**TESTIMONY OF**

**KENT A. MASON**

**of**

**DAVIS & HARMAN LLP**

**before the**

**SUBCOMMITTEE ON HEALTH,
EMPLOYMENT, LABOR AND PENSIONS**

**of the**

**HOUSE EDUCATION AND THE
WORKFORCE COMMITTEE**

**for the hearing entitled**

**RESTRICTING ACCESS TO FINANCIAL ADVICE: EVALUATIN THE COSTS AND CONSEQUENCES FOR WORKING FAMILIES AND RETIREES**

**June 17, 2015**

My name is Kent Mason. I am a partner in the law firm of Davis & Harman LLP and I have worked in the retirement plan area for over 30 years. I am currently working with plan sponsors, plan sponsor trade associations, and a wide array of financial institutions on the concerns that have been raised with respect to the Department of Labor's proposed regulation modifying the definition of a fiduciary.

I want to thank you, Chairman Roe and Ranking Member Polis, for holding this hearing and for inviting me to testify. It is important that the critical issues raised by the proposed regulation be addressed in a robust public dialogue.

I am speaking today on my own behalf based on extensive discussions with plan sponsors, plan sponsor trade associations, and numerous financial institutions.

On April 14, the Department of Labor ("DOL") issued a re-proposed definition of a fiduciary applicable to retirement plans and IRAs, along with a set of proposed prohibited transaction exemptions.

In brief, I will make the following points:

- **Industry supports best interest standard.** Contrary to indications from the Administration and statements in the press, most of the industry is completely fine with a best interest standard. The problem with the DOL proposal is not the best interest standard; the problem is the "prohibited transaction rules" that cut off low and middle-income individuals and small businesses from access to personal investment assistance.
- **Small businesses will lose critically needed help in setting up retirement plans.** The seriousness of this problem is well illustrated by expressions of great concern from the U.S. Chamber of Commerce, NFIB, the U.S. Hispanic Chamber of Commerce, and the Small Business and Entrepreneurship Council.
- **Small accounts will lose all access to professional investment advice.** It is well documented that this occurred in the United Kingdom under a very similar rule.
- **Under the current timetable, the following message will be delivered to many millions of individual IRA investors with small accounts *in the fall of 2016:*** *neither their current advisor nor any other advisor can service their accounts because of new government rules.*
- **The DOL proposal would eliminate any meaningful assistance for employees terminating employment regarding their distribution and rollover options.** According to a comprehensive study by former government economists, this would result in $20 billion to $32 billion more in annual leakage from retirement plans.
- **The DOL proposal significantly reduces the scope of permissible investment education.** Even the 2010 DOL proposal did not do this.
- **The DOL proposal inadvertently applies to the simple marketing of health, life, and disability insurance to small businesses, making such marketing arguably impermissible.** This inadvertent error is more evidence that the adverse ramifications of the proposal have not been fully considered.
- **The 2015 proposal is far less workable than the 2010 proposal.**

- **All of this can be solved by legislation establishing a best interest standard, with workable rules that maintain access to investment assistance for low and middle-income individuals and small businesses.**
- **In this context, we need bipartisan legislation.** This proposal can fundamentally alter the private retirement savings system, and there are critically important disagreements about what those effects will be on the retirement security of low and middle-income individuals across the country. Fundamental policy decisions like this are the province of Congress, not the agencies charged with interpreting the law.

## INDUSTRY SUPPORT FOR A BEST INTEREST STANDARD

Under the DOL rules, an advisor's treatment as a fiduciary has two main significances. First, a fiduciary is required to provide advice that is in the best interest of the fiduciary's customer. ***There has been a lot of confusion in public discussions and media reports that state that the industry opposes a best interest standard. That is not the case. The vast majority of the financial services industry is completely fine with being required to act in the best interest of their customers.*** Advisors know that if they do not act in their clients' best interest, they will not have those clients for long.

