



January 14, 2011

U.S. Department of Labor  
Employee Benefits Security Administration  
Public Disclosure Room  
200 Constitution Avenue, NW, Suite N-1513  
Washington, DC 20210

Dear Regulators,

I would like to submit Fiduciary Compliance Center's reaction and comments regarding the proposed Target Date Disclosure rules. As you know, Fiduciary Compliance Center has served as an active participant in the target date fund debate. We usually express the unpopular view in the room when it comes to these products and the providers who sell them. We have and continue to provide the Department and other authorities with the information about the management and distribution of these products which is not always common knowledge nor easily obtainable. Our professional resources and insider industry experience enable our firm to offer points of view and analysis that is unique to other professionals involved in regulatory policy.

I have focused my comments on the requirements specified in the proposed amended paragraph (d)(3), the inclusion of managed accounts and then offered our critique of the proposal.

**Paragraph (d)(3) Amendment**

In an attempt to provide specific guidelines as to what should be included in the disclosures to participants and beneficiaries the Department has laid out the following six requirements:

1. Name of Issuer
2. Investment Objectives/Goals
3. Principal Strategies (assets held, principal risks)
4. Historical Performance Data (including other ancillary features and general statements)
5. Basic Fee & Expense Disclosures (including underlying investment expenses)
6. Asset Allocation Information
  - a. Explanation (including changes over time, point in time when the allocation reaches its most conservative allocation, a chart or visual demonstrating the glide path)
  - b. Age Group/Retirement Date the Product is Designed for (including the relevance of the date, assumptions about contributions/withdrawals on or after the date)
  - c. A Statement that the Investor May Lose Money

Upon reviewing the proposal which sets forth these six elements, I fail to see where the proposed regulation is in any way progressive in protecting the interests of participants and beneficiaries who invest in these vehicles. This limited information has traditionally been disclosed by most QDIA providers, especially true for the providers who manage the majority of QDIA assets, and the disclosures have been easily accessible and presented in an understandable format.

## **Glide Path Description Element of Disclosure**

I find the only real change from the pre-2008 catastrophes to the present time is the required description of the glide path design which now must be explained in a manner that represents the catchy concept, “through retirement”. This wasn’t an issue before pre-2008 because it wasn’t given a second thought by the providers or anyone else for that matter. The entire argument of “through” verses “to” was only presented after the catastrophes when the major providers sought to explain themselves out of liability for their overly aggressive investment allocations in near term target date products. Now we are suddenly making sure it is stated as it somehow only now provides meaningful information for participants and beneficiaries to consider. This is nothing more than a measure for the providers to “disclose themselves out of liability”, an all too common practice in the industry already. A disclosure provision they have already adopted long before the Department issued the proposal.

Any argument that this information is relevant or meaningful is absurd under most arrangements. The fact is that not a single provider that offers these products intends to leave participants or beneficiaries invested in such products post retirement. Each and every one of the full service/bundled providers offer participant call centers and many offer personal advisors or “education specialists” who all seek to sell the retiring participant or newly endowed beneficiary a new investment product. It is no secret to the providers and should not be a surprise to the Department that these products are not meant for or stood behind in any way as a vehicle to be used beyond that magical life changing event date. The reality of that date means a commission check for the representative who sells the participant or beneficiary a new product, hopefully one of the guaranteed income options because the commissions are really good in the insured product arena. The providers are very well aware of this fact as they come up with enhanced marketing and sales schemes every quarter to capture their share of the rollover marketplace.

The Department should not advocate that it is acceptable to now adopt a disclosure statement that was designed simply as a cover for previous wrongdoing as that sends the wrong message to those who have successfully escaped accountability. In reality the service provider is well aware it does not support this product as the recommended choice post retirement. The products should be managed as designed, labeled and sold – to produce the account balance that the participant starts with when they end the accumulation and begin the distribution phase of their lives. The balance is effectively due on that date. Taking unnecessary risks to chase returns and earn higher undisclosed fees and expenses right before the balance is due makes no sense. Arguing that the investor has many more years to make it up at that point also defies reality. When you start with less in your account, you end up with less when you draw it down.

The service providers’ very own licensed, commissioned brokers and advisors who come dressed as personal advisors, planners and educators will attempt to sell the participant on a rollover or periodic distribution product the minute they receive word the event is taking place. How can we allow service providers to claim a product is designed to do one thing, get you “through” retirement when we know they in fact are not using the product that way? They’re selling the participants out of them as soon as the opportunity arises for a rollover. This disclosure is a “cop-out” that has already been widely adopted now the Department as simply endorsed its usage.

