

For Immediate Release

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FACT SHEET: Middle Class Economics: Strengthening Retirement Security by Cracking Down on Backdoor Payments and Hidden Fees

“That’s what middle-class economics is—the idea that this country does best when everyone gets their fair shot, everyone does their fair share, and everyone plays by the same set of rules.”

President Barack Obama, State of the Union Address, January 20, 2015

Middle class economics means that Americans should be able to retire with dignity after a lifetime of hard work. But today, the rules of the road do not ensure that financial advisers act in the best interest of their clients when they give retirement investment advice, and it’s hurting millions of working and middle class families.

A system where Wall Street firms benefit from backdoor payments and hidden fees if they talk responsible Americans into buying bad retirement investments—with high costs and low returns—instead of recommending quality investments isn’t fair. These conflicts of interest are costing middle class families and individuals billions of dollars every year. On average, they result in annual losses of 1 percentage point for affected investors. To demonstrate how small differences can add up: A 1 percentage point lower return could reduce your savings by more than a quarter over 35 years. In other words, instead of a \$10,000 retirement investment growing to more than \$38,000 over that period after adjusting for inflation, it would be just over \$27,500. [Today, President Obama is taking a step](#) to crack down on those Wall Street brokers who benefit from backdoor payments or hidden fees and don’t put the best interest of working and middle class families first.

Many advisers do not accept backdoor payments or hidden fees and work on a different business model that puts their customers’ best interest first. They are hardworking men and women who got into this work to help families achieve their dreams and want a system that provides a level playing field for offering quality advice. But outdated regulations, loopholes, and fine print make it hard for working and middle class families to know who they can trust.

During the financial crisis, we saw the devastation caused on Main Street when outdated policies let lenders steer their customers into bad mortgage products. That’s why in the wake of the crisis, the President fought to create the Consumer Financial Protection Bureau. Since then, the CFPB has cracked down on many of the abusive lending practices that led borrowers to lose their homes.

Because of outdated rules protecting retirement savings, we’re seeing similar types of bad incentives and bad advice lead to billions of dollars of losses for American families saving for retirement every year—with some families losing tens of thousands of dollars of their retirement savings. That’s why today, the President directed the Department of Labor to move forward with a proposed rulemaking to protect families from bad retirement advice by requiring retirement

advisers to abide by a “fiduciary” standard—putting their clients’ best interest before their own profits.

Backdoor Payments & Hidden Fees Are Hurting the Middle Class: [Today’s report](#) from the White House Council of Economic Advisers (CEA) shows conflicts of interest cost middle-class families who receive conflicted advice huge amounts of their hard-earned savings. It finds conflicts likely lead, on average, to:

1 percentage point lower annual returns on retirement savings.

\$17 billion of losses every year for working and middle class families.

A Wide Array of Research Shows Why Conflicts Hurt Working and Middle Class

Families: A strong set of independent research shows that these losses result from brokers getting backdoor payments or hidden fees for:

Steering clients’ savings into funds with higher fees and lower returns even before fees.

Inappropriate rollovers out of lower-cost retirement plans into higher-cost vehicles.

President Obama is Cracking Down on Conflicts of Interest: Today, the President called on the Department of Labor to crack down on Wall Street and protect families from conflicted and bad retirement advice. DOL will move forward with a proposed rulemaking that would require retirement advisers to abide by a “fiduciary” standard—putting their clients’ best interest before their own profits.

Proposed Rule Coming Soon: In the coming months, the Department of Labor will issue a notice of proposed rulemaking, beginning a process in which it will seek extensive public feedback on the best approach to modernize the rules on retirement advice and set new standards, while minimizing any potential disruption to good practices in the marketplace.

Our Retirement Rules Have Not Kept Up with Seismic Shifts in How People Save

Over the past several decades, the share of Americans’ employer-based retirement savings that takes the form of traditional pensions—where investment decisions are generally made by professionals—has fallen sharply. Today, Americans are largely responsible for making their own choices about how much to save and how to invest their retirement savings.

To help make informed choices, families often look for trusted advice on how to manage their hard-earned nest egg. However, despite the significant changes in the retirement landscape, the regulations that set the basic rules of the road on giving investment advice to retirement savers have not been updated in almost forty years. Under these outdated rules, savers cannot count on receiving the unbiased advice that they need and expect. In other words, today’s rules allow brokers to put their bottom line ahead of their clients’ retirement security. A system where middle class families shoulder 100% of the risk for their investments, but brokers receive incentives for directing them into investments that aren’t in their best interest isn’t fair.

