



Consumer Federation of America

September 15, 2017

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

Re: ZRIN 1210-ZA27, Extension of Transition Period and Delay of Applicability Dates,
Fiduciary Rule

Ladies and Gentlemen:

We are writing on behalf of the Consumer Federation of America (CFA)¹ to express our strong opposition to the proposed extension of the transition period for the conflict of interest (or “fiduciary”) rule and its related exemptions, which the Department also refers to as a “delay” of the applicability dates. Extending this transition period will mean that the full protections and benefits of the fiduciary rule won’t be realized and retirement savers, particularly IRA investors, will continue to suffer the harmful consequences of conflicted advice. The Department has not provided an adequate factual or legal basis for this proposal, nor is the proposal consistent with the Department’s previous analysis and findings in promulgating the rule and its related exemptions.

I. This is clearly not a proposed delay; it’s a proposed stay.

To characterize what the Department is proposing as a “delay” is simply incorrect. Delay implies that the rule will be implemented at the end of the proposed 18 month delay period. However, that’s clearly not the Department’s intent here. Rather, the intent is to grant what is effectively a revocation of the applicability of the most consequential provisions of the rule, by staying them, with the goal that implementation of these provisions never occurs. Meanwhile, the Department suggests that it will work to ease the compliance requirements for the industry, whether that takes the form of “propos[ing] in the near future a new and streamlined class exemption built in large part on recent innovations” or changes to the existing conditions, “which may be revised, repealed, or replaced.”

¹ The Consumer Federation of America is a non-profit association of nearly 300 consumer groups that was established in 1968 to advance the consumer interest through research, advocacy, and education.

While it may be reasonable for an agency to phase in regulatory compliance in order to provide firms with more time to come into compliance, stays that grant firms a reprieve from certain regulatory requirements while the agency determines whether and how to permanently revise, repeal, or replace those requirements are a different matter. Stays of regulatory requirements are only appropriate under certain specific circumstances, laid out in 5 U.S.C. § 705. The reasoning offered in the Department’s RFI, which first sought comment on a potential delay of the January 1, 2018 applicability date, reflected the proper purpose of a delay, albeit one we did not support. It asked if a delay would “allow[] for more efficient implementation responsive to recent market developments.” This proposal, in contrast, dispenses with that fiction and now acknowledges that the real purpose is to ensure that regulated parties do not “incur undue expense to comply with conditions or requirements that [the Department] ultimately determines to revise or repeal.” It is a stay, aimed at effectively repealing the exemptions’ critical conditions and must be justified as such.

II. The Department has predetermined the outcome of this regulatory action.

At the most basic level, the Department decided before publishing the RFI that the industry should not be required to come into full compliance with the rule’s exemptions, particularly the provisions that ensure compliance and provide an enforcement mechanism to hold firms and advisers accountable for non-compliance. Now, the Department is going through a cursory process to get to its desired result. We expressed our deep concern about the harmful impact of such a delay in our comment responding to the RFI, stating, “Unfortunately, by posing the question about whether there should be a further delay, the Department is creating unnecessary uncertainty and confusion in the market. More concerning, it is creating a self-fulfilling prophecy: firms, in anticipation that a delay will be granted, are likely to stall their compliance efforts, which the Department is then likely to point to as the justification to delay.”²

Just as we anticipated, the Department has relied on that reasoning in this proposal. In its Regulatory Impact Analysis for the proposal, for example, the Department states that firms “are encountering uncertainty regarding the potential future revision or possible repeal of the Fiduciary Rule and PTEs. Therefore, as reflected in the comments, many financial firms have slowed or halted their efforts to prepare for full compliance with the exemption conditions that currently are scheduled to become applicable on January 1, 2018, because they are concerned about committing resources to comply with PTE conditions that ultimately could be modified or repealed. The proposed applicability date extension will assure stakeholders that they will not be subject to the other exemption conditions in the BIC and the Principal Transaction PTEs until at least July 1, 2019.”

The use of the words “until at least July 1, 2019” also suggests that the Department is prepared to provide further extensions to relieve the industry of having to comply with the full requirements of the rule. This reinforces the view that the Department really isn’t providing a temporary and circumscribed delay so much as an indefinite stay. This provides strong evidence that the Department’s real purpose behind this proposal is to eliminate, through an end run, the operational requirements of the PTEs that ensure compliance with and enforcement of the Impartial Conduct Standards.

² Letter from Micah Hauptman and Barbara Roper, CFA, to the DOL, July 21, 2017, <http://bit.ly/2jvTbZV>.

