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at Risk?

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Regulation of the Financial Services Industry: Whose Money is it that is at Risk?

By

Dana Muir*

I. Introduction

In today's financial geography, Wall Street intersects Main Street. When it comes to sound bites, politicians recognize that ordinary Americans feel the effects of plummeting financial markets in their retirement savings.¹ But, when the discussion turns to reforming financial services regulation, the reformers forget that much of the money that greases the cogs of Wall Street comes from dedicated retirement savings accounts, such as 401(k) accounts.

The continuing turmoil in the financial services sector almost certainly will result in regulatory reform.² Numerous commentators and policy makers have blamed deregulation, lack of federal oversight, fragmentation of agency authority, or some similar regulatory failing for allowing the growth in subprime mortgages, credit default swaps, and other financial products that have contributed to the financial crisis.³ Even during continuing economic instability, the new Presidential administration has stated that regulatory reform is a high priority.⁴

In March 2008, Secretary of the Treasury Henry M. Paulson, Jr. set out an aggressive proposal, *The Department of the Treasury Blueprint for a Modernized Financial Regulatory Structure*⁵ (*Blueprint*), for the reorganization of regulatory authority over the financial services industry. The *Blueprint's* publication date shortly followed the near bankruptcy of Bear Stearns, which was one of the early events to rattle US financial markets and challenge regulators to intervene aggressively.⁶ The proposal, though, was not a hastily compiled reaction to the Bear Stearns situation or to the later and more widespread financial instability in the US markets. In March 2007 Treasury had convened a conference on the competitiveness of US capital markets.⁷ Following the conference, Treasury initiated a study on how other countries allocate authority over financial services and sought comments on potential reform.⁸

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¹ John Harwood & Michael Cooper, *McCain and Obama Urge Greater Oversight in Financial Bailout Plan*, N.Y. TIMES, Sept. 22, 2008, at A18 (quoting Senator Barack Obama on the financial crisis: "Regardless of how we got there, we now have a situation where people's jobs, people's savings, people's retirement accounts, their job security, all that is at risk."); Carl Hulse, *Faced With Financial Upset and an Election, Lawmakers Lash Out*, N.Y. TIMES, Sept. 24, 2008, at A24. (quoting Representative John A. Boehner of Ohio: "But I am going to argue that if we do nothing, we are jeopardizing our economy, jobs, people's retirement security. Congress has to act and we have to act quickly.").

² See e.g., Kara Scannell, *Revamp of Regulatory Agencies Expected to Grow*, WALL ST. J., Sept. 16, 2008, at A10.

³ Kara Scannell, *Crisis on Wall Street: Schapiro Pledges Vigilance as SEC Chief*, WALL ST. J., Jan. 16, 2009, at C3 (quoting SEC Chair Mary Schapiro at her confirmation hearings as saying: "One of the real tragedies and one of the real lessons of this tragedy is that we have this stovepiped approach to regulation that allows misconduct to take place out of the sight of at least some of the regulators....").

⁴ See, e.g., Monica Langley, *Summers Crafts Broad Role in Reshaping Economy*, WALL ST. J., Feb. 7, 2009, at A2.

⁵ DEPT. OF THE TREASURY, *BLUEPRINT FOR A MODERNIZED FINANCIAL REGULATORY STRUCTURE* (2008) (hereinafter *BLUEPRINT*). Throughout this article I use the regulatory framework proposed by the *Blueprint* as a basis for discussing the implications for regulation of retirement-specific accounts. I do this not because I believe that framework is likely to be adopted exactly as proposed. In fact, reform of financial services legislation will be contentious and draw out many proposals. See, e.g. Arthur Levitt, *How to Restore Confidence in Our Markets*, WALL ST. J., Oct. 22, 2008, at A15. Rather the *Blueprint* is a widely accessible, detailed, and thoughtful starting point.

⁶ Roddy Boyd, *The Last Days of BEAR STEARNS*, FORTUNE, Apr. 14, 2008, at 86.

⁷ *BLUEPRINT*, *supra* note 5, at 1.

⁸ *Id.*

As a result of that year-long effort, the *Blueprint* proposes sweeping revision of the regulatory structure used to oversee the institutions at the heart of the US financial system, such as investment banks, commercial banks, and insurers, as well as the operation of stock markets.⁹ Its approach would in the long term, among other things, increase the authority of the Treasury Department, decrease the authority of the Securities and Exchange Commission (SEC), and create new regulatory agencies.¹⁰ Though primarily focused on the allocation of authority among regulators, the proposal embeds significant substantive regulatory change by, for example, for the first time subjecting investment vehicles such as hedge funds to federal oversight.¹¹

