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TO THE HOUSE WAYS AND MEANS COMMITTEE

OVERSIGHT SUBCOMMITTEE

ON THE DEPARTMENT OF LABOR'S PROPOSED FIDUCIARY RULE

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Good morning, Chairman Roskam, Ranking Member Lewis, and members of the subcommittee. My name is Damon Silvers, and I am the Policy Director and Special Counsel for the AFL-CIO, a voluntary, democratic federation of 56 national and international labor unions that represent 12.2 million working people. We at the AFL-CIO work every day to improve the lives of people who work for a living. We help people who want to join together in unions so they can bargain collectively with their employers for fair pay and working conditions and the best way to get a good job done. Our core mission is to ensure that working people are treated fairly and with respect, that their hard work is rewarded, and that their workplaces are safe. Further, to help our nation build a workforce with the skills and job readiness for 21st century work, we operate the largest training network outside the U.S. military. We also provide an independent voice in politics and legislation for working women and men, and make their voices heard in corporate boardrooms and the financial system.

The rulemaking we are discussing today affects everyone in America who saves for retirement or who hopes to save for retirement.

In the last thirty years, there have been dramatic changes in how, and from where, working people in America build and receive retirement income, with the responsibility for retirement investing increasingly falling on the individual rather than her employer and professional asset managers. One of the many things wrong with this system is that almost none of us have the expertise to manage our own money or to oversee money managers effectively—and too many in the financial sector who seek to give us the advice we need have a profound conflict of interest affecting their recommendations.

Nowhere is this truer than in the area of Individual Retirement Accounts ("IRAs"), which are the single largest and fastest growing form of retirement savings, outstripping both private-sector defined benefit and defined contribution plans. A key projection in the Department of Labor's Regulatory Impact Analysis accompanying the proposed rule is that IRA rollovers from

employer-based plans are expected to approach an astronomical $2.5 trillion over the next five years.[1]

Even workers who are fortunate enough to have accrued a defined benefit pension—and these are disproportionately union workers—may be confronted with whether to take a lump sum distribution that they invest in an IRA, and how rolled over assets should be invested. Today, many pension plan participants—one-in-four in traditional defined benefit plans and nearly all participants in hybrid plans[2]—are given the option of a lump sum distribution when they retire or separate from employment in addition to the default annuities required by law. In some cases, decisions about benefit form—whether to take a lump sum or whether to take a qualified joint and survivor annuity[3]—can impact eligibility for other valuable benefits, such as retiree health benefits.

Numerous accounts have appeared in the media following the same story line—an adviser convinces a retiree to take a lump sum distribution so the adviser can invest that money; and the retiree loses out in the end.[4] We have even seen entire groups of union members targeted by financial advisers who encouraged them to take lump sum distributions from their pension plans so that the adviser could manage the money without any apparent regard as to what was in each worker's best interest.

Often what we hear here in Washington appeals to the idea that markets are level playing fields; information is free and universal; and the best of all possible outcomes prevail in the best of all possible worlds. But capital markets are all about information advantages. And there are two kinds of participants in the capital markets. First, there are those who follow information in the market in real time, and have powerful analytic tools to understand the information as they receive it—big banks and mutual fund companies, hedge funds, proprietary trading funds. And then there are the rest of us—you and I and the tens of millions of people here in America who are trying to save for their retirement. Given the complexity of the financial products on the market today, there is no way an ordinary consumer can fully unpackage the costs of what he or she is being sold, or what the incentives are of the person doing the selling or the advising.

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[1] *Regulatory Impact Analysis* at p. 3, citing Cerulli Associates, "Retirement Markets 2014: Sizing Opportunities in Private and Public Retirement Plans" (2014).

[2] Wiatrowski, William J., Bureau of Labor Statistics, "The Last Private Industry Pension Plans: A Visual Essay," *Monthly Labor Review* (Dec. 2012) p. 2, 16, *available at* http://www.bls.gov/opub/mlr/2012/12/art1full.pdf.

[3] Even if a participant settles on an annuity, payment options can have significant implications, particularly for surviving spouses.

[4] *See, e.g.*, Gibbs, Lisa and Ian Salisbury, "4 Disastrous Retirement Mistakes and How to Avoid Them: Advisers Touting Sunny Scenarios in Hopes of Snagging Your IRA Rollover Can Imperil Your Retirement," *Money*, *available at* http://time.com/money/3546592/ira-rollover-mistakes-retirement/.