***The public policy dialogue regarding the fiduciary issue over the last 4 ½ years has never been about the best interest standard. The real debate has been over DOL's "prohibited transaction rules," which under the DOL proposal would cut off access to investment and distribution assistance for low and middle-income individuals and small businesses.*** Under those rules, an advisor cannot provide any advice that could affect the advisor's compensation, in the absence of a prohibited transaction exemption (provided by DOL). Assume, for example, that an IRA owner calls a broker/dealer for advice regarding whether to buy a particular stock. The advisor responds by saying that that stock is regarded as a good value and could help the IRA owner's portfolio. The IRA owner buys the stock, which earns the broker/dealer a commission. Absent an exemption, if the broker/dealer is a fiduciary, the simple favorable statement about the stock purchase is a prohibited transaction under the DOL proposal, regardless of whether the statement is in the best interest of the IRA owner. That is because the broker/dealer earns a commission on the purchase; thus, the broker/dealer's favorable statement led to the broker/dealer earning a commission.

***The Administration's doctor analogy is a perfect analogy.*** The Administration has said:

> When you go to a doctor, you expect that advice you get is in your best interest. If you have cancer, you don't want your doctor telling you what's suitable for you. Rather, you want your doctor telling you what's best for you, and what will maximize the chances of saving your life. But when it comes to financial advice, conflicts of interest can lead to bad advice and hidden fees that too often keep us from getting investment advice that's in our best interest.

The industry is completely fine being subject to a best interest standard like doctors. But to picture the unworkability of the prohibited transaction rules, just imagine if those rules applied to doctors:

- A patient goes to a doctor with ankle pain. The doctor recommends an X-ray – which they do at the doctor's office -- to determine if the ankle is broken. Under the DOL rules, the doctor would have committed a prohibited transaction because the advice to get an X-ray leads to the doctor earning more money attributable to providing X-ray services for a fee. The doctor would be required to send the patient to another doctor for an X-ray.
- ***A patient goes to a doctor with back pain. The doctor prescribes rest and anti-inflammatories, and recommends the patient come back in three weeks for a follow-up visit. The doctor would have committed a prohibited transaction by recommending a follow-up visit, which will earn the doctor more money. The doctor would be required to send the patient to another doctor for the follow-up visit.***

## HIDDEN FEE REFERENCES ARE FICTION

In 2012, the DOL issued rules making hidden fees illegal with respect to retirement plans, which were the product of work by both Democratic and Republican Administrations. Thus, it is somewhat mystifying to hear DOL make reference to hidden fees in 2015. In the IRA market, Richard Ketchum, the CEO of FINRA (which oversees broker/dealers) has noted that FINRA's robust disclosure rules "require that principal trades, commissions, fees and expenses must be disclosed to the customer and . . . require that revenue sharing arrangements with mutual funds generally must be disclosed if they form a basis for the selection of funds that the broker-dealer recommends." Where are the hidden fees?

## OVERALL STRUCTURE OF THE DOL PROPOSAL

The DOL proposal has three basic components:

- **Expansion of the basic definition of the term "fiduciary."** Under current law, a person is treated as a fiduciary if, for a fee, the person provides individualized advice regarding investments on a regular basis pursuant to a mutual understanding that the advice will be a primary basis for decision-making. In other words, there must be a mutual expectation of reliance on the advice.
  - Under the DOL proposal, a person is treated as a fiduciary if, for a fee, the person provides individualized recommendations regarding investments, rollovers, or distributions that could be considered in making decisions. Any recommendation that would be viewed as a "suggestion" that someone take an action – or not take an action – is sufficient. ***So any casual comment that could be considered would give rise to fiduciary status.***
- **Exceptions from the definition of a fiduciary.** The proposal includes exceptions from fiduciary status, i.e., persons covered by the general definition above are not fiduciaries if they fall within certain exceptions, such as an exception for investment education (narrower than under current law or under the 2010 DOL proposal) and an exception for recommendations provided as a seller (not as an advisor) to large plans.
- **Exemptions from the prohibited transaction rules.** For persons that are treated as fiduciaries, the proposal provides limited exemptions from the prohibited transaction rules. The main exemption is the Best Interest Contract Exemption (the "BIC

exemption"). For reasons discussed below, the conditions required to satisfy the BIC exemption are so extensive and onerous as to make it unusable. Effectively there is no exemption.

## EFFECTS OF THE DOL PROPOSAL

The DOL proposal would have the following adverse effects.

**In general**. The framework set up by the DOL could work conceptually, but ***in its current form, it would, like the original 2010 proposal, cut off the option for low and middle-income individuals and small businesses to receive personalized investment assistance, even if that assistance is in the best interest of the recipient.*** This is the case because the BIC exemption is unusable.

