leadership of Labor Secretary Thomas Perez and Asst. Secretary Phyllis Borzi, and their fearless, resolute team. Their collective efforts will have an enduring and positive effect on millions of Americans.

The courage and commitment of the White House and DOL to make these proposed rules a priority is vital to helping to ensure that millions of American working and investing for a secure, dignified retirement will keep more of their nest egg.

This is especially significant in light of the current environment in Washington – since 2009 but in a most acute campaign at this moment – in which insurance and Wall Street special interests are attempting to overrun Washington with enormous amounts of money and propaganda to fight off the DOL's proposal, and retain the status quo and the enormous profits to firms at a directly correlated cost to retirement investors. The status quo carries with it short- and long-term negative impacts on the American economy.

Thank you also for covering IRA rollovers and IRA retirement investors in this proposal. This vitally important life transition – many retirement investors' most vulnerable point – needs and deserves every aspect of fiduciary duty and care. We appreciate that the DOL has issued a significant proposed rule covering so many retirement investors, many of whom have not been beneficiaries of fiduciary advice. The current rules are ineffective in preventing harm to IRA owners and especially that most vulnerable, infrequent decision about whether or not to roll over retirement plan assets into IRAs. Millions of American retirement investors would, once the proposal is effective, have the benefit of advice that is in their "Best Interest" – fiduciary advice.

We also appreciate the continued "special emphasis," as DOL's proposal puts it, "on the elimination or mitigation of conflicts of interest and adherence to substantive standards of conduct as reflected in the prohibited transaction rules and ERISA's standards of fiduciary conduct."

"The specific duties imposed on fiduciaries by ERISA and the Code stem from legislative judgments on the best way to protect the public interest in tax-preferred benefit arrangements that are critical to workers' financial and physical health. The Department has taken great care to honor ERISA and the Code's specific text and purposes."

We support the elimination of conflicts of interest and mitigating conflicts, by which we mean *managing unavoidable conflicts of interest in the investor's favor*.

Please call upon us for our individual and collective areas of fiduciary expertise, best practices and processes during this vitally important rulemaking.

Sincerely,

Kathleen M. McBride, AIFA®
Chair, The Committee for the Fiduciary Standard, www.TheFiduciaryStandard.org
Accredited Investment Fiduciary Analyst®, CEFEX Analyst
Centre for Fiduciary Excellence, www.CEFEX.org
732.241.4988 kmcbride@FiduciaryPath.com

Members of The Committee for the Fiduciary Standard Steering Group

Clark M. Blackman II, CPA/PFS, CFA, CFP®, CIMA®, AIF® is founder, president and CEO of Alpha Wealth Strategies, LLC

Harold Evensky, CFP®, is Chairman, Evensky & Katz and Professor of Practice, Texas Tech

Sheryl Garrett, CFP® is founder of the Garrett Planning Network, a national organization of hourly based, fee-only financial advisors.

Roger C. Gibson, CFA, author of the investment classic, Asset Allocation: Balancing Financial Risk and founder and Chief Investment Officer of Gibson Capital, LLC

Tim Hatton CFP, AIF®, is Founder and President of Hatton Consulting, author, The New Fiduciary Standard

Patricia P. Houlihan, CFP® is President and Owner of Houlihan Financial Resource Group, Ltd.

Deena Katz, CFP®, Associate Professor in the Personal Financial Planning Division at Texas Tech University, in Lubbock, Texas. She is also Co-Chairman and a founding partner of Evensky & Katz.

Ron A. Rhoades, JD, CFP, Program Director, Financial Planning, Asst. Professor of Finance, Gordon Ford School of Business, Western Kentucky University, President of ScholarFi, Inc., an investment advisory firm, and President of Ron A. Rhoades, P.A., a law firm.

Ronald W. Roge, MS, CFP®, is a nationally recognized fee-only wealth manager. He is founder, Chairman, and CEO of R. W. Roge & Company, Inc.

I. Public Policy on Retirement in America – The Current Landscape

From a public policy perspective, Americans saving and investing for retirement have been forced, without requisite training, into the role of "portfolio manager" for one of the most critical elements of financial security – their retirement. This is no small issue. Rather, it is akin to asking someone to remove their own appendix, defend himself or herself in court, or interpret a complex issue in the tax code. One needs professional and technical knowledge in order to practice any of those professional endeavors. In fact, regular individuals are not allowed to do any of those things without proper training.

Yet, we demand that individuals do just that, when making decisions about their retirement accounts.

What was supposed to be an adjunct savings vehicle, meant to *supplement* an individual's employer pension plan – the traditional monthly payment to the retiree for life, is now, for most Americans, the primary vehicle in which to save and invest for retirement. Funding risk, investment risk, and distribution risk, all risks formerly borne by the employer, now rest on the shoulders of the individual employee. Professional, institutional, pension fund management as a responsibility of the employer, is, for most Americans, gone.

Americans are captive in their employer's 401(k)-type plan. For some investors, when the plan is well run, investment alternatives are high quality and lower cost. But for too many retirement investors, the opposite is true – lower quality, high cost investment alternatives dominate, undermining American retirement investors' nest eggs from the start.

As individuals began saving and investing in 401(k)-type and IRA accounts, fund companies, banks, brokers, insurance companies and registered investment advisory firms; and recordkeepers and third-party administrators (TPAs) benefited from the investment vehicles used and/or from the advisory services rendered.

The Employee Retirement Income Security Act of 1974 (ERISA) is the federal law that sets minimum standards for most voluntarily established pension and health plans in private industry to provide protection for individuals in these plans.

In 1974, when ERISA was enacted, nobody would have predicted that the primary retirement investment vehicles in the United States in 2015 would be, rather than traditional pensions, these adjunct, side pocket accounts – 401(k)-type and IRA accounts. And nobody could have foreseen how the regulations enacted then would be systemically abused or skirted in order to cull revenue for firms and individuals who were to be serving retirement investors.

But the fact remains that many investors in these accounts are being steered into high commission and high fee investment vehicles, through the guise of "advice" that is *not* in the investor's best interest.

Why Fiduciary Advice Is A Necessity, not a Luxury

Fiduciary law came about because when an individual entrusted their property to another who had specialized, professional knowledge that the lay person did not have. The "professional" had to care for that property as if it were his or her own. The entrusted property was not to be used for the gain of the professional but to be managed in the best interest of the individual. The professional could be paid a reasonable amount for the work they did and the knowledge, skill, diligence and expertise they possessed. But the work they did was required to be in the best interest of the individual “entrustor”.

Now, when an individual, who does not possess anywhere near the level of professional knowledge that in investment professional does, invests for their retirement, this “fiduciary” concept should hold true for the advice they receive. And it does, when a retirement investor is serendipitously fortunate enough to receive that advice from a fiduciary.

But all too often, professionals and companies seeking personal or corporate gain from pretending to “advise” retirement investors, (plans, participants, beneficiaries or IRA owners), have taken advantage of unintended loopholes in ERISA. These loopholes led to systemic conflicts of interest that let these professionals to put their own personal or corporate interests ahead of the best interests of the retirement investors they were meant to serve.

These are the loopholes that Department of Labor proposes to, and must, close.

"This boils down to a very simple concept: if someone is paid to give you retirement investment advice, that person should be working in your best interest," said Secretary of Labor Thomas E. Perez. "As commonsense as this may be, laws to protect consumers and ensure that financial advisers are giving the best advice in a complex market have not kept pace. Our proposed rule would change that. Under the proposed rule, retirement advisers can be paid in various ways, as long as they are willing to put their customers' best interest first."

We agree.

Private Taking of Retirement Investor Assets and Economic Harm

With $7.2 Trillion in IRA accounts and another 5.3Trillion in 401(k)-type retirement there is a tremendous amount at stake for America’s retirement investors.

As DOL points out, “A wide body of economic evidence supports a finding that the impact of these conflicts of interest on retirement investment outcomes is large and, from the perspective of advice recipients, negative.”

We appreciate the DOL’s careful analysis of the abundant data, including, “among other things, statistical analyses of conflicted investment channels, experimental studies, government reports documenting abuse, and basic economic theory on the dangers posed by conflicts of interest and by the asymmetries of information and expertise that characterize interactions between ordinary retirement investors and conflicted advisers. “

As DOL notes in the preamble to the Fiduciary proposal, the data “consistently points to substantial failures in the market for retirement advice, suggests that IRA holders receiving conflicted investment advice can expect their investments to underperform by an average of 100 basis points per year over the next 20 years. The underperformance associated with conflicts of interest – in the mutual funds segment alone – could cost IRA investors more than $210 billion over the next 10 years and nearly $500 billion over the next 20 years. Some studies suggest that the underperformance of broker-sold mutual funds may be even higher than 100 basis points, possibly due to loads that are taken off the top and/or poor timing of broker sold investments. If the true underperformance of broker-sold funds is 200 basis points, IRA mutual fund holders could suffer from underperformance amounting to $430 billion over 10 years and nearly $1 trillion across the next 20 years."

Necessity of Government Response if Status Quo Continues

We note that the DOL has been very conservative in its estimates of the harm to retirement investors of current retirement advisory rules, set up for a very different retirement landscape in America.

That shortfall to retirement investors, of $1 Trillion dollars (just in one segment, mutual funds, in one retirement vehicle, IRAs) is unworkable and unacceptable. Many well respected thought leaders and experts in retirement investing lean toward the higher, 200 basis points per year underperformance. When you add in other types of investment alternatives in IRAs, such as annuities, where the costs to investors are much higher, 4% to 10%, and another 7% to 10% in penalties the actual retirement investor shortfall is likely to be much higher.

Add in the impact of conflicted advice in the $5.3 Trillion 401(k)-type retirement accounts, from higher than reasonable and often hidden commissions, fees, and backdoor revenue sharing payments among banks, brokers, mutual fund companies and insurance companies, and you soon have a setting that could easily approach a similar additional shortfall for retirement investors over the next 20 years.

One has to ask: **If private companies are allowed to continue extracting such a toll from retirement investors**, and retirement investors would be missing $1 to $2 Trillion from their retirement nest eggs, how will these retirement investors get by in retirement? **Who will make up this shortfall?** Would this mean that the federal government would need to engineer a bailout plan bigger than we've seen over the past eight years because private companies have extracted so much from retirement investor's nest eggs?

Variation of Retirement Plan Quality, and Captivity in Company 401(k)-type Plans

Since 401(k)-type plans are sponsored by companies, there is an element of serendipity in terms of plan quality. Most individuals have no way of examining the retirement plan as they take a position at a company, and plan sponsors sometimes change service providers. Though plan fiduciaries have fiduciary obligations to the plans and participants, quality and knowledge of plan fiduciaries, and plans themselves, varies widely from excellent to very poor.

As a captive to their company plan a participant may be fortunate to have access to a terrific plan, with fiduciary advice to the plan, prudent, high quality, lower cost actively managed and very low cost passively managed mutual funds and or ETFs -- or the plan may be at the opposite end of the spectrum: high cost, poorly performing, investment alternatives.