The wrong asset allocation can cripple a retiree's future. And so can investing in high fee products when lower fee products with the same performance characteristics are available. And in the aggregate, the money involved is huge.

The prominence of investment advisers in rollover decisions[5] and the harm incurred from conflicted advice is well-documented. IRA holders receiving conflicted advice can expect their investments to underperform by an annual average of 100 basis points over the next 20 years, and that the underperformance associated with conflicts of interest in the mutual funds segment alone could cost IRA investors more than $210 billion over the next 10 years.[6] The White House Council of Economic Advisors (CEA) has concluded that conflicts of interest overall cost retirement savers $17 billion a year. On an individual level, this means that a $10,000 investment, over 35 years, would grow to just $27,000, rather than $38,000 without the high cost of conflicted investment advice.

Mitigating financial advisors' conflicts of interest will serve to improve the dramatic and very worrisome $7.7 trillion gap between what American households have actually saved today and what they need to have saved today to maintain their living standards in retirement.[7] Assertions that reforms that address harmful conflicts of interest will increase costs for Retirement Investors are fundamentally misleading. Retirement Investors are paying huge costs for conflicted advice; the costs are just hidden. Bringing these costs out into the open will create genuine choice and help prevent overpaying. Consider that every single working American with a 401(k) account could pay $200 a year for investment advice and the net cost would not be as much as conflicted advice is costing the minority of 401(k) participants who receive it, according to the CEA study.

Let's be clear about what this rulemaking is about. It is not about whether investment advice is a good idea. Of course it is—but only if it is advice that is in the investor's best interest. The question for members of Congress in evaluating this rulemaking is: should we put the onus on your constituents to protect themselves from the costs of conflicted advice or should we create a set of rules for fair play?

Further, despite the better security traditional pensions provide to plan participants, investment decisions by plan trustees and fiduciaries can also be compromised by conflicts of interest. The Regulatory Impact Analysis shows how advisers on whom plans rely to guide investment decisions "calibrate" their behavior so as to avoid fiduciary status,[8] and pension plans using

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[5] 54.5 percent of IRA investors with rollovers consulted a professional financial adviser as their primary source of information; sixty percent consulted a professional adviser in some capacity regarding a rollover decision. *Regulatory Impact Analysis* at p. 54.

[6] *Regulatory Impact Analysis* at p. 211.

[7] Testimony of Alicia Munnell, Director of the Center for Retirement Research at Boston College, "Bridging the Gap: How Prepared are Americans for Retirement?" Senate Special Committee on Aging, March 12, 2015, *available at* http://www.aging.senate.gov/imo/media/doc/Munnell_3_12_15.pdf.

[8] R*egulatory Impact Analysis* at p. 19.

consultants with financial conflicts of interest earned 1.3 percentage points less per year than other plans.[9] This is not an insignificant cost given the role of investment performance in a plan's ability to fund the long-term cost of promised benefits, and how plans' historical investment performance, broadly defined, informs federal legislation regarding the funding requirements for defined benefit pension plans.

Last, it is important to remember that retirement savings are tax-preferred savings. Most retirement contributions, both those made by employers and those made by workers, are government subsidized, with those subsidies valued at more than $130 billion for 2015 alone.[14] Whatever you think of that tax subsidy, we probably all agree it should be benefitting America's workers and retirees, not simply accruing to Wall Street's bottom line. Financial institution representatives, who characterize the DoL proposal as an unjustified interference with their long-standing business models, mistakenly overlook the fact that the success of their retirement business overall is a product of, and dependent on, government subsidy.

The enormous sums found by the Labor Department and the CEA to flow from Americans' retirement money to financial institutions and advisers as a result of conflicted advice is unconscionable. It is a direct transfer from the American public to Wall Street, and to allow it to continue is crony-capitalism. The least we can do is require financial advisers to have an absolute duty of loyalty to their retirement investor clients and create basic rules ensuring advisers and financial institutions do not have financial incentives to give retirement investors advice that is not in their best interests.

We applaud the Department of Labor for initiating this important and long-overdue rulemaking and urge it to move forward to a final rule as soon as possible. Thank you for your consideration of our views.

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[9] *Regulatory Impact Analysis* at p. 8, citing U.S. Government Accountability Office, GAO-09503T, *Private Pensions: Conflicts of Interest Can Affect Defined Benefit and Defined Contribution Plans* (2009); *available at* http://www.gao.gov/new.items/d09503t.pdf.