We encourage the Department to stop allowing service providers to hide behind disclosure language that isn’t relevant to the product sales and usage strategies adopted by the provider. The Department needs to send the message that service providers must “stop making excuses” to explain away inappropriate behavior after the fact. This entire position makes no sense whatsoever as we are all aware of how the rollover game is played in this industry. Why are you giving them a free pass to mislead fiduciaries and participants and deceptively market these products?

## **Asset Allocation Element of Disclosure**

As for the asset allocation disclosure requirement, again we see nothing explicit that has not already been a traditional aspect of standard disclosure; the devil is in the details of such information. The industry

standard is to disclose the allocation of the major asset categories, like US equities, foreign equities, fixed income and cash, in glide path graphs and pie charts. Most providers go farther and include a table that shows the allocation amongst underlying asset classes, like market cap, growth and value and intermediate, short and high yield fixed incomes. However, the allocation disclosed in the table is creatively drafted and typically includes language like, "The following table represents the target allocation into the following categories of "funds"..." This single sentence that is commonly found in most of the QDIA product materials is unknowingly the most critical concern for the purchasers of these products and should be the most important concern for the Department.

The disclosure is the investment into the underlying "funds" that the allocation represents and should in no way be confused to represent the methods these QDIA products are actually invested. There is a huge difference between stating an allocation to a type of fund verses an allocation to a specific type of security. This difference has been and continues to be where the break down in regulatory oversight, fiduciary evaluation processes and participant disclosure concerns are most prominent. Unless the underlying funds only consist of passive investment funds which very closely reflect the specified market index which they are categorized to represent, then this "fund" allocation disclosure provides misleading and damaging information to everyone who relies on it. The commonly used actively managed underlying funds that make up these allocations are never style pure and rarely reflect typical investment strategies found in passively managed funds of the same investment style.

Fixed income funds can be labeled intermediate and invest in whatever fixed income instrument they desire within sometimes, unlimited parameters. Large cap US equity funds often buy mid cap stocks and foreign equities to enhance returns. The flexibility within the underlying funds is the exact source of the 2008 catastrophes that sparked this effort, not the overall allocation into major asset categories. The underlying funds all invest much more aggressively than their labels would indicate, especially as understood by the common investor.

Near term target date funds and models lost up to 40+% of participant investments for those that were literally 2 years away from their retirement dates. How can we (the Department especially) forget this fact? How did this happen? What went wrong? Answering these questions and figuring out how to prevent such an embarrassing and more importantly, a devastating catastrophe in the future should be top priority with this proposal. That said where in this proposal are we seeing these answers? This is more of the same and in its current form is not reflective of a progressive effort to protect retirement savings.

The answers to what went wrong were nearly impossible to calculate as the information needed to properly assess the true movements in the allocation of these vehicles is not readily available and certainly not available in a manner that enables such an aggregate calculation. What we have in this industry is 100's of pages of written disclosures to convey the endless authorities to invest these products however the provider chooses without any consolidation of such information to enable the reader to evaluate what it all means. This is not by accident, buried in these voluminous documents are many pieces to a puzzle that is not intended to be put together. It doesn't have to be that way as the manager has the right information to disclose and could do so regularly, but that is all we demand of these product manufacturers and this proposal only blesses such fraudulent practices.

The bottom line is this, how are the QDIA products "really" allocated? For example, a product that looks conservative by stating a 70% allocation to fixed income is oftentimes not at all a conservative choice because what is held in that 70% fixed income allocation is the magic question. When examining the largest target date fund providers, Fiduciary Compliance Center consultants found that most current income and near term target date funds ranging from 2000-2015 actually invested 2 and 3 times their stated allocation to high yield/junk bonds. At some high points it was found that over 16% of the product was invested in these high risk fixed income securities, meanwhile the disclosure stated a target allocation into "high yield "funds" at only 1.5%. That is 1100% times the stated allocation that was disclosed to the fiduciaries, participants and beneficiaries. Many of these same products while only alluding that the underlying funds may invest in mortgage backed securities or whatever else they so choose, also invested in excess of 25% of the total target date fund in these sorts of securities. This is an

astounding fact that not a single reader of these disclosures could have figured out on their own, and notably a fact that this new proposal will not change. There are many more examples of high risk allocations that remain common in these products which Fiduciary Compliance Center experts have been able to identify.

It is clear from the proposal and all that I have seen publicly issued by the Department and the SEC that neither agency has performed a true investigation into these products prior to offering to put a band aid on the situation. The efforts to understand how these products were and continue to truly invest has been almost non-existent. The information is out there, in fact, Fiduciary Compliance Center has already compiled the data. There is no excuse for the lack of thorough investigation that took place following the embarrassing losses of 2008 in the products that were lobbied so extensively to be blessed by the Department. The minimal disclosure requirements set forth under this proposed amendment clearly reflect the lack of desire on behalf of the agencies to truly fix these problems and prevent another round of catastrophic losses in the future.