The reasoning and the exact structure of the “delay” action appear to be merely a means to an end. As discussed above, the Department’s stated reasoning for a “delay” here has changed drastically from the reasoning that the Department provided in its RFI. In addition, the Department seems to express a certain ambivalence in the proposal about the exact structure of the “delay.” While the Department proposes a time-certain “delay” of 18 months that has no rational connection to any concrete purpose or event, it also seeks comment on a variety of other approaches, including a “delay” that would end a specified period after a certain action on the part of the Department, and a tiered approach in which the “delay” would last until the earlier or the later of a) a date certain or b) the end of a period following the occurrence of a defined event. These various alternatives demonstrate the fact that the exact amount of time for the “delay” and the nature of how the “delay” is formulated are incidental details to the Department’s main objective, to ensure the industry is never subject to provisions of the rule designed to ensure its enforceability.

As we’ve discussed in previous comments, statements by Trump Administration officials support the view that this Administration is embracing the industry rule opponents’ baseless criticisms of the rule.³ More recently, Secretary Acosta stated in a *Wall Street Journal* op ed that “the Fiduciary Rule as written may not align with President Trump’s deregulatory goals.”⁴ He then echoed industry rule opponents’ claims against the rule, further suggesting that he has embraced their position. He stated, for example, “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.”⁵ His statements reflect neither a willingness to understand the nature and extent of conflicts of interest in the retirement investment advice market, nor an appreciation for the purposes underlying the rule and its exemptions.

³ See, e.g. statement by then White House spokesman Sean Spicer during a press briefing to announce the signing of the Presidential Memorandum. The White House, Office of the Press Secretary, Press Briefing by Press Secretary Sean Spicer, Feb. 3, 2017, <http://bit.ly/2lbwoyS> (calling the rule “a solution in search of a problem” and echoing industry rule opponents’ favorite talking point, that “its effect has been to limit the financial services that are available to” retirement savers. Spicer also restated as if it were fact industry’s contention that the Department had overstepped its authority in promulgating the rule, an argument that has been soundly debunked in four court decisions). See also statement by White House National Economic Director Gary Cohn, Lisa Beilfuss and Michael Wursthorn, *Trump Moves to Kill Off Obama’s Landmark Retirement Rule*, THE WALL STREET JOURNAL, Feb. 3, 2017 <http://on.wsj.com/2jFvgqZ> (using a tortured analogy suggesting that the rule was harming retirement investors by depriving them of access to “unhealthy” retirement investments. See also statement by an unnamed senior White House official to Time Magazine Zeke J Miller and Haley Sweetland Edwards, *White House Stalls Obama Administration Rule on Retirement Advisers*, TIME, Feb. 2, 2017 <http://ti.me/2l2sWr5> (stating that the rule had “taken away a huge variety of investment options for individual investors.” The official continued, stating, “We actually think we’re giving consumers back what they want,” this individual reportedly stated, “which is the ability to invest in a variety of asset classes,” adding, “I don’t think you protect investors by limiting choices.”)

⁴ Alexander Acosta, *Deregulators Must Follow the Law, So Regulators Will Too*, Wall Street Journal, May 22, 2017, <http://on.wsj.com/2q57jwk>.

⁵ *Id.* See also statement by DOL Nominee Acosta to Senator Elizabeth Warren, that, “The [fiduciary] rule goes far beyond simply addressing the standard of conduct.” John Hilton, *DOL Nominee Stands Up to Sen. Warren on Fiduciary Rule*, INSURANCENEWSNET, March 22, 2017, <http://bit.ly/2h6v53L>.

In short, the evidence suggests that the Department has already embraced the industry rule opponents' claims and decided that it is more important to protect the industry from incurring potentially unnecessary compliance costs under the rule than to ensure retirement savers are protected from conflicts of interest that drain their retirement security. If, despite what the evidence suggests, the Department genuinely maintains an open mind about the reexamination, the mere possibility that firms "may" incur undue expenses to comply with conditions that "may be" revised, repealed, or replaced is much too speculative a justification for such an economically far-reaching regulatory action that leaves retirement savers vulnerable to abuse.

