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## United States Senate

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December 11, 2019

The Honorable Eugene Scalia  
Secretary of Labor  
U.S. Department of Labor  
200 Constitution Avenue NW  
Washington, D.C. 20210

Dear Secretary Scalia:

I am writing to express concern that in rewriting the fiduciary rule, the Department of Labor (DOL) is considering standards of conduct that would allow advisers providing advice regarding retirement investments to engage in conflicts of interest that harm working families saving for retirement. DOL's submission to the Office of Management and Budget's (OMB) Unified Regulatory Agenda reveals that the agency intends to issue a Notice of Proposed Rulemaking sometime this month.<sup>1</sup> Given your past statements that the fiduciary rule "is a matter that ought to be addressed by the SEC,"<sup>2</sup> I am concerned that the DOL may simply copy the wholly inadequate standards of conduct framework developed by the Securities and Exchange Commission (SEC) in its recently-finalized Regulation Best Interest (Reg BI), including the Investment Advisor interpretation and Form CRS disclosure. That would be a costly mistake—those standards not only allow broker-dealers to give clients advice that is not in their best interest, but significantly water down the longstanding fiduciary standard that has protected the clients of the investment advisers for decades.

### The Need for a Strong Conflict of Interest Rule

Americans' savings should never be willfully compromised by conflicted actors operating under anemic rules – but they are. According to a 2015 report by the Council of Economic Advisers, American families lose \$17 billion in retirement savings every year as a result of financial advisers' conflicts of interest.<sup>3</sup> These losses have a particularly substantial impact for our retirement savers.<sup>4</sup>

<sup>1</sup> Office of Management and Budget Unified Regulatory Agenda, "Fiduciary Rule and Prohibited Transaction Exemptions," <https://www.reginfo.gov/public/do/eAgendaViewRule?pubId=201910&RIN=1210-AB82>

<sup>2</sup> ThinkAdvisor, "Scalia: DOL Fiduciary Rule Will Be Obliterated," Melanie Waddell, March 23, 2018, <https://www.thinkadvisor.com/2018/03/23/scalia-dol-fiduciary-rule-will-be-taken-off-the-books/>.

<sup>3</sup> Council of Economic Advisers, "The Effects of Conflicted Investment Advice on Retirement Savings," February 2015, pp. 2, [https://obamawhitehouse.archives.gov/sites/default/files/docs/cea\\_coi\\_report\\_final.pdf](https://obamawhitehouse.archives.gov/sites/default/files/docs/cea_coi_report_final.pdf).

<sup>4</sup> U.S. Securities and Exchange Commission, "Statement on Final Rules Governing Investment Advice," Public Statement by Commissioner Robert J. Jackson Jr., June 5, 2018, [https://www.sec.gov/news/public-statement/statement-jackson-060519-iabd#\\_ftn1](https://www.sec.gov/news/public-statement/statement-jackson-060519-iabd#_ftn1).

A series of investigations by my office on conflicts of interest in the annuity industry in October 2015 and February 2017 showed that 13 of the 15 leading annuity providers offer their agents lavish, secretive kickbacks for sales to often-unwitting purchasers, including all-expenses-paid vacations, iPads, professional sports tickets, and more.<sup>5</sup> These kickbacks create a perverse incentive for broker-dealers to sell whatever products reap them the greatest personal reward, even if it comes at the expense of retirees' savings.

Congress has given the Federal agencies with jurisdiction over retirement and investing the authority to regulate investment professionals under their purview. The *Employee Retirement Income Security Act of 1974* (ERISA) provides that “a person is a fiduciary with respect to a plan” if they exercise control, provide advice for a fee or compensation, or have discretionary authority to administer the plan.”<sup>6</sup> Since the 1970s, the DOL has defined fiduciary duties by regulation.<sup>7</sup> Similarly, in the *Dodd-Frank Wall Street Reform and Consumer Protection Act* (Dodd-Frank), Congress gave the SEC authority to establish a fiduciary standard by “commenc[ing] a rulemaking, as necessary or appropriate in the public interest and for the protection of retail customers . . . to address the legal or regulatory standards of care for brokers, dealers, investment advisers . . . [and] for providing personalized investment advice about securities to such retail customers.”<sup>8</sup> Congress further specified that if the SEC undertakes such a rulemaking, the standards of conduct for broker-dealers “shall be the same as the standard of conduct applicable to an investment adviser under section 211 of the Investment Advisers Act of 1940,”<sup>9</sup> meaning a fiduciary standard that requires the advice to be provided “without regard to the financial or other interest of the broker, dealer, or investment adviser providing the advice.”<sup>10</sup>

