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March 24, 2009

The Honorable Robert E. Andrews
The Honorable John Kline
Subcommittee on Health, Employment, Labor, and Pensions
Committee on Education and Labor
U.S. House of Representatives
Washington, D.C. 20515

Dear Chairman Andrews and Ranking Member Kline,

We, the undersigned, write to congratulate you for holding today's hearing on the importance of an independent investment adviser for participants in self-directed, defined contribution plans. Americans' retirement security depends on their investing their plan assets wisely, yet many of them lack the financial sophistication to make prudent choices among different investment options. Professional investment advice has the potential to help participants to accumulate sufficient assets on which to live in retirement. However, investment advice provided by advisers who have an economic interest in steering their clients to particular investment options can make participants worse off than if they had not received any advice at all. We agree with the Subcommittee that participants should be protected from such conflicted advice.

Under self-directed, defined contribution plans, investment risk is borne by plan participants, which increases the likelihood that many will have insufficient assets at retirement to provide an adequate stream of income. For this reason, we agree with Congress and the Department of Labor that access to professional investment advice benefits participants. Unbiased investment advice helps participants take a more disciplined approach to investing in the equity markets at a time when they are saving far less than they need for retirement. The Pension Protection Act's statutory exemption for conflicted advice and the Department's interpretation thereof, however, have exposed trillions of dollars of participant assets to unnecessary risk by allowing financial services firms with significant conflicts to advise participants to invest in products that serve the financial interests of the firms rather than the best interests of the participant.

We strongly recommend that Congress repeal the PPA's conflicted advice exemption. Congress designed ERISA's prohibited transaction provisions to prevent precisely the kind of conflicted advice for which the PPA has now provided a limited exemption. Once advisers are permitted to be compensated by the affiliates of plan product providers, these providers will find ways to incentivize advisers to recommend more profitable products rather than the products that are best suited to participants' needs. The participant protections established by the statutory exemption are not adequate, particularly in light of the interpretation of the exemption by the Department. No regulatory mechanism can adequately insulate participants from the conflicted advice permitted by the PPA. We encourage members of the Subcommittee to seek legislation that eliminates the influence of conflicts of interest on participants' investment decisions.

In the absence of such statutory reform, we strongly recommend that the Department revise its interpretation and application of the statutory exemption, to the extent permitted by the statute, to narrow the potential scope of conflicted advice. The Department should withdraw the class exemption, which by the Department's express admission expands the already inappropriate and overbroad statutory exemption for conflicted advice. Rather than limiting the adverse effects of the statutory exemption, the Department's position has increased the potential for participants' investment decisions to be guided by the interests of conflicted advisers rather than of participants.

The current financial crisis has highlighted the importance of protecting plan participants from advisers who are paid to recommend investment options that will profit the adviser and his affiliates rather than beneficiaries. Many participants have experienced losses not as the unavoidable result of an appropriate asset allocation among equity and fixed income products, but because of precisely the kind of overweighting of equities that conflicted advice is likely to produce. Equity funds are generally more profitable to their sponsors, and advisers who work for the sponsor's affiliate have an incentive to recommend such an equity overallocation. Congress should act now to ensure that the investment advice provided to participants is free of financial conflicts of interest.

Sincerely,

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Employee Benefits Security Administration