Small or startup plans, which have with fewer participants and, at least initially, smaller amounts of assets, are particularly vulnerable. They are often subject to very unreasonable fees, and often have less knowledgeable plan fiduciaries without adequate fiduciary knowledge, processes or training. This often leads to a poorly selected array of plan alternatives for participants to choose from, and an uninformed service provider selection process.

Participants in this kind of plan have no recourse unless they leave the company or retire. If they complain to plan fiduciaries, they risk retaliation, as the plan may be "run" by the CFO's golf buddy, for example.

Public Policy and The Privilege of Advising America's Retirement Investors

Is it good public policy to allow the continued taking of retirement assets from retirement investors, by private corporations, when the long-term effect would be the need to make up that shortfall by taxing Americans so that America's retirees are not impoverished?

Why not avoid this issue by acting now and requiring that all advice to retirement investors be in the investor's best interest?

It is time for every professional, and every company that has the privilege of advising retirement investors, to do so in the investor's best interest, as a fiduciary. It is good public policy. American workers are working hard to save and invest for retirement and they expect that the advice they are getting on their retirement investing is in their best interest.

Let us make it so.

II. Public Policy Recommendations

Safe Zone IRA

Recently, a policy discussion focused on the idea of a safe-zone IRA where participants who are captive in poorly run or expensive company 401(k)-type plans could rollover retirement assets that are vulnerable to erosion or worse. Ideally it would be federally run, perhaps an arm of the government employee Thrift plans, with no penalty for direct transfer in, and no minimum or limit on how much could be transferred in or how long they could stay. This is an idea worth pursuing.

Starting Retirement Plans Much Sooner

Another idea that is worth serious discussion and inclusion in this or additional rulemaking in ERISA is this: Make it easier for parents to start children off with retirement savings when they are very young. Whether the vehicle is a very low cost IRA or the ability for 401(k)-type plans add spouses and dependents, the idea of compounded growth starting 20-plus years earlier than when many adults begin retirement saving is appealing on many levels. One author and fiduciary expert, Christopher Carosa, articulates the idea in the article, "What Every 401(k) Plan Sponsor and Fiduciary Should Disclose to Employees: How to Retire a Millionaire, (Hint: It's Easier Than You Think.)"[1]

---

[1] Christopher Carosa, http://fiduciarynews.com/2014/02/what-every-401k-plan-sponsor-and-fiduciary-should-disclose-to-employees-how-to-retire-a-millionaire-hint-its-easier-than-you-think/

III. Comments on DOL Proposal: Definition of the Term "Fiduciary" Conflict of Interest Rule - Retirement Investment Advice

Coverage of IRAs

We are heartened to see DOL using its IRA Rulemaking Authority to cover advice to IRA owners under the proposed rules. We know firsthand the harm that, too often, is inflicted on retirement investors during the decision whether to roll over retirement savings into an IRA, or when the "advice" that is provided on the IRA account investments is not in the investor's best interest. "Advice" that is not in the investor's best interest is not actually advice.

Arguments from financial services and insurance company special interests that claim investors will not have access to "advice" if non-fiduciary firms are "forced" to provide advice that is in the investor's best interest, have no basis at all. As a point of fact, many firms espousing that line of protest are not serving retirement investors with smaller or mid-sized accounts at all. If they interact with these investors at all, it is primarily to steer them into the highest cost annuities or funds, not to provide advice.

This underscores why the proposed rules that eliminates the current ERISA five-part test of who is a fiduciary is so important. If one holds oneself out as an "adviser" (including any of the trust engendering titles and/or advertising) one must actually provide bona fide advice that is in the investor's best interest.

The provision for investor recourse via a private right of action (or class action) for IRA owners and on rollovers is vitally important to the financial wellbeing of America's retirement investors.

We agree with DOL: "If one engages in specified activities, such as the provision of investment advice for a direct or indirect fee, [or commission] the person engaging in those activities is a fiduciary, irrespective of labels."[2]

We agree with DOL that the DOL application of fiduciary duty for retirement advice should cover anyone who is providing advice to retirement investors, including broker-dealer registered representatives, investment advisers and their representatives, financial planners, and insurance company agents, representatives, consultants or producers – including any other assorted advisory titles that the broad financial industry uses, or may use in future.

To be clear: We support DOL in providing no carve-out from fiduciary duty when it comes to retail investors, including IRA owners, IRA rollovers, plan participants and beneficiaries and all but the very largest plans. We expect this will include any company or individual providing advice, or financial professionals: brokers, insurance agents, and planners, et al.

We support inclusion of advice on "other non-ERISA plans such as Health Savings Accounts (HSAs), Archer Medical Savings Accounts and Coverdell Education Savings Accounts other non-ERISA plans such as Health Savings Accounts (HSAs), Archer Medical Savings Accounts and Coverdell Education Savings Accounts, and agree it is appropriate that "these accounts are included in the scope of covered plans in paragraph (f)(2) of the new proposal."[3]

---

[2] "Definition of the Term "Fiduciary": Conflict of Interest Rule – Retirement investment Advice p 68
[3] Ibid, p 72

IV. Impact and Coordination of DOL Rulemaking Across Existing Business Models and Regulatory Schemes

We appreciate and support the care that DOL has taken to "to understand the impact of the proposed rule on firms subject to the securities laws and other federal laws, and to take the effects of those laws into account so as to appropriately calibrate the impact of the rule on those firms. The proposed regulation reflects these efforts. In the Department's view, it neither undermines, nor contradicts, the provisions or purposes of the securities laws, but instead works in harmony with them."

We support the care with which the DOL consulted with Treasury and IRS particularly on IRAs and the DOL's jurisdiction for rulemaking on IRAs: "The Department has also consulted with the Department of the Treasury and the IRS, particularly on the subject of IRAs. Although the Department has responsibility for issuing regulations and prohibited transaction exemptions under section 4975 of the Code, which applies to IRAs, the IRS maintains general responsibility for enforcing the tax laws. The IRS' responsibilities extend to the imposition of excise taxes on fiduciaries that participate in prohibited transactions.14 As a result, the Department and the IRS share responsibility for combating self-dealing by fiduciary investment advisers to tax-qualified plans and IRAs. Paragraph (e) of the proposed regulation, in particular, recognizes this jurisdictional intersection."

The Committee supports the application of a Best Interest Contract Exemption (BIC) to business models that include conflicts of interest that taint advice and cause harm to retirement investors. In particular, the Committee agrees that the BIC should require a stringent fiduciary standard rooted in ERISA and trust law, as DOL says: "As proposed, the best interest standard is intended to mirror the duties of prudence and loyalty, as applied in the context of fiduciary investment advice under sections 404(a)(1)(A) and (B) of ERISA. Thus, the "best interest" standard is rooted in the longstanding trust-law duties of prudence and loyalty adopted in section 404 of ERISA and in the cases interpreting those standards."

"Accordingly, the Best Interest Contract Exemption provides: Investment advice is in the "Best Interest" of the Retirement Investor when the Adviser and Financial Institution providing the advice act with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person would exercise based on the investment objectives, risk tolerance, financial circumstances and needs of the Retirement Investor, without regard to the financial or other interests of the Adviser, Financial Institution, any Affiliate, Related Entity, or other party." [4]

V. The Impact of Titles on Retirement Investors

As we discuss the impact of DOL rules on differing business models, we wish to comment on the impact of titles on retirement investors. We agree that any entity that provides advice to retirement investors must do so as a fiduciary – in the investor's best interest, no matter the business or compensation model.

That said, there could be specific improvements to retirement (and other) investor understanding as to the type of relationship they have with someone who advises them. Therefore we recommend *the elimination of titles that convey a relationship of trust and confidence for any financial professional who is not a fiduciary to all their clients at all times.* In

[4] DOL Fiduciary Proposal, p34-35

this sense, use of the titles adviser/or, counselor, and any others conveying a relationship of trust and confidence would automatically mean one is subject to all of the tenets of a fiduciary relationship and that the retirement investor would have, in addition to contractual recourse, fiduciary breach recourse in the event of harm.

In this sense, we include both the relationship under a written contract, as well as circumstances when no contract is used and advice is provided. (We recommend the practice of always using a contract that acknowledges fiduciary duty).

Financial professionals working with investors every day acknowledge that investors have trouble differentiating sales from advice. A recent survey[5] of professional intermediaries across business models and registration types – broker-dealer, investment adviser and insurance – indicates that investors are confused about the similar sounding titles financial professionals use. Most convey a relationship of trust and confidence, although many financial professionals are not required to put the interests of investors first, as fiduciaries.

The survey asked, “Do you believe the titles “advisor,” “consultant,” and “planner” imply that a fiduciary relationship exists?” Overall, 72% of survey participants say these titles imply a fiduciary relationship with clients. There is strong agreement across compensation models and registration types, including 73% of RIA/IARs, 75% of registered reps, 73% of dually registered, and 66% of dually registered-plus insurance respondents. When results are analyzed by compensation model, 73% of fee-only, and 69% of fee/commission respondents concur.

- 96% say clearer differentiation between product providers and advice providers is necessary
- 72% say the titles “advisor,” “consultant,” and “planner” imply that a fiduciary relationship exists

VI. Seller’s Carve Out --- For Very Large Plans Only

We agree that the seller’s carve-out should only apply to only very large plans that either have an in-house, full time, knowledgeable fiduciary or a contractual relationship with an independent fiduciary (with no tie to the seller).

We appreciate DOL’s thought process in not permitting the seller’s carve-out to include participant advice, advice on whether to rollover plan assets into an IRA and advice to IRA account holders – and we concur.

Very large plans *may* have the services of full-time or independent fiduciaries who possess the prudent expertise and are sophisticated and knowledgeable about their fiduciary duty to the plan, participants and beneficiaries, and possess deep knowledge and common sense about the kinds of securities that may be offered via the “Seller’s Carve out.” We understand DOL’s reasoning for offering the “Seller’s Carve-out.” However we caution that the use of “incidental advice” may be taken more broadly by some who advise plans and caution that the terms of use should remain *very narrow* and that the test of whether a plan indeed *has* a the capable expertise in house should be *very stringent*.

[5] 2015 fi360 Fiduciary Standard Survey Report, “Seeking Trustworthy Advice,” p 28 http://www.fi360.com/uploads/media/2015fiduciarysurvey.pdf

In addition, we are mindful of serious fiduciary breaches among very large, multibillion-dollar plans, even when it comes to something as simple as monitoring share classes for the appropriate institutional class with the most reasonable costs to participants, such as in Tibble v. Edison, to cite just one recent example. If DOL proceeds with this carve-out, *the effects of harm to participants from abuse of the seller's carve-out may be irrevocable.*

What Constitutes a Very Large Plan?

A concern remains on the size of the threshold for plans that may be considered to have sufficient in-house or external independent fiduciary knowledge. Is the threshold of $100 million in plan assets and 100 participants protective enough? A plan may have $10 million and 400 participants, and run by plan sponsor personnel with less fiduciary and technical knowledge. Or a plan may have $100 million in assets or billions in assets and not have sufficient expertise to truly protect participants from an unscrupulous seller.

