SIFMA DOL Fiduciary Seminar: Assessing the Intended and Unintended Consequences
Remarks: The Industry View
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Good morning. I am Ken Bentsen, president and CEO of SIFMA. I want to thank you all for joining us at the SIFMA Conference Center today as we discuss a very complex but extremely consequential matter. I want to take a moment to thank all of our panelists who have taken the time to present today and my staff and colleagues, in particular Lisa Bleier and Jillian Enoch. And of course thank all of you both in the room and by web for participating.

Today we are taking a deep dive into the mechanics of the Department of Labor's proposed amendments to ERISA: How it works, or in our perspective, how it doesn't work; what are the intended and unintended consequences; and as written, what will this mean for firms and most importantly the clients you all serve.

As we've watched this rule progress from its initial proposal (and withdrawal) in 2010 through its re-proposal earlier this year, it's no secret that the industry has been in disagreement with the rule's proponents on a host of levels.

The fact of the matter is, the discussion or debate around the Department of Labor proposal is not about who is for or against a best interests standard. That question has been asked and answered.

SIFMA's members, who provide multiple services in both retail and institutional markets, including commission based brokerage services under the Securities Exchange Act of 1934 and fee based investment advisory services under the Investment Advisors Act of 1940, long ago endorsed a best interest or uniform fiduciary standard of care for all retail investors, including the retirement sector, when providing personalized investment advice. In fact, we endorsed it before Congress enacted Section 913 of Dodd-Frank, or the Department published its originalproposal. We have subsequently made our position very clear in comment letters to the SEC in 2010, 2011, 2012 and 2013, as well as to the Department in 2010 and 2011.

To this day, SIFMA continues to strongly support the SEC taking action under Section 913 of Dodd-Frank as it recommended in its 2011 report to Congress and we applaud SEC Chair White's support for rulemaking under Section 913.

While the SEC continues its important work in this regard however, it is worth noting that the rules and precedents governing broker-dealers conduct with respect to retail investors, both in retirement and non-retirement accounts, have been migrating toward a best interests standard. FINRA, on behalf of the SEC, has been increasingly refining its definition of suitability under Rule 2111 and most recently through guidance related to 401(k) and similar plan rollovers under Regulatory Notice 13-45 to require brokers to put clients' best interests ahead of their own. Further, investor claims in FINRA arbitration routinely include a fiduciary duty component.

To underscore this point, just last week at FINRA's annual compliance conference in Washington, FINRA chairman and CEO Rick Ketchum outlined his goal for the broker-dealer industry to adopt a best interests standard with core elements to ensure that customers' interests do indeed come first. Mr. Ketchum also detailed his practical concerns with the Department of Labor's proposal and stated "the current Labor proposal is not the appropriate way to meet that goal." Rather, Mr. Ketchum said that a broker-dealer best interests standard should be established under the securities laws, building upon "the effectiveness and fundamental integrity of the present FINRA/SEC regulatory structure." SIFMA's members agree with Mr. Ketchum – and in fact we even agree with the DOL - that there should be a best interests standard. To that end and in furtherance of our long established position and out of concern that policy makers are headed down separate and inconsistent paths, SIFMA today is proposing a "Best Interests of the Customer Standard for Broker-Dealers", which can serve as an investor-focused, comprehensive regulatory solution that works.

We believe that an optimal "best interests of the customer" legal standard for broker-dealers should do the following:

1. Apply across *all* investment recommendations made to individual retail customers in *all* brokerage accounts (not just limited to IRA accounts);

2. Serve as a benchmark for, be consistent with, and integrate seamlessly into, the SEC uniform fiduciary standard that ultimately emerges under Dodd-Frank § 913;

3. Provide interim, strong, substantive, "best interests" protections for retail customers; and

4. Follow the traditional securities regulatory approach of establishing a rules-based heightened standard, including robust disclosure, coupled with robust examination, oversight, and enforcement by the SEC, FINRA and state securities regulators, as well as a private right of action for investors, as exists today.

We believe that this standard could be articulated, for example, through amendments to existing FINRA Rules, as approved by the SEC. The standard would include the following core elements:

1. Articulate a legal and enforceable best interests obligation;

2. Consider investment-related fees as part of the best interests standard;

3. Avoid and/or manage material conflicts of interest; and

4. Provide disclosures about material conflicts and investment-related fees to enhance transparency.

Our proposed solution is consistent with SIFMA's historical position, Section 913 of Dodd-Frank, the evolution of a best interests regime under FINRA Rules, and the DOL's specific definition of a best interests standard under the proposed Best Interest Contract Exemption. As such, we believe our proposal outlines the broad contours of how a best interests standard for broker-dealers might be developed as part of the path forward on this most important investor protection issue in regards to Section 913 rulemaking and any consideration by the DOL, which should be consistent.