Regulatory approaches, such as that of the *Blueprint*, which assume investor funds are interchangeable amalgamations of assets, fail to recognize and react to the way in which current regulation differs in its applicability based on the source of the funds. The terms are defined more extensively below,¹² but this article uses “retirement-specific accounts” to refer to dedicated, tax-favored retirement savings vehicles, which wrap around investor assets and enable the accounts to receive favorable tax treatment. In benefits terminology, these are typically referred to as defined benefit (DB) or defined contribution (DC) plans,¹³ and even more specifically as 401(k) plans, employee stock ownership plans, and so forth. The specialized benefits terminology, however, may be counterproductive where the focus should be, as it is here, on the assets held inside the benefits plan accounts and how the regulation of those accounts compares to regulation of non-retirement plan retail investment accounts such as brokerage accounts. To facilitate the discussion I use the ‘accounts’ terminology, modified as appropriate, to refer to the various types of vehicles that hold investment assets. This terminology also eases the discussion of international approaches to the regulation of retirement wealth accumulation since each country tends to use a unique terminology to refer to its retirement-specific programs.¹⁴ In contrast to retirement-specific accounts, “generalized investment accounts,” as used in this article, encompasses the broad universe of nonspecialized savings vehicles, such as bank savings accounts, brokerage accounts, and other retail investment vehicles that do not receive tax incentives intended to stimulate asset accumulation for retirement.

The *Blueprint* concludes that Australia’s regulatory structure for oversight of its financial services industry and markets provides the closest model to what would be the optimal structure for the US.¹⁵ Australia uses an objectives-based approach to financial services regulation. That approach requires establishing a few key objectives and assigning a regulator to each objective.¹⁶ Another regulatory model, known as the single consolidated regulator approach, has been adopted by the United Kingdom (UK)¹⁷ and praised by commentators on the basis of its efficiency, effectiveness, and predictability.¹⁸

Australia and the UK each made significant changes in their retirement income systems within a few years of undertaking reform of regulation over their financial services sectors. Both countries addressed the interdependency of stable financial markets and healthy private-sector mechanisms that provide retirement income by giving financial services industry regulators some authority over aspects of

⁹ *Id.*

¹⁰ *See id.* at 13-21.

¹¹ *See id.* at 19.

¹² *See infra* Part II

¹³ For a discussion of the definition of defined benefit (DB) as compared to defined contribution (DC) plans, see *infra* text accompanying notes 54-60.

¹⁴ In the US, the holding vehicles and their governing terms are called plans. In the UK the equivalent reference typically is to schemes. Australia does not even typically refer to retirements or pensions, instead preferring the term superannuation.

¹⁵ *See BLUEPRINT*, *supra* note 5, at 143.

¹⁶ *Id.* at 142.

¹⁷ *Id.* at 141.

¹⁸ Elizabeth F. Brown, *The Tyranny of the Multitude is a Multiplied Tyranny: Is the United States Financial Regulatory Structure Undermining U.S. Competitiveness?*, 2 *BROOK. J. CORP. FIN. & COM. L.* 369, 372-73 (2008); Elizabeth F. Brown, *E Pluribus Unum – Out of Many, One: Why the United States Needs a Single Financial Services Agency*, 14 *U. MIAMI BUS. L. REV.* 1, 9 (2005); Heidi Mandanis Schooner & Michael Taylor, *United Kingdom and United States Responses To the Regulatory Challenges of Modern Financial Markets*, 38 *TEX. INT’L L.J.* 317 (2003).

retirement-specific accounts. This is not to say that the path chosen by either Australia or the UK is the appropriate model for US regulation. Their approaches, however, help to show how the seemingly different worlds of financial services and retirement savings are now intrinsically linked and provide a basis to establish principles to guide US reform efforts.

Even before the most recent instability in the financial markets, the overlapping nature of retirement-specific investment accounts and other retail investment accounts in the US had increasingly blurred the boundaries between the authority of the SEC and Department of Labor (DOL). For example, after the Enron and other corporate scandals in the early part of the century, courts struggled to rationalize a DOL supervised disclosure regime for retirement-specific accounts, which arguably required earlier and more extensive disclosure to employee-shareholders than to non-employee shareholders, with the SEC's insider trading provisions, which would seem to prohibit the more extensive disclosures.¹⁹ Not only did the colliding regulations potentially put fiduciaries in a position where they would be forced to violate one of the requirements, the DOL's resolution of the conflict essentially gave it power to nullify the long tradition of securities law enabling companies to remain silent between required disclosure periods.²⁰ In another example of overlap, recently the SEC and DOL each issued separate regulatory proposals detailing requirements for disclosure of investment account fees and costs.²¹ The DOL's regime applies to retirement-specific accounts while the SEC's regime applies to some, but not all, types of generalized investment accounts. From an overall perspective, the regulatory overlaps have become so extensive that in July 2008, the SEC and DOL entered into a formal Memorandum of Understanding (2008 MOU) in order to clarify the division of authority over retirement specific accounts.²²