We ask that DOL consider lifting the threshold of $100 million, 100 participants to a higher threshold, and clarify what will be required of a plan's fiduciary to ensure they can meet the challenge of arms-length sales transactions of what may be complex securities—for the sole benefit of the plan. What will be required for considering whether a plan has an in-house or outside independent fiduciary? How will DOL ascertain that the plan fiduciary possesses the plan fiduciary knowledge, as well as investment fiduciary knowledge, (which are quite different areas of expertise, in practice) to act solely in the interest of the participants, given the human tendency to overestimate one's skills and competence?

VII. Carve-out for Service Providers, Recordkeepers and Third-Party Administrators

Selection and monitoring of plan investments is crucial to the long-term success of plan participants' retirement goals, as much academic evidence has shown. The recent SCOTUS decision in Tibble v. Edison regards the duty to regularly monitor and replace imprudent investments as a fiduciary function: "Under trust law, a trustee has a continuing duty to monitor trust investments and remove imprudent ones. This continuing duty exists separate and apart from the trustee's duty to exercise prudence in selecting investments at the outset."

Many plan sponsors do not have prudent experts in-house to develop "objective criteria" for use in prudently selecting a plan's investment offerings. If they need help setting up the criteria they may need to engage a prudent expert. There may be overconfidence bias at many plans, or the feeling (as there is now in many cases, or we would not have to make this effort) that whomever they engage will "take care" of the plan. The "It's my brother-in-law," scenario. As we all know, that is not a prudent reason or process for choosing a service provider.

A seller's carve-out for TPAs and Recordkeeper platforms is not going to provide the prudent expert help many plan sponsors will need, and this carve-out could actually harm the plan and participants. The plan sponsor will be in the same situation so many plans fall into today: "Help" from someone who is not functioning as a fiduciary, and not in the "best Interest of the plan and its participants and beneficiaries." Rather, "help" from a salesperson, in the best interest of their platform, not participants and beneficiaries. The fiduciary burden will be on the plan sponsor and they will not be prudently serving plan participants if a proposed exemption for TPA and recordkeeper platform sales stands as is. We can envision a common scenario in which the seller says a lot of plan "customers" need help in developing their "objective criteria" – here is what many of them do – and then proceed to steer the plan into products that, again, benefit their platform, rather than participants.

Selection, Monitoring and Replacement Are Fiduciary Functions – Tibble

Selection, monitoring and replacement of plan investment alternatives are important fiduciary functions; ones which, if done well, can help participants achieve better outcomes, but if done poorly or on a conflicted basis can mean participants end up with only or mostly high cost, poorly performing investment alternatives, thereby greatly harming participants and beneficiaries. [6] [7] [8]

Applying the proposed "Seller's Carve-out to recordkeepers and third-party administrator (TPA) platforms may harm retirement investors. TPAs and Recordkeepers vary greatly in quality, motivation and cost. Their platforms of plan investment alternatives vary widely in quality and cost, as well. For example, if a platform receives indirect payments such as revenue sharing through the investment alternatives on the platform, the inherent conflict of interest could drive a platform to only offer higher-cost, poorly performing or more risky investment alternatives that increase revenue to the platform – which would come from plan participants.

The ability for a platform to steer plan sponsors into unreasonably high-cost choices that would harm plan participants clearly could undermine what DOL has intended in eliminating conflicts of interest.

Therefore we would not recommend a Seller's Carve-out for TPA and Recordkeeper Platform providers for investment selection, monitoring and replacement.

Further, we agree with DOL that the proposed "Seller's Carve-out" for platforms, in which the "provider has financial or other relationships with the offered investments and is not purporting to provide impartial investment advice," would be inappropriate for advice to IRA owners, or to plan participants or beneficiaries.

---

[6] "It Pays to Set the Menu: Mutual Fund Investment Options in 401(k) Plans," Veronika K. Pool, Clemens Sialm, Irina Stefanescu, NBER Working Paper No. 18764 February 2013 http://www.nber.org/papers/w18764

[7] "Broker Incentives and Mutual Find Market Segmentation," Diane Del Guercio, Jonathan Reuter, and Paula A. Tkac, National Bureau of Economic Research, http://www.nber.org/papers/w16312

[8] "Broker Incentives and Mutual Find Market Segmentation," Diane Del Guercio, Jonathan Reuter, and Paula A. Tkac, National Bureau of Economic Research, http://www.nber.org/papers/w16312

VIII. Recommended: A Carve-out for Information and Data Service Providers

There are information and data service providers available to plan sponsors that can help the plan sponsor to develop objective criteria for selecting, monitoring and replacing plan investment alternatives. When those service providers receive reasonable compensation, with no benefit, direct or indirect, from the plan investment alternatives that the plan sponsors choose, we believe they should have a seller's carve-out.

We recommend that DOL separate information service providers that do not receive compensation based on selected investment options, from platforms such as Recordkeepers and TPAs that may be compensated in various and sometimes harmful ways according what the plan chooses to include in its choices for participants.

IX. Education Or Advice?

Specific Funds in an Asset Allocation

We appreciate the care that DOL has taken in proposed rules about education versus advice with regard to asset allocation and specific investment recommendations from a plan's investment alternatives.

DOL has asked for comment on whether to use FINRA's recommendations and rules on what constitutes education and what constitutes advice. In the context of DOL's Fiduciary proposal to Eliminate Conflicts of Interest, FINRA's goal is, as DOL points out, geared for suitability, not fiduciary, recommendations. In addition, there is no way to know now how or whether FINRA's own policies on education versus recommendations will change, and what that would mean from a fiduciary perspective, especially in light of based on recent FINRA comments in media regarding DOL's proposal.

Therefore, we recommend that DOL *not* use FINRA's rules on education vs. advice, but rather look at principles on education vs. advice from DOL's fiduciary perspective, with assistance from fiduciary experts, if necessary.

Education or Advice – Help From Other Sources

Now, with many interactive portals and software, it may be possible to show participants a listing of where plan alternative investments would fit into an asset allocation, IF there is: 1) more than one reasonably priced alternative available for each asset class, 2) there is an array of low cost investment alternatives as well, and 3) where there is the ability to have the participant take an online risk assessment to ascertain where they fit into the risk spectrum.

(See table below)

For example, if there is an array of risk assessment outcomes, including the typical risk based or age based options, there might be an array of choices:

Aggressive, Moderately Aggressive, Moderate, Conservative

For example, an investor whose risk assessment found to be Moderate might see an interactive online array, where a retirement plan's choices looked something like this:

Moderate Asset allocation

	Cash or Equiv	Short Term Note/Bond	Intermed/ Long Bond	Corp Bd	US Eq	Internat Eq	Emerg Mkt Eq	Sectors Commod RE Fds
Low cost Index option	MM Fd	Index Fd or ETF	Index Fund or ETF	Index Fund or ETF	Index Fund or ETF	Index Fund or ETF	Index Fund or ETF	Index Fund or ETF
Index Fd/ ETF and active mix	·MM ·SV Fd	·Index ETF/ ·Active Fund	·Index/ETF ·Active Fund	·Index/ETF ·Managed Fund	·Index/ETF ·Managed Fund	·Index/ETF ·Managed Fund	·Index/ETF ·Managed Fund	·Index/ETF ·Managed Fund
Active Fund Managers	·Fund ·Fund	·Fund ·Fund	·Fund ·Fund	·Fund ·Fund	·Fund ·Fund	·Fund ·Fund	·Fund ·Fund	·Fund ·Fund

> Click on any investment alternative for more information (one pager, prospectus)
> Compare what-if portfolios here to see projected returns and costs over 1, 5, 10 years, risk measures and other information.

X. Conflicts and Compensation: The Best Interest Contract Exemption - BIC

The Contract itself

We applaud DOL's Best Interest Contract for requiring any person or company that would receive conflicted compensation to do so *only* if it is in the retirement investor's best interest, with comprehensive transparency and projected fee vs. performance and risk comparisons. Much of this information is available, for example, within investment companies that sponsor mutual funds, and they should be called on to provide this already available data in forms usable by any entity, or for that matter, any interested investor.

Business models with non-beneficial, conflicted compensation incent sales behaviors that are rarely in the best interest of a retirement investor, but very often serve the interest of the companies that share the revenue among themselves or seller's rep who makes that sale. These behaviors are often harmful to the retirement investor.

Conflicts and Compensation under BIC

We appreciate the thought and care with which DOL has accommodated differing business and compensation models, as the DOL proposal eliminates many of the conflicts of interest in existing rules by which America's retirement investors accumulate retirement nest eggs.

The Committee agrees that no advisory or sales entity that has the privilege and responsibility of serving retirement investors should be allowed to avoid fiduciary status. Further, we agree that the provisions of the BIC contract should be required before proceeding, and would appropriately apply to banks, broker-dealers, insurance companies, and mutual fund companies and their respective representatives.

We concur with DOL that call-in order-taking aspects of online or discount brokers should *not* be subject to the fiduciary standard, so long as they are truly taking orders and not steering retirement investors into particular high cost funds or securities or annuities.

The Committee is not keen to encourage the continued use of compensations types with imbedded conflicts of interest, such as commissions, 12b-1 fees, revenue sharing of all kinds, especially if it is not refunded to a plan for its expenses or refunded to participant accounts. We find these conflicted and often hidden payments are frequently engineered to be deceptive and misleading.

One newer version of deceptive revenue sharing, payments from custodians to firms, should also be included in this. While not very widespread among independent RIAs, wherever it is used, it is a conflict of interest, another cost to the investor, and one that should be avoided or fall under a BIC contract.

Any compensation that is hidden from retirement investors is deceptive, and chances are, more expensive than compensation that is fully, comprehensively transparent so that the investor understands exactly what they are paying for advice, or investment management, and how much is received by any entity and how that may affect the advice the investor receives. The burden should be in the advice provider to ensure the retirement investor understands this compensation. Of course, under BIC, this would have to be in the retirement investor's best interest.

With regard to conflicted compensation—with 12b-1, rev share, commissions, custodian payments, and myriad annuity commissions and fees: **the Committee is hard pressed to come up with examples of when these would be in the best interest of the retirement investor**. We are hard put to find examples of retirement investors who would not benefit from non-conflicted compensation, in which the adviser is compensated directly by the client, as doctors, lawyers, accountants and other professionals are, and does not receive compensation or selling inducements from any employer, company, partner, third party service or product provider et al, (which always is ultimately paid for by the investor, though the investor seldom is aware of that material fact).

When is Revenue Sharing or Hidden Commissions or Fees in the Interest of Retirement Investors?

For example, is it disloyal and inappropriate, under the auspices of advice in retirement investors' best interest, to recommend or sell funds or other products that pay hidden revenue share? We say yes it is. Even in a retirement plan, when revenue share, if any, must be used to defray plan costs (there should be no exemption to this, if revenue sharing, et al compensation is permitted at all), plan participants are often unaware of the revenue sharing arrangement or other hidden commissions or fees. Some commission, expense and fee disclosures deliberately obscure what retirement investors pay. Even when retirement investors – even plan sponsors – are aware of a third-party arrangement, they are not typically aware of the variation of fund expenses for differing share classes or the proportion of the expenses that comprises revenue share. Often, this creates a situation in which the lion's share of fund expenses are paid by a small number of plan participants, who don't realize the impact of their choice of plan alternative.

