

Industry preparedness for the Department of Labor's Fiduciary Rule

Majority of market participants say preparation is underway, but very few have begun implementing



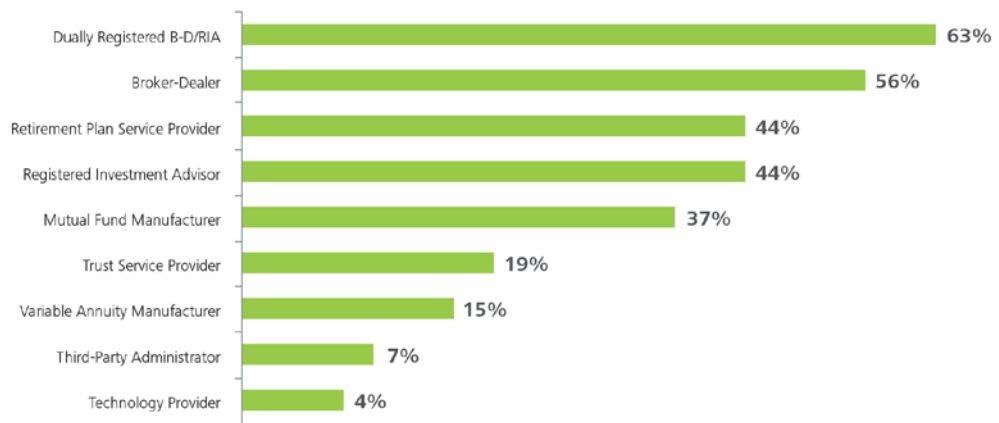
In the year since the Department of Labor (DOL) proposed the “Conflict of Interest” Rule (the Rule) that would require investment advice to retirement investors to adhere to strict fiduciary standards, the industry has begun preparing for the Rule's enactment. With the proposed Rule currently under review by the Office of Management and Budget, many firms expect to see a final version of the Rule in the coming weeks. In this context, this paper presents the results of a survey of 27 financial services firms that was conducted to gain a better understanding of industry preparedness for the Rule. Unless otherwise indicated, all percentages reflected are based on questions which received responses from the full survey population of 27 respondents.

The survey revealed wide variations in preparedness among respondents. However, all survey respondents view adoption of the Rule as imminent and all firms have taken some steps to prepare. Notably, only 55% of firms call their preparation work “significant” and only 8% of firms have actually moved from preparation to implementation activities as they await issuance of the final Rule.

Composition of survey respondents

The surveyed firms include many of the industry's largest private client firms, as well as drawing responses from a subset of the industry's small and middle-market firms. These firms engage in a broad and diverse set of businesses that includes broker-dealers, investment advisers, dually registered broker-dealers/investment advisers, mutual fund manufacturers, retirement plan service providers, trust service providers, variable annuity manufacturers, technology providers and third-party administrators.

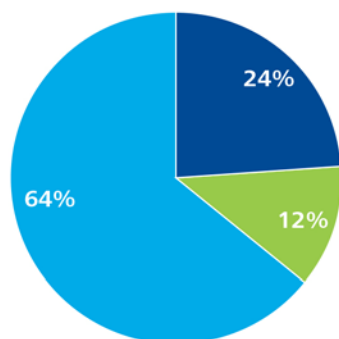
Percent of Respondents by Business Line*



*Respondents were able to identify multiple business types that they engage in.

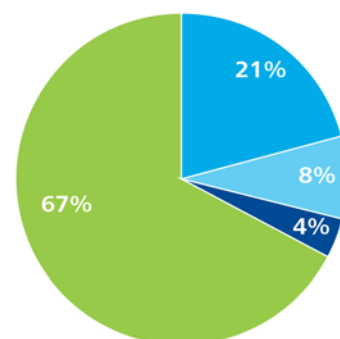
Many respondents have substantial businesses that serve the retirement investor marketplace. Almost two-thirds¹ of respondents reported that their firms earn \$1 billion or more in annual revenues from businesses that are directly impacted by the Rule. Additionally, over 95%² of respondents indicated that a quarter or more of the customer assets held with them would be considered retirement assets and therefore impacted by the Rule.