**Small businesses could not get help setting up a retirement plan.** When a financial institution talks to a small business owner about possibly setting up a 401(k) plan, the small business owner naturally wants to know if the plan can be established simply and inexpensively, with the financial institution taking care of almost everything. Today, that works well. The financial institution can, for example, provide the plan document, agree to do all the plan administration, and agree to help with all employee communications.

One other key item is selecting the investment options for the plan to offer to employees. Typically, the financial institution has a large portfolio of possible investment options, such as, for example, 2,000 options, but the business likely may only want to offer, for example, 10 or 15 options to its employees. Accordingly, a critical step in setting up a plan is choosing the 10 or 15 out of the 2,000 that the plan will offer. Today, the financial institution can provide "education" to the business owner about which 10 to 15 to choose, without the financial institution becoming a fiduciary. For example, the financial institution could provide examples of investment options offered to employees by similar businesses, including sets of options that are conservative, moderate, and aggressive. The financial institution can explain the difference between the different sets of options and provide additional information that the owner needs to make the right decision for him. (The financial institution will be clear that it cannot make the decision for the business owner and cannot act as a fiduciary, but can provide information and education.)

Under the DOL proposal, the assistance described above regarding the selection of the 10 or 15 investment options would be treated as advice and thus make the financial institution a fiduciary. This would make the assistance a "prohibited transaction," subject to severe penalties. Fiduciary advice is a prohibited transaction if the advice affects how much compensation the fiduciary earns. In almost all cases, the financial institution will make different amounts of money based on which investment options are chosen by the business owner. Some options may be proprietary funds and some may not be. Generally, the non-proprietary funds will pay the financial institution a fee, but the fee varies from fund to fund. Proprietary funds also vary in the management fee charged because certain investment strategies are more expensive to manage than others.[1] So in short, even if the financial institution recommends the best possible funds for

[1] These fees are not hidden. The fees earned both for proprietary and non-proprietary funds **are fully disclosed before the business owner adopts the plan** under DOL's fee disclosure rules.

the business owner to offer to his employees, the advice is a prohibited transaction because the advice affects how much the financial institution earns.

So if the financial institution cannot help the business owner select the 10 or 15 investment options, the owner has two choices:

- Select the investment options himself without any assistance, subject to fiduciary liability. If the owner is not an expert on investments, this would subject the owner to liability, since ERISA holds fiduciaries to an expert standard. A fiduciary *must* seek help and guidance if the fiduciary is not an expert.
- Conduct a diligent search, subject to fiduciary liability, for a qualified independent third party to do the selection ***for an additional fee.***

Neither of the above choices is really viable in most cases, so that there would be far fewer small business plans established. The adverse effects of the original proposal would continue to apply, since the 2015 proposal is, with respect to the small business issue, effectively identical to the original proposal. The adverse effects were powerfully demonstrated by the results of a 2014 survey of small businesses by Greenwald & Associates (which our firm co-sponsored, along with the U.S. Hispanic Chamber of Commerce). For example, the survey found that:

- Almost 30% of small businesses with a plan indicate that it is at least somewhat likely that they would drop their plan if this regulation were to go into effect.
- Close to 50% of small businesses without a plan state that the regulation would reduce the likelihood of them offering a plan, with 36% saying it would reduce the likelihood greatly.

**Small accounts will lose all access to an investment professional.** There are two main ways that an IRA owner can get access to an investment professional: the brokerage model and the advisory model. Under the brokerage model, the amount of the payments to the advisor – such as commissions and payments from a mutual fund (e.g., marketing, recordkeeping, and shareholder servicing fees) – varies based on the investment made. Thus, any advice made under the brokerage model violates the prohibited transaction rules unless an exemption applies. Because the BIC exemption is unusable, the brokerage model is effectively illegal with respect to IRAs and retirement plans under the DOL proposal.

This means that the only source of personal investment assistance for an IRA owner is through an advisory account. However, advisory accounts are not available to small accounts. Under an advisory account, typically, the advisor takes full responsibility for managing the investments on an around the clock basis in exchange for a fee based on the amount of assets, such as a 1% of assets fee. Small accounts are not eligible for advisory accounts in part because the economics cannot work. An advisor cannot accept around the clock liability for $4,000 IRA for an annual fee of $40. Moreover, under the securities laws, an advisory account may not be suitable for a small account (or even a large account) under which the IRA owner simply buys and holds securities. It is not in the best interest of a IRA owner to pay a 1% a year on a security that will likely be held until retirement; it is much less expensive to pay a single commission when the security is purchased.