Another issue with hidden compensation such as revenue sharing is the often deliberate lack of transparency to the investor. If firms wanted investors to know what they are paying, hidden revenue sharing wouldn't exist.

BIC and Investor's Best Interest Finding

If revenue share of any kind is permitted under BIC, it is necessary to have a finding that this is in the best interest of the retirement investor, and why that is the case. In order for a retirement investor to make any informed choice of a plan alternative (mutual fund, ETF, or any other investment choice) that involves commission and/or revenue sharing compensation of any kind, full disclosure of the cost to the investor before the purchase, and over time, should be explicitly disclosed in a way that ensures the investor understands both the dollar amount and percentage of that compensation's impact, each year and over 5, 10, 15, 20 years.

The Committee agrees with the DOL proposal's requirements to disclose and ensure investor understanding of all costs to the retirement investor and performance data, both historical and forward-looking.

BIC Contract First – Private Right of Action and Class Action

The BIC contract, with its private right of action and the ability to form a class will be a strong deterrent to wrongdoing, and actionable if an investor is wronged. This is very important and beneficial, essential to the retirement investor. The BIC contract exemption wouldn't be necessary if a company or advisory representative did not have a model that contained inherent conflicts of interest that incent sales or recommendations that often harm the retirement investor. Some firms and groups have commented are that the contract within this exemption would be cumbersome to use, however the Committee feels it is a very important, especially where there are hidden payments among companies and their representatives.

Some firms have said the application of a BIC contract is "unworkable" or "unwieldy." But one of the very important points of the BIC Contract is the Contract, and retirement investors' rights for recourse under contract law. What do dissenters propose instead of the contract, that would provide the same investor's right to action and to form a class for class action, if necessary?

The point of BIC is to permit conflicted types of compensation models to exist and be used in the event that it is in the best interest of the investor to do so. If these entities would avoid or mitigate the conflicts of interest in their model, they wouldn't need the BIC contract, although we would think that some kind of contract would be in order, as it is with advisers who currently are fiduciaries.

This is a "can't have your cake and eat it too, issue." Avoid and mitigate the conflicts, (then would need a fiduciary contract), or use the BIC contract and act in the investor's best interests.

Annuities and the Opportunity for Mischief Under BIC

While compensation would Ideally be commensurate with the amount of time and work involved when considering how to advise a retirement investor, we are very concerned that this concept will be used to the detriment of retirement investors by sellers of annuities of various kinds, to retirement investors. Investors typically do not understand all of the many commissions, fees, penalties and other costs involved with annuities, which essentially involve the lock-up and return of the investor's own principal over time. Sales practices are abysmal and misleading in the extreme.

We would like to know more about how the DOL will ensure that annuities are not sold inappropriately to so many retirement investors, how DOL will determine what commissions and fees are reasonable, when they may be appropriately sold in an investor's best interest, and how DOL might tackle the misleading scare tactics so often used against retirement investors who are often pressured into buying these when it is not in their best interest. So in a nutshell, how will DOL help ensure that the fraction of appropriate annuity sales, are in fact in the investor's best interest?

Investor Cost and Performance Benchmarking

Regarding commission or revenue sharing, all-in costs to the investor, it would be extremely helpful to the retirement investor to require third-party benchmarking of both performance and fees both pre-sale and annually, as this is the only way to truly understand the context of the retirement platform or IRA alternatives and whether this is a good recommendation or choice, or not.

There are software and data information platforms available that benchmark investor costs and performance and would enable retirement investors to do "what if" scenarios with their plan choices and see the impact of their choices' costs and performance to enable them to fine-tune their choices. This would greatly help retirement investors to understand the impact of, for example, their 401(k)-type plan alternative choices, and their long-term impact on the investor's nest egg for retirement.

Firm Warranty

BIC's proviso of a firm warranty in which the firm explains how it is eliminating and mitigating conflicts of interest is an interesting concept and the Committee requests more information on how this would work and be monitored.

Collective Funds and Other Hard to Compare/Benchmark Assets

The Committee agrees in general with the provisions of what types of assets are permitted under the BIC. We would lean toward the vehicles on which there is readily available data, for transparency, performance and fee benchmarking and the ability to compare similar vehicles. Collective funds are often less transparent than mutual funds, for example. They offer different share classes, including classes with revenue share and commissions. It is easy to structure a CIF to provide fees to adviser, sub-adviser, custodian, and sponsor, making them fee-laden and better for the companies offering them than the retirement investor.

It's often harder to benchmark fees and expenses as well as performance on CIFs against peers. This could cause a run toward them because of their opaque nature, compared with mutual funds. If BIC contract users want to use CIFs, there should be a finding as to why this is a better option – in the best interest of the retirement investor, than a comparable and readily available, reasonable cost mutual fund or ETF. With CIF vehicles, there is often a chance and the incentive to add more fees to more entities, eliminating any retirement investor's advantage in owning those.

XI. SIFMA and FINRA's Recent "Best Interests" Proposals

SIFMA and FINRA, as well as assorted other associations or lobby groups for broker-dealers and insurance companies, mutual fund companies and banks, have proposed their own version of a standard, which in our view has nothing to do with either a fiduciary standard or a "Best Interests" standard. In fact, some opine that what they propose is in the Best Interests of the industry rather than the Best Interests of retirement investors.

On the following pages, with permission, we adopt the language of our esteemed Committee colleague, Prof. Ron Rhoades, JD, CFP. Prof. Rhoades is past Chair of The Committee for the Fiduciary Standard; Program Director, Financial Planning, and Asst. Professor of Finance, Gordon Ford School of Business, Western Kentucky University. Prof. Rhoades is also President of ScholarFi, Inc., an investment advisory firm, and President of Ron A. Rhoades, P.A., a law firm.

This space intentionally left blank.

" SIFMA'S AND FINRA'S "BEST INTERESTS" PROPOSALS: MISLEADING AND WHOLLY INEFFECTIVE

"Goldman's arguments in this respect are Orwellian. Words such as 'honesty,' 'integrity,' and 'fair dealing' apparently [in Goldman's eyes] do not mean what they say; [Goldman says] they do not set standards; they are mere shibboleths. If Goldman's claim of 'honesty' and 'integrity' are simply puffery, the world of finance may be in more trouble than we recognize." – Judge Paul Crotty, *Richman v. Goldman Sachs Group, Inc.*, 868 F. Supp. 2d 261 (S.D.N.Y. 2012).

In just the past couple of months, SIFMA has advanced a "best interests" standard of conduct, as an amendment to FINRA's suitability obligation.[9] FINRA, in its July 17, 2015 comment letter to the U.S. Department of Labor regarding the Conflict of Interest rule proposal and the exemptions relating thereto, also proposes a "best interests" standard. Upon close examination it is apparent that the rhetoric emanating from SIFMA and broker-dealer firms regarding the "best interests" proposal, and the proposals themselves, are but eleventh-hour attempts to defeat the U.S. Department of Labor's proposed Conflict of Interest Rule. SIFMA and FINRA, by these proposals, seek to deny the imposition of fiduciary status upon those who provide investment advice to retirement plans and retirement accounts, and in so doing seek to preserve a product-sales-driven "caveat emptor" relationship which is inappropriate for the delivery of personal investment advice. It is also apparent that the term "best interests" should not be utilized by either SIFMA or FINRA at all, given its understanding for centuries in the context of delivery of trusted advice to mean adherence to the fiduciary duty of loyalty.

For example, Richard Ketchum, Chairman and CEO of FINRA, recently summarized the protections for customers of brokers, stating that these protections "show that depictions of the present environment as providing 'caveat emptor' freedom to broker-dealers to place investors in any investment that benefits the firm financially with no disclosure of their financial incentives or the risks of the product, are simply not true."[10] However, Mr. Ketchum's characterization of broker-dealer firms' customers as not being subject to the ancient principle of 'caveat emptor'[11] is largely incorrect; by his statement he obfuscates the sales origins and present reality of today's broker-customer relationships. Additionally, while certain disclosure obligations are imposed on broker-dealers, these disclosures are often casual in nature, do not require the adviser to ensure client understanding of the conflicts of interest and their ramifications, and do not require that any proposed transaction wherein a conflict of interest exist remain (even with disclosure and informed consent) substantively fair to the client.

I would observe FINRA's recent support of a new "best interests" standard recently advanced by SIFMA,[12] the broker-dealer lobbying organization, grounded upon a weak suitability obligation accompanied by somewhat enhanced casual disclosures of additional information to investors, continues 75 years of FINRA's failure to advance standards to the highest levels, as envisioned by Senator Maloney and others, and fails to protect individual investors. FINRA's stated opposition to the Department of Labor's Conflict of Interest rule proposal is further evidence that FINRA serves only the interests of its broker-dealer

---

[9] SIFMA announced a "best interests" proposal in late May 2015, and then provided a "mark-up of existing FINRA Rules that outlines the broad contours of how a best interests standard for broker-dealers might be developed as part of the path forward on this most important investor protection issue." Retrieved from SIFMA web site, June 10, 2015.

[10] Richard G. Ketchum, Remarks From the 2015 FINRA Annual Conference, Washington, DC (May 27, 2015).

[11] BLACK'S LAW DICTIONARY 252 (9th ed. 2009) (defining "caveat emptor" as a Latin phrase meaning "let the buyer beware"); *see also* Matthew P. Allen, A Lesson from History, Roosevelt to Obama – The Evolution of Broker-Dealer Regulation: From Self-Regulation, Arbitration, and Suitability to Federal Regulation, Litigation, and Fiduciary Duty, 5 ENTREPRENEURIAL BUS. L.J. 1, 20 n.77 (2010) ("*Caveat emptor* is an old property law doctrine under which a buyer could not recover from the seller for defects in the property that rendered it unfit for ordinary purposes. The only exception was if the seller actively concealed latent defects.").

[12] SIFMA provided a "mark-up of existing FINRA Rules that outlines the broad contours of how a best interests standard for broker-dealers might be developed as part of the path forward on this most important investor protection issue." Retrieved from SIFMA web site, June 10, 2015.

members, and fails to adequately protect the investing public. Rather than embrace any changes to FINRA's suitability obligation by means of a misleading and wholly ineffective "best interests" standard, I would suggest that FINRA should be disbanded and its quasi-government oversight functions of the market conduct of broker-dealer firms and their registered representatives should be returned to federal and state agencies.

SIFMA has proposed that its "best interests" standard be adopted in lieu of the imposition of fiduciary standards of conduct upon brokers who provide investment advice. Yet, SIFMA's proposed "best interests" standard is also a far cry from the significantly enhanced protections afforded to consumers by a bona fide fiduciary standard of conduct, as proposed by the U.S. Department of Labor in its "Conflict of Interest" rule proposal (April 2015) and as found in existing common law applicable to those in relationships of trust and confidence with their clients. SIFMA's proposed "best interests" standard would – if enacted – deny consumers, in today's complex financial world, important protections by keeping individual investors in the situation where "caveat emptor" remains the rule for investors, even for those in relationships of trust and confidence with individuals and firms who provide personalized investment advice.