To date the reform proposals and literature have focused on either the financial system and securities side of regulatory reform²³ or on the pensions side.²⁴ In this article I argue that the two perspectives should be merged. Although the complexity of each of the areas has no doubt contributed to the paucity of literature merging the two, US reform of regulation over the financial services industry must take into account the trillions of dollars held by Americans in retirement-specific accounts.²⁵ A financial oversight structure that fails to recognize that some assets are held in retirement-specific accounts would create negative externalities on disclosures and other information flows. It would fall short of maximizing application of the insights of researchers in the fields of behavioral finance and behavioral economics. And it would create inefficiencies as entities could exploit regulatory differences between the formal retirement savings regime and the regulation of other investment vehicles to the detriment of investors.

Part II begins by examining the importance to the US financial system of assets held in retirement-specific accounts. It also analyzes the role of those assets in contributing to retirement income security. The Part concludes by explaining the fragmented approach taken by the US to regulating the relationship between the financial services industry and retail investors. It shows how that approach depends on the nature of the account used to facilitate investment. Part III explains the paradigm shift that has taken place in the basic nature of retirement-specific accounts. That shift changed the nature of the risks associated with the assets held in retirement-specific accounts. The current legislative approach was targeted at mitigating the risks of the prior paradigm.

¹⁹ See *infra* text accompanying note 140.

²⁰ See *infra* text accompanying note 140.

²¹ See *infra* Part V.A.1.

²² Memorandum of Understanding Concerning Cooperation Between the U.S. Securities and Exchange Commission and the U.S. Department of Labor (2008), www.dol.gov/opa/media/reports/mou072908.pdf.

²³ See, e.g., BLUEPRINT, *supra* note 5,

²⁴ See TERESA GHILARDUCCI, WHEN I'M SIXTY-FOUR: THE PLOT AGAINST PENSIONS AND THE PLAN TO SAVE THEM 260-88 (2008) (DATA AS OF 2003 YEAR END).

²⁵ Investment Company Institute, 2008 Investment Company Fact Book 87 (48th ed. 2008) (citing a figure of \$17.6 trillion as of year-end 2007). The financial market declines have resulted in trillions of dollars of losses in these accounts. See Congressional Budget Office, *The Effects of Recent Turmoil in Financial Markets on Retirement Security* 2 (Oct. 7, 2008) (estimating a drop of \$1 trillion through the second quarter of 2008).

Part IV considers the allocation of regulatory responsibility over retirement-specific accounts and compares it to the regulation of generalized investment accounts. Although changes in the basic structure of retirement-specific accounts have decreased many of the differences between those accounts and generalized investment accounts, neither the substantive regulation nor the assignment of regulatory authority has changed. The Part undertakes an operational analysis of the risk in retirement-specific accounts, which reveals specific types of problems that have arisen in these accounts.

Part V argues that reform of financial services industry oversight must recognize the attributes and regulation of retirement-specific accounts. To ignore this sector of investment would further entrench overlapping regulation, disregard the substantive risks to individual investors, and endanger the use of tools intended to maximize the accumulation of wealth for retirement support. In conclusion the Part discusses competing principles that must be balanced as reform moves forward. It suggests that a different balance may be struck for product-level regulation than for account-level regulation. Throughout the article, the approaches used by the UK and Australia are used to inform the discussion and analysis.

II. The Role and Regulation of Retirement-Specific Accounts in the US Financial System

This Part considers the importance of retirement-specific assets to the US financial system and to the individuals who rely on those assets for retirement security. The Part ends by describing how the current regulation of the relationships between financial services firms and investors differentiates based on whether assets are held in retirement-specific accounts or in generalized investment accounts.

A. Deployment of Assets

In the US, assets designated as formal retirement savings exceeded \$17.6 trillion in 2007.²⁶ Seventy-one percent of households in the US reported in 2007 that they had an Individual Retirement Account (IRA),²⁷ an employer-sponsored retirement plan or both.²⁸ Almost two-thirds of those assets are held in accounts that are formatted as workplace (employer-sponsored) employee benefit plans.²⁹

An important indicator of the importance of retirement assets to a national economy is the size of those assets compared to the size of the economy. As of year-end 2006, Organisation for Economic Cooperation and Development (OECD) data indicates that the percentage of US pension fund assets relative to the size of the US economy was 73.7 percent.³⁰ Another indicator of the importance of retirement savings is the comparison of retirement-specific assets to market capitalization of US companies. The \$17.6 trillion held as formal retirement savings compares to \$25.1 trillion, which was the worldwide market capitalization of operating companies listed on the New York Stock Exchange (NYSE) as of 2006 year end.³¹

The \$17.6 trillion held as formal retirement savings in the US can also be compared to the division of assets among various financial sectors. At year end 2006 the assets held by US insurers totaled \$6 trillion.³² The US securities sector and banking sectors each held assets of approximately \$12.5 trillion.³³

Not surprisingly, retirement assets have not been immune to the economic downturn. The Congressional Budget Office estimated losses of retirement assets at one trillion dollars through the

²⁶ *Id.* at 86.

