IMPACT OF THE DOL FIDUCIARY RULE ON THE CAPITAL MARKETS

HEARING

BEFORE THE

SUBCOMMITTEE ON CAPITAL MARKETS, SECURITIES, AND INVESTMENT

OF THE

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IMPACT OF THE DOL FIDUCIARY RULE ON THE CAPITAL MARKETS

Thursday, July 13, 2017

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON CAPITAL MARKETS,
SECURITIES, AND INVESTMENT,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10:03 a.m., in room 2128, Rayburn House Office Building, Hon. Bill Huizenga [chairman of the subcommittee] presiding.

Members present: Representatives Huizenga, Hultgren, Stivers, Wagner, Poliquin, Hill, Emmer, Mooney, MacArthur, Davidson, Budd, Hollingsworth; Maloney, Sherman, Lynch, Scott, Himes, Foster, Sinema, Vargas, Gottheimer, and Gonzalez.

Ex officio present: Representative Waters.

Also present: Representative Delaney.

Chairman HUIZENGA. The Subcommittee on Capital Markets, Securities, and Investment will come to order. Without objection, the Chair is authorized to declare a recess of the subcommittee at any time.

Today's hearing is entitled, "The Impact of the DOL Fiduciary Rule on the Capital Markets."

And I now recognize myself for 2 minutes to give an opening statement. Now more than ever, sound financial advice has become critical for every individual looking to invest and save for their future. Every day, millions of Americans are working to achieve financial independence by using an investment adviser or a broker-dealer to help them plan and prepare for a prosperous retirement.

However, the Department of Labor's complex fiduciary rule not only fails to protect customers, it harms them by driving up costs and limiting investor choice. According to research by the American Action Forum, the DOL fiduciary rule is the most expensive regulatory action of 2016, and the second-most expensive non-environmental rule since 2015. The rule has the potential to increase consumer costs by $46 billion, or approximately $800 annual per account—$800 annually per account—in addition to the $1,500 in duplicative fees for retirement savers that have already paid a fee on their commission-based account.

So not only is the DOL denying American savers and small business access to investment advice, and limiting their choice in investment products, but it is also crippling them with added costs. Why is the Federal Government paralyzing hard-working Americans who are trying to save for retirement?

Like so many big government policies, this misguided rule hurts the very people it supports, claiming that it would help low- and middle-income families. By increasing costs, the fiduciary rule is having a direct effect on the marketplace and forcing advisers to limit their services to only those accounts that can handle higher costs. This ultimately prices out the low- and middle-income savers who would benefit the most from having access to this information and financial advice.

How is this in the best interest of those trying to save for their retirement? The Federal Government should not be limiting consumers' choices as Americans work towards achieving retirement savings goals. Instead, the Federal Government should be providing these investors with the tools that they need to build a better future.

As the numbers rise of the millions of American families who are unable to save for retirement, Congress should be making it easier for these families to save, not making it more difficult. This should be an issue where Members of both parties can stand together. Putting the interests of hard-working Americans first is the only way that the government can help all savers achieve financial security.

I look forward to hearing from our witnesses today. And the Chair now recognizes the ranking member of the subcommittee— well, actually, I think we are going to have the ranking member do her opening statement and then I have a couple of other folks on our side of the aisle. So with that, the Chair now recognizes the ranking member of the subcommittee, the gentlelady from New York, Mrs. Maloney, for 5 minutes for an opening statement.

Mrs. MALONEY. Thank you for calling this hearing. And I thank our distinguished panelists for being here today.

This hearing addresses a very important issue: the Department of Labor's fiduciary duty rule. I am a supporter of the rule because it provides critical protections to Americans who are saving for retirement. And I am glad that even the Republican Labor Secretary, Secretary Acosta, appears to agree that the fiduciary rule is an important protection that should not be tossed out.

The fiduciary rule is a much-needed update of the rules governing investment advice to retirement savers. And it will plug some key holes in our regulatory system. The rule advances a very simple principle: If you are giving investment advice to our retirement savers and you are being compensated for your advice, then you have to put your customers' interests first. This is just common sense and no one would oppose this principle.

We should also remember that most investors already think it is the law, even though it isn't. So really, the DOL rule is simply updating the law to reflect what investors already believe is the law.

When President Trump took office, he required the Labor Department to conduct a review of the fiduciary rule to determine whether or not the start date for the rule should be delayed, either for a short period of time or indefinitely. After conducting the review, the Labor Department concluded that it could not justify delaying the start date for very long and ordered that the core aspects of the fiduciary rule would take effect on June 9th.

This conclusion was based on the overwhelming benefits that investors will enjoy under the rule. According to the Council of Economic Advisers, this rule will save consumers roughly $17 billion—that is "billion"—per year. The Labor Department ran its own numbers again and concluded that delaying implementation of the rule past June 9th would simply be too costly for retirement investors.

Now, I know there were some concerns about the implementation of this rule when it was first proposed back in 2015. But instead of simply opposing the entire rule, some of us—particularly on the Democratic side—actually engaged with the Labor Department and got the vast majority of those technical issues fixed in the final rule. I wrote my own letter to the DOL on the proposed rule asking for six technical fixes and clarifications, and DOL made all six changes that I asked for in the final rule.

And I was very pleased with the final rule because I believe that it properly balances the need to protect retirement investors with the need to streamline compliance costs. Unfortunately, this hearing will also address yet another legislative proposal that would repeal the fiduciary rule. I am disappointed that we are going through this exercise again.

How many more times do these efforts to repeal the fiduciary rule need to fail before my colleagues on the other side of the aisle realize that this is not a productive use of time and that the only realistic way to make changes to the rule is to engage with the Labor Department on reasonable changes that don't harm investors? Believe me, they are responsible. Every issue that I am aware of that my constituents raised, the DOL addressed, and they took care of six that I raised myself.

By repealing the fiduciary rule, this bill would leave millions of Americans saving for retirement without the protections that we have seen time and time again are necessary. According to a letter from the Consumer Federation of America, this bill will, "dramatically weaken existing protections for retirement savers without providing meaningful new protections for investors in non-retirement accounts."

I would like to enter this letter into the record, and the letter that I wrote myself that achieved the changes.

Chairman HUIZENGA. Without objection, it is so ordered.

Mrs. MALONEY. So I am very concerned that by repealing the DOL rule, and replacing it with a watered-down vague standard that wouldn't even take effect for a year-and-a-half, this bill would undermine the retirement security of millions of middle-class Americans, but I look forward to a robust debate and to hearing from our witnesses. And I do want to note that this was one of President Obama's major goals, because he felt like it would help and protect people.

I yield back. Thank you.

Chairman HUIZENGA. The gentlelady's time has expired. The Chair now recognizes the gentleman from Illinois, the vice chairman of the subcommittee, Mr. Hultgren, for 1 minute.

Mr. HULTGREN. Thank you. I would like to thank Chairman Hensarling for his help in getting this hearing today, but especially Chairman Huizenga for all his work of convening this and pulling together a great panel to be able to present to us. I have been proud to work with them and others to fight for retirees in my district and across the country to protect their access to retirement advice and the investment products that will help them build their nest egg that they will need.

As someone who is a licensed financial adviser, I am extremely concerned with the overly prospective regulatory framework that the Department of Labor has proposed for retirement accounts. As I said before and as we have discussed in this committee over and over, the Obama Administration's fiduciary rule is not workable. My constituents, especially those with low retirement account balances, cannot afford for this rule to go into effect as currently proposed.

If we are going to institute a fiduciary standard, we need to do it right. That is why I have supported efforts such as the legislation sponsored by my colleague, Ann Wagner, for the Securities and Exchange Commission, the primary investor protection regulator, with the proper expertise and resources to act first and be generally more engaged in this process.

I look forward to the witnesses' testimony today so this committee can understand the compliance challenges that are underway and so we can hear recommendations on what actions Congress can take now that the Labor Department's rule is finalized.

Chairman HUIZENGA. The gentleman's time has expired. I now recognize the gentlelady from Missouri, Mrs. Wagner, for 2 minutes. She is the author of the discussion draft that in the first article repeals it, but in the second then puts in an SEC regime. And with that, the gentlelady is recognized for 2 minutes.

Mrs. WAGNER. Thank you, Chairman Huizenga. This is a very important hearing today focusing on a critical issue that threatens the access of affordable and reliable retirement investment advice for millions of low- and middle-income Americans.

America is in a retirement savings crisis today. And Washington needs to be empowering individuals to save for retirement, not making it more difficult. The current Department of Labor fiduciary rule will leave Americans who are just starting to build their retirement savings without access to financial advice or paying more for fewer options and decreased service.

Republicans on this committee have for years been warning about the harmful effects this rule will have. And unfortunately, we are starting to see those with the rule now partially in effect on June 9th. I look forward to hearing our witnesses discuss their experiences and observations of the market leading up to and after the rule's implementation.

To remedy these issues we have seen develop, I have prepared, in fact, a discussion draft as the chairman has noted, for consideration that would apply a workable best-interest standard for broker-dealers when providing investment advice without losing access for such advice for millions of low- and middle-income investors.

This legislation would also keep this issue under the jurisdiction of the SEC, the expert regulator who has the experience of overseeing the industry. Broker-dealers should provide advice that is in their customers' best interest. And this draft bill will make that absolutely clear with a standard that applies to both investment and retirement accounts, unlike the Department of Labor's rule.

Mr. Chairman, this has been a bipartisan issue in the past, and I would like to thank my colleagues on this committee across the aisle who have worked with me in the past on this. And I hope that we can all work on this draft bill together going forward. I yield back.

Chairman HUIZENGA. The gentlelady's time has expired.

Today, we welcome the testimony of a great panel in front of us here. First, we have Mr. David Knoch, president of 1st Global, on behalf of the Financial Services Institute.

Second, we have Mr. Mark Halloran, senior director, head of industry and regulatory strategy for Transamerica, on behalf of the American Council of Life Insurers.

Third, we have Mr. Jerome Lombard, president, Private Client Group at Janney Montgomery Scott, LLC, on behalf of the Securities Industry and Financial Markets Association.

Fourth, we have Ms. Cristina Martin Firvida, director of financial security and consumer affairs for AARP.

And last but not least, we have Dr. Douglas Holtz-Eakin, president of the American Action Forum.

Each of you will be recognized for 5 minutes to give an oral presentation of your testimony. And without objection, each of your written statements will be made a part of the record.

With that, Mr. Knoch, you are recognized for 5 minutes.

STATEMENT OF DAVID KNOCH, PRESIDENT, 1ST GLOBAL, ON BEHALF OF THE FINANCIAL SERVICES INSTITUTE

Mr. KNOCH. Good morning, Chairman Huizenga, Ranking Member Maloney, and members of the subcommittee. I am David Knoch, president of 1st Global based in Dallas, Texas. I am a certified investment management analyst with nearly 20 years of experience in the financial services industry.

1st Global is the largest independently-owned wealth management partner to CPAs and legal firms across America. I am here representing the Financial Services Institute, which advocates on behalf of independent financial advisers and independent financial services firms, and is a strong supporter of a uniform fiduciary standard.

I am here today to discuss the DOL fiduciary rule and its impact on retirement savers. I believe strongly that the DOL rule adds unnecessary complexity to an already complicated regulatory environment. The DOL rule's intricate regulatory framework raises new barriers to serving millions of Americans. Let me start by sharing some examples of problems with the rule, beginning with its impact on investors. In many cases, investors with small account balances are losing access to lower-cost, commission-based solutions due to the DOL rule.

For example, one of the lowest-cost methods for clients to own mutual funds is to custody them directly with the mutual fund company, often known in our industry as direct business. Since 2016, the number of accounts held by our clients directly with mutual fund companies has dropped nearly 10 percent, and the number of new accounts established has dropped 19 percent during the first 6 months of 2017. We expect this trend to accelerate and by the end of this year anticipate that the total number of accounts held in these programs will drop by more than a third.

We are also challenged to offer a viable, cost-effective solution for small employer retirement plans, particularly simple IRAs, where account balances can be as low as $100. Many of these accounts are offered on a commission basis and will be subject to the best-interest contract. Due to the threat of class-action lawsuits, many of our affiliated firms will no longer offer these plans to small-business clients and some will end their existing relationships. In fact, since the start of 2016, we have seen the number of simple IRA accounts drop by over 20 percent. We project that these accounts will shrink from the 2016 levels by 28 percent before the end of this year and by 41 percent by the end of 2018.

Furthermore, the DOL rule creates significant new disclosures that are cumbersome and expensive to create, will confuse investors with their sheer volume and complexity, and are simply not necessary to hold financial advisers to a fiduciary standard of care. As of the January 1st applicability date for a small, commission-based account which can be opened with as little as a $50 initial investment utilizing the best-interest contract exemption, our clients will receive nearly 100 pages of paperwork, with 70 of those pages being disclosures.

When the prospectus is added, disclosure pages grow to 81 percent of the total 145-page paperwork burden imposed on clients, all to open a $50 account.

Now, finally, my testimony would not be complete without dedicating at least one paragraph to defend the honor of the CPA financial advisers I have the privilege to serve. Every CPA financial adviser I know was called to serve for two reasons: they enjoy solving complex problems; and they enjoy doing good for others. And offering financial services to their clients lies at the intersection of this calling.

These people do what is right for their clients, not because of a rule or a standard of care, but because it is simply the right thing to do. Clients in our industry need reasonable and effective regulation, and it is a dishonor to the vast majority of our profession who are called to serve their communities first and happen to earn a living for doing so to assume they are only acting in their own self-interests. It is simply not what I see.

What I see is the family member suffering from cancer who can focus on his recovery because his financial affairs are in order. Or the widow who relies on her financial adviser to transition to life without her spouse. Or the person entering retirement who can enjoy the fruits of their hard work because they have an adviser who helped them plan and save and who now guides them on living a dignified life sustained by the power of choice.

My wish for you is to see what I see and help independent financial advisers like ours all across America serve more clients, serve them better, and serve them more completely by reducing their regulatory burden without reducing the standard of care. I thank the chairman, the ranking member, and the rest of the subcommittee for allowing me to share my thoughts on this matter, and I look forward to answering your questions.

[The prepared statement of Mr. Knoch can be found on page 70 of the appendix.]

Chairman HUIZENGA. In a rare move, the gentleman yields back with additional time. So, thank you.

Moving on, Mr. Halloran, you are recognized for 5 minutes.

STATEMENT OF MARK HALLORAN, SENIOR DIRECTOR, HEAD OF INDUSTRY AND REGULATORY STRATEGY, TRANSAMERICA, ON BEHALF OF THE AMERICAN COUNCIL OF LIFE INSURERS (ACLI)

Mr. HALLORAN. Chairman Huizenga, Ranking Member Maloney, and members of the subcommittee, thank you for the opportunity to testify before you today on behalf of the American Council of Life Insurers.

As was stated, I am the senior director of industry and regulatory strategy at Transamerica. Transamerica is one of the Nation's largest providers of financial products, insurance, and annuities. And we work with Americans to help them save for retirement, insure against risk, and build solid financial foundations.

ACLI supports reasonable and appropriately tailored rules that require all sales professionals to act in the best interests of customers. Rules impacting savings and in particular retirement savings must be appropriately tailored, effective, straightforward, and consistent, and provide America's savers and retirees with the ability to achieve their financial and retirement security goals.

A best-interest standard should protect the interests of retail investors and ensure consumers can access the full range of financial advice and products. A best-interest standard should be administered by the prudential regulators that have the most expertise and experience in investor protection and financial markets. The SEC and the State insurance regulators are best-positioned for that role and are the appropriate authorities for oversight of financial professionals.

The SEC, state insurance regulators, and the Department of Labor should work together to establish a harmonized standard of care that applies across the entire relationship between financial professionals and consumers. We are very encouraged by the recent statements in this regard by the SEC and the DOL with respect to their plans to work together in this regard, as well.

ACLI supports a discussion draft being reviewed by the subcommittee at today's hearing. ACLI thanks Chairman Huizenga, Representative Ann Wagner, and the other members of the subcommittee for their strong leadership on this issue.

The best-interest standard under the discussion draft would apply holistically to recommendations regarding any asset, not just the one dimension of the relationship that involves ERISA plan and IRA assets. The standard would be consistent across all aspects of consumers' finances, providing clear and consistent rules for both financial professionals and consumers.

The discussion draft harmonizes the various bodies of law and regulation applicable to the sale of insurance and annuity products at the retail level. To harmonize the regulation of advice to retail investors, the discussion draft facilitates coordination by the appropriate prudential regulations. The draft bill sensibly places responsibility for issuing regulations in the hands of the primary prudential regulators: the SEC; and the State insurance regulators.

Importantly, the draft bill would also place a statutory obligation on the SEC to coordinate and cooperate with State insurance regulators. The draft would also install important statutory safeguards to permit transaction-based financial professionals, including broker-dealer registered representatives and insurance agents, to continue to offer products and services to retail customers under traditional compensation models. These safeguards would effectively preserve retail investor access to information, freedom of choice over how to pay for financial advice, and a robust competitive marketplace for insured retirement solutions.

The Department of Labor's fiduciary rule is the wrong approach because it harms middle-income savers and limits consumer choices. However well-intentioned the rule is, it makes it much harder for the average American family to access financial advice and save for retirement.

The fee-based advice model favored in the DOL regulation may not always be the right model for the small and medium account holders. That is particularly true for buy-and-hold investors and purchasers of annuity products that are designed for long-term retirement goals. Many fee-based arrangements do not include options of the purchase of annuities, which are the only products available to consumers and retirees that guarantee lifetime income.

Furthermore, the DOL regulation is diminishing access to advice at a time when financial advice is more important than ever. An advice gap has developed for small and medium retirement accountholders who do not meet the higher account minimums for fee-based arrangements. Less advice from financial professionals can contribute to reduced savings on the part of working Americans and diminished retirement security for retirees in need of guaranteed lifetime income through annuities.

The discussion draft would ensure that consumers have more access to information and advice and more choices about how to pay for advice. Thank you for the opportunity to testify today, and I look forward to answering any questions you may have.

[The prepared statement of Mr. Halloran can be found on page 57 of the appendix.]

Chairman HUIZENGA. Thank you. I appreciate that.

Mr. Lombard, welcome. We appreciate you being here and your time here. And with that, you are recognized for 5 minutes.

STATEMENT OF JERRY LOMBARD, PRESIDENT, PRIVATE CLIENT GROUP, JANNEY MONTGOMERY SCOTT, LLC, ON BEHALF OF THE SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION (SIFMA)

Mr. LOMBARD. Thank you, Chairman Huizenga, Ranking Member Maloney, and distinguished members of the subcommittee. I am Jerry Lombard, president of the private client group at Janney Montgomery Scott.

I greatly appreciate the opportunity to testify today on behalf of the Securities Industry and Financial Markets Association (SIFMA), and share our perspective on the best path forward to establish a best-interest standard for the broker-dealer industry. We are grateful to this committee for its willingness to consider legislation that would allow the Securities and Exchange Commission to establish a best-interest standard for broker-dealers that would create a high standard of care for retail clients across all accounts.

On June 9th, some key provisions in the Department of Labor's fiduciary rule became applicable. And as an industry, we are beginning to see the harmful impact on America's retirement savers, limiting product choice and access to advice while increasing costs. At Janney, we have already experienced many of these issues. Our customers and advisers are very confused by the phalanx of new DOL rules applying to retirement accounts. They do not understand why there are now two sets of rules, one for retirement accounts and one for taxable brokerage accounts.

Since June 9th, clients are now restricted from making certain investments in their retirement accounts. By years-end, we estimate upwards of 10,000 of our client retirement accounts, about 1 in 8, will be relegated to a no-advice service desk as they are too small for the risks imposed by the DOL or too costly to be placed into an advisory account that would remove the supposed conflicts the DOL is trying to relegate. How switching small retirement savers from a full service adviser to a no-advice service desk is in these clients' best interest, I will never understand.

It is the position of SIFMA that the right answer for investors is a consistent best-interest standard that could apply across all types of accounts, but does not have the additional onerous conditions created by the DOL rule. A best-interest standard done right by the SEC, the expert agency responsible for broker-dealer standards of conduct, would provide protection for retail clients without a bifurcated compliance regime imposed on those same market participants by different regulators.

We are greatly encouraged by the SEC's June 1st request for public comment on standards of conduct for investment advisers and broker-dealers. It is SIFMA's intention to share with the SEC our desire that they consider establishing a best-interest standard for broker-dealers that mirrors the elements of the impartial conduct standards under the DOL rule, but unlike the DOL rule would apply across all broker-dealer accounts, not just retirement accounts. For that reason, the DOL should at a minimum delay the January 2018 applicability date to allow the SEC to lead the effort to put in place a standard that works for all accounts.

Congresswoman Wagner's legislative draft provides this path forward by establishing an SEC-applied principles-based standard to ensure that all broker-dealer recommendations about securities are driven by the best interest of retail clients. We firmly believe that this approach would provide a number of significant regulatory efficiencies and investor protections, benefits which would enhance the existing suitability obligation under FINRA rules to create a heightened and more stringent best-interest standard for the benefit of retail clients, apply across all security recommendations made to retail clients in all broker-dealer accounts, not just limited to IRA accounts, build upon and fit seamlessly within the existing and longstanding securities regulatory regime for broker-dealers, coupled with robust examination, oversight, and enforcement by the SEC, FINRA, and state securities regulators, and be akin and well-aligned with the investment adviser standard under the Advisers Act, insofar as the new standard would include a duty of loyalty and a duty of care, an obligation to manage investment costs, and would require upfront disclosure to clients of important information.

Thus, we greatly appreciate Congresswoman Wagner's work on this legislative discussion draft, and we look forward to continuing to work with her and this committee on language that ensures the best-interest standard established in the bill operates in harmony and consistency with all existing standards of conduct, including the current broker-dealer, investment adviser, and DOL rule regulatory frameworks, as well as any future rulemaking by the SEC or FINRA.

In doing this, we will help relieve America's retirement savers from the burdens that have already arisen as a consequence of the DOL's misguided rule. Thank you.

[The prepared statement of Mr. Lombard can be found on page 89 of the appendix.]

Chairman HUIZENGA. Thank you.

Ms. Firvida, you are recognized for 5 minutes.

STATEMENT OF CRISTINA MARTIN FIRVIDA, DIRECTOR, FINANCIAL SECURITY AND CONSUMER AFFAIRS, AARP

Ms. FIRVIDA. On behalf of our 38 million members and Americans saving for retirement, AARP thanks Chairman Huizenga, Ranking Member Maloney, and the members of the subcommittee for the opportunity to testify today. AARP has enthusiastically supported the fiduciary rule requiring retirement advice that minimizes conflicts, is solely in the interest of the investor, and which is provided with the care, skill, and diligence that a prudent person would use.

Today, we are joined by several AARP members who are here to show support for your rule. In 2015, AARP members submitted close to 60,000 messages to the Department of Labor and delivered over 26,000 petitions to the House Financial Services Committee. You have those petitions before you today.

We are frequently communicating with our members about the rule, including in multiple articles in the AARP bulletin, which is the world's largest circulation publication. In surveys, we have always found that people overwhelmingly want fiduciary advice. In collaboration with the North American Securities Administrators Association, we have also developed a tool to help investors determine if their adviser is a fiduciary.

Many States also agree that the fiduciary rule is needed. Earlier this year, nine attorneys general, including the AGs from New York and North Carolina, sent supportive letters to the Department of Labor. Additionally, five States, including Missouri, already impose a fiduciary standard on brokers in their States. Most recently, Nevada established a fiduciary standard with the support of AARP.

The financial services industry itself generally agrees that investment advice should be provided in the best interests of investors, which is unsurprising, given that these standards have been in place since ERISA was enacted in 1974. Indeed, registered investment advisers and certified financial planners have for decades successfully provided fiduciary advice.

Repealing the fiduciary rule would be very costly to retirement investors. Savers could lose 17 percent of their 401(k) account over 20 years and close to 25 percent of the account over 30 years as the result of conflicted advice. That is the equivalent of 5 years of retirement income.

The risk of loss is greatest for IRA investors who are moving their life savings from a more protected 401(k) to a significantly less protected IRA. Small accounts are especially vulnerable to conflicted advice because they have fewer economic resources to replace lost savings.

The rule has overall resulted in lower fees and better financial advice for savers. Many firms have already incurred compliance costs, but we have not seen prices increase for investors served by those companies. New products and services have developed to meet consumer demand for lower fees and greater transparency, and the rule does not prohibit any type of product or service.

Given the nearly $8 trillion in assets in IRAs and the almost $5 trillion in 401(k) plans, AARP is confident that financial firms will continue to innovate and compete for America's nest egg.

AARP does agree that the Securities and Exchange Commission should act in addition to, but not in lieu of, the Department of Labor. We appreciate that that draft bill seeks to impose a best-interest standard on broker-dealers, but the bill fails to define that standard as a fiduciary standard, which the bill does not strengthen and which may even meet the bill's benchmark.

Many brokers market themselves today as financial advisers, and investors can bear high costs for investments that satisfy a suitability standard but not a fiduciary standard. The bill does not specify how conflicts should be managed. Disclosure alone is not adequate and neither compels mitigation of nor shields investors from conflicts of interest.

Finally, the draft bill could potentially preclude both the Securities and Exchange Commission and the Department of Labor from taking action to adopt stronger protections for investors even if the market evolves with unanticipated consequences.

We thank the committee for the opportunity to share AARP's views on the Department of Labor's fiduciary rule and on the draft bill which would repeal that rule and replace it with a discretionary best-interest standard for broker-dealers. AARP remains committed to the strongest possible fiduciary standard for retirement investment advice and recommends a similar standard for all other advice that will promote and protect the financial security of American families.

[The prepared statement of Ms. Firvida can be found on page 46 of the appendix.]

Chairman HUIZENGA. And with that, Dr. Holtz-Eakin, we recognize you for 5 minutes, and welcome you here.

STATEMENT OF DOUGLAS HOLTZ-EAKIN, PRESIDENT, AMERICAN ACTION FORUM

Mr. HOLTZ-EAKIN. Thank you, Chairman Huizenga, Ranking Member Maloney, and members of the subcommittee for the privilege to be here today to discuss the implications of the DOL fiduciary rule for capital markets.

I would like to note at the outset that there is a consensus about the desirability of a standard of conduct to protect small retirement savers against any bad actors that might short-change them in their desire to protect their lifestyle. The only issue is whether such a standard is workable, and I believe the DOL rule is not workable, and I applaud efforts to replace it with something that is more effective.

I am going to make three very simple points briefly, and then I look forward to answering your questions. The first is that the DOL fiduciary rule is very expensive, and this expense derives from changes in business practice that the rule will force on the retirement industry and those changes in the end will be most harmful to small retirement savers, and they will bear the brunt of the costs of this rule.

First of all, the rule is very costly. The chairman noted at the outset, the American Action Forum has an ongoing effort to track the costs of Federal regulation, not just financial regulation but across-the-board in all agencies, and the fiduciary rule was the single most expensive rule in 2016. Our estimate is $31.5 billion, plus another $2 billion annually to comply with the rule. This is the second most expensive non-environmental rule since 2005. And so it stands out as an extremely costly enterprise.

Those costs derive really from two main things. The first is the move to primarily fee-based accounts. If you look at the data for the 57 million individual retirement accounts, two facts jump right out. The first fact is, the vast majority of them are quite small—74 percent are under $100,000—and the other fact is that they are largely in commission-based accounts.

And so this rule which would eliminate the capacity to do those commission-based accounts, by and large, and would move people into the fee-based world, which is much more expensive. Our estimate, as the chairman noted, is this amounts to about $800 per year per account, an amount that many people simply will not be able to come up with.

For those who are already in somewhat of a fee-based account, there will be an additional $1,500 in duplicative fees. And so these are costs that these individuals are going to bear. It is also quite likely that because of the nature of the service required in this fee-based world, minimum account balances will be raised. And if they were raised even to $20,000, you would lose about 40 percent of the accounts. And so the threat of pricing people out and the threat of having them dropped from investment advice is very real in the data.

This is also not a hypothetical from two other perspectives. Number one, we have seen this experiment run roughly in the same fashion in the United Kingdom, where commission-based accounts were, in fact, banned in 2013, and the result, as I note in my written statement, was a more than doubling of the number of the fraction of firms that required 100,000 pounds as the minimum account balance, about 45 percent firms report that they provided very little advice to any small accounts. They just didn't do that anymore. And you saw people get less and less retirement advice.

It has also begun to happen in the United States. We have seen companies like MetLife and AIG exit the business. And we have seen companies like Raymond James move to a fee-based model. So the notion that these changes would occur, I think is very real.

The second route for these costs is the potential for litigation. The best-interest contract is in the eyes of most people a real opening for additional litigation. If you look at the data for FINRA, there were 4,000 complaints filed in 2016. Only 158 were found in favor of the complainant, the consumer. That suggests there is going to be a lot of litigation at high cost with no particular benefit to the individuals. And that is a concern.

Obviously you could insure against that litigation cost, but that is a cost of doing business that is going to show up in these accounts. And so between the litigation, which the DOL recognized in doing its cost estimate, but only put at $150 million a year—most people think that is too low—and the movement to fee-based accounts, you are going to see additional costs. Those costs are going to hurt the small retirement saver. They are going to price some people out of the market. There are going to be some increases in minimum balances, which are going to preclude people from getting advice. And a ballpark estimate of the number of people affected looks like 28 million, a number equal to half of the number of IRA accounts right now. So this is a substantial threat to the actual advice that we want small retirement savers to get, and I encourage the committee to move to a more workable approach to standards of conduct.

Thank you.

[The prepared statement of Dr. Holtz-Eakin can be found on page 62 of the appendix.]

Chairman HUIZENGA. Thank you. I appreciate all of your testimony. And with that, the Chair will recognize himself for 5 minutes for questions.

I just want to quickly jump on what you were talking about. Obviously in your experience with the Council of Economic Advisers and then head of the CBO, you have certainly been through this. I have had conversations with those companies, some who have shifted to fee-based regimes, and they freely acknowledge that they are going to make more money doing this with fewer clients.

It is a marketing tool that some are using. And what is a little frustrating to me is that this is being somehow portrayed that if you don't like this Department of Labor fiduciary rule, then you must not like savers. Well, I can tell you this. My nearly 86-year-old mother—please don't tell her I told you how old she is—doesn't have a broker on Wall Street. It is Bruce and Brandon on 8th Street in Holland, Michigan. That is who her advisers are. That is who my advisers are.

These are the people that we go to. It is not some massive building in New York or some other place. And I think that it is important to note that the reason why the Obama Administration did what it did is it could not get a bipartisan board of the Securities and Exchange Commission to agree on a fiduciary rule, but they were able to get a political appointee at the Department of Labor to move ahead with a politically driven rule, who ironically and interestingly enough is now head of the DNC.

I think it is just fascinating when this is getting portrayed as somehow political when this is really about making sure that people like my mom, and people like me coming up, and others are going to have the ability, and my constituents are going to have the ability to get the advice that they need.

So as you had pointed out, 41 percent of the U.S. working households ages 55 to 64 have no retirement savings, 55 percent of households age 55 to 64 have less than $25,000 in savings, and only 23 percent of Baby Boomers believe their savings will last them through retirement. Even more disturbing is that many experts believe that this figure is, frankly, optimistic.

Rather than put forward a rule that would expand retirement saving opportunities for hard-working Americans, the Administration pushed through these regulations with costs that far outweigh any marginal benefits. Equally troubling is the fact that the data released in response to the Department's recent July 6th request for information shows that the Obama Administration significantly underestimated the negative effects of the rule, in particular in reducing access to advice for small retirement savers and small businesses.