### **Previous DOL Efforts to Impose a Fiduciary Rule – and Your Opposition to those Efforts**

In April 2016, the DOL finalized the “Definition of the Term ‘Fiduciary’; Conflict of Interest Rule-Retirement Investment Advice” Rule (Fiduciary Rule) which would have protected investors from costly conflicts of interest, and leveled the playing field for financial advisers who are already putting their clients’ interests first.<sup>11</sup> During the short period the Fiduciary Rule was partially implemented, investors saw positive results: firms eliminated their highest-fee products

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<sup>5</sup> Office of Senator Elizabeth Warren, “Villas, Castles, and Vacations: How Perks and Giveaways Create Conflicts of Interest in the Annuity Industry,” October 2015, [https://www.warren.senate.gov/files/documents/2015-10-27\\_Senator\\_Warren\\_Report\\_on\\_Annuity\\_Industry.pdf](https://www.warren.senate.gov/files/documents/2015-10-27_Senator_Warren_Report_on_Annuity_Industry.pdf); Office of Senator Elizabeth Warren, “Villas, Castles, and Vacations: Americans’ New Protections from Financial Adviser Kickbacks, High Fees, and Commissions are at Risk,” February 2017, [https://www.warren.senate.gov/files/documents/2017-2-3\\_Warren\\_DOL\\_Rule\\_Report.pdf](https://www.warren.senate.gov/files/documents/2017-2-3_Warren_DOL_Rule_Report.pdf).

<sup>6</sup> 29 U.S.C. § 1002 (21)(a).

<sup>7</sup> 29 CFR 2510.3-21.

<sup>8</sup> 15 U.S.C. § 78o note.

<sup>9</sup> *Id.*

<sup>10</sup> 15 U.S.C. § 80b-11.

<sup>11</sup> Employee Benefits Security Administration, Federal Register Final Rule, “Definition of the Term ‘Fiduciary’; Conflict of Interest Rule-Retirement Investment Advice,” April 8, 2016, <https://www.federalregister.gov/documents/2016/04/08/2016-07924/definition-of-the-term-fiduciary-conflict-of-interest-rule-retirement-investment-advice>.

and cut prices on funds.<sup>12</sup> Some firms eliminated commission-based sales practices entirely.<sup>13</sup> A study conducted by Morningstar found that “flows into mutual funds paying unusually high excess loads declined after the DOL proposed its fiduciary rule in 2015,” a shift that was statistically significant.<sup>14</sup>

As a lawyer in private practice, you sued the DOL on behalf of the U.S. Chamber of Commerce, the broker-dealer industry, and other big business interests to the overturn the Fiduciary Rule, and, after hand picking the most amenable appellate court (the U.S. Court of Appeals for the Fifth Circuit),<sup>15</sup> you were ultimately successful.<sup>16</sup> Despite the DOL’s work to sift through thousands of public comments, hundreds of meetings with stakeholders, and the almost 400-page economic analysis of the rule’s impact, the Trump Administration refused to appeal that ruling.<sup>17</sup>

In the aftermath of the 5<sup>th</sup> Circuit decision, you told the investing newsletter ThinkAdvisor: “Dodd-Frank made clear that the question of a uniform fiduciary standard is under the SEC’s purview. Eyes now turn to the SEC, and Labor can go back to focusing on the areas that Congress put under its responsibility.”<sup>18</sup>

### **Problems with SEC’s “Reg BI” Conflict of Interest Rule**

The SEC indeed began work on its standards of conduct rule that governs broker-dealers and investment advisers and in June 2019, SEC approved Reg BI, which despite Congress’s instruction in sections 913(f) and 913(g) of Dodd-Frank establishes neither a uniform standard for broker-dealers and investment advisers, nor a fiduciary standard for broker-dealers.<sup>19</sup> DOL also began work on a new Fiduciary rule to replace the vacated regulation. Your predecessor,

