The DOL Wants Ethically and Competently ERISA IRA Rollovers: Then Let ONLY Professional Financial Planners Do It

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What is This?
The DOL Wants Ethically and Competently ERISA IRA Rollovers: Then Let ONLY Professional Financial Planners Do It

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Abstract
The Department of Labor (DOL) has issued guidance, warning advisers still serving a retirement plan in a fiduciary capacity that soliciting IRA rollovers or cross-selling additional products to plan participants is prohibited. But plan participants are not a monolithic group. Their financial literacy as to retirement savings and general financial management concepts ranges from the illiterate to the sophisticated. (Discussed later in this article.) The poor decision-making as to retirement planning at a national level is at least partially a product of Department of Labor administrative policy. While providing educational investment materials to workers as to their 401(k) is laudable in the abstract, it takes a somewhat pernicious form when these generalist materials are deemed sufficient in and of themselves to create investment retirement portfolios and strategies. The Department of Labor is, or should be, fully aware that the average American worker does not have the requisite investment acumen to year-in and year-out steer their 401(k) retirement strategies safely into retirement. Too much is at stake to sugarcoat this. This DOL behavior is negligent at best, and patently unethical otherwise.

Keywords
financial literacy, direct rollovers, financial planners, The American College, IRA

Background: The Current Regulatory and Legal Environment
Millions of American employees contribute to their retirement in employer-sponsored retirement savings plans, such as 401(k)s and 403(b)s. From 1975 to 2010, plan participants in private sector defined-contribution plans increased from 11.2 to 73.4 million while during the same time period, plan participants in private sector defined-benefit plans declined from 27.2 to 17.1 million. The foundation of the entire U.S. retirement savings system is the individual retirement account (IRA), the ultimate destination for many defined-contribution plan assets, via rollovers. When employees change jobs, IRAs provide the portability, and for small-businesses, they are the only type of account allowed (SEPs [simplified employee pensions]/SIMPLEs [savings incentive match plans for employees]).

The Employee Benefits Security Administration (EBSA) administers and enforces the fiduciary provisions of the Employee Retirement Income Security Act (ERISA), which oversees both employer plans and employer-sponsored IRAs (SIMPLEs, SEPs). EBSA, a branch of the Department of Labor (DOL), is striving to make the fiduciary definition for IRAs the same as with ERISA plans. Presently, ERISA fiduciaries to employee benefit plans (but not IRAs) owe clients a duty of care and a duty of loyalty, and any breach of these two duties by the fiduciaries results in personal liability. EBSA’s objective is to one fiduciary definition for the administration of all retirement plans, while addressing through exemptions any substantial practical differences between IRAs and employer plans. This Final Rule is anticipated sometime this spring.

The DOL has also issued guidance that warns advisers still serving in a fiduciary capacity that soliciting IRA rollovers or cross-selling additional products to plan participants is prohibited. Additionally, if the fiduciary adviser persuades the plan participant to take a distribution and invest the proceeds and that results in additional compensation to the adviser, such actions may trigger a
prohibited transaction under ERISA, subjecting the adviser to significant penalties such as disgorgement, excise taxes and so on.\(^5\)

Admittedly, IRA owners are least protected by fiduciary standards and are especially vulnerable to conflicting advice. As EBSA’s Fiduciary Fact sheet observes, IRA holders have substantial investment responsibility, like 401(k) plan participants. However, unlike 401(k) plan participants, IRA owners are qualitatively more vulnerable since no other plan fiduciary protects IRA investments.\(^6\)

In October 2010, the DOL issued a proposed fiduciary rule (subsequently withdrawn) making it much easier to find advisors “rendering investment advice for a fee.” Advisors including brokers now could be deemed fiduciaries even when just trying to make a sale. This extension of “investment advice” clearly threatens the existing advisor business models that provide plan participants with investment advice as a business strategy to develop a long-term relationship with the participant and eventually capture rollovers.

Under the proposed DOL regulation reissued in March 2010 (subsequently withdrawn), Advisors would only be able to offer investment advice in one of two ways: (a) Advisors must disclose fees and acknowledge in writing that they are fiduciaries. Those who sell financial products for IRAs or rollovers will need to clearly disclose they do not provide objective advice, and cannot wrap their products with planning services. This should have a grave impact upon commission-based annuity IRAs, since they are often sold as part of retirement income plans. (b) Advisors must render “advice” only via a certified computer model.\(^7\)

The newly proposed DOL investment advice rules would apply to both retirement plans and IRAs. As a fiduciary under ERISA, an advisor must act solely in the interests of participants and beneficiaries. Advisors receiving 12b-1 compensation that varies by asset class will not be able to offer participants or IRA holders investment advice due to the prohibited conflict of interest under ERISA. The reasoning here is that the advisor may make more money if participants invest in equity versus fixed income or money market funds. If so, this is self-dealing and a clear conflict of interest under ERISA’s fiduciary rules.