SIFMA's new "best interests" standard is also inherently misleading and deceptive, as the term "best interests" is commonly understood by consumers to mean that the advisor is acting on behalf of the consumer/investor, keeping the consumer's interests paramount at all times.[13]

FINRA's July 17, 2015 comment letter to the DOL also outlines its version of a "best interests" standard. This proposal demonstrates FINRA's continued inability to substantially raise the standards of conduct of brokers to the highest levels, as contemplated by Senator Maloney and others at the time of FINRA's inception (when it was called the NASD). FINRA's willingness to continue to protect brokers, under the shield of an inherently weak suitability standard (whether or not "enhanced" by its "best interests" proposal), also confirms the necessity of the U.S. Department of Labor moving forward to impose fiduciary status upon investment advisers to ERISA-governed retirement plans and to IRAs, as contemplated by the proposed rule.

In the table below I summarize the flaws in SIFMA's and FINRA's recent "best interests" proposals and demonstrate why SIFMA's proposed changes to FINRA's suitability rule do not come even close to the protections provided by the fiduciary standard:

---

[13] Legal commentators also continue to equate the term "best interests" with the requirement of the fiduciary duty of loyalty. *See, e.g.*:

- Edward J. Waitzer and Douglas Sarr, Fiduciary Society Unleashed: The Road Ahead for the Financial Sector, 69 Bus.Lawyer 1081, 1090 (Aug. 2014). ("these individuals need to *trust* that the specialists they rely upon will keep their best interests at heart ... Fiduciary law aims to promote this trust. It applies to relationships in which one party, the fiduciary, gains discretionary power over another party, the beneficiary, in circumstances where both parties would 'reasonably expect' that the fiduciary will exercise this power in the ***best interests*** of the beneficiary") (*Emphasis* in original; ***emphasis*** added.)
- Gold, Andrew S., The Loyalties of Fiduciary Law (December 20, 2013). Philosophical Foundations of Fiduciary Law, Andrew S. Gold & Paul B. Miller, eds., Oxford University Press, 2014, Forthcoming. Available at SSRN: http://ssrn.com/abstract=2370598 ("Another conception of fiduciary loyalty suggests that the fiduciary must act in the *best interests* of the beneficiary ... This conception can readily be linked to the first conception, given the possibility that the rules against conflicting interests are designed to increase the likelihood that a fiduciary will act in the beneficiary's *best interests*.") (*Emphasis* added.)

The influential Restatements of the Law also equate "best interests" or "placing the interests of the principle first" with the fiduciary duty of loyalty:

- American Law Institute, Restatement of the Law of Trusts (Third) § 78. ("[A] trustee must refrain, whether in fiduciary or personal dealings with third parties, from transactions in which it is reasonably foreseeable that the trustee's future fiduciary conduct might be influenced by considerations other than the *best interests* of the beneficiaries.") (*Emphasis* added.)
- Restatement (Third) of Agency § 8.01 comment b. ("Although an agent's interests are often concurrent with those of the principal, the general fiduciary principle requires that the agent subordinate the agent's interests to those of the principal and *place the principal's interests first* as to matters connected with the agency relationship.") (*Emphasis* added.)

A Concise Comparison: Bona Fide Fiduciary Standard vs. SIFMA's "Best Interests" Proposal

What requirements are imposed upon the person providing personalized investment advice?	Bona Fide Fiduciary Standard	SIFMA's "Best Interest" Proposal (as outlined in its June 2015 release)	FINRA'S "Best Interest" Proposal (as outlined in its July 17, 2015 comment letter)[14]
Who does the financial representative represent?	The client.	The brokerage firm, and, through the firm, various product manufacturers. The financial representative functions as a "seller's representative" with no substantial allegiance required to the purchaser (customer).	The brokerage firm, and, through the firm, various product manufacturers. The financial representative functions as a "seller's representative" with no substantial allegiance required to the purchaser (customer).
Does a duty exist upon the representative to clearly and fully disclose all compensation received by the person providing advice, and by his/her firm?	Yes.	<u>No.</u> While annual disclosure occurs of "a good faith summary of the *investment-related fees*" associated with an investment, there is no requirement in SIFMA's proposal that the *compensation* of the broker-dealer or its registered representative be affirmatively quantified and then disclosed. As a result, customers will remain uninformed of the precise amount of the compensation of the broker and its registered representative. Hence, the client will not possess the means to assess the reasonableness of the compensation so provided, and the receipt of only "reasonable compensation" is a requirement for a fiduciary actor.	<u>No.</u> While annual disclosure occurs of a product's "fees and all related expenses," there is no requirement in FINRA's proposal that the *compensation* of the broker-dealer or its registered representative be affirmatively quantified and then disclosed. As a result, customers will remain uninformed of the precise amount of the compensation of the broker and its registered representative. Hence, the client will not possess the means to assess the reasonableness of the compensation so provided, and the receipt of only "reasonable compensation" is a requirement for a fiduciary actor. Why do broker-dealer firms resist the fiduciary requirement to fully disclosure a material fact – their compensation – to their customers? *Because a large proportion of these customers believe that their registered representative and brokerage firm is acting gratuitously,*[15] *given broker-dealers' ability to hide compensation from the customers.*[16]

[14] FINRA states, in its comment letter of July 17, 2015 to the U.S. Department of Labor, that "any best interest standard for intermediaries should meet the following criteria:

- The standard should require financial institutions and their advisers to:
  - act in their customers' best interest;
  - adopt procedures reasonably designed to detect potential conflicts;
  - eliminate those conflicts of interest whenever possible;
  - adopt written supervisory procedures reasonably designed to ensure that any remaining conflicts, such as differential compensation, do not encourage financial advisers to provide any service or recommend any product that is not in the customer's best interest;
  - obtain retail customer consent to any conflict of interest related to recommendations or services provided; and
  - provide retail customers with disclosure in plain English concerning recommendations and services provided, the products offered and all related fees and expenses."

[15] *See, e.g.*, Study Regarding Obligations of Brokers, Dealers, and Investment Advisers, Rel. No. IA-3058; File No. 4-606 (a.k.a. the "Rand Report" of 2008), in which over one-fourth of consumers surveyed related that they paid "$0" for the brokerage or advisory services they were provided. Since registered investment advisers are required to provide clients with periodic statements of the fees paid, under the requirements of the Investment Advisers Act of 1940 and regulations thereunder, and since the survey included a large number of clients of dual registrants (which fosters confusion among titles), it is likely that the survey understates the number of customers of broker-dealer firms who hold such firm. I have personally observed many, many customers of brokers who believed that their broker provided his or her services "for free" and "without compensation," and I have never met a customer of a full-service brokerage firm who understood *all* of the ways, or the high amounts, of the compensation received by the broker or the brokerage firm.

What requirements are imposed upon the person providing personalized investment advice?	Bona Fide Fiduciary Standard	SIFMA's "Best Interest" Proposal (as outlined in its June 2015 release)	FINRA'S "Best Interest" Proposal (as outlined in its July 17, 2015 comment letter)[14]
Is there a duty *upon the representative* to ensure client understanding of material facts, including material conflicts of interest?	Yes.	No. Under SIFMA's proposal disclosures must only be "*designed* to ensure client understanding." There is no requirement, as exists for a fiduciary, that client understanding of conflicts of interest, and their ramification, actually occur.	No. Under FINRA's proposal disclosures relating to products must only be provided to the customer. There is no requirement, as exists for a fiduciary, that client understanding of conflicts of interest, and their ramification, actually occur by means of affirmative obligations placed upon the registered representative.
Is *informed* consent of the client required prior to the client undertaking *each and every* recommended transaction?	Yes.	No. There is no requirement in SIFMA's proposal that the client's consent be "informed" – a key requirement of fiduciary law before client waiver of a conflict of interest can take place. Nor is there a requirement that the client provide informed consent prior to each and every transaction. Rather, SIFMA would only require: "Customer *consent* to material conflicts of interest or for other purposes as appropriate *may be provided at account opening*." Of course, consent "at client opening" often involves a customer briefly initialing a line, as one of many initials or signatures provided in account opening forms which are often dozens of pages long. The result of SIFMA's proposal is that clients can and will consent to be harmed – an outcome which cannot exist under a bona fide fiduciary standard. And such "consent" will hardly ever be "informed."	No. There is no requirement in FINRA's proposal that the client's consent be "informed" – a key requirement of fiduciary law before client waiver of a conflict of interest can take place. Nor is there a requirement that the client provide informed consent prior to each and every transaction. Rather, FINRA would only require brokers to "obtain client consent" to conflicts of interest. Such consent, often given with little or no understanding by the customer of the broker, creates an estoppel defense for the broker, who is in an arms-length relationship with the customer. As explained in this comment letter, the role of estoppel is very limited in fiduciary relationships, and much more than "simple consent" is required for the fiduciary to proceed when a conflict of interest is present.

[16] Information regarding all of the compensation paid by product providers to the brokers is not provided by brokers to their customers, except piecemeal and in multiple lengthy documents, such as often 50+ page disclosure statements signed upon the opening of accounts, mutual fund prospectuses, and various web site disclosures. Even then, such disclosures are often ambiguous, such as "we may receive compensation from" a product provider or (in product provider documents, such as prospectuses) "we may compensate a broker." Indeed, even the author – who is trained in reading legal documents and who possesses a broad and deep knowledge of investment products, often cannot discern the sum total of compensation provided to a full-service broker resulting from many investments, given that the sum total includes not only commissions and 12b-1 fees, but also payment for shelf space, sponsoring of seminars for prospective customers, sponsorship of events at broker-dealer firm meetings, payment of brokerage commissions including soft dollar compensation, and other forms of revenue-sharing payments. The disguising of the total compensation paid to broker-dealer firms and their registered representatives appears to be a central concern of the broker-dealer community, since if full and complete disclosures were made of the compensation arrangements, the fact of differential compensation, and the amounts paid, most customers would likely choose not to be business with the brokerage firm. I have observed many a client, once I informed them of my estimate of what they had been paying to their broker-dealer firm over the past year, become very angry. Yet, a remedy for their grief is usually not available, as the "suitability" standard does not require that a broker-dealer firm receive only "reasonable compensation." In contrast, the fiduciary standard of conduct requires affirmative disclosure to the client of all material facts, which by necessity includes all compensation the fiduciary investment adviser receives, stated in terms that are clear, concise and understandable by the client. In addition, the fiduciary standard of conduct requires that compensation received be reasonable.