So small IRA accounts would be entirely cut off from personal investment assistance. This could have devastating effects, since it is advisors who encourage individuals to save, explain how IRAs work, explain how to open and maintain an IRA, explain investment diversification, and encourage individuals to stay in the market during down times and avoid the urge to sell low. In 2011, Oliver Wyman performed an extensive study of 40% of the IRA market, measuring the effect of the 2010 DOL proposal, which would have had the exact same effect as the 2015 DOL proposal. Oliver Wyman found that:

- Over 7 million IRAs could lose access to an investment professional (just within the study sample, which, as noted, was approximately 40% of the IRA market) because the brokerage model, which serves 98% of IRAs under $25,000, would become unworkable with respect to IRAs.
- As many as 360,000 fewer IRAs could be opened every year.

**Lessons from the United Kingdom**. The defenders of the DOL proposal maintain that the industry would never walk away from servicing small accounts because there is too much money to be made. The response is that somehow the industry will figure this out. That is a frightening basis on which to risk the retirement security of low and middle-income individuals: "if the brokerage model becomes illegal, industry will figure out some other way to service small accounts – we don't know what it is, but they will figure it out."

That is effectively what the regulators in the U.K. said before new rules took effect as of January 1, 2013 that have an effect almost identical to the effect of DOL's prohibited transaction rules – making payments from mutual funds illegal. Instead, advisors ceased servicing small accounts in droves, as shown below. Some of these practices were implemented before the U.K. rule went into effect but clearly in anticipation of the rule, as recognized by a study commissioned by the U.K. regulator itself.

- **U.K.'s "big four" banks (an important source of investment advice in the U.K.)**

  - **HSBC:** provided investment advice only for customers with at least $80,000 in total assets or $160,000 of annual income.
  - **Lloyds:** provided face-to-face investment advice only for customers with at least $160,000 in assets.
  - **Royal Bank of Scotland:** charged $800 to set up a financial plan, and made changes to gear investment advice services to high net-worth clients.
  - **Barclays:** provides investment advice only for customers with at least $800,000 in assets.

    These banks previously had entire business arms or strategies providing investment advice to investors with less assets, but just prior to the U.K.'s implementation of its new rule, HSBC, Lloyds, and Barclays completely pulled out of offering investment advice to such investors, and, as noted, Royal Bank of Scotland overhauled its offerings to target high net-worth clients. For example, Barclays closed Barclays Financial Planning, leaving only Barclays Wealth to offer financial advice to individuals with at least $800,000 in assets.

- **Examples of other actions taken.**
  - **Aviva:** ceased offering face-to-face investment advice.
  - **AXA:** ceased offering face-to-face investment advice.
  - **Advisor firm AWD Chase de Vere:** stopped accepting clients with $80,000 or less in assets.
  - **Advisor firm Towry:** stopped accepting clients with less than $160,000 in assets.

- **Millions of small investors will be told in the fall of 2016 that they will no longer be permitted to talk to their advisor.** The Oliver Wyman study lines up exactly with the experience in the United Kingdom and leaves us with a clear picture of the future under the DOL proposal. Based on DOL's time line, the applicability date for the new rules will be some time around January 1, 2017 or slightly earlier. That means that in the fall of 2016 financial institutions will need to deliver the message to millions of small investors that they will no longer be permitted to consult with their advisor for assistance.

**Meaningful assistance regarding rollover and distribution options would be prohibited.** Under the DOL proposal, financial institutions would be prohibited from providing any specific assistance to individuals seeking help with the rollover and distribution process. This is the case in large part because any financial institution providing IRA services would have a conflict of interest with respect to advice regarding the rollover decision, thus creating a prohibited transaction. Most read the BIC exemption in the re-proposal as not covering this type of assistance, thus rendering the assistance categorically prohibited. Others read the BIC exemption as technically applicable to this assistance, but effectively unavailable because of the exemption's unworkable conditions. Either interpretation denies assistance to many in need of help in navigating the retirement savings options that exist after termination of employment. Among many unfortunate consequences, this would cause a drastic curtailment of call center, brokerage, and other assistance to those terminating employment, leading to greatly increased leakage of assets from the retirement system.