So very quickly, I am going to go through the panel, and I would like yes-or-no responses on a couple of quick questions. Do you support the delay of the applicability date of the DOL fiduciary rule beyond January 1st? Mr. Knoch?

Mr. KNOCH. Yes.

Chairman HUIZENGA. Mr. Halloran?

Mr. HALLORAN. Yes.

Chairman HUIZENGA. Mr. Lombard?

Mr. LOMBARD. Yes.

Ms. FIRVIDA. No.

Chairman HUIZENGA. No.

Mr. HOLTZ-EAKIN. Yes.

Chairman HUIZENGA. Okay. Do you support the best-interest standard as outlined in the Wagner discussion draft? Mr. Knoch?

Mr. KNOCH. Yes.

Mr. HALLORAN. Yes.

Mr. LOMBARD. Yes.

Ms. FIRVIDA. It is too vague, but we don't think so.

Chairman HUIZENGA. I think that is a "no."

Ms. FIRVIDA. It might be a "no."

Chairman HUIZENGA. Okay.

Ms. FIRVIDA. I think it is a "no."

Mr. HOLTZ-EAKIN. Yes.

Chairman HUIZENGA. All right. And then do you agree that the Securities and Exchange Commission is the expert regulator in this space and should act as the lead agency crafting an applicable rule regulating the standards of care for individualized investment advice? Mr. Knoch?

Mr. KNOCH. Yes.

Mr. HALLORAN. Yes.

Mr. LOMBARD. Again, yes.

Ms. FIRVIDA. No, there is a rule for both, the DOL and the SEC.

Mr. HOLTZ-EAKIN. Yes.

Chairman HUIZENGA. Okay. So you don't agree that the SEC is the actual expert regulator in this? Because Secretary Acosta has said that they don't have that expertise.

Ms. FIRVIDA. We believe that both agencies have expertise—

Chairman HUIZENGA. They have a role.

Ms. FIRVIDA. —that investors benefit from when both sets of expertise—

Chairman HUIZENGA. All right, reclaiming my time for this last minute, do you believe that robo-advisers are better for investors than real people giving advice? Mr. Knoch?

Mr. KNOCH. No.

Chairman HUIZENGA. Mr. Halloran?

Mr. HALLORAN. Absolutely not.

Chairman HUIZENGA. Mr. Lombard?

Mr. LOMBARD. No.

Chairman HUIZENGA. Ms. Firvida?

Ms. FIRVIDA. We do not believe that it is wrong to get advice from robo-advisers and other new technologies.

Chairman HUIZENGA. Okay, so I guess that is a "no." Mr. Holtz-Eakin?

Mr. HOLTZ-EAKIN. No.

Chairman HUIZENGA. Okay. Well, I am very concerned about how this flawed rule will impact the U.S. capital markets, as well. I am even more concerned with its impact on small-business owners. And Mr. Knoch, I would like you to address really quickly, how has the DOL fiduciary affected businesses' abilities to offer services for small employer retirement plans, such as simple IRAs? And will there be a loss of access for retirement services for small businesses that have not grown large enough to even consider a 401(k) plan?

Mr. KNOCH. Yes, thank you for the question. This is where we have seen probably the largest impact so far of the rule and where the financial advisers I work with are most concerned about how to comply. It is particularly with simple IRAs. As I mentioned in my opening testimony, we have seen the number of accounts in those programs drop by 20 percent, and looking forward 18 months, we expect those to continue to drop to a little over 40 percent.

I am concerned. And I don't today have a workable solution for simple IRAs that our financial advisers are willing to use under the DOL rule as currently written.

Chairman HUIZENGA. My time has expired, but I will note that a study conducted by the U.S. Chamber of Commerce found that small-business owners through SEP and simple type IRA plans provide roughly $472 billion in retirement savings for over 9 million households. And I am afraid that in light of this DOL rule, those small-business owners will stop providing those plans to their employees.

My time has expired. The Chair recognizes the ranking member for 5 minutes.

Mrs. MALONEY. Thank you, Mr. Chairman, for calling this hearing and assembling such a distinguished, outstanding panel on a critically important issue for retirees and in protecting investors.

Regrettably, most of us have had the experience in their offices, even though we represent very honest and wonderful financial institutions and wonderful honest people in the business, that as one of you said, there are bad actors out there. And we have all had the experience where people come to me and say, I put all of my savings with this adviser. They said they would be protected. I have lost everything. What do I do? There is nothing you can do for them.

So the reason this rule was put in place was to protect people. And President Obama felt passionately about it. And the principle is very simple, that you have to put your customers' interests first. In other words, you can't put making money for yourself over a retiree looking for advice. And it is a higher standard because they are retirees, many of whom have very little money and it needs to be protected. Maybe that is why President Obama felt so passionately about this rule.

And he told me that often in the negotiations—we are in a political body; we negotiate all the time—the opposing side wanted the fiduciary rule thrown out, and they would give him XYZ, and he would say, no, I want the fiduciary rule. It is important to protecting people.

Now, many of you have said that the regulation is terrible and it should be more regulation efficiency. I know firsthand that they will work with you. I took six different problems and had them removed and changed because it made it honestly better and more efficient. And I put the letter in the record. You can read it. Every single recommendation I made after much negotiation, we got it changed. So they will work with you.

If you think you can make it more efficient and faster, fine. Go to DOL. They will work with you. And by the way, it is a Republican leader now at DOL who has called for the rule to go in place and says that it will preserve savings for millions of Americans. And also, you say you are for investor protections. Do you have any ideas for more investor protections? I am sure DOL will respond to them.

This is an important rule that will save people's savings and will have professionals—most of whom have that same goal anyway—we are just protecting against bad actors. That is what this rule does.

So my question first is to Cristina Martin Firvida. Can you talk about the differences between the DOL's fiduciary rule and this bill's watered-down standard? And are the protections that are included in the DOL rule but not this bill important to protecting retirement savers?

Ms. FIRVIDA. Thank you, Congresswoman. So a big concern we have about the discussion draft—and we recognize it is a draft only—is that the standard as described is quite vague. We are concerned that the current suitability standard could even satisfy the benchmark that is described in this bill.

And if that would be the case, perhaps that is not correct, but if that would be the case, we don't see how this bill is an improvement on the current situation before the fiduciary rule went into place. The fiduciary rule very specifically directs how to manage conflicts. It is more than just disclosure. And disclosure alone is inadequate.

We know that when we have done surveys, people who are saving for their retirement, if they understand, they hear someone say, look, I have conflicts of interest, I will earn a commission based on what I recommend, ironically that leads someone to trust that adviser more, even though the conflict is not managed, even though the conflict is not avoided.

So disclosure alone is not enough. And the concern we have with this bill is, disclosure alone could satisfy the benchmark, suitability could satisfy the benchmark. There is $40 billion that the DOL estimates for IRA investors alone that could be lost to conflicted advice. They have a very strong rule, it helps investors, and we strongly support it.

Mrs. MALONEY. Okay. Now, following up on this bill's watered-down standard for broker-dealers, it wouldn't even take effect for 18 months after the bill is enacted, even though the repeal of the DOL rule would be immediate. And that means for the first 18 months under this bill, brokers would have no duty to act in their clients' best interests.

The Labor Department, under a Republican Labor Secretary, concluded that the cost to investors of delaying this rule for even half this long would be absolutely overwhelming. So is it fair to say that the cost to retirement investors of this 18-month gap would be substantial?

Ms. FIRVIDA. The cost would be substantial. And something that I would like to address in statements that have been made this morning, when we talk about the cost of the regulation and we talk about that in the absence of the cost of conflicted advice to savers, is we are missing the big picture. Conflicted advice is not free. It is costing people saving for their retirement, people like the AARP members who are here today in support of the rule.

So, yes, a delay of 18 months would be very significant on the nest eggs of people saving for their retirement.

Mrs. MALONEY. My time has expired.

Chairman HUIZENGA. The gentlelady's time has expired. The Chair recognizes the vice chairman of the subcommittee, Mr. Hultgren, for 5 minutes.

Mr. HULTGREN. Thank you, Mr. Chairman, again. And thank you all for being here.

Mr. Knoch, I represent a district just—the far west suburbs of Chicago, with many small communities in that area. It's a wonderful place to represent. You talk about this a little bit in your testimony, but I wondered if you could elaborate a little bit further about why the Department of Labor's rule will result in fewer choices of affordable financial advice in smaller communities across the country?

Mr. KNOCH. Thank you, sir. As I talk to the CPA financial advisers I work with, perhaps the greatest concern they have today is twofold. The biggest one is being exposed to the possibility of class-action lawsuits, which is part of the utilization of best-interest contract. A number of people on the panel here today have discussed a move to fee-based accounts. As they correctly mention, fee-based accounts are typically for larger investors, which means smaller investors will be in relationships with their financial advisers using the best-interest contract.

There is some concern about having that standard applied. It is not that our financial advisers are worried about accountability. They are worried about being part of class-action lawsuits. And they are exiting the marketplace.

Mr. HULTGREN. Mr. Knoch, do you believe M&A to absorb compliance costs across economies of scale could contribute to monopolies or at least greatly reduce competition in some areas? And what will this mean for investors, my constituents saving for retirement?

Mr. KNOCH. I'm sorry. Would you repeat that?

Mr. HULTGREN. Yes, I wondered if you believe M&A would absorb compliance costs across economies of scale, could contribute to monopolies or at least greatly reduce competition in some areas, and ultimately what the cost on smaller investors would be?

Mr. KNOCH. Yes, I do have some concern about that. Some of our financial advisers that we work with have indicated—especially ones who are working with smaller investors—that they may choose to leave the financial services industry, try to sell their practice.

I think the biggest concern I have with that may be less about monopolies—at least in our case. I can certainly see it industry-wide—but a lot of times these are small financial advisers who are serving small communities. There isn't somebody else in that community in a number of cases to take over services. So that is where my M&A concern is for our organization.

Mr. HULTGREN. Dr. Holtz-Eakin, we all agree that cost-benefit analysis is important to policymaking. It doesn't happen very often around this place. But especially economically significant rules like that finalized with the Department of Labor. You are an economist. Do you believe President Obama's Administration conducted a credible cost-benefit analysis before this rule was put out? And what do you think are the most significant flaws in the analysis?

Mr. HOLTZ-EAKIN. I think there are some concerns on both sides of the equation. On the cost side, we think that the DOL rule underestimates the litigation costs significantly. And that is a concern. I think on the benefit side, the widely cited $17 billion number produced by the Council of Economic Advisers is not an estimate that I think stands up to close scrutiny. We have written on this in the past. There have been other critiques of it.

But it was incomplete in the assets that it surveyed and covered. It took rates of return that weren't risk-weighted and sort of conventional measures of, what is a real financial return. And I think if you poke hard at that, you are not going to find $17 billion worth of loss.

Mr. HULTGREN. Okay. Would you agree that the SEC would have better perspective for weighing benefits and costs for investors than the Department of Labor?

Mr. HOLTZ-EAKIN. I think they are the primary regulator. They are the perfect entity to be doing this.

Mr. HULTGREN. Thanks. Mr. Knoch, back to you. It would be helpful if you could speak directly to the merits of the draft legislation from Mrs. Wagner from Missouri that we are discussing today. What will happen if the DOL's rule goes into effect before the SEC is able to implement its own standard? And from an investor protection standpoint, wouldn't my constituents be better served by a uniform standard that applies to both retirement accounts and investment accounts?

Mr. KNOCH. Thank you. I think the biggest thing that will happen if the rule is finalized before this bill is enacted is the trend that I was describing in my oral testimony will continue. We will continue to see a decline in utilization of the platforms most often offered to investors with small account balances. Direct business, simple IRAs, as I mentioned will continue to shrink.

I do believe that the rule—that the draft bill has merits in that it will provide a uniform standard of care. It will cover more than just retirement accounts. I think everyone on this panel would agree in a best-interest standard being applied to financial advisers working with clients. We would be in favor of seeing that applied across not just retirement accounts, but all of investors' accounts. The financial advisers I work with work with the entire person.

Mr. HULTGREN. Thank you. I just have a few seconds left and many more questions, and so maybe we will follow up in writing. With that, I yield back.

Chairman HUIZENGA. The gentleman yields back. The Chair recognizes the gentleman from Georgia, Mr. Scott, for 5 minutes.

Mr. SCOTT. Thank you very much, Mr. Chairman.

We are in this shape that we are in today because, as an original co-sponsor of Dodd-Frank years ago, we told the SEC that they needed to come up with a rule that would raise the broker-dealer standard and, more importantly, harmonize that standard with the obligations investment advisers have to follow today. And not the Department of Labor. It is the SEC that is best suited to do that. Failure of them to take the initiative and to do that and recognize the true role that the Department of Labor plays, we are wondering here, because the great need is harmonizing it.

Here is what the law said about this situation in terms of the fiduciary rule. It says that both the SEC and the DOL have jurisdiction over investment advice that must meet a fiduciary standard and advice that is exempt from such a standard. Specifically, the SEC has jurisdiction over advice to individuals, regarding both retirement and non-retirement accounts, but only if the advice relates to securities. In contrast, the DOL has jurisdictions over advice regarding retirement accounts, regardless of whether the advice is securities related.

This means that in many circumstances, both the agencies share jurisdiction, while in others, only one agency has jurisdiction. And this is enough evidence to know that these two entities, DOL and SEC, need to harmonize. They didn't do it. So what were we left with?

We are left with a bill and to move to define the fiduciary. And I worked with Mrs. Wagner before on several of her bills to do that, was the lead Democrat to do that. But because we told the SEC in those bills to do that.

But right now, this bill that Mrs. Wagner has put before us is a very troubling bill. And let me tell you why. For starters, this discussion draft—I am glad it is just a discussion—will most certainly undermine the SEC's rulemaking authority in this space, because the bill says that no additional obligations related to the standard of care of broker-dealer can added on top of the ones set forth in this discussion draft.

This is worrisome, because what if the drafters of the bill got something wrong? I noticed in my quick read through this—and keep in mind, I only got this bill yesterday—that dual registrants, those firms that dually registered as both broker-dealers and investment advisers, is not even mentioned in the discussion draft.

I am also worried about this because what if the market evolves? We have seen in the past 10 years how retirement savings and investment advice has been flipped on its head because of technology. Imagine what it is going to be 5 years ahead. So tying the hands of the SEC, being overprescriptive as this discussion draft bill is, is dangerous.

Additionally, this new bill creates an entirely new standard that isn't a fiduciary standard or a suitability standard. It is something entirely new. And so why are we being so prescriptive in drafting of this bill? Why don't we direct the SEC, who are the experts in this, to do their job instead of tying the hands of the SEC?

And this bill reminds me of a straitjacket. It is like this bill is putting the SEC—it is almost like forcing them to do their job, but yet putting these overly prescriptive in here.

Now, finally, this bill would be devastating to low-income, to middle-income, to senior citizens. When you add contrapulations and make it much more complex and complicated, where you can't even understand it, and you have no harmonization in the bill, and you have put on top of that prescriptive directions, it is harmful.

With all due respect to Mrs. Wagner, but this is a very troubling bill. I hope we get a chance to work and iron out some of these to make it fair to everyone.

Chairman HUIZENGA. The gentleman's time has expired.

Mr. SCOTT. Especially those at the low-income and our seniors.

Chairman HUIZENGA. The gentleman's time has expired. With that, we will turn to the author of the draft legislation, the chairwoman of our Oversight and Investigations Subcommittee, the gentlelady from Missouri, Mrs. Wagner, for 5 minutes.

Mrs. WAGNER. Thank you, Mr. Chairman.

And I certainly appreciate Congressman Scott and the ability to work with you, sir. I will say that we have codified the standard, best-interest standard in this draft legislation, which I think is a key step forward. I want to thank all of you for appearing today and for your testimony on the DOL's fiduciary rule and the capital markets and how it impacts it, as well as the ability of millions of low- and middle-income American families to continue receiving retirement advice.

Dr. Holtz-Eakin, in your testimony, you stated that the fiduciary rule as it stands right now was the most expensive regulation of 2016. I think you said even the most expensive since 2005, with $31.5 billion in total costs and $2 billion in annual burdens. You elaborated a little bit about those cost mechanisms. First of all, do you want to add anything to that in terms of how much of these costs would be passed on to customers, consumers, those retail investors? And second, would the cost burdens for firms and consumers be similar under the best-interest standard envisioned in the discussion draft?

Mr. HOLTZ-EAKIN. So, thank you, Congresswoman, for the question. The cost mechanisms, as I mentioned, really are from two sources. One is the increased likelihood of litigation and the costs that come from directly litigating, and then in some cases, choosing to purchase insurance against litigation costs. Those are costs of doing business. They will inevitably be passed along to customers in one form or another. That will price some people out of investment advice. And then that way, that cost is ultimately very much borne by the least affluent among the retirement savers. And that is a concern that comes through very clearly.

The second cost really is this move to the more fee-based system. And as I mentioned in my testimony, the United Kingdom went to this entirely fee-based, eliminated the commission-based, and we saw a dramatic increase from 13 percent to 32 percent in the fraction of firms that required a minimum of 100,000 pounds.

Mrs. WAGNER. And to the discussion draft, would the cost burdens be the same?

Mr. HOLTZ-EAKIN. No, they will be lower. That is one of the—the litigation is clearly going to be a much lower standard and it doesn't drive people out of the commission-based model, and so you are not driven into a fee-based model that is far more expensive.

Mrs. WAGNER. Right. Mr. Knoch and Mr. Lombard, could you both please take some time to discuss how the best-interest standard described in the discussion draft improves upon the suitability standard currently subjected to broker-dealers? Mr. Knoch?

Mr. KNOCH. Thank you. I think one of the areas—and I marked it in here, and we have had a discussion about this—is it requires a broker-dealer to avoid, disclose or otherwise reasonably manage any conflict of interest. So there is a requirement for disclosure, which we would agree with, as well as attempts to avoid and manage conflicts of interest.

We are also asking financial advisers to uphold a duty of loyalty and a duty of care. We have definitions that look substantially similar to what is expected in, let's say, fee-based investment advisory accounts, as well, under an SEC standard. I am particularly pleased with seeing that there and applying a standard.

Mrs. WAGNER. Mr. Lombard?

Mr. LOMBARD. It is clearly a higher standard than the suitability, both duty of loyalty, duty of care, which includes the prudent management of client assets. I would also point out that this would apply to all accounts, not just retirement accounts, and that is important to our clients.

Also, with the SEC's and FINRA's examination, oversight and enforcement capabilities, abilities that are limited at the Department of Labor, I think downstream you are going to get implementation of a best-interest standard much more effectively by having SEC and FINRA's oversight.

Mrs. WAGNER. Mr. Knoch, could you please explain how the discussion draft implements an effective and meaningful disclosure system—you did a little bit—and effectively mitigates material conflicts of interest?

Mr. KNOCH. Yes, this is actually one of the areas where I am most pleased with the discussion draft. I think one of the areas of disclosure that works very well in the fee-based accounts that we have a fiduciary standard today under the SEC is the utilization of the Form ADV. This appears to have a substantially similar disclosure requirement put at the beginning of the relationship. We think that form of disclosure works very well. While it adds some due paperwork burden, the paperwork burden of a form like this at the beginning of the process is far less than what is contemplated by the DOL rule.

Mrs. WAGNER. Quick yes or no, does the discussion draft provide a more comprehensive best-interest standard than the DOL fiduciary rule by applying to both retirement and investment accounts?

Mr. KNOCH. Yes.

Mrs. WAGNER. Mr. Halloran?

Mr. HALLORAN. Yes.

Mrs. WAGNER. Mr. Lombard?

Mr. LOMBARD. Yes.

Mr. HOLTZ-EAKIN. Yes.

Mrs. WAGNER. Ms. Firvida?

Ms. FIRVIDA. I think we answered previously that we feel that it is vague, so we don't think so.

Mrs. WAGNER. That is a "no?"

Ms. FIRVIDA. I think that is a "no."

Mrs. WAGNER. Thank you, Mr. Chairman. I yield back my time. Thank you all.

Chairman HUIZENGA. The gentlelady's time has expired. The Chair recognizes the gentleman from Texas, Mr. Gonzalez, for 5 minutes.

Mr. GONZALEZ. This is to Ms. Cristina Martin Firvida. Often in this committee, my colleagues on the other side of the aisle complain about Washington's regulatory overreach with respect to the DOL's fiduciary rule. We have heard allegations that the Department of Labor has gone beyond its statutory mandate or outside its regulatory jurisdiction.

Is there any indication that the DOL overstepped its statutory boundaries in promulgating its fiduciary rule?

Ms. FIRVIDA. Absolutely not. And multiple Federal courts have upheld that view.

Mr. GONZALEZ. Is regulation of investment advice in connection with retirement accounts within the scope of the DOL's mandate under the Employee Retirement Income Security Act of 1974 (ERISA)?

Ms. FIRVIDA. Yes, it is. And it has extensive expertise doing so and has developed dozens of prohibited transaction exemptions and enforces them, and through that has a lot of expertise that I think we are ignoring today in talking about the DOL's lack of expertise.

Mr. GONZALEZ. That is right. Thank you for your response. I yield back the balance of my time.

Chairman HUIZENGA. The gentleman yields back. The Chair recognizes the gentleman from Maine, Mr. Poliquin, for 5 minutes.

Mr. POLIQUIN. Thank you very much, Mr. Chairman. I appreciate it. And thank you all very much for being here today.

When someone is in the business of providing advice or services, it is common sense for all of us to realize that folks and firms are attracted to the biggest accounts. They just are. If you are an accountant, you want a larger business because they pay a bigger fee.

If you are an attorney, you want a bigger client because they pay a bigger fee.

And if you are in the business of selling real estate, you want to sell a $500,000 home instead of a $200,000 home because your commission is bigger. It is just common sense.

Now, if you are in the business of providing insurance products, or retirement plan advice for savers, you are obviously still attracted to the larger accounts because they pay a bigger fee. This is common sense. I don't worry about folks who have large accounts. I really don't. They are going to do fine. They are going to get the best products. They are going to get the best advice. And they are going to do just fine.

I will tell you who I worry about. I worry about the folks that I represent in northern Maine. We have a highly rural State. We have a small number of large businesses. But we have the most honest, hard-working, small savers, small investors that you could find anywhere in our country.

I worry about a single mom with two kids who is trying to put aside $25 a week to save for her kids who might want to go to a community college, get an associate's degree. I worry about a teacher in Lewiston who is trying to make ends meet. I worry about a boat builder in downeast Maine who is trying to save for his or her retirement.

Now, we know some of the facts here. We know that if you increase regulations in this part of our economy or any other part of our economy, the costs go up. And when the costs go up, it means the rate of return on your savings go down. It means your nest egg is smaller as you get older into the golden years.

And we also know that the number of product offerings, the choices that you have go down, and we also know that the number of firms that provide retirement advice go down because they are leaving the market. We know this. The facts are in front of us. You can't argue the facts. They are what they are.

Now, my mom is 89. My dad is 87. I am very close to my parents. I love them to death. They cannot use a cell phone anymore. So we heard today that if over-regulating this industry causes folks with small accounts, not the big folks, folks who have $25,000, $30,000 in savings, and they are counting on that so they can live in dignity for the remainder of their lives, they might have to go to a robo-call. You have to be kidding me.

So, okay, let's say you are 70 and you have a small account. What should your asset allocation be? Should you own some stocks or should you be all in fixed-income because you don't have any more current income coming in, you are retired. Should you buy an annuity? Maybe all your money should be in cash and money market funds to pay those medical bills and you need access to that cash on a regular basis. Who is going to tell them that?

Who is going to tell them? How about that single mom who is working 2 jobs at the diner and at the convenience store trying to save $25 a week? Who is going to tell her how to invest that money?

Here is what I worry about, Mr. Chairman, is that we have a potential here of so over-regulating the people who provide good advice to our small savers in this country that you are driving away that advice. And if the advice is still there, you are driving up the costs so high that their rate of return over time is going down. That is who I worry about.

Did I get this right, Mr. Holtz-Eakin?

Mr. HOLTZ-EAKIN. I think your concern is entirely well-placed, sir.

Mr. POLIQUIN. Mr. Knoch, am I pronouncing it right? You are in this business. Mr. Halloran, you are in this business. Have you folks started to increase your minimum account size such that the folks at the bottom aren't going to get advice, your advice? Or are your costs going up so far or is the liability so great because of these increased regulations that you say, "I'm out of here?" And who is going to provide that advice to the little guy? Tell us. You are in the business.

Mr. KNOCH. As I mentioned, we have seen our financial advisers discontinuing service or serving the small marketplace—

Mr. POLIQUIN. Okay, Mr. Halloran, how about you?

Mr. HALLORAN. So, we are on the manufacturing side. And the way I could speak to that is we like large accounts, but our wheelhouse is not there. We provide income products to people who need lifetime products.

Mr. POLIQUIN. And does this regulation hurt you providing that advice to small savers?

Mr. HALLORAN. They are not getting that advice about our products.

Mr. POLIQUIN. There you go. Mr. Lombard?

Mr. LOMBARD. So one of the ways to avoid the more onerous aspects of this is to move to a level fee account. Level fee accounts at my firm average 0.95 percent. Brokerage accounts average 0.55 percent. That is almost double the cost by sidestepping more onerous aspects.

Mr. POLIQUIN. Thank you, sir. Thank you, Mr. Chairman.

Chairman HUIZENGA. The gentleman's time—

Mr. POLIQUIN. Let's all get on the same page and agree with the facts.

Chairman HUIZENGA. The gentleman's time has expired.

Mr. POLIQUIN. We do not want to over-regulate our small savers such that they lose the ability to plan for their retirement. Thank you, Mr. Chairman.

Chairman HUIZENGA. The gentleman's time has expired. The Chair recognizes the gentleman from Massachusetts, Mr. Lynch, for 5 minutes.

Mr. LYNCH. Thank you, Mr. Chairman. And I want to thank the panelists for helping the committee with its work.

Mr. Chairman, I would ask unanimous consent to submit for the record a Wall Street Journal opinion and commentary by Secretary of Labor Alexander Acosta supporting the fiduciary rule, and also a letter to you and to Mrs. Maloney of New York authored by Phyllis Borzi, a former Assistant Secretary of Labor for the Employee Benefits Security Administration from 2009 to 2017.

Chairman HUIZENGA. Without objection, it is so ordered.

Mr. LYNCH. Thank you, sir.

I appreciate the comments of my friend from Maine, the beautiful State of Maine. However, it is a two-edged sword in this case, where you would also like the advice that is given to the most vulnerable investors, AARP members, many of whom are here, and it is a good thing you are here. It is a good thing you are here to try to hold people accountable to make sure that future retirees, and current retirees, as well, are treated fairly under the law.

But we want vulnerable investors, those at the lower end of the investment scale, to get advice that is in their best interest, and that is what the fiduciary standard requires. Under the proposed standard in Mrs. Wagner's draft, a broker adviser could simply give advice to purchase or recommend the purchase of whatever product gives the highest commission, as long as it is "suitable." That is a very loose standard. And we have seen abuse in that regard.

This has been a 6-year process. And it has been a long fight. It has been a long fight. And I just want to point out the simplicity of this. Those on our side, we would like investors—especially retirees—to get advice that is in their best interest. We would like to compel those who advise them to do so in a way that is in the investor's best interest.

Also, people in my district think this is already the law. They are shocked when they find out that brokers and advisers, financial advisers are not required to act in their best interests and there is no fiduciary duty to do so.

So the visceral opposition to implementing a simple fiduciary duty that requires advisers to act in the best interest of their clients, the opposition to that sort of makes our argument. We are asking for something very, very simple here. We are asking that we maintain the integrity of our financial markets. We are asking to persuade Americans to invest in their retirement especially.

And we should do so in a way that actually is protective of those interests and protective of our retirees. And right now, that is not the case. Now, there has been a 6-year discussion between the SEC and the Department of Labor. They have worked together on this. The Department of Labor has had the statutory authority to define fiduciary, what that means, since 1975. I am a former labor lawyer. I worked in ERISA quite a bit. This is the first time in the country's history that we are changing this standard, and it is in response to the way the industry has evolved and the way products have evolved.

The SEC does not have any of the authority to manage or oversee many of the products that are being sold to our retirees each and every day. So the Department of Labor is the proper agency to rule on this. I know that folks are asking for a delay, but I think we have had 6 years of discussion. The American people have gone without this protection for some time now. And I think it is entirely reasonable that we go forward with this. I oppose Mrs. Wagner's bill. I think it strips Americans of a basic protection that they need for their retirement.

And with that, Mr. Chairman, I yield back the balance of my time.

Chairman HUIZENGA. The gentleman's time has expired. The Chair recognizes the gentleman from Ohio, Mr. Stivers, for 5 minutes.

Mr. STIVERS. Thank you, Mr. Chairman. And I applaud the sponsor of the discussion draft for this bill. I think it will provide some needed relief for a lot of investors.

We saw this play out in Great Britain. Mr. Holtz-Eakin alluded to that earlier. Essentially, what this fiduciary rule says is, if you are rich, it is okay, you will be able to talk to a person. If you are poor or middle-class, you are at risk. You have to get what is called robo-advice. That means you talk to a computer. And it means you are not going to really get real advice. Imagine getting your investment advice from Siri. That is what is going to happen to a lot of poor and middle-class people.

The other thing that Mr. Holtz-Eakin brought up is that millions of dollars of middle-class and lower-class investment savings are going to be eaten up by fees and minimum balance requirements that they can't meet. There will be extra fees. And the cost of compliance is going to really hurt them.

This is an issue for people of lower means in this country who are being hurt and trampled on by a giant government. I do want to admit to the record an article in Bloomberg about the AARP's role in this standard and what they did. I think it is important that we admit it to the record, without objection.

Chairman HUIZENGA. Without objection, it is so ordered.

Mr. STIVERS. Thank you. My first question is to Mr. Lombard, to follow up on something the chairman asked earlier about the differences between the Securities and Exchange Commission and the Department of Labor. Can you help us understand the difference in their expertise with regard to investment, just in a brief explanation?

Mr. LOMBARD. I can comment on the SEC's role. They have worked as our primary regulator since I have gotten into this business 35 years ago. During that period of time, I headed our advisory services. They audited our advisory activities probably on an every 3-year cycle. So I have seen them. I have never had the Department of Labor in as an auditor or an overseer in the 35 years I have been with Janney Montgomery Scott.

Mr. STIVERS. Thank you, Mr. Lombard. And that speaks mostly for itself. Why is it that they have never come in and audited you? What is their role in investment?

Mr. LOMBARD. Their role, up until this point, has been limited to investment retirement plans, not individual retirement accounts.

Mr. STIVERS. Let me be more specific. Do they have any role in regulating investments and appropriateness of investments?

Mr. LOMBARD. On the retirement plan side, I believe they do.

Mr. STIVERS. For individual investments and the choosing of investments, does the Department of Labor have any expertise in that?

Mr. LOMBARD. I think that is what is being argued right now.

Mr. STIVERS. The answer, I believe, is "no," but I don't think that they have a big experience in that.

Mr. Halloran, can you tell me—

Chairman HUIZENGA. Will the gentleman yield on that point briefly?

Mr. STIVERS. I would be happy to yield.

Chairman HUIZENGA. I know in conversations that Mr. Acosta has had at various times out publicly, he has said that the Department of Labor is ill-suited to do this and that the Securities and Exchange Commission does have that expertise. So I just wanted to make note of that.