²⁷ In the US, Individual Retirement Account (IRA) assets have risen from \$1.1 trillion in 1994 to \$4.2 trillion in 2006. Paul Brady & Sarah Holden, *The US Retirement Market, 2006*, 16 ICI RESEARCH FUNDAMENTALS 1, 4 (2007).

²⁸ *Id.*

²⁹ *Id.* at 2.

³⁰ OECD Pension Markets in Focus, Nov. 2007, available at <http://www.oecd.org/dataoecd/46/57/39509002.pdf>, at Figure 4A.

³¹ 2006 Annual Report, NYSE Group, Inc. 4 (2007). The NYSE did not break out the market capitalization of its listed operating companies for year-end 2007. The combined market capitalization for listed operating companies on NYSE Euronext was \$30.4 trillion. 2007 Annual Report, NYSE Euronext, 2 (2008).

³² BLUEPRINT, *supra* note 5, at 165.

³³ *Id.*

second quarter of 2008.³⁴ Estimates taking into account losses later in 2008 put the decline in retirement assets at a minimum of two trillion dollars.³⁵

According to OECD data, the percentages of retirement assets to the size of the national economy were slightly higher in the UK and much higher in Australia, with 77.1 percent and 94.3 percent respectively.³⁶ Estimates indicate that, among all of the major Asia-Pacific countries, Australia will continue to have the largest value of pension assets under management at least through 2015.³⁷ Almost fifty percent of total Australian pension account assets are invested in equity securities of Australian companies.³⁸

While the amounts invested are important because of the proportion and volume of the assets, investments made through retirement accounts also have an effect on the financial products offered by the financial services industry. Assets invested through retirement-specific accounts where the investors make their own investment choices have changed the market, and marketing, for retail investment products. In 1990 only eight percent of long-term mutual fund holdings were held in the type of retirement-specific accounts known as defined contribution (DC) plans.³⁹ By 2007 that percentage tripled, to twenty-four percent.⁴⁰ Decision-making on investments in those accounts is typically the responsibility of the individual account holders. Thus, pension trends mean that mutual funds increasingly must recognize and target the individual investor market. As a comparison, institutions, including financial institutions, not-for-profit companies and other institutional investors, held fourteen percent of mutual fund assets in 2007.⁴¹ Acknowledgement of the scope of overall retirement assets invested in mutual funds would require knowing the extent to which those institutional investors were investing other types of plan assets, most specifically defined benefit plan assets.

Less quantitative measures of the importance of retirement savings to the US economy and the financial services industry were evidenced in legislation passed as the Pension Protection Act (PPA) of 2006.⁴² PPA amended prior law to permit hedge funds to receive more investments from pension plans without causing the hedge funds to become subject to complex and limiting rules that apply to pension plan fiduciaries.⁴³ And, although for a number of years there has been significant demand from employees for investment advice connected with their DC plans, until 2006 significant hurdles discouraged employers and others from directly or indirectly providing advice.⁴⁴ PPA provisions addressed those issues by reducing barriers to the provision of information on DC plan investments by employers and professional investment advisors.⁴⁵ The PPA provisions had been heavily lobbied for by hedge funds and investment advisors who wanted easier access to the business opportunities in retirement-specific accounts. In addition, to signaling the importance of the retirement assets to the financial services market, the enactment of those PPA provisions illustrates that as recently as 2006 legislation effectively reduced the regulatory effect on the relationship between investors in retirement-specific accounts and the financial services industry

From the investor-side of the equation, retirement-specific accounts play an important role in providing some level of financial security in a system where the governmental Social Security system of

³⁴ See Congressional Budget Office, *The Effects of Recent Turmoil in Financial Markets on Retirement Security* 2 (Oct. 7, 2008).

³⁵ Eleanor Laise, *Big Slide in 401(k)s Spurs Calls for Change*, Wall St. J., at A1 (Jan. 8, 2009).

³⁶ OECD Pension Markets in Focus, Nov. 2007, available at <http://www.oecd.org/dataoecd/46/57/39509002.pdf>, at Figure 4A.

³⁷ IFSA, *Essential Super Stats: New Year Edition* 4 (2008).

<http://www.ifsa.com.au/Information%20Area/Essential%20Super%20Stats%20January%202008.pdf>.

³⁸ *Id.* at 5.

³⁹ Investment Company Institute, 2008 Investment Company Fact Book 82 (48th ed. 2008).