III. The Department has provided a completely shoddy economic analysis that fails to justify this proposed action.

Without any factual basis, the Department states that it "believes that investor losses from the proposed transition period extension could be small," because "the Department believes that firms already have made efforts to adhere to the rule and [Impartial Conduct Standards.]" First, it's not clear what "small" means, because the Department doesn't attempt to quantify it. More troubling, the Department provides no verifiable evidence to support those beliefs. The Department states that, "Comments received by the Department indicate that many financial institutions already have completed or largely completed work to establish policies and procedures necessary to make many of the business structure and practice shifts necessary to support compliance with the Fiduciary Rule and Impartial Conduct Standards..." The Department provides no explanation or analysis of who these "many" financial institutions are or how representative they are of the industry. And statements from market participants suggest that the Department's beliefs may not comport with market realities. While some firms surely are taking their compliance obligations seriously and moving in good faith to come into compliance, that is not the case throughout the retirement investment advice industry.

In our comment responding to the RFI, we cited a statement by Envestnet, Inc. Chairman and CEO Judson T. Bergman, who contrasted the more "compliance minded" firms that are adopting new programs to comply with the rule in the IRA market from those who are "back to the way it was earlier."⁶ According to Bergman, "Most independent broker dealers are not rushing to implement any new DOL or fiduciary compliant programs, rather they are allowing advisors to continue to do their business, as they've always done it."⁷ Similarly, Pershing's managing director of investment and retirement solutions Robert Cirotti stated, "I think there are still pockets of the industry that suspended either their implementation or their belief that this thing was actually going to take effect. I think that really puts them behind the eight ball. On the flip side of that, there are plenty of other firms that are well prepared."⁸

More recently, it was reported in *InvestmentNews* that a number of brokerage firms still have not completed compliance projects relating to rationalizing broker compensation and culling investment products from platform shelves.⁹ Several firms suggested that, with a delay,

⁶ Envestnet (ENV) Q1 2017 Results - Earnings Call Transcript, SEEKING ALPHA, May 10, 2017, <http://bit.ly/2vbbZQ9>.

⁷ *Id.*

⁸ Diana Britton, *DOL in the Real World*, WEALTHMANAGEMENT.COM, June 19, 2017, <http://bit.ly/2tAwYgm>.

⁹ Greg Iacurci, *Anticipating delay to DOL fiduciary rule, broker-dealers and RIAs change course*, INVESTMENTNEWS, August 16, 2017, <http://bit.ly/2vGvqm5>.

they would likely put off these projects. “They now get to push [compliance] off into the horizon, and the horizon is kind of beyond vision,” said Daniel Bernstein, chief compliance counsel at the consulting firm MarketCounsel.¹⁰ According to one brokerage executive who requested anonymity due to his firm’s policy regarding speaking publicly about the rule, “Our initial reaction is, everything we were planning on doing in January, we will review all of those things and see if we want to continue to do them in January or just put them off...I think in most cases we’ll put them off.”¹¹

Adviser compensation is the most direct mechanism firms employ to structure advisers’ incentives in ways that encourage and reward advice that is not in clients’ best interest. Refusing to change these critical incentives raises serious questions about whether firms truly are reining in conflicts of interest and whether advisers are able to meet their obligations under the Impartial Conduct Standards in the face of these conflicts of interest. In addition, to the extent firms maintain investment menus with products that don’t meet due diligence standards, it creates the potential for advisers to recommend funds that do not comply with the Impartial Conduct Standards. The potential for violations of the Impartial Conduct Standards increases if the sale of such products results in higher compensation to the adviser and firm. However, without an administrable enforcement mechanism, there will be no avenue for retirement savers to recover the resulting losses from these violations.

We also understand, based on conversations with industry participants, that substantial pockets within the insurance annuity industry are resistant to changing their practices in meaningful, pro-investor ways. We understand, for example, that many firms and advisers in this space assume that the rule is temporary. Instead of spending resources to meaningfully root out conflicts of interest and improve recommendations, they have spent minimal resources to put in place perfunctory procedures that are largely outcome-determinative and serve only to justify the recommendations that they would’ve made anyway. Their ability to get away with practices that flout the requirements of the Impartial Conduct Standards results from both the lack of an effective enforcement mechanism and the Department’s non-enforcement policy.

While it is difficult to know the extent to which firms are complying with the Impartial Conduct Standards and delivering corresponding gains to investors, it is irrational to assume, as the Department has done in this proposal, that “a substantial portion of the investor gains predicted in the Department’s 2016 regulatory impact analysis of the Fiduciary Rule and PTEs (2016 RIA) would remain intact for the proposed extended transition period.” First, just as it is unclear what the Department means when it says it “believes that investor losses from the proposed transition period extension could be small,” it is equally unclear what the Department means when it says “a substantial portion of the investor gains...would remain intact” because the Department hasn’t attempted to quantify them. And, as we discussed above, this assumption appears to be at odds with market realities.