### **Response to Managed Account Products Affected by the Proposal**

The managed account providers have taken the position that this proposal should not be applied to them. Arguing the requirements are unnecessary for managed account arrangements and not their responsibility to meet, but instead that of the underlying fund managers or bundled service provider. These concerns should be considered carefully. "In addition, the Proposal would require disclosure of...(iv) a list of the assets comprising the portfolio of the QDIA and the value of each such asset" "Again, these are not appropriate for managed account services as QDIA because they are either not pertinent or not appropriate to provide at the Plan level." It goes further to argue that it may be relevant at the participant level but that information is already provided by the underlying funds that make up the model as required.

Again, this goes back to what exactly is provided and required to be provided going forward under this proposal. The fact is that no one is consolidating the actual asset allocation. If the managed account service also is not dissecting the underlying funds to examine and quantify the true asset allocation of the model then they may have designed these models blindly using asset class assumptions which are not represented by the actual investments of the underlying funds. The Department should look deeper into these very expensive managed account services and understand just what it is they truly examine when designing the models. Again, you cannot simply allow these products to be adopted in these plans without thoroughly understanding how they work and who they stand to benefit. Managed accounts should not be treated any differently than target date funds, they operate very similarly. They should appropriately compile the data for the models and not force participants to figure it out on their own. If they have the information, then share it, if they don't have it, well that should really make you wonder about the firm's diligence.

### **Overall Critique of Proposal**

Different than Fiduciary Compliance Center's submissions on regulatory efforts in the past, we would like to offer our overall critique of the proposal. We feel very strongly about the issues imposed by the chain of events that has led up to this proposal and contest this is one of the Department's most critical concerns currently affecting defined contribution plans. We are very concerned at the rate this administration is issuing new proposals and find that significant areas of participant account abuse is being routinely overlooked.

I want to reiterate that we now have target date funds as common investments and the fastest growing type of investments (in terms of asset gathering) only due to the aggressive lobbying, insufficiently investigated adoption of the QDIA regulations and aggressive selling to fiduciaries – which all contributed to the products' success. 2008 proved that we allowed these products to rapidly enter our retirement plans with little to no protections awarded to participants. The fiduciaries have and continue to fail to understand how to thoroughly evaluate the products and the agencies clearly have no desire to

understand and properly regulate the products. The participants are left holding onto what is left in their accounts after the conflicted provider has squandered it all away.

We've all watched the song and dance, the SEC is supposed to be responsible for the oversight of these products and providers and the DOL is supposed to watch over the interests of the plans. Meanwhile neither agency is really doing anything to put a stop to what is nothing more than all out "fraud". The SEC had the investment companies under the "truth in labeling" violation, but failed to acknowledge the rule was actually broken. The solution was to add more language to the rule. Why not just hold them accountable for the rule that has been in force and that was clearly broken? It is clear to those of us who are watching this whole chain of events play out, the ICI and other leading lobbyists have successfully mitigated the concerns and distracted both agencies away from the real issues and the real culprits.

These concerns have been in debate and in the front page news since 2008, over 2 years. After all of this debate, the facts of what is really going on in the investment of these products being leaked and making front page news, the undeniable identification of obviously damaging conflicts of interest, threats of intervention from Congress, lack of regulatory effort promised on behalf of the SEC and the losses incurred by investors, this is proposal is what the Department puts forth? I cannot express at this point my disappointment and frustration that so much critical information has fallen on deaf ears. If this information is all that the EBSA leaders feel is important to protect retirement savings, the same old information that was already provided, then why don't we just ask the ICI to regulate the target date providers? Afterall, this seems to be right in line with what the ICI would have issued. No matter what comments are issued by the industry to debate over sentence structures, I conclude this proposal was certainly a win for the industry and a great notable loss for the retirement saver community.

I encourage the Department to stop and start completely over with this effort. I am well aware that will not happen as clearly the influence inflicted by the lobbyists in Washington who are paid very well to protect the interests of the financial industry supersede common sense and effective policy making. However, please note that if you fail to fix this issue, it will not go away and no one will forget that you had the opportunity and the obligation to do this right after the first major downturn causing these inexcusable losses. It is only a matter of time before we see another 2008 or similar period of market losses, when that time comes the participants are going to want answers.

For the participants' and their beneficiaries, Fiduciary Compliance Center is hopeful that Senator Kohl's office is successful in their efforts to assign accountability appropriately to these providers as clearly that is their only hope for protections.

Thank you for allowing Fiduciary Compliance Center to once again publicly put forth the voice of reason and point out the 800 lb gorilla that just won't leave this room. I sincerely hope that the Department will stop ignoring that well trained, sweet faced gorilla and recognize that lots of animals look very cute and fluffy but they can in fact cause permanent damage with the power they have been awarded.

Respectfully submitted by,

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