⁴⁰ *Id.*

⁴¹ *Id.* at 83.

⁴² Pub. L. No. 109-280, 120 Stat 780 (codified as amended in scattered sections of 26 USC. & 29 USC.).

⁴³ Craig C. Martin & Joshua Rafsky, *The Pension Protection Act of 2006: An Overview of Sweeping Changes in the Law Governing Retirement Plans*, 40 J. MARSHALL L. REV. 843, 864-65 (2007).

⁴⁴ See, e.g. Dana M. Muir, *The Dichotomy Between Investment Advice and Investment Education: Is No Advice Really the Best Advice?*, 23 BERKELEY J. EMP. & LAB L. 1 (2002).

⁴⁵ Sarah D. Burt, Note, *Pension Protection? A Comparative Analysis of Pension Reform in the United States and the United Kingdom*, 18 Ind. Int'l & Comp. L. Rev. 189, 225 (2008).

retirement benefits is fragile. More than a third of Americans receive pensions or annuities from retirement-specific accounts attributable to employer-sponsored benefit plans.⁴⁶ Those pensions and annuities contribute more than 19 percent of the income received by the population age 65 and over.⁴⁷

In sum, in the current retirement regime, many individuals rely on the capital markets for the stability and integrity of their retirement income. In turn, the capital markets rely on retirement assets as both a source of assets to be invested and of fees for the financial services industry. Regulatory reform proposals such as Treasury's *Blueprint* recognize that the framework for regulation of the financial markets including futures exchanges, securities offerings, and depository institutions, and futures exchanges is now more than 70 years old and increasingly archaic.⁴⁸ The regulatory framework has not kept up with evolution of the capital markets, which has developed sophisticated products and faces increased competition from foreign capital markets.⁴⁹ What is rarely recognized though is the extent to which that framework also has departed from the current paradigm in retirement asset accumulation. Given the importance of retirement-specific accounts to the economy, the financial services industry, and individuals, regulatory reform will be inadequate unless it addresses the way in which retirement plan regulation intertwines with financial services regulation.

B. Regulation of Interactions between Financial Services Firms and Investors

Much of the regulation that is of relevance in reform proposals such as the *Blueprint* focuses on the operation and governance of the capital markets, the relationships between financial services firms, and the connections between the government, including government guarantees, and the financial firms. Another important set of relationships covered by the reform proposals, however, is the interaction between the financial services industry and retail investors. It is in this latter set of relationships that the *Blueprint* appears to assume, without discussion or a plan for transition, that the new regulatory regime will apply to retail investments as undifferentiated amalgamations of assets. But, that ignores the current regulatory approach, which differentiates depending on the type of account in which assets are held.

Figure 1 shows a simplistic model⁵⁰ of the relationships between the financial services industry and retail investors. Those retail investors all purchase financial products hoping for a positive return on their assets. But, the current regulatory regime splinters authority for regulation of investment-related matters among a variety of agencies depending on the type of account that holds the investor's assets. Without considering all the possible retail investment alternatives, a few examples can make the point. Some investors may put after-tax money in retail brokerage accounts and invest in products such as mutual funds or securities of individual companies (A\$). Others may decide to hold after-tax money in what have historically been viewed as more conservative products such as bank savings accounts, certificates of deposits, or US Treasuries (B\$). In either case, this article refers to the investments as generalized investment accounts.

Still other investors save in tax-favored dedicated retirement-specific accounts that generally provide an array of investment product choices (R\$). US tax rules provide favorable tax treatment to the accumulation of retirement-specific assets so long as the assets are held in a plan or account that meets detailed requirements. Those requirements are intended to achieve specific policy goals such as ensuring the fairness of any employer contributions and controlling foregone tax revenue. It is the accounts or plans that meet these requirements that this article refers to as retirement-specific accounts. Within R\$, the assets may be held in accounts created through plans sponsored by private-sector employers (referred

⁴⁶EBRI: Databook at chapter 7, p. 1 (data as of 2006 year end), *available at* <http://www.ebri.org/pdf/publications/books/databook/DB.Chapter%2007.pdf>.

⁴⁷ *Id.* at 3, chart 7.1b.

⁴⁸ BLUEPRINT, *supra* note 5, at 2.

