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The Fiduciary Rule Needs To Benefit Brokers And Savers

Alex Verkhivker

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By law, anyone age 70 ½ or older is obligated to begin withdrawing money from their retirement accounts. Termed required minimum distributions (RMDs), the amount is calculated by incorporating one's life expectancy and applies to traditional 401(k), 403(b) and 457(b) plans as well as traditional IRAs and simplified employee pension (SEP) plans. According to data from the U.S. Census Bureau, the number of people crossing the 70 ½ mark will nearly double to 60 million over the next two decades.

These forced withdrawals are creating headaches for Wall Street's biggest money managers, particularly as the flow of contributions to retirement plans has begun to wane compared with deductions from those plans. Investors pulled a net $9 billion from employer sponsored retirement-savings plans in 2013 with the figure skyrocketing to $24.9 billion in 2014. According to executives at brokerage firms across the country, companies will have to lower fees and offer more client services that persuade those nearing retirement age to keep their savings with their money managers. Charles Schwab is just one such money management firm that has felt the effects of retiring baby boomers beginning mandatory withdrawals from their retirement accounts. The firm, which manages over $200 billion in 401(k) assets, has had to lower fees and educate their clientele about the legislation regarding deductions from 401(k) retirement accounts.

The Department of Labor's Fiduciary Rule is making headways since President Donald Trump's recent attempts at overhauling Dodd Frank. The ruling expands the "investment advice fiduciary" definition under the Employee Retirement Income Security Act of 1974 to require financial advisors to act in the best interests of their clients. With more than 1,000 pages of legalese, the Fiduciary Rule requires fiduciaries to put their clients' interests above their own. The rule, set to take effect April 10, is meant to ensure that retirees receive advice that protects their financial interests but has drawn the ire of the Republican dominated Congress. Financial industry experts predict that a revision will likely follow the April 10 implementation date, most likely causing the rule to be delayed for many months after April. The annuities industry in particular has taken issue with the rule as agents earn commissions and other sales perks from the number of annuities sold. Prior to the rule, brokers worked under suitability standards that merely required them to make recommendations that were suitable for their clients, not necessarily those that were in their best interests.

A number of recent court orders have upheld the rule, making it tougher for the Trump administration to altogether repeal the rule. The brokerage industry has already spent hundreds of millions of dollars in preparation for the April implementation date, but Trump and the Republican led Congress are looking for any and all ways to minimize regulation for Wall Street firms. Firms like UBS Group AG and LPL Financial Holdings that both house thousands of brokers believe a single fiduciary standard that applies to both retirement savings and non-retirement accounts would simplify implementation of a best-industry standard for mitigating conflicts of industry from financial advisers offering financial services to clients.

Paul Smith, Chief Executive of the CFA Institute, the group that administers the chartered financial analyst exams, has said that removing the rule would do more harm than good, including those that voted for Trump. The Obama administration believed the rule would save American families nearly $17 billion a year from bad advice and eliminate lower annual returns on retirement savings vehicles. Outside consultant firms like A.T. Kearney have projected upwards of $20 billion in lost revenue for the financial services industry.

It's difficult to think that brokers would do anything but try to give advice that pays them the biggest commissions rather than hone in on the best actionable suggestions for their clients. Thaya Brook Knight, associate director of financial regulation studies at the Cato Institute, offered the following view:

"The biggest risk is that the cost of compliance in particular for a broker who typically works on commission would be so great that they would just stop offering advice." Brokerage Merrill Lynch, which manages more than $2 trillion in client assets, says it will stop commission-based compensation for the management of retirement accounts, and instead, charge a flat fee based on the percentage of an account holder's assets. Other brokerages like Wells Fargo & Co, LPL Financial Holdings Inc. and Morgan Stanley aren't ready to do away with commissions entirely.

Barbara Roper, director of investor protection at the Consumer Federation of America, suggests that investors need to do the work that the fiduciary rule tries to set up. "Try on an individual level to re-create the protections that the regulation would have put in place," notes Roper. "Or you can go to a firm that says they're moving forward with putting in place a fiduciary standard and reward them."

So do financial advisers owe their clients a duty of loyalty and prudence with retirement saving dollars, or do advisers have a right to provide advice that is also in the best interest of their personal pocket books? The Trump administration appears to believe that American investors should make independent financial decisions and be well-informed participants in the financial marketplace, building individual wealth the best way they know how. These investors also happen to include financial advisers, who also must save for retirement and provide for their families in their non-working years.

The rule has clearly divided both sides of the political spectrum particularly for the reason that some believe financial advice is an inherently conflicted construct. Those receiving financial advice argue for broader regulation for those issuing the advice. I believe that advisers should be advised to conduct their business under law-abiding standards for professional conduct, such that those receiving financial advice benefit from prudent and accurate advice, while financial industry brokers also have the ability to make increased profits from more sales.

President Trump's decision to sign an executive order calling for a review of the rule suggest that his presidency will favor consumer choice, placing the onus on retirees to invest their money prudently by searching for the best money manager for them and their families.

"We think it is a bad rule. It is a bad rule for consumers," notes White House National Economic Council Director Gary Cohn. In an interview with the Wall Street Journal, Cohn notes that the rule is akin to "putting only healthy food on the menu, because unhealthy food tastes good but you still shouldn't eat it because you might die younger."

Revising the regulation will hopefully mean what is in the best interests of brokers, insurance agents and consumers, such that main street and Wall Street can see to it that both their interests are kept in mind. By lessening the regulation on the financial industry, Trump reminds Americans that the onus is on them to take any advice with a grain of salt.