The Asset Management Industry
SERVING INDIVIDUAL INVESTORS
INVESTMENT COMPANY INSTITUTE

MEMO# 13746

July 19, 2001

INSTITUTE SUBMITS WRITTEN TESTIMONY FOR HOUSE SUBCOMMITTEE HEARING ON H.R. 2269, "THE RETIREMENT SECURITY ADVICE ACT"

[13746] July 19, 2001 TO: PENSION COMMITTEE No. 48-01 INVESTMENT ADVICE AD HOC COMMITTEE No. 3-01 RE: INSTITUTE SUBMITS WRITTEN TESTIMONY FOR HOUSE SUBCOMMITTEE HEARING ON H.R. 2269, "THE RETIREMENT SECURITY ADVICE ACT" On July 17, 2001, the House Committee on Education and the Workforce, Subcommittee on Employer-Employee Relations, held a hearing on H.R. 2269, the “Retirement Security Advice Act.”1 As you know, H.R. 2269, introduced by Chairman John Boehner (R-OH) of the House Committee on Education and the Workforce, would provide a statutory exemption from ERISA’s prohibited transaction rules for the provision of investment advice. The Institute submitted written testimony urging enactment of the bill. The following witnesses testified at the hearing: (1) Ann Combs, Assistant Secretary, Pension and Welfare Benefits Administration, U.S. Department of Labor, (2) Betty Shepard, Human Resources Administrator, Mohawk Industries, (3) Richard Hiller, Vice President, Western Division, TIAA-CREF, (4) Jon Breyfogle, Principal, Groom Law Group, on behalf of the American Council of Life Insurers (ACLI), (5) Damon Silvers, Associate General Counsel, AFL- CIO, and (6) Joseph Perkins, Immediate Past President, AARP. Four of the testifying parties — the Department of Labor, Mohawk Industries, TIAA-CREF and ACLI — expressed support for H.R. 2269. The AFL-CIO and AARP opposed the bill. Institute Testimony. The Institute’s written testimony noted that despite participants’ need for investment advice regarding their retirement assets, only 16 percent of 401(k) participants have an investment advisory service available to them through their retirement plan. The “advice gap” is a result of current legal constraints imposed by ERISA’s prohibited transaction rules, which prohibit participants from receiving investment advice from the financial institution managing their plan’s investment options. And although current law allows “third-party” advice providers to give advice to participants, the advisory services they offer have not sufficiently addressed the problem. In light of the gap that currently exists, the Institute’s testimony urged enactment of H.R. 2269. By removing the legal barriers that significantly inhibit participants’ access to investment 1 See Institute Memorandum to Pension Committee No. 40-00 and Investment Advice Ad Hoc Committee 2-01, dated June 25, 2001. 2advice, the bill would expand and enhance the investment advisory services available to participants by allowing advice to be obtained from a broad array of providers, including the financial institutions already providing investment options to their plans. In addition, the bill would impose a panoply of protections for participants. Advisers under the bill would assume fiduciary status under the stringent standards for fiduciary conduct set forth in ERISA; such “fiduciary advisers” also

would be subject to an extensive disclosure regime under which they would be required to provide timely, clear and conspicuous disclosures to participants that identify any potential conflicts of interest. Finally, the testimony noted that plan participants would have legal recourse under the bill if a fiduciary adviser were to violate the standards set forth in the bill or ERISA. Department of Labor Testimony. Representing a significant shift from the Department's opposition to the bill last year,2 Assistant Secretary Ann Combs expressed support for H.R. 2269. Specifically, Ms. Combs' testimony provided that the protections in H.R. 2269 "create a basic framework for assuring that advice is fairly provided and [that she] would welcome the opportunity to work with the Committee to ensure that these protections are adequate." Additionally, she stated that "legislation like [H.R. 2269] will bring flexibility to the area by setting forth rules for all affiliated investment advisors. The Advice bill will also place affiliated advisors on a more equal competitive footing with non-affiliated advisors, will foster competition among firms, and promote lower costs to participants." In conclusion, Ms. Combs commended the Subcommittee's efforts "to deal with this important issue and seek the same objectives as proposed by [the] bill — strong protections and certainty for participants, employers and service providers, a level playing field, greater choice among advisers and the expansion of needed investment advice for participants and beneficiaries in 401(k) type plans." She indicated, however, that the Department "would like to work with [the Subcommittee] further on other aspects of the bill that go beyond the provision of investment advice to participants and beneficiaries." Testimony of Other Witnesses. Ms. Shepard of Mohawk Industries, an employer that sponsors a large defined contribution plan, testified that their employees seek "specific investment advice." However, because of the "substantial fiduciary liability associated with the delivery of specific advice under current law," Mohawk currently does not offer access to advice to their employees. Additionally, Ms. Shepard noted that "while Internet based services can assist many plan sponsors, [Mohawk does] not feel that this will adequately address [their] employees' needs, as the majority do not have access to the Internet at home or work." Thus, Mohawk supported passage of "this important law so that [they] can provide [their] employees with the professional investment advice that they need to make good, sound investment decisions." Mr. Hiller of TIAA-CREF also observed that participants are "seeking out retirement savings advice" — advice that is "personalized to the individual's situation." Because H.R. 2269 "will provide employees with much needed investment advice in an increasingly complex retirement planning environment . . . [while affording] substantial protections to employees.", he expressed TIAA-CREF's strong support for the bill. Similarly, Mr. Breyfogle, representing 2 See Institute Memorandum to Pension Committee No. 51-00 and Ad Hoc Committee on Investment Advice, dated July 20, 2000 (referencing Department of Labor letter opposing investment advice legislation). 3ACLI, highlighted participants' desire for investment advice and described the legal impediments that prevent its availability. His testimony encouraged enactment of H.R. 2269 because it would address these legal barriers by striking "the right balance of allowing comprehensively-regulated financial services firms to provide specific investment advisory services, while at the same time carefully protecting the interests of plan participants." As noted above, the AFL-CIO and AARP expressed strong opposition to the bill. Mr. Silvers of the AFL-CIO asserted that "there is no crisis in the provision of investment advice that requires the solution of allowing conflicted investment advice. On the contrary, given the prevalence of independent advice firms, there is real reason to believe that financial services firms' desire to get into the business themselves is self-interested, and it is easy to understand what [is the] source of that self-interest — the possibility of literally shifting billions of dollars from workers' retirement accounts to their own firms." Likewise, Mr. Perkins, representing AARP, opposed the provisions of H.R. 2269, arguing that it would be "premature to weaken ERISA's current conflict of interest rules" in light of the availability of

third-party advice providers under current law. Rather, AARP supported efforts to encourage employers to provide advice under existing legal standards. To the extent that an approach similar to H.R. 2269 is considered, Mr. Perkins suggested two alternatives: first, a “conflicted advisor” could be permitted to “provide advice so long as the plan also makes available at least one other alternative independent advisor on the same terms and conditions for plan participants”; second, a “higher duty” could be imposed on a plan sponsor in the event that it chooses an adviser that is “subject to a conflict of interest.” For additional details, please refer to the following attached documents: (1) the Institute’s written testimony, (2) the Department of Labor’s testimony, (3) testimony submitted by the other witnesses, and (4) opening statements made at the hearing by Representative Sam Johnson, Chairman of the Subcommittee, and Representative Boehner. Thomas T. Kim Assistant Counsel Attachment Attachment (in .pdf format)

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