***A study conducted by Quantria Strategies LLC found that this could increase annual cash-outs of retirement savings for employees terminating employment by $20 billion to $32 billion. These withdrawals could reduce the accumulated retirement savings of affected employees by 20% to 40%.***

**Elimination of the ability of financial professionals to continue to provide meaningful investment education.** The DOL proposal would significantly restrict the type of investment education that can be provided without triggering fiduciary status and the prohibited transaction rules. Under current law, education includes (1) guidance on the extent to which an individual should invest in different asset classes (such as large and small cap equity funds, and long and short-term bond funds) based on her age and other factors, and (2) examples of investments that fit within such asset classes. This definition of education has worked very well for nearly 20 years, ensuring that a basic level of needed assistance was widely available to retirement investors often with no cost; moreover, this definition was explicitly preserved under DOL's 2010 proposal. Under the 2015 proposal, providing examples of investments that fit within asset classes would be fiduciary advice, not education. Thus, education would be limited to hypothetical and abstract conversations about investment theory that will simply be of little use to most retirement savers. As a result, we will have less informed plan participants who will be less able to put investment education to practical use and will be much less able to make informed decisions about investing their 401(k) account assets.

**Prohibition on promoting your own products, services, or yourself.** With respect to individuals and small businesses, there is no seller's exception from the fiduciary definition, unlike the 2010 DOL proposal. So individualized marketing to individuals and small businesses would be treated as fiduciary advice. DOL's rationale for this is the following: "Most retail investors and many small plan sponsors are not financial experts, are unaware of the magnitude and impact of conflicts of interest, and are unable effectively to assess the quality of the advice they receive." This position is directly contrary to the structure of ERISA and to DOL enforcement positions which place a fiduciary duty on small employers to make prudent fiduciary decisions. It is also cutting off marketing to individuals. The DOL's view seems to be that individuals are unable to process marketing. But if individuals are unable to process marketing, how are they expected to make decisions?

- **Effect of absence of seller's exception.** Let's translate the lack of a seller's exception into real terms with a few examples. One could argue that these results were not intended, but after a four and a half year debate about the need for a seller's exception, and the nature of any such exception, concern levels are high.
    - **Prohibition on promoting a company's own products or services**. A company should be permitted to market its own products and services if it is made completely clear that the company is not providing advice but is selling a product or a service. Unfortunately, such promotion is prohibited with respect to individuals and small plans. Almost any discussion of a company's own products or services with any individual or small business plan is a fiduciary discussion. The result is that companies would be prohibited from, for example, promoting their own services, such as rollover services or managed account services.
    - **Interviews to be hired.** Assume that a broker is interviewing with a prospective customer and asking that she be hired to help with the customer's IRA. She talks about her firm and her hard work and her dedication to her customers. She does not make any investment recommendations. Under the proposal, the broker is acting as a fiduciary. In fact, the individual would actually be committing a prohibited transaction by recommending that she be chosen. Obviously, that is an absurd result, but the fact that this result is inherent in the structure of the proposal says a lot about how the proposal is structured far too broadly.
    - **How do we know the difference between the absurd results that are not intended and the very strange results that may be intended?** It is not enough to say that the above examples were not intended and cannot be the law. There is no hint in the proposal regarding what promotion by a financial services provider is permissible and what promotion is prohibited, leaving all of us to make guesses. Unfortunately, this lack of clarity is built into the structure of the proposal.

## ADDITIONAL ANALYSIS AND CONCERNS

**The BIC exemption is unusable**. Initially, there was hope that the BIC exemption would address many of the concerns that had been raised with respect to the original proposal. For many reasons, however, as noted above, the BIC exemption is unusable. For example:

- **The BIC exemption does not even apply to advice provided to small businesses.** With rare exceptions, small business 401(k) plans permit employees to direct the investment of their own account. The BIC exemption does not apply to advice provided with respect to any such plan.
- **The BIC exemption only applies if a contract is entered into before discussions begin.** So an individual who wants to interview different advisors, the individual would have to enter into contracts with all those advisors before talking to them, which simply would not happen.
- **The BIC exemption only applies to individual advisors who sign a contract.** So if an individual advisor is on vacation or leaves her employer, a new contract would be needed.
- **The BIC exemption requires disclosure of an unimaginable amount of detailed information.** The advisor's company must maintain a webpage with detailed information – updated at least quarterly -- about all direct and indirect compensation payable to the adviser, his company, and all company affiliates with respect to ***every single asset*** purchased, sold, or held by a retirement customer during the last 365 days (excluding only certain assets not commonly purchased). In addition, the webpage must include the same information about ***all assets that a retirement customer could possibly purchase (subject to the same exclusion).*** It is hard to imagine that almost anyone would be able to process this staggering amount of data, which would be extremely costly to provide.
- **Inconsistent with existing DOL rules.** Every year, the advisor must provide information to the customer about that year's transactions, including the total dollar amount of all indirect compensation received by the adviser and his company during the year attributable to the customer. We understand that systems do not exist that could produce this data. Also, this data is very different from existing DOL requirements about disclosing indirect compensation.
- **Predictions of future investment performance required.** Before a recommended purchase of an asset is made, the advisor must provide a chart to the customer with the "Total Cost" of the asset over 1, 5, and 10 year periods, as a dollar amount, ***which requires the advisor to make assumptions about future investment performance.***

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**There is no way to comply with the applicability date.** The proposal provides eight months to analyze and understand lengthy final regulations and exemptions that we have not yet seen, make business decisions that affect the entire retirement business, restructure that business, revise compensation packages and structures for advisors, renegotiate fee arrangements, design and implement company policies and procedures, create and modify systems to produce an unprecedented amount of new data, draft contracts for IRA owners across the country, and enter into contracts with tens of millions of existing customers. That will take a minimum of two years; eight months is simply not realistic.

- **Feasibility of entering into contracts with all existing customers.** A financial institution has no way to compel existing customers who are not actively using their services to enter into any contract. So not only is the applicability date unrealistic, the entire contract requirement is problematic as a transition matter.
- **Transition rule inadequate.** The proposed transition rule protects assets purchased by the applicability date but does not protect (1) assets purchased after the applicability date pursuant to advice given before the applicability date, or (2) advice provided after the applicability date that was paid for before the applicability date.

**None of the above issues, which have been raised for four and a half years, received the attention they deserved at OMB.** OMB's 50-day review of the re-proposal was startlingly brief:

- The review period *was almost a month shorter* than the next shortest review period for any significant retirement regulatory proposal in the last 10 years.
- It was less than half the average review period of other significant retirement regulatory proposals in the last 10 years (which was 109 days).
- Equally startling is that the review period after OMB received significant public input was actually just a few days. For example, a critical meeting to discuss new information was held on April 9, 2015, and the DOL proposal was issued on April 14, 2015, a mere five days later.

**Insurer promotion of its own health, life, and disability products**. The proposal would convert the promotion by an insurer (or its agent) of the insurer's own group health,[2] life, and disability insurance products to small businesses (or their fiduciary, such as a broker) or employees (of employers of any size) into fiduciary acts even in circumstances where no plan assets are held in trust. In other words, an insurer would be treated as a fiduciary with respect to certain welfare benefit plans simply by reason of promoting its own products.

If the promotion of these insurance products to small businesses (or their broker/fiduciary) or employees does become a fiduciary act, (1) the insurer would be vulnerable to a lawsuit simply for selling its own product without sufficiently considering the advantages of competitors' products, and (2) it is unclear whether a prohibited transaction exemption would be available to permit the continued sale by an insurer of its own insurance products to small businesses.

This result might seem counterintuitive, especially because DOL did not, in the preamble to the proposal, address this issue or provide any analysis of the economic effects of this aspect

[2] All references herein to health insurance also include dental, vision, and other similar forms of health-related insurance coverage.

of the proposal. Nonetheless, DOL's proposal applies to the sale of common employment-based insurance. There are several steps in the analysis of this issue.