Mr. STIVERS. I will let the Secretary speak for himself. And thank you, Mr. Chairman. Reclaiming my time—

Ms. FIRVIDA. If I may, however—

Mr. STIVERS. No, ma'am. This is my time. You were asked some questions. Mr. Halloran, I am curious if you believe the current DOL fiduciary rule disadvantages annuities compared to other investments?

Mr. HALLORAN. Significantly, actually. As I was stating before, we don't typically serve the wealthy. At least they don't have as great a need for this kind of product as middle-class Americans do. We are talking about people with smaller balances who need to— one of the easiest things to do in investing is to invest, is to accumulate. That is not the hard part of the job, typically.

And actually, in that respect, Americans have done a pretty poor job. But then to take that money and stretch that over the rest of your retirement life, and potentially two lives, that is a very difficult task. And that is precisely what annuities with living benefits do.

Mr. STIVERS. Thank you. So this rule essentially disadvantages a tool that many middle-class and low-income people can use to preserve their retirement and their quality of life in retirement? Is that correct?

Mr. HALLORAN. Without question. We have already seen that.

Mr. STIVERS. Thank you. I will just finish by allowing Mr. Holtz-Eakin maybe to expand on what I talked about at the beginning about how this rule impacts poor and middle-class people and what it means to their future. Mr. Holtz-Eakin?

Mr. HOLTZ-EAKIN. I think it is a very simple story, which is the rule was intended to provide high-quality advice, but that is only going to work if you get some advice at all. And the net impact of the rule is to put many of the lower-income smaller savers out of the ability to get any advice at all.

Chairman HUIZENGA. The gentleman's time has expired.

Mr. STIVERS. Thank you, I yield back.

Chairman HUIZENGA. And at the request of the ranking member, we do have a guest here who is a member of our full Financial Services Committee, but is not on this subcommittee. And without objection, the gentleman from Maryland, Mr. Delaney, is permitted to participate in today's subcommittee hearing. Mr. Delaney is a member of the full committee, as I had pointed out, and we appreciate his interest on this topic.

And with that, I am willing to recognize you for 5 minutes.

Mr. DELANEY. Thank you, Mr. Chairman, for permitting me to participate in this hearing. And thanks for calling it.

The reason I asked to participate is because I have been a strong supporter of the fiduciary rule. And you know I found this conversation very interesting because if you didn't know better, you would think the fiduciary rule prevents people from owning annuities. It, in fact, doesn't prevent people from owning annuities, for example. It discourages people from selling annuity products if when you include all the fees it is deemed to be not in the best interest of the client.

And I think there is somewhat of a broad agreement here that investment products that are in a client's best interest is a more important standard than the current standard, the suitability standard. I think in a perfect world, everyone here would agree that we would love for every client to receive investment advice that is in their best interests as opposed to just suitable.

So the issue seems to be that because of this rule, which—trust me, I agree that it would be terrific if the SEC would have put forth this rule. They do probably have more expertise in the area, but they didn't do it. And I think a future where the SEC comes up with a rule for all investment advice and we synchronize the fiduciary rule from the Department of Labor with that could be a great outcome. But I wouldn't want to delay the Department of Labor fiduciary rule, because it seems to be the forcing function to get the SEC to finally try to do something on this.

So I think that is a false choice. I think we can have the SEC do something on this, and then we can see what they come up with, and we could look at the fiduciary rule, and we could synchronize them in one standard.

But what I find amazing about this discussion is, the notion is that the current business model of, say, your firm, Mr. Lombard—and I am sure most of the—the overwhelming majority of your advisers do a terrific job for their clients. Your firm has a great reputation. It has a good brand. The name is on the door. And people wake up every day and do the best thing for their clients.

But the issue with the fiduciary rule in the eyes of three of the four guests here seems to be that for some reason because of this rule we will be left with a world that it is all robo-advisers and there is no innovation and there is no adaptation to this new standard. And that just seems so contrary to how we think about our capital markets and our entrepreneurial economy.

Because as someone who started two financial services companies from scratch and took them public on the New York Stock Exchange prior to being here, and specifically started companies that focused on opportunities that were created by larger financial institutions who weren't adapting to the market's needs, either because they had legacy systems or legacy compensation structures or some legacy practices that made them hard to respond to the model, I guess my question for Mr. Lombard and Dr. Holtz-Eakin is—and I am a huge admirer of your work, by the way, so thank you for being here—why do you think for some reason that suddenly the private economy, the entrepreneurial economy of the United States won't take this new standard, and if your firm can't respond with a high-quality product where human combined with technology allows people to get advice at a best-interest standard, why don't you think all kinds of entrepreneurs raising all kinds of private capital won't start all kinds of new businesses to exactly meet that need and outcompete you if you are stuck throwing your clients out of your firm or putting them on some automated Siri-like system?

I just don't understand why you would bet against the entrepreneurial economy of the United States. Mr. Lombard?

Mr. LOMBARD. So, we have already made the innovation. We have brought down our minimums on advisory fees fivefold, from $25,000 to $5,000. We still have upwards of 10,000 accounts with balances less than $5,000. We have certain fixed costs that those clients, if we charge those fixed costs to them, would pay an unreasonable fee.

Mr. DELANEY. All right, so reclaiming my time back, so hearing that, I would say, okay, I am going to start a new company without those fixed costs and out-compete you and provide great service to these people. Why don't you think that will happen? Because that is how it happens everywhere in this economy.

Ms. FIRVIDA. And it is happening.

Mr. DELANEY. Right, Dr. Holtz-Eakin.?

Mr. HOLTZ-EAKIN. I have two responses to this. First of all, it is a fantastic question. It is right on the mark. And there is a broad concern which is also going on in the financial services about the birth rate of firms in the U.S. economy, which has been declining steadily, and which a few years ago actually fell below the death rate of firms. And that is a troubling trend.

Mr. DELANEY. There are other reasons for that.

Mr. HOLTZ-EAKIN. So I worry that the regulatory burden contributes to the inability to enter and provide the competition you are describing.

Mr. DELANEY. I agree with you in other markets.

Mr. HOLTZ-EAKIN. And I say this lovingly: I hope you are afraid of going out of business every day. You want that kind of competition.

The second thing I am worried about is exactly the mirror image of the concern that has been expressed earlier, which is, how long does that take? And in the interim, what happens to everybody who had advice and is now gone?

Mr. DELANEY. Transitions are tough, I acknowledge that. And we ought to be smart about that. But I just think people innovate out of this issue.

Chairman HUIZENGA. The gentleman's time is—

Ms. FIRVIDA. And if we could add, it is that innovation that is serving the small accounts.

Chairman HUIZENGA. I'm sorry, the gentleman's time has expired. The Chair recognizes the gentleman from Arkansas, Mr. Hill, for 5 minutes.

Mr. HILL. Thank you, Mr. Chairman. And thanks to the panel for being with us today.

And this is a subject—I am relatively new to Congress, only 2½ years, but I spent 35 years in the financial services business. And a good part of that 35 years was doing business with individual retail investment clients, both in a capacity of being a trustee and running a trust bank operation, as well as a broker-dealer. So I am somewhat familiar with this issue and account sizes of all sizes, including the young family starting out with just a few dollars a month.

I have sort of grown irritated with the previous Administration and now this Administration on this topic. And I really associate myself with many of the comments made by my friend from Georgia, Mr. Scott. At its heart, this is a failure of governance because the statute was quite clear, asking the Commission to do a study on this matter and then recommending action. And it is a failure of the previous Administration through its Treasury and OMB regulatory function to insist that the SEC and the DOL work this out and create one uniform standard in this arena instead of creating the mess that we have now of expensive, duplicative, conflicting regulation.

And to me, I have just called it—it is part of the war on savings. DOL has done that by watering down the importance of long-term investment returns by muddying up the definition of what is preeminent in looking for long-term returns.

The previous Administration proposed a tax and did tax investment income. They proposed to cap IRA balances, claiming that you couldn't save unlimited money in your IRA. People propose still today forcing people to Roth their IRAs, which I think is a bad idea. And ultimately, because it has been so hard to save, even propose that the government set up savings accounts and cut out the private sector completely.

So it has been a disturbing trend in trying to encourage retirement savings. We should be doing everything we can to remove regulatory paperwork, cost barriers to faster and better retirement.

And to also say that people aren't concerned about our seniors, I think FINRA in the early 2000s led that work with notice to members and sweep examinations across the whole investment industry on breakpoints, on mutual funds, and educating consumers about that, variable annuity product sales, how those should be done, what kind of accounts they are appropriate for, what kind of accounts they are not appropriate for, and then sweep exams on investor sales practices for seniors.

So this is not a new issue in the investment industry, and it should be done in the right way, which is through the SEC and the investment regulatory environment, coordinated with whatever views Labor has on ERISA-based accounts.

There are a couple of things I am concerned about. One, think of all the small broker-dealers out there, small investment managers who are now told they were going to get a good delay of this rule and get improvements to it, have maybe the commission take a look at it with the incoming Administration, our Trump Administration, and then told, no, it is going to go forward.

So I have heard from a lot of small investment advisers in Arkansas that if the fiduciary rule is not delayed by the end of August, companies will have to start millions of dollars to prepare for provisions to the rule that may actually go away or be changed. And I don't think that is fair. That is what I call the failure of governance to get this right on the front end.

And then I am concerned about this State law trend that was mentioned earlier. And Mr. Halloran, I think on July 1st, Nevada has a law going into effect on fiduciary standards on broker-dealers for all accounts, and other States are considering that. Again, that is going to create even more conflict in this space when we are trying to get a uniform standard that applies to investment broker-dealers, insurance people and others in this space.

Can you talk about how these State actions are inconsistent with the Federal securities laws and what your concerns are on that?

Mr. HALLORAN. Yes, sure. So we don't actually know everything about Nevada that we should. It is kind of vague in itself, as well. But the greater concern here is that if you are looking for harmonization, which we think is a very good thing from a regulatory standpoint, then having 50 States doing 50 different things really doesn't help that in any regard at all.

Certainly that increased cost—we deal with that from the insurance aspect all the time. We have 50-plus insurance regulators that we have to deal with on a State-by-State basis, every time we do something from an insurance product, and so forth. So we know the difficulty in doing that. It works. And it works slowly. But adding on legislative State actions to that just mucks up the water that much more.

Mr. HILL. Thank you. And I yield back.

Chairman HUIZENGA. The gentleman's time has expired.

The gentleman from Minnesota is recognized for 5 minutes.

Mr. EMMER. I thank the Chair, and I thank the panel for being here today.

I want to focus on one specific area probably because of my professional background. And why don't we start with Mr. Halloran? Would you agree with Secretary Acosta that the private right of action, the right to sue advisers and their firms, is the biggest flaw with the rule, the DOL rule?

Mr. HALLORAN. It is certainly, if not the biggest, among the biggest, yes.

Mr. EMMER. There appears to be some misunderstanding of the litigation risk under the DOL fiduciary rule. Many people say that the litigation risk will not arise until January 1st of 2018, but I have heard this may not be correct. My understanding is that a lack of clarity and certainty regarding the rule has created concern about a very substantial litigation risk for advisers starting on June 9th.

Again, Mr. Halloran, can you explain?

Mr. HALLORAN. This doesn't get a lot of press or publicity, but the actions by class has always been present in ERISA rule. By taking ERISA law and applying that to IRA accounts, as an example, you are now exposing financial advisers even as of June 9th to a potential class-action litigation, because just giving rise to advice of moving out of a 401(k), for example, rolling over to an IRA. So, yes, that is a real and present concern, absent any private right of action that arises from a best-interest contract.

Mr. EMMER. You believe it is a real concern starting on June 9th?

Mr. HALLORAN. Oh, yes.

Mr. EMMER. Also, as long as I have focused on you, why is the litigation risk so great under the rules, as it is constructed? I am just going to tell you, as a lawyer, 1,000 pages makes it a huge litigation risk to have a rule that long.

Mr. HALLORAN. Yes, so that is a great point. It sounds very simple, we want a best-interest standard, we want to act in the best interests of our clients. The rule is 1,000 pages. The preamble was 204 pages. There are many, many ambiguities we are still going to deal with, notwithstanding changes that have been made, with, frankly, not a whole lot of guidance yet, either.

So there is more concern about what we don't know necessarily than what we do know. We don't really have case law to look to right now to understand the actual consequences of this private right of action and these kinds of actions. All we can look to is what we see in other businesses. And it is of significant concern.

Mr. EMMER. And unfortunately, in order to get that body of case law, you are going to have to have a lot of people suffer in courts of law, and you are going to have to pay a lot of attorneys, which I suppose the bar is probably not too disappointed with.

Mr. Lombard, my understanding is—and I am hoping because of your relationship with the current Chair of SIFMA—my understanding is that SIFMA has conducted a survey of its members about the effects of the rule. Are you familiar with that at all?

Mr. LOMBARD. I am aware that there have been surveys. There have been several of them. I am not sure I can quote their exact findings.

Mr. EMMER. Can you give me an idea? Do you know what the client experience has been to date and what effect the rule has had on their ability to serve their clients?

Mr. LOMBARD. As I said, there has already been disruption. There is limited product selection in certain areas, specifically fixed-income. Some of the members of SIFMA have stopped selling mutual funds. Some have stopped offering commission-based brokerage accounts in their retirement space.

As I also pointed out, costs are rising as many firms ask their clients to move into fee-based accounts, which are more expensive than traditional brokerage accounts.

Mr. EMMER. I think a lot of people agree that the time has come for some kind of fiduciary best-interest rule in this industry. But the rule as it is drafted—and I covered one area that is of big concern to me, and there are others—and unfortunately, the way it works around here is we have to step in and out, so I am assuming that people have covered some of these.

But I guess I would like to ask the panel, if the rule stays in effect, what changes would you like to see to make it more workable to allow advisers to sell products and services that they offer their clients? And for me, it is the lower end, the entry-level folks that we are all concerned with. We want to make sure they get the right advice.

Why don't we just start on this end?

Mr. KNOCH. So if the rule remains in effect, there are five specific things that the FSI would want to see changed in the rule. One would be streamlining the advice documentation and disclosure. Two, is creating a single best-interest standard applicable to all investors. Three, is revising and broadening the reasonable compensation rules. Four, is revising the rules for IRA rollovers. And five, is expanding the rule's grandfathering provisions.

Mr. EMMER. And my time has run out, it looks like, so I will be in touch with the rest of the panel. Thank you.

Chairman HUIZENGA. The gentleman's time has expired.

The Chair recognizes the gentleman from New Jersey, Mr. MacArthur, for 5 minutes.

Mr. MACARTHUR. Thank you, Mr. Chairman.

I really appreciated Mr. Scott's remarks earlier. There are not that many issues where both parties actually want the same outcome around here. We debate a lot of things back and forth. This may be one of those areas. I don't see that much daylight between what any of us want. We want investors to be protected with the optimal outcomes and the least costs. I don't think there is anybody on either side of the aisle who wants anything different. So if there is ever an issue for us to work together on and figure out the best way to get there, it seems to me this is one of them.

I have a very basic question first for Mr. Lombard. You mentioned in your opening remarks that your clients are confused by different sets of rules applying to investment accounts and retirement accounts. They are not alone in being confused. I like to think I am a pretty sophisticated investor. I have made my living on investments for some years now. I don't understand the different kind of rules that apply.

I don't think I have a good grasp on what the actual legal standard is for different kind of advisers. So if you could help my ignorance, for starters, I would appreciate it. What are the current rules that apply to different kinds of investors, briefly?

Mr. LOMBARD. There is the suitability rule that applies to broker-dealer activities. There is the SEC fiduciary standard that applies to investment advisory activities. And now there is the ERISA Department of Labor rule that applies to the retirement space that heretofore applied to retirement plans if you were deemed a fiduciary.

Mr. MACARTHUR. Do you think most advisers are crystal-clear on what their duties are as they deal with different kinds of clients?

Mr. LOMBARD. It is not just clients, sir. It is also advisers, people who have been in the business for decades are just coming to grips with these new regulations.

Mr. MACARTHUR. I asked maybe 2, 3 months ago my own advisers—I asked three of them what the standards were that applied to them. None of them gave me a clear answer, which is why I am asking you, none of them. They are all very smart. I rely on these people to not make too many mistakes with my investments.

So we clearly need a clearer standard. Is there anyone on the panel who doesn't support a single standard?

Ms. FIRVIDA. We support—AARP certainly supports a single standard as long as the standard is a fiduciary standard. And I would agree that there is confusion, and that confusion is creating the demand for a single standard. I think that is absolutely where the market is headed and where consumer demand is at.

Mr. MACARTHUR. Okay. Then it is obviously incumbent on all of us up here to figure out that standard with the most clarity and without the potential for litigation, because let's face it, that is a real issue. A single standard that does nothing but line the pockets of trial lawyers, either with individual lawsuits or class-action lawsuits, isn't good for anybody. That is not good for anybody.

It is not good for—so I had a question, Ms. Firvida, for you, too. You mentioned before that you were okay—I think you were the only one who suggested you were okay with robo-advisers. And forgive me if you have addressed this. I had to step out.

Ms. FIRVIDA. No, I would be very happy to.

Mr. MACARTHUR. I just want to better understand where you think robo-advisers are a better—and maybe I am putting words in your mouth, tell me if I am—but do you think that is equal to or better than live advice?

Ms. FIRVIDA. We really appreciate the opportunity to expand on that, on that question especially, since the question of robo-advice has come up several times in this hearing. The point that we would like to make is related to the point that Congressman Delaney made. There is a lot of innovation happening in the products and services that are being offered, and some of those are technological in nature. So robo-advisers is part of the innovation that is helping serve Americans saving for retirement, especially at small-dollar accounts. It can provide a lot of value, and it can provide fiduciary services.

And I will add, I understand that everyone here except for myself said, no, they don't believe robo is a good idea. But many traditional firms are adopting robo-services. The record is replete with examples of this. And those are traditional firms that many of the organizations testifying today are—those are firms—

Mr. MACARTHUR. I hate to cut you off—

Ms. FIRVIDA. —that are members of those organizations. So I think robo-services will be a part of the landscape even for traditional firms.

Mr. MACARTHUR. My time is—

Mr. HALLORAN. May I respond to that, as well?

Mr. MACARTHUR. My time has expired, but I will say—I just want to add this. There probably is a place for that, but let's not drive people away from human interaction where a human being can really understand the needs of another human being. Let's not force people into that because we have ruled out the other type.

Just one last thing, Mr. Chairman, if I can beg your indulgence. Mr. Lombard, I didn't write down your answer to my question. I would be grateful if you would send that to my office in writing.

Mr. LOMBARD. I would be happy to.

Mr. MACARTHUR. Thank you. I yield back.

Chairman HUIZENGA. The gentleman's time has expired.

The gentleman from Ohio, Mr. Davidson, is recognized for 5 minutes. And I am wondering if he would briefly yield to the Chair?

Mr. DAVIDSON. Thank you, Mr. Chairman. And I yield to the Chair.

Chairman HUIZENGA. Thank you. I just wanted to—I know that there was an answer to that, and I was hoping that you would be able to allow that and indulge it. Because I have to tell you, again, I love my mother, but she is not going to be on a computer to figure out how in the world she is going to manage her investments. She is not going to go through a voicemail tree when she is having a hard time and difficulty hearing it. It is tough enough getting prescriptions, much less investments.

So with that, I would yield back to the gentleman.

Mr. DAVIDSON. Thank you, Mr. Chairman. And thank you all. I have really enjoyed the dialogue that we have had here today. And I think it is an important issue that we address, because we really do have to protect the ability of people to save for their retirement.

I guess my question is really basic, in the sense that the premise—it seems to me that the premise of why you would invest in the market is you believe the market works. You believe that there is a path that would produce better investment alternatives than—and therefore, what is in the best interest of the saver is something that could be discerned through the forces of the market.

And I just wonder if the premise of this assumes that these people who have money—I think we can agree, without going down the line, that it is their money that they are saving—that they can't know who they should trust without the Federal Government in this case, particularly the Department of Labor, telling them who they can trust, and saying, hey, we are adding another layer of regulation in this.

So we need the Federal Government to tell us that it is okay to invest with these sorts of investors. We already have a lot of regulation from the SEC. This rule adds a layer. And as has been shared by a number of folks, the concerns of what happens to those savers—I talked with some investment advisers in the Eighth District of Ohio. And here is a story.

Darrell and Cynthia are a dual-income family, a young couple in their early 30s with 2 small children. Both have solid careers and are making ends meet. A year earlier, Cynthia lost her job, and because she didn't have a solid financial understanding, she withdrew roughly $20,000 from her 401(k), rather than rolling it over to an individual retirement account. After taking huge Federal and State tax hits, they parked the money in a savings account at a bank and left it there for several years because they didn't know how or where to invest it.

The couple knew a financial adviser from their church activities and they sought his help after becoming frustrated with the very low return their money had earned in the bank. The financial adviser shared basic financial concepts with that couple that they had never heard about, compound interest, the benefits of tax-deferred IRAs, and why parking retirement savings at a bank savings account is not as good of a path as something with better yields.

Darrell and Cynthia were frozen in fear because they lacked fundamental financial knowledge and made a bad decision by cashing out the 401(k). They have now moved their money into a retirement option that is right for them, and they are making smart financial decisions with the input from their financial representative.

Under DOL's fiduciary rule, millions of Americans like Darrell and Cynthia would be forced to fend for themselves and likely make similar mistakes, like cashing out their retirement savings too soon, and paying high fees and fines, which really alludes to some of the problems with ERISA in the first place and puts DOL already at too central of a role in how people manage their money.

As a former small business guy, we use simple and separate IRAs, simple IRAs. And one of the concerns I have is that many savers have this from small employers. Small businesses are a huge part of the growth in employment in our country. Mr. Knoch, how does the DOL fiduciary rule affect a business's ability to offer services for small employer retirement plans, such as simple IRAs?

Mr. KNOCH. Thank you, sir. I share the same concern you share, as well. This is the area where we have seen the largest impact based on the prospect of the rule, as well as its initial implementation. Simple IRA accounts at our firm are down 20 percent since 2016, and we forecast that simple IRA accounts will be down over 40 percent over the next 18 months.

Mr. DAVIDSON. Thank you for that. And that is a big concern. I will mention, as time flies by, that in 2011, DOL estimated consumers who invest without professional advice make investment errors that collectively cost them $114 billion per year. To anyone's knowledge on the panel, has DOL factored these statistics into its economic analysis for the rule? And how would those costs affect the rule?

Chairman HUIZENGA. And this has to be very quick.

Mr. KNOCH. I will answer that. I do not believe they have. And in fact, I think it is the single biggest flaw in the calculation.

Mr. DAVIDSON. Thank you. Mr. Chairman, I yield back.

Chairman HUIZENGA. The gentleman's time has expired. At this time, we welcome the ranking member of the full Financial Services Committee, the gentlelady from California, Ms. Waters, who is recognized for 5 minutes.

Ms. WATERS. Thank you very much, Mr. Chairman. I am sorry I was not able to be here earlier. But it is very important for me to be here because of the terrific fight that we had to put up on fiduciary. This is a very important issue. And of course, we had to go through quite a bit in order to make sure that the work that had been done at DOL could be realized following an Executive Order that was put forth by this resident that delayed it.

So I did not think that we were going to have to come back and have this fight all over again, but it looks as if we have to. So I want to thank all of the red shirts out there—AARP, I understand, is here. I am so glad you are here to remind folks what this is all about.

So with that, I would like to pose a question to Ms. Cristina Martin Firvida. As you know, before DOL promulgated the fiduciary rule, rules governing investment advice on retirement accounts had not been meaningfully updated in 40 years. As a result, there are many loopholes or gaps in the law that allowed—that were that allowed individuals to avoid fiduciary status and provide conflicted investment advice that cost our Nation's workers and retirees $17 billion each year.

Can you explain what those loopholes or gaps are and how they harm investors?

Ms. FIRVIDA. Thank you, Congresswoman. So as we stated in our statement earlier, there has been a standard in ERISA for over 40 years now to require fiduciary advice, but over the years, there have been many exemptions developed by the Department of Labor itself. And those are the loopholes that the rule that was finalized last year—those are the loopholes that were closed, in essence. Those were the loopholes that were revisited.

And we asked ourselves, in the current environment, where so many individuals need to make so many decisions about their own nest egg, because we no longer have the prevalence of defined benefit plans, do these continue to make sense? And the answer was no.

And to your point, we have estimated that the conflicted advice that could result from those loopholes was costing savers 5 years' worth of retirement income, which is unacceptable, because conflicted advice, again, is not free. There is a cost to regulation. We recognize that. There is a cost to enforcement. We recognize that. But there is also a cost to conflicted advice. It is not free.

There are two additional things that I would just like to add briefly, because we have talked a lot about the litigation risk in this rule. And I would like to make sure that we say today, reminding everyone that the litigation that is permitted in the rule is class-action litigation. And there are two things about that we need to remember. First, there has to be a systemic problem before a class-action cause of action can be brought, and I think that we can all agree that if there is a systemic issue in advice that is being provided, we would want to address that. So this is not about individual rights of action. This is about a systemic problem that affects a class.

And second, it is extremely difficult to certify a class, extremely difficult and more so in recent years after certain Supreme Court cases have been decided. So I really just wanted to make sure that we were all clear on what is the scope of the litigation risk.

Ms. WATERS. Thank you very much. To any of our other witnesses who are here today, prior to the DOL's fiduciary rule, if an employee sought advice on a one-time basis to roll over the assets in their employer-sponsored 401(k) to an IRA, the person from whom she sought that advice would not owe her any fiduciary duty. Tell me, if you were transferring your life savings from your 401(k), would you want your adviser to give you advice that is merely suitable? Or would you want that person to be held to a higher standard, like the DOL fiduciary rule, where they would be required to act in your best interests? Who would like to answer that question? Mr. Mark Halloran?

Mr. HALLORAN. I would answer it by, first of all, it is not necessarily the case that the person giving the advice would not be a fiduciary. They could be under the 1940's Act. It could be an IRA, RIA.

Secondly, I do think the suitability standard has been—it is a pretty high standard. That suitability standard has changed 6 times from 1992 to 2002, another 4 times, most recently in 2011. What I want is a trusted adviser to give me sound advice, regardless of the suitability standard—

Ms. WATERS. Reclaiming my time, since you think—

Chairman HUIZENGA. The gentlelady's time has expired.

Ms. WATERS. —suitable is fine, do you think that fiduciary is better?

Mr. HALLORAN. The fiduciary standard is a higher standard under the law.

Ms. WATERS. Thank you very much. I yield back the balance of my time.

Chairman HUIZENGA. The gentlelady's time has expired.

With that, the gentleman from Indiana, Mr. Hollingsworth, is recognized for 5 minutes.

Mr. HOLLINGSWORTH. Good afternoon. Thank you all for being here. I really appreciate all of the conversations and dialogue.

I am reminded of a cartoon I saw a few years ago that made me chuckle. It is a gentleman sitting across from his financial adviser with a big desk in between them. And he says, "I am retiring next Friday. I have nothing in savings. This is your chance to become a legend."

And I am worried with this rule that too many individuals will find themselves in that same situation. And what is the reason? The reason we have talked about so frequently during the course of this hearing, which is we are not able to get people started early saving small amounts because of the way this rule change in how the regulatory burden impacts small account holders, and they will be pushed out.

And I have just a couple of examples of that that I have continued to hear from constituents, both financial advisers as well as those seeking out financial advice. One talks about how as a financial adviser he has always prided himself on helping people getting started into retirement savings as early as possible and applauds individuals who come into his office. And just recently, he had the experience of having to turn away a young client who at 27 had the foresight to think he needed to start saving for retirement. But all he could put away was $100 to $150 a month.

And this financial adviser, much to his chagrin, had to turn it away, because his firm said that the new account minimum is going to be set at $5,000 on account of this, because it didn't make any sense for somebody to save in retirement $100 to $150 a month if fees were going to eat up that entire principal, not the earnings on that, but that entire principal each and every month.

And so the problem is, we have created this system now where people had to have significant funds and be able to have a significant account balance in order to get advice. And I think that is the great fallacy of over-regulation. The people we are most trying to help, those that are most on the fringe and margin of the financial system, we want to bring them in, but regulation continues to push them further and further away from getting good and reasonable advice. I want those people to participate.

My second example comes from a financial adviser in my district who has talked about how he has always worked hard to get people in the door, even goes to local fairs and tries to advertise how people should be saving for their retirement. Even if they don't choose him, he sees it as his mission across the district to increase awareness for retirement savings, because he doesn't want to see individuals come in and be that person and that gentleman in that cartoon.

And he talks about how he has recently had to give up some of his licenses because he is worried about the potential liabilities, because he doesn't know everything about every single customer who walks in the door. They are trying to save $300 or $500, what they might have outside that they don't disclose to him, and what that defense might look like. And he wanted me to ask a few questions.

I know most of them have been reviewed already. But for Mr. Holtz-Eakin, does it make sense to have a rule become effective while that rule continues to still be under review? There has been a lot of confusion in his mind about whether this rule is going into effect or not going into effect, what he has to mail out and what he doesn't have to mail out. And he finds the situation really troubling for himself and his business, but also for the many clients. And so does this make any sense?

Mr. HOLTZ-EAKIN. There are a lot of things about the current situation that doesn't make a lot of sense. That is one. The fact that the SEC hasn't moved is another. There is a litany of failures that bring us to this point. The best thing would be to go forward with a single standard and clean that standard up.

Mr. HOLLINGSWORTH. All right. The other thing that is really important to people back home in my district, which is a very rural district where there is very little access to broadband and there is very little access to the Internet, is this idea that robo-advice is going to fill the gap for these small individuals, and even without encouragement they will go out and seek robo-advice and rely on robo-advice. These individuals don't have access to the Internet. They don't have access to robo-advice.

And so they wanted me to ask you, are you concerned that robo-advice won't be able to fill the gaps for those who don't have access to the Internet, who come in to see me face-to-face? Either they are in rural areas or they might be one of our senior citizens, but they don't have real and general access to the Internet and thus need the in-person advice that I can provide, but I am being forced not to provide through this rule. Yes?

Mr. HOLTZ-EAKIN. I think the chief concern is not robo-advice. It is choice. People should get the advice which is best suited for them.

Mr. HOLLINGSWORTH. Right.

Mr. HOLTZ-EAKIN. And pushing people away from having that choice is what I am concerned about.

Mr. HOLLINGSWORTH. Are we currently barred from offering fiduciary products right now? Does the law prevent us from offering products that have a fiduciary standard right now? No.

Mr. HOLTZ-EAKIN. No.

Mr. HOLLINGSWORTH. Right, that is correct.

Ms. FIRVIDA. No product is barred under the DOL rule.

Mr. HOLLINGSWORTH. Or before the DOL rule, we can certainly offer fiduciary advice right now and people can have that. It is about choice. What I think Hoosiers back home are most concerned about is that bureaucrats in Washington more and more are telling them what products they can use, what products they should use, and what products are best for their futures and families when they are the ones who know what is best for themselves and their own futures. And so, I appreciate the panel.

Ms. FIRVIDA. But to be clear, in every survey we have ever done—

Chairman HUIZENGA. The gentleman's time has expired.

Ms. FIRVIDA. —9 out of 10 respondents want fiduciary advice.

Chairman HUIZENGA. Sorry, the gentleman's time has expired. So you may ask the next speaker for your time.

The gentleman from California, Mr. Sherman, is recognized for 5 minutes.