So as I've stated, the debate is not if, but how we should implement such a standard. In our view, such standard should be consistent across the entire retail market. It should be consistent with the intent of Congress as defined in Section 913 of protecting investors and investor choice.

Our concern with the Department of Labor's proposal therefore is not with its definition of "best interest," for as I stated we support such a standard as I've laid out today. Rather, it is the further conditionality and restrictions on investors that the Department seeks to impose on top of and beyond that standard that we believe is extraneous, burdensome and perhaps ultimately in practice inconsistent with the best interests of the client.

While we have many concerns with the proposal, let me raise just a few points.

The DOL's proposed definition of who is a fiduciary is very broad - encompassing many more activities as was ever intended, or that the Department originally proposed in 2010. For example, the seller's exception for the previous version allowed brokers to market their products and activities to retail customers. This time around, there is no seller's exception to market one's services or products to a retail customer or even to sell a plan to a small business owner.

In addition, while there is an education exception to being a fiduciary, it is more narrowly crafted than the education bulletin that has been in place since 1996. Under the current proposal, one can no longer name any specific investments without the activity becoming a fiduciary activity.

The Department's mechanism by which the rule could be business model neutral and allow for commission based accounts, the Best Interest Contract Exemption, contains so many conditions and restrictions that our members believe it is unworkable as drafted.

This is material as the vast majority of IRAs, and for that matter all retail accounts, are held in commission brokerage accounts. Investors routinely choose between commission brokerage and fee based managed accounts, most of our members offer both, and investors have overwhelming chosen brokerage, particularly for IRAs.

The Best Interest Contract Exemption would subject firms and advisors to a new legal liability (on top of existing legal liability), explicitly limit investor choice of product, impose level fees at the firm level and thus seek to set market prices and require firms to develop and build unprecedented new disclosure and compliance regimes, some of which may well conflict with other securities laws. Because of the increased liability risks and compliance costs, firms have indicated that the safer course of action would be to migrate most commission brokerage accounts to fee based accounts that in most cases are exempt from the rule.

However, as stated fee based accounts cost the investor more than commission brokerage accounts. And, because of the higher service and compliance costs associated with fee based accounts, most firms limit such accounts to higher balanced accounts, thus potentially leaving millions with no option for advice or guidance. Further, the SEC has questioned whether higher cost fee based accounts are always in the clients' best interests, particularly buy and hold investor, which creates a conundrum. And, perhaps most importantly, clients have largely already made the choice of the type of account they wish to purchase, a choice they may be forced to lose.

Ironically, in the Department of Labor's regulatory impact analysis accompanying the rule and a previous Council of Economic Advisors' study in support of the rule, a study that we believe is seriously flawed including its asserted cost which is not supported by the research cited in the report, the Department cites the recent experience in the United Kingdom through its Retail Distribution Review in support of its effort. However, if you read the UK's own analysis of the

RDR cited, you will find that more than 300,000 investors have lost service from brokers, 60,000 new clients turned down as the cost of advice has risen and firms have established account balance thresholds of 50,000 GBP. So in our view, the UK experience should be a warning as to the potential for unintended consequences.

We believe the Labor Department's proposal goes far beyond such a best interests standard to limit choice and raise costs, unnecessarily so in our opinion. Equally troubling is that this experience underscores a failure in the public policy market place. Rather than adopting a policy prerogative that will apply consistently across the entire retail market place, we are headed in a direction of bifurcated rules, compliance and disclosure regimes imposed on the same market participants from different regulators. It is hard to see how investors won't be confused and the industry forced to build duplicative and redundant systems that will further affect costs. It seems illogical that we cannot address this in a uniform manner.

I want to reiterate that this is not about being for or against the best interests standard. The industry's position in support of such a standard is quite clear and well documented before, and on today. Rather it's how you do it, and it is there where we have an issue.

Thank you for taking the time to participate in this seminar on such an important issue.

At this time, we're going to take a quick break before we dive deeper into the inner workings of the proposed rule and its impact on the retirement system and ultimately the retirement investors you all serve.

Thank you.