What requirements are imposed upon the person providing personalized investment advice?	Bona Fide Fiduciary Standard	SIFMA's "Best Interest" Proposal (as outlined in its June 2015 release)	FINRA'S "Best Interest" Proposal (as outlined in its July 17, 2015 comment letter)[14]
Must the transaction remain, at all times, *substantively fair* to the client?	Yes.	No. There is only a requirement that the transaction be in accord with the client's "best interest" – a new SIFMA-proposed standard that is ill defined and which remains subject to much interpretation. Such interpretations will primarily occur through FINRA's much-maligned system of mandatory arbitration. In contrast, the fiduciary standard possesses centuries of interpretation and application. Under a bona fide fiduciary standard, clients are unable to waive core fiduciary duties; the role of estoppel is quite limited. This is enforced by the courts by requiring both *informed* consent of the client and that the transaction remain *substantively fair* to the client.	No. There is only a requirement that the transaction be in accord with the client's "best interest" – a new FINRA-proposed standard that is ill defined and which remains subject to much interpretation. Such interpretations will primarily occur through FINRA's much-maligned system of mandatory arbitration. In contrast, the fiduciary standard possesses centuries of interpretation and application. Under a bona fide fiduciary standard, clients are unable to waive core fiduciary duties; the role of estoppel is quite limited. This is enforced by the courts by requiring both *informed* consent of the client and that the transaction remain *substantively fair* to the client.
Does there exist a duty to *properly manage* investment-related fees and costs that the client will incur at all times?	Yes.	No. SIFMA expressly states: "Managing investment-related fees does not require recommending the least expensive alternative, nor should it interfere with making recommendations from among an array of services, securities and other investment products consistent with the customer's investment profile." These caveats leave the door wide open for the broker to recommend highly expensive products, including products which pay the broker more, in which the total fees and costs incurred by the customer will substantially lower the long-term returns of the investor.	No. FINRA does not appear to recognize that, under fiduciary law, there is an obligation imposed upon the fiduciary to ensure that any expenditures of the client's funds, through payment of product-related fees and costs, be undertaken with close scrutiny. FINRA appears to desire that high-cost products could still be recommended compared with lower-cost products that possess nearly the same risk and other characteristics. The fiduciary standard of due care requires that the client's expenses be controlled and that avoidable expenses be avoided. The fiduciary is permitted to obtain reasonable, professional-level compensation, through agreement with the client at the inception of the relationship, and with full disclosure of same.
Does there exist a duty to properly manage the design, implementation and management of the portfolio, in order to reduce the tax drag upon the customer's investment returns?	Yes.	No. There is no express duty under SIFMA's proposal to properly manage the tax consequences of investment decisions. Far too often under the suitability standard, and under this proposed "best interests" standard, customers of broker-dealers have and will possess substantial tax drag upon their investment returns that otherwise could have been avoided through expert advice.	No. Nothing in FINRA's proposal addresses portfolio management. FINRA is mired in the ancient practice of providing products under the suitability standard. Today's investors deserve expert advice from true fiduciaries, not the sale of products which generate high profits for the broker without proper consideration of how the product fits into the client's overall portfolio.

As seen, SIFMA's and FINRA's proposed "Best Interests" standards fall far short of the protections afforded by ERISA's fiduciary standard. The fact of the matter is that Wall Street wants to eat its cake and have it too. It wants to be perceived as acting in customer's "best interests," but enjoy the freedom to act in its own interests. Wall Street's new "Best Interests of the Consumer" proposal is, in reality, only "Wall Street's Self-Interest."

As alluded to in the chart above, by its "Best Interests" proposal SIFMA and FINRA do not turn brokers from sell-side merchandizers into buy-side purchaser's representatives and fiduciaries. Rather, SIFMA's and FINRA's proposal are nothing more than an attempt to obfuscate into some kind of obscene and confusing hybrid between the two. In fact, the enhancement to the inherently weak suitability standard under these proposals is extremely modest.

This begs the question – who does the broker under SIFMA's and FINRA's proposed "best interests" standards represent? This is a key question, for the following is well known in the law:

> The characters of buyer and seller are incompatible, and cannot safely be exercised by the same person. *Emptor emit quam minimo potest; venditor vendit quam maximo potest.* The disqualification rests ... on no other than that principle which dictates that a person cannot be both judge and party. No man can serve two masters. He that it interested with the interests of others, cannot be allowed to make the business an object of interest to himself; for, the frailty of our nature is such, that the power will too readily beget the inclination to serve our own interests at the expense of those who have trusted us."[17]

It is obvious that under SIFMA's and FINRA's proposed "best interest" standards the registered representative would continue to act as sellers of products, thereby representing the broker-dealer firm and product manufacturers. This is a far, far cry from acting as a fiduciary, and acting as the representative of the purchaser. And it fails to achieve a key objective that the U.S. Department of Labor alluded to in its release for the BIC exemption: "In the absence of fiduciary status, the providers of investment advice are neither subject to ERISA's fundamental fiduciary standards, nor accountable for imprudent, disloyal, or tainted advice under ERISA or the Code, no matter how egregious the misconduct or how substantial the losses."[18]

The U.S. Department of Labor should reject any proposal from SIFMA, FINRA, or broker-dealer firms, or insurance companies, which seeks to advance such a woefully inadequate rule. These are proposals that, like the suitability standard today, protect Wall Street, and utterly fail to protect consumers from Wall Street's greed.

Let us not permit Wall Street profess to act in the "best interests" of customers, when any sensible consumer would conclude that Wall Street's definition of "acting in your best interests" is wholly deceptive to consumers. Such fraud[19] has no place in government regulatory efforts, nor even in self-regulatory organization rulemaking activities. SIFMA's and FINRA's proposals should be loudly and firmly rejected by the DOL and other policymakers. And the recent embrace by FINRA of SIFMA's proposal should subject FINRA to further scrutiny over whether FINRA's market conduct regulation of brokers should be transferred back to federal and state governments for direct oversight,[20] especially when FINRA characterizes its proposal as a "fiduciary 'best interests'" proposal – when it clearly is not."

[17] Carter v. Harris, 25 Va. 199, 204 (1826); 1826 Va. LEXIS 26; 4 Rand. 199 (Va. 1826).

[18] BIC exemption release at pp. 21962-3.

[19] As Professors Angel and McCabe observed: "The relationship between a customer and the financial practitioner should govern the nature of their mutual ethical obligations. Where the fundamental nature of the relationship is one in which customer depends on the practitioner to craft solutions for the customer's financial problems, the ethical standard should be a fiduciary one that the advice is in the best interest of the customer. To do otherwise – *to give biased advice with the aura of advice in the customer's best interest – is fraud.* This standard should apply regardless of whether the advice givers call themselves advisors, advisers, brokers, consultants, managers or planners." James J. Angel, Ph.D., CFA and Douglas McCabe Ph.D., *Ethical Standards for Stockbrokers: Fiduciary or Suitability?* (Sept. 30, 2010). (*Emphasis* added.)

[20] I have previously written about FINRA's seven-decades long failure to live up to the aspirations of the Maloney Act to raise the principles of broker-dealers firms to the highest level. *See* "Disband FINRA," available at http://scholarfp.blogspot.com/2013/07/disband-finra-unabridged-and-with.html. "

"On the Integration of DOL's Fiduciary Standard with Other Standards."

"Various objections to the DOL's proposal have been raised in the public sphere that differing fiduciary standards may exist, between providing advice to accounts covered by the Conflicts of Interest Rule and other types of accounts, and that compliance with differing standards would prove too difficult. This is patently false and non-sensible. It has long been understood by providers of services under two different standards of conduct that the easiest path to ensure compliance is to simply apply the higher standard to the entirety of the relationship.

Indeed, the SEC staff in 2011, following in the footsteps of the Certified Financial Planner Board of Standards, Inc.'s professional rules of conduct, explained that the federal fiduciary standard applies to a fiduciary adviser's "entire relationship" with clients and prospective clients.[21] In this regard, it must be understood that "contract law concerns itself with transactions while fiduciary law concerns itself with relationships."[22]

While the DOL cannot, through its own regulations, mandate the fiduciary standard applicable to non-ERISA and non-IRA accounts, any "dilemmna" posed by the existence of differing standards is easily solved, as set forth above. The highest standards applicable to any account should govern the entirety of the relationship. This is likely the perception the client will possess, and this solution follows upon accepted common law that fiduciary status attaches to relationships, not accounts.

One must wonder why FINRA, in existence for over 75 years, has not incorporated into its conduct rules for brokers the requirements of a fiduciary standard, and acknowledge that under certain circumstances (*e.g.,* when a relationship of trust and confidence is formed, when *de facto* discretion exists, etc.) that brokers can (and have been, repeatedly) held to be fiduciaries under state common law. If FINRA is concerned about the "confusion" that might exist among brokers and their registered representatives about varying standards of conduct, the solution for FINRA's concern is very apparent: (1) simply copy into FINRA's conduct rules the fiduciary standards of conduct under DOL (or other) regulatory regimes; (2) specify when such fiduciary standards of conduct apply (easily discernible from the DOL's proposals, and guided by established law in other areas); and (3) instruct the broker and its registered representatives to simply apply the highest standard of conduct imposed upon any account or any aspect of the relationship to the entirety of the relationship.

Adherence to the highest standard imposed, when differing standards exist, isn't rocket science. FINRA's protests (and those of the broker-dealer industry associations such as SIFMA and FSI, and those of many broker-dealers themselves) should be dismissed as meritless and mere attempts to deny to Americans the important fiduciary protections they deserve."

---

[21] Securities and Exchange Commission Staff, Study on Investment Advisers and Broker-Dealers 22 (2011).

[22] Rafael Chodos, *Fiduciary Law: Why Now! Amending the Law School Curriculum*, 91 Boston U.L.R. 837, 845 (and further noting that "Betraying a relationship is more hurtful than merely abandoning a transaction.")

XII. Disclosures and Investor and Adviser Behavior: Not What You Would Expect

We applaud the DOL for requiring transparency and disclosure of cost and performance projections and comparisons to like investments.

We also are heartened to see that it is not an option to "disclose and waive" best interest provisions, or "disclose and harm" – that the best interests of the retirement investor are paramount, and not negotiable.

While transparency is crucial, disclosures of costs (and other information) to the investor have many unexpected and perverse effects on the investor, and on many well-meaning advisors, and certainly on salespeople, according to current academic research.

Disclosures are necessary, but not sufficient to fulfill fiduciary duty. Transparency is essential. The adviser needs to avoid the conflicts in the first place, and manage unavoidable conflicts in the investor's best interest – not disclose, proceed, and harm.

The effects of disclosures are surprising and quite unsettling. **Regulators may not be aware of the effects even good disclosures have on even well-meaning advisers and investors**, according to Prof. Dalian Cain, Yale School of Management, in "The Dirt on Coming Clean: The Perverse Effects of Disclosing Conflicts of Interest,"[23] According to Dr. Cain's research:

"*Conflicts of interest can lead experts to give biased and corrupt advice. Although disclosure is often proposed as a potential solution to these problems, we show that it can have perverse effects. First, people generally do not discount advice from biased advisors as much as they should, even when advisors' conflicts of interest are disclosed. Second, disclosure can increase the bias in advice because it leads advisors to feel morally licensed and strategically encouraged to exaggerate their advice even further. As a result, disclosure may fail to solve the problems created by conflicts of interest and may sometimes even make matters worse."*

While we understand that, for firms that currently do not provide advice or investment management in the retirement investor's best interests, this transition to advice in the best interest of the retirement investor will take time.

We support the idea of doing away with non-beneficial compensation models over time.