Mr. SHERMAN. We got this rule from an exhaustive process. The DOL considered and then withdrew its 2010 proposal, went back to the drawing board, published an updated proposal in April 2015. For its updated proposal, they had a comment period of 5 months, receiving feedback, including 3,000 comment letters, 300,000 signatures on petitions. They had more than 100 meetings with stakeholders, including the financial services industry, worker retirees, and consumer representatives.

The DOL also held 4 days of public hearings, which included 25 panels of witnesses and an opportunity for those not on a panel to submit written testimony. And there was an attempt consistently to consult with the SEC. So it was a good process.

On the other hand, it was absolutely absurd that we have one rule for the SEC and a different rule for the Department of Labor. Either consumer protection is necessary or free-fettered Wild West choice is necessary, but we actually ended up with the absurdity of greater restrictions and/or greater protections on Baby Boomers with their IRA and rollover accounts than with people in the greatest generation who are in their 80s and 90s whose accounts are not in Department of Labor-regulated provisions.

So we have a hard-working process that led to a bifurcated consumer protection system. Economists and some of the Democratic think groups are focusing on reducing cost, and that does make sense. But if you wanted to just reduce the cost of ice cream, then require that only vanilla ice cream be sold. That is efficient. You don't need an ice cream counselor. It is vanilla ice cream. That would get ice cream to everybody as cheaply as possible, as efficiently as possible, but people would eat an awful lot less ice cream because it is pretty boring.

By providing 31 flavors, Baskin-Robbins demonstrates that if you want people to save, you have to give them interesting choices as to how to save. And the focus here ought to be on how to get people to save more for their retirement, because Social Security is not sufficient.

Now let's get more to the details here of how we apply a rule. I will ask Ms. Firvida. Do you have any concerns that the fiduciary rule could have an unintended consequence of eliminating the ability of small financial institutions, small banks, credit unions, to provide IRA rollovers and other savings opportunities?

Ms. FIRVIDA. Thank you, Congressman. Our biggest concern, really, is not from the perspective—given who we are—of who is offering the services, but from the perspective of the client. And so I think what we understand is there are going to be some disruptions to the marketplace, and some of those disruptions are beneficial—many have been—for those saving for retirement.

So we would say small account holders, which is what I worry about—and many of them are going to smaller vendors—are coming out ahead in this rule. And that is beneficial to them and to their retirement and is one of the reasons why we support this rule.

Mr. SHERMAN. Okay. Dr. Holtz-Eakin?

Mr. HOLTZ-EAKIN. I have repeatedly said exactly the opposite, which is my concern is for those same small account holders, and that the combination of the fee-based accounts and the litigation costs will, in fact, make investment advice unavailable to them.

Mr. SHERMAN. And are people going to be subjected to just robo-advice under this rule? Or are they going to be able to talk to a human being?

Mr. HOLTZ-EAKIN. That will depend on what kind of person you are and the size of your account. As has been noted, if you are an affluent investor with a very large account, this is not going to change your ability to get that advice. The people most at risk are the smaller savers.

As I noted in my testimony, if you set the threshold at a $20,000 minimum balance in an IRA, about 42 percent of people would not be able to qualify for that. I am deeply concerned about that.

Mr. SHERMAN. People would be able to get a bank account IRA, but they might not be able to get other flavors.

Mr. HOLTZ-EAKIN. So we know that they would not get the current advice they get, and they would be thrown into an unknown regime. And that is the concern. They chose this set of advisers, and the rule does not allow them to keep them.

Ms. FIRVIDA. And I think as regard to robo, we had a discussion a little bit earlier where we do understand that many traditional firms are adopting robo-services, in addition to what they already offer, and that we believe the landscape in the future will include a combination of both, even at traditional firms. So we think that is probably where this is going.

Mr. SHERMAN. There is the argument that if you are only saving $10,000 and you get $500 worth of advice every year, maybe that is too much advice for the amount of money you are saving. But if you get $500 worth of advice every year, you are going to pay $500 one way or another.

Ms. FIRVIDA. And we have also discussed, of course, that conflicted advice is not free.

Chairman HUIZENGA. The Chair was not paying attention. Your time has expired.

Mr. SHERMAN. The comments were scintillating.

Chairman HUIZENGA. Yes, they were.

Mr. SHERMAN. I distracted you from the clock. You were paying attention to the—

Chairman HUIZENGA. Yes, I actually was, Representative. The gentleman from California often does have insightful questions. And with that, last but certainly not least, we will recognize the gentleman from West Virginia, Mr. Mooney, for 5 minutes.

Mr. MOONEY. Thank you. I am pleased to have an opportunity to participate here. This is a big issue in my district. I have had several town hall roundtables about it.

So under the final rule, this final fiduciary rule, one-size-fits-all from the Federal Government, if an investor likes their broker, they can keep their broker. Will the DOL rule harm investors?

Mr. HALLORAN. May I answer that question?

Mr. MOONEY. Sure.

Mr. HALLORAN. My dad likes his broker. My mom likes his broker. My mom and dad received a letter about 3 weeks ago saying that they are no longer eligible to work with their broker. I am probably eligible for AARP; certainly they are. That is the crux of this issue here for us, is it is—robo-advice is not bad. Robo-advice, frankly, was introduced many years before the DOL. Firms are embracing robo-advice. If you don't do that, you do it at your peril, frankly. It is a matter of choice.

My parents would love to continue to working with that trusted adviser who has been working for them for the last 15 years. They can't. Not unless that adviser leaves that firm.

I received a similar letter, if not the same letter. And in my case, I actually qualified for the fee-for-service. But what I would have to do is I would have to take my account, which I am averaging about 25 basis points paying for right now getting advice, and for the same advice from that same adviser, pay at least 75 basis points more. That is my choice right now.

This is not about—these are interesting academic arguments, frankly. The argument that Mr. Delaney put forward that annuities are permitted, sure, they are permitted under this rule. Are they going to be sold? No. They are not being sold, because they are disadvantaged by the rules bias towards fee-for-service.

It is about what is happening. It is about what is happening today, not what is potentially going to happen. We are seeing it every single day.

Mr. MOONEY. Thank you. I would like to kind of—as a follow-up related question, I would like to direct this one to Mr. Lombard. In your opinion, has the DOL—or just factually, has the DOL substituted its judgment, its own judgment, the DOL's judgment, for that of the expert regulator of the broker-dealers? And as a follow up, will the end result for investors be a loss of choices in product services of financial professionals?

Mr. LOMBARD. It is my opinion that the Department of Labor chose one business model—that of level fee advice advisory—over the traditional brokerage account, even though that doesn't fit for every client. And it is not just a matter of size. There are clients of substance who prefer, as my colleague here does, to keep their costs low, and that is not possible in advisory programs.

So again, it comes down to choice. And the DOL is forcing the hands of investors and providers to offer one in favor of the other, whereas before, investors had choice.

Mr. MOONEY. Dr. Holtz-Eakin, I see you nodding your head there, and so one more follow up here in the remaining minute-and-a-half that I have. You referenced the U.K. retail distribution review in your testimony as a comparison to the DOL fiduciary rule and how the U.K. financial conduct authority in 2016 conducted a review of that rule. What caused the U.K. to initiate the review?

Mr. HOLTZ-EAKIN. There was concern about the fallout from the 2013 decision to ban commission-based accounts. And when they looked, they found probably three striking results. The first was about a quarter of the advisers had exited the industry. And we have seen some exits in the U.S. already. They found that about 45 percent of the firms no longer provided advice to small accounts at all, or very rarely, so there was a clear departure from advice, either because the advisers were gone or because those who remained weren't talking to small account holders.

And we saw minimum balances go up. As I said, 13 percent of firms initially required 100,000 pounds or more. That moved up to

32 percent in only 3 years. That is exactly the kinds of concerns that have been expressed about the DOL rule.

Mr. MOONEY. But supporters of the rule have stated that the DOL rule will not have a similar impacts to that of the U.K. rule. Do you agree with that? Why or why not?

Mr. HOLTZ-EAKIN. We have seen some of the early evidence—some of the members of this panel have talked about it, and I mentioned some examples in my testimony where, for example, MetLife and AIG have exited the business. And we have seen Raymond James move to fee-based accounts. And this is exactly the sort of early indicators of the pattern that emerged in the United Kingdom. So I don't think these are hypothetical or academic or theoretical arguments. This is an experience that we saw in the U.K. and we are beginning to see in the United States.

Mr. MOONEY. Thank you. I think the facts show that some of these rules are well-intended, but they have the exact opposite effect. They hurt the very people you are trying to help. It is a shame we do that.

Chairman HUIZENGA. The gentleman yields back. And I guess I will just note that this strikes me as just fewer advisers giving less advice with greater government control and less choice for consumers. And that ultimately we have to make sure that consumers are protected and that they have the ability to do what is best for them.

So I deeply appreciate the time and effort of all of our panelists here. This was, I felt, a very informative and great panel. Without objection, I would like to submit the following statements for the record: a letter from the U.S. Chamber of Commerce; a letter from the National Taxpayers Union; and a letter from the Credit Union National Association (CUNA). Without objection, it is so ordered.

The Chair notes that some Members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 5 legislative days for Members to submit written questions to these witnesses and to place their responses in the record. Also, without objection, Members will have 5 legislative days to submit extraneous materials to the Chair for inclusion in the record.

And again, I want to say thank you to our panelists, and I appreciate them being here today. And with that, we are adjourned.

[Whereupon, at 12:18 p.m., the hearing was adjourned.]

A P P E N D I X

July 13, 2017

AARP
Real Possibilities

STATEMENT FOR THE RECORD

SUBMITTED TO THE

HOUSE FINANCIAL SERVICES
CAPITAL MARKETS SUBCOMMITTEE

Impact of the DOL Fiduciary Rule on the Capital Markets

July 13, 2017

AARP
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On behalf of our 38 million members and Americans saving for their retirement, AARP thanks Chairman Huizenga, Ranking Member Maloney and members of the Capital Markets, Securities and Investments Subcommittee for the opportunity to testify today on the Impact of the DOL Fiduciary Rule on the Capital Markets.

AARP is the nation's largest nonprofit, nonpartisan organization dedicated to empowering Americans 50 and older to choose how they live as they age. With nearly 38 million members and offices in every state, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands, AARP works to strengthen communities and advocates for what matters most to families with a focus on health security, financial stability and personal fulfillment. As a trusted source for news and information, AARP produces the world's largest circulation publications, AARP THE MAGAZINE and AARP BULLETIN. Nearly half of our members are employed full or part-time, with many of their employers providing retirement plans.

A major priority for AARP is to assist Americans in accumulating and effectively managing adequate retirement assets to supplement Social Security. The shift from defined benefit plans to defined contribution plans has transferred significant responsibility to individuals for investment decisions that will directly impact the adequacy of the assets available to fund future retirement needs. Unfortunately, the state of America's retirement landscape is cause for great concern. According to calculations by the Center for Retirement Research at Boston College, only about half of households have retirement savings and the rest of Americans have no source of income other than Social Security and the "retirement income deficit" for American households continues to grow.[1] According to recent analysis by EBRI, 47 percent of workers in 2017 reported the total value of their household's savings and investments, not just for retirement, was less than $25,000 and 24 percent had less than $1,000.[2] Given these trends, it is critical to do all we can to help Americans keep as much of their hard-earned nest egg as possible.

AARP has enthusiastically supported the Fiduciary Rule ("rule") as a necessary protection for savers when they make investment decisions concerning their retirement monies. Without this protection, it is difficult for an individual to effectively plan for a secure and adequate retirement. The rule requires retirement investment advice in the best interest of the client saving for retirement—that is to say, advice that minimizes conflicts of interest, is solely in the interest of the client, and which is provided with the care, skill, prudence and diligence that a prudent person would use. AARP agrees with the simple and basic tenet that retirement plan advisers should act in the best interest of retirement savers, and not in their own best interest.

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[1] Alicia H. Munnell, *401(K)/IRA Holdings in 2013: An Update from the SCF* (Sept. 2014), http://crr.bc.edu/wp-content/uploads/2014/09/IB_14-151.pdf.
[2] Lisa Greenwald et al., *The 2017 Retirement Confidence Survey: Many Workers Lack Retirement Confidence and Feel Stressed About Retirement Preparations* (Mar. 21, 2017), https://www.ebri.org/pdf/briefspdf/EBRI_IB_431_RCS.21Mar17.pdf.

I. The Public Has Demanded The Protections Of This Rule.

AARP members and the public generally have demanded and supported the protections of this rule. In survey after survey, we have found that retirement savers overwhelmingly want advice that is in their best financial interest. In an AARP 2013 survey of over 1,400 adults who had money saved in either a 401(k) or a 403(b) plan, more than nine in ten (93 percent) respondents favored requiring retirement advice to be in their sole interest, and fewer than four in ten (36 percent) respondents indicated they would trust the advice from an adviser who is not required by law to provide advice that is in their best interests.[3] A survey taken after the rule was promulgated demonstrated that an overwhelming percentage of respondents were in favor of the rule and believe it is important for financial advisers to give financial advice in a client's best interests.[4] Among those individuals who have received professional financial advice, the support was the deepest, with nearly 8 in 10 (78 percent) strongly agreeing with the rule.
In addition, plan sponsors generally favor the rule. In a survey of over 3,000 plan sponsors of all sizes, nearly nine in ten (89 percent) plan sponsors said that they would favor requiring giving advice that is in the sole interest of plan participants.[5]

In the Committee room today are several AARP members who have traveled here today to attend the hearing and show their support for the rule. AARP members were actively engaged in voicing their support for this rule during the open comment period in 2015. Close to 100,000 AARP members took over 200,000 actions in support of the rule in 2015, including submitting close to 60,000 messages to the U.S. Department of Labor, and delivering over 26,000 petitions to the House Financial Services Committee. The 26,000 petitions we delivered to the Committee have been resubmitted to the Committee for the record.

We are communicating with our members now about the Department of Labor's current open comment period on modifications to the rule and further delay of its enforcement and expect that many of our members will write or call to support the rule. AARP has also used its own channels to inform our members and the broader public about the benefits of the rule, including multiple articles in AARP's Bulletin, which is mailed to all 38 million members. We have worked in collaboration with organizations such as Yahoo Finance to produce educational videos regarding the rule and its benefits. Finally, AARP is developing a tool that will walk investors through the questions they should ask a prospective or existing financial adviser,

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[3] AARP, *Fiduciary Duty and Investment Advice: Attitudes of 401(k) and 403(b) Participants* (Sept. 2013), http://www.aarp.org/research/topics/economics/info-2014/fiduciary-duty-and-investment-advice---attitudes-of-401-k--and-4.html.
[4] S. Kathi Brown, *Attitudes Toward the Importance of Unbiased Financial Advice* 4, 6 (May 2016), http://www.aarp.org/content/dam/aarp/research/surveys_statistics/econ/2016/attitudes-unbiased-fin-advice-rpt-res-econ.pdf.
[5] AARP, *Fiduciary Duty and Investment Advice: Attitudes of Plan Sponsors* (Mar. 2014), http://www.aarp.org/research/topics/economics/info-2014/fiduciary-duty-and-investment-advice---attitudes-of-plan-sponsor.html.

including whether the adviser operates under a fiduciary standard. We developed the app in collaboration with the North American Securities Administrators Association and anticipate launching the tool this fall.

In addition to the support of individuals saving for their retirement, many states agree the fiduciary rule is needed to protect residents and deter potential exploitative practices. In fact, earlier this year Attorneys General from across the country, including Hawaii, Illinois, New York, North Carolina, Iowa, Oregon, Pennsylvania, Washington, and the District of Columbia, issued letters urging the Department of Labor to proceed with the rule that would require financial advisers to put their clients' best interests ahead of their own. Additionally, California, Missouri, South Carolina and South Dakota already impose a fiduciary standard on brokers in their states. In response to recent efforts to dilute the Department of Labor rule, Nevada enacted legislation to subject broker-dealers and investment advisers to a fiduciary standard, with the support of AARP Nevada. We expect more states to establish this standard going forward.

The rule also has the support of personal finance columnists and reporters who have repeatedly touted the beneficial effects of the rule. In scores of articles, personal finance writers from diverse publications have informed their readers of the rule's requirements and protections. Many of them have provided their readers with questions to ask their advisers to ensure that their advisers are fiduciaries.

I. Most of the financial services industry agrees that a fiduciary standard is the appropriate standard for providing retirement investment advice.

The financial services industry generally agrees that investment advice should be provided in the best interests of the participant and retirement investor. Registered investment advisers and certified financial planners have for decades successfully provided fiduciary advice. Noting that the public demand for fiduciary advice has increased dramatically and that the market continues to move in the direction of providing fiduciary advice, the Certified Financial Planner Board of Standards last month issued for public comment proposed revisions to its *Standards of Professional Conduct*, which sets forth the ethical standards for CFP® professionals. The draft revision broadens the application of the fiduciary standard, effectively requiring CFP® professionals to put a client's interest first at all times. The current *Standards* require CFP® professionals to act in a fiduciary capacity only when providing financial planning. The CFP Board is expected to finalize its updated *Standards* later this year.

Public comment letters to the Department of Labor also demonstrates the overwhelming consensus on the best interest standard. *E.g.*, Transamerica Comment Letter 894 ("The Company has consistently indicated its support for a best interest standard, transparency and treating customers fairly"); SIFMA Comment Letter 506 ("The industry ... shares that goal" "to ensure financial services providers are looking out for their customer's best interest"); Plan Sponsor Council of America Comment Letter 614 ("[W]e believe our retirement system will be greatly strengthened by ensuring that investment advice is provided in the recipient's best interest consistent with those fiduciary standards and that any financial conflicts are disclosed."); American Council of Life Insurers Comment Letter 621 ("We share the Department's interest in seeing that plan sponsors, plan participants and Individual Retirement Accounts (IRA) owners receive advice that is in their best interest."); American Bankers Association Comment Letter 622 ("We agree with the Department that retirement service providers, when acting in their capacity as fiduciaries, should act in the best interest of customers and that such customers deserve to be protected from financial abuse."); Insured Retirement Institute Comment Letter 626 ("Financial professionals should be held to a best interest standard when recommending investments to retirement investors."); Business Roundtable Comment Letter 645 ("Financial professionals should be required to act in the best interests of employee benefit plan participants when providing investment advice to a retirement plan or its participants."); Wells Fargo Comment Letter 647 ("[W]e remain supportive today of a "best interest" standard of care for clients.").

There should be no surprise about this consensus since these statutory standards have been in place since the Employee Retirement Income Security Act (ERISA) was enacted in 1974. Indeed, treating those who provide investment advice for a fee as a fiduciary is consistent with both the statute and the common law of trusts upon which ERISA was based. Significantly, although there have been attempts to weaken the rule requiring those who provide investment advice for a fee to be treated as a fiduciary, Congress has never agreed to dilute the standard adopted over 40 years ago to protect and preserve employees' hard-earned retirement savings.

II. Weakening The Fiduciary Rule Will Undermine The Financial Security Of Americans Saving For Retirement.

Although AARP is extremely disappointed that enforcement of the rule has been delayed until January 2018, we appreciate that the Department of Labor has decided to go forward with the applicability date for the fiduciary rule, beginning last month on June 9, 2017. To dilute or rescind the fiduciary rule is simply too costly to retirement investors. Retirement investors are at risk of a 1 percent drop in annual returns on retirement savings without the rule.[6] Increasingly, the way that most Americans save and invest is through their employer sponsored retirement plans, most typically a 401(k) type savings plan. The Government Accountability Office (GAO) has estimated that $20,000 in a 401(k) account that had a one percentage point higher fee for 20 years would result in an over 17 percent reduction in the account balance, a loss of over $10,000.[7] We estimate that over a 30-year period, the account would be about 25 percent less. Even a difference of only half a percentage point — 50 basis points — would reduce the value of the account by 13 percent over 30 years. Conflicted advice resulting in higher fees and expenses can have a huge impact on retirement income security levels.

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[6] U.S. Gov. Accountability Office, *GAO-11-119, Improved Regulation Could Better Protect Participants from Conflicts of Interest* 31 (Jan. 2011), http://www.gao.gov/assets/320/315363.pdf.
[7] U.S. Gov. Accountability Office, *GAO-07-21, Private Pensions: Changes Needed to Provide 401(k) Plan Participants and the Department of Labor Better Information on Fees* 7 (Nov. 2006).

Risks caused by conflicted investment advice are also increasing as the baby boomers retire and are encouraged to move their money from protected ERISA plans to IRAs. The Department of Labor (DOL) found that advice from conflicted investment advisers could cost these retirees between 12 to 24 percent in lost retirement savings over thirty years.[8] The DOL found that IRA investors tend to be older as they are close to or at retirement. These IRA investors are more vulnerable to the negative impact of conflicted advice because the amount of assets available for rollover are large, many older investors do not have strong financial literacy skills, and they are making significant and often one-time decisions to move their retirement savings from more protected employer based plans into significantly less protected IRAs.[9]

Lower and middle-income retirement investors need every penny of their retirement savings. "Among the 48 percent of households age 55 and older with some retirement savings, the median amount is approximately $109,000 — commensurate to an inflation-protected annuity of $405 per month at current rates for a 65- year-old."[10] DOL likewise has established that "small investors" (that is, those with low balances or those with modest means) are most negatively impacted by the detrimental effects of conflicted advice. Those with small accounts have fewer economic resources, and consequently any additional costs or losses diminish what little savings they have worked so hard to amass.

Congress sought to protect the retirement savings of millions of workers, retirees, and their families when it enacted the Employee Retirement Income Security Act of 1974. ERISA, the result of a decade of legislative consideration, established far-reaching standards to protect consumers through timely disclosure of information, minimum standards for participation, funding rules, fiduciary duty over invested monies, and access to legal redress for violations of the law. ERISA specifically applies to financial service firms that handle retirement monies, including insurance companies, investment firms, and broker-dealers. All of these actors are subject to ERISA when they are providing retirement advice, even if they are also subject to standards promulgated by other agencies or self-regulating bodies. These entities have largely successfully complied with ERISA for over forty years.

The rule could have important benefits for the broader economy. If households — especially lower and middle class older individuals — have more money in their modest retirement accounts because of lower fees, they will have more money to spend in the economy on goods and services. Conflicted advice may also impact the broader economy by misallocating capital, resulting in inefficiencies that do not promote economic growth.[11]

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[8] U.S. Dep't of Labor, *Fiduciary Investment Advice: Regulatory Impact Analysis* 3-4 (2015).
[9] *Id.* at 59-60.
[10] U.S. Gov't. Accountability Office, *GAO-15-419, Retirement Security: Most Households Approaching Retirement Have Low Savings* 11 (May 2015), http://www.gao.gov/
assets/680/670153.pdf.
[11] Benjamin P. Edwards, *Conflicts and Capital Allocation*, 78 Ohio St. L.J. 1 (2017) at 21.

Regardless of the method used to calculate the losses, it is clear that repeal of the rule jeopardizes the retirement security of hard working Americans, and could have a negative impact on the economy more broadly.

III. The Rule Has Not Reduced Access To Retirement Information And Financial Advice.

While some disruption within the retirement services industry can be expected after updating a 40-year old regulation to make it relevant to the current retirement marketplace, the disruption has overall been positive for retirement investors. The disruption has resulted in lower fees, advice in the best interest of the saver or retiree, and minimized conflicts in advice provided to individuals. Many investment firms and their advisers have also taken steps to meet the requirements of the regulation and already have incurred one-time, up-front compliance costs. Significantly, we have not seen prices increase for those companies that have significantly complied with the rule. In fact, repealing the rule, as this proposal seeks, will not only harm consumers but place these firms and advisers at a disadvantage.

Under the rule, Americans will still be able to access a variety of retirement savings offerings. There is no prohibition in the rule against any type of retirement investment product. The rule does not require investment firms to abandon products, but instead allows the investment marketplace to evolve and innovate to provide investments and products that answer the needs of individuals who now shoulder greater responsibility for their retirement security as well as provide protection for their hard-earned retirement monies. Indeed, the market is responding already to the public demand for fewer conflicts of interest, greater transparency, and lower fees. The recent development of new investments with differentiated fees such as clean shares and T shares by leading investment firms demonstrate this point. Conversely, as individual firms respond to market signals, they may discontinue offerings that do not meet client demands. The choice to develop or discontinue an offering is up to an individual adviser, broker or firm. Because ERISA does not have an authorized or legal list of investments, the rule is consistent with Congress's design of ERISA's broad fiduciary rule.

In addition, investment firms will continue to make business decisions on how to structure their customer relationships. Firms will determine whether to make use of the Best Interest Contract Exemption for certain products or particular fee arrangements. The decision of each firm may be different depending on an analysis of its business model and its client base. By way of example, three of the largest defined-contribution plan providers are reported to have chosen three distinctly different compliance strategies.[12]

Americans saving for retirement have the majority of their savings in defined contribution plans and IRAs. Given the nearly $8 trillion in assets in IRAs and the almost $5 trillion in 401(k) plans, there is neither evidence— nor any reason to believe — that financial service providers will

[12] Greg Iacurci, *Fidelity, Empower and T. Rowe take three different approaches to the DOL fiduciary rule*, INVESTMENT NEWS (Mar. 7, 2017), http://www.investmentnews.com/article/20170307/FREE/170309941/fidelity-empower-and-t-rowe-take-three-different-approaches-to-the

abandon this lucrative market.[13] Thus, to the extent there are disruptions, retirement savers stand to benefit as the various players in the financial services industry adjust to maintain their competitive edge. AARP has every confidence that the financial services industry and the retirement advice market will continue to develop innovative new products and systems to help hard working Americans save for retirement.

IV. Broker-Dealers, Investment Advisers, and the Fiduciary Standard

Both broker-dealers and investment advisers play an important role in helping Americans manage their financial lives, and accumulate and manage retirement savings. Clients receiving investment advice should receive a standard of care that is in their best interest, regardless of whether the advice comes from a broker-dealer or an investment adviser. Any effort to dilute existing safeguards, whether through rulemaking or legislative channels, puts consumers and their savings at unacceptable risk.

AARP appreciates that the draft bill under discussion today seeks to impose a best interest standard on broker-dealer recommendations. Advice in the best interest of individuals saving or investing is something AARP has long supported. However, by failing to identify the standard as a fiduciary standard and deviating from the standard applicable to all other advisers, the bill permits something short of full fiduciary protections. It could even suggest that compliance with the existing suitability standard, which makes reference to the best interest of the customer but does not require brokers to rein in conflicts or consider other investments, would meet this benchmark. If that is not the bill author's intent, we respectfully suggest that this point needs to be clarified. If this failure to impose a full fiduciary standard is intentional, however, that falls well short of the protections investors need and deserve.

a. The draft bill does not strengthen the suitability standard, leaving investors confused and at risk.

The regulatory imbalance between the duties of brokers and investment advisers has persisted for many years, even as evidence demonstrating that brokers have transformed themselves from salesmen into advisers has grown. Many brokers today call themselves "financial advisers," offer services that clearly are advisory in nature, and market themselves based on the advice offered. For example, one firm advertises that it "proudly strive[s] to embrace [its] own fiduciary responsibilities" and that its "highest value is to 'always put the client first,'"[14] even though its Form ADV brochure (a regulatory filing that the SEC requires to be given to clients after a transaction is completed) demonstrates otherwise, noting that "[d]oing business

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[13] ICI Research Report, *Defined Contribution Plan Participants' Activities, First Three Quarters of 2016* at 2 (Feb. 2017), https://ici.org/
pdf/ppr_16_rec_survey_q3.pdf.

[14] Letter from Robert Reynolds, President and CEO of Putnam Investments, to U.S. Dep't of Labor (July 20, 2015), *available at* https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-ZA25/00077.pdf.

with our affiliates could involve conflicts of interest if, for example, we were to use affiliated products and services when those products and services may not be in our clients' best interests."[15] As a result of such deceptive statements, the average investor cannot distinguish between brokers and advisers and does not recognize that their "financial adviser" operates under a lower legal standard than that to which an investment adviser is held. Nor is it surprising that investors expect that those who advertise themselves as a trusted adviser will provide financial advice in the best interest of the investor.

Federal regulations have not kept pace with changes in business practice, and broker-dealers and investment advisers continue to be subject to different legal standards when they offer advisory services. According to the Commission's 2011 Study on Investment Advisers and Broker-Dealers, as of the end of 2009, FINRA-registered broker-dealers held over 109 million retail and institutional accounts and approximately 18 percent of FINRA-registered broker-dealers also are registered as investment advisers with the Commission or a state.[16] The draft bill is silent on the legal standards that will apply when a dually registered investment adviser and broker-dealer acts in both capacities and offers investment advice and/or executes sales.

Ensuring all securities professionals who offer investment advice to retail investors are subject to a fiduciary standard is needed to ensure a level and transparent market for investors seeking advice. Investors deserve a regulatory system that is designed to promote the best interests of the investor and imposes comparable standards on investment professionals who are performing essentially the same function as financial advisers. Research has found investors typically rely on the recommendations they receive from brokers and investment advisers alike. The trust most investors place in financial professionals is encouraged by industry marketing, leaving investors vulnerable not only to fraud but also to those who would take advantage of that trust in order to profit at their expense. Investors who place their trust in salespeople who market services as financial advisers can end up paying excessively high costs for higher risk or underperforming investments that only satisfy a suitability standard, but not a fiduciary standard. That is money most middle-income investors cannot afford to waste.

b. The duties of brokers must be clearly defined.

As currently drafted, the draft bill focuses on what is *not* required of a "best interest standard" and what the standard does *not* preclude (e.g., transaction-based compensation, including third-party payments, principal trades and recommendations of proprietary products). However, the proposal does not illustrate what *is* definitively required of broker-dealers in order to meet the standard (other than a newly conceived comparison to the business practices of another broker or dealer).

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[15] Putnam Advisory Company, LLC, SEC Form ADV Part 2A at 25 (Mar. 30, 2016), available at http://www.adviserinfo.sec.gov/IAPD/Content/Common/crd_iapd_Brochure.aspx?BRCHR_VRSN_ID=375046. (Putnam Investments wholly owns Putnam Advisory Company through various subsidiaries.)

[16] S.E.C, *Study on Investment Advisers and Broker-Dealers* (Jan. 11, 2011).

In addition, the section on disclosures is concerning. As currently drafted, the bill lists three options for the handling of conflicts -- avoid, disclose, or manage. Disclosing conflicts is not adequate and does not shield investors from conflicts nor does it compel mitigation of existing conflicts. Furthermore, the draft bill is ambiguous as to whether disclosures are required only at initiation of the relationship between the broker-dealer and the investor, and as to whether the disclosures described in this bill supersede other disclosures that do not pose a material conflict. The bill also does not specify the ways in which a broker-dealer must manage conflicts of interest. Failure to address this flaw in the proposal would leave investors vulnerable to unscrupulous advisers.

c. Agencies should retain authority to protect consumers and enforce rules under ERISA.

The draft proposal could potentially preclude both the SEC and DOL from taking action to adopt stronger protections for investors and retirement savers, even if they find that this bill's approach is inadequate, or the market evolves with unanticipated consequences. In addition, it could substantially weaken the standard that applies under ERISA to advice from registered investment advisers.

d. The draft bill raises numerous additional concerns.

The draft bill raises numerous additional concerns. The draft bill does not ensure broker-dealers who provide investment advice meet minimum training and competency requirements. By contrast, fiduciaries are affirmatively required to obtain training on their duties and their legal obligations. The draft bill fails to require brokers to apprise investors in advance of a sale of the amounts of all compensation (only the types of compensation must be reported). The bill covers retail sales and exempts institutional sales, but fails to define either term. It permits broker-dealers to provide advice for "non-discretionary" roll-overs of retirement assets, but also fails to define what meets this standard. Finally, it broadly exempts investment advisers for variable annuities, which are costly and complex, from adhering to a fiduciary standard when recommending variable annuities to investors.