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<sup>12</sup> Huffington Post, Editorial, “President Trump Just Cost Americans Saving for Their Retirement \$3.7 Billion,” Senator Elizabeth Warren and Senator Cory Booker, April 10, 2017, [https://www.huffpost.com/entry/president-trump-just-cost-americans-saving-for-their-retirement-37-billion\\_b\\_58ea602ce4b00de1410421fb](https://www.huffpost.com/entry/president-trump-just-cost-americans-saving-for-their-retirement-37-billion_b_58ea602ce4b00de1410421fb).

<sup>13</sup> *Id.*

<sup>14</sup> Investment News, “Morningstar: DOL Fiduciary Rule Reduces Inflows to Mutual Funds With High Loads,” Mark Schoeff, Jr., November 15, 2018, <https://www.investmentnews.com/article/20181115/FREE/181119940/morningstar-dol-fiduciary-rule-reduces-inflows-to-mutual-funds-with>.

<sup>15</sup> ThinkAdvisor, “DOL’s Perez Vows to Fight Mounting Fiduciary Lawsuits,” Melanie Waddell, June 20, 2016, <https://www.thinkadvisor.com/2016/06/20/dols-perez-vows-to-fight-mounting-fiduciary-lawsuits/>.

<sup>16</sup> U.S. Chamber of Commerce v. U.S. Department of Labor, 885 F.3d 360, 388 (5th Circuit, 2018).

<sup>17</sup> Department of Labor, Employee Benefits Security Administration, “Fact Sheet: DOL Finalizes Rule to Address Conflicts of Interest in Retirement Advice, Saving Middle-Class Families Billions of Dollars Every Year,” August 22, 2016, <https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/fact-sheets/conflict-of-interest>; Department of Labor, Employee Benefits Security Administration, “Regulating Advice Markets, Definition of the Term ‘Fiduciary’ Conflicts of Interest- Retirement Investment Advice, Regulatory Impact Analysis for Final Rule and Exemptions,” April 2016, <https://www.dol.gov/sites/dolgov/files/ebsa/laws-and-regulations/rules-and-regulations/completed-rulemaking/1210-AB32-2/ria.pdf>.

<sup>18</sup> ThinkAdvisor, “Scalia: DOL Fiduciary Rule Will Be Obliterated,” Melanie Waddell, March 23, 2018, <https://www.thinkadvisor.com/2018/03/23/scalia-dol-fiduciary-rule-will-be-taken-off-the-books/>.

<sup>19</sup> U.S. Securities and Exchange Commission, “SEC Adopts Rules and Interpretations to Enhance Protections and Preserve Choice for Retail Investors in Their Relationships With Financial Professionals,” press release, June 5, 2019, <https://www.sec.gov/news/press-release/2019-89>.

former DOL Secretary Alex Acosta, told a House committee that the DOL is “communicating with [the SEC], and based on our collaborative work we will be issuing new rules in this area.”<sup>20</sup>

If the DOL’s intent is to protect Americans’ savings, Reg BI, which SEC Commissioner Robert J. Jackson Jr. called, “a muddled standard that exposes millions of Americans to the costs of conflicted advice,”<sup>21</sup> must not be a model for the DOL’s new rule, as Congress has provided that advice for retirement savers is subject to a fiduciary standard. The rule and the standards it sets out are ambiguous and confusing—tellingly, the term “best interest,” which is the central concept that defines the duty imposed on broker-dealers, is never given a definition in Reg BI.<sup>22</sup> “Best interest” was similarly undefined in the rule proposal, and as the final rule notes, “a variety of commenters offered suggestions on ... whether the standard should define ‘best interest.’”<sup>23</sup> Rather than fix this significant drawback, the SEC leaves the meaning of “best interest” vague, putting investors at risk.

