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Conflict of Interest Proposed Rule

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U.S. Department of Labor (DOL)

Employee Benefits Security Administration (EBSA)

I want to thank the panel for allowing me the opportunity to speak today. I also want to thank you personally for the time and effort you have exerted, and will continue to exert, in crafting this rule, which is *clearly* intended to protect American consumers as they prepare for retirement.

My name is Benjamin Cummings. I am an assistant professor of financial planning at Saint Joseph's University in Philadelphia, where I also serve as the academic liaison for our CFP Board-registered financial planning program. I have also obtained my CERTIFIED FINANCIAL PLANNER™ certification. Although I will echo the thoughts of others who have spoken and written about this issue, the thoughts I express today are my own. In large part, I agree with the proposed rule, although I do see some areas for improvement.

I come today out of concern for consumers of individualized advice regarding retirement assets. I also come out of concern for seniors, who are especially vulnerable to expensive and complex financial products that can be difficult to reverse. Lastly, I am also concerned for the taxpayers who forego tax revenues in an effort to encourage individuals to save through tax-sheltered retirement accounts, like 401(k) plans and IRAs. The intent of these accounts and their favorable tax treatment is to enhance the retirement savings and preparedness of Americans. However, excessive rent extraction can create a significant drain on accumulated assets.

At the same time, the financial products available to consumers within these retirement accounts can be complex, and many individuals benefit from the assistance of a financial professional. Yet it's well established that the advice they receive may not be in their best interest, and evidence is widely cited that investors are confused about the duties of care to which financial professionals are held.

As these points have been widely discussed, I would like to focus my comments on areas that, in my opinion, may benefit from additional attention. First, I want to briefly reiterate what others have said regarding what I argue is an unfounded claim that the rule will limit access to financial advice for middle-income households. In their comment letter for this proposed rule, The Financial Planning Coalition (2015) cites considerable evidence to the contrary. To highlight just one of their examples, in a study of advisors who are personally familiar with operating under a suitability standard and a fiduciary standard, 80% report either an *increase*, or at minimum, no change in the range of services when operating under a fiduciary standard. To suggest that providers who are willing to operate under a fiduciary standard could not easily fill any potential gap left by advisors who are unwilling to rise to the occasion seems rather naïve.

Second, I would like to emphasize the importance of incentivizing financial services firms to better align policies, training, and supervisory practices with the interests of their clients. Much emphasis has been given on the need to align the incentives of advisors with the interests of their clients, but less attention has been given to the culture of the firms which employ advisors.

Currently, many firms recognize the conflicts of interest that exist for their advisors, yet they do little more than disclose those conflicts. For example, in their comment letter related to this rule, the Financial Planning Coalition cites part of a Form ADV of a large financial services firm. The Form states that the firms' advisors have a "conflict of interest based on an incentive to recommend investment products based on the compensation received, rather than based on your needs." (Financial Planning Coalition, 2015, p.7) The Financial Planning Coalition also references the code of conduct of a large insurance firm, which "states that rather than acting in the client's best interest, Advisers must act in the best interest of the firm." (Financial Planning Coalition, 2015, p.7) The proposed rule is certainly an attempt to align the incentives, not only of advisors and their clients, but also of firms and the clients of their advisors.

To aid firms in the desired direction, I draw from legislation passed by the Washington state legislature, in which they define the standard of care for medical professionals as "that degree of skill, care, *and learning* possessed at that time by other persons in the same profession" (RCW 4.24.290, emphasis added). I emphasize the learning aspect, which is imperative when providing expert advice on complex subjects, like medicine. Similarly, I believe that one way financial firms can be incentivized to better align their interests with those of their clients is to provide guidance about the training and educational attainment required of their advisors, especially when they provide advice regarding complex financial products. Too often, advisors provide advice about and promote the sales of products that they do not fully understand themselves. If advisors do not fully understand the products they sell, financially unsophisticated clients certainly cannot be expected to make fully informed decisions about such financial products. Most importantly, I question how such an uninformed advisor can act in the best interest of their client.

Third, I am concerned about the continued allowance for financial services firms to require mandatory pre-dispute arbitration clauses. In an article in 2010, Arthur Laby, who testified before this panel yesterday, commented, "Unlike court litigation, arbitration generally does not yield a well-reasoned written decision" (Laby, 2010, p. 706). According to recent data from FINRA (2015), breach of fiduciary duty is consistently the leading controversy involved in arbitration cases, yet little is divulged about the legitimacy of the claims or the resolutions of the cases. This lack of transparency makes it difficult to identify whether investors achieve some sort of financial restitution as a result of these claims. Allowing firms to require arbitration in cases involving breach of fiduciary duty as it relates to registered representatives of a broker-dealer has led to what Laby (2010) argues is "an underdeveloped jurisprudence" (p.710).

Another concern about mandatory arbitration is that, depending on the regulatory regime of the advisor, investors in retirement plans may have access to only one of two rather dissimilar routes to seeking redress for allegations against an advisor, yet few consumers realize the distinction. This spring, the Consumer Financial Protection Bureau (CFPB, 2015) did a study on the impact of arbitration cases and found that:

> *"…more than 75 percent of consumers surveyed did not know whether they were subject to an arbitration clause in their agreements with their financial service providers, and fewer than 7 percent of those covered by arbitration clauses realized that the clauses restricted their ability to sue in court."*

The CFPB study also finds "no evidence of arbitration clauses leading to lower prices for consumers" (CFPB, 2015). With little evidence of its benefit to investors, I question the value of continuing to allow financial services firms to use mandatory pre-dispute arbitration clauses.

To conclude, the main concerns I hope to address today are:

1. Claims that the proposed rule will limit access for middle-income households to receive individualized advice are unfounded. To the contrary, considerable evidence suggests that services either remain the same or increase under a fiduciary standard.
2. Only educated and well-informed advisors are capable of providing quality advice in the best interest of their clients. Firms need regulatory incentives to properly train and educate their advisors.
3. Allowing firms to continue the use of mandatory pre-dispute arbitration clauses limits the benefit of the proposed rule.

That concludes my comments. Thank you again for your time.

References

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