We thank the Committee for the opportunity today to share AARP's views on the Department of Labor's fiduciary rule and on the draft bill which would repeal that rule and replace it with a discretionary best interest standard for broker-dealers. AARP remains committed to the strongest possible fiduciary standard for retirement investment advice and recommends a similar standard for all other investment advice. Repealing the fiduciary rule as promulgated by the Department of Labor would significantly diminish retirement security, and we oppose its repeal. AARP stands ready to serve as a resource and partner in developing an effective standard for investment advice that will promote and protect the retirement security of American families.

STATEMENT OF THE AMERICAN COUNCIL OF LIFE INSURERS

BEFORE THE HOUSE COMMITTEE ON FINANCIAL SERVICES

SUBCOMMITTEE ON CAPITAL MARKETS, SECURITIES, AND INVESTMENT

ON THE IMPACT OF THE DOL FIDUCIARY RULE ON THE CAPITAL MARKETS

THURSDAY, JULY 13, 2017

STATEMENT MADE BY MARK HALLORAN, SENIOR DIRECTOR,

HEAD OF INDUSTRY AND REGULATORY STRATEGY, TRANSAMERICA

Chairman Huizenga, Ranking Member Maloney, and members of the Committee, I am pleased to present this statement expressing the views of the American Council of Life Insurers on the impact of the DOL Fiduciary rule on the capital markets. Thank you for the opportunity to testify before you today.

My name is Mark Halloran and I am the Senior Director, Head of Industry and Regulatory Strategy at Transamerica. Transamerica is one of the nation's leading providers of financial services and insured products, including annuities, to America's families and individuals working to build a solid financial foundation. For the past several years I have worked with the ACLI and many of its member companies on the difficult challenges confronting both retail investors and the financial professionals who serve them under the U.S. Department of Labor's Fiduciary Regulation.

The American Council of Life Insurers is a Washington, D.C.-based trade association with approximately 290 member companies operating in the United States and abroad. ACLI advocates in federal, state, and international forums for public policy that supports the industry marketplace and the 75 million American families that rely on life insurers' products for financial and retirement security. ACLI members offer life insurance, annuities, retirement plans, long-term care and disability income insurance, and reinsurance, representing 95 percent of industry assets in the United States.

ACLI supports reasonable and appropriately tailored rules that require all sales professionals to act in the best interest of their customers. Prudential regulators such as the

SEC and state insurance regulators, not state courts and the plaintiffs' bar, are best positioned to apply and enforce a best interest standard of care. To meet their financial and retirement security needs, America's savers and retirees deserve rules that ensure continued access to a wide variety of retirement product offerings, retirement savings information and related financial guidance from financial professionals acting in their best interest.

ACLI supports the Discussion Draft being reviewed by the Subcommittee at today's hearing. ACLI thanks Chairman Huizenga, Representative Ann Wagner, and other members of the Committee for their strong leadership on this issue. The Discussion Draft would establish a "best interest" standard of conduct to govern the relationship between broker-dealers and their individual representatives with retail investors.

Perhaps most importantly, the best interest standard of conduct under the Discussion Draft would apply to the totality of the relationship between consumers and financial professionals; not just the one dimension of the relationship that involves ERISA plan or IRA assets. The bill also installs important statutory safeguards to permit transaction-based financial professionals, including broker-dealer registered representatives and insurance agents, to continue to offer products and services to retail investors under traditional compensation models. These safeguards would effectively preserve retail investor access to information, freedom of choice over how to pay for financial advice and a robust, competitive marketplace for insured retirement solutions. The Discussion Draft at long last harmonizes the multi-faceted bodies of law and regulation applicable to the sale of insurance and annuity products at the retail level.

My testimony today focuses on three key areas. First, I will briefly review the clear and present danger that the Department of Labor's Fiduciary Regulation poses to the financial well-being and retirement security of average working Americans. Second, I will address how the Discussion Draft addresses and resolves that threat by preserving retail investor freedoms of access and choice under a coherent "best interest" standard of conduct. Third, I will offer some final thoughts on why we at ACLI believe the Discussion Draft approach brings much needed regulatory harmony, stability, and certainty to the marketplace for retail investment advice.

The Department of Labor's Fiduciary Regulation Harms Middle Income Savers and Limits Consumer Choices

However well-intentioned it may be, the DOL's Fiduciary Regulation poses a very real threat to the financial well-being and retirement security of working Americans. It is difficult to overstate the magnitude of that threat. The continued availability of what today is taken for granted – a vibrant and competitive marketplace for insured retirement solutions, readily available access to cost effective financial advice and true consumer choice about how to pay for that advice – is seriously jeopardized under the DOL's approach.

The core problem with the DOL Regulation is that it re-characterizes virtually **all** financial services and product sales activity directed to employer-sponsored retirement plans, including participants, or to individual retirement accounts ("IRA's"), as "fiduciary" conduct within the meaning of ERISA and the Internal Revenue Code. That sweeping approach is enormously problematic for distributors of insurance and annuity products. ERISA's fiduciary standard, which strictly prohibits financial conflicts of interest and the receipt of payments (including sales commissions) from third parties in connection with a recommended transaction, renders the compensation structures that are best tailored for insurance and annuity sales distribution organizations illegal unless and except to the extent that a prohibited transaction exemption is available to cover the transaction.

The Department of Labor has devised a prohibited transaction exemption known as the "Best Interest Contract" or "BIC" Exemption that, in theory, would exempt the receipt of sales commissions and other incentives by fiduciary advisers. As a practical matter it effectively forbids the use of sales commissions as a manner of payment. The conditions of the BIC Exemption are so exceedingly complex and technical as to present serious questions as to whether they can realistically be met. Moreover, the BIC Exemption contains an inherent, deeply-rooted bias that strongly favors the provision of investment advice on a fee for service basis and strongly disfavors the provision of products and services by those who are compensated on a commission, or transaction-based basis. It has retained this bias even though commentators have warned DOL that for all but the wealthiest segment of the retail investor community, fee-based advice is frequently uneconomical and unaffordable.

To make matters worse, the BIC Exemption has been intentionally designed to expose distributors of financial services and products to a significant risk of widespread private plaintiffs' class action claims.

The fee-based advice model that the DOL Regulation favors may meet the needs of active traders and the very wealthy, but not the needs of "buy and hold" investors or purchasers of annuity products, which are designed for long term retirement goals. Fee-based arrangements often carry hefty account minimums (typically between $100,000 and $250,000), and rarely include annuities, as these products do not typically necessitate continual advice and investment management. Retail investors with small or mid-sized accounts need continued access to experienced, knowledgeable transaction-based financial professionals who can inform them about the guaranteed lifetime income features available through annuity products and assist in fitting those products to individual investor needs.

Under the DOL Regulation, an advice gap has developed for small and medium retirement account holders who do not meet higher account minimums for fee-based arrangements. Small and medium retirement account holders are consequently left without any advice. For these savers, the DOL inappropriately relies on computer generated asset allocation platforms, commonly referred to as "Robo-Advisers". Yet, the DOL concedes that these automated asset allocation services likely do *not* offer the same benefits as financial professionals – benefits that include encouraging greater savings, responding to client-specific questions, and dissuading emotional investing, such as liquidating assets during a downturn like the 2008 market crash. The DOL has failed to explain how computer-generated asset allocation platforms, given these crucial limitations, can serve as an adequate substitute for a financial professional.

Less advice from financial professionals can contribute to reduced savings on the part of working Americans and diminished retirement security for retirees in need of guaranteed lifetime income through annuities.

The Discussion Draft Protects the Interests of Retail Investors

The Discussion Draft takes a common sense approach to addressing and resolving the threats posed by the DOL Regulation and by doing so preserves access to investment advice for average investors and their families. It amends certain provisions of the Securities Exchange Act of 1934 (the "34 Act"), the Dodd Frank Act, ERISA, and the Code to weave together a coordinated and complete "best interest" standard for transaction-based financial professionals that protects all dimensions of the retail investor client relationship, including but not limited to the portion of the relationship that concerns ERISA and IRA assets. By doing so, it renders moot the exceedingly complex, highly technical conditions of the BIC Exemption that today threaten to stifle retail investor freedoms of choice and access.

At the centerpiece of the bill is an amendment to the '34 Act that enshrines a "best interest" standard governing the delivery of investment recommendations by broker-dealers and their individual representatives to retail customers. Best interest recommendations would need to reflect reasonable diligence, care, skill, and prudence in light of the client's investment profile.

The Discussion Draft contains disclosure rules to complement the new standard. At the outset of the customer relationship, broker-dealers would need to clearly and concisely disclose the type and scope of the services to be provided, the standard that may apply to the relationship, the types of compensation that the broker-dealer and its representatives may receive, and any material conflicts of interest. Importantly, the bill safeguards the legal validity of traditional, transaction-based compensation structures by providing that the receipt of sales commissions, recommendations of principal transactions, recommendations of affiliated, unaffiliated or proprietary products or services, or limitations on the range of products and services offered would not, in and of themselves, constitute violations of the '34 Act's best interest standard of care.

Since the Discussion Draft amends the federal securities laws, the new "best interest" standard would govern the totality of a broker-dealer's securities relationship with a retail investor; not just the portion of the relationship that pertains to ERISA plan and IRA recommendations. In regards to ERISA plan and IRA recommendations, the Discussion Draft would stay the hand of DOL by forbidding the promulgation of any regulations defining the circumstances under which a person is deemed to be a "fiduciary" if those regulations would impose any obligations on a broker-dealer or its representatives or on a life insurance company or its agents that is either inconsistent with or in addition to the obligations set forth under the '34 Act. In addition, the ERISA statute and its parallel Internal Revenue Code provisions would be amended to add a new statutory prohibited transaction exemption to cover any recommendations made by a broker-dealer or its registered representatives that are consistent with the '34 Act standard. Similarly, the exemptions would be available to registered investment advisers, banks, and other financial institutions who comply with standards substantially similar to the '34 Act standard. This assures a level playing field for all financial professionals and financial institutions.

Life insurance companies and their agents frequently distribute annuity and other insurance products through registered broker-dealer organizations. To that extent, the ERISA protections afforded by the Discussion Draft would be directly available. To cover those instances where annuity and insurance products are distributed other than through a broker-dealer, the same prohibited transaction exemption would be applicable where the manufacturer or distributor of insurance products adopts and implements practices on a nationwide basis that meet or exceed the '34 Act's standard and substantially complies with that standard.

The Discussion Draft's straightforward approach protects the interests of retail investors. Sales recommendations of securities and annuity products will reflect the investors' best interests, in light of their customer profiles. At the same time, the preservation of transaction-based compensation structures will ensure that consumers have continued access to information and advice and freedom of choice about how to pay for advice.

The Discussion Draft Facilitates Coordination By Prudential Regulators and Harmonization of the Regulation of Advice to Retail Investors

The regulatory environment governing the delivery of investment advice to retail investors, which has already been de-stabilized by the DOL Regulation, threatens to become even more fractured unless Congress takes action. The bill sensibly places responsibility for issuing regulations in the hands of the primary regulators, the SEC and state insurance regulators. The bill would also place a statutory obligation on the SEC to coordinate and cooperate with state insurance regulators.

Conclusion

The Discussion Draft's establishment of a unified standard of care to govern the delivery of financial advice to the retail investor community, its identification of the SEC as the lead regulator for purposes of implementing that standard for securities, and emphasis on coordination and cooperation with state insurance regulators reflects good policy, will stabilize the marketplace for the delivery of retail financial products and services to consumers and will benefit consumer interests by restoring freedom of access and choice.

Thank you for the opportunity to testify today and for your consideration of the views of ACLI.

Impact of the DOL Fiduciary Rule on the Capital Markets

United States House of Representatives

Committee on Financial Services

Capital Markets, Securities, and Investment Subcommittee

Douglas Holtz-Eakin, President *

American Action Forum

July 13, 2017

*I thank Meghan Milloy for her assistance in preparing this testimony. The views expressed here are my own and not those of the American Action Forum.

Chairman Huizenga, Ranking Member Maloney, and members of the Subcommittee, thank you for the opportunity to appear today and share my views on the impact of the Department of Labor's (DOL's) fiduciary rule on capital markets. And thank you for your efforts to repeal the rule and to enact a rule that is more workable and effective for both consumers and the retirement advice market.

When the fiduciary rule was finalized in 2016, it was (and still is) the most expensive regulation that year, with $31.5 billion in total costs and $2 billion in annual burdens[1] on the companies– many of which are small businesses – and advisors it affects. Although the rule has not yet been fully implemented, research from the American Action Forum (AAF) has found that several major companies have already left part of the brokerage business or are drawing down their business and/or switching to a fee-based arrangement. From these companies alone, reported compliance costs have already topped $100 million, affecting 92,000 investment advisors, $190 billion in assets, and at least 2.3 million consumers.[2]

Advocates for DOL's fiduciary rule argue that it is necessary to prevent bad actors from prioritizing their own interests above those of their clients. They argue that without it, consumers will be short-changed in their retirement savings by being steered into investments that don't work for them. On its face, a fiduciary standard is widely supported throughout the industry. The only issue is the best way to implement a standard. The problem with DOL's fiduciary rule is not the requirement to act in a client's best interest, but the dissuasion of commission-based accounts and the imposition of the Best Interest Contract (BIC) Exemption, which exposes financial advisors to the risk of litigious clientele.

Despite its length and complexity, the fiduciary rule can be broken down into two basic paths of compliance for advisors: 1) Moving to a primarily fee-based model or 2) Entering into the BIC with clients. The consequences resulting from each of these options are explored in detail below.

1. Moving to a primarily fee-based model

Created by the Employee Retirement Income Security Act of 1974 (ERISA), individual retirement accounts (IRAs) have become an integral part of Americans' retirement saving strategies. Based on data from the Internal Revenue Service (IRS), by the end of 2014, 57.3 million Americans owned at least one IRA, all totaling nearly $7.3 trillion in assets.

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[1] See, http://regrodeo.com/?year%5b0%5d=2016&regulation=Definition%20of%20the%20Term%20%E2%80%9CFiduciary%E2%80%9D;%20Conflict%20of%20Interest%20Rule--2016--31500000000

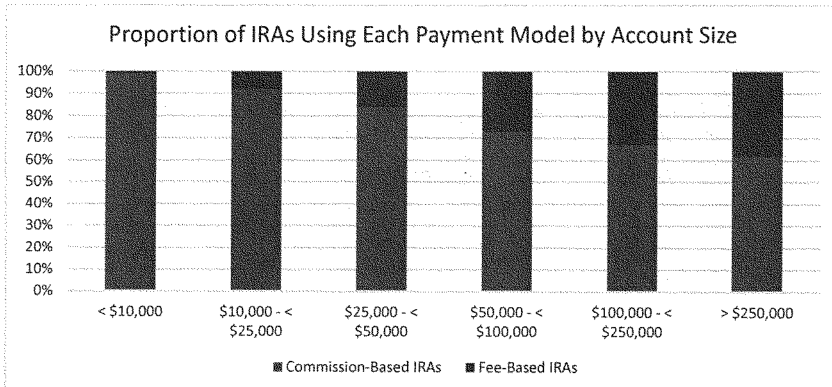
[2] https://www.americanactionforum.org/insight/fiduciary-rule-already-taken-toll-100-million-costs-fewer-options/

Table 1. Taxpayers with Individual Retirement Arrangement (IRA) Plans, by Filing Status and Gender, Tax Year 2014
(All figures are estimates based on samples--money amounts are in thousands of dollars)

Filing status and gender	Number of taxpayers			Taxpayers with IRA accounts reported on Form 5498 or Form 1099-R					
	Total	With pension coverage on Forms W-2 [1]	Eligible to make IRA contributions [2]	Roth conversions [3]		Withdrawals [4]		End-of-year fair market value of IRAs	
				Number of taxpayers	Amount	Number of taxpayers	Amount	Number of taxpayers	Amount
	(1)	(2)	(3)	(10)	(11)	(12)	(13)	(14)	(15)
All taxpayers	**202,530,196**	**71,427,452**	**155,481,150**	**488,827**	**8,255,152**	**17,985,606**	**275,107,505**	**57,279,386**	**7,291,587,418**
Men	98,259,891	36,501,418	79,643,021	272,918	5,326,927	8,939,710	167,122,701	28,146,406	4,483,874,245
Women	104,270,305	34,926,034	75,838,129	215,909	2,928,225	9,045,896	107,984,804	29,132,980	2,807,713,173
Taxpayers filing joint returns, total	**110,797,852**	**41,879,949**	**77,554,816**	**367,962**	**6,285,405**	**11,600,461**	**185,056,156**	**40,120,901**	**5,495,436,967**
Men	55,447,186	23,033,568	42,299,478	207,034	4,366,251	6,805,223	134,236,273	21,140,438	3,809,952,218
Women	55,350,666	18,846,381	35,255,338	160,928	1,919,154	4,795,238	50,819,883	18,980,463	1,685,484,749
Taxpayers filing non-joint returns, total	**91,732,345**	**29,547,502**	**77,926,336**	**120,865**	**1,969,747**	**6,385,145**	**90,051,348**	**17,158,485**	**1,796,150,451**
Men	42,812,705	13,467,850	37,343,544	65,884	960,676	2,134,487	32,886,428	7,005,968	673,922,027
Women	48,919,640	16,079,652	40,582,792	54,981	1,009,071	4,250,658	57,164,920	10,152,517	1,122,228,424

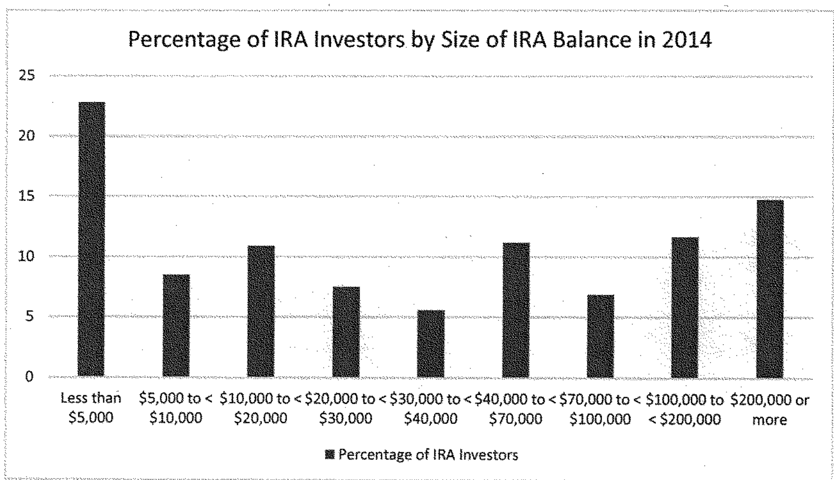
[1] Number of taxpayers with pension coverage is determined from Form W-2 box 13, which indicates participation in a retirement plan.
[2] Those individuals qualifying under Federal Income Tax law to make deductible or non-deductible contributions to a traditional IRA and/or Roth IRA plan.
[3] Owners of traditional IRAs were able to convert them to Roth IRAs as long as they met the income limitations for making Roth IRA contributions. Under certain circumstances, SEP or SIMPLE IRAs could also be converted to Roth IRAs; however, these amounts could not be identified separately for the purpose of these statistics.
[4] Withdrawals are reported on Form 1099-R; does not include withdrawals for the purpose of rollovers to other IRA accounts if the transfer was made by the trustee. Roth IRA conversions are shown separately.
For additional explanations, see Bryant, Victoria and Jon Gober, "Accumulation and Distribution of Individual Retirement Arrangements, 2010", SOI Bulletin, Fall 2013, Volume 33, Number 2.
Note: Details may not add to total due to rounding.
Source: Matched file of Forms 1040, 1099-R, and 5498 for Tax Year 2014.
IRS, Statistics of Income Division, Individual Retirement Arrangements Study, September 2016.

In 2011, a survey of 25.3 million IRA accounts[3] found that a large majority of IRA investors opted for a commission-based instead of a fee-based arrangement, and that those investors with lower IRA account balances opted for a commission-based arrangement at higher rates than those with higher account balances as seen in the chart below.[4]



[3] https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB32/oliverwymanreport.pdf
[4] Source, Oliver Wyman Study, 2011

In a 2014 study, the Investment Company Institute (ICI) found that nearly 23 percent of the 57.3 million Americans with IRAs have balances less than $5,000, over 42 percent have less than $20,000, and almost 74 percent have less than $100,000.[5]



All of this data is important in understanding the fiduciary rule's effects on consumers. The fiduciary rule will force many investment advisors to move away from a commission-based model to a fee-based model in order to avoid any possibility of an apparent conflict of interest. In fact, some firms have already announced[6] that they are doing away with their commission-based IRAs entirely. This presents two major problems for consumers. First, fee-based accounts are much more expensive for investors. As Morningstar explains[7], fee-based accounts yield upwards of 50 percent more revenue for firms than commission-based accounts because "[f]ee-based accounts are already under a fiduciary standard of care that is defined by the Securities Exchange Commission (SEC). This SEC fiduciary standard requires increased monitoring, legal liability, and typically is accompanied with a higher service level than commission-based accounts, so clients are charged more." By way of background, the reason DOL is involved in a developing a fiduciary standard is because of its oversight of ERISA and the retirement plans under it, which are the only ones covered by this rule.

One study found[8] that advisors earn 0.54 percent on commission-based accounts versus 1.18 percent on fee-based accounts. With nearly $7.3 trillion of assets in IRAs, that's a difference

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[5] Source: ICI's IRA Investor Database

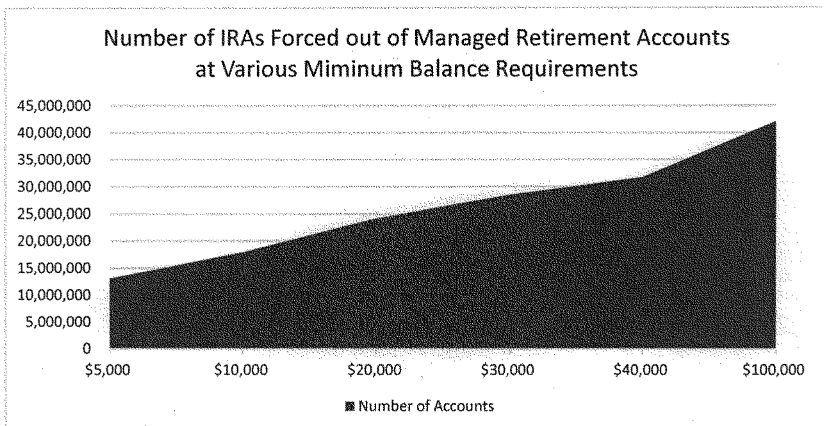
[6] https://www.ml.com/articles/delivering-a-higher-standard-of-care.html

[7] http://ibd.morningstar.com/article/article.asp?id=733096&CN=brf295,http://ibd.morningstar.com/archive/archive.asp?inputs=days=14;frmtId=12,%20brf295

[8] http://www.pricemetrix.com/cms/wp-content/uploads/PriceMetrix-Insights_Transitioning-To-Fee_English.pdf

between consumers paying a total of $39.4 billion or $86 billion in fees each year. This is an average of $813 per IRA account holder – an unaffordable amount for many.

The second major problem is that because fee-based accounts mean increased monitoring, liability, and servicing, advisors will be forced to require higher minimum balances in order to remain financially viable. For example, Edward Jones will require[9] investors to have $100,000 in retirement assets to open a fee-based IRA, whereas other firms will require[10] minimum balances of $20,000 or $30,000. Looking back at the third chart above, even with a minimum account balance requirement of $20,000, over 42 percent of IRA holders will be forced out of managed retirement accounts and almost half of all IRA holders will be forced out if that minimum is increased to $30,000. Even with a minimum balance requirement of just $5,000, over 13 million accounts will fail to qualify for managed advice.



In 2013, the Retail Distribution Review initiative (RDR) was implemented in the United Kingdom. It's not an exact match of DOL's fiduciary rule, in that it explicitly forbids commission-based accounts, but it is a close-enough comparison to merit attention. Since the RDR was implemented, several studies[11] have looked at its effects on investment advisors and their clients. Without getting bogged down in the details because it is, in fact, an imperfect comparison, I would be remiss to ignore them completely.

The UK's Financial Conduct Authority (FCA) conducted a review in 2016 of the changes in the retirement advice market as a result of the RDR. One of the more telling findings is that "over

[9] http://time.com/money/4459130/edward-jones-bans-funds-etfs-in-iras/
[10] https://www.merrilledge.com/pricing#tab3
[11] See, http://www.cass.city.ac.uk/__data/assets/pdf_file/0016/202336/The-impact-of-RDR-Cass-version.pdf and https://www.fca.org.uk/publication/corporate/famr-final-report.pdf and https://www.fsb.co.za/NewsLibrary/FSB%20Retail%20Distribution%20Review%20Status%20as%20at%20December%202016.pdf, for example.

the last two years, the proportion of firms who ask for a minimum portfolio of more than £100,000 has more than doubled, from around 13 percent in 2013 to 32 percent in 2015. The FCA's recent survey of advisors also supports this, suggesting that 45 percent of firms very rarely advise customers on retirement income options if those customers have small funds (i.e. less than £30,000) to invest."

Another review of the RDR's impact on the UK's financial advice market conducted by the Cass Business School at the City, University of London found that the enhanced requirements on advisors would drive advisors out of the investment advice market completely. "Advisor numbers fell from 40,000 at the end of 2011 to 31,000 by the start of 2013: we find that the remaining financial advisors are unduly optimistic about their own business prospects in the RDR world." Further, they found that "the average advisor expects to garner around £1,500 from each of roughly 150 clients to sustain the £220,000 of gross revenue that they tell us they require to function as a business. With fees averaging approximately 1 percent of assets under advisory this means that the average client will need to have around £150,000 in investible assets on average."

In sum, the fiduciary rule will force many IRA investors into fee-based accounts which, at a minimum, will noticeably increase the amount they pay their advisor each year, and, at a maximum, will cut them out of the investment advice market completely. Considering that the IRAs with the lowest account balances will be hit the hardest, it's reasonable to conclude that the fiduciary rule will do the most harm to those low- to middle-income retirement savers it was intended to protect.

2. Entering into the BIC with clients

The second option presented to investment advisors by the fiduciary rule is to enter into the BIC with their clients. Like the rule itself, on its face, the BIC sounds good – a best interest contract between advisor and advisee. But in reality, the BIC will open the door to excessive litigation, especially class action lawsuits. Specifically, the BIC exemption purports to[12] "allow entities such as registered investment advisors, broker-dealers, banks and insurance companies...and their employees, agents and representatives...that are ERISA or Code fiduciaries by reason of the provision of investment advice, to receive compensation that may otherwise give rise to prohibited transactions as a result of their advice to plan participants and beneficiaries, IRA owners and certain plan fiduciaries..."

In other words, the BIC exemption allows advisors to provide investment advice that may seem conflicted as long as they enter into a contract with their client stating that it is in the client's best interest, and, if the client decides that it's not, the client can sue them for breach of contract. And while it does allow for the inclusion of mandatory arbitration clauses, the BICs cannot waive the client's ability to file or participate in a class action lawsuit.

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[12] https://www.federalregister.gov/documents/2016/07/11/2016-16355/best-interest-contract-exemption-correction

In 2016 alone, consumers filed nearly 4000 arbitration cases[13] with the Financial Industry Regulatory Authority (FINRA) alleging some wrongdoing by broker-dealers. However, yet only 158 cases were decided in favor of the consumer. This means many broker-dealers spent significant time and money defending themselves, and perhaps unnecessarily. One could expect BIC litigation to fall along the same lines, but with the added threat of class action lawsuits and, at times, their resulting settlements.

One study estimated the costs[14] of class action lawsuits under the BIC using historical restitution data from wealth management firms, claims on implied errors and omissions insurance policies, DOL monetary estimates, and previous settlements on retirement plan class actions. It found that the long-term costs for class action lawsuits is between $70 million and $150 million each year – in addition to DOL's estimate of $1.5 billion in ongoing costs. The study also found that the near-term class action settlements could exceed the long-term estimates by a multiple "as firms try to figure out how to determine, demonstrate, and document best interest." Some strategic litigation could force targeted investment advisors into some extremely costly settlements – not as a result of their malpractice, but as a result of gray area in the law of the fiduciary rule and the BIC. The same study estimated that near-term class action settlements could decrease the operating margins on commission-based IRAs by 24 to 36 percent.

In an effort to curb potential litigation costs, investment advisors may purchase liability insurance. DOL's cost estimates[15] identify the increase in premiums at approximately 10 percent, or $300 per year, but independent studies estimate that number to be much higher. In an Oxford Economics study[16], researchers found that the potential cost of litigation stemming from the fiduciary rule was the greatest concern to investment advisors, largely because it is the area of the greatest unknown. Due to that uncertainly, the study does not give an exact estimate of the increase in the cost of insurance, but it does say, "importantly, from an economic perspective, the full cost of all this may be far larger than the ultimate amount spent on litigation – although that could end up being quite large as well. The cost of the uncertainty caused by the proposed rule could be far greater, as firms waste resources and forgo opportunities because of the risk of litigation…DOL assumes that Error and Omission insurance costs for some representatives will increase by 10 percent. This appears to be a wild underestimation of the potential costs of litigation, and the uncertainty it fosters as a result of the proposed rule."

Morningstar estimates that, in the short-term, class action settlements could double the costs of the fiduciary rule for firms.

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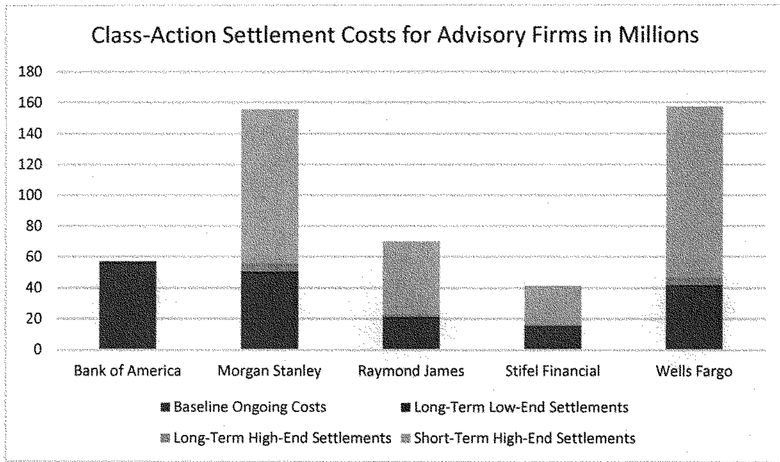
[13] https://www.finra.org/arbitration-and-mediation/dispute-resolution-statistics
[14] http://news.morningstar.com/articlenet/article.aspx?id=793268
[15] https://www.federalregister.gov/documents/2016/04/08/2016-07924/definition-of-the-term-fiduciary-conflict-of-interest-rule-retirement-investment-advice#h-10
[16] https://d2rpq8wtqka5kg.cloudfront.net/311980/open20150818044300.pdf?Expires=1491316097&Signature=eM4yKMJvLWy2Js24XLrWtFXiTWfuyaz2dI2dH7opibHCVrFh0V7Tv5fZrJrH48C1CYoqWgUf3eyLa0d7NKytou20LIpKe4stR-hasRYiNCrj5F5spBLqw-PpKdu-WGZwb38TLkT-~~YzE9-EtdqwTNkw11R1A7BVUyNkFAYsGmmVnOMYoXA0x~S86-6lyjPAHzo1HFetJV9CGNoC7FvZDnBGOVbMwtn6lQdQB9MIAYy7GrSDvg5K7-JMymZj1MzZR51vlcLcraAqtGuqkytFTqFKAjpbskpeEXnGuikBVp1cJ34geCQo9xWjbIs9tjpnRJ5ekRjYMcs68SsgMNsVRg&Key-Pair-Id=APKAJVGCNMR6FQV6VYIA



Conclusion

At the end of the day, the fact remains that the fiduciary rule is the most expensive regulatory action of 2016 and the second most expensive non-environmental rule since 2005. Even DOL's own conservative compliance cost estimate is astronomical.

