**Written Testimony of Nick Lane**

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**Department of Labor Public Hearing:**

**Proposed Definition of the Term "Fiduciary" and Proposed Exemptions**

**Monday, August 10, 2015**

Good morning, my name is Nick Lane, and I am Head of U.S. Life and Retirement for AXA, one of the country's largest life insurance and retirement savings companies with nearly 2.5 million customers nationwide. In addition to serving on the company's Executive Management Committee, I am Chairman of the Board, President and Chief Executive Officer of AXA Distributors, the wholesale distribution arm of AXA, and a member of the Board of Directors of AXA Advisors, AXA's retail broker-dealer and registered investment adviser with over 4,600 financial advisors.

I am also the Chairman of the Board of Directors of the Insured Retirement Institute, and I'm honored to be here today representing IRI. IRI is the only national trade association that represents the entire supply chain of the retirement income industry, including major life insurance companies, broker-dealers, banks, and asset management companies, and is therefore uniquely positioned to comment on the implications of the proposal for manufacturers, distributors and consumers of annuity products that provide guaranteed lifetime income.

IRI members account for more than 95% of annuity assets in the United States, include the top 10 distributors of annuities ranked by assets under management, and are represented by more than 150,000 financial professionals serving over 22.5 million households in communities across country. IRI members therefore represent not only their own views, but also those of their clients on Main Street across America.

As you know, IRI has provided a detailed comment letter aimed at constructively helping the Department to carefully develop a rule that will avoid the unintended consequences of depriving consumers of access to guaranteed lifetime income products and the professional advice needed to understand, purchase, and manage those products. President Barack Obama and his administration have done more than any other administration to promote the use of annuities to provide guaranteed lifetime income and to break down the barriers to access to annuities in workers' retirement plans. Of course, both the Department and the IRI want to assure that this rule does not undermine those efforts. So, on behalf of IRI's members, I am here today to help the Department avoid the harmful unintended consequences that will be caused by the rule as currently written.

## **The Context for IRI's Comments on the Proposal: America's Retirement Income Challenge and the Need for Retirement Income Products**

Before going any further, I'd like to briefly provide some context for my comments today. As we all know, Americans today are living longer than ever before, while access to traditional defined benefit pension plans continues to drop and health care costs continue to rise, creating a significant risk that far too many Americans – more than 30 million Baby Boomers and nearly half of all Gen Xers – will outlive their savings. Middle-income Americans seeking a financially secure retirement are faced with challenges that simply did not exist for their parents and grandparents.

Outside of Social Security and private pensions, annuities are the only products available in the market that can provide guaranteed lifetime income during retirement to help retirees ensure that they will not outlive their savings. IRI research has shown that Boomers who own insured retirement products, including all types of annuities, are more confident in their overall retirement expectations and are more likely to engage in positive retirement planning behaviors. And, 9 in 10 annuity owners are satisfied with their annuity products.

Unfortunately, we believe the proposal would significantly limit consumer access to these critical lifetime income guarantees through employer-sponsored retirement plans and IRAs at precisely the point in time when access to them is most needed.

**<u>Support for Best Interest Standard</u>**

Before I address specific elements of the proposal let me begin with two very simple and clear points, which I am sure you will hear from many others throughout this hearing. First, IRI and our members support a best interest standard for financial professionals who provide personalized investment advice or recommendations to plans, plan participants and beneficiaries, and IRA holders. We believe the vast majority of financial professionals already act in their clients' best interest, and recent IRI research found that nearly all consumers agree. Second, the availability of lifetime income guarantees for plan participants and IRA investors is critical, and needs to be addressed in each element of the proposal.

Turning now to the specific elements of the proposal, my comments will address three areas:

1. Proposed amendments to PTE 84-24;
2. Proposed "Best Interest Contract Exemption" or BICE; and
3. Proposed definition of the term "fiduciary", including the proposed carve-outs to that definition.

I want to start with PTE 84-24 and the BICE because, as I noted just a moment ago, it is critical that both exemptions clearly facilitate the offering of a broad spectrum of lifetime income guarantee alternatives, from living benefits to immediate annuities to deferred income annuities and QLACs. Both exemptions raise unique concerns, which I will address in turn. And then I will conclude with the threshold issue of the fiduciary definition itself.

**<u>Comments on the Proposed Amendment to PTE 84-24</u>**

Turning to the proposed amendments to PTE-84-24, under the proposal, this PTE would no longer be available for transactions involving variable annuities in the IRA market. This change explicitly limits choice for retirement savers by strongly discouraging the sale of variable annuities, which offer retirement savers an essential and unique vehicle for accessing guaranteed lifetime income while still retaining some effective control over investments. While this PTE has been in place for both variable and fixed annuities for over 30 years, the Department has not provided any evidence to support the need for this disparate treatment, which appears to be based on an inaccurate perception that variable annuities are simply a "package" or "bundle" of mutual funds.