In absence of clear definition, the rule attempts to describe instances in which brokers do or do not meet the vague “best interest” standard. Those examples seem to suggest that “best interest” is similar to the inadequate Financial Industry Regulatory Authority’s (FINRA) existing “suitability” standard, which, according to FINRA guidance, already “prohibits a broker from placing his or her interests ahead of the customer’s interests”<sup>24</sup> and based on analysis by my office and others, is clearly insufficient to address harmful conflicts of interest in the brokerage industry.<sup>25</sup>

Given this ambiguity, it is unlikely that Reg BI will make any significant difference in protecting investors. The rule includes no obligation to eliminate conflicts of interest—the SEC clearly states “we are not requiring broker-dealers to develop policies and procedures to disclose and mitigate all conflicts of interest.”<sup>26</sup> Instead, Reg BI imposes a limited requirement to disclose conflicts.<sup>27</sup> If “a broker-dealer cannot fully and fairly disclose a conflict of interest” the rule states a broker-dealer “should eliminate the conflict or adequately mitigate the conflict” – but doesn’t define what adequate mitigation looks like.<sup>28</sup>

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<sup>20</sup> House Committee on Education and Labor, “Examining the Policies and Priorities of the U.S. Department of Labor,” May 1, 2019, <https://edlabor.house.gov/hearings/04/24/2019/examining-the-policies-and-priorities-of-the-us-department-of-labor>.

<sup>21</sup> U.S. Securities and Exchange Commission, “Statement on Final Rules Governing Investment Advice,” Public Statement by Commissioner Robert J. Jackson Jr., June 5, 2018, [https://www.sec.gov/news/public-statement/statement-jackson-060519-iabd#\\_ftn1](https://www.sec.gov/news/public-statement/statement-jackson-060519-iabd#_ftn1).

<sup>22</sup> U.S. Securities and Exchange Commission, Federal Register Final Rule, “Regulation Best Interest: The Broker-Dealer Standard of Conduct,” July 12, 2019, pp. 33325, <https://www.govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12164.pdf>.

<sup>23</sup> *Id.*, pp. 33323.

<sup>24</sup> Financial Industry Regulatory Authority, “Suitability: Additional Guidance on FINRA’s New Suitability Rule,” May 2012, <https://www.finra.org/sites/default/files/NoticeDocument/p126431.pdf>.

<sup>25</sup> Office of Senator Elizabeth Warren, “Villas, Castles, and Vacations: Americans’ New Protections from Financial Adviser Kickbacks, High Fees, and Commissions are at Risk,” February 2017, [https://www.warren.senate.gov/files/documents/2017-2-3\\_Warren\\_DOL\\_Rule\\_Report.pdf](https://www.warren.senate.gov/files/documents/2017-2-3_Warren_DOL_Rule_Report.pdf).

<sup>26</sup> U.S. Securities and Exchange Commission, Federal Register Final Rule, “Regulation Best Interest: The Broker-Dealer Standard of Conduct,” July 12, 2019, pp. 33388, <https://www.govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12164.pdf>.

<sup>27</sup> *Id.*

<sup>28</sup> *Id.* pp. 33388-33389.



In addition, Reg BI only suggests broker-dealers “should consider” reasonable alternatives for high-priced products, and allows them to still recommend a higher-cost option that pays the broker-dealer more.<sup>29</sup> Reg BI specifies that broker-dealers are under no obligation “to recommend [one] ‘best’ product.”<sup>30</sup> And the final rule allows broker-dealers to freelance the language they use to describe their obligations to investors on their disclosure forms, opening the door for abuse.<sup>31</sup>

Shockingly, the final rule also undermines the fiduciary standard that has governed investment advisers for decades, putting investors in a worse position. In a departure from the proposed rule, the final rule removes language that the law “requires an investment adviser to put its client’s interest first,” which Commissioner Jackson noted contradicts an earlier SEC interpretation based on “careful reading of decades-old cases.”<sup>32</sup>

Finally, the rule itself stands on a shaky analytical foundation. You have previously argued that the SEC “has been inattentive to economic analysis”<sup>33</sup> and that regulators need to assess the economic impact of proposed rules.<sup>34</sup> Unlike the 400-page economic analysis of the Fiduciary Rule, Reg BI’s economic analysis is so deficient that a bipartisan group of former SEC Senior economists took the unusual step of responding to the proposal, writing:

“[w]e find it worrisome that the proposals’ economic analysis does not fully consider some potentially-important dimensions of the retail client-adviser relationship;” “the analysis appears inconsistent with parts of the Commission’s own adopted guidance for fashioning a rule’s [economic analysis];” and “[o]verall, we find the [economic analysis’] discussion of potential problems in the customer-adviser relationship to be incomplete.”<sup>35</sup>

The final rule does not fix these problems—instead, it reaches the meaningless circular conclusion that “it is important to recognize that the Commission has been studying and carefully considering the issues related to the broker-dealer-client relationship and the related standard of

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<sup>29</sup> U.S. Securities and Exchange Commission, Federal Register Final Rule, “Regulation Best Interest: The Broker-Dealer Standard of Conduct,” July 12, 2019, pp. 33321, <https://www.govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12164.pdf>.

<sup>30</sup> *Id.* pp. 33326.

<sup>31</sup> U.S. Securities and Exchange Commission, “Statement on Final Rules Governing Investment Advice,” Public Statement by Commissioner Robert J. Jackson Jr., June 5, 2018, [https://www.sec.gov/news/public-statement/statement-jackson-060519-iabd#\\_ftn1](https://www.sec.gov/news/public-statement/statement-jackson-060519-iabd#_ftn1).

<sup>32</sup> *Id.*

<sup>33</sup> Wall Street Journal, Editorial, “Why Dodd-Frank Rules Keep Losing in Court,” Eugene Scalia, October 3, 2012, <https://www.wsj.com/articles/SB10000872396390444004704578032223012816236>.

<sup>34</sup> Wall Street Journal, “Another Scalia Vexes Regulators,” Jamila Trindle, October 2, 2012, <https://www.wsj.com/articles/SB10000872396390443862604578032692057219364>.

<sup>35</sup> U.S. Securities and Exchange Commission, “Public comment regarding SEC File Number 57-07-18,” public comment, February 6, 2019, <https://www.sec.gov/comments/s7-07-18/s70718-4895197-177769.pdf>.

conduct for broker-dealers for many years, which led to the development of the Proposing Release and the economic analysis therein.”<sup>36</sup>

In discussion of a SEC rule that you challenged, you once wrote, “When you regulate the economy, you ought to find some room for economic analysis in your analysis of regulations’ effects.”<sup>37</sup> You also stated that “under law, an agency must listen carefully to what the public says about a proposed regulation, reconsider its approach in light of that public input, and then cogently explain (not merely assert) why it made the regulatory choices it did in crafting the final rule.”<sup>38</sup> As Secretary of the DOL, I hope you will take your own advice.

### **Questions about the DOL’s New Fiduciary Rule Proposal**

In response to Questions for the Record I submitted after your confirmation hearing, you wrote:

“As a nominee, I am not yet familiar with the details of any DOL prospective rulemaking on this topic, the SEC’s ‘Regulation Best Interest’ or how the two would or would not relate. If confirmed (and if my recusal is not required), I would look forward to being briefed by the Department on the present status of its work in this area, and if any proposed rule is issued, I will work to ensure that the rulemaking processes [sic] is transparent, allows full stakeholder input, and complies with the Administrative Procedure Act.”<sup>39</sup>

You have now been in office for just over two months and the DOL is apparently preparing to imminently propose a new Fiduciary Rule. In order to better understand whether you share my commitment to ensuring Americans receive the best possible financial advice without fear of being cheated by conflicts of interest, I ask that you provide answers to the following questions no later than December 18, 2019:

1. In your response to my questions for the record following your confirmation hearing in September 2019, you wrote: “I do not believe that it is legally necessary for the DOL to defer to the SEC regarding regulation of financial advisers to ERISA plans.”<sup>40</sup> How, if at all, are you planning to consider Reg BI in developing a new DOL rule? Do you intend to defer to the Reg BI definitions and rules regarding conflicts of interest?

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<sup>36</sup> U.S. Securities and Exchange Commission, Federal Register Final Rule, “Regulation Best Interest: The Broker-Dealer Standard of Conduct,” July 12, 2019, pp. 33321, <https://www.govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12164.pdf>.