When the DOL issues the Final Rule, sometime this spring, the new Fiduciary Definition and the new Plan and IRA Investment Advice rules will change the fiduciary landscape for good. Advisors providing advice to retail clients who also have IRAs will need to offer advice under this level fee rule or use a certified computer model. These rules affect every advisor.

Assistant Secretary for DOL’s EBSA, Phyllis Borzi, in testifying before Congress, stated, “Unlike plan participants, IRA holders do not have a plan fiduciary to represent their interests. They cannot sue fiduciary advisors under ERISA . . .”\(^8\) EBSA is quite aware that many investment firms use “education” services as door openers to capture new IRA business. While EBSA wants more education for plan participants, it wishes a more clear separation between these “educational” services and commission-based product sales. In response, the mutual fund industry is advocating for pure platforms that do not provide individualized advice and instead deliver general education and guidance.\(^9\) Neither the mutual fund industry nor EBSA, as we shall see, has gotten it right.

The issue of rollovers is financially titanic. According to a recent study, 88% of IRA accounts are with commission-based brokerage firms. The other 12% are in fee-based advisory models. After more than 22 million IRA brokerage accounts were analyzed, the study concluded that EBSA’s proposed rule would cause 7.2 million (roughly 30% of the total) to have insufficient assets to qualify for their firm’s advisory channel.\(^10\) For these accounts, most support services would cease since they would be within the brokerage model. To meet advisory channel minimums, another 4.4 million accounts (20%) would need to change firms. The remaining 12 million (55%) could migrate to advisory status, but at more cost.

Whenever an advisor has a preexisting relationship with a retirement plan or a plan participant, any financial services offered in conjunction with rollovers is dangerous. The DOL defines cross-selling as using existing participants and beneficiaries to market additional services or products. The Department believes that cross-selling is particularly prone to abuse whenever advisors receive fees from rollovers to IRAs. This is why the DOL drafted the infamous Advisory Opinion 2005-23A, which posed three questions. The crux lay in the second part of the DOL’s answer to Question 2 stating that advisors who are currently plan fiduciaries are still under fiduciary obligations as to any rollover recommendations. If such an advisor for compensation provides investment advice through a plan, he or she is by default a fiduciary. Unless an exception applies, he or she also comes under the prohibited transaction rules that preclude self-dealing. As a result, virtually any advice affecting the amount of compensation earned could violate the rules. Furthermore, those who are in compliance with state insurance laws, the Securities and Exchange Commission and the Financial Industry Regulatory Authority may still be afool of ERISA. Damned if you do, and damned if you do not.

**Unless The DOL Helps This Nation Radically Increase Retirement Savings, We Are Headed for a Geriatric Abyss**

DOL retirement policy today puts each plan participant on the horns of a dilemma.\(^11\) Everyone agrees that plan
participants need both retirement planning education and investment advice. But when does a bunch of sticks become a pile and when does education become investment advice? Plan participants, oftentimes at a daily level, receive education materials either too simple for those financially literate or too complex for the financially illiterate. So long as the DOL continues to focus on creating what is too often a distinction without a difference, this will continue. And to discipline those who advise when all investment advice, if sound, involves education is worse than misguided. This policy within the DOL creates and then institutionalizes a self-referential culture believing that evermore compliance will solve this nation’s retirement ills.

The core problem is that participants are not getting professional investment advice before they direct the investment of their retirement savings. Why? For one, this advice is not coming from professionals. Instead of mandating that rollovers can only be accomplished by professional financial planners—only these letters will suffice: (a) ChFC, (b) MSFS and/or (c) CFP—plan participants are systematically not getting sufficiently applicable investment advice when they do rollovers within the rubrics of the nigh-infinite rulings and regulations promulgated by the DOL, which interprets and enforces the byzantine ERISA of 1974.

As yet Congress is unwilling, or politically unable, to modernize ERISA. And so the burden to save these plan participants falls onto the shoulders of the unelected DOL. The DOL by sheer fiat can and should “modernize” ERISA through its largely unaccountable authority to interpret the statute. Yesterday, the DOL should amend its own administrative policies to professionalize the rollover situation, thereby better guaranteeing that sound, prudent, ethical investment advice is rendered. When this professionalism does not transpire, the same civil liability of professionalism in the financial planning industry. Together, they have long been recognized as the vanguard of professionalism within the Industry, and there the DOL should go and initiate the required professionalization of financial planners/advisors.