Based on the above data, the fiduciary rule has the potential to increase consumer costs by $46.6 billion, or $816 annually per account, in addition to the $1500 in duplicative fees for retirement savers that have already paid a fee on their commission-based accounts that move the same investments into a fee-based account. Worse, based on a minimum balance requirement of $30,000, the fiduciary rule could force 28 million Americans out of managed retirement accounts completely. Add that to $150 million in annual litigation costs and operating margins reduced by 24 to 36 percent, which will ultimately be passed on to consumers, or will force firms out of the market, decreasing the supply of advice.

In short, the DOL's fiduciary rule will end up doing much more harm than good. Despite its good intentions, the costs it imposes – especially to low- and middle-income consumers – are far too high to justify implementing the rule as it is currently written.

Thank you, and I look forward to answering your questions.

FINANCIAL SERVICES INSTITUTE

VOICE OF INDEPENDENT FINANCIAL SERVICES FIRMS AND INDEPENDENT FINANCIAL ADVISORS

Testimony of
David Knoch, CIMA
President
1st Global
and
Member, Board of Directors
Financial Services Institute

Before the
United States House of Representatives Committee on Financial Services
Subcommittee on Capital Markets, Securities, and Investment

On

"Impact of the DOL Fiduciary Rule on the Capital Markets"

July 13, 2017

Introduction

Good morning, Chairman, Ranking Member and members of the Subcommittee. I am David Knoch, President of 1st Global based in Dallas, Texas. I am a Certified Investment Management Analyst® with nearly 20 years of experience in the financial services industry. 1st Global is the largest independently owned wealth management partner to nearly 400 Certified Public Accountant (CPA) and legal firms across the United States. The company was founded in 1992 by CPAs who believe that accounting, tax and estate planning firms are uniquely qualified to provide comprehensive wealth management services to their clients. 1st Global is a research and consulting partner that provides our affiliated financial advisors with the education, technology, business-building framework, and client solutions that make these firms leaders in their professions.

I am here representing the Financial Services Institute (FSI).[1] I first became involved with FSI in 2005, one year after it was initially founded in 2004, by Dale Brown, the CEO of FSI and Tony Batman, the founder, Chairman and CEO of our firm, 1st Global.

As President of 1st Global and a member of FSI's Executive Committee, I have seen the power of having a voice in Washington, as well as the need for being a pragmatic participant in important conversations impacting our industry. FSI is the only organization advocating solely on behalf of independent financial advisors[2] and independent financial services firms[3], representing the industry's interests before Congress, the SEC, FINRA, NASAA, other federal and state regulators, and, of recent note, the Department of Labor (DOL). FSI engages in the state and federal legislative and regulatory process, working to create a healthy and thoughtful regulatory environment for their members so they can provide affordable, objective advice to hardworking Americans. Since 2004, FSI has successfully promoted a more responsible regulatory environment through advocacy, education, and public awareness, including on key programs to improve financial literacy and prevent elder abuse in communities across the nation.

At 1st Global, our purpose is clear: 1st Global exists to enable intentional living.

We believe in the virtue of personal responsibility and that all Americans must be accountable for their actions and must intentionally take total responsibility for all of their

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[1] The Financial Services Institute is the only organization advocating solely on behalf of independent financial advisors and independent financial services firms. Since 2004, through advocacy, education and public awareness, FSI has successfully promoted a more responsible regulatory environment for more than 100 independent financial services firm members and their 160,000+ affiliated financial advisors – which comprise over 60% of all producing registered representatives. We effect change through involvement in FINRA governance as well as constructive engagement in the regulatory and legislative processes, working to create a healthier regulatory environment for our members so they can provide affordable, objective advice to hard-working Main Street Americans. For more information, please visit financialservices.org.

[2] The term "financial advisor" is used to denote registered representatives of broker-dealers, investment advisor representatives of investment advisors, and persons who are dually registered in both capacities.

[3] FSI firm members operate as broker-dealers subject to SEC, FINRA, and state oversight; and registered investment advisers under SEC or state authority.

decisions, the choices they make, the beliefs they carry, and what motivates them to live lives with dignity and humility.

We believe in free enterprise as one significant essence of liberty, and economic freedom is grounded in large part in the opportunities we pursue through our vocations. Creating and building businesses provides opportunities for us and others to pursue happiness and live dignified lives.

We believe in the virtue of moral courage and that we must always morally and courageously do only the right thing for ourselves and our clients, even if this means refusing what could be a lucrative financial opportunity. In addition, we must always boldly advocate for both the nobility of business enterprise and we must advocate for the protections of those who suffer injustice.

We believe that honoring promises is at the core of our successful business. Whether to our partner CPAs and advisors, their clients, or each other, we are dedicated to enabling all individuals to make and keep their important promises.

Lastly, we believe that independence and objectivity are the key to providing the right financial solutions that meet every client's unique financial needs and independent financial advisors are particularly well-situated to provide advice and services to hard-working Americans with a wide range of incomes and needs.

1st Global-affiliated advisors are knowledgeable and professional and, as CPAs, among the most trusted professions in America. In fact, according to a recent Gallup study, accountants are the eighth most trusted profession in America,[4] with 39 percent of respondents indicating that the honesty and ethical standards of individuals in this profession are "high" or "very high." Wealth management is a natural complement to the complex services and high practice standards of CPAs. As evidence of these high standards and "client first" principles of professional care, 93 percent of 1st Global-affiliated advisors are CPAs, Certified Financial Planner® (CFP) professionals, or Accredited Investment Fiduciaries, and as such are already today held to varying levels of fiduciary duty to their clients.

Our Regulatory Environment

Independent financial services firms such as 1st Global play a critical role in American lives. However, the future of the independent firm is in question due to persistently expansive new regulations, such as the DOL Rule, creating an overly complex and increasingly burdensome regulatory environment.

Furthermore, 1st Global-affiliated financial advisors are also unique in terms of the many layers of regulations to which they must comply in order to provide both tax and financial

[4] http://www.gallup.com/poll/187874/americans-faith-honesty-ethics-police-rebounds.aspx

planning services to their clients. As CPAs, our affiliated financial advisors are already subject to a separate and distinct duty to work in their clients' best interest as it relates to their accounting services, which include their wealth management and retirement planning practices.[5] In addition, our CPA financial advisors are also subject to the SEC standards and FINRA's standards of commercial honor and just and equitable principles of trade.

I believe strongly that the DOL Rule adds unnecessary complexity to an already complicated regulatory environment for broker-dealers, investment advisers, financial advisors, and, in the case of 1st Global, CPAs. The DOL Rule's intricate regulatory framework raises new barriers to the availability of professional investment services for millions of Americans. More importantly, the DOL Rule requires already confused investors[6] to understand several standards of care. In fact, the SEC's own study, performed in 2008 by the RAND Corporation, indicates that, "investors typically fail to distinguish broker-dealers and investment advisers along the lines that federal regulations define. Despite their confusion about titles and duties, investors express high levels of satisfaction with the services they receive from their own financial service providers."[7]

Furthermore, I believe that, whether through the DOL Rule's intent, or the prevailing public view of the standard of care to which financial advisors should be held, there is no way for anyone who provides a service to another, financial advisor or otherwise, to be "conflict free." It is an impossibility in all businesses. The purpose of business and commerce is to make people's lives better. Any business or person who is selfishly motivated only by profit will perish in a society of fierce market competition to make people's lives better at a fair value which implies a fair price for the services and goods rendered.

Conflicts of interest are inherent in democratic capitalism. Coupled with the temperance of a moral foundation, these conflicts of interest are what make America's commercial society function, make people's lives better, and has created widespread prosperity for employees, consumers, and producers for over 250 years. No alternate system has come close to improving the happiness of mankind as that of democratic capitalism. Every business and every consumer have something to sell or purchase, respectively, thus creating a conflict in each side attempting to maximize their own utility. The elimination of conflicts of interest effectively eliminates the frictional engine of all commerce and thus the engine that improves people's lives. A conflict is inherent in free market capitalistic societies in all services provided and all transactions rendered for profit. The paradox of conflicts of interest is essential to happiness for all. A society's moral foundation, its transparency of the market pricing mechanism, transparency of the inherent conflicts of both producers and consumers, and a fair system of justice can temper the occasional temptations of a few that may contemplate violating the happiness of others.

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[5] See the American Institute of CPAs (AICPA) code of professional conduct *available at* http://www.aicpa.org/Research/Standards/CodeofConduct/DownloadableDocuments/2014December15ContentAsof2016August31CodeofConduct.pdf.

[6] https://www.sec.gov/news/press/2008/2008-1_randiabdreport.pdf

[7] Ibid

In a recent *Wall Street Journal* article titled "Why Your Financial Adviser Can't Be Conflict Free," columnist Jason Zweig eloquently wrote, "All financial advisers—like all people who perform a service for anyone else, including journalists—have conflicts of interest. That's true regardless of whether they work for someone else or for themselves, whether they earn fees or commissions, or whether they call themselves 'fiduciaries' who put clients' interests ahead of their own." Neither the DOL's rulemaking, nor any bill proposed by Congress, should expect to eliminate conflicts which are inherent and unavoidable, nor should they propose excessive disclosure of conflicts, which will continue to add to the already problematic epidemic of clients ignoring the enormous volume of regulatory disclosures they are required to read. Instead, a more realistic approach is to require firms and financial advisors to effectively manage conflicts of interest to ensure that investors are aware they may exist and can choose whether to work with the financial advisor or not. Managing conflicts of interest can also assure that the financial advisor is not incentivized to work in their own interest. The more practical approach of managing conflicts of interest can be done in a way that does not diminish customer protection and still effectively protects investors from harm.

FSI supports the Draft Bill because it creates a uniform standard of care enforced by the SEC as the appropriate jurisdictional agency with the necessary expertise, and provides for reasonable and streamlined disclosures as a way to require industry participants to communicate their conflicts. In addition, 1st Global and firms like ours, are already subject to their direct oversight and examination. My testimony will first answer the several questions you asked and then focus on how the Draft Bill will achieve what I believe is the true intention of the DOL Rule, and allow for independent financial advisors to continue to provide advice and investment options that are tailored to their clients' needs, by establishing a simplified, uniform fiduciary standard in the correct agency.

Questions specifically asked by the subcommittee

In light of the partial implementation of the rule on June 9, 2017, please discuss the ability of financial advisers, including broker-dealers, to provide affordable and reliable investment advice to their customers.

The DOL Rule reached its initial implementation date on June 9, 2017, and is now part of the compliance responsibilities of financial services firms like 1st Global. Segments of the financial services industry have expressed concern that the DOL Rule, even with the recent partial implementation, will reduce the willingness and ability of financial advisors to provide affordable retirement advice to their clients, particularly those working with a broker-dealer affiliated advisor. In our view and experience, this concern has merit.

In many cases, the least expensive method for clients to hold mutual funds is to custody them directly with the originating mutual fund company (often referred to as "direct business," "direct-way business," or "retail direct.") Since the beginning of 2016, the number of accounts held by 1st Global clients directly with mutual funds companies has declined nearly 10 percent and the number of new accounts established dropped 19 percent during the first six months of 2017. We expect this trend to increase and by the end of this year anticipate that the total number of accounts held in these programs will drop 35 percent from 2016 levels. In contrast, we have seen a 123 percent increase in new accounts established using our "level-fee" [8] advisory programs since the beginning of the year. These are accounts offered through our Registered Investment Adviser (RIA), held to a fiduciary standard, supervised by the SEC, and expected to qualify for the level-fee exemption offered by the DOL Rule.

There are two key drivers behind this trend and both are derived from compliance with the DOL Rule. The first driver is our affiliated financial advisors moving the accounts to our fee-based advisory platform where the onerous requirements and legal risks of relying on the Best Interest Contract Exemption (BICE) are eliminated, and supervision of advice and aggregation of clients' assets is more manageable. The second is related to policy actions that 1st Global has enacted in response to both the DOL Rule and a need to modernize our firm.

The DOL Rule has also required us to adopt the "level-fee" fiduciary exemption for our discretionary retirement accounts. These are accounts where the financial advisor has contractual authority to purchase or sell securities in the account without prior notification to clients. While previously we charged reasonable transaction fees, we will be removing these fees and charging a reasonable base platform fee instead. While this will largely be a re-characterization of existing costs to clients, it will nevertheless raise the costs for the median client. Moving from a "pay for what you use" method to a "level-fee" method, in order to qualify for the level fee exemption offered as part of the BICE, as well as by the Impartial Conduct Standards applicable on June 9, will mean that those clients who place trades less frequently will subsidize frequent traders as all clients on the platform will be assessed the same "level fee."

Next, we have been particularly challenged to offer a viable solution for small employer retirement plans, particularly SIMPLE IRAs[9] where account balances can be quite small, as low as $50 for a newly established plan. Even with new "level fee" advisory programs created by 1st Global, we have been challenged to find a viable, cost-effective solution. As a result, many of our affiliated firms are exiting this marketplace and will no longer offer these plans to small business clients, and in some cases, will end their client relationship with existing plans. Since the beginning of 2016, we have seen the number of accounts in these programs decline by just over 20 percent and project that these accounts will shrink from the 2016 levels by 28 percent before the end of this year, and by 41 percent by the end of 2018. These changes will negatively impact small

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[8] A "level fee" is a fee or compensation provided to a financial advisor based on a fixed percentage of the value of the assets or a set fee that does not vary with the particular investment recommended. A level fee also does not include a commission or other transaction-based costs.

[9] Per the IRS, "A SIMPLE IRA plan (Savings Incentive Match PLan for Employees) allows employees and employers to contribute to traditional IRAs set up for employees. It is ideally suited as a start-up retirement savings plan for small employers not currently sponsoring a retirement plan." More information *available at* https://www.irs.gov/retirement-plans/plan-sponsor/simple-ira-plan.

businesses and their employees, who rely on these solutions to offer retirement benefits to their employees before they are large enough to consider the adoption of a 401(k) plan.

Additionally, we have seen our affiliated financial advisors increasing the minimum account size to serve clients and even ending relationships with clients whose accounts are not cost effective to continue to service. This is due in large measure to the increased paperwork and operating burden imposed by increasing regulation, as well as by the potential risks to their business posed through the utilization of the BIC, points I discuss in greater detail throughout this writing. Since the DOL Rule's announcement, our call center leaders estimate that inquiries on how to end relationships with clients have increased four-fold, a sentiment I hear expressed by my industry peers.

Finally, we have worked over the past few years to lower the costs of more expensive commissionable solutions by lobbying product manufacturers[10] to lower their costs, as well as decreasing ours. However, this change was not initially prompted by the DOL's rule-making, rather it was the result of a well-functioning, competitive marketplace, largely characterized by firms and financial advisors who do this work because they want to help people (first) and earn a reasonable living (second).

As you can see through these examples, there is merit to the argument that the cost of DOL Rule compliance is being borne in part, or in whole, by the consumer. These examples also highlight that client access to investment products, solutions, platforms, and methods of compensation are also being restricted and that this is particularly pronounced for clients with smaller accounts.

Finally, as a firm that has worked hard to be among the best in terms of preserving client choice, we believe strongly that as one expands their view of the market to include all financial services firms, particularly those like ours, the number, type, and impact of decisions such as those described above will grow substantially, as will the impact on smaller clients, typically not served by the RIA/fee-only marketplace.

Discuss the impact of the DOL's fiduciary rule once it becomes effective on Jan. 1, 2018, as it relates to the ability of broker-dealers to continue to provide retirement investment advice to low and middle-income investors.

While the DOL Rule has already gone into effect on June 9, 2017, the rule's full implementation has still yet to occur. On January 1, 2018, when the DOL Rule is fully applicable, the withdrawal from certain markets, products, and methods of compensation described above will be even greater than it is today.

In our view, the most problematic aspect of the full DOL Rule is the myriad documentary requirements it imposes. In fact, streamlining the documentary requirements is at the forefront of

[10] See https://financialadvisoriq.com/c/1457773/165863.

our recommendations, as detailed throughout this testimony, and one of the areas where we are in full support of the Draft Bill. These documentary requirements, in particular the utilization of the contract per the BICE, are at the forefront of an accelerated withdrawal by financial advisors across America from serving low- and middle-income investors, and they are at the forefront of the changes our firm has already seen. These documentary requirements lie at the heart of the debate about "can" vs "will." Yes, financial advisors can use the Prohibited Transaction Exemptions (PTEs) to continue to offer commissionable solutions to smaller account holders. But will they accept the financial and reputational risks of doing so? We believe, and have seen through our experience, that the answer is no.

Those who disagree would say that if financial advisors are doing nothing wrong, they have nothing to be afraid of, but that argument is overly simplistic and disconnected from reality. Before the DOL Rule became effective, clients did not need to suffer actual harm, receive poor or conflicted advice, or have a fraud committed against them to pursue legal recourse. And in fact, cases where no wrongdoing or negligence on the part of financial advisors are brought all the time and are often settled to avoid the exorbitant costs of defense. With class action lawsuits a possibility after January 1, a financial advisor no longer needs to have personally committed a fiduciary violation, they merely need to be part of a class where a fiduciary violation *may* have occurred or part of a class where attorneys, armed with the benefit of hindsight, opportunistically attack a marketplace. This will cause the legal and compliance costs of firms like ours and our associated financial advisors to increase, as well as our costs of insurance. In fact, while our Errors & Omissions (E&O) insurance carrier has not yet raised rates as they are waiting for claims to occur, we have felt compelled to raise our policy limits in anticipation of the DOL Rule, which increased our premiums by 7 percent, and was passed along to our affiliated firms despite no change in our pattern of claims, and despite making every effort to be compliant with the rule.

Next, we have also heard our associated financial advisors discuss retirement from the financial services industry and the sale of their practices should the rule's impact be too great. These are, more often than not, sole practitioner CPAs who offer both tax preparation and wealth management services to small business owners and individuals in small rural communities. Given the geographic dispersion of these firms, it may be hard for them to merge with other larger practices and maintain service to their clients. We expect to see an acceleration in these retirements or sales after the rule's final implementation date on January 1, should the rule be enacted as written. The result will be fewer choices of affordable financial advice in smaller communities across the country.

I can use our experience at 1st Global to put the impact of the DOL Rule in real terms. To date we have spent 35 percent of our profits on DOL Rule compliance, through both direct costs and increased payroll costs. In addition, we expect to incur future costs that will continue to erode these profits by over half the amount spent to date. So far, these costs have been borne by us and have not been passed along to clients or our affiliated financial advisors. However, this is likely to change as we are contemplating increased affiliation fees in the fourth quarter of this year to offset any ongoing costs of increased compliance. Additionally, should revenues decline as a result of the DOL Rule requirements, we would expect to increase these costs to offset some or all of these declines. An example of this is the restructuring of our pricing related to fee-based advisory accounts described earlier. The DOL Rule, as written, will no longer allow reasonable transaction-based costs in discretionary accounts, therefore we will apply a level, reasonable asset-based fee to investors in order to offset the elimination of these costs.

In addition to these metrics about our own costs of implementation, FSI engaged Oxford Economics in 2017 to conduct another study, "How the Fiduciary Rule Increases Costs and Decreases Choice" (2017 Oxford Economics Study) to update their economic analysis on the impact of the final Fiduciary Rule.[11] The findings of the 2017 Oxford Economics Study are based on the actual experience of FSI member firms implementing measures to comply with the DOL Rule, not assumptions or projections, which makes these figures far more reliable than the DOL's Regulatory Impact Analysis figures. This new report found that even Oxford's own 2015 predictions of the cost of the DOL Rule were significantly underestimated, as FSI members had already spent nearly half of the $400 million implementation cost the study predicted.[12] More specifically, the 2017 Oxford Economics Study found that FSI members have already spent $190 million preparing for DOL Rule implementation and will continue to spend an additional $205 million in preparation costs if the DOL Rule was to go into effect.[13] This means that start-up costs of the regulation are roughly 20 times higher than even the updated DOL Regulatory Impact Analysis estimated.[14] Whether because DOL's 2016 revisions to their 2015 proposed rules were not as effective at cost reduction as it thought, or because Oxford's original cost estimates were too low, the new estimates of total start-up costs are roughly 1.8 to 3.0 times higher than the DOL's most recent estimates.[15] If the FSI members' experiences were extrapolated to the universe of all broker-dealers, the total implementation costs to the industry will likely approach $1.8 billion.[16] Once implemented, these firms expect to pay an additional $230 million per year in recurring costs complying with the DOL requirements.[17] The DOL's revised Regulatory Impact Analysis did not provide a new detailed estimate of recurring costs, relying on the 2015 Regulatory Impact Analysis, while Oxford estimates the actual recurring costs to be 16.4 to 41.5 times higher than what the DOL has estimated.[18] Based on these results for startup and recurring

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[11] Oxford Economics 2017 Report, "How the Fiduciary Rule Increases Costs and Decreases Choice" (April 2017), *available at* http://www.financialservices.org/uploadedFiles/FSI/Advocacy_Action_Center/The_Fiduciary_Rule_Increases_Costs_And_Decreases_Choice.pdf.
[12] *Id.*
[13] *Id.*
[14] *Id.*
[15] *Id.*
[16] *Id.*
[17] *Id.*
[18] *Id.*

costs, Oxford calculated the total 10-year costs to the industry of the DOL Rule to be approximately $14.2 billion.[19]

Comparison of Cost Estimates

	Per-firm costs			Total BD industry costs
	Small BD	Medium BD	Large BD	
Industry size (DOL)	2,320	147	42	2,509
	Start-up costs			
DOL original estimates (Apr 2015)	$53,000	$145,000	$1,091,000	$190,097,000
DOL "high" estimates (Apr 2015)	$242,000	$663,000	$5,000,000	$868,901,000
OE/FSI 2015 report (Aug 2015)	$1,118,000	$3,350,000	$16,266,000	$3,769,382,000
DOL adjusted estimates (Apr 2016)	$556,301	$1,777,688	$7,366,036	$1,861,311,968
Current estimates (Apr 2017)	$911,000	$3,787,000	$13,105,000	$3,220,619,000
Ratio of current estimate to 2015 DOL estimate	17.2	26.1	12.0	16.9
Ratio of current estimate to 2016 DOL estimate	1.6	2.1	1.8	1.7
	Recurring costs			
DOL original estimates (Apr 2015)	$21,000	$58,000	$436,000	$75,558,000
DOL "high" estimates (Apr 2015)	$97,000	$265,000	$2,000,000	$347,995,000
DOL adjusted estimates (Apr 2016)				$413,000,000
Current estimates (Apr 2017)	$344,000	$2,407,000	$7,375,000	$1,461,659,000
Ratio of current estimate to 2015 DOL estimate	16.4	41.5	16.9	19.3
Ratio of current estimate to 2016 DOL estimate				3.5

Source: Oxford Economics and DOL Regulatory Impact Analyses

Additionally, FSI's research indicates that there will also be other consequences of rising compliance and other costs. FSI members widely report that one consequence of the DOL Rule is that the economics of managing small accounts will cause these investors to lose access to retirement planning services and investment education, a concern I expressed as it relates to our firm above. The reality is that for many small accounts, the fixed cost of servicing the account will exceed revenue that will be earned. As a result, most FSI member firms indicate that smaller investors will be offered robo-investing type account services or be asked to move their accounts. These small (often entry level, novice investors) would lose access to the personalized retirement planning services to which they have become accustomed. This area of the market is already underserved when it comes to receiving professional financial advice. Only 32 percent of adults in the U.S. receive professional financial advice[20] and only 8 percent of financial advisors focus on targeting and serving American households with less than $100,000 in investable assets.[21] Roughly 71 percent of American households (89.6 million) have less than $100,000 in investable assets.[22] Financial advisors play a critical role in the retirement investing process by counteracting one of the challenges to investors achieving this goal – their own behavior. A 20-year analysis

[19] *Id.*
[20] Northwestern Mutual 2016 Planning & Progress Study *available at* https://www.northwesternmutual.com/about-us/studies/planning-and-progress-study-2016.
[21] Id.
[22] Id.

from DALBAR showed that voluntary investor behavior – actions such as panic selling, excessively exuberant buying, and attempts at market timing – was the single-largest contributor to long-term underperformance.[23]

While the definition of a small investor varies among our member firms, they generally estimate that the breakeven point for servicing a client's investment account ranges from $35,000 to $75,000 in assets.[24] Since the median IRA balance ranged from $23,785 to $33,185 between 2010 and 2014, it is clear that without significant changes the DOL Rule will have a devastating impact on investor access to retirement planning services.[25]

Figure 3
Average and Median IRA Balances, by IRA Type, Age, and Gender, 2010–2014

	Average					Median				
	2010	2011	2012	2013	2014	2010	2011	2012	2013	2014
All	$91,864	$87,668	$105,001	$119,804	$127,583	$25,296	$23,785	$27,987	$32,179	$33,185
Type										
Traditional-Conts.^	88,403	78,051	97,286	112,943	120,163	29,756	24,721	32,161	37,611	39,389
Roth	24,798	25,741	31,288	37,010	39,544	11,471	11,344	12,796	15,190	15,847
Traditional-Rlvrs^	123,426	110,918	134,354	150,261	157,277	38,138	31,944	39,172	43,535	43,598
SEP/SIMPLE	55,733	56,479	67,457	79,424	84,599	15,471	15,711	17,794	20,257	20,604
All Traditional	103,346	98,797	118,645	134,791	142,780	32,647	28,457	35,803	40,996	42,157
Unknown	96,441	83,062	60,212	66,950	70,508	18,815	21,982	6,443	6,318	6,241
Age										
Under 25	21,986	11,434	11,165	13,103	13,264	5,782	3,238	3,360	3,708	3,433
25–29	10,290	12,278	11,009	12,537	12,552	4,769	4,488	4,721	5,000	4,826
30–34	16,236	18,106	17,704	20,456	21,120	7,229	6,612	7,036	7,661	7,531
35–39	25,683	27,664	29,202	33,784	34,903	10,819	10,072	11,003	12,325	12,138
40–44	36,968	38,354	42,826	49,948	52,582	14,745	13,751	15,770	17,745	17,864
45–49	50,998	51,006	59,471	68,683	72,177	19,329	18,312	21,463	24,264	24,564
50–54	74,046	66,771	80,525	91,976	96,726	24,505	23,216	28,056	31,692	32,639
55–59	92,196	86,572	108,074	122,957	130,459	31,762	29,080	36,363	41,149	42,950
60–64	129,976	116,415	147,739	165,139	175,418	42,998	38,838	49,899	55,807	59,138
65–69	170,672	145,575	191,208	212,812	224,144	58,965	50,122	66,852	75,277	79,928
70 or older	162,857	144,252	192,961	219,790	232,389	56,198	49,994	65,419	75,627	80,500
Unknown	108,765	280,290	160,233	126,759	177,699	35,255	116,475	43,666	45,801	44,692
Gender										
Female	71,112	66,529	81,700	96,339	94,774	23,246	21,642	27,826	30,660	29,651
Male	128,719	114,745	139,467	160,589	153,649	32,752	30,704	40,103	43,449	41,057
Unknown	85,037	76,604	85,230	91,853	128,631	22,820	19,916	26,589	23,576	30,923

Source: EBRI IRA Database.
^ Traditional-Conts.=Traditional-Originating from Contributions, Traditional-Rlvr=Traditional-Originating from Rollovers. Both of these accounts could have received contributions or rollovers after their origination, so these are NOT proxies for employment-based dollars versus IRA only dollars. The Traditional-Originating from Rollovers do provide an estimate of the dollars that have been moved into a new IRA.

Source EBRI.org "Individual Retirement Account Balances, Contributions, Withdrawals, and Asset Allocation Longitudinal Results 2010-2014: The EBRI IRA Database" (January 17, 2017).

<u>What additional interim actions should the DOL adopt as it continues to review the rule's implementation as part of its Request for Information?</u>

The most meaningful interim action the DOL should take is to immediately delay the DOL Rule's final applicability date until April 10, 2019. This will allow one of three major actions to be undertaken. First, it would allow the DOL an appropriate amount of time to fully review and

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[23] 20th Annual Quantitative Analysis of Investor Behavior, DALBAR (April 2016) *available at* http://kyestates.com/wp-content/uploads/2015/02/DALBAR-QAIB-2014.pdf.
[24] Id.
[25] "Individual Retirement Account Balances, Contributions, Withdrawals, and Asset Allocation Longitudinal Results 2010-2014: The EBRI IRA Database" (January 17, 2017) *available at* https://www.ebri.org/pdf/briefspdf/EBRI_IB_429_IRA-Long.17Jan17.pdf.

consider the industry's input and make meaningful and necessary modifications. Second, it would allow Congress to fully analyze and adopt meaningful, comprehensive measures such as The Draft Bill. Third, should it be necessary, it would allow the industry additional time to implement sales and operating practices that incorporate industrywide changes being contemplated in response to the DOL Rule.

Furthermore, while a clear and substantial delay is an appropriate interim action, it also does not address our overarching concerns with the DOL Rule. To that end, we make three recommendations. First, and most importantly, is the implementation of a uniform fiduciary standard of care by the SEC, as recommended by the Draft Bill. Second, if this outcome should fail to be achieved, it is our recommendation that the DOL discontinue all further implementation of the rule, leaving in place the existing implementation requirements that became effective June 9. Third, failing both these outcomes we offer the following recommendations, taken from our response to the DOL's Request for Information:

1. Streamline BICE documentation and disclosure.
2. Create a single best interest standard applicable to all investors.
3. Revise and broaden the reasonable compensation rules.
4. Revise the rules for IRA rollovers.
5. Expand the rule's grandfathering provisions.

Please provide an overview of how the SEC is better equipped to update the standard of care for broker-dealers.

FSI has long supported a uniform fiduciary standard of care applicable to all professionals providing professional investment advice to retail clients.[26] This uniform standard of care would require financial advisors to act in the best interest of their clients, consistent with the intent of the Draft Bill.

While broker-dealers are already subject to a robust regulatory and enforcement regime designed to protect investors, FSI recognizes that multiple and differing standards of care between retirement versus non-retirement investments and transaction-based versus advisory-fee based advice leads to several negative unintended consequences for the client. These include but are not limited to overly complex disclosures, increased costs, limitations of investment choices, and reduced access to professional financial planning services.

As such, FSI supports the creation of a uniform fiduciary standard of care that would be applicable to all financial advisors regarding all investment products, not just tax-deferred retirement savings. FSI is uniquely situated to provide input on such a standard because its

[26] See, e.g., Letter from David T. Bellaire, Executive Vice President & General Counsel, Financial Services Institute, to Elizabeth M. Murphy, Secretary, U.S. Securities and Exchange Commission (Jul. 5, 2013) (commenting on Duties of Brokers, Dealers, and Investment Advisors, Release No. 34-69013; IA-3558; File No. 4-606), *available at* https://www.sec.gov/comments/4-606/4606-3138.pdf.

members, including 1st Global, are either dually-registered firms, or own separately registered BDs and RIAs (as we do), that provide both brokerage (commission-based) and advisory (fee-based) services to all types of American investors.

