August 7, 2017

Office of Regulations and Interpretations
Office of Exemption Determinations Employee Benefits Security Administration
U.S. Department of Labor
200 Constitution Avenue, N.W.
Washington, D.C. 20210

Re: Fiduciary Rule and Prohibited Transaction Exemptions; Request for Information, EBSA-2017-0004-0001

Dear Secretary Acosta:

The American Association for Justice (AAJ), formerly the Association of Trial Lawyers of America (ATLA), hereby submits the organization's response to the Department of Labor's (DOL) request for information (RFI) regarding potential revisions to the Best Interest Contract Exemption (BIC Exemption), Principal Transactions Exemption and amendments to PTE 84-24 (together the "Exemptions").[1]

AAJ, with members in the United States, Canada, and abroad, is the world's largest trial bar. It was established in 1946 to safeguard victims' rights and strengthen the civil justice system. AAJ members represent victims of fraud. It is in this capacity, as representatives of those who have been on the receiving end of the abuses that have permeated the financial services market, that we voice our concerns with further revisions to the Exemptions, especially any revisions that would weaken the DOL's core mission of protecting retirement investors.

The Department's July 6, 2017 request for information directed stakeholders to answer a number of complex policy questions surrounding potential revisions to the DOL's fiduciary rule generally and the Exemptions particularly.[2] AAJ strongly encourages the Department to implement the full fiduciary rule as written and to dispense with any additional changes to the Exemptions. While any changes may benefit the banks and brokerage firms that have chosen not to begin compliance with the rule, it would only do so by allowing these late- and bad-actors to

[1] 82 Fed. Reg. 31278.
[2] Id., at 31279.

continue to defraud everyday retirement savers by steering "Mr. and Mrs. 401(k)"[3] into products and services that are not in their best interest.

1. The Full Fiduciary Rule is Necessary to Protect Investors

We strongly urge the Department to implement the entire fiduciary rule, without significant revisions, as the entirety of the rule is necessary to protect investors from the worst abuses of the financial industry. The Department spent many arduous years working with industry and consumer stakeholders to draft a comprehensive, forward-looking rule that protects everyday savers without unduly burdening the financial industry. We can think of no reason to turn away from this regulation now.

Since 1975, millions of everyday Americans have transferred their retirement savings to the private sector, trusting in their retirement advisors to give them unconflicted, appropriate advice that meets their long-term goals. Over the past forty years, the number of active participants in private-sector defined contribution plans increased from 11.2 million to 75.4 million in 2012, while the number of active participants in private sector defined benefit plans declined from 27.2 million to 15.7 million during the same time period.[4]

Many of these private-sector investors do not realize that the people they turn to may not owe them a legal obligation to serve their best interests. In fact, many financial professionals who are typically not fiduciaries hold themselves out as trusted advisers and use titles such as "financial adviser" or "financial consultant." Use of these titles is deliberate and intended to give consumers the reasonable belief that they are getting advice designed to serve their best interests and to convince consumers that they are in a relationship of trust. According to a Rand Corporation survey of investors' beliefs about different financial service professionals, 59 percent mistakenly believed that "financial advisors or financial consultants" are required by law to serve their client's best interest.[5] The Rand study also indicated that many investors are incapable of telling whether their own adviser is a broker or an investment adviser, let alone whether he or she owes them a fiduciary duty.

When consumers receive financial advice that is not in their best interest, it can cause real harm. Financial professionals who are not required to put their client's interests first are free to steer retirement savers into excessively high cost, low performing investments that drain hard-earned savings while maximizing the professional's profits. Practices like theses can cost retirement savers a lot of money. Working from the various studies, the Department estimated

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[3] SEC Chairman Jay Clayton, Remarks at the Economic Club of New York (Jul. 12, 2017) *available at* https://www.sec.gov/news/speech/remarks-economic-club-new-york.
[4] U.S. Department of Labor. Employee Benefits Security Administration, Private Pension Plan Bulletin Historical Tables and Graphs (June 2013) http://1.usa.gov/Rp8Bwu.
[5] Angela A. Hung, et al., Investor and Industry Perspectives on Investment Advisers and Broker-Dealers, Rand Corporation, Sponsored by the United States Securities and Exchange Commission, January 2008, http://1.usa.gov/1nePF0L.