IRI strenuously rejects this notion. All fixed and variable annuities, whether required to be registered as securities or not, are insurance products that provide guaranteed lifetime income. While variable annuities have investment features, the products' benefit base and lifetime income guarantees are the primary attributes that make them attractive to many consumers. In addition, variable annuities commonly include multiple layers of meaningful guarantees, including: one or more fixed investment options, with both periodic and lifetime crediting rate guarantees, alongside a set of variable investment options; living benefits providing lifetime income guarantees; death benefit guarantees; and guarantees of the right to convert all or a portion of the contract to an income for life or for joint lives. Put simply, variable annuities share much more in common with fixed annuities than they do with mutual funds and other securities products.

With this in mind, IRI strongly urges the Department to remove the exclusion for variable annuity IRA sales from the proposed amendment to PTE 84-24. Retirement savers would continue to benefit from the best interest standard and reasonable compensation requirement in PTE 84-24, as well as existing SEC and FINRA disclosure requirements that achieve the same fee transparency goals of the requirements in the BICE, which I will discuss shortly.

With this said, PTE 84-24 needs additional modifications to make it workable. Under both PTE 84-24 and the BICE, the "Best Interest" standard as defined is unworkable. Although the preamble to the proposal clearly indicates that, under the "Best Interest" standard, the adviser must put the client's interests first, ahead of their own, the actual wording of the standard in both 84-24 and BICE seems to suggest that the adviser, as well as any affiliates, can have no interest at all. We believe that this is both impractical and unnecessary, as the same goal can be accomplished by simply requiring advisers and financial institutions to always put their clients' interests first as the preamble to the proposal indicates. Therefore, we urge the Department to modify the definition of the "best interest" standard to clearly reflect this point. Otherwise, as a practical matter it will be impossible for any adviser or financial institution to rely on either PTE 84-24 or the BIC Exemption, meaning millions of Americans would lose access to advice and to products which can provide guaranteed lifetime income.

We also request that the Department clarify the guidance in 84-24 to encompass any compensation in the product itself, and broaden the definition of "Insurance Commission" in the proposed amendments to make sure that advisers are not inadvertently prohibited from receiving customary and important employee benefits. In order to avoid this unintended result, the



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proposal needs to be revised to avoid any inference that advisers are not allowed to receive health insurance coverage or access their own employer-sponsored retirement plans.

To be clear, we are not suggesting that PTE 84-24 should be the exclusive exemption for annuities. Rather, we believe both PTE 84-24 and the proposed BIC Exemption can provide appropriate levels of consumer protection with respect to annuities, and thus both exemptions should be available for sales of all types of annuities so advisers and financial institutions can choose the path that makes the most sense for their respective businesses and clients.

## Comments on the Proposed Best Interest Contract Exemption ("BICE")

The BICE is second aspect of the proposal I'd like to discuss here today. We believe many of the conditions included in this proposed new exemption will be so onerous or impossible to comply with that lifetime income products and vital sources of annuity product distribution information will no longer be available to consumers. In our comment letter, we provide extensive feedback on the logistics of the required "best interest contract" and the disclosure requirements included under this exemption, and I would encourage you to review those comments. In addition to the concerns I just covered about the fact that the definition of "Best Interest" under 84-24 and the BICE would require advisers and financial institutions to completely disregard their own legitimate financial and business interests, I'd like to highlight two specific issues regarding the BICE.

***Reasonable Compensation.*** The first relates to the conditions included in the proposed exemption regarding "reasonable compensation" as it would apply to annuity products. The BICE would measure reasonable compensation strictly in relation to the value of services provided by the adviser and the financial institution. While that may seem sensible on its face, it fails to account for the costs associated with the guaranteed features of annuity products, which, as I noted earlier, are the main reason most consumers decide to purchase these products as part of their overall retirement income plans. Fortunately, a simple and straightforward solution is readily available for the Department to address this issue. The definition of "reasonable compensation" in the proposed amendments to PTE 84-24 does, in fact, distinguish between amounts paid for services provided and amounts paid for the annuity contract itself. We urge the Department to incorporate this same distinction into the BICE for purposes of measuring reasonable compensation in the context of annuity transactions.

***Proprietary Products.*** The second point I want to raise on the proposed BICE relates to its impact on proprietary annuity distribution models. Many insurers offer proprietary investment menus under their variable annuity contracts and IRA products. Similarly, a number of insurers have career agents who contractually agree to limit their annuity sales and servicing efforts primarily or exclusively to the insurer's own products. These insurers may sponsor benefit plans to cover qualifying career agents, provide office housing allowances and offer substantial training and education support.

Unfortunately, the proposed BICE implies that such arrangements are inherently problematic by imposing additional conditions on advisers and financial institutions that offer only proprietary products. These conditions would create a bias in favor of advisers and firms that offer unlimited product choice and against those that choose to develop more extensive expertise on a smaller universe of products. The benefits of the proprietary distribution business model are vital to a healthy marketplace and need to be preserved. As such, we are asking the Department to remove the additional conditions on advisers and financial institutions that offer only proprietary products and clarify that merely offering such products would not subject them to any additional requirements in order to satisfy the BICE.