Percent of Respondents by Amount of Annual Revenue Impacted



■ < \$0.5B
 ■ \$0.5B-\$1B
 ■ > \$1B

Percent of Respondents by Amount of Customer Retirement Assets



■ < 25% Retirement Assets
 ■ 25%-50% Retirement Assets
 ■ 50%-75% Retirement Assets
 ■ > 75% Retirement Assets

¹ Based on survey question receiving a response from 25 respondents.

² Based on survey question receiving a response from 24 respondents.

¹ Based on survey question receiving a response from 25 respondents

² Based on survey question receiving a response from 24 respondents

Key outcomes

Variations in preparedness among respondents

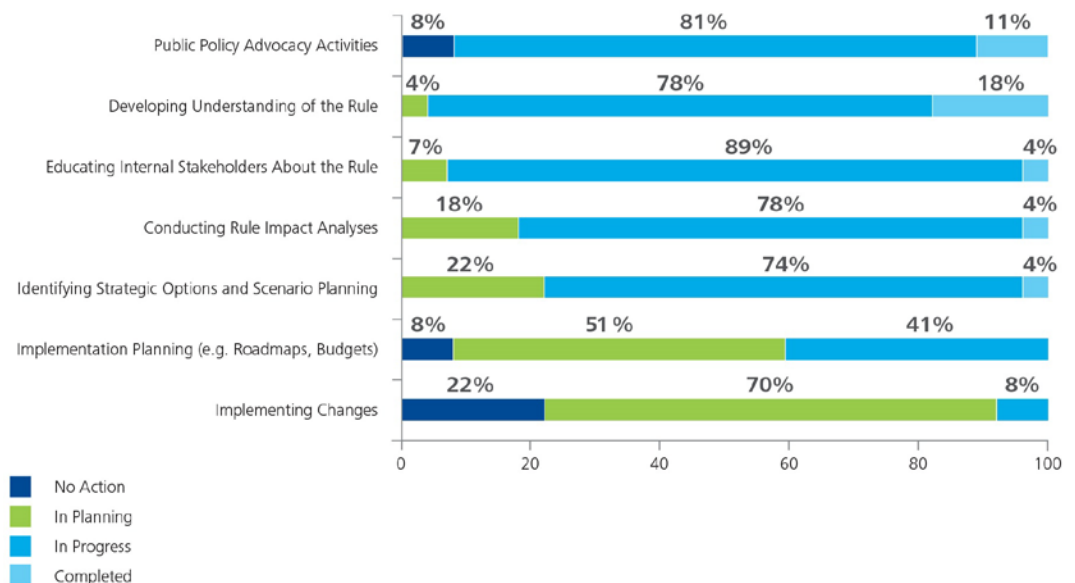
All of the respondents indicated that they view the adoption of the Rule as imminent, with no respondent planning for the Rule to not be enacted. Despite this universal agreement amongst respondents, the survey revealed differences in preparedness for the Rule.

- **55% of respondents** indicated they have undertaken significant planning activities to date.
- **41% of respondents** indicated they are awaiting Rule finalization before taking significant action.
- **Only one respondent (4%)** indicated the Rule is unlikely to have an impact on their company's business.

The majority of preparatory actions are still in a planning or in-progress state, with few respondents reporting any preparation activities to be fully completed.

- **92%³ of respondents** are in the process of, or have completed, some form of public policy advocacy activities specific to the Rule (e.g. lobbying, involvement with trade groups).
- **78% of respondents** are still in the process of developing an understanding of the Rule.
- **89% of respondents** are still in the process of educating internal stakeholders about the Rule.
- **Approximately 75% of respondents** are still in the process of conducting a Rule impact analysis, identifying strategic options, and performing scenario planning

Percent of Respondents Engaged in Preparation Activities by Level of Activity Completion