Moreover, this assumption is contradicted by the Department’s previous analysis, which found that the enforcement provisions scheduled to kick in January 1, 2018 are “critical” to ensuring compliance with the protective provisions of the rule and the corresponding gains to

¹⁰ *Id.*

¹¹ *Id.*

investors.¹² Without an effective accountability and enforcement mechanism, particularly for the IRA market, the requirements of the BIC and Principal Trading Exemptions would be effectively toothless. There would be no administrable means of ensuring compliance and enforcing the Impartial Conduct Standards if they are violated.¹³ Moreover, absent the contract requirement and the legal enforcement mechanism that goes with it, firms would no longer have a powerful incentive to comply with the Impartial Conduct Standards, implement effective anti-conflict policies and procedures, or carefully police conflicts of interest, according to the Department.¹⁴ It could be too easy for firms to claim that they are complying with the PTEs, but still pay advisers in ways that encourage and reward them for non-compliance.

As discussed above, that appears to be what is happening in some segments of the industry, which likely includes firms whose compensation structures are the most laden with acute conflicts of interest and who, not coincidentally, have been the most hostile to the rule. It is these firms that the Department is disproportionately benefiting and it is these firms' customers that the Department is disproportionately harming with this proposal. The Department even recognizes this fact, stating, "the benefits of extending the transition period generally will be proportionately larger for those firms that currently have committed fewer resources to comply with the full exemption conditions." This statement also underscores the importance of the enforcement provisions because, the firms that haven't taken seriously their January 1, 2018 compliance obligations likely also haven't been taking seriously their compliance obligations under the Impartial Conduct Standards. Only a meaningful and administrable enforcement mechanism will ensure that everyone fully complies with the rule's protective conditions.

In addition, while the Department recognized in its 2016 RIA that there was uncertainty regarding the anticipated investor gains from the rule and related exemptions, which depended upon the extent to which firms comply with the rule's protective conditions, the Department doesn't acknowledge the same uncertainty here with regard to the potential for lack of compliance.¹⁵ As discussed above, the full provisions provide a powerful incentive for firms to comply with the Impartial Conduct Standards. However, without that powerful incentive to comply, as is contemplated under this proposal, there is greater likelihood that the Department's anticipated investor gains decrease. As the Department stated in its 2016 RIA, "If advisers were to fail to adhere to the protective conditions, including conditions that prohibit compensation practices and employment incentives that are intended or would reasonably be expected to compromise advisers' impartiality, then anticipated gains to retirement investors and other economic benefits would be reduced."¹⁶

¹² See Letter from Barbara Roper and Micah Hauptman, CFA, to the DOL, August 7, 2017, at 29-36, <http://bit.ly/2fa6Ggy>. (citing the DOL's 2016 RIA and preamble, which directly addressed the full provisions of the rule that are scheduled to become applicable on January 1, 2018) (including RIA at 289, stating, "The Department remains convinced of the critical importance of the core requirements of the exemption, including an up-front commitment to act as a fiduciary, enforceable adherence to the impartial conduct standards, the adoption of policies and procedures reasonably designed to assure compliance with the impartial conduct standards, a prohibition on incentives to violate the best interest standard, and fair disclosure of fees, conflicts of interest, and material conflicts of interest.")

¹³ BIC at 21022.

¹⁴ *Id.*

¹⁵ See RIA at 303-306.

¹⁶ RIA at 303.

The Department specifically recognized that the effectiveness of the rule and the corresponding estimated gains to retirement investors were contingent on the exemptions' conditions being "fully phased in" and that "some gaps in effectiveness are likely during the months after the final rule and exemptions become applicable but before some of the protective PTE conditions take effect."¹⁷ For example, the Department estimated that, "If the rule and exemptions are only 50% effective in the first year following the initial applicability date (which includes an approximately nine-month transition period when some Best Interest Contract Exemption provisions are not yet in effect), the quantified subset of gains – specific to the front-load mutual fund segment of the IRA market – would amount to between \$30 billion and \$33 billion over 10 years." That amounts to a \$3 billion loss to retirement savers over 10 years, as compared with the Department's estimate of the full gains of \$33 billion to \$36 billion over 10 years. Based on the assumption that the exemptions are only 50% effective because the full protections of the rule won't be applicable for more than 2 years, rather than 1 year, the estimated losses to retirement savers would be considerably larger than \$3 billion. Moreover, as discussed above, because some firms are treating the Impartial Conduct Standards as temporary and are not spending resources to meaningfully change their behavior, it is even less likely that the Impartial Conduct Standards, without an administrable enforcement mechanism or a requirement for firms to rein in incentives that encourage and reward harmful advice, will fully mitigate adviser conflicts of interest.

