GARRETT PLANNING NETWORK

Making competent, objective financial advice accessible

Submitted via: e-ORI@dol.gov

August 21, 2015

Office of Regulations and Interpretations
Employee Benefits Security Administration
Attn: Conflict of Interest Rule
U.S. Department of Labor
200 Constitution Avenue NW
Washington, DC 20210

Re: Conflict of Interest Rule – RIN 1210-ZA25

I write in support of the DOL's proposed Conflict of Interest Rule. It's time for a healthy update!

A lot has changed in the 40 years since the current rules were written. Individuals are now responsible for their own retirement security and most are not prepared to take on that responsibility without professional guidance.

The investment options and strategies have sky-rocketed since the current law was enacted. We now have retirement plans/accounts and investment strategies and options that weren't available a few years or decades ago. The financial services industry responded and helped give birth to the personal finance boom and the development of the financial planning profession – out of a need to more holistically advise to middle-Americans. Personal finance journalism, discount brokerage firms, no-load mutual funds, ETF/ETNs, fiduciary investment advice and planning advisory firms and organizations focusing on the middle-market, (e.g. Financial Engines, IRA Rebal, Betterment, Wealthfront, XY Planning Network, and the Garrett Planning Network), have come into the marketplace to fill this need and the options are going rapidly.

However, due to the current regulations, most Americans are receiving advice, which is considered "incidental" to a sales transaction, and therefore not subject to the fiduciary standard of care.

Unfortunately most Americans are unaware of the inherent conflicts of interest built into these "advisory" relationships. The proposed rule will close major loop-holes in the definition of advice and what duties financial advisors owe their clients.

This is what the public wants, needs and expects when they seek out a financial professional. In a survey conducted by the Financial Planning Coalition, Consumer Federation of America and NASAA, 97% of investors agree that "when you receive investment advice from a financial professional, the person providing the advice should put your interests ahead of theirs".

Segments of our industry have stated that if this rule is enacted middle-Americans will be shut-off from receiving advice, and/or that is will cause middle-Americans to pay substantially more for advice from a fiduciary. However, the 2015 fi360 Fiduciary Standard Survey once again flatly refutes industry myths that imply it costs more to work with an adviser who puts the investor first, or that holders of smaller accounts would be shut out of the market for fiduciary advice. The survey went on to confirm that nearly 91% of advisors surveyed said that it does not cost more to work with a fiduciary advisor than a broker.

Americans pay a heavy price – amounting to ten to hundreds of thousands of dollars in lost retirement income – as a consequence of the status quo, which permits so called "advisors" to profit unfairly at their client's expense. Cerulli Associates released a survey a few years ago which concluded that approximately one quarter of those surveyed didn't know they paid for advice and another quarter didn't have any idea of how much they paid. How can the fact that about half of the investors surveyed didn't know how much they paid for advice not be a conflict of interest? How can a person make an educated decision if all of the material facts are not revealed and understood?

The advice industry has changed radically over the last few decades, much more so over the last few years. I've been in the industry for 28 years, and I've witnessed hundreds of instances where retirement savers made poor decisions on their own, but what is most egregious are those instances where a financial professional was involved. Sales professional would be a much more appropriate term.

I've worked on a series of lawsuits over the last ten years as an expert witness and/or consultant, in which middle-income pensioners became eligible for early retirement from a major publically traded company. These retirement savers had a solid company pension and most also had healthy 401(k) plan balances. But, they were only in their late 40s to early 50s. They were eligible to retirement, however nearly all of them could not afford to quit working and live off their nest-egg they had accumulated by that age.

Faced with a big decision, limited time, and likely a lot of questions, dozens of employees sought of the advice of a couple registered representatives. The claimants testified that the advisors held themselves out as experts in the employer's retirement plans and ensured them that they were "set for life". Many financial professionals can't get paid, or won't be paid as much, if they can't get their hands on these retirement assets.

Most of these claimants should have turned down the early retirement offer, or at least they should have been informed that their retirement nest-egg would not support them for life, if they did elect to stop working. These were hard-working people who saved well and they should be enjoying a very comfortable financial position. Instead, most are nearly broke and have long since returned to the workforce, in nearly every case, at a much reduced income.

There was no law requiring the "advisor" to consider the pros and cons of taking a lump sum distribution from pension plan, before encouraging, supporting or downright advising these people to take the lump sum distribution. The advisors completed all the necessary paperwork to transfer each claimant's qualified plan accounts to IRAs where they were subsequently placed in variable annuities.

FINRA has issued guidance to members discussing the appropriate use of variable annuities, and these rollovers didn't qualify in my opinion. The rollovers resulted in at least an extra 2.4% average mortality and expense fee, which is in addition to the subaccount management fees. The rollovers were inappropriate, and the variable annuity sale was inappropriate.

Due to the fact that all of these individuals were under 59 ½ and no longer receiving a paycheck, they needed income from their nest-eggs immediately. The variable annuities imposed a 7% surrender penalty on each monthly distribution. These penalties decreased by one percent a year. The advisors calculated the claimants' withdrawals in accordance with the Section 72(t), which resulted in the most modest initial withdrawal rate of just over 8% per year, in addition to the 2.4% M&E and the underlying subaccount management fees. Never in the history of financial markets has a withdrawal rate in excess of 10% been sustainable for any length of time! These retirement savers had a right to know this fact.