The need to do this is clear. Achieving retirement security depends on both the plan participant’s contribution and investment decisions. Investment decisions for the long-term inherently involve financial literacy, as well as a financial planning discipline incessantly applied to one’s own retirement account. This bunch of individual sticks will then become a huge pile of gold since as a nation the cumulative successes of well-informed participants rolling over their 401(k) plans will help circumvent the abyss. The need for action is now.

Many studies have scrutinized the “three-legged stool” of federal retirement policy and concluded that two “legs,” personal savings and Social Security, are rotten. Social Security is projected to fiscally collapse within the next 20 to 25 years unless hugely controversial changes are implemented, and personal savings rates are at their lowest levels since 1939. As it stands, retirement income security will primarily emanate from plan participants’ investment decisions over the years. Thus, whether plan participants are making sound investment decisions is crucial. Nothing is more important to our nation’s financial future than this. Nothing.

Sex Education and 401(k) Education Have This in Common: How Much Disclosure Is Too Much!

Most Americans have unrealistic retirement expectations. Read the proof. A 1993 study (the Bernheim Study) revealed that nearly two thirds of those most financially poor felt their retirement standard of living would be as high or higher than it was today, even though most
heartyly acknowledged they had not squirreled away enough nuts, and had put no genuine faith in Social Security. This is a national malady of grave consequence. We have become a ship of fools.

As for more proof this ship has sailed, the 1997 Retirement Confidence Survey discovered that only 6% of Americans believe this nation has “saved” enough money to live comfortably throughout their retirement years. Sixty-eight percent were confident they would enjoy a comfortable white-sandy retirement, despite roughly 55% having never bothered to calculate their retirement savings needs. Only 36% had tried to figure out how much they needed for retirement.

The DOL is at the wheel of this ship, shouting ever-more orders of compliance. The investment industry is shackled down below, rowing harder to comply, not invest. Agencies with many faces are also chiming in more orders at the rowers. There are more personalities, positions, perspectives and officers than there are people on this ship. The madness continues . . . out of the 36% who had attempted a calculation, 24% could not give a figure when asked. Approximately 75% of employees have no idea of how much money must be saved for a rational retirement. Every financial planner (ChFC, MSFS and/or CFP) knows that there can be no withdrawal rate unless one knows how much should be saved. And issuing another compliance order absolutely will not give one plan participant this critical figure. Somebody call a financial planner, or soon enough, you will be calling in the lawyers.

It has been repeatedly proven that the public lacks the financial literacy needed to properly invest their retirement monies. The Bernheim Study concluded this: Existing literature demonstrates that most Americans cannot manage their personal finances, and their bad choices are indicative of this ignorance. Many Americans do not understand the most basic and common financial instruments, and almost half could not explain the difference in average returns between mutual funds and federally insured certificates of deposit. Likewise, the 1996 Retirement Confidence Survey reached a similar conclusion, finding that most American workers had limited financial literacy regarding key issue in retirement planning. Only one third displayed superior financial literacy, half had moderate financial literacy and the rest only a modicum of financial literacy. Not surprisingly, workers’ educational level and household income were highly predictive of their financial literacy as to retirement planning.

Given that the final amount of money in a retirement account is primarily dependent on the long-term investment decisions, from a DOL policy perspective it is crucial for plan participants to be informed, not merely educated, as to how to best invest. A deluge of disclosed information does not inherently educate, or even help. Who actually reads any significant portion of a mutual fund prospectus? Not the average American worker.

Simply put, employees don’t know how to invest. Too many do not understand basic investment strategies, nor should they. Too often, they buy high in the market and sell low, rather than vice versa. If you shorted everything they did, you would probably make a fortune. As evidence, except for company stock, mutual funds dominate the investment options offered under participant-directed 401(k) plans. DALBAR, Inc. conducted a study that concluded mutual fund investors earn far less than the widely quoted benchmark returns. For example, from 1984 to 1997 the S&P 500 Index reported an average annual return of 17% per year yet the average equity fund investor earned real returns of only 6.71% per year. These gaps between real and theoretical (benchmark) returns for the average equity fund investors were due to investors timing the market. By trying to time the market, these fund investors ended up “buying high and selling low,” thereby committing the cardinal sin of investing.

By now, it should be apparent that many individuals have no real working knowledge of the historical returns of stocks or bonds. Only two thirds of workers knew that the U.S. stock market over the past 20 years provided a greater rate of return than U.S. government bonds. Only half knew an employee stock ownership plan is typically more volatile than a diversified stock portfolio. And as if this were not bad enough, American workers do not comprehend Longevity Risk, by greatly underestimating how long they will live. When asked about male life expectancy of a 65-year old retiree, less than half knew life expectancy was 80 years. Significantly, a majority underestimated average life expectancy.