- **<u>The ERISA definition of "fiduciary" applies by its terms to both retirement plans and welfare benefit plans.</u>** Under ERISA, the term "fiduciary" applies by its terms to all types of plans, including both retirement plans and welfare plans. Moreover, the DOL proposal explicitly defines a "plan" covered by the fiduciary proposal as including both retirement plans and welfare benefit plans. See § 2510.3-21(f)(2)(i).
- **<u>The DOL proposal applies to any "recommendation as to the advisability of acquiring . . . securities or other property."</u>** Under the proposal and generally, it is clear that insurance contracts are "property." For example, the DOL proposal uses the term "Asset" to refer to a specific subset of property both covered by the new definition and eligible for an exemption. The term "Asset" is defined to include insurance contracts. See Section VIII(c) of the Proposed Best Interest Contract Exemption.
- **<u>The DOL proposal only applies to advice regarding the property of a plan or IRA; this requirement is satisfied too.</u>** Under longstanding DOL rules, if employees contribute toward the cost of benefits, such as health, life, or disability insurance, the employee contributions are considered property of a welfare benefit plan, even if the contributions are not held in trust. See 29 C.F.R. § 2510.3-102; DOL Advisory Opinion 96-12A. Thus, in every case where employees contribute to the cost of a plan, advice regarding the insurance products is advice regarding the property of a plan.
- **<u>The advice is rendered for a fee.</u>** Under the definition of fiduciary investment advice, the advice must be rendered for a fee or other compensation, direct or indirect. The DOL has long taken the position that this does not require a separate fee for the advice; on the contrary, it is sufficient for the advisor to receive compensation in connection with the recommended transaction, as clearly occurs when an insurer receives premiums for health, life, or disability insurance. If this were not the rule, financial institutions would, for example, be able to give free advice to purchase their own proprietary investment products and thus avoid fiduciary status.
- **<u>The DOL proposal specifically treats individualized marketing to small plans and individuals as fiduciary advice, not as marketing.</u>** Under the proposal, individualized marketing to large plans can be selling, not advising; individualized marketing to small plans and individuals cannot be selling, but rather is treated as investment advice. See § 2510.3-21(b)(1). DOL explains this rule in the preamble to the proposal: "in this retail market [for small plans and individuals], a seller's carve-out would run the risk of creating a loophole that would result in the rule failing to improve consumer protections. . . ." It is this dramatic change in position, from both current law and the 2010 DOL proposal, that causes this issue to arise.

Let's put the above points together in the context of a simple example. An insurer markets its group-term life insurance product to employees of any size employer in a situation where employees are required to contribute toward the cost of the plan. The insurer, as expected, promotes the virtues of its product, as compared to its competitors' products. Under the DOL proposal, this promotion is fiduciary advice because:

- Individualized marketing to an employee is advice under the proposal.

- The advice is for a fee, i.e., the premium that would be paid for the insurance.
- The advice relates to the acquisition of property, i.e., the insurance contract.
- The advice relates to the use of plan property, i.e., the employee contributions.
- The advice is specifically directed to the employee for her consideration.
- The advice relates to an ERISA plan, i.e., a group-term life insurance plan.

DOL informally indicates that the above result was not intended. But the above result very clearly flows from the actual language of the proposal and is further evidence that the full adverse ramifications of the proposal are not fully understood.

## THERE IS A VERY STRAIGHTFORWARD SOLUTION

**After 4 ½ years and massive input, the DOL proposal got much worse between 2010 and 2015.**

- The 2010 proposal preserved investment education; the 2015 proposal significantly restricted such education.
- The 2010 proposal permitted financial institutions to do direct marketing of their products to individuals and small businesses; the 2015 proposal does not.
- The 2010 proposal permitted financial institutions to provide meaningful distribution and rollover assistance; the 2015 proposal does not.
- The 2010 proposal did not provide any prohibited transaction relief; the 2015 proposal provides unusable relief.
- There are very small improvements in the 2015 proposal, mostly addressing glaring glitches in the 2010 proposal, such as clarifying that ads on television are not fiduciary advice.

**We need legislation establishing a best interest standard with workable rules that preserve access to investment assistance for low and middle-income individuals and small businesses.** The industry is completely fine with a best interest standard and is ready to support legislation that would establish a best interest standard with workable rules that preserve consumer choice and access to information.

**Bipartisan legislation is the right answer.** The DOL proposal can fundamentally alter the private retirement savings system, and there are critically important disagreements about what those effects will be on the retirement security of low and middle-income individuals across the country. Fundamental policy decisions like this are the province of Congress, not the agencies charged with interpreting the law.