<sup>37</sup> The Regulatory Review, Editorial, “Cost-Benefit Analysis and Reasoned Agency Decision-Making,” Eugene Scalia, September 26, 2017, <https://www.theregreview.org/2017/09/26/scalia-cost-benefit-analysis-reasoned-agency-decision-making/>.

<sup>38</sup> Wall Street Journal, Editorial, “Why Dodd-Frank Rules Keep Losing in Court,” Eugene Scalia, October 3, 2012, <https://www.wsj.com/articles/SB10000872396390444004704578032223012816236>.

<sup>39</sup> Written response from Eugene Scalia to Questions for the Record submitted by Senator Elizabeth Warren, September 23, 2019.

<sup>40</sup> *Id.*

2. Has the DOL spoken to or engaged with any lobbyists, financial industry representatives, or agents regarding a new rule? If so, please provide a copy of all communication with any lobbyists or financial industry representatives on this matter, as well as a list of all lobbyists and financial industry representatives and when you spoke with them about this new rule.
3. Will the DOL conduct any new studies or analyses about the effects of conflicts of interest on retirement savers in support of its proposal?
4. The SEC left “best interest”—the key term that describes the standard of conduct for broker-dealers—undefined. Will the DOL define “best interest” and the relevant standards of conduct in its rule?
5. In your view, what if any distinction exists between the “best interest” standard of conduct set forth in the new SEC rule and the “suitability” standard established by FINRA that predated it?
6. Throughout your career, you have often been successful challenging in rules promulgated by executive agencies by challenging their cost-benefit analyses. In response to the SEC’s proposal for Reg BI, a bipartisan group of eleven former SEC Senior economists wrote in a comment, “[w]e find it worrisome that the proposals’ economic analysis does not fully consider some potentially-important dimensions of the retail client-adviser relationship.”<sup>41</sup> Given these flaws, do you believe the cost-benefit analysis that supports Reg BI is sufficient? Please explain.
7. In your response to my questions for the record following your confirmation hearing in September 2019, you wrote: “it is appropriate for agencies to take special care in considering the impact that proposed regulations may have on the most vulnerable Americans.”<sup>42</sup>
  - a. Does the DOL have a plan or strategy to assess the impact of the financial adviser rule it proposes on the most vulnerable Americans? What is that plan or strategy? Please provide any written documentation outlining how the DOL plans to conduct this assessment.
8. In your response to my questions for the record following your confirmation hearing in September 2019, you wrote you would “work to ensure that the rulemaking processes [sic] is transparent, allows full stakeholder input, and complies with the Administrative Procedure Act.”<sup>43</sup>
  - a. In what ways are you building transparency into this rulemaking process?

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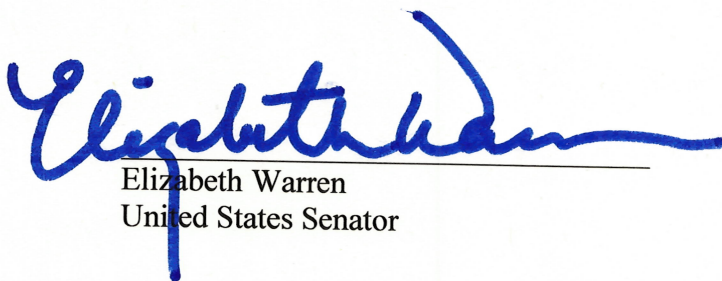
<sup>41</sup> U.S. Securities and Exchange Commission, “Public comment regarding SEC File Number 57-07-18,” public comment, February 6, 2019, <https://www.sec.gov/comments/s7-07-18/s70718-4895197-177769.pdf>.

<sup>42</sup> Written response from Eugene Scalia to Questions for the Record submitted by Senator Elizabeth Warren, September 23, 2019.

<sup>43</sup> *Id.*

- b. Who do you consider stakeholders with respect to this rule, and how are you soliciting their input with respect to this rule?
- c. Have you discussed anything related to this rulemaking process with your former clients? If so, please provide records of which clients and when.
- d. Please provide a list of all discussions—in writing, in person, or on the phone—that you have had with non-DOL personnel about the fiduciary rule proposal.

Sincerely,



Elizabeth Warren  
United States Senator