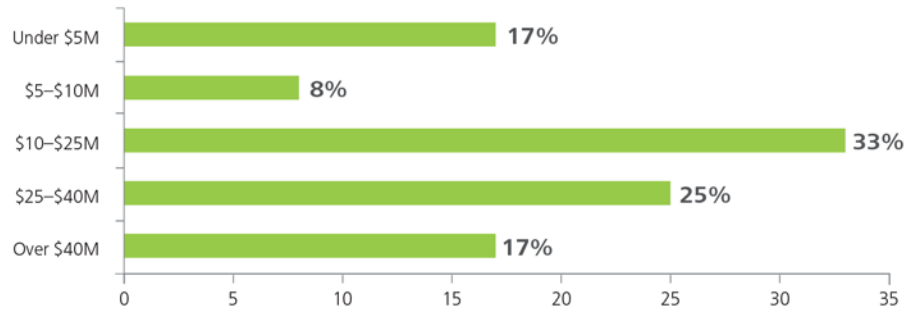
Almost all respondents are in the process of planning for implementation (e.g., roadmaps, budgets), however, only **two respondents** have begun to actually implement changes in preparation for the Rule.

³ Based on survey question receiving a response from 26 respondents

Varying estimates of Rule related costs

54%⁴ of the respondents have yet to conduct a budgeting exercise for actions related to the Rule. Among firms that have completed budgets, cost estimates vary, but **42% have budgeted \$25 million or more.**

Amount Budgeted for 2016* to Prepare for the Rule



*Above amounts reflect the answers of the respondents who indicated that they had actually performed a budgeted exercise specific to the Rule.

Broad usage of exemption

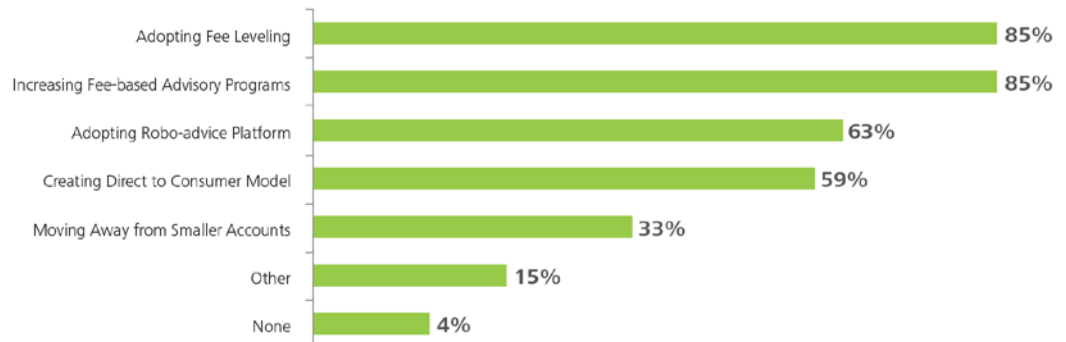
Nearly **75% of respondents** anticipate using at least one of the existing or new exemptions provided by the DOL, whether they use one of the many current class exemptions or current statutory exemptions, or have their own individual exemption, or look to a new exemption (e.g., the Best Interest Contract and/or Principal Transaction Exemptions), while only **one respondent (4%)** does not plan to rely on exemptions. The remaining **22% of respondents** were unsure if they would rely on an exemption.

Range of compliance, product and business model responses to the Rule

More than half of the respondents indicated they are considering at least one of four approaches to compliance with the Rule:

- **85% of respondents** are considering adopting fee leveling.
- **85% of respondents** are considering increasing their emphasis on fee-based advisory programs.
- **63% of respondents** are considering adopting a robo-advice platform.
- **59% of respondents** are weighing the creation of a direct-to-customer model.

Percent of Respondents Considering Each Business Approach in Response to the Rule



⁴ Based on survey question receiving a response from 26 respondents

In addition to the approaches outlined above, **33% of respondents** indicated they were considering moving away from smaller accounts and **15% of respondents** are evaluating other approaches, including:

- Utilization of digital advice software
- Creation of a small account solution
- Reliance on the counterparty exception and prohibited transaction exemption 84-24

Only one firm (4%) believes no change is necessary to their business approach based on the Rule.

What it all means

The industry will likely need to implement substantial changes to support the anticipated widespread adoption of exemptions as well migrating to different or new service models and offerings. The industry's capacity to support this amount of change all at once under what is anticipated to be an accelerated timeline may be challenging. As the industry awaits the final rule, the next few weeks may prove critical to organizations to complete their planning and organizing activities so that once the final rule is published they can quickly finalize their compliance and business approaches and begin implementation activities.

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