Consumer Alert: What to Expect When the DOL Conflict Rule Goes Into Effect

Thanks to the Department of Labor's new conflict of interest rule set to take effect on June 9, workers and retirees will finally be legally entitled to retirement investment advice that serves their best interests, regardless of who provides that advice or how they choose to pay for it.

The conflict of interest (or "fiduciary rule") rule requires all financial advisers, including broker-dealers and insurance agents, to act in their customers' best interest rather than their own, charge reasonable fees, and refrain from making misleading statements.

This is a major win in the decades-long fight to ensure that investors receive appropriate protections when they turn to financial professionals for help with their investments.

So what does that mean for you?

If you are like most people, you probably assumed all financial advisers were already required to put their customers' interests first. But, while registered investment advisers were required to meet that standard, broker-dealers and insurance agents generally were held to a lower "suitability" standard. That means that they were allowed--and often did--recommend investments that cost the customer more, but made the adviser more money, as long as those investments were generally "suitable" for the customer.

Beginning Friday (June 9, 2017) that changes. But only for investment advice regarding retirement accounts. That includes advice about workplace retirement plans, such as 401(k) plans, as well as individual retirement accounts (or IRAs). For all other non-retirement accounts, the old rules still apply.

The following are a few of the changes investors who previously received advice from non-fiduciary advisers can expect as the rule takes effect.

1) You should see new, more investor-friendly investment options recommended in your IRA.

In order to meet the best interest standard, your adviser may recommend new and different types of shares of mutual funds, such as "T" shares, that were introduced in response to the rule. These new shares can cut several percentage points off the sales charges you pay to purchase those funds. That's money that will stay in your retirement account rather than going to pay your financial adviser.

Or your adviser may offer new "clean" shares, which allow you to negotiate how much she gets paid for the services she provides in selling you that fund.

Mutual fund investors aren’t the only ones who’ll see benefits from the rule. Annuities have also been given a tune-up. New annuities with more investor-friendly features, including much shorter surrender periods and lower fees, have been introduced in response to the rule.

2) You should get a better deal if you rollover money from your workplace retirement account.

Financial firms make big money encouraging retirement savers to move their money out of workplace retirement plans and into IRAs managed by the firm. Even reputable firms have been accused of recommending such rollovers when the customer would have been better off leaving his money in the company plan, where investment costs are often considerably lower.

The new conflict of interest rule only allows such recommendations if they are in the best interest of the customer. One possibility is that you will see fewer rollover recommendations once the rule takes effect, but firms may also respond by offering retirement savers a better deal on their rollover investments.

If your adviser recommends you roll money out of a company 401(k) plan and into an IRA, ask on what basis she determined that you would be better off in the IRA. Ask in particular how your costs will compare. While costs shouldn’t be your only consideration, minimizing costs is one of the surest ways investors have of improving their long-term investment performance.

3) You may be encouraged to move your money to a fee account.

Some firms have concluded that the easiest, cleanest way to minimize conflicts is by moving clients from commission accounts to accounts where investors pay a fee for advice. That can take the form of a flat fee, hourly fee, or a percentage of assets under management.

Fee accounts can offer a good deal for investors, assuming the fees are reasonable and the investor wants and benefits from the ongoing advice offered with such accounts. When firms have both fee and commission accounts available, the rule requires that advisers recommend the type of account that is best for the investor.

If your adviser suggests moving from a commission account to a fee account, ask on what basis she determined you’d be better off in a fee account. In particular, ask how your costs in the fee account would compare to the costs you previously paid in your commission account.

If your costs would go up, ask what additional services you will receive to justify those higher costs, and determine whether those are services you want or need. Don’t be afraid to try to negotiate a lower fee. Some firms have reportedly been willing to lower fees to match average commission costs from previous years in order to demonstrate that the fee account really is in the customer's best interests.

If your adviser insists on moving you to a fee account and you prefer to continue to pay through commissions, you can always look elsewhere to get retirement advice on the terms you prefer. Most brokerage and insurance firms continue to offer commission accounts as an option under the rule.

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The good news about Friday's conflict of interest rule implementation comes with a couple of caveats.

First, the rule only applies to retirement accounts. If you have been working with a non-fiduciary adviser, such as a broker-dealer or insurance agent, you'll likely continue to get *suitable* sales recommendations rather than *best-interest* advice in your non-retirement accounts.

Second, only portions of the rule take effect in June. Other provisions, including those that make the best interest standard for IRA advice legally enforceable, aren't scheduled to take effect until January 2018.

Third, while most firms have moved forward in good faith to implement the rule in an investor-friendly fashion, others have been more resistant. Some, for example, have threatened to drop smaller retirement accounts rather than serve them under a best-interest standard.

What should you do if this happens to you? Take a moment to count your lucky stars. A firm that will only "advise" you if it can profit unfairly at your expense is not where you want to keep your money. There are many firms willing to serve even the smallest accounts under the new standard and at a reasonable cost.

Once you find such an adviser, have them do a careful review of your existing investments. Chances are your money is in investments that pay generous compensation to the seller, but charge high fees to the investor or expose you to inappropriate and unnecessary risks. In these circumstances, the long-term benefit to your retirement savings from switching advisers – tens or even hundreds of thousands in added savings once your reach retirement – should greatly outweigh any temporary inconvenience of moving accounts.

Finally, the benefits provided by this rule could still be snatched away. The Department of Labor, which is conducting a "reconsideration" of the rule, is under heavy pressure from special-interest lobbyists to roll back and water down its central protections. If your adviser is one of those bellyaching about the rule, perhaps it is time to consider switching to one who eagerly embraces their fiduciary duty to minimize conflicts of interest and put the customer first.