---

[23] Cain, Daylian M., George Loewenstein, and Don A. Moore. "The dirt on coming clean: Perverse effects of disclosing conflicts of interest." *The Journal of Legal Studies* 34.1 (2005): 1-25.

Disclosures: Transparency is Necessary But Disclosures Are "Ineffective" and Often, Worse

Some of the most recent work on disclosures and their effect on even well-meaning advisers, and investors receiving advice after being disclosed to, indicates that the effects are extremely perverse, according to Daylian Cain, Yale School of Management. Dr. Cain's research is compelling and it underscores the fact that disclosure is not enough to mitigate conflicts of interest or fulfill fiduciary duty to investors.

A 2013 research paper, "The Burden of Disclosure: Increased Compliance with Distrusted Advice," by Sunita Sah, George Loewenstein, and Prof. Cain, continues work they have led for years.[24] That research indicates:

"Professionals are often influenced by conflicts of interest when they have a personal, often material, interest in giving biased advice. Although disclosure (informing advisees about the conflict of interest) is often proposed as a solution to problems caused by such conflicts, prior research has found both positive and negative effects of disclosure. ***We present four experiments that reveal a previously unrecognized perverse effect of disclosure:*** *While disclosure can decrease advisees' trust in the advice, it simultaneously increases pressure to comply with that same advice. We demonstrate that the increased pressure results from advice recipients feeling obliged to help satisfy their advisors' personal interests when those interests have been disclosed. Hence, disclosure can burden those it is ostensibly intended to protect. We show that the increased pressure to comply is reduced if (1) the disclosure is provided by an external source rather than from the advisor, (2) the disclosure is not common knowledge between the advisor and advisee, (3) a cooling-off period is introduced, or, (4) the advisee can make the decision in private."*

One More Thought on Disclosures

Few put it better than writer James Surowiecki, writing in *The New Yorker*: "Transparency is well and good, but accuracy and objectivity are even better. Wall Street doesn't have to keep confessing its sins. It just has to stop committing them."[25]

---

[24] "**The Burden of Disclosure: Increased Compliance with Distrusted Advice,**" Sah, Sunita and Loewenstein, George and Cain, Daylian M., The Burden of Disclosure: Increased Compliance with Distrusted Advice (December 7, 2011). Sah, S., Loewenstein, G., & Cain, D. (2013). The Burden of Disclosure: Increased Compliance with Distrusted Advice. Journal of Personality and Social Psychology, Vol 104(2), 289-304. doi: 10.1037/a0030527. SSRN: http://ssrn.com/abstract=1615025 or http://dx.doi.org/10.2139/ssrn.1615025

[25] "The Talking Cure," *The New Yorker*, 12/9/2002, http://www.newyorker.com/magazine/2002/12/09/the-talking-cure

XIII. Abandoning Retirement Investors if "Forced" to Act in Investor's Best Interest?

When any firm or sector in the financial services industry, including less progressive insurance, banks, broker-dealers or mutual fund companies, says they will abandon a segment of clients because they do not want to be "forced" to put the retirement investor's best interests before their own, we have to ask:

What, exactly, are they doing to retirement investors under the current, conflicted system? Would that investor actually be better off elsewhere, with advisers who are already serving as fiduciaries to retirement investors?

In a study of broker-dealers in states where a fiduciary duty was imposed by the state, Texas Tech University Prof. Michael Finke and Roger Williams University Prof. Thomas Langdon found **predictions that the fiduciary standard would limit recommendations, advice to middle market clients and the range of products, did not come true**.[26] They note:

"*It has been suggested that the imposition of a fiduciary standard on registered representatives would result in significant changes in how broker-dealers conduct business by limiting a representative's ability to recommend commission investments, provide advice to middle-market clients, and offer a broad range of financial products. We take advantage of differences in state broker-dealer common law standards of care to test whether a relatively stricter fiduciary standard of care impacts the ability to provide services to consumers. We find that the number of registered representatives doing business within a state as a percentage of total households does not vary significantly among states with stricter fiduciary standards. A sample of advisers in states that have either a strict fiduciary standard or no fiduciary standard are asked whether they are constrained in their ability to recommend products or serve lower-wealth clients. We find no statistical differences between the two groups in the percentage of lower-income and high-wealth clients, the ability to provide a broad range of products including those that provide commission compensation, the ability to provide tailored advice, and the cost of compliance."*

[26] Finke, Michael S. and Langdon, Thomas Patrick, The Impact of the Broker-Dealer Fiduciary Standard on Financial Advice (March 9, 2012). Available at
SSRN: http://ssrn.com/abstract=2019090 orhttp://dx.doi.org/10.2139/ssrn.2019090

XIV. IRA Rollovers

Rollovers from 401(k)-type Accounts to IRA Accounts and Conflicts of Interest

The question of whether to rollover assets from a 401(k)-type retirement account to an IRA is one of the biggest financial questions a retirement investor will ever face. In a well run plan that has competent fiduciary advice and plan management, the advantages of size, (institutional share classes, with lower costs) reasonable overall costs, and well chosen investment alternatives, there are many good reasons that retirement investor may want to stay in the 401(k)-type account even if they own several of them.

There are at times, however, reasons it may be in the investor's best interest to roll out of a 401(k)-type plan: if the plan is poorly run, has high costs and a poor array of investment alternatives; if a retirement investor wishes to consolidate a number of 401(k)s into one IRA for administrative ease; or if they desire to move their assets to the care of a fiduciary who is managing other assets. In this comment, all the rollovers would be advised by a fiduciary. As mentioned earlier, there are many smaller and mid-sized plans in which costs are very high and investment alternatives are poor and expensive.

Rollovers from Traditional Pension Plans

Then there are the surprising examples of rollovers out of traditional pension plans that pay monthly income to the retiree for life. One would think that investors would want to hold on for dear life to that traditional pension plan.

Here is an example that left us saddened, but not shocked, as this is more common than we would have thought.

David Franklin (not his real name to protect his privacy) had just celebrated his 65th birthday. After graduating from college he entered the Navy, achieved the rank of Lieutenant, retired after his tour of duty and entered the private sector. Over his successful career he has had, as many who are now retiring, a combination of traditional, defined benefit pension plans and 401(k)-type plans. Mr. Franklin worked hard to contribute to his 401(k) plans and accumulate a retirement nest egg. His resume lists a handful of mostly Fortune 100 companies. Two of the large, very stable companies where Mr. Franklin worked had traditional pension plans. He was a beneficiary of those multibillion-dollar pension plans, which pay retirees a certain amount every month, for life.

Shortly after his birthday, Mr. Franklin got a phone call from an "adviser" working with one of the traditional plans, this investment professional said. He wanted to discuss Mr. Franklin's retirement situation. This "adviser" began by asking whether Mr. Franklin was confident he'd have enough to live on for the rest of his life. He insinuated that the (Fortune 100) companies that ran the traditional pension plans might go out of business, taking his monthly payout with them. What would Mr. Franklin do then? He strongly urged Mr. Franklin to take the lump sum payout and put it into a "guaranteed" annuity in an IRA at his well-known firm. Sure it would pay Mr. Franklin *several hundred dollars less* every month than the pension plan would, but it would be "guaranteed." He hounded Mr. Franklin until Mr. Franklin did, in fact, rollover one of his pension plans into an IRA at that major mutual fund company, ready for that annuity. And then Mr. Franklin called a friend. It is too late for Mr. Franklin to reverse his lump sum pension payout so he now has to find a way to replace that retirement income.

While Mr. Franklin will not be taking any more "advice" from that "adviser," he's already incurred damage.

This happens every day, to thousands of America's retirement investors.

We all, at a certain age, get the invitations to the "dinner" where we can "learn about strategies for retirement." "Are you sure your money will last?" "This is strictly educational. No insurance agents or brokers allowed," -- this from an insurance agent herself. "Sign up for this seminar – at a local university – where you will learn how to ensure your financial security in retirement! Just $69!" Once there, retirees or the soon-to-retire are scared and manipulated into buying high cost, low performing annuities that will ensure the seller's retirement, but not necessarily the annuity owner's retirement.

This practice must stop.

When a Fiduciary is Advising a Plan and a Participant Wants to Rollover

There is a scenario that has come up dozens of times in conversations with independent fiduciaries since the announcement that there would be a proposed DOL rule. It's a concern and frustration voiced by fiduciaries about the current scenario regarding rollovers, and those fiduciaries that advise and/or manage plan assets. Here is a typical version of the conversation:

"*Our RIA works exclusively with retirement plans. In that capacity, we are the ERISA section 3(38) investment manager (i.e., a discretionary fiduciary via ERISA section 3(21)(A)(i)) to all our plan clients. Some plan participants come to us upon their retirement and want to roll over their money and have us manage it. We cannot provide that service for them because we are a plan fiduciary and ERISA deems that to be a conflict of interest.*

And yet, an insurance company that's providing bundled services (e.g., trust, recordkeeping but sans investment advisory services since we are the 3(38) solely in charge of the investment options) to the plan can waltz in and place participants in lousy investments at four times the cost to the "sky's the limit" cost for what we would charge.

ERISA allows this because the insurance company is not a fiduciary to the plan. That's a fundamentally flawed proposition. Let's see: with us, participants would get a low cost, broadly diversified portfolio and with the insurance or BD side they would likely get expensive, lousy (under-diversified, illiquid, et al.) investments. With us, in retirement plan participants could even be placed in the exact same portfolio they had in their plan if they wished. Here is a narrative from one RIA who works with plan sponsors.

Since our plan fee – either invoiced directly to the plan sponsor or scraped from participants' accounts and disclosed to them clearly - is so low our fee to manage rollover money (if we otherwise could) is a multiple of that, but is still a mere fraction of the fees that would be charged by a brokerage firm or insurance company. We're about as pure as you can get in this scenario but still, as seen from the outside, it looks like a conflict. OK, fine, agreed.

What I don't want to see emerge in a final rule, however, is to give the brokerage firms, insurance companies, et al. an edge in the preceding scenario over someone like us.

In that scenario, ERISA almost guarantees a strange, sub-optimal result for retiring plan participants. That's why – from a cursory glance – I favor the idea of having BIC apply to all dually registered RIAs (those wearing two hats) and non-RIAs (Broker Dealers, insurance companies) and exempt RIA Fiduciaries (those wearing the one, white hat) from BIC.

Quite frankly, I'm not even sure that our firm could make all that much money from rollovers. We've never done them, plus in plans where the sponsor doesn't kick out participants when they retire, it's usually better for participants to stay invested since the costs (low because we're in charge of the investment options) are so much lower. But the insurance or broker-dealer side will (almost) always counsel leaving a plan and investing in their current super-duper annuity, et al.

In this area, then, I'm not so much concerned about lining my own pockets as I am about keeping the wirehouses, et al. from (richly) lining theirs. I cannot tell you how it pains me to see a participant who has built a tidy portfolio (due in part to our firm's efforts in placing only low cost, broadly diversified portfolios on a plan's investment menu) and then having to watch that poor participant, upon rolling over at retirement, get fed to the circling sharks out there because we cannot help her/him due to the fact that we're a fiduciary to the plan. If a retiring participant doesn't want to invest and manage their own money in retirement, then honestly, (under the current scenario) what choices do they really have other than the sharks?"