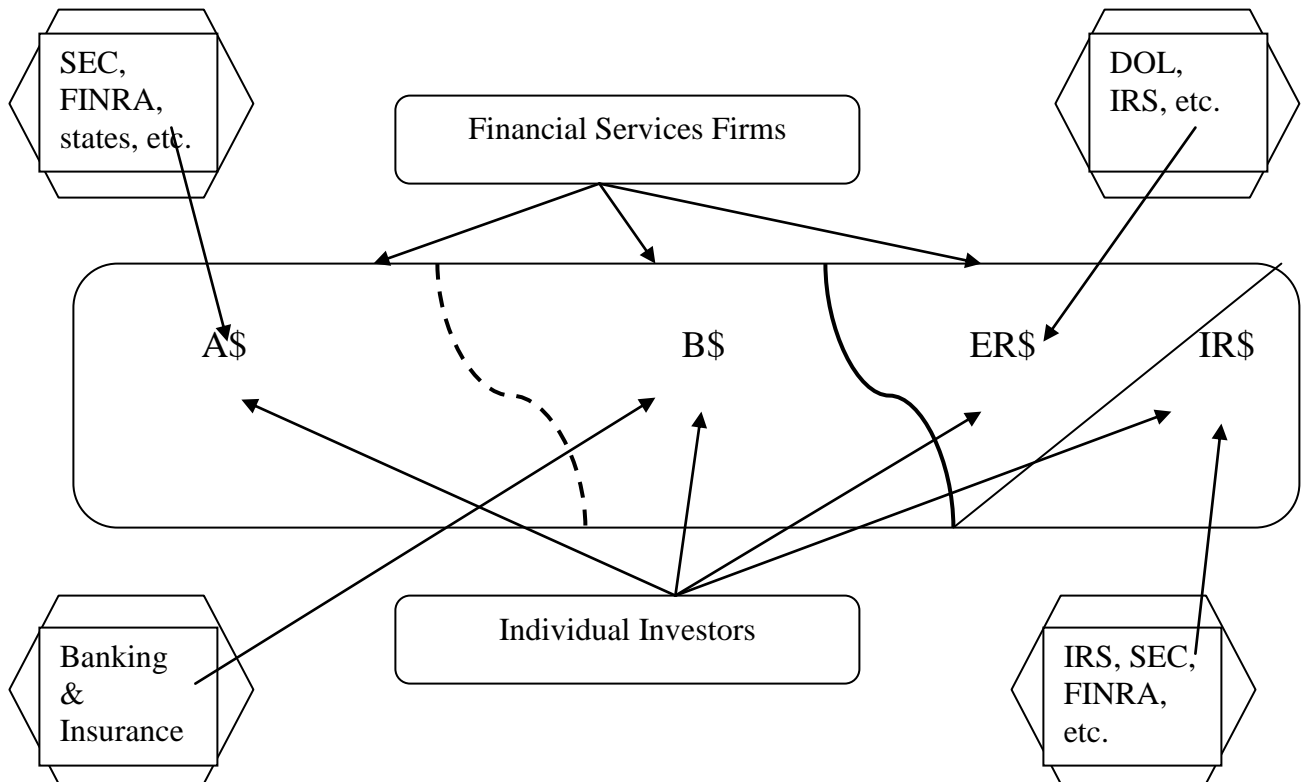
⁴⁹ *Id.*

⁵⁰ The model ignores the layers of financial services firms involved in a retail investment transaction because the critical point for this article is the relationship between the retail investors and the financial services industry writ large, not the relationship among the various firms in the financial services industry.

to here as employer retirement dollars (“ER\$”)) or be in accounts established by individuals, not employers (individual retirement dollars (“IR\$”)).⁵¹

Currently federal regulation differentiates R\$ not just by establishing minimum tax policy requirements for retirement-specific accounts but also by sometimes setting different standards for the relationship between the investors of R\$ and the financial services industry. The differentiation is observable in both the substantive requirements that govern that relationship and in the regulatory entities that develop, administer, and enforce those substantive requirements. More specifics of the differentiation are explored below in Part IV, which also considers the resulting inefficiencies. First, however, the next Part explains how this regulatory differentiation came to exist and why it is becoming a historical anachronism.

Figure 1



⁵¹ A third possibility is that assets are held in retirement-specific accounts established by governmental employers. Because neither the tax nor the labor provisions of ERISA reach those plans, this article treats them as beyond its scope.

III. Paradigm Shifts in Asset Accumulation for Retirement

The US, UK, and Australia now share an individual savings oriented approach to the accumulation of retirement assets. Over the past thirty years, workers in the US and the UK have taken on more individual responsibility in planning for their financial security in retirement.⁵² Australia's history is a bit different. Its recent success in generating retirement savings is traceable to 1992 when it began requiring employers to contribute to retirement asset accumulation programs.⁵³ This Part examines those trends and discusses the import for retirement adequacy.

