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Financial Engines

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The Honorable Jay Clayton
Chairman
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549

Re: Standards of Conduct for Investment Advisers and Broker-Dealers

Dear Chairman Clayton:

Financial Engines appreciates the opportunity to respond to your recent request for comments about potential action by the Securities and Exchange Commission ("SEC" or "Commission") regarding the standards of conduct that apply to investment advisers and broker dealers when they provide investment advice to retail investors (the "Request").[1] We are proud to be in full compliance with the Department of Labor's ("DOL") regulation entitled *Definition of the Term "Fiduciary; Conflict of Interest Rule - Retirement Investment Advice* ("DOL Fiduciary Duty Rule"), and commend you for your inclusive and deliberative approach to examining this important area.

Since 1996, Financial Engines has provided high-quality, objective investment advice in a fiduciary capacity to millions of defined contribution plan participants. Our experience demonstrates that it is possible to put the interests of investors first by providing personalized, unconflicted investment advice, even for investors with modest account balances, while still achieving solid business results.

Financial Engines is encouraged by the recent invitation to engage with the Commission as you revisit the standards of conduct applicable to investment advisers and broker-dealers. As America's largest independent registered investment adviser[2] with over $151.8 billion in assets under management, we certainly share the view that you articulated in your statement that clarity and consistency are key elements to keep in mind as the Commission seeks to serve the interests of our country's retail investors in this area.[3] We would like to offer our comments that any future Commission action should complement the robust DOL Fiduciary Duty Rule in order to ensure that all investors have access to high quality, unconflicted investment advice as they continue to take charge of their retirement investment decisions.

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[1] Jay Clayton, Chairman, SEC, *Public Comments from Retail Investors and Other Interested Parties on Standards of Conduct for Investment Advisers and Broker-Dealers* (June 1, 2017), https://www.sec.gov/news/public-statement/statement-chairman-clayton-2017-05-31.
[2] For independence of methodology and ranking, see InvestmentNews RIA Data Center, http://data.investmentnews.com/ria/.
[3] Clayton, *supra* note 1.

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Critical Need for Retirement Investment Advice

The retirement landscape has changed significantly in the past forty years. Professionally managed pension plans have given way to individually managed 401(k)s and IRAs. The shift in responsibility from professional managers to individual investors has led to an increase in investment options, making investment decisions ever more difficult for individuals and increasing the risk of underperformance. A recent Financial Engines study, for example, found that more than 60 percent of participants who did not have retirement help had inappropriate portfolio risk levels.[4]

With more than 94 million individual investors now responsible for managing their own retirement assets, there has never been greater demand for high-quality investment advice. Investors obtain advice from a range of sources, which differ in legal and conduct standards and the way in which they are compensated. Studies have shown that, although most investors are content with the advice they receive from these sources, they often do not fully understand the legal differences among various sources or the types of payments their advisors receive.[5] It is imperative that the regulatory structure governing investment advice protect the integrity of this service.

Additionally, we note that the fiduciary standard predating the DOL Fiduciary Duty Rule ("prior regulations") was no longer tenable given the immense stakes associated with the shift to the defined contribution model for retirement savings. Under the prior regulations, conflicted advisors could steer investors toward products that offered higher fees and commissions for the advisor, and not necessarily those products that will provide the best retirement outcome for the investor. Complex fee-sharing arrangements, commission structures, and other conflicts of interest create pressures—sometimes overt, sometimes subtle—to shade recommendations toward the interests of the advisor. The vast majority of investors are entirely unaware that these conflicts of interest even exist, and often end up with investments that have lower returns and higher fees.