Even if the claimants chose to retire because they believed they had enough money, a fiduciary advisor would be obligated to inform the individual that they were not "set for life"...unless they didn't plan on living long. Opponents may say that this level of analysis is inappropriate for their salesforce...I mean "advisors"...or not possible with middle-Americans. However, this is not a complex concept to a qualified financial advisor.

I've shared these stories with hundreds of financial advisors, and regardless of their distribution or compensation model, they are appalled. They've also shared instances of abuse they've witnessed, and this abuse ranges from mild to very extreme.

The most common conflicts I've heard involve the blatant misuse and extremely common overuse of variable annuities. These are complex investment and insurance products, which compensate the sales organization and salesperson (aka advisor) significantly more than any other commonly used investment vehicle.

An advisor in Oregon shared with me that a client she began working with had had their defined benefit plan converted into a cash balance plan in order to take a lump sum distribution place it in a variable annuity, which was then immediately annuitized by their former advisor. Why wouldn't the defined benefit plan be the better option?

Another advisor in Tennessee shared the story of a recent widow who walked into her local bank where she had a long-term relationship and they sold her a $225,000 variable annuity when she only had $250,000 in total investment assets.

Another advisor in Maryland shared a story of a retiree who had nearly $1,000,000 to invest. The representative sold this person three separate annuity contracts. Presuming the annuity was in the best interest of the client, this sale failed to meet the best interest standards because they missed out on the breakpoints available that would have saved them almost $10,000 in excess fees.

Another advisor in Oregon shared a story regarding a broker who had the customer "rollover" (aka exchange) existing IRA annuity contracts from an old policy to a new policy. There was an error on the switch and the client ended up with an IRA distribution. End result – client paid taxes on a $68,000+ IRA withdrawal and now has an annuity with a new surrender schedule.

Private Placements are another area of complexity and therefore a huge potential conflict of interest. Direct investments are typically very concentrated, often leveraged, illiquid, and a purchaser is really relying on what the salesperson or advisor has to say because these are so complex that no one is going to read and understand every work of the prospectus – yet that is all they have to rely on in reality under the current rules. An investor with a complaint against an advisor who's not regulated as a fiduciary cannot rely upon the "advisor's" explanation, answers to questions or anything they say, only the offering document and account application apply are to be relied upon. It doesn't work that way in the real world.

Retirees in California needed income and shared that with their advisor. The advisor sells them an illiquid, income producing real estate private placement. The monthly statements show that the value is remaining stable at $10 per unit, month after month. The retirees had no reason to be concerned, until the income payments changed drastically. Shortly thereafter they receive a solicitation from a third-party offering to buy their interests for a fraction of the price listed on the account statement. The solicitation letter also revealed significant problems with the investment and the company behind it. This was the last $100,000 this couple had to their name.

An advisor in the Chicago area has run into a number of cases where "advisors" recommended that retirement savers mortgage their homes, take lump sum distributions, and even do a reverse mortgage to raise money to invest with them. One of these individuals requested more yield than C.D.s but wanted safety. They were sold a residential real estate lending scheme for Accredited Investors. Loans were all concentrated in high priced real estate markets and when real estate plummeted the fund went belly up and the investors lost $250,000.

An advisor in Ohio shared a story of clients whose broker recommended that they take a distribution from their IRA account (supposed to be an indirect transfer) and use these funds as a 10% down payment and borrow money at a very high rate to buy 3 stocks.

Advisor in California shared the story of a retiring couple whose broker convinced them to take a lump sum distribution from a defined benefit plan and invested 100% of the proceeds in tech stocks. The couple lost every penny in the Internet crash of 2000.

Advisor in Virginia shared the story of a husband who was already retired, financial secure but in poor health. Wife retired from federal government and was advised to rollover her Thrift Savings Plan to an annuity contract with a joint and survivor benefit. Husband died and her income stream from the annuity dropped in half. This was a poor execution of duty of inquiry or to know your client.

When giving investment advice it's critical to know from where the money to purchase an investment comes and if they are more appropriate uses for these funds. Fiduciary duty fills this void.

I could go on and on with the stories I've heard over the years from fellow financial advisors and planners. Many in the opposition to this rule have asked why retirement savers and investors haven't spoken up much more frequently if these abuses are so commonplace. I can only share what I've been told by claimants and other victims of financial abuse. They feel stupid or embarrassed, and often say "I should have known better". I argue that they sought out the advice of a professional and they should have every right to rely up and trust that advice. Not one of them was told "I'm a salesperson and if you don't rollover your retirement plan assets I can't get paid, and by the way, I'm going to recommend products that are in my best interest, which most likely won't be the same as yours".

A witness in one of the lawsuits mentioned lost over $500,000, but refused to file suit. When asked why she refused she replied that she didn't want to relive that painful event. It sounded to me like what a rape victim must confront if they report sexual abuse to the police. The victim has to relive the event over and over again, with police, medical professionals, lawyers, then face the accused in court, presuming the perpetrator is caught, and the outcome is unknown.

So the bottom line is – If you're giving advice regarding people's financial lives, putting their best interest first should be your only interest.

Sincerely,

Sheryl Garrett