A. The Transition from Receiving Monthly Checks to Writing Your Own Checks

For most of the twentieth century one of the many traditions shared by the US and the UK is that those employees fortunate enough to have pension plans sponsored by their employers, retired knowing that they would receive a monthly check for the rest of their lives. In benefits terminology, these plans are called defined benefit (DB) plans. All of the plan assets are held in a single retirement-specific account and the terms promise a monthly life-time pension check to retirees who meet minimum criteria. The amount of the pension promise is based on a formula often related to salary and years of work at the employer that established and funded the DB plan. The employer accepts responsibility to ensure the account holds sufficient funds to pay the promised benefits. The employer, therefore, takes on the investment risk of the pension promise.⁵⁴ In the US these types of plans date back to 1875 when the American Express Company, then in the railroad business, established a DB plan for its workers.⁵⁵

In both the US and the UK, DB plans appear to be on their way to becoming historical artifacts. Commentators typically point to the unpredictable and significant funding obligations borne by employers and increasing regulatory burdens as primary factors that have caused many employers in the US and UK to terminate or freeze their DB obligations and the accounts that hold the assets.⁵⁶ Regardless of the impetus, which also may be affected by employee mobility, diminished rates of unionization, and the increase in global competition,⁵⁷ the number of US workers who participated in DB accounts fell to approximately 18.5 percent of workers in 2003 from 22.9 percent in 1995. Much of the drop in DB coverage occurred earlier in the US than in the UK. One has to go back to 1980 to find a 35 percent coverage rate in the US.⁵⁸ But, although the trend in the UK is more recent, employers there also have reduced their use of DB accounts, often by not permitting new employees to earn those benefits.⁵⁹

The decrease in the numbers and coverage of DB accounts did not spell the end, however, of employment-related retirement-specific accounts in either the US or the UK. Instead, employers shifted their focus to accounts that function very much like individual brokerage or savings accounts. Those are known as defined contribution (DC) plans or, in this article's terms, DC retirement-specific accounts. All employer-sponsored DC accounts establish an individual investment account for each employee who participates in the employer's plan. And, for purposes of this article, I only include accounts governed by terms that make the assets held in the account eligible for tax incentives explicitly intended to encourage

⁵² See *infra* Section III.A.

⁵³ Hazel Bateman & John Piggott, *The Australian Approach to Retirement Income Provision*, 8 (2001), available at <http://www.ier.hit-u.ac.jp/jprc/soukai2002/piggott-paper.pdf>.

⁵⁴ EMPLOYEE BENEFITS LAW (Jane Stanley ed., 2000).

⁵⁵ See e.g. Dana M. Muir, *From YUPPIES to GUPPIES: Unfunded Mandates and Benefit Plan Regulation*, 34 GA. L. REV. 195, 209 (1999).

⁵⁶ Dana M. Muir, *Contemporary Social Policy Analysis and Employee Benefit Programs: Boomers, Benefits, and Bargains*, 54 WASH. & LEE L. REV. 1351, 1414-17 (1997).

⁵⁷ GHILARDUCCI, *supra* note 24, at 67-80.

⁵⁸ Pension Benefit Guaranty Corp., PENSION INSURANCE DATA BOOK 60 (2005).

⁵⁹ Four out of five DB plans in the UK have been closed to new employees. James Salmon & Ian Drury, *Final Salary Pensions now 'Extinct' for Private Sector Workers – as State Staff Enjoy 'Gold-plated' Deals*, THE MAIL ON SUNDAY, Aug. 25, 2008. Between 2000 and 2006 the number of open private sector occupational DB plans with only one section dropped from 18,350 to 3,470. During the same period, membership in those plans fell from 4.1 million to 1.6 million employees. UK Office for National Statistics, OCCUPATIONAL PENSION SCHEMES ANNUAL REPORT 8, 16 (2007) (*hereinafter* "UK ANNUAL REPORT").

retirement savings. Even given the constraints imposed on tax-favored plans, the terms of the DC plan that wraps around the assets can vary widely. A plan may cover one individual or thousands of employees. Those individuals may work for one employer or a variety of employers. It may be formed as a trust or the terms may be set out in a contract. Contributions to DC retirement-specific accounts may come from employers, individuals, or both. Here, I exclude all programs where benefits are paid by a government, such as the US social security program.⁶⁰

In the US, 401(k) accounts, named after the Internal Revenue Code (Code) section that authorizes the accounts, constitute the most frequently held type of employer-sponsored DC retirement-specific account.⁶¹ Sponsorship of accounts that conform with Code section 401(k) has grown from essentially zero in 1981⁶² to the point that those plans now have more participants and assets than any other type of employer-sponsored DB or DC account. At year-end 2006, approximately 50 million US workers owned 401(k) accounts with assets totaling an estimated \$2.7 trillion.⁶³

Federal tax law also recognizes a number of types of employer-sponsored DC retirement-specific accounts with terms that differ from those of 401(k)s. Profit sharing plans exist to allow employers to contribute a portion of their profits to retirement accounts for their employees.⁶⁴ Regulation provides streamlined options for retirement plan sponsorship to small employers such as the Simplified Employee Plan (SIMPLE).⁶⁵ All of these accounts hold what is shown in Figure 1 above as ER\$.