The potential harm to consumers from these conflicts of interest is significant. A 2013 study showed that even brokers who are unaffiliated with a mutual fund

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[4] Help in Defined Contribution Plans: 2006 through 2012 (May 2014), available at: http://www.financialengines.com. Aon Hewitt and Financial Engines contributed complementary participant data, financial technology, and portfolio analytics. The report is based on a dataset of fourteen plan sponsors representing more than 723,000 individual participants and more than $55 billion in plan assets. This report looked at how participant behavior affected portfolio risk and returns over the seven-year period between January 1, 2006, and December 31, 2012, which includes one of the most volatile periods in stock market history. Help is defined to include target-date funds, professional management, or online advice, the latter two of which were provided by Financial Engines.

[5] Angela Hung et al., *Investor and Industry Perspectives on Investment Advisors and Broker-Dealers* (2008).

company tend to steer their clients toward mutual funds that pay the brokers more, but that underperform by over one percent annually on average.[6] Although one percent might not appear significant, such annual underperformance can quickly translate into a retirement balance that is tens of thousands of dollars lower over a 30-year career.

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Preservation of Strong DOL Fiduciary Duty Rule

As the Commission carefully examines the scale and scope of possible action, we urge you to consider the underlying premise of the DOL Fiduciary Duty Rule - protections for investors involves a two-step approach. First, the definition of fiduciary investment advice must appropriately address the actual retirement investment advice that retirement investors rely on today. Second, the expanded scope of fiduciary investment advice must be balanced and enforced by a series of protections to ensure that retirement investment advice would be in the investor's best interest.

Financial Engines believes that there continues to be a strong and clear need for the investor protections given the changing retirement landscape and the shift toward defined contribution models. Potential conflicts of interest exist across retirement investment products and services, sometimes leading financial advisors to steer investors toward products with higher fees and commissions for the advisor but lower returns for the investor. As empirical research has shown, these conflicts of interest can dramatically impact investors' retirement savings over a 30-year career.[7]

We support maintaining a strong DOL Fiduciary Duty Rule that will help to promote the trend toward high-quality, low-cost, technology-based financial services and products that will make unconflicted advice increasingly cost-effective for advisors and accessible for investors of all means. Technology has democratized high-quality, objective advice, once only available to high net-worth investors. Our business model and market experience are an example of how technology can help investment advisors profitably offer high-quality, unconflicted advice to investors, provided both through web-based interactive experiences and through human advisors.

SEC Action

Based on our experience, we believe that possible action by the Commission in this area should further the regulatory trend. Americans need investment advice that is free of conflicts and provided with their highest and best interests in mind. The current landscape for investment advice now sees oversight from the DOL, the SEC, and FINRA, each of which requiring different standards of care with respect to the

[6] Susan E. K. Christoffersen, *What Do Consumers' Fund Flows Maximize? Evidence from Their Brokers' Incentives* (2013).
[7] Susan E. K. Christoffersen, *What Do Consumers' Fund Flows Maximize? Evidence from Their Brokers' Incentives* (2013).

advice provided. Under FINRA's rules, a broker-dealer must determine that a recommended investment is "suitable" based on the customer's profile. While this may have been reasonable when broker-dealers and registered advisers provided distinct services, broker-dealers have increasingly offered services that resemble those provided by registered advisers. Under the SEC, registered advisers have a stronger standard that requires recommended investments to be in the best interests of the customer. We recommend that future SEC actions harmonize these standards of care in a manner that advances high-quality, unconflicted advice, as supported by the DOL Fiduciary Duty Rule. We believe such a harmonized rule must go beyond mere disclosure of conflicts of interest, and should include enforceable protections to ensure that all advisors are acting in the best interests of their clients.

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Conclusion

Financial Engines seeks to ensure that all investors have access to unconflicted investment advice that promotes their interests and helps them to accomplish their financial objectives. We appreciate the opportunity to furnish our views in response to the Request and welcome the opportunity to work with the Commission and provide any additional information that may be required. Please do not hesitate to contact us should you have any questions. For over 20 years, we have helped Americans with modest savings achieve greater financial security and would be happy to share our extensive experience with you.

Very truly yours,

Christopher Jones
Executive Vice President of Investment Management and Chief Investment Officer