We are living much longer than before. The problem now is not dying too soon; but rather, plan participants outliving the source of income, a factor that makes wise investment for retirement years a national concern. Studies have shown that even relatively prosperous members of the baby boom generation have expressed fears about living too long, thereby outliving their source of income. This is why most of the business done by life insurance companies is now in annuities and not in life insurance. The shift toward an older population meant that financial service professionals began to look at their clients’ financial and estate plans. Thus, the market created financial planners, so ready to be used by the DOL, instead of more compliance. One more compliance rule is needed. No ERISA plan rollovers unless executed by a professional financial Planner (ChFC, MSFS and/or CFP).

The combination of a marketplace in transition, an aging population and evolving judicial standards translates into increased legal liability and a more complex range of ethical responsibilities. But any artful response
by the DOL is yet forthcoming. The American public is part of the problem. This systematic lack of retirement planning financial literacy within the public means that this nation as a whole has no realistic retirement goals or quality long-term investment advice or knows roughly how much money will be needed for an adequate retirement. This deficit of financial literacy might be manageable if plan participants sought advice from retirement professionals such as financial planners. But according to the Blenheim Study, people rarely seek professional guidance. Instead, most wing it, take offhand advice from friends, relative or parents. Workers with their unwillingness or inability to calculate the amount needed for retirement and their poor investments, coupled with their gross underestimation of how many years they will live in retirement, are blithely sailing for financial disaster.

Ironically, there is a small Continental Army, a small cadre of professional financial planners who could very possibly turn the tide of impending doom headed to our nation. Despite all the recent vitriolic projectiles hurled at the financial planning community, the ever-increasing inability to survive in an industry evermore so commoditized along all fronts, there still remains a stalwart group waiting in the dead cold for any viable opportunity from the DOL to serve this nation ethically and competently. To allow only professional financial planners to execute ERISA rollovers would supply this small cadre the chance to help this nation win the War Against Retirement Scarcity.

### The Fact That Plan Participants Might Change Their Asset Allocations in Response to Education Is Not Dispositive These Changes Will Generate Gains as Opposed to Losses

An EBRI study at IBM, AT&T and New York Life Insurance Company discovered that most plan participants made irrational investment allocation decisions that put them at risk of accumulating insufficient assets for retirement. All of the EBRI study 401(k) plan participants received ample education materials. However, portfolio theory is highly complex, with successful experts often contradicting each other on key theoretical and practical points. In addition, due to DOL regulations, education materials concerning investment allocation tend to be banal in nature. It would be like receiving a primer on football tackling, and then thinking you could single-handedly beat the Green Bay Packers. How can the DOL honestly expect a worker to use primer educational material, which apparently if properly inculcated according to the DOL would enable said worker to beat Wall Street? Let’s have the DOL invest their own retirement by using only their approved educational materials and see how they fare against Wall Street.

The service provider scrupulously avoids the rendering of investment advice so as not to be deemed a fiduciary. With their withdrawn 2010 fiduciary rule proposal, the DOL has signaled that any recommendation by a nonfiduciary to take a distribution, combined with a recommendation about how to invest the rollover, may very well result in functional fiduciary status for the adviser. As a result, service providers carefully avoid investment advisor status by providing only drab educational materials instead of valuable investment planning advice.

Section 405(a)(2) does not mandate the employer have actual knowledge of the investment advisor’s fiduciary breach to trigger cofiduciary liability. Therefore, cofiduciary liability could be triggered unknowingly as a result of an advisor’s breach of the duty of care by, for example, failing to monitor the activities of the cofiduciary investment advisor. Thus, both the employer and any investment advisor are highly motivated to give plan participants educative substance with the culinary value of frozen oatmeal. And the blame here lies with the DOL and its regulations.

The 404(c) regulations did eliminate an employer’s potential fiduciary liability for investment losses, thereby encouraging employers to allow participants to direct the investment of their retirement savings. But 404(c) regulations do not require the employer to provide plan educational materials or investment advice. And to do the latter, could confer fiduciary status on the investment advisor under the DOL’s broad definition of a “fiduciary investment advisor?” Thus, both employers and plan service providers work hard to limit information and assistance strictly to those specific types of information and disclosures required by the 404(c) regulations. To do otherwise is to risk that these educational materials or assistance will be interpreted by the DOL to be the fiduciary; thus rendering individualized “investment advice” to plan participants. By avoiding fiduciary investment advisor status, both the service provider and the employer avoid potential cofiduciary liability.