The SEC has clear statutory authority to regulate all financial advisors and securities products and has done so since it was established by Congress in 1934 for the sole purpose of regulating the commerce in investment products. The SEC Office of Compliance Inspections and Examinations (OCIE) has designed existing examination and enforcement protocols and trained staff to perform these functions. The SEC divisions such as enforcement, corporate finance, investment management, trading and markets as well economic and risk analysis all work to regulate and enforce U.S securities regulations for the purpose of investor protection.

The DOL lacks the expertise to effectively develop, implement, and regulate the standard of care afforded to the investing public. The DOL expertise lies in the development and implementation of regulations pertaining to wage earners, employment discrimination, employer-sponsored retirement accounts, workers compensation, and other legal and regulatory aspects pertaining to employment. Therefore, it is FSI's firm belief, and I fervently agree, that the SEC is the most appropriate governmental agency to regulate the standard of care afforded to the investing public.

This Draft Bill achieves this necessary uniform standard of care by establishing the standard of conduct for broker-dealers and their registered persons when providing recommendations to a retail customer. The recommendation must be in the customer's best interest and reflect reasonable diligence, care, skill, and prudence. The Draft Bill also empowers the SEC to issue additional regulations with regard to the standard of care. The SEC has unique expertise in regulation of broker-dealers and investment advisers as evidenced by numerous studies the SEC has conducted as required by Congress since its inception and, unlike the DOL, has the ability and authority to examine for compliance with the standard and bring corrective actions when necessary. By establishing this standard for broker-dealers, investors will no longer have to wonder what the difference is between various financial professionals and what duty of care their financial advisors owes to them.

What steps could the SEC take as part of its June 1, 2017 request for public comment on standards of conduct for investment advisers and broker-dealers?

FSI is still in the process of developing comments to the SEC in response to their request. Once the comments are complete, FSI will provide a copy to the Committee.

Comment on the discussion draft to create a best-interest standard for broker-dealers

In addition to the commentary already provided in support of the Draft Bill, I offer the following additional comments.

Meaningful Disclosures

The DOL rule creates a significant volume of disclosure that are cumbersome and expensive to create, will confuse investors with their sheer volume and complexity, and because of the private right of action created by the DOL Rule, could create immeasurable legal liability. Today, in our entry-level investment advisory programs for a fiduciary account with a minimum asset size of $5,000, the paperwork bundle that the client is required to sign is 191 pages in length. Of these 191 pages, 149 are disclosure, including the delivery of Form ADV and its required inclusions. This means that 78 percent of the paperwork a client signs in our "entry level" investment advisory program is disclosure. If you add the prospectus delivery requirement to the count, a client receives 503 pages of paperwork, totaling 461 pages of disclosure, or 92 percent of the paperwork. Additionally, after the January 1 applicability date, for a small commission-based account, which can be opened with as little as $50 initial investment utilizing the Best Interest Contract Exemption, we expect the number of pages of paperwork to be 98 pages, with 70 of those pages being disclosure. When prospectus delivery is added, the number swells to 117 of the 145 total pages, or 81 percent of the total paperwork burden imposed on clients.

The DOL itself acknowledged in their Regulatory Impact Analysis that disclosures are ineffective by stating, "Disclosure alone has proven ineffective to mitigate conflicts in advice. Extensive research has demonstrated that most investors have little understanding of their advisers' conflicts of interest, and little awareness of what they are paying via indirect channels for the conflicted advice. Even if they understand the scope of the advisers' conflicts, many consumers are not financial experts and therefore, cannot distinguish good advice or investments from bad. The same gap in expertise that makes investment advice necessary and important frequently also prevents investors from recognizing bad advice or understanding advisers' disclosures. Indeed, some research suggests that even if disclosure about conflicts could be made simple and clear, it could be ineffective – or even harmful."[27]

Furthermore, the DOL Rule's website and transaction level disclosure obligations are particularly burdensome and do not provide investors the type of information that they actually want, such as the fees they are paying and what they are receiving for those fees. Investors want and need relevant disclosures in a simplified way they can understand. The complicated and comprehensive nature of the DOL Rule disclosures makes it highly unlikely that they will be effective in achieving the DOL's goal of transparency and usability for investors. Investors do not need or want these voluminous and duplicative disclosures, and will not read, refer to, or rely on them. Especially when they drive up their investment costs and limit their access to solutions.The cost of complying with the heavy disclosure requirements vastly outweighs any marginal usefulness of them for the investor.

[27] See page 9 of the Regulatory Impact Analysis *available at* https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/completed-rulemaking/1210-AB32-2/conflict-of-interest-ria.pdf.

Additionally, as FSI firms, including 1st Global, have worked in the months since the DOL Rule was released to try to scope and begin building technological systems to comply with the transaction-level disclosures, it has become apparent that industry-wide changes must be considered, reviewed, structured, and implemented. This would necessitate considerable time and expense that are unrealistic with a January 1, 2018 implementation date. Further, these complex requirements make it possible, or even likely, that firms operating in good faith will make unintentional errors in their disclosures, which could further confuse clients and potentially have significant financial consequences for firms. For business leaders who partner with the owners and leaders of other businesses, the act of investing large sums of money and employee time into a likely source of increased liability and risk does not make business sense. Add in the likelihood for client frustration and you've got an excellent example of regulatory overreach.

In contrast, this Draft Bill includes a disclosure requirement at the outset of the account relationship, when the information is the most relevant, and provides a workable format: a clear and concise disclosure with a description of the type and scope of services to be provided, the standard of conduct applicable to the relationship, the types of compensation that may be charged, and any material conflicts of interest. It also allows the SEC to require disclosure of fees received by the broker-dealer prior to the transaction. The Draft Bill allows the SEC to establish the timing and content of the disclosures, which is appropriate given that the SEC has expertise and knowledge about how financial advisors work with investors.

Furthermore, the Draft Bill does not proscribe the medium for disclosure as the DOL Rule does. The provisions of the Draft Bill would allow firms the flexibility to deliver the disclosure in ways the investor wants to receive it, such as in writing, electronically, or both.

Additionally, the North American Securities Administrators Association (NASAA) has recently established a voluntary model fee disclosure template which also offers a concise and cogent summary of account expenses. This template serves as a model for disclosing relevant information to investors via the Internet. In fact, 1st Global was one of the first firms to voluntarily adopt the template on our website as we felt the information it contained was useful to investors and the format of the template is easy to read and understand.[28] Finally, the Form ADV disclosure already used by investment advisers provides useful information for client disclosure in this context.

Again, the SEC has jurisdiction over both investment advisors and broker-dealers and will have actual ability and expertise to examine for compliance with disclosure requirements and take corrective action where necessary. The common-sense disclosure requirements of the Draft Bill along with other already-available options will provide investors with the information they need to make intelligent decisions without confusion or information overload.

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[28] NASAA model template information *available at*: http://www.nasaa.org/industry-resources/broker-dealers/model-fee-disclosure-resource-center/. 1st Global fee template *available at*: http://www.1stglobal.com/downloads/acctfees2.pdf.

Material Conflicts of Interest

The DOL Rule requires firms and financial advisors to avoid conflicts of interest or avail themselves to one of the PTEs and in any case, provide advice "without regard to the financial interest of the adviser."

As FSI member firms, including 1st Global, have worked in the months since the DOL Rule was promulgated to try to comply with the vague standard of "reasonable compensation" and "eliminating" conflicts of interest, it has become apparent that industry-wide changes must be considered, reviewed, structured and implemented. Although the industry has worked diligently to consider how to implement these changes, more time is required for all parties in the product manufacturing and distribution chain to implement all the necessary adjustments.

Some FSI member firms may choose to address the compensation and conflicts of interest challenges by becoming level fee fiduciaries. As stated earlier, "level fee" is a fee or compensation provided to a financial advisor based on a fixed percentage of the value of the assets or a set fee that does not vary with the particular investment recommended. A level fee also does not include a commission or other transaction-based costs. The DOL has indicated that such an approach may be a powerful means of reducing conflicts of interest with respect to mutual fund recommendations and correspondingly reduce the need for heightened surveillance around conflicts of interest. Broadening the availability of this option may be beneficial to FSI member firms that would like to offer institutional share classes (also known as "clean shares") and reduce their regulatory burden given this payment structure is likely to meet the current definition of "level fee." However, the success of this approach depends upon the availability of appropriate investment products. There has been considerable public comment from DOL about the development and availability of "clean shares" as a primary means of creating a levelized compensation structure for sales of mutual funds, but it does not appear these shares can be made fully operational for at least 18 months, if not more.

As mutual fund, insurance, and other companies develop new share classes or other pricing options, clearing, as well as introducing firms such as 1st Global must wait to develop the necessary trading, surveillance, commission, and other systems to support their use. Once these products and resulting systems are finalized and implemented, firms will need to not only train their staff on the particulars of the products and how to supervise them but will also need to train financial advisors as well. The result is a sequential process of systems development that simply cannot be completed by the January 1, 2018 deadline.

This Draft Bill takes a more practical and reasonable approach, requiring firms and their registered persons to "avoid, disclose, or otherwise reasonably manage" material conflicts of interest that may influence a financial advisor to make recommendations in their own interest instead of the best interests of their clients. The Draft Bill specifically states that transaction-based compensation, proprietary products, and principal transactions are not per se violations of the best interest standard nor does the standard does require advisors to recommend the least expensive product. The least expensive product is not automatically the best product for every customer. Advisors take into account a wide range of factors when making a recommendation and the least expensive product may not have important features a more costly product can provide.

Instead, the Draft Bill recognizes that it is essential to continue to allow investors to have several options for ways in which they can work with a financial professional and the means by which they choose to protect themselves and their families and plan for their future. In fact, it was Congress' expressed intent in section 913 of the Dodd-Frank Act that any uniform standard developed by the SEC should be reflective of various business models.[29] By providing for commissions and acknowledging that the lowest cost option is not always the best option, this Draft Bill avoids preferential treatment of one business model over another and recognizes that commissions and sales charges are acceptable ways to compensate investment professionals and even preferable to many investors.

Most importantly, the Draft Bill clearly recognizes the value of advice. The language of the Draft Bill acknowledges the reality that investors need and flexibility in the means by which they have access to financial advice.

Conclusion

While the DOL no doubt had good intentions when it developed their fiduciary standard and requirements, the unintended consequences that many in the financial services industry have continued to raise are without a doubt already coming to fruition. I wish to emphasize that my concern and the concerns of FSI are not that the DOL Rule expands the ways in which we are held to a fiduciary standard of care. Both FSI and I agree that a carefully-crafted, uniform fiduciary standard of care would be beneficial for investors and reduce regulatory confusion. We believe, however, that this standard of care should be created and overseen by the SEC, which is what this Draft Bill accomplishes. We also believe that investors need and deserve clear and concise disclosures that provide them with useful information in an easy-to-read format of their choice. Again, the DOL Rule fails on this point while the Draft Bill accomplishes helpful disclosures for investors.

Furthermore, we strongly believe that all investors must retain access to valuable advice in order to provide them the means and resources to plan for a dignified retirement. The DOL Rule's focus on eliminating conflict and reducing fees is miscalculated, misdirected, and misapplied. The result is that it threatens investor access to advice by creating favored means of working with an advisor.

This Draft Bill makes the important distinction between low cost advice and valuable advice. The value of working with a financial advisor goes well beyond fees. A 2016 study conducted by Vanguard determined that the value of a financial advisor to a client is worth up to

[29] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 913, 124 Stat. 1376 (2010).

2.95 percent, net of fees, if the advisor focuses on relationship-oriented services — such as providing cogent wealth management via financial planning, discipline and guidance — rather than by trying to outperform the market.[30] Investors who have access to and receive financial advice enjoy both tangible and intangible benefits that cannot be expressed in dollar terms.

This Draft Bill will allow the financial advisors 1st Global serves, who are already heavily regulated and, because of their high ethical standards, already working in their clients' interests, regardless of the regulatory framework they operate under, to focus on the investor rather than unnecessary and cumbersome regulatory requirements.

Finally, my testimony would not be incomplete without dedicating at least one paragraph to defend the honor of the CPA wealth management firms I have the privilege to work with daily. This DOL Rule has been hard on them, not just for the compliance burden which has been discussed here at length, but because their good work and honor has been needlessly attacked. I work with nearly 1,000 professionals, as well as 200 employees in our home office, who show up every day to serve their clients and their communities, and make their world just a little bit better each day. Every CPA financial advisor I have ever spoken with is called to service for two reasons: they enjoy solving complex problems and they enjoy doing good for others, and offering wealth management services to their clients lies at the intersection of this calling. Without eschewing the need for reasonable regulation, what I see are people who do what is right for their clients, not because of a regulatory requirement or a published standard of care, but because it is merely the right thing to do. It is a dishonor to the vast majority of our marketplace who are called first to serve their communities, and happen merely to earn a living for doing so, to accuse them of putting selfish interests first. It is simply not what I see. What I see is the business owner who has worked her entire life to grow a business and is now graced with the sale of it, and has no idea what do with the proceeds so that she can honor the promises she has made. What I see is the family member suffering from cancer who can focus on his recovery because his financial affairs are completely and fully in order. What I see is the widow who relies on her financial advisor to transition to life without her spouse. What I see is the person entering retirement who can enjoy the fruits of their hard work, because they have an advisor who helped them plan and save, and who now guides them on living a dignified life, sustained by the power of choice. Where the authors of the DOL Rule see the financial services industry as populated with shadowy characters out for themselves, I see nothing but genuine concern and valuable expertise when I work with our financial advisors. My wish for you is to see what I see and help independent financial advisors like ours across America serve more clients, serve them better, and serve them more completely by reducing their regulatory burden without reducing the standard of care.

I thank the Chairman, Ranking Member, and the rest of the Subcommittee for allowing me to share my thoughts on the major challenges and unintended consequences of the DOL rule and the ways in which this Draft Bill provides the same investor protections while applying practical,

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[30] Putting value on your value: Quantifying Vanguard Advisor's Alpha®, September 2016 *available at* https://www.vanguard.com/pdf/ISGQVAA.pdf.

common-sense requirements that will ensure that Americans can continue to receive professional financial advice while they work toward a dignified retirement.

sifma®

Invested in America

Written Testimony of Jerry Lombard, the President of the Private Client Group at Janney Montgomery Scott, LLC

On behalf of the Securities Industry and Financial Markets Association

before the U.S. House of Representatives

Committee on Financial Services

Subcommittee on Capital Markets, Securities, and Investment

Hearing entitled "Impact of DOL Fiduciary Rule on the Capital Markets"

July 13, 2017

Chairman Huizenga, Ranking Member Maloney, and distinguished members of the Subcommittee, I am Jerry Lombard, the President of the Private Client Group at Janney Montgomery Scott, LLC. I greatly appreciate the opportunity to testify today on behalf of the Securities Industry and Financial Markets Association (SIFMA)[1] and share our perspective on the best path forward to establish a best interest standard for the broker dealer industry. SIFMA represents the broker dealers, banks and asset managers who play an active role in the capital markets and are dedicated to promoting investor opportunity, access to capital, and an efficient market system that stimulates economic growth and job creation. We are grateful for this Committee's willingness to consider legislation that would allow the Securities and Exchange Commission (SEC) to establish a best interest standard for broker dealers that would create a high standard of care for retail customers across all accounts.

On June 9, 2017, some key provisions in the Department of Labor (DOL) fiduciary rule became applicable, and as an industry we are beginning to see its harmful impact on America's retirement savers - limiting product choice and access to advice, while raising costs. At Janney, we are already experiencing many of these issues. Our customers and advisors are very confused by the phalanx of new DOL rules applying to retirement plans. They do not understand why there are now two sets of rules one for retirement accounts and one for taxable brokerage accounts. Since June 9th customers are restricted from making certain investments. Upwards of 10,000 of our customer retirement accounts will be relegated to a "no advice service" desk –as they are too small for the risks imposed by the DOL or too costly to place in an advisory account that would remove the supposed conflicts the DOL is trying to regulate. How switching small retirement savers from a full-service advisor to a "no advice" service desk is in their best interest, I will never understand.

It is the position of SIFMA that the right answer for investors is a consistent best interest standard that could apply across all types of accounts, but does not have the additional onerous conditions created by the DOL rule. A best interest standard done right by the SEC, the expert agency responsible for broker dealer standards of conduct, would provide protection for retail customers without a bifurcated compliance regime imposed on the same market participants by different regulators.

We are greatly encouraged by the SEC's June 1st request for public comment on standards of conduct for investment advisers and broker dealers. It is SIFMA's intention to share with the SEC our desire that they consider establishing a best interest standard for broker dealers that mirrors the elements of the Impartial Conduct Standard under the DOL Rule, but unlike the DOL Rule, would apply across all broker dealer accounts, not just retirement accounts. For that reason, the DOL should at a minimum delay the January 2018 applicability date to allow the SEC to lead the effort to put in place a standard that works for all accounts.

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[1] "SIFMA is the voice of the U.S. securities industry. We represent the broker-dealers, banks and asset managers whose nearly 1 million employees provide access to the capital markets, raising over $2.5 trillion for businesses and municipalities in the U.S., serving clients with over $18.5 trillion in assets and managing more than $67 trillion in assets for individual and institutional clients including mutual funds and retirement plans. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit http://www.sifma.org."

Congresswoman Wagner's legislative draft provides this path forward by establishing a SEC applied principles-based standard to ensure that all broker dealer recommendations about securities are driven by the best interest of the retail customer. Specifically, the Suitability Rule would be amended to provide that when making a 'recommendation' to a 'retail customer' a broker dealer shall act in the best interest of such customer at the time the recommendation is made. Further, the recommendation shall reflect the 'reasonable diligence' and the reasonable care, skill, and prudence that a registered representative would exercise based on the 'customer's investment profile.'

We firmly believe that Congresswoman Wagner's approach could provide a number of significant regulatory efficiency and investor protection benefits which would:

- enhance the existing suitability obligation under FINRA rules, building upon them to create a heightened and more stringent best interest standard of conduct for the benefit of retail customers;

- apply across all securities recommendations made to retail customers in all broker dealer accounts (not just limited to IRA accounts);

- build upon, and fit seamlessly within, the existing and long-standing securities regulatory regime for broker dealers, coupled with robust examination, oversight, and enforcement by the SEC, FINRA and state securities regulators; and

- be akin to, and well aligned with, the Investment Advisor standard under the Advisers Act insofar as the new standard would include a duty of loyalty and a duty of care, and an obligation to manage investment costs, and would require up-front disclosure to the customer of important information.

Thus, we greatly appreciate Congresswoman Wagner's work on this legislative discussion draft, and we look forward to continuing to work with her and this Committee on language that ensures the best interest standard established in the bill operates in harmony and consistency with all existing standards of conduct, including the current broker dealer, Investment Advisor, and DOL Rule regulatory frameworks, as well as any future rulemaking by the SEC or FINRA.

In doing this, we will help relieve America's retirement savers from the burdens that have arisen as a consequence of the DOL's misguided rule.

Thank you.

CHAMBER OF COMMERCE
OF THE
UNITED STATES OF AMERICA

NEIL L. BRADLEY
SENIOR VICE PRESIDENT &
CHIEF POLICY OFFICER

1615 H STREET, NW
WASHINGTON, DC 20062
(202) 463-5310

July 12, 2017

The Honorable Bill Huizenga
Chairman
Subcommittee on Capital Markets,
Securities and Investment
Committee on Financial Services
U.S. House of Representatives
Washington, D.C. 20515

The Honorable Carolyn B. Maloney
Ranking Member
Subcommittee on Capital Markets,
Securities and Investment
Committee on Financial Services
U.S. House of Representatives
Washington, D.C. 20515

Dear Chairman Huizenga and Ranking Member Maloney:

The U.S. Chamber of Commerce remains seriously concerned about the impact of the Department of Labor's (DOL) misguided "fiduciary duty" rule, and welcomes the hearing by the Subcommittee on Capital Markets, Securities, and Investment entitled "Impact of the DOL Fiduciary Duty Rule on Capital Markets."

The fiduciary rule is hampering the ability of low and moderate income earners to save, and restricting the ability of small businesses to provide employees with retirement savings options.

In May, the Chamber released a report, *The Data Is In: The Fiduciary Rule Will Harm Small Retirement Savers*, which demonstrates the rising costs and limited choices the fiduciary rule is imposing on American workers. A survey by *Investment News* found that 35% of advisers will no longer serve accounts under $25,000 because of the rule, a large mutual fund provider reported that the number of abandoned or "orphaned" accounts has nearly doubled in the first quarter of 2017 and 70% of insurance service providers report that they have exited or are considering exiting the market for small balance individual retirement accounts (IRAs). These are real life consequences of a rule built on a faulty premise and inadequate analysis.

We hope that this hearing will illustrate some of the challenges the fiduciary rule has imposed on American workers, businesses and capital markets.

The Chamber also believes that the draft legislation by Representative Wagner and other bills currently under consideration can help alleviate these issues. The Chamber remains committed to working with the Congress, DOL, and the Securities and Exchange Commission to help craft a long-term solution to this important issue.

Sincerely,

Neil Bradley

cc: Members of the Subcommittee on Capital Markets, Securities, and Investment

Credit Union National Association
CUNA

Jim Nussle
President & CEO

Phone: 202-508-6745
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601 Pennsylvania Avenue NW
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July 13, 2017

The Honorable Bill Huizenga
Chairman
Subcommittee on Capital Markets, Securities, and Investment
Committee on Financial Services
House of Representatives
Washington, DC 20515

The Honorable Carolyn Maloney
Ranking Member
Subcommittee on Capital Markets, Securities, and Investment
Committee on Financial Services
House of Representatives
Washington, DC 20515

Dear Chairman Huizenga and Ranking Member Maloney:

On behalf of the Credit Union National Association (CUNA), I am writing to thank you for holding the hearing entitled "Impact of the DOL Fiduciary Rule on the Capital Markets." CUNA represents America's credit unions and their 110 million members.

CUNA supports the underlying intent of the Department of Labor (DOL) fiduciary rule to protect investors but sought clarity about the overly broad definition of investment advice in addition to other concerns with the DOL's rule, which was finalized in April 2016. We appreciate that the DOL provided some clarifications in its final rule. However, we believe more time for compliance and other changes to minimize the impact on low-to-moderate income investors could benefit credit union members.

CUNA urged the DOL to delay the applicability of the Fiduciary rule and it has also supported efforts to conduct additional research to ensure that credit union members are not harmed by unintended consequences of overly broad rules. Additional analysis about whether choices may be limited for consumers is beneficial for all consumers, including credit union members.

We urge the Committee to examine unintended consequences of the rule in today's hearing. Furthermore, we appreciate that the Committee is further examining the fiduciary rule when considering Representative Wagner's legislation to amend the Securities Exchange Act of 1934 to establish standards of conduct for brokers and dealers that are in the best interest of their retail customers. As Credit Union Service Organizations (CUSOs) and credit unions continue to navigate this rule, particularly the complexity surrounding whether it applies when offering certain investment products in individual retirement accounts (IRAs), we appreciate further consideration about how it could impact credit union members.

On behalf of America's credit unions and their 110 million members, thank you very much for your efforts.

Sincerely,

Jim Nussle

Jim Nussle
President & CEO

National Taxpayers Union

The Honorable Bill Huizenga
House Financial Services Committee
2129 Rayburn House Office Building
Washington, D.C. 20515

The Honorable Carolyn Maloney
House Financial Services Committee
2129 Rayburn House Office Building
Washington, D.C. 20515

Dear Chairman Huizenga and Ranking Member Maloney,

On behalf of NTU and our members across the country, I would like to thank you for holding a hearing on the impact the Department of Labor's fiduciary rule. As you are keenly aware, the rule has already been partially implemented, and barring no legislative action, will be fully implemented at the start of 2018. NTU opposes the rule and hopes this hearing will further highlight the disastrous and costly impact it will have on the ability for low and middle-income investors to receive financial advice.

According to a study by American Action Forum, data indicate the fiduciary rule will disqualify up to 7 million IRA holders from investment expertise and reduce the number of IRA openings by 400,000 a year. Consumers will face an additional $46.6 billion in costs, or $813 annually per account. If this rule creates obstacles to high-quality, individualized investment advice, more Americans could be deterred from saving and investing for retirement, especially in tax-advantaged vehicles. As Americans continue to retire at an unprecedented rate, the government should actively support policies that reduce the costs of saving for retirement, not the opposite.

Investment firms have stated that this rule will simply shift their business model from a commission-based system to a fee-based system. Many consumers, however, view this fee-based model less favorably. Unfortunately, this rule will harm those it was supposed to protect. When firms increase their price or choose to deal only with big money investors, lower and middle income investors will be priced out of the market.

Already, businesses have seen compliance costs and man-hours skyrocket to implement this rule. A Department of Labor report issued in April of last year estimates that brokerage firms will spend upwards of $35 billion on final rule compliance over ten years. The industry will also lose out on $11 billion in revenue by 2020 as more Americans exit the market. Even with fewer accounts, firms will see their compliance burden increase by 60,000 paperwork hours annually. Instead of complying with costly regulations, some larger firms like AIG, Metlife and Merrill

Lynch have decided to exit the market completely. The decision to entirely avoid the rule affects billions of dollars in assets, countless customers, and has resulted in thousands of employee layoffs.

The hearing will also focus on a draft of Congresswoman Ann Wagner's (R-MO) proposal to amend the Securities Exchange Act of 1934. In addition to repealing the fiduciary rule, the draft legislation would create a standards of conduct for brokers and dealers that are in the best interest of their customers. It would require brokers to make recommendations that "reflect reasonable diligence, care, skill and prudence" and provide protections to the consumer by requiring brokers to disclose any material conflict of interest. While this legislation is only a draft, I am optimistic that the full legislative text will be a more effective and consumer-friendly alternative to the fiduciary rule.

Sincerely,
Thomas Aiello
Policy and Government Affairs Associate

25 Massachusetts Avenue NW, Suite 140 * Washington, DC 20001 * Phone: (703) 299-8680 * Fax:(703) 683-5722 * ntu.org

The Honorable Bill Huizenga	The Honorable Carolyn B. Maloney
Chairman	Ranking Member
Capital Markets, Securities and Investments Subcommittee	Capital Markets, Securities and Investments Subcommittee
Committee on Financial Services	Committee on Financial Services
United States House of Representatives	United States House of Representatives
Washington, DC 20515	Washington, DC 20515

Re: Hearing entitled, "The Impact of the DOL Fiduciary Rule on the Capital Markets"

July 12, 2017

Dear Chairman Huizenga and Ranking Member Maloney:

My name is Phyllis C. Borzi and I served as the Assistant Secretary of Labor for the Employee Benefits Security Administration from 2009-2017.

I am writing to provide background information for the record on the coordination and cooperation activities between the U.S. Department of Labor (DOL) and the Securities and Exchange Commission (SEC) during the period of 2010-2017 in connection with the Department's development of its 2016 Final Regulation on Conflicts of Interest in the Investment Advice Marketplace, also known as the "COI Rule" or the "Fiduciary Rule," and the accompanying prohibited transaction class exemptions (PTEs). Throughout this document when I refer to the Rule, I intend to include these PTEs in my reference.

Industry opponents of this Rule, as well as former Republican SEC Commissioners and the current Secretary of Labor, have been repeatedly quoted in the press mistakenly characterizing these past efforts as perfunctory and not genuine efforts at coordination. The purpose of this letter is primarily to clarify the scope and extent of the actual interagency efforts during the approximately six-year process during which the rule was developed.

Because I am no longer a government employee, the information I am providing has neither been shared with nor cleared by my former employer, the U.S. Department of Labor, but represents my own thoughts, recollections and opinions about the process through which the DOL sought and received the input of the SEC staff as the COI Rule was developed.

I understand that the Subcommittee on Capital Market, Securities and Investments of the House Committee on Financial Services will be holding a hearing entitled "Impact of the DOL Fiduciary Rule on the Capital Markets" on Thursday, July 13, 2017.

I am providing this information on DOL/SEC cooperation and collaboration so that the hearing record will correctly reflect the long history that DOL and the SEC have had of working together on issues of shared interest. Those issues usually included enforcement matters, but more recently have focused on other consumer protections through coordination of regulatory projects, such as the DOL and SEC efforts that each agency undertook to improve consumer disclosure with respect to target date funds, DOL's fee disclosure rules for pension plans, and the COI Rule. My comments will be specifically directed toward the COI Rule since that is the focus of the July 13 Subcommittee hearing.

I have recently learned, however, that the hearing will also consider the latest legislative proposal by Representative Ann Wagner to block implementation of the DOL COI rule. Among other things, I understand that proposal would strip jurisdiction from the DOL to define the term "fiduciary" with respect to brokers and dealers and their registered representatives as well as with respect to those individuals who sell annuities. The bill generally transfers that authority to the SEC, or, in the case of annuities, relies entirely on state insurance regulators without any Federal oversight, thus apparently stripping the SEC of its current authority over annuities that are treated as securities.

The stated reason for these radical changes is to allow the SEC to develop a rule that could broadly apply to all segments of the investment marketplace (both taxable and tax-exempt investments), not just the tax-exempt retirement advice marketplace covered by the existing COI DOL rule, thus allegedly reducing consumer confusion. It is unclear why the insurance industry deserves separate and weaker standards for annuity sales, especially since the harm consumers have experienced with conflicts of interest regarding the sale of some of these products is well-documented. Later in this letter I will share my own preliminary observations regarding the new Wagner proposal.

Stripping the DOL of its long-standing authority and relying instead on the SEC and state insurance regulators will expose retirement savers to continued abuses from conflicts of interest.

Efforts to subordinate DOL regulatory authority to that of the SEC will not solve the problem caused by conflicts of interest in the retirement investment advice marketplace.

For many years, opponents of the COI Rule have insisted that the best way to protect consumers is to assure a uniform set of standards for investment advisors that apply to all forms of investment advice - whether that advice is rendered with respect to retirement or non-retirement (or taxable or non-taxable) investments. The "solution" to this "problem" that COI Rule opponents tout is to allow the SEC to set these uniform standards and for the Department's statutory authority over retirement plans and individual retirement accounts (IRAs) to be subordinated to the SEC's efforts by nullifying the existing Final COI regulations and requiring any future DOL regulations to be consistent with and reflective of any SEC fiduciary rule. Alternatively, COI Rule opponents propose to eliminate DOL's authority to regulate investment advice fiduciaries entirely.

Establishing a uniform standard for investment advisors with regard to both retirement and non-retirement advice is a laudable goal. However, given the SEC's history of inaction in this important consumer protection area and the limitation of its statutory authority to "securities," it is much more reasonable, protective of consumers/investors, and consistent with the varying statutory authorities of the DOL and the SEC for the Final DOL COI Rule and its accompanying final prohibited transaction class exemptions (PTEs) to be fully implemented as scheduled on January 1, 2018 and for the SEC to issue subsequent guidance within its own statutory authority that is consistent with the DOL rules. That would be the simplest and most cost-effective method of achieving the DOL's rule opponents' oft-stated goal of "uniformity" in the advice marketplace without further delay.

The argument that the SEC has superior expertise to the DOL in regulating financial products generally is questionable at best, if not misleading. The scope of the SEC's statutory reach is at the same time broader than DOL's (because the SEC regulates securities in both the non-taxable retirement and taxable non-retirement contexts) and narrower than the DOL's (because the SEC regulates securities, not the entire range of investment products available to and utilized by pension plan sponsors and individuals saving for retirement).

