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VIA ELECTRONIC SUBMISSION

The Honorable Lisa M. Gomez
Assistant Secretary
Employee Benefit Security Administration
U.S. Department of Labor
200 Constitution Ave., NW
Washington, DC 20210

Re: RIN 1210-AC02 Retirement Security Rule: Definition of an Investment Advice Fiduciary and related exemptions, RIN 1210-ZA32 Proposed Amendment to Prohibited Transaction Exemption 2020-02, and RIN 1210-ZA33 Proposed Amendment to Prohibited Transaction Exemption 84-24

Dear Assistant Secretary Gomez:

For nearly twenty years, I have been grappling professionally with ERISA's prohibited transaction and other regulatory requirements from an unusual variety of vantage points. I began as an associate in the Employee Benefits practice group of Covington & Burling, advising institutional clients on their ERISA compliance obligations, especially around prohibited transactions. I remember when Advisory Opinion 2005-23A was issued, resolving certain ambiguities in a direction that frankly surprised me, but was welcome for my clients at the time. I went on to provide counsel for a trade association during the discussions in 2011 around the first proposal to redefine "fiduciary" under ERISA §3(21)(A)(ii). Soon after, I decided to become a financial advisor myself instead of providing legal advice and advocacy *about* the profession. I have worked as a captive agent, as in-house consultant to a large insurance wholesaler, and as a comprehensive financial planner employed by the wealth management division of a regional bank. I am now an independent financial planner, a Certified Financial Planner™, and member of the Financial Planning Association, but I speak only for myself and not any of these organizations with which I am or have been associated.

I am sure that all the fiduciary rulemaking efforts dating back to 2010 have been well-intentioned, but it is my well-considered belief that redefinition of ERISA §3(21)(A)(ii) to include financial professionals who are not considered fiduciaries under any other laws is fundamentally flawed and will only make the advice landscape more confusing and inaccessible to the vast majority of retirement savers.

The unique nature of ERISA's fiduciary definition and duties

As a CFP® professional, I enthusiastically embrace my fiduciary duties to my clients under equitable principles under which I pledge my loyalty and professional care, skill, prudence, and diligence to them. But being deemed a "fiduciary" for purposes of §3(21) of ERISA invokes a set of restrictions that go well beyond traditional fiduciary duties; most importantly, the strict prohibition on third-party compensation found in ERISA §406(b)(3), even if it is disclosed to and approved by the beneficiary of the plan.

In the numerous fiduciary rulemaking documents the Department has published over the past thirteen years, it seems to be taken for granted that ERISA's heightened duties and restrictions on "fiduciaries" are related to the importance of retirement savings for individual investors. But this distinction is unjustified, since many other types of investments besides tax-qualified accounts covered by ERISA are also important for the retirement security of Americans. Many retirees are drawing on "nonqualified" securities accounts and annuities, home equity, insurance policies, and a variety of other sources to cover their living expenses and gifting goals.

I would propose that the reason why ERISA strictly regulates the compensation and dealings of §3(21) fiduciaries is that *employers* are generally the persons exercising primary discretionary authority and control over assets that are purportedly set aside for the benefit of their employees. Employers and employees inherently have adverse positions to a certain degree. Employers need to be strictly monitored to ensure that when they set aside and continue to control tax-advantaged assets, instead of paying the employees directly, they are indeed using and managing those assets *solely* in the interests of the beneficiaries (§404(a)(1)). Sponsoring employers are not entitled to *any* compensation for the work of administering their benefit plans.

Sponsoring employers *can* delegate fiduciary duties, in which case ERISA continues to constrain how those delegates are compensated. Prohibited Transaction Exemptions provide guardrails to make sure expenses support the plan beneficiaries rather than lining the pockets of the employer's affiliates and cronies.