When fiduciary status is avoided successfully, the service provider must only adhere to prohibited transaction rules of section 406(a), and not to the more stringent fiduciary prohibited transaction rules of section 406(b). Since there are no clearly applicable class exemptions, these fiduciary-prohibited transaction rules disallow the service providers from receiving fees deducted at the mutual fund level out of mutual fund assets. Therefore, the nonfiduciary service provider can still receive a reasonable fee or commission through a deduction from the participant’s account for nonfiduciary services provided to the plan. Consequently, there is substantially less liability and
substantially more revenue to be gained by not providing investment advice to plan participants, and thereby remaining a nonfiduciary. These are some of the key reasons fiduciary status is avoided. In the end, plan participants do not get the personalized financial plan they need, and the education materials they receive due to DOL regulations are intended and written for the general public.

To make matters worse, these required disclosures and education materials, while of a general nature, are directed at a high level of financial literacy, which the vast majority of workers simply do not possess. In fact, only the upper end financial planners plan with these education materials subsumed in their comprehensive financial plans.

As for employers, if through the service providers’ actions they are deemed a co-fiduciary, they then must fulfill their own fiduciary duty of care, by prudently monitoring the investment advisor. This supervisory responsibility grates employers, who want fewer administrative tasks, not more. Few employers have the expertise to determine whether or not an advisor is acting professionally.

The DOL Policy Approach Stymies Core ERISA Objectives

ERISA involves two core legislative objectives at seemingly cross-purposes. On one hand, Congress endeavored to protect plan participants and ensure the security of their retirement benefits. On the other hand, Congress retained the existing system of voluntarily sponsored retirement plans by private parties, and wanted to prevent ERISA from becoming so complex that administrative costs or litigation expenses unduly discourage employers from offering employee benefits plans in the first place.

The most grievous error within the 404(c) regulations is their monolithic treatment of plan participants as highly financially literate decision makers. This article has already cited evidence indicating participants vary widely as to their financial literacy, although much of it is quite low. Plan participants’ ability to apply sophisticated investment theories needed for comprehensive financial planning is largely nonexistent.

The 404(c) regulations do not require simple and straightforward educational materials be provided to plan participants. Rather, the 404(c) regulations’ informational requirements conveniently presume a financial level of literacy that could aptly analyze a securities prospectus. That is an unreasonably high bar for the typical plan participant.

The 404(c) regulations then add grievous injury to insult by providing that the employer has no obligation to provide investment advice. Plan participants are presumed sufficiently financially literate once merely given the required disclosure material. This bureaucratic blizzard of information, so much of it incomprehensible, frees the employer of its fiduciary duty and ensures that plan assets are professionally diversified.

Yes, it gets worse. For most Americans, to have any real hope of an adequate income in retirement, they must invest largely in securities. In general, a bond portfolio will simply not do in the long run. This puts the employee in the double-trouble of having to invest in risky assets over the long haul and of eventually being separated from his or her employment, which statistically speaking, most employees will undergo more than a few times in their vocational lifetime. This means multiple rollovers subsequent to multiple jobs. A long-term professional is needed for each of these key junctures, and the only financial planner up to the task is one having ChFC, MSFS and/or CFP behind his or her name.

Interpretive Bulletin 96-1 continues the DOL’s monolithic “one-size-fits-all” policy approach. Safe Harbors 1 and 2 motivate employers to provide generic educational materials to participants. ERISA’s summary plan description requirements already administratively forced employers to submit much of this “safe harbor” information to plan participants. For any educational material not already required, such as the blasé investment information of safe harbor Category 2, the DOL’s own 1975 regulation made it clear that such general investment material was not fiduciary investment advice. Thus, Safe Harbors 1 and 2 merely codified preexisting DOL policy.

The incessant problem addressed by Interpretive Bulletin 96-1 concerns the asset allocation models and the interactive investment materials of Safe Harbors 3 and 4. Material is “educational” and does not constitute investment advice if disclosure requirements are satisfied, and all participants can assess the relevance of the models and materials for their individual circumstances and apply them accordingly. Thus, the DOL rationalizes, participants will not “rely” on the models and materials when making investment decisions. This rationale presumes that every participant has the financial literacy to properly assess the facts and assumptions that underlie the models and materials and, after such, ably apply this assessment to their own fact-specific situation.

This rationale conflicts starkly with the empirical evidence. It is simply untrue to believe plan participants are not relying on the investment allocations and specific mutual funds suggested by these models and materials. Participants must rely on these materials; they are not financial planners. They lack the requisite financial literacy to evaluate the key assumptions imbedded in the models and materials, such as life expectancies, replacement income ratios, inflation rates, income levels, financial resources and investment rates of return.
Initially, the DOL initially issued Interpretive Bulletin 96-1 to encourage investment education for plan participants. Interpretive Bulletin 96-1 in relation to 404(c) regulations imposes a substantial burden on the employer, which results in plan participants being less likely to receive real help in making investment decisions. By imposing on the employer a fiduciary duty to select and monitor any education provider or investment advisor, Interpretive Bulletin 96-1 makes it increasingly difficult for the employer to figure out his or her fiduciary duty as the education provider advances up the Interpretive Bulletin’s safe harbor levels (1, 2, 3 and 4).

