



TRUST

INVESTMENT PERSPECTIVES

July 2017

A Publication of TRUST COMPANY OF OKLAHOMA



Ryan Short
Trust Officer

THE FIDUCIARY RULE WHAT IT MEANS FOR YOU

Recently I had the strangest dream: Paul Revere, iconic folk hero of the American Revolution, was shouting at my window, “The red tape is coming! The red tape is coming!” And indeed, it did. At 11:59 p.m. on June 9, 2017, the highly publicized Department of Labor Fiduciary Rule finally became effective.

After years of debate, new rules have been established for firms handling retirement accounts. This regulatory change is so sweeping that it covers over 1,000 pages and affects the entire landscape of retirement savings, from 401ks to IRAs. Many in the financial industry have lobbied Congress, decrying the new requirements as excessive regulation. And there may be some truth to that. It’s hard to argue that 1,000 pages of anything aren’t excessive. But this rule makes at least one fundamental change that will benefit many Americans with IRA assets: all advisors must now act in the client’s best interest.

THE OLD STANDARD

Previously, an advisor could make recommendations on a simple suitability standard, meaning that the advisor was required to contemplate a client’s circumstances and recommend an investment appropriate for those circumstances. That standard *seems* reasonable enough on its face; so why change anything?

CONFLICTED ADVICE

The old standard did not address conflicts of interest. Advisors compensated by commissions have an inherent conflict. They have a monetary incentive to steer investors toward products that pay the largest commissions. This fact does not mean that all commission-based advisors are scoundrels, but there are significant pressures that may affect their advice. Imagine a scenario where an advisor has two products considered suitable for a client. One pays a 2% commission; the other, a 5% commission. Which product is likely to be recommended?

I recently evaluated an equity indexed annuity that a client had purchased from an advisor. The advisor’s company approved the sale as “suitable.” The advisor earned a 7% commission. Meanwhile, the investor only experienced a 1.94% average annual return in one of the best bull markets of all time. Even worse, the client cannot leave the product until 2024 without incurring significant charges. Whose best interest was served in this situation?

Continued on Page 2

“The Fiduciary Rule – What It Means For You” continued

THE NEW STANDARD

At its basic level, the new rule changes the duty owed by an advisor to an investor. Any advisor working with IRAs or qualified retirement plans will now owe clients a fiduciary duty, which is the highest standard of care. An advisor serving in this capacity has a legal obligation to act only in the client’s best interest. The suitability standard no longer applies to advice about retirement assets, such as IRAs. Understandably, firms who have advised clients under a commissioned-based model are adapting their systems to comply.

HOW THIS MIGHT AFFECT YOU

Some of the nation’s largest investment management companies are making radical changes to their client service model. Some firms are dropping commission-based retirement accounts from their platform. In one instance, an institution informed some IRA clients that their “financial adviser will no longer be able to provide investment guidance.”

Still, other firms plan to continue charging commissions. They will rely on provisions permitting them to offer conflicted advice if they disclose their conflicts and enter a contract with the client promising to act in the client’s best interest. If you have a commission-based IRA with an investment firm, you may anticipate future changes to your account.

WHAT MAKES TRUST COMPANY DIFFERENT

If your IRA is with TCO, don’t expect any change in your relationship with our firm. We have served our clients with a fiduciary duty since our founding in 1981. We do not receive product commissions. We have no incentive to steer you to a particular investment. We manage your wealth for your benefit – not someone else’s.

We didn’t need Paul Revere to warn us that the red tape was coming because we didn’t need a rule to tell us the right way to do business. 