that retirement savers will lose between $210 billion and $430 billion over 10 years, and between $500 billion and $1 trillion over 20 years, as a result of conflicted advice just with regard to mutual fund investments in IRAs. The Department also estimated that a retirement saver who rolls money out of a 401(k) plan and into an IRA based on conflicted advice can expect to lose 12 to 24 percent of the value of his or her savings over 30 years. Ultimately, retirees who receive conflicted advice end up losing significant savings—conflicts of interest likely lead to a one percentage point reduction in each year's expected annual return.[6] A 2015 report by the Council of Economic Advisors (CEA) found the estimated aggregate annual cost of conflicted advice to be about $17 billion to retirees every year.[7]

Unfortunately, moderate income Americans—those who save for retirement in the smallest amounts—can least afford to have their retirement savings diminished due to conflicted advice and are at the greatest risk. According to the industry's own data, moderate income savers ("Mr. and Mrs. 401(k)") are disproportionately served by advisers who are not required to serve their best interests.[8] Moderate income savers are therefore the most likely to receive and follow harmful advice.

Importantly, if the Department should decide not to implement the entire rule as written, the DOL would solidify the legality of the current loopholes that allow advisors not to be held personally liable for any losses to investors caused by their misconduct.[5] Only the full fiduciary rule, with the Exemptions applied as written will help fix this problem by providing a mechanism to hold firms and advisors accountable. By enforcing a ban on class action waivers (a fundamental part of the BIC Exemption), the Department achieves the President's stated goal of "American empowerment" by preventing financial advisors from taking advantage of retirees while enabling the latter to save more money.

The Exemptions close loopholes created when investment advisors use forced arbitration clauses to shield themselves from class action claims. Although forced arbitration clauses are still permitted under the rule, investment advisors seeking to benefit from the BIC Exemption's safe harbor provisions are prohibited from blocking their clients from participating in class actions against them. The Exemptions act as a deterrent while ensuring that financial advisors that do not act in their client's best interest are responsible for their own behavior, rather than passing that burden on to retirement savers. These transgressions cost working and middle class Americans an estimated 17 billion dollars a year.[9]

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[6] Counsel of Economic Advisors, The Effects of Conflicted Investment Advice on Retirement Savings (Feb. 2015) *available at* https://obamawhitehouse.archives.gov/sites/default/files/docs/cea_coi_report_final.pdf
[7] *Id*.
[8] Letter from Kent Mason, Partner at Davis and Harman, citing Oliver Wyman's "Assessment of the impact of the Department of Labor's proposed 'fiduciary' definition rule on IRA consumers," April 12, 2011, http://1.usa.gov/1CyB9V2.
[9] Counsel of Economic Advisors, The Effects of Conflicted Investment Advice on Retirement Savings (Feb. 2015) *available at* https://obamawhitehouse.archives.gov/sites/default/files/docs/cea_coi_report_final.pdf

2. Implementing the Full Rule as Written Will Not Result in an Increase in Litigation

At numerous points, the Department asks about the "costs" associated with implementing the full rule, and whether the provisions in the Exemptions will lead to an increase in compliance costs for firms due—in part—to an increase in litigation. While complying with the rule may have some up-front costs, litigation will not be one of them. This is partly because the rule, as written, does not ban binding pre-dispute arbitration clauses from retirement services contracts (though we would encourage the Department to re-examine whether these contracts really benefit consumers as the Department seems to think[10]). This is also because there are significant procedural safeguards that prevent consumers from filing and bringing class action lawsuits against retirement advisors.

The current procedural barriers to class action litigation ensure that very few classes are certified. Class action plaintiffs must already satisfy stringent requirements to be certified as a class under Federal Rule of Civil Procedure 23, including demonstrating commonality and typicality of facts and law across the entire class, a large enough size, and adequate representation. Similarly, Rule 23 requires that the injury incurred by all members of the class is comparable in size and scope, and that the application of the relevant law to each plaintiff be substantially the same. The class must also be large enough to warrant a court certifying it as a class action—rather than simply deciding to join multiple, individual cases. Finally, the prospective class must include adequate representatives that accurately reflect the interests of all putative class members.