At the Safe Harbor Level 1 (plan information), the employer easily can ascertain that the educational materials are accurate in their description of the employer’s own plan and its basic features, benefits and investment options. At Safe Harbor Level 2, educational information on general financial and investment concepts, it is more difficult for the typical employer to monitor for accuracy. At Safe Harbor Levels 3 and 4, asset allocation models and interactive investment materials, the employer must monitor whether the models and materials are based on “generally accepted investment theories” and disclose all underlying “material facts and assumptions.” This DOL burden is far beyond the expertise of many, if not most, employers.

From this, one can see that many problems with service providers arise because the responsible plan fiduciary either does not truly understand his or her role and responsibility in the selection and monitoring of service providers or exercises poor judgment in not having sufficient experience or an appropriate source of information concerning legal requirements and industry practices.

The Solution Is Not More Compliance but, Rather, Is to Rely on Institutions That Prepare Professional Financial Planners

The DOL has three notable goals it wants achieved from educational service providers: (a) to have participants participate in the plan as soon as eligible, (b) to encourage participants to maximize contributions to the plan and (3) if participants change jobs, instead of withdrawing retirement savings in a lump sum, to execute a direct rollover into an IRA.

But to effectuate these goals, the DOL blames a “vacuous” regulatory framework in relation to the financial services industry. The solution is to put more meat on the too-thin regulatory frame, which means more rules as opposed to better administration of rules already in place. A more accountable and better DOL is needed, not more DOL. Novel strategies are needed, not necessarily more rules. Most important, assiduous supervision can compensate for ambiguous or incomplete regulations, but the most comprehensive and explicit rules cannot make up for superficial oversight or feckless enforcement. The informal and nonpublic dimension of agency supervision is well suited for the financial services industry. Rigid rules are inherently imperfect for rapidly changing and inordinately complicated institutions with a propensity to generate lethal risks out of seemingly benign activities. Try as they may, agencies have struggled to craft rules that cannot be interpreted opportunistically or otherwise circumvented. As such, supervision is a rational response to the formidable obstacles to achieving legislative objectives.

Thus, to accomplish its intended policy goals, the DOL needs to supervise financial planners who are professionals. The DOL can create this situation by deeming that all direct rollovers must be done by a financial planner (designated as one having the ChFC, MSFS or CFP) instead of issuing evermore compliance.

Client discovery involves assisting the client to formulate his or her goals and objectives. This is often quite difficult, and it takes times to conduct the client interview and fact finding, which will delve into income needs and sources, assets and liabilities as well as qualitative questions that ferret out an individual’s priorities and values. Based on the information gathered, the financial planners will then draft and present a plan clearly illustrating how a plan participant will use his or her rollover, as well as other economic resources, to accomplish his or her stated goals and objectives. For many retirement-ready participants the greatest concern involves generating sufficient cash flow to fulfill their lifestyle needs while lowering the risk of depleting their accounts. Other considerations would include the optimal age to apply for Social Security benefits as well as who to designate as their IRA rollover beneficiary. Younger plan participants would need to fully understand the adverse tax implications in taking early taxable distributions from their 401(k) plan or in determining whether a Roth IRA conversion is an appropriate action.

After the plan is presented, the next step is constructing a portfolio to generate a sufficient rate of return over time while not exceeding the individual’s risk tolerance. Risk is difficult to quantify since an individual’s tolerance for risk will vary due to various factors. Tools such as Investment Policy Statements will also educate plan participants about their portfolios, set realistic expectations and provide guideposts to discipline behavior in times of uncertainty.

Once the rollover is executed and the proceeds invested, the final step is ongoing monitoring. Unexpected market movements or tax law changes must be taken into account. At other times, there may be changing family
circumstances or renewed priorities. All of these life events trigger review and possible amendment to the financial plan, if appropriate. Financial planners should be particularly diligent with respect to excessive spending immediately following retirement. These actions, if not corrected, can thwart the ability to generate sufficient cash flow during the latter years of retirement. Needless to say, the aforementioned involves a comprehensive financial planning process done by professional financial planner, herein designated by one having the ChFC, MSFS and/or CFP.

The founder of The American College, Solomon Huebner, stated what it takes to be a professional, which is as valid today as in 1915. He cited four characteristics of the professional.