If more retirement advisers were fiduciaries, they would have to put the customer’s best interest before their own.

Report Released Today Finds Huge Losses to the Middle-Class from Conflicts of Interest

A new [report](#) from the President's Council of Economic Advisers shows that the current, broken regulatory environment creates misaligned incentives that cost working and middle class families billions of dollars a year—with some individual families losing tens of thousands of dollars of their retirement savings. These incentives cause some Wall Street brokers to encourage working and middle class families to move from low-cost employer plans to IRA accounts that typically entail higher fees—and to steer working and middle class families into higher-cost products within the IRA market. Many advisers currently act as fiduciaries and provide advice in their clients' best interest, but many others do not. CEA's analysis of the latest academic research finds that:

Conflicted advice leads to lower investment returns for working and middle class families.

Working and middle class families receiving conflicted advice earn returns roughly 1 percentage point lower each year (for example, conflicted advice reduces what would be a 6 percent return to a 5 percent return).

An estimated \$1.7 trillion of IRA assets are invested in products that generally provide payments that generate conflicts of interest. Thus, CEA estimates the aggregate annual cost of conflicted advice is about \$17 billion each year.

A typical worker who receives conflicted advice when rolling over a 401(k) balance to an IRA at age 45 will lose an estimated 17 percent from her account by age 65. In other words, if a worker has \$100,000 in retirement savings at age 45, without conflicted advice it would grow to an estimated \$216,000 by age 65 adjusted for inflation, but if she receives conflicted advice it would only grow to \$179,000—a loss of \$37,000 or about 17 percent.

A retiree who receives conflicted advice on how to invest his IRA at retirement will lose an estimated 12 percent of the value of his savings if drawn down over 30 years compared to a retiree who receives unconflicted advice.

A marketplace where some advisers are encouraged to steer their clients into inferior products based on these payments creates bad incentives and an unfair playing field for the many firms who choose instead to put their clients' interests first.

Updating our Outdated Retirement Protections

Since 1974, the Department of Labor has protected America's tax-preferred retirement savings under the Employee Retirement Income Security Act (ERISA), working closely with the Treasury Department and the Pension Benefit Guaranty Corporation. ERISA provided the Department of Labor with this authority, recognizing the special importance of consumer protections for a basic retirement nest egg and the large tax subsidies provided for them. In the coming months, the Department of Labor will propose a new rule that will seek to:

Require retirement advisers to put their client's best interest first, by expanding the

types of retirement investment advice subject to ERISA: The definition of retirement investment advice has not been meaningfully changed since 1975, despite the dramatic shift in our private retirement system away from defined benefit plans and into self-directed IRAs and 401(k)s. The Department's proposal will update the definition to better match the needs of today's working and middle class families. Whether you are an employer trying to design a quality plan for your workers, a worker starting to save, or a retiree trying to avoid spending down your nest egg too quickly, you deserve access to quality advice, without fear that financial bias is clouding your broker's judgment.

Preserve the ability of working and middle class families to choose different types of

advice: The Department’s proposal will continue to allow private firms to set their own compensation practices by proposing a new type of exemption from limits on payments creating conflicts of interest that is more principles-based. This exemption will provide businesses with the flexibility to adopt practices that work for them and adapt those practices to changes we may not anticipate, while ensuring that they put their client’s best interest first and disclose any conflicts that may prevent them from doing so. This fulfills the Department’s public commitment to ensure that all common forms of compensation, such as commissions and revenue sharing, are still permitted, whether paid by the client or the investment firm.

Preserve access to retirement education: The Department’s proposal will allow advisers to continue to provide general education on retirement saving across employer-sponsored plans and IRAs without triggering fiduciary duties.

The Department’s proposal will seek to crack down on irresponsible behavior in today’s market for financial advice by better aligning the rules between employer-based retirement savings plans and IRAs. To balance increased protection for working and middle class families while minimizing disruptions to their access to advice, the Administration is committed to a robust and transparent process for receiving input on the proposal. When the Department of Labor issues a Notice of Proposed Rulemaking (NPRM) in the coming months, there will be opportunities to submit comments in writing and in a public hearing. The Administration welcomes and invites stakeholders from all perspectives to submit comments as the proposal moves forward. Only after reviewing all the comments will the Administration decide what to include in a final rule—and even once the Department of Labor ultimately issues a final rule, it will not go into effect immediately.

To learn more, visit [DOL.gov/ProtectYourSavings](https://www.dol.gov/ProtectYourSavings).