In addition, as the Department's 2016 RIA made clear, the estimated quantified gains reflected an assessment of only a fraction of potential conflicts, associated losses, and affected retirement assets. According to the Department, "The quantified investor gains alone dramatically understate the total gains expected under the final rule and exemptions, albeit by an uncertain amount."¹⁸ However, the unquantified gains, similar to the quantified gains, are seriously in doubt without an effective mechanism to ensure compliance with the exemptions' protective conditions. For example, IRA recommendations of variable and fixed-indexed annuities, non-traded REITs, and other assets that are typically subject to acute conflicts of interest but are not included in the Department's quantified estimate of harm could continue to be subject to conflicts of interest and resulting losses for retirement savers. Similarly, excessive markups and markdowns on principal trades could go undeterred.

The losses investors suffer from this regulatory action will not be recouped. As the Department stated in its previous proposal to delay the rule, but failed to acknowledge in this proposal, "While losses would cease to accrue after the funds are re-advised or withdrawn, afterward the losses would not be recovered, and would continue to compound, as the accumulated losses would have reduced the asset base that is available later for reinvestment or spending." The Economic Policy Institute has estimated that the unrecoverable losses to retirement savers over the next 30 years that could result from another 18 month period in which the full protections of the rule are not applicable could be between \$5.5 billion and \$16.3 billion, with a middle estimate of \$10.9 billion.¹⁹ Based on these estimates, there is no reasonable basis on which the proposal can be economically justified.

¹⁷ RIA at 304.

¹⁸ RIA at 305.

¹⁹ Heidi Shierholz, EPI comment on the proposed 18 month delay of key provisions of the fiduciary rule, Economic Policy Institute, September 11, 2017, <http://bit.ly/2fbNFKW>.

IV. The Department has not made and indeed cannot credibly make its required showing under ERISA and the Code to grant these administrative exemptions.

There is yet another significant procedural and substantive infirmity with this proposal. Before granting or modifying an exemption under ERISA and the Code, the Department must find that the exemption is administratively feasible, in the interests of plans and their participants and beneficiaries and IRA owners, and protective of the rights of participants and beneficiaries of plans and IRA owners.²⁰ The Department has not even attempted to make a preliminary finding here, nor could it without disregarding its previous analysis and findings and engaging in other irrational actions.

V. We strongly urge the Department to reconsider its regulatory approach.

We strongly urge the Department to reconsider its approach and implement the full protections of the rule so that working families and retirees finally benefit from the meaningful, legally enforceable best interest standard they so desperately need and deserve. Providing certainty by stating unequivocally that there will be no more delays will benefit not only retirement savers, but also industry participants who are willing to serve their clients' best interest and compete based on cost and quality, firms that have moved forward responsibly to develop pro-investor implementation plans, and small businesses that have built technology solutions for compliance with the rule.

Should the Department decide to finalize the extension of the transition period, on the grounds that it is more important to protect firms' bottom lines than to protect retirement savers from conflicts of interest, at a bare minimum, the Department must require firms and advisers to comply with the original transitional requirements of the exemptions, as set forth in Section IX of the BIC Exemption and Section VII of the Principal Transactions Exemption, not just the Impartial Conduct Standards. These include: 1) the minimal transition written disclosure requirements in which firms acknowledge their fiduciary status and that of their advisers with respect to their advice, state the Impartial Conduct Standards and provide a commitment to adhere to them, and describe the firm's material conflicts of interest and any limitations on product offering; 2) the requirement that firms designate a person responsible for addressing material conflicts of interest and monitoring advisers' adherence to the Impartial Conduct Standards; and 3) the requirement that firms maintain records necessary to prove that the conditions of the exemption have been met.

These requirements will help better apprise retirement savers of the nature of the advisory relationship and the duties that will be owed to them. Should the Department revise or rescind the rule and exemptions, including changing the scope or nature of the fiduciary relationship or conditions of the exemptions, we expect that firms would be required to provide further clarification regarding the nature of the relationship, the services being provided, and the duties owed. Doing so would help reduce investor confusion and assist customers in making more informed choices, which is consistent with the task set forth in the Presidential Memorandum.

²⁰ 29 U.S.C. 1108(a); 26 U.S.C. 4975(c)(2).

Respectfully submitted,

A handwritten signature in cursive script that reads "Micah Hauptman".

Micah Hauptman
Financial Services Counsel

A handwritten signature in cursive script that reads "Barbara Roper".

Barbara Roper
Director of Investor Protection