1. The professional is involved in a vocation useful and noble enough to inspire love and enthusiasm on the part of the practitioner.
2. The professional’s vocation in its practice requires an expert’s knowledge.
3. In applying that knowledge the practitioner should abandon the strictly selfish commercial view and ever keep in mind the advantage of the client.
4. The practitioner should possess a spirit of loyalty to fellow practitioners, of helpfulness to the common cause they all profess, and should not allow any unprofessional acts to bring shame upon the entire profession.39

According to Huebner, the second characteristic of a professional is possessing expert knowledge.40 The true professional needs to be competent, and stay abreast of the latest developments, not only learning what are latest beneficial practices but also understanding why they are beneficial. A special obligation is placed on the professional to put the best interest of the client ahead of the professional in dealing with those products. That leads to the Holy Grail of what the DOL has been after all along, the hardest requirement of the profession—abandoning the strictly commercial point of view.41

Professor Duska is quite correct in noting, “This is possibly the most interesting characteristic of the professional cited by Huebner, for it lays out an ethical prescription.”42 It requires the professional “to abandon the strictly selfish commercial view and ever keep in mind the advantage of the client.” It requires that in a situation where the financial planner’s interest and the client’s interests conflict, the professional must surrender his or her interest to that of the client. By the “strictly selfish commercial view” Huebner has in mind the view of those for whom the only concern of business is making money or increasing profit. It is a view voiced by extreme advocates of the free market system who insist, “The primary and only responsibility of business is to increase profit.” Such a view is inevitably a “selfish” point of view.

Significantly, Professor Duska insightfully recognizes that this is a complete distortion of the position of Adam Smith, the 18th-century economist-philosopher, who in The Wealth of Nations argued that a great deal of good comes from a system that allows people to pursue their own interests.43 This well-known appeal to the beneficial results of an invisible hand became the theoretical foundation and justification of the capitalist free market economic system. However, it is important to note that Smith insisted that the pursuit of self-interest be constrained by ethical considerations of justice and fairness. It should be enlightened self-interest.44 One may not always look out for one’s interest. There are times when it is ethically necessary to constrain self-interest in the name of justice or fairness and look out for the interests of others.

And so, how does one take the road of enlightened self-interest instead of selfishness?45 Yet again, Solomon Huebner anticipated this quandary and captured the solution in the term vocation.46 Huebner’s use of the term vocation points to his belief that an attachment to a vocation results in a personal transformation. Professor Ragatz notes that for Huebner, it is impossible to become a professional without adopting professional values.47

Conclusion

Plan participants are not a monolithic group. Their financial literacy as to retirement savings and general financial concepts ranges from the illiterate to the sophisticated. Research reveals that many plan participants do not make 401(k) plan contribution and investment allocation decisions that probably will result in adequate retirement savings; others do. This type of diversity necessitates that the DOL administer its policies for all plan participants, not just the sophisticated. Employers already give most participants adequate educational materials. But what plan participants really need, and do not receive, is comprehensive personalized investment advice. This poor decision making as to retirement planning at a national level is a direct product of DOL administrative policy.

Despite this pervasively questionable decision making, the DOL still adheres to archaic interpretations of ERISA’s fiduciary-prohibited transaction provisions that were formulated for defined-benefit plans. As a result, both employers and plan service providers are deterred from doing anything more than the bare minimum required by the 404(c) regulations. Meanwhile, the plan participants, whom ERISA was designed to protect, must accumulate adequate savings for retirement without the benefit of professional financial planners.
The ultimate goal of ERISA is to promote and protect retirement income security for plan participants. This purpose can best be achieved by providing plan participants with professional financial planners, who are fiduciaries fully accountable in making retirement planning and investment decisions. The DOL’s current interpretation of ERISA, originally developed in the context of the employer-controlled defined-benefit plan, is ill suited to today’s participant-directed 401(k) plan. This article invites the DOL to interpret ERISA in a more flexible manner and modernize its administrative policy to conform to the reality of participant decision making.

The DOL wants to leave the decision to the client. However, since being a professional means having a certain expertise, it follows that professionals usually know more than their client, so that the client is vulnerable in a market transaction. In that case, the client must trust the word of the professional, who has sufficient knowledge about what courses of action are advantageous to the client. In the end, the client as always has final say. Everyone agrees on informed consent. It’s the kind of informing that the fuss is all about. Doctors, attorneys, accountants inform, as do DOL Assistant Secretaries, and no employee or plan participants has the last say with the DOL, irrespective of whether or not their national policies hurt or help this nation.

By far, most plan participants do not understand the complexities or do not have the time or desire to understand them. They need a financial planner to enable them to decide which rollover option is in their best interest. If you want to prevent cross-selling, then stop treating financial planners like salesmen. The DOL must stop commoditizing whole areas of financial planning and then hypocritically demanding that the treatment of the product, the client and the entire situation be analyzed and addressed by a professional with a fiduciary duty. The DOL must start helping by molding a professional class that is treated like a professional by carving out a niche area wherein only professionals are licensed to do what the DOL wants done. Only someone with an MSFS, ChFC or CFP should be able to do a rollover to an IRA. Stop holding salesmen to a professional standard and then make sure they paid like transactional salesmen for a situation (the rollover) that is so regulated by the DOL as to commoditize the very product the DOL wants deeply and professionally analyzed before moved into any possible IRA.