Under common law fiduciary principles, fiduciaries can get paid reasonable compensation if the principal agrees to it, because the principal (e.g. the grantor of a trust) is assumed to have the beneficiaries' best interests at heart. Having to get permission for compensation from the Department in the form of a PTE, instead of from the principal, makes no sense for individual retirement accounts where the principal and beneficiary are the same person. Neither does this leave IRAs wholly unregulated, as anyone transacting with or providing advice regarding IRA assets is still a party-in-interest and thus needs to meet the §408(b)(2) standard of "reasonable compensation" for "necessary" services.

From this perspective, it makes sense why the Department in 1975 defined §3(21)(a)(ii) investment advice fiduciaries narrowly, and should continue to only include advisors who are clearly taking on fiduciary duties with respect to plan assets under *other* legal principles. This is not to suggest that the 1975 definition is perfect or should be definitive for all time—only that if there is to be any mismatch between the definition of §3(21)(a)(ii) fiduciaries and the definition of "fiduciary" under the Investment Advisers Act of 1940, common law, or similar legal standards, the ERISA definition should be narrower, not broader.

Requiring financial professionals or institutions to claim the label "fiduciary" under ERISA when they are not acting as fiduciaries in any other capacity is highly likely to confuse consumers and undermine the value of the term. How could it provide consumer protection to require an annuity salesperson to state in writing that they are a fiduciary when they sell a qualified annuity, but leave unsaid the fact that when they sell the very same product to the very same customer using non-qualified funds, they are *not* subject to fiduciary duties? And even if such a distinction must be made in writing, does that not multiply the consumer confusion that is identified as a key reason for this rulemaking?

Narrowly target the solution to the problem

A number of participants in the recent hearings identified one-time, “hit and run” advice as being a serious regulatory gap under the 1975 five-part definition. This is a fair observation, and the frequency of advice has little to do with the considerations discussed above. I would suggest that the Department simply propose removing the “regular basis” prong of the regulation, which would surgically treat this identified problem. Leaving intact nearly fifty years of interpretation and practice around investment advice for qualified retirement accounts, but applying it to one-time transactions too, would expand protection for consumers without producing the types of confusion and disruption that more extensive changes would bring.

Anything other than such a narrowly tailored modification is unlikely to survive legal challenges in today’s federal judiciary, rendering the costly efforts at rulemaking and compliance all for naught. In the recent hearings, the Department seemed to be reaching for something to hang the hat of “relationship of trust and confidence” upon, as if addressing this one point from the 5th Circuit *Chamber of Commerce* decision would be enough to hold up the whole structure. But if anything has characterized the direction of the federal judiciary between 2018 and now, it is the moving of goalposts and discarding of precedent, particularly in the interests of corporations and advocates of deregulation. However unjust it may seem, it is far better to realistically assess the situation and negotiate acceptable peace terms than to charge into unwinnable battles.

PTEs should not place more trust in financial institutions than individual financial professionals

The consequence of dragging more financial professionals into the ERISA fiduciary net is to require them to qualify for a PTE so they can receive any type of compensation for their services. The Department is also proposing to amend existing PTEs to funnel nearly all financial professionals into PTE 2020-02 as the one permissible path to compliance. Advocates of these proposals say they want to eliminate conflicts of interest, but this does nothing of the sort. PTE 2020-02 removes trust from the individual financial professionals and invests it in financial institutions that are charged with supervision and self-reporting.

Individual financial professionals often have long-standing and personal relationships with their clients, as well as heavy reliance on reputation and referrals to maintain and grow their client base. These personal factors regularly outweigh the lure of a few extra basis points when recommending one investment or another, and guard against “hit and run” sales being prevalent, at least among successful, long-term financial professionals.

Financial institutions, by contrast, do not have emotional and relational bonds with their customers. According to classic shareholder value theory, they exist solely for the purpose of generating profits by maximizing revenue and minimizing expenses, and will set their policies and procedures accordingly. Yet unfeeling, profit-maximizing institutions are the entities charged under PTE 2020-02 with annually certifying that their employees or agents are not putting their own interests ahead of the customers’.