This situation is emblematic and identical to many other cases that fiduciaries have discussed with us these past six months. Here you have the already expert fiduciary that is abiding by current DOL rules, but the participant has a frustratingly bad outcome.

The Committee appeals to DOL to find an answer to this scenario that does not involve the participant being "thrown to the wolves."

We have one suggestion: The Fiduciary Interest Contract - FIC

Recommendation: The Fiduciary Interest Contract -- FIC

The Fiduciary Interest Contract would replace the BCI contract in instances where an independent, fee-only RIA, is advising a plan participant on a rollover (not fee based, fee-only – paid only by the investor on an all costs fully disclosed basis – (not affiliated with any broker-dealer, insurance company, no income tied to any investment or insurance offering, etc.) This could apply whether that RIA is advising the plan or not.

The FIC contract has several benefits to the investor that the BIC does not:

1) Consultation on the rollover is treated as a separate, fiduciary advisory engagement from any ongoing work, to ascertain IF it is in the investor's best interest that to rollover.
2) The advice whether to rollover or not is fully fiduciary, and the investor has a brief FIC contract to that effect, with the requisite discussion of rollover alternatives, pros and cons and the inherent conflict of a rollover.
3) The investor is protected by both fiduciary law and contractual law and their inherent rights to take action.
4) IF the finding is made that it is in the retirement investor's best interest to rollover, that ends the rollover engagement and a new, fiduciary RIA – retirement investor contract is made.

To explain in more detail, we include below the IRA Rollovers portion of the DOL comment of our Committee colleague, Prof. Ron Rhoades, JD, CFP. Here now, is Prof. Rhoades' comment:

"On the Regulation of IRA Rollovers"

"When undertaking a rollover from an ERISA plan to an IRA account, a great deal of care must be undertaken. This requires any fiduciary adviser to possess a great deal of knowledge of the many factors and tax rules which come into play, in order to ensure maximum benefits to the individual client. In addition, a rollover into an individual IRA account often involves a much higher level of service provided to the individual investor, during and following the rollover process; as a result of this differing level of service and the lack of economies of scale which are often present in the defined contribution space, the compensation for individual accounts is higher. Accordingly, this results in a potential prohibited transaction, even for fee-only independent registered investment advisers.

Any fiduciary adviser providing advice on an IRA rollover should fully understand, and be able to apply, the often-complex tax and other considerations that may affect the decision, including but not limited to:

(1) the availability under many qualified retirement plans (QRPs) to undertake distributions commencing at age 55, rather than the age 59½ requirement imposed upon IRAs;

(2) the existence and best methods for undertaking a series of substantially equal periodic payments from traditional IRA accounts using the 72(t) election;

(3) the 2-year-from-inception restriction on distributions from SIMPLE IRA accounts;

(4) the ability to distribute appreciated employer stock from certain QRPs and receive long-term capital gain treatment upon its later sale, under the technique commonly referred to as "net unrealized appreciation";

(5) the most tax-efficient manner to design, implement and manage a client's entire portfolio, which might consist of QRPs, traditional IRAs, Roth IRAs, nonqualified annuities, life insurance cash values, taxable accounts, 529 college savings plans accounts, HSA accounts, and other types of accounts, generally, in order to best secure for the client the likely attainment of the client's objectives;

(6) the ability to undertake due diligence on the investment options within a QRP account, including but not limited to the potential availability of guaranteed investment accounts (and the risks and characteristics of same, including the reduced exposure to interest rate risk which might be present);

(7) the restrictions which exist on the availability of foreign tax credits and/or deductions for foreign stock funds held in certain types of accounts;

(8) the best manner to minimize future potential income tax liability for both the clients and the client's potential heirs, including the role of stepped-up basis;

(9) the availability of tax-managed or tax-efficient stock mutual funds in taxable accounts;

(10) the marginal rates of tax (federal, state and local) which might be imposed upon ordinary income and long-term capital gain income, and qualified dividend income, both in the current year and in future years;

(11) the ways to avoid realization of short-term capital gains and long-term capital gains;

(12) the harvesting of losses in accounts and how such losses may offset either various types of capital gains or ordinary income (up to certain annual limits);

(13) whether Roth IRA conversions should be considered, and if so when and to what extent, whether separate Roth IRA accounts might be established during conversions for different investment assets, and whether re-characterizations might take place thereafter;

(14) whether distributions might be undertaken to generate additional ordinary income, in order to mitigate the effect in any year of the alternative minimum tax;

(15) the increased amount of premiums for Medicare Part A which might result should the client's/clients' modified adjust gross income exceed certain limits;

(16) the effect of additional income resulting from QRP or IRA distributions, or from other investment-related income, on the taxation of social security retirement benefits;

(17) the interplay between the timing of taking social security retirement benefits, income tax itemized vs. standard deduction strategies, the receipt of various forms of income, and the taking of QRP or IRA distributions, given the various marginal income tax rates the client is likely to possess, then and in the future, for both federal and state tax purposes;

(18) the ability to take investment advisory fees from certain types of accounts, the best methods to allocate fees and pay them from various types of accounts, the potential for deductibility of fees when paid from certain types of accounts, and avoidance of prohibited transactions which might otherwise result if fees for non-investment advisory services are incorrectly paid from QRP or IRA accounts;

(19) the ability to delay QRP distributions past age 70½ in certain circumstances, for certain clients;

(20) the availability of lifetime annuitization options for a portion of any QRP or IRA, both inside the QRP and in a rollover IRA, including an evaluation of the single life, spousal (with and without reduced benefits to the survivor), term certain, and combinations of the foregoing, and including further an evaluation of the possible use of CPI adjustments in the annuity contract to keep pace with increased spending needs, and including further the possible use of a staggered approach to annuitization, and including further the available of deferred annuities with payouts commencing at later ages, and including further the risks and return characteristics of certain annuities, the costs and fees associated with same, the possible applicability of premium taxes, the various riders which might be employed and their costs and benefits and limitations; and

(21) the best method to ensure asset protection of the rollover IRA, such as by segregating it from contributory IRA accounts.

As to broker-dealers, dual registrants, and insurance agents, the DOL's requirements for the BIC exemption (with modifications, as suggested above) seem wholly appropriate. The DOL might seek, in its issuing release, to remind fiduciary advisers of the need for a high degree of competence when planning for IRA rollovers and the extensive knowledge required to provide advice on proper structuring of investment portfolios to best secure the client's retirement income needs over the long term or to meet other objectives of the client.

However, for independent registered investment advisers, who are not affiliated with any broker-dealer and who receive no third-party compensation (i.e., compensation from providers of investment products or insurance products), the requirements of the BIC exemption (especially as to the requirement of no discretion) seem inapplicable. These "fee-only" registered investment advisers already agree to adhere to the tough "sole interests" standard found under ERISA and the prohibited transaction rules when providing ongoing investment advice. The conflict of interest that occurs is only in whether to undertake a rollover to an IRA, where the fees paid by the client will be higher than those in the qualified retirement plan account, such higher fees reflective of a higher level of service provided.

Hence, I suggest that the DOL promulgate a new prohibited transaction exemption for advice provided with respect to rollovers from an ERISA-covered retirement plan to an IRA account. This prohibited transaction exemption would be applicable only to independent registered investment advisers who receive no cash payments from any broker-dealer or insurance company. Under this prohibited transaction exemption the following requirements would be imposed, over and above the fiduciary requirements already imposed under ERISA and the various requirements of the SEC and state securities administrators:

1) That the independent investment adviser fully disclose to the client the difference in the amount the client would pay in the estimated total fees and costs if client continued in the client's current qualified retirement plan account versus the recommended rollover IRA, expressed both as a percentage of the amount invested and as a dollar amount (estimated in good faith);

2) That the independent investment adviser fully disclose to the client that the client has other options, including self-managed IRA accounts, and that some options will possess lower fees and costs; and

3) That the independent investment adviser fully disclose to the client that the higher the total fees and costs associated with investments and the delivery of investment advice, the lower the return of the investor, on average, and that such lower returns can significantly affect the size of the investment portfolio over the long term.

Again, this exemption would be limited to independent fee-only registered investment advisers – *i.e.,* those who receive no payments from broker-dealer firms, insurance companies, or investment product manufacturers. Upon the sunset of the BIC exemption, as suggested above, it would be anticipated that all providers of rollover IRA advice would be able to adhere to the "sole interests" requirements of ERISA and its prohibited transaction rules, under this new proposed prohibited transaction exemption.

Since this would be a new PTE, and it is relatively straightforward, I believe that this PTE could be proposed and finalized under the normal timeline for agency rulemaking. There would be no need to delay the rulemaking process for the DOL's Conflicts of Interest Rule and for the BIC exemption and other exemptions the DOL has proposed, simply as a result of the promulgation of this new, simple and limited exemption."

In Conclusion

We've heard from some companies or parts of the financial services and insurance industries that there will be "fewer product alternatives" for retirement investors. If this means that the more conflicted, higher cost, more harmful "products" will be unavailable -- because they are inappropriate when advising in the best interest of retirement investors – it can't happen soon enough.

The Committee believes that any firm can arrange its model to place the investor's best interests before their own, and control and reveal all costs to the investor.

The Committee for the Fiduciary Standard's Five Core Fiduciary Principles:

• Put the client's best interests first;
• Act with prudence, that is, with the skill, care, diligence and good judgment of a professional;
• Do not mislead clients--provide conspicuous, full and fair disclosure of all important facts;
• Avoid conflicts of interest;
• Fully disclose and fairly manage, in the client's favor, unavoidable conflicts.

We applaud the courage and tenacity of the White House and Department of Labor in proposing the Definition of the Term Fiduciary – Conflict of Interest Rule – Retirement Investment Advice. We stand ready to act as a resource as you go forward. We especially commend your steadfastness in the face of immense and formidable opposition. And we wish to help in any way with this rulemaking to ensure that advice to the millions of Americans that are working hard and investing for retirement is, indeed, in their best interests.

Respectfully submitted,

Kathleen M. McBride, AIFA®, Chair
The Committee for the Fiduciary Standard, www.TheFiduciaryStandard.org
POB 492
Rumson, NJ 07760
732.241.4988 kmcbride@FiduciaryPath.com

About The Committee
The Committee was formed in June 2009 by an all-volunteer group of investment professionals and fiduciary experts, just as policymakers and industry leaders were reviewing the repercussions of the financial crisis, to advocate that all investment and financial advice be rendered as fiduciary advice and meet the requirements of the five core fiduciary principles. The Committee's work is pro bono.

The Committee's goal is to advocate for the authentic fiduciary standard. The Committee seeks to help inform and nurture a public discussion on the fiduciary standard. Its objective is to ensure that any financial reform regarding the fiduciary standard, 1) meets the requirements of the authentic fiduciary standard, as presently established in the Investment Advisers Act of 1940, or ERISA, and 2) covers all professionals who provide investment and financial advice or who hold themselves out as providing financial or investment advice, without exceptions and without exemptions. www.TheFiduciaryStandard.org