These requirements are exceptionally difficult to meet for small businesses with limited consumer bases. Thus, large corporations tend to be more affected by class actions than small businesses because the smaller entities simply don't have enough clients impacted by the same illegal activity to warrant class relief. Clients of a local investment advisor offering individual advice to retirees on a case-by-case basis, for example, likely could not form a class, because the numerosity requirement of Rule 23 designed to encourage judicial economy would never be met. This system ensures that the class action cases that would go forward—when the Exemptions are permitted to go into effect—would only be cases where the harm in question is systemic, widespread, and a clear violation of the Exemptions under the full Fiduciary Duty Rule.

For cases that do not meet the onerous requirements proscribed in Rule 23, they simply would not be joined as a class, and the individuals would be permitted to pursue their claims individually. If the individual signed a forced arbitration agreement with their investment advisor, then any legal disputes would be adjudicated by arbitration.

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[10] *See, e.g.*, Economic Policy Institute, Correcting the record: Consumers fair better under class actions than arbitration (Aug. 1, 2017) (noting that on average in financial arbitration, the average consumer recovers nothing and is instead ordered to pay the bank or lender $7,725) *available at* http://www.epi.org/publication/correcting-the-record-consumers-fare-better-under-class-actions-than-arbitration/

Investment advisors are not the first to be banned from including class action waivers in forced arbitration agreements—and the markets that have banned class action waivers have not experienced an explosion of litigation. For example, the Financial Industry Regulatory Authority (FINRA)[11] has prohibited the inclusion of class action waivers in forced arbitration agreements since 1992, and has not seen abuses of the system or drastic changes in price. Similarly, overall workplace class action activity has decreased since the National Labor Relations Board (NLRB) found class action bans unenforceable in 2012.[12] Furthermore, the Exemptions are based on common law developed in state courts, where there are also no skyrocketing costs for investment advisors or state-wide surges in class action litigation—which is in part due to the onerous complexity of bringing class action claims under the current rules.

3. Conclusion: The Department's Emphasis on Industry Cost is Misplaced

Throughout this misdirected Request for Information, the Department continually asks for stakeholder input on the cost to industry participants of implementing the full rule as written. While we recognize that industry cost is an important consideration when regulating the financial markets, we strongly encourage the DOL to examine its own previous analysis which balanced projected cost to the industry with the utility (and cost savings) of protecting investors from conflicted investment advice. As we previously discussed, conflicted advice can cause real harm to middle-income savers; these unsophisticated market participants, many working their way towards a stable and secure financial future for themselves and their families, should not be overlooked in the Department's maniacal drive to marginally reduce compliance costs for huge financial institutions.

As we stated earlier and repeat now, the Department itself estimated that retirement savers will lose between $210 billion and $430 billion over 10 years, and between $500 billion and $1 trillion over 20 years, as a result of conflicted advice just with regard to mutual fund investments in IRAs. The Department also estimated that a retirement saver who rolls money out of a 401(k) plan and into an IRA based on conflicted advice can expect to lose 12 to 24 percent of the value of his or her savings over 30 years. The White House Council of Economic Advisers estimated that retirees who receive conflicted advice end up losing significant savings—conflicts of interest likely lead to a one percentage point reduction in each year's expected annual return.[13] In this same report the Council found the estimated aggregate annual cost of conflicted advice to be about $17 billion to retirees every year.[14] Surely the Department agrees that these costs should not be borne by retirement savers. The Department already designed appropriate regulations over the

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[11] FINRA Rule 13204 (2012).
[12] Seyfarth & Shaw LLP, Workplace Class Action Report (2017) *available at* http://www.workplaceclassaction.com/2017/02/the-story-behind-workplace-class-action-filings-in-2016-trend-4/. *See also* In Re D. R. Horton, Inc., 357 NLRB 2277 (2012).
[13] Counsel of Economic Advisors, The Effects of Conflicted Investment Advice on Retirement Savings (Feb. 2015) *available at* https://obamawhitehouse.archives.gov/sites/default/files/docs/cea_coi_report_final.pdf
[14] *Id*.

course of many years and careful input from all stakeholders: we encourage the Department to follow its own analysis and implement that regime. Everyday retirement savers that work their whole lives for a secure financial future deserve no less.

AAJ encourages the DOL to implement the rule as it was originally written without any further revisions. If you have any questions or comments, please contact Sarah Rooney, Director of Regulatory Affairs at (202) 944-2805.

Sincerely,

Kathleen L. Nastri
President
American Association for Justice