The cost of an institution complying with PTE 2020-02 well enough to mitigate the risk of penalties is substantially the same whether a client is investing \$5,000 or \$5,000,000. Consequently, financial institutions pressure their employees or agents to drop smaller investors off their books to preserve their profit margins. When compliance costs are ratcheted up for large financial institutions, individual financial professionals with the best of intentions end up having to choose between losing long-time relationships with clients of more modest means and losing their own access to health insurance and other employee benefits if they quit or fail to meet the firm’s performance (profitability) expectations.

Non-compete and non-solicitation agreements often prevent financial professionals from taking their clients to more accommodative firms. Wealth gaps widen as more resources shift to managers and legal counsel and away from individual advisors and small investors.

As it stands today, PTE 2020-02 at least requires extra scrutiny and justification for rollover recommendations. But the proposed changes to this PTE only make the conditions more vague and subjective. As many commenters have noted, there has been no evidence presented that PTE 2020-02 is not working as intended. Changing it so soon after financial institutions scrambled to comply in its present form would impose enormous costs for no apparent benefit.

Meanwhile, PTE 84-24 gives ERISA fiduciaries an option to provide guaranteed products to qualified retirement plans, and would apply to more recommendations for IRA rollovers if the definition of “fiduciary” is expanded in any way. Disqualifying most insurance-licensed professionals from using this exemption, which is tailored to these products and their distribution methods, would decimate consumer access. The Department may “believe that insurance companies can effectively exercise fiduciary oversight with respect to independent agents’ recommendations,” but it lacks the regulatory expertise and evidence to justify such a belief.

As should be apparent from my previous remarks, I am no apologist for large financial institutions, but it is my conclusion from my many years of trying to figure out how the 2010 proposal or 2016 regulation might be implemented for independent insurance producers, that this is indeed impossible. Even if it were possible for insurance companies to develop entirely new systems of distribution and compensation to deliver guaranteed products to market without paying front-loaded commissions, funneling these transactions through PTE 2020-02 would impel them to cut off distribution through independent agents, the very professionals who are *least* subjected to institutional conflicts.

Ignoring risks and the existence of products to mitigate them is imprudent

Underpinning much of the rhetoric justifying the fiduciary proposals over these years has been an assumption that the expenses and liquidity restrictions inherent to annuities and life insurance policies are pure waste. Straight-line projections of account balances with and without insurance expenses are compared, and used to estimate the “benefit” of snuffing out these products by aggressive regulation. This approach to (de)valuing insurance products is as misleading as rogue agents claiming illustrations of non-guaranteed returns can be counted upon.

It would be imprudent and therefore a dereliction of duty for a fiduciary to advise a client whether their retirement savings are adequate on the basis of constant rates of return, a fixed life expectancy, and no consideration of potential long-term care expenses. This is why Monte Carlo analysis is preferable to straight-line projections, especially as clients approach the decumulation stage of life, and why insurance needs-analysis is an essential part of a comprehensive financial plan. The Department likewise would violate its fiduciary duty to the public if it ignores the practical impact of risks and variables on personal financial security and blithely endangers the distribution of financial products that mitigate these very risks.

There is a real human cost to uncertainty and worry, and real benefit to taking particularly harsh possibilities off the table. Many retirees would prefer to have certainty that they will have enough income to cover necessary expenses for the rest of their lives, no matter how long, than to (probably, but maybe not) have a larger sum left for heirs at their death. The value of this trade-off is highly subjective and can’t be quantified the same for every retirement investor. This is why regulation of

annuities and similar products should emphasize clear disclosure and consumer choice—only the individual consumer can decide if the trade-offs are worthwhile.