Unquestionably, as result of its statutory mandate, the SEC has developed substantial expertise in regulating securities. However, the DOL has substantial expertise in regulating and analyzing the products sold in the retirement marketplace, through which most individuals save. Although securities are an important class of investment products purchased by ERISA-covered pension plans and individuals, both through their plan investments and individual retirement arrangements, many other types of investments, not subject to SEC regulation, are also an important component of current and future retirement savings.

The SEC has neither the current expertise nor the authority to regulate these other investments, such as non-security insurance products, real estate, bank collective trusts, and many alternative investments. For decades, the Department has overseen and enforced ERISA and certain Internal Revenue Code rules for all retirement investments, including securities and non-security investments. To say that the Department lacks expertise in regulating and overseeing asset classes that are commonly found in retirement savings arrangements is simply incorrect. This is particularly true with respect to the many decades of experience the DOL has gained as it crafted and enforced prohibited transaction exemptions (PTEs) both on a class and individual exemption basis. The possibility that the financial services industry may be more comfortable dealing with the SEC does not mean that the DOL understanding of industry practices in the retirement marketplace is deficient.

Clearly both the SEC and the Department possess considerable expertise in their own areas of authority, some of which may overlap and some of which may not. That is why neither agency acting alone can protect consumers from the well-documented economic harms that occur from conflicted investment advice in both the taxable and tax-exempt investment world.

The legal basis underpinning the DOL COI/Fiduciary Rule is the Department's statutory authority to define the term "fiduciary." This authority is not new – it was included in the original enabling statute, the Employee Retirement Income Security Act of 1974 (ERISA). And the DOL's Final COI Rule simply is an exercise of the Secretary of Labor's broad authority to clarify and expand the category of individuals who are ERISA investment advice fiduciaries. The Rule replaces the Department's 1975 definitional regulatory guidance with an updated approach, drawing on the current definition of a "recommendation" utilized by the Financial Industry Regulatory Authority (FINRA) to distinguish a fiduciary communication from other forms of non-fiduciary consumer communication. Utilizing FINRA s definition was a deliberate decision on the part of DOL designed to minimize industry confusion. The three Federal courts that have addressed the legal challenges mounted by various industry trade associations challenging the Department's right to exercise this statutory authority have uniformly and unanimously rejected the arguments of industry opponents that the Department lacked such authority or exercised it in an unreasonable fashion.[1]

[1] *See Chamber of Commerce v. U.S. Dep't of Labor*, No. 17-10238, 2017 WL 1284187 (5th Cir. Apr. 5, 2017) (*"Chamber III"*) (denying appellants' motion for injunction pending appeal and for expedited appeal); *Chamber of Commerce v. Hugler*, No. 3:16-cv-1476-M, 2017 WL 1062444 (N.D. Tex. Mar. 20, 2017) (*"Chamber II"*) (denying appellants' motion for injunction pending appeal); *Mkt. Synergy Grp., Inc. v. U.S. Dep't of Labor*, No. 16-CV-4083-DDC-KGS, 2017 WL 661592 (D. Kan. Feb. 17, 2017) (*"Market Synergy II"*) (granting summary judgment to the Department of Labor); *Chamber of Commerce v. Hugler*, No. 3:16-cv-1476-M, 2017 WL 514424 (N.D. Tex. Feb. 8, 2017) (*"Chamber"*) (granting summary judgment to the Department of Labor); *Mkt. Synergy Grp., Inc. v. U.S. Dep't of Labor*, No. 16-CV-4083-DDC-KGS, 2016 WL 6948061 (D. Kan. Nov. 28, 2016) (*"Market Synergy I"*) (denying plaintiff's motion for preliminary injunction); *Nat'l Ass'n for Fixed Annuities v. Perez*, 219 F. Supp. 3d 10 (D.D.C. Nov. 23,

The statutory language of ERISA stands in marked contrast to the statutory framework of securities laws administered by the SEC. Securities law generally tolerates conflicts of interest among investment advisors as long as these conflicts are properly disclosed and mitigated.

Among other things, ERISA requires fiduciaries to act with undivided loyalty and prudence and flatly bans fiduciaries who receive compensation either directly or indirectly for advice from providing investment advice to plans or individuals that is tainted by conflicts of interest (this would be is a "prohibited transaction" under ERISA). Certain conflicted behaviors may be permitted under ERISA, however, if the adviser's conduct falls within the conditions of a specific prohibited transaction exemption (PTE). Generally, in the IRA context, ERISA's fiduciary definition applies through the prohibited transaction rules contained in the Internal Revenue Code.

Industry opponents have asserted that DOL has no authority under ERISA to regulate investment advice fiduciary duties in the IRA context, but that is incorrect. The DOL authority to define fiduciary status for purposes of ERISA extends to the parallel prohibited transaction rules under IRC section 4975. This was explicitly established by transferring all interpretive, rulemaking, and exemption authority from the Secretary of the Treasury to the Secretary of Labor through the terms of President Carter's Reorganization Plan #4 (October 17, 1978). That authority transfer was codified and ratified by Congress through a statutory provision enacted in 1984.

Since ERISA's passage in 1974, the Secretary of Labor has exercised broad authority to issue administrative exemptions to the prohibited transaction rules, either on a class or individual basis. Because of the substantial statutory differences in the securities laws and ERISA, even if both the SEC and the DOL used the exact same definition of "fiduciary" (and under the DOL's Final COI Rule, they are very close), the duties to which an investment advice fiduciary would be subject in connection with conflicted investment advice under the two statutory schemes would be different.

The DOL's collaboration and coordination with the SEC throughout the rulemaking process was sustained, high-level, and productive, leading to a better Final COI Rule.

Turning now to the question of the collaboration and coordination between the DOL and the SEC, I will briefly outline the history of DOL/SEC interactions among the SEC staff, the Employee Benefits Security Administration (EBSA) staff at the DOL, and myself. This description is not intended to be an exhaustive list of all DOL/SEC contacts with respect to the COI Rule.

The original proposal identifying changes to the definition of a fiduciary under ERISA was issued in the fall of 2010. At about that same time, I reached out to the then Chair of the SEC, Mary Shapiro, to discuss the problem caused by conflicted investment advice and the harm suffered by unsuspecting consumers because certain individuals in the investment advice marketplace were holding themselves

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2016) ("NAFA II") (granting motion for expedited ruling and denying plaintiff's motion for preliminary injunction); *Nat'l Ass'n for Fixed Annuities v. Perez*, 217 F. Supp. 3d 1 (D.D.C. Nov. 4, 2016) ("*NAFA I*") (granting summary judgment to the Department of Labor).

out as skilled financial, investment or retirement advisers without having to meet a fiduciary standard of care regarding the advice they were giving to their customers.

I explained our proposal in very general terms but noted that because it was just a proposal, we planned to reach out to a variety of experts, including other government agencies with relevant expertise, and industry representatives, to seek comment and suggestions for improvement.

When I met with Chair Shapiro, I had one request: that she authorize the SEC career staff to provide technical assistance to DOL career staff as we developed our rule because I was well-aware of the SEC's expertise regarding securities, an important component of many retirement investment portfolios. My major concern was simple: I wanted to be able to assure the regulated community that nothing in the rule we were developing would conflict with any other provision of law or any regulation administered by the SEC. In other words, my goal was to be sure that nothing we required under our rulemaking would create a situation where compliance with our developing rule would put a regulated entity or individual in the position where they were likely to violate an existing SEC or FINRA rule.
Chair Shapiro readily agreed to this request and my career Deputy Assistant Secretary for Program Operations became the contact for the person(s) on her staff who would meet and work with us. Our staffs held several meetings during the next several months to discuss the 2010 proposal, until I announced in 2011 that the Department would withdraw the proposed rule and work toward a future reproposal.

During the ensuing years, as DOL staff continued to work on the rule itself, the accompanying prohibited transaction exemptions, and a more comprehensive and robust economic analysis that would support the rule, staff discussions between DOL and SEC staff continued. When Chair Shapiro left the Commission and Acting Chair Elisse Walter took over, I met with her and renewed the request for continuing technical assistance by the SEC career staff. Acting Chair Walter was also supportive of my request and career staff level meetings between DOL and SEC staff picked up again and continued on a more frequent basis throughout the intervening years as we worked on a new proposal. I believe that then Secretary of Labor Hilda Solis accompanied me to one of the meetings with Acting Chair Walter. In addition, Seth Harris, in his capacity as the Acting Secretary of Labor after Secretary Solis' departure, also attended at least one of my meetings. I apologize for not being able to pinpoint the dates of these meetings with more specificity but I no longer have access to my calendar or files at the DOL, so I am relying on my memory to describe these events.

When the Senate confirmed SEC Chair Mary Jo White, the new Secretary of Labor, Thomas Perez, reached out to her to meet and discuss continuing our cooperative process on the COI rule. I was also present at that meeting and at a few subsequent meetings between the two agency heads. Secretary Perez also established a separate line of communication consisting primarily of periodic phone check-ins between himself and Chair White to assure that our staffs continued the cordial and constructive dialogue as we got closer to the publication of the new proposal. I believe that there were approximately 10 of these follow up contacts between the Secretary and the Chair. This level of involvement at the highest level of agency leadership was, in my experience, not at all typical, but does reflect the serious commitment that both agencies had to working together collaboratively on the COI project.

In describing these ongoing staff communications, I would note that my Deputy Assistant Secretary for Program Operations would arrange meetings and calls with SEC career staff through the point person identified by the Chair. Although I did attend a few of these staff-level discussion meetings, I was typically briefed by my staff after the meetings about the topics covered, the additional research that might be necessary to enhance our decisionmaking, and the types of changes that were likely to be considered as a result of the discussions. Who from the SEC was present at each of these meetings was entirely within the control of the SEC Chair's office, although it is worthy to note that the meetings typically included representatives of both the Divisions of Investment Management and Trading and Markets. In my experience, the discussions were substantive, frank and robust, but everyone understood that they were staff discussions, not official Commission or DOL communications.

In addition, DOL career staff freely shared drafts of possible sections of the rule or of proposed PTEs as they were drafted by DOL staff.

The DOL staff working on research and economic analysis also met with their counterparts at the SEC. Participants in these meetings from the SEC were similarly individuals identified by the Chair's office. The research and analysis that DOL staff were examining to develop the economic analysis that would accompany the new proposed rule were also freely shared with SEC staff. Given the difficulty both we and the SEC had in obtaining relevant data from the financial services industry, the agency staffs also shared data and research as it became available. In each of these meetings, the input of the SEC staff was solicited and given. As previously noted, the primary goal continued to be to avoid developing a proposed (or final) rule that created regulatory conflicts for the regulated community.

Following established interagency protocols, we made no attempt to reach out to individual commissioners or their staff – we simply followed the lead of the Chair's office. Ironically none of the other commissioners, even those most publicly and vocally critical of what the Department was doing, ever asked us for a meeting or a briefing on the substance of our developing proposal or the DOL/SEC coordination efforts. Yet they, like the industry opponents of the Rule, continued to assert that we were not really coordinating with the SEC.

Both the Department and the SEC Chair and their respective staffs understood from the outset that this coordination was not designed to develop a joint rule. Nor were these efforts designed to determine what the SEC would have done were they drafting the COI proposal. As previously explained, given the statutory differences between the securities laws and ERISA, that task would have been at best extremely difficult, if not impossible. But the DOL staff welcomed and encouraged suggestions and comments by the SEC staff on what the DOL was thinking about proposing and the SEC's input was usually incorporated in some form in the ongoing drafts. The comments and input this cooperation and collaboration yielded were in addition to any comments provided by the SEC as part of the formal OMB/OIRA clearance process required of any rulemaking, in which various Federal agencies with a potential interest in the subject matter of another agency's rulemaking are given the opportunity to review and comment on the rule as a whole as submitted for Administration approval prior to publication.

One feature of this ongoing coordination that was much appreciated by the DOL was the willingness of the SEC staff to predict and confirm the DOL staff's understanding of what the likely industry response would be to what was being developed in the rulemaking process. The DOL staff was well-aware that some segments of the financial services industry, particularly the insurance companies, would be required to make a number of changes in their policies, procedures and compensation practices to implement an enforceable best interest standard under ERISA so it was reassuring, but not surprising, to DOL staff when the SEC staff reached similar conclusions regarding the likely areas of concern to the industry. The SEC staff also provided valuable insight and advice on how best to structure the various provisions of the Rule and the conditions of the PTEs to minimize industry disruption and maximize the effectiveness of the Rule.

On balance, the input we received from the SEC career staff was extremely helpful and resulted in a better, more effective and efficient set of proposals and a final rule. More than once I have publicly expressed the deep appreciation I have for the cooperation and collaboration we received from the various SEC chairs and their career staff. This appreciation was widely shared during the Obama Administration by the DOL leadership and the DOL staff.

In addition, during the COI rulemaking process, DOL staff also worked closely with other federal regulators, such as staff from the Treasury Department, particularly those under the purview of the Office of Domestic Finance (especially staff from the Federal Insurance Office) and the Office of Tax Policy (especially the employee benefits staff). In addition, the DOL worked with the Commodity Futures Trading Commission (CFTC) to be sure that swaps rules issued by the CFTC and the SEC under Dodd-Frank were not in conflict with ERISA so that pension plans that engaged in swap transactions could continue to do so without creating regulatory problems under either Dodd-Frank or ERISA. And, as noted in the preamble to the Final Rule, we also received valuable input from the National Association of Insurance Commissioners (from both their staff and several individual commissioners), FINRA staff, and the North American Securities Administrators Association (NASAA) (again from both staff and several individual state securities regulators).

Ironically, although I continued to assure the regulated community that nothing in the Final COI Rule would conflict with any other SEC rule, for all the close coordination we had with the SEC and the several instances where we changed our draft language in response to their specific concern about a possible regulatory conflict, when the new proposed rule was issued in April of 2015, FINRA staff immediately identified a component of the proposed notice requirements that had not been previously brought to our attention but would likely violate a FINRA rule. We immediately dropped that requirement. Unfortunately, while we had numerous staff discussions with FINRA during the latter two years of the process, because it is not a Federal government agency, but rather an industry self-regulatory body, while we briefed them on what we were doing and engaged in a helpful and substantive dialogue with FINRA staff, under the Administrative Procedures Act, we could not share actual draft language with them without having to make those drafts available to the public in general. But nonetheless, this is a simple example of the type of input that we received that allowed us to improve and strengthen the workability of the Final Rule.

The Wagner bill is a thinly disguised attempt to protect and preserve highly profitable but seriously conflicted business models at the expense of ordinary Americans struggling to save for retirement.

Finally, I offer a few personal observations and concerns about the latest version of the Wagner bill. Opponents of the Rule have proposed yet another legislative vehicle to thwart the implementation of the DOL COI/Fiduciary Rule. Like its predecessors, it purports to establish a statutory best interest standard that applies broadly to all recommendations: those involving both retirement investments and non-retirement investments. It nullifies the Final DOL COI Rule and replaces it with a substantially weaker set of so-called "consumer protections." In fact, these are even less protective of consumers than the requirements that existed even before the Department of Labor began to work on its COI/Fiduciary project in the first place; in some cases, they may appear to be a return to the pre-ERISA world. These "protections" would be administered by the SEC, not the DOL. A special set of even weaker rules would apply to those insurance brokers giving investment advice regarding annuities. These lower standards would be administered by state insurance departments, not the DOL or the SEC.

In addition to taking a wrecking ball to the decades old statutory framework for oversight of investment advice provided to plans and individuals under ERISA and the Internal Revenue Code, a framework that was created after more than a decade of study and careful analysis by various Congresses and several commissions with public and private sector members and substantial public input, the new Wagner bill will generate significant and extended litigation, not to mention exacerbate consumer and industry confusion over the applicable regulatory principles.

Although its sponsors and supporters claim the statutory language is self-executing, substituting an entirely new and vaguely drafted statutory scheme for one that has been in place for nearly 45 years and providing broad new regulatory authority over investment products that have not traditionally been under their purview to an entirely different agency (the SEC) is likely to create havoc in the marketplace and great uncertainty for financial services companies, especially those that have been trying to do the right thing and prepare for compliance under the existing Final DOL COI Rule. Moreover, the weaker standards for annuity products administered by state insurance regulators that are established by the Wagner bill will create additional risk of harm from advisor financial conflicts for consumers, who will now be stripped of the important enforcement protections that the SEC has provided for annuity products that were treated as securities.

To what end? As many in the financial services industry and their supporters have been asking with respect to the DOL efforts, "What's the problem you are trying to solve?" The only logical explanation for this radical approach is that some in the industry still are not willing to commit to a legally enforceable best interest standard, but, in order to preserve their highly profitable and highly conflicted compensation arrangements and business models, they are willing to create the precise effect on the investment advice marketplace – chaos, confusion and uncertainty – that they have continually alleged, without factual evidence to prove it, that the Final DOL COI Rule supposedly creates.

For more than six years, while the DOL rule was in development, opponents of the Rule alleged, again without proof, that the so-called "unintended consequences" of the DOL Rule were to undermine access to investment advice for small savers, a market that actual data shows is not currently served by many of the Rule's opponents. But my concern today is not limited to the unintended consequences of the current version of the Wagner bill, but to the serious harm to all savers, and most especially retirement savers, that will result from the INTENDED consequences of the bill.

The harm to investors and the market confusion and upheaval that will be caused by the bill are not unintended, they are fully intended to reward and protect those industry players and their representatives that are unwilling to be legally accountable to act in their clients' best interests. To achieve that end, the bill pays lip service to a best interest standard but by its very terms would return consumer protections for retirement savers to their pre-ERISA state and leave consumers even more confused and vulnerable to the harms caused by conflicted investment advice than ever before.

Opponents of the COI Rule continually repeat the false charge that the Rule reduces "consumer choice." But the latest version of the Wagner bill makes it crystal clear that the only choice that some in the industry and their allies want to preserve is their own choice to continue their current reliance on conflicted compensation arrangements and the business models that reward investment recommendations that maximize profitability at the expense of their customers who are struggling to save for retirement.

I will leave it to others to critique in detail the technical shortcomings of this legislative proposal, but even a quick reading of the bill reveals the obvious: stripping away from the Department of Labor its long-standing role to define what it means to be a fiduciary, a position of trust that has existed in the law for centuries, and creating a separate and lesser standard of care for the very classes of people that individual savers need to rely on for solid, reliable financial advice they can trust, is more than a step backward. It flies in the face of the careful, measured and quite deliberate actions of Congress in 1974 in enacting ERISA.

The Congress that adopted ERISA was well-aware of the existence and the expertise of the SEC, but instead, it chose to place the responsibility for defining and overseeing fiduciary activities and investment advice in the context of retirement savings in a different agency -- in the Department of Labor. That regulatory structure has worked well for more than four decades and is generally well-understood by the industry. Where is the evidence and thoughtful and deliberate analysis that documents that the decision made by Congress in 1974 was wrong and justifies the supposed need for the radical change proposed by the Wagner bill? And why must Congress rush to consider it now? I think we all know the answers to those questions.

Thank you again for the opportunity to provide input for the Committee's consideration as it examines the DOL's COI/Fiduciary Rule. Please feel free to contact me if you have any further questions.

Sincerely,

Phyllis C Borzi

Phyllis C. Borzi
Former Assistant Secretary of Labor for the
Employee Benefits Security Administration

Deregulators Must Follow the Law, So Regulators Will Too

As the Labor Department acts to revise the Fiduciary Rule and others, the process requires patience.

By
Alexander Acosta
May 22, 2017 7:00 p.m. ET
117 COMMENTS

President Trump has committed—and rightly so—to roll back unnecessary regulations that eliminate jobs, inhibit job creation, or impose costs that exceed their benefits. American workers and families deserve good, safe jobs, and unnecessary impediments to job creation are a disservice to all working Americans. As the Labor Department approaches this regulatory rollback, we will keep in mind two core principles: respect for the individual and respect for the rule of law.

America was founded on the belief that people should be trusted to govern themselves. Citizens sit on juries and decide the fate of their fellow citizens. Voters elect their representatives to Washington. By the same token, Americans should be trusted to exercise individual choice and freedom of contract. At a practical level, this means Washington should regulate only when necessary. Limiting the scope of government protects space for people to make their own judgments about what is best for their families.

The rule of law is America's other great contribution to the modern world. Engraved above the doors of the Supreme Court are the words "Equal Justice Under Law." Those four words announce that no one is above the law, that everyone is entitled to its protections, and that Washington must, first and foremost, follow its own rules. This means federal agencies can act only as the law allows: The law sets limits on their power and establishes procedures they must follow when they regulate—or deregulate.

The Administrative Procedure Act is one of these laws. Congress had good reason to adopt it: In the modern world, regulations are akin in power to statutes, but agency heads are not elected. Thus, before an agency can regulate or deregulate, it must generally provide notice and seek public comment. The process ensures that all Americans—workers, small businesses, corporations, communities—have an opportunity to express their concerns before a rule is written or changed. Agency heads have a legal duty to consider all the views expressed before adopting a final rule.

Today there are several regulations enacted by the Obama administration that federal courts have declared unlawful. One is the Persuader Rule, which would make it harder for businesses to obtain legal advice. Even the American Bar Association believes the rule goes too far. Last year a federal judge held that "the rule is defective to its core" and blocked its implementation. Now the Labor Department will engage in a new rule-making process, proposing to rescind the rule.

Another example of a controversial regulation is the Fiduciary Rule. Although courts have upheld this rule as consistent with Congress's delegated authority, the Fiduciary Rule as written may not align with President Trump's deregulatory goals. This administration presumes that Americans can be trusted to decide for themselves what is best for them.

The rule's critics say it would limit choice of investment advice, limit freedom of contract, and enforce these limits through new legal remedies that would likely be a boon to trial attorneys at the expense of investors. Certainly, it is important to ensure that savers and retirees receive prudent investment advice, but doing so in a way that limits choice and benefits lawyers is not what this administration envisions.

The Labor Department has concluded that it is necessary to seek additional public input on the entire Fiduciary Rule, and we will do so. We recognize that the rule goes into partial effect on June 9, with full implementation on Jan. 1, 2018. Some have called for a complete delay of the rule.

We have carefully considered the record in this case, and the requirements of the Administrative Procedure Act, and have found no principled legal basis to change the June 9 date while we seek public input. Respect for the rule of law leads us to the conclusion that this date cannot be postponed. Trust in Americans' ability to decide what is best for them and their families leads us to the conclusion that we should seek public comment on how to revise this rule. Under the Obama administration, the Securities and Exchange Commission declined to move forward in rule-making. Yet the SEC has critical expertise in this area. I hope in this administration the SEC will be a full participant.

America is unique because, for more than 200 years, its institutions and principles have preserved the people's freedoms. From administration to administration, respect for the rule of law has remained, even when Americans have been bitterly divided. Some who call for immediate action on the Obama administration's regulations are frustrated with the slow process of public notice and comment. But this process is not red tape. It is what ensures that agency heads do not act on whims, but rather only after considering the views of all Americans. Admittedly, this means deregulation must find its way through the thicket of law. Casting aside the thicket, however, would leave Americans vulnerable to regulatory whim.

The Labor Department will roll back regulations that harm American workers and families. We will do so while respecting the principles and institutions that make America strong.

Mr. Acosta is secretary of labor.

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How AARP Helped Obama Thwart Wall Street on Tougher Broker Rule

B www.bloomberg.com/politics/articles/2016-04-12/how-aarp-helped-obama-beat-back-wall-street-on-tough-broker-rule

As the Obama administration reached the end of its nearly six-year battle with financial firms over setting tougher rules for brokers who handle retirement accounts, an emissary went up to Capitol Hill to smooth the way for the rollout.

AARP, in a meeting with Democratic congressional aides last month, stressed the policy's importance to its millions of retiree members, according to people briefed on the gathering. The more significant message, however, was left unsaid: lawmakers besieged by industry pushback should keep in mind there was an equally powerful lobby on the other side.

AARP's leading role in advocating for the Labor Department rule that makes brokers put clients' interests ahead of their own was no accident. The administration, seeking to cement a legacy of being tough on Wall Street, spent months trading information and coordinating with the group as it campaigned for the plan, hundreds of pages of e-mails obtained from the department under public records law show.

The collaboration -- which opponents decried as overly cozy -- included AARP and Labor staff discussing guest lists for events, writing questions for an appearance in Miami by Labor Secretary Thomas Perez and strategizing on how to plant positive media articles. President Barack Obama himself announced the policy's revival last year at AARP's headquarters in Washington. And last week after the rule's completion, he wrote the group a thank-you note.

'Own Country'

The alliance helped resuscitate the regulation after many thought it was dead in 2011 due to vociferous lobbying by banks, brokerages and insurers. AARP's muscle will also be important going forward, supporters say, as the industry tries to get Congress or the courts to reverse one of its biggest losses since the Dodd-Frank Act passed in 2010.

"The AARP is its own country," said Knut Rostad, president of the Institute for the Fiduciary Standard, who has called for the stepped up protections for years.

The new rule, which brokers must fully adopt by January 2018, requires advisers to act in the best interests of their clients, an obligation known as fiduciary duty. Previously brokers could recommend investments that they believed were merely suitable.

Labor Department spokesman Michael Trupo said input from a broad array of groups led to a strong regulation that also minimizes burdens on industry.

Broad Group

"The Department of Labor welcomed feedback on how to address conflicts of interest in retirement advice through meetings, hearings, phone calls and written comments from a broad range of stakeholders, including consumer and retirement advocates, representatives from the financial services industry, and others," he said.

AARP (formerly known as the American Association of Retired Persons) carries great weight in Washington because of its massive war chest and membership, a group of 38 million people over the age of 50 who tend to vote in great numbers. Non-partisan and non-profit, it has made financial issues a top priority and had been working in some capacity on getting the broker rule enacted since the late 1990s.

Cristina Martin Firvida, the group's director of financial security, said that while AARP was able to provide something of a counterweight to the finance industry's opposition, it still sees the fight more in David v. Goliath terms.

"Certainly our 38 million members are very, very important," she said. "But there is no mistaking that the power of the lobbying on the other side of this issue is staggering."

Calculated Move

The Labor Department records, which cover the first six months in 2015 when the push to revive the rule kicked into high gear, provide a rare glimpse into how the Obama administration courts, and relies on, outside allies in tough policy fights.

Opponents included big banks like Morgan Stanley, major mutual fund companies like Fidelity Investments and independent brokers across the U.S. Many see the Labor-AARP partnership as a calculated move by the government to use the retirees' group as its own de facto lobbyist. With the administration unable to persuade scores of congressional Democrats to support the rule, they say, it turned to AARP.

The result, the industry says, is that a rulemaking impacting millions of investors and $12 trillion in retirement savings was marred by politics. The message of beating back Wall Street, they add, quickly took precedence over a deliberative process that could have led to a less-flawed regulation. In particular, they say the policy could lead to lower-income clients being shunted aside because of the increased compliance costs.

"It is one thing to win a political race, it is another thing to make good policy," said Kenneth Bentsen, president of the Securities Industry and Financial Markets Association which represents hundreds of brokerage firms, banks and asset managers. "In this instance, the politics don't make it right."

'Sea Change'

Bentsen said he was especially struck when Obama appeared at AARP's offices in February 2015 to announce the rule's revival.

The event left some wondering when a U.S. president last made a personal plea for an adjustment to the Employee Retirement Income Security Act of 1974. "That is just a sea change," Bentsen said.

AARP wasn't the only advocacy group that worked with the White House. Some, like the Consumer Federation of America, have fought for a fiduciary rule for years. Other backers included the AFL-CIO labor federation, Americans for Financial Reform and Better Markets.

Also significant, people involved say, was Perez, who made the rule's enactment a priority when he became secretary in 2013. He personally briefed members of the House and Senate and called advocates before key developments, according to a copy of his daily appointment calendars for the first half of last year.

Democrats' Opposition

With the White House interested in showing its support for Main Street, as opposed to Wall Street, the fiduciary regulation got fresh attention toward the end of 2014. It had first been proposed in 2010 and then withdrawn by Labor the next year after industry lobbying sparked bipartisan complaints.

This time, the rule was given a make-over. First, the term "fiduciary" was de-emphasized. Instead, an easier-to-understand concept, brokers' conflicts of interest, was highlighted. Driving the point home, the president's Council of Economic Advisers claimed in a study that retirement savers lost up to $17 billion annually due to excessive commissions, high fees and other dubious practices.

A few weeks after the study was made public in January 2015, the White House reached out to AARP and other consumer groups to invite them to a "closed press and off the record" session with senior officials from the National Economic Council and Labor. The plan, an e-mail said, was to discuss "campaign efforts."

The biggest of those came when Obama made his announcement. AARP and the Labor Department closely consulted about the 40 guests the association could invite, according to e-mails.

Reid, Schumer

Working throughout the weekend before the Feb. 23 event, AARP lobbyists e-mailed with senior Labor staff members, trading spreadsheets that ranked guests in two tiers of priority. The first level included Richard Trumka, head of the AFL-CIO, Cornell Brooks, CEO of the NAACP and Lee Saunders, president of the American Federation of State, County and Municipal Employees.

Congressional aides were also considered.

"My preference with any seats that open up is to make sure we can add Hill staff," wrote AARP's Martin Firvida, adding that her "top priority" would be somebody from Democratic Senate Leader Harry Reid's office, followed by an aide to Senator Charles Schumer of New York.

Obama's appearance at AARP resembled a campaign rally. Appearing on a stage with Perez and Massachusetts Democratic Senator Elizabeth Warren, he fired up the crowd with references to financial advisers who "receive backdoor payments or hidden fees for steering people into bad retirement investments."

26,000 Signatures

Once the plan was released, AARP stayed in close touch with the Labor Department.

In late April of 2015, for example, Martin Firvida reached out to senior Labor Department officials to discuss a petition drive in support of the rule. The group had generated 26,000 signatures backing the plan and wanted Labor's advice on how to maximize the visual impact of 52 reams of paper being dropped off at the agency by volunteers in AARP t-shirts.

"We will take your direction on what type and size box in which you would like those," Martin Firvida wrote.

In an e-mailed statement, Martin Firvida said AARP has made "countless petition drops" on a variety of different issues and closely coordinates with the government because many federal "facilities have understandably enhanced security."

'Grassroots Support'

Preparations were also extensive for a May 2015 conference in Miami, where Labor staff agreed to send Perez, hoping to "build grassroots support" for the initiative, according to one e-mail.

Ahead of the event, AARP senior adviser John Cummings wrote to Perez's office that the crowd could be as large as 1,000 people, and to ensure attendance it would advertise the speech "as well as offer refreshments to entice."

AARP and Labor traded draft press releases as the meeting approached, with the trade group's representative also offering to send talking points to the agency.

An AARP official also suggested Yahoo Finance might be a good place to get news coverage. "We typically have pitched the producer/writer and she pitches her editors and then does the soft piece," wrote Josh Rosenblum of AARP media relations on April 29 to a Perez spokeswoman.

Preparing Questions

Rosenblum, in an interview, explained that his reference to "soft" pieces was about stories that help educate consumers, as opposed to hard-hitting, investigative journalism.

As they prepped for an on-stage discussion between Perez and the AARP president in Miami, the two sides exchanged a four-page document of possible questions and answers. "How specifically are people being harmed under the current regulatory environment?" read one. "Some may say that financial professionals are already well regulated. Are they really?" read another.

"We are open to any and all suggestions and any questions your team may want to use instead," AARP's Cummings wrote to Labor.

Perez's staff was also told in a memo from AARP dated April 29 that during an audience question and answer period, an executive from the group "would handle and deflect any questions that are not germane to the topics or are deemed inappropriate."