The DOL must realize that the market is demanding that financial planners and their products be blended together with services provided by multidisciplinary firms offering financial, tax, legal and accounting advice.48 By and large, there are no insurance “salesman” anymore, and none with the ChFC, MSFS and/or CFP levels of education. The number of insurance agents has dropped dramatically in the past several years, almost 25% from 1991.49 Today, no financial planner would describe themselves as simply insurance professionals. The DOL must be fully aware that the insurance industry’s sales force was only surviving by becoming more professional in terms of financial planning, estate planning and taxes. These are the financial planners of today, having attained higher levels of expertise at The American College (ChFC or MSFS) and/or becoming a CFP.50

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Notes

3. Individual IRAs do not come under the administrative jurisdiction of ERISA, and are currently regulated by IRS under the Prohibited Transaction Rules of the Internal Revenue Code. The IRS can also enforce excise taxes on fiduciaries engaged in prohibited transactions and self-dealing in IRAs.
5. For these reasons, most errors and omissions policies do not cover fiduciary services from registered representatives.
or insurance agents to ERISA-covered clients. Thus, most broker-dealers and insurance companies prohibit advisers and agents from acting as ERISA fiduciaries.


7. Four types of plan service providers can aver ERISA fiduciary status: (a) adversaries, (b) employer educators, (c) platform providers and (d) appraisers. Note: Adversaries must be clear that they are acting on behalf of a vendor and do not provide impartial advice. Educational materials provide general financial, tax or investment information and are covered separately under DOL Interpretative Bulletin 96-1. The original EBSA proposal is located at http://webapps.dol.gov/FederalRegister/PdfDisplay.aspx?DocId=24328

8. www.dol.gov/ebsa/newsroom/ty072611.html


10. Twelve large financial firms, representing 19 million IRA holders and $1.8 trillion in assets, participated in a study. Its findings were submitted to EBSA and made public in April 2011: http://www.dol.gov/ebsa/pdf/1210-AB32-PH060.pdf


13. JD, MBA, CPA, Series 6, 65 or 7 will not suffice. What is needed is a professional who by training takes a comprehensive financial viewpoint, a long-term–planning viewpoint.

14. ERISA is primarily responsible for the regulation of private employer-sponsored retirement plans. ERISA’s original section numbers were changed in Title 29 of the United States Code, which contains the federal labor provisions.


17. The 1997 Retirement Confidence Survey was organized by the Employee Benefits Research Institute, the American Savings Education Council and Mathew Greenwald & Associates, Inc.

18. 1997 Retirement Confidence Survey, p. 3.


20. 1997 Retirement Confidence Survey, p. 3. The 1998 Retirement Confidence Survey discovered the figure increased to 45%.


24. Dalbar Study update, p. 3.


41. Duska (2005, p. 48; Note 26).
42. Duska (2005, p. 48; Note 26).
43. Duska (2005, p. 49; Note 26).
44. This mandate is embodied in the pledge that all new Chartered Life Underwriter and ChFC designees of The American College must make. In all my professional relationships, I pledge myself to the following rule of ethical conduct: I shall, in light of all conditions surrounding those I serve, which I shall make every conscientious effort to ascertain and understand, render that service which, in the same circumstances, I would apply to myself. (*The professional pledge: The eight canons*, http://www.theamericancollege.edu/assets/ethics/Ethics_PledgeCannons.pdf)
45. The words *self-interest* and *selfishness* have very different meanings. It is important and natural for people to look out for their own interests. In fact, if people are not self-interested, or if they do not have a healthy self-love, they do both their neighbors and themselves a disservice. Ragatz and Duska (2010, p. 299; Note 12). At times, one senses that the DOL is so busy trying to create the New Man by evermore compliance that they fail to note the goodness in proper self-love, so ably noted by Professors Duska and Ragatz.
46. Ragatz and Duska (2010, p. 298; Note 12).
47. Ragatz and Duska (2010, p. 298; Note 12).
49. “At year end 2001 there were almost 179,000 full-time affiliated agents contracted with 97 companies, down 8 percent from the count in 1998, and down 25 percent from 10 years ago”: LIMRA International, Inc. (2003). *Census of U.S. sales personnel: Calendar year 2001* (p. 6). Windsor, CT: Author.
50. Duska (2005; Note 26).

**Author Biography**

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