<u>REQUEST TO TESTIFY</u>

To the Employee Benefits Security Administration

Re: Docket No. EBSA–2023–0014: Hearings, Meetings, Proceedings etc.: Retirement Security Rule; Definition of an Investment Advice Fiduciary and Associated Prohibited Transaction Exemption Amendments

Name:	Ron A. Rhoades, JD, CFP®
Title:	Associate Professor of Finance and Director of the Personal Financial Planning Program, Gordon Ford College of Business, Western Kentucky University; and Principal, Scholar Financial, LLC, a fee-only registered investment adviser
Address:	1441 Riva Ridge Ave., Bowling Green, KY 42104
Phone:	352.228.1672
Email (preferred):	ron@scholarfinancial.com

Organization:	(N/A) My testimony will not represent the views of any institution, firm, organization, motley crew, gang or cult with whom I am presently associated or have ever been kicked out of.
Written Comments:	Not yet submitted.

Outline of Testimony:

1) I review the requirement that all choices in defined contribution plans governed by ERISA meet the requirements of the prudent investor rule, a tough standard of care which requires adequate diversification to minimize certain risks, not wasting plan participants' assets through high-fee/high-cost investments, and the minimization of the long-term tax drag upon investment returns.

2) The argument made by some broker-dealer firms, asset managers, and insurance companies that the DOL's rulemaking limits "choice" is a *red herring*. By its very nature, the fiduciary duties imposed by ERISA constrain conduct, and by doing so counter greed. The U.S. Supreme Court, when opining on ERISA's prudent investor rule, concluded that bad investment choices have no place in retirement plan accounts. Defined contribution plan accounts benefit from economies of scale, that should not be thwarted by high-cost products. The academic evidence is clear - higher-cost products underperform, on average, similar investments that have lower fees and costs.

3) The DOL's rule proposals align with the common law imposition of fiduciaries for those in relationships of trust and confidence between the fiduciary and the entrustor. Very few plan sponsors are experts as to investment strategies and products. Plan sponsors rely upon those who provide recommendations as to investments and annuities for their expertise. Most "retirement plan consultants" implicitly accept the imposition of

fiduciary duties under common law principles through their titles, words and conduct. Yet many of these retirement plan consultants provide conflicted advice, or, even worse, provide illusory "fiduciary guarantees" that are meaningless. Plan sponsors, and plan participants, deserve the protection of fiduciary advice, and more importantly conflict-free investment recommendations.

4) The DOL should go further:

    a. Plan sponsors, who are fiduciaries, should be cautioned to always engage only fiduciaries as investment consultants who proactively eschew conflicts of interest. A true fiduciary avoids revenue-sharing payments and other third-party compensation that create nefarious conflicts of interest, in recognition of the fact, as many a jurist has opined, that a fiduciary cannot serve two masters.

    b. The DOL should encourage providers of investment solutions to defined contribution plans where both "traditional" and "Roth" options exist to develop and implement tax-efficient asset placement, so as to adhere to the prudent investor rule's often-overlooked requirement to minimize the tax drag upon investment returns. The DOL should encourage providers to address this often-overlooked requirement of the prudent investor rule through software solutions that undertake tax-efficient asset placement and/or through plan participant education.

    c. The DOL should encourage plan sponsors to realize that the decision to annuitize a portion of a retiree's nest egg is not merely the choice of an annuity product but is rather a key lifetime financial planning decision. Considerations before annuitization involve health / genetics / estimated longevity of the retiree (and spouse), the presence of debt, both present and future cash flow needs, the interplay with the participant's (and spouse's) strategy to maximize the utility of Social Security retirement benefits and/or pension benefits, the desire or need of the retiree (or couple) to provide support to other family members (including by means of inheritance), the presence of other assets or resources, the risk tolerance and capacity of the client, the current interest rate environment, whether inflation adjustments occur over time with annuitization, and the current expected returns of various asset classes given valuation levels in the capital markets. Even when annuitization, following this complex financial planning process, is to be undertaken, annuities should be competitively shopped, as payout rates change frequently among insurers. Strong consideration should be given to the financial strength of the insurer and the presence (and limitations of) state guaranty programs. Moreover, given the emergence of immediate annuities with no commissions, the DOL should encourage plan sponsors to entertain proposals from fiduciary (trusted, expert) and completely independent financial advisors (even going so far as to exclude those who manage investment portfolios for a fee) for flat or fixed fee engagements for the annuitization analysis. Should annuitization be undertaken, such independent fiduciary advisers should be charged with the conduct of proper due diligence in the current marketplace to obtain the best possible annuitization solution(s) for the plan participant. To avoid conflicts, payment for such flat fee(s) for the annuitization analysis, and the subsequent choice of annuity(ies), should be paid from the defined contribution account, with the fiduciary adviser not receiving any third-party compensation.

d. While the theory behind the investment strategy underlying fixed index annuities has some academic support, the implementation of that strategy by insurance companies is heavily flawed. I suggest that non-commissioned fixed index annuities, with no surrender fees and with other structural changes that limit the compensation received by insurance companies, could be developed that would serve a useful purpose in retirement portfolios.

e. I further suggest that variable annuities only "win" when the variable annuity product's investments miserably fail over shorter periods of time. Over long periods of time high-cost, high-fee variable annuities with "downside protection" and "guarantees" upon annuitization nearly always are poor investment solutions. Given the availability of other investment and annuity strategies to limit downside risk there is little justification for the use of variable annuities in defined contribution plans (or elsewhere).

f. I suggest that the decades-long movement to limit the number of funds in any defined contribution plan to 20, or even 30, is based on outdated research, given the rise of target date funds as well as developments in modern academic research into investment strategies and better discernment of the risks and potential range of returns for various asset classes. I further suggest that most ERISA-governed defined contribution plans fail to adequately diversify among asset classes by not including low-cost multi-factor funds (based upon sound academic evidence) in U.S., foreign developed, and foreign emerging markets, and/or by excluding other asset classes which can enhance investors' portfolios. The arbitrarily imposed limits on the number of funds within defined contribution plans pose a potential violation of the prudent investor rule, and the plan sponsor's duty of care, generally. I encourage plan sponsors, and the DOL using its survey and information-gathering capabilities, to re-visit the requirement of diversification among asset classes in order to ensure that asset classes worthwhile of inclusion into plan lineups not be excluded, in order that plan participants (and their investment advisors) are afforded the opportunities to maximize the expected returns, and/or seek steps to minimize risks, through properly diversified portfolios applying evidence-based investment techniques.

Respectfully submitted,

Ron A. Rhoades