FinancialPlanning

Obama to Lead Push for Fiduciary Rules

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(Bloomberg) -- The White House plans to throw its full weight behind a Department of Labor proposal to make it harder for brokers to push higher-fee mutual funds or other expensive products on people saving for life after work. The plan would require brokers to act in a customer's best interest, a change that could limit the earnings of financial advisors.

President Obama's expected involvement Monday underscores the opposition the government faces in revising 40-year-old rules that affect tens of millions of baby boomers nearing retirement and younger workers without pensions. Having beaten back previous efforts to update the rules, Wall Street now has more at stake. Banks have boosted their asset-management businesses after the 2008 financial crisis, while curtailing riskier and more capital-intensive trading units.

The move amounts to the Obama administration picking a fight with Wall Street over the handling of Americans' $11 trillion of retirement savings, accusing brokers of skimming significant sums annually from small investors and urging new protections against biased financial advice.

'OUTDATED RULES'

The outdated rules create an unfair playing field making it hard for good advisors to compete, and making it harder for working and middle-class families to know who they can trust, Jeff Zients, director of the White House National Economic Council, said on a conference call with reporters Sunday. He was joined by other administration officials and Vanguard Group founder John Bogle.

Obama is scheduled to tout the Labor Department proposal at an AARP event Monday along with U.S. Senator Elizabeth Warren of Massachusetts, whose popularity has surged among Democrats based on her claims that bankers and the financial industry too often try to take advantage of workers.

Officials declined to outline specifics of the plan to impose a fiduciary duty, which will crack down on backdoor payments and hidden fees earned by brokers, according to a fact sheet issued by the White House. The proposal will be sent Monday to the Office of Management and Budget for review, Labor Secretary Tom Perez said on the conference call.

It could take several months before the rule is publicly released, Perez said. That step will allow the securities industry, investor groups and lawmakers to comment on the plan before the Labor Department can issue a final regulation.

ISSUE DISTORTED

At the heart of the proposal is an effort to tighten the legal standard for brokers handling retirement funds in individual retirement accounts and 401(k)s, which now hold more than $11 trillion. Under current rules, brokers can sell any product that is suitable for an investor, meaning it fits the client’s needs and tolerance for risk.

Industry groups say the White House and Labor Department have distorted the issue and disregarded existing tough rules that regulate how brokers make money. Those measures are enforced by the SEC and FINRA.

Brokers typically earn money from upfront sales commissions or fees paid by investors who purchase mutual funds. White House officials said that kind of compensation arrangement provides an incentive to recommend products that net higher fees or commissions without yielding better returns for investors. Clients lose as much as $17 billion a year from such conflicted advice, according to the Obama administration.

“ The corrosive power of fine print, hidden fees and conflicted advice can eat away like a chronic illness at people’s hard-earned retirement savings, Perez said.

MORE LAWSUITS

Investors are particularly vulnerable to conflicts of interest when moving investments from an employer-sponsored 401(k) plan to an IRA, the White House said. That process allows brokers to steer investors into products that earn them higher fees. The average IRA rollover for investors between 55 and 64 years old in 2012 was more than $100,000, according to Jason Furman, chairman of Obama’s Council of Economic Advisers.

Subjecting brokers to a fiduciary duty, a standard that now applies to professional money managers, will lead to more lawsuits against the industry and add burdensome compliance requirements, industry groups argue.

The added costs will probably prompt brokers to drop client accounts with less than $50,000 of assets, leaving those investors to manage their own savings, according to the SIFMA.

We have ongoing concerns that the DOL and the White House have completely ignored the existence of the robust regulatory regime under SEC and FINRA, and this re-proposal could make it harder to save for retirement by cutting access to affordable advice and limiting options for savers, SIFMA Chief Executive Officer Kenneth Bentsen said in a statement. The DOL re-proposal could ultimately raise the cost of saving and hurt all Americans trying to save for retirement, particularly middle- class workers.

RESTRICTING CALL CENTERS

When the Labor Department issued a fiduciary duty proposal in 2010, financial companies including JPMorgan Chase and Fidelity Investments said it was overly broad and would cover activities such as communications with call centers that process routine questions from investors. Morgan Stanley questioned whether selling investors bonds from a broker’s inventory could have been prohibited by the earlier plan.

Congressional Republicans also opposed the earlier plan, with the House approving legislation in 2013 that would have blocked the Labor Department from taking action.

Perez said the new rule will be very different from earlier versions of the plan and would spell out practices, such as sales commissions and fee sharing, that would still be allowed.

I’m confident we can actually do more to help the small and moderate savers in the context of the proposal we will be putting forth, he said.

--*With assistance from Toluse Olorunnipa in Washington.*