In addition, even though the Department has repeatedly noted that it is preserving the availability of commissions under the BICE, the examples provided in the preamble to illustrate the types of compensation arrangements that could qualify for the exemption are antithetical to such commissions. We ask that the Department add examples consistent with its position that commissions are permitted under the exemption.

**Comments on the Proposed Definition of the Term "Fiduciary"**

As we all know, the proposal would significantly expand the circumstances under which a person giving investment advice to a plan, its participants, or an IRA owner would be considered a fiduciary under ERISA and the Internal Revenue Code. In the preamble to the proposal, the Department explains that the goal is to make sure the term "fiduciary" is defined to clearly include relationships that are appropriately regarded as fiduciary in nature and clearly exclude those that are not. This is an admirable goal that we wholeheartedly support.

***Overly Broad Definition of Fiduciary.*** However, the proposed definition is so broad that it captures many customary financial marketing and sales activities where no reasonable consumer would expect that the financial professional is performing such activity as their fiduciary. By way of example, the definition would include each of the following activities:

- giving a mere factual description of the features of an annuity product, such as an immediate fixed annuity or a deferred variable annuity, and explaining how the product can meet certain needs;
- answering questions from plan participants about the operation of a specific "in-plan" guaranteed lifetime income product and its available features;
- proprietary product "wholesaling" activities where representatives of an annuity product manufacturer meet with financial professionals – either one-on-one or in group sessions – to explain the features of the product and to conduct training; and
- counseling a recent retiree about his or her likely income replacement needs and the features available under various annuity products that could help meet those needs.
- Routine customer service provided by a call center.



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If the fiduciary definition is not appropriately narrowed to clearly exclude activities that are not fiduciary in nature, the result will be that millions of Americans with modest means or who are just starting to save will not receive information and advice to help them plan for a secure and dignified retirement.

In our comment letter, we offer a number of recommended changes to the proposed definition of "fiduciary" to distinguish between conduct that is properly considered and understood to be fiduciary in nature and clearly non-fiduciary sales and marketing activities.

***Overly Narrow Carve-Outs From the Fiduciary Definition.*** And while we note that the Department has provided a number of so-called carve-outs from the proposed definition that in theory could alleviate these concerns, those carve-outs are too narrowly tailored to do that.

First, the proposal includes a counterparty carve-out designed to allow advisers and financial institutions to engage in basic sales activities without becoming a fiduciary (commonly referred to as a seller's exception). Unfortunately, this carve-out is not available for nearly any retail transactions, such as those involving small 401(k) plans or individual participants, beneficiaries or IRA owners. The proposal justifies the limited availability of this carve out based on the view that, "as a rule," recommendations to small plans and individual customers do not fit the arm's length characteristics the carve-out is intended to preserve.

IRI disagrees with this premise, and therefore urges the Department to provide a carve-out from fiduciary status for a person who: "provides advice or recommendations . . . under facts and circumstances where there can be no reasonable expectation on the part of the advice recipient that the advice provider is undertaking to provide unbiased and impartial advice."

Absent such change, tens of thousands of small businesses will either not open retirement plans for their employees or will not maintain their current plan, and millions of Americans with low and moderate savings will not receive information and advice to help them plan for a secure and dignified retirement.

Another important carve-out in the proposal relates to investment education. While the Department has wisely expanded investment education to include education about distribution options, the proposal nevertheless impairs the ability of advisers and financial institutions to provide meaningful investment education because it excludes discussions of specific investment alternatives from the definition of investment education. We believe the existing guidance under Interpretive Bulletin 96-1 allowing discussions about investment alternatives in connection with asset allocation education is very important for savers, and therefore urge the Department to revert back to that definition. Otherwise, savers will not be able to know which specific investments match their preferred asset allocation, and they risk choosing investments that do not meet their risk tolerance and needs.



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**Comment on Timing of Implementation for Proposal**

As my time draws to a close, I want to make one final but critical point. IRI recently asked Deloitte & Touche to conduct a study on the operational impact of the proposal on the insured retirement industry. A copy of the report was included with our comment letter, but one of the most important takeaways from the study is that the proposed eight-month implementation period is simply not feasible. Given the complex requirements and conditions in the proposal, our members would have to undertake massive information technology re-design and build outs that would likely take several years to complete. The DOL and the financial services industry have recent experience with adoption of a new, more limited disclosure regime in the form of the Department's regulations under ERISA Section 408(b)(2) in 2012. The implementation date for those regulations, which are much narrower in scope than those contained in the proposed rule, was delayed on several occasions, and ultimately extended by more than two years. This was largely in response to logistical issues experienced by the industry in developing new technology and processes to comply with the regulations, and the Department correctly concluded that a longer implementation period was necessary. The changes that will be necessitated by adoption of the proposed rule are far more extensive and complex. To avoid significant and harmful disruptions in the availability of annuity products and their guaranteed lifetime income features to millions of retirement savers, and advice about whether these products fit their needs, the implementation period should be extended to at least three years.

Thank you for the opportunity to share these views with you here today. I'd be happy to answer any questions you may have.



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