Asking insurance companies to determine if these trade-offs are worthwhile, as if there were an objective analysis that could be applied, is incoherent. If they weren't worthwhile for a significant number of potential clients, a market for these products wouldn't exist, especially since premiums, surrender fee structures, and marketing materials have to be approved by state insurance regulators. This is why the informed consent standards of the existing PTE 84-24 make good sense and should continue to be available for insurance-licensed financial professionals operating under any type of firm or business model.

The Department should also take notice of the fact that the market for standalone long-term care insurance has shriveled, despite Congress's attempts to provide tax incentives, but hybrids and riders with annuities or life insurance products are gaining traction instead. Long-term care expenses that ultimately get paid by Medicaid after retirees run out of assets are an enormous actual and potential liability for federal and state budgets alike, making private insurance against these expenses a clear public good, in addition to providing private peace of mind. The Department should be helping the public understand the benefits of using some of their retirement savings towards purchasing these multipurpose protective policies, rather than casting doubt on the entire category of annuities.

If the Department's concern is the potential for "hit and run" rollovers to these products for clients who don't truly understand the ramifications of their choices, it should again narrowly tailor any regulatory changes to this specific problem. For instance, PTE 84-24 could be amended to require the covered party to "document the specific reasons that any recommendation to roll over assets ... is in the Best Interest of the Retirement Investor," as is currently required for PTE 2020-02, except that the person making the recommendation would be responsible for this documentation, instead of a financial institution. It could incorporate the NAIC's annuity best interest language or even borrow the care obligation of natural persons making recommendations under the SEC's Regulation Best Interest (Sec. (a)(2)(ii)). Such approaches would require greater documentation and diligence for rollover recommendations without upsetting the entire market and regulatory structure of annuity distribution.

Redefining "fiduciary" is not the only way for the Department to fill regulatory gaps

The regulatory environment for sales of securities and annuities has matured significantly since the Department first proposed to change the definition of ERISA-fiduciary in 2010. These sales are now subject to best interest standards that did not exist in 2010, or even in 2016. Imposing additional regulations on top of other regulators' careful and recent constructions is simply disruptive now.

There *are* still regulatory gaps that the Department legitimately may want to fill. In particular, sales that are not regulated as securities, investment advice, and insurance products are present the greatest dangers for unsuspecting retirement savers today. IRAs can hold assets such as real estate, commodities, and cryptocurrency that fall outside the regulated landscape. While it might be beneficial to make sure any recommendation about retirement savings is subject to some kind of best interest standard, ERISA was not constructed for this purpose in 1974. Redefining salespersons in these less-regulated fields as "fiduciaries" is not a feasible way to expand regulation beyond Congress's original intent, especially in today's judicial landscape.

As mentioned previously, persons who sell products or services to a plan or IRA *are* defined as "parties in interest" and subject to certain prohibited transaction rules, even if they are not fiduciaries. There is a

broad statutory exemption from non-fiduciary prohibited transactions (ERISA §408(b)(2)) for “reasonable compensation” for “necessary” services. The Department has never done much to flesh out what makes compensation “reasonable” or whether it is “necessary” for plans and IRAs to invest in high-risk, unregulated assets. I believe taking a strict interpretation of this statutory exemption would be a reasonable alternate route to filling the regulatory gaps that persist today and may arise tomorrow.

Finally, the Department could consider asking Congress to legislatively address its concerns. Retirement security is one of the few areas in recent years where there has been significant bipartisan legislative progress, particularly in the form of the SECURE Act and SECURE 2.0. A number of approaches could be taken, from categorically excluding high-risk investments from IRAs, to imposing best interest standards on all qualified retirement asset recommendations, to funding high-quality free financial literacy initiatives so that consumers can be empowered to more confidently exercise their choices.

Conclusion

Undoubtedly, the Department is seeking to improve the health of Americans’ retirement savings and security. But doing so by pulling salespersons into ERISA’s definition of “fiduciary” amounts to performing surgery with a blunt and rusty instrument. I urge you to withdraw this proposal and invest in evidence-based and laser-precise regulatory interventions in the future.

Respectfully,

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