In addition, federal tax law permits individuals to open retirement-specific accounts without any employer sponsorship or action. For example, individuals may establish IRAs, which are permitted to accept rollovers from employer-sponsored tax-favored plans.⁶⁶ The assets held in these kinds of accounts are shown in Figure 1 above as IR\$. The detailed differences certainly matter for tax policy but, regardless of those details and the technical plan designations, all of these accounts provide an opportunity for the accumulation of retirement wealth in individual accounts.⁶⁷ The non-tax regulatory treatment varies significantly between accounts hold ER\$ and those holding IR\$.

The UK also has approved a variety of DC retirement-specific accounts in an attempt to encourage employees to accumulate assets for retirement. The first wave of DC accounts in the UK consisted of private sector occupational (employer-based) accounts that were established after 1979. The number of those plans has fallen from a peak of 46,730 in 2004 to 33,770 in 2006. Those accounts were established through the use of a trust and membership has remained at about one million.⁶⁸ Beginning in 1988 the UK provided opportunities for far more people to open a kind of DC account known as a personal pension. Workers were allowed to opt out of a portion of the UK public pension system (the portion then known as SERP) and open a personal pension instead. Alternatively they could opt out of their current or former employer-sponsored occupational pension scheme in favor of a personal pension.⁶⁹

⁶⁰ This definition matches generally to the scope of DC plans covered by ERISA and used by widely-available surveys and research.

⁶¹ In addition to work-based DB and DC plans, in the US other formal and informal financial vehicles provide mechanisms for the accumulation of retirement wealth. A full catalog of the many possibilities would require a level of detail not necessary for purposes of this Article. To complicate matters further, these retirement savings vehicles that are based outside the workplace may contain assets that originated in work-based plans. For example, about one-half of the assets held in IRAs originated in work-based plans. Of course, individuals also may save for retirement using methods that are not retirement-specific, whether that involves cash stuffed in a mattress or the purchase of an exotic financial instrument.

⁶² Muir, *supra* note 44, at 6.

⁶³ Sarah Holden, *401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2006*, 13 ICI RES. PERSP. 1, 2 (2007).

⁶⁴ *Complementary & Private Pensions Throughout the World 2007*, Organization for Economic Cooperation & Development 97 (2008).

⁶⁵ *Id.*

⁶⁶ *See id.*

⁶⁷ One type of tax-favored plan that is different is known as an Employee Stock Ownership Plan (ESOP). While similar in many ways, including individual accounts, longevity risk, and assignment of investment risk, ESOPs must invest primarily in employer stock. Therefore, the choice of investment alternatives issue typically does not occur in ESOPs.

⁶⁸ UK ANNUAL REPORT, *supra* note 59, at 8-9, 16.

⁶⁹ Elizabeth D. Tedrow, *Social Security Privatization in Other Countries – What Lessons Can Be Learned for the United States?*, 14 ELDER L.J. 14, 35-59 (2006).

The UK next created a new type of retirement-specific account in 2001, which was intended to avoid the problems it had encountered with personal pensions. The goal of those accounts, known as stakeholder pensions, was to operate at low cost while meeting a set of minimum requirements intended to protect account holders. The UK requires most employers that do not offer any other type of pension plan meeting minimum standards to select a stakeholder scheme and make it available to employees. There is no obligation, though, for either employers or employees to contribute to stakeholder pensions. For this reason, pension participation in the UK remains much lower than in Australia. As of 2004 only about one million individuals had contributed to a stakeholder plan.⁷⁰ Currently the UK has another set of pension reforms underway in an effort to increase pension coverage and income.⁷¹ It plans in 2010 to introduce a type of retirement-specific account to be called personal accounts.⁷²

In Australia historic pension coverage for private sector employees has been best explained as “haphazard[], covering some occupations and not others and providing markedly variable conditions and benefits.”⁷³ There was, and continues to be, some use of DB pensions.⁷⁴ In the mid-1980s DC pensions, called accumulation pensions in Australia,⁷⁵ became widespread through union agreements, with coverage reaching 79 percent in the early 1990s.⁷⁶

Against that backdrop, Australia made a bold move in 1992 by adopting a mandatory private pension scheme known as its Superannuation Guarantee.⁷⁷ The Guarantee began as a requirement that employers contribute three or four percent of earnings for almost all employees to individualized accounts. The accounts are held by and invested in superannuation funds, which vary widely in factors such as numbers of members, investment strategy, whether they are open to the public or restricted in some way such as to a particular industry.⁷⁸ The amount of the mandatory contribution made by employers has increased over time and currently is nine percent of earnings.⁷⁹ The mandatory, employment-based nature of the Australian system has resulted in a participation rate above 90 percent.⁸⁰

Superannuation Guarantee accounts operate as DC accounts, which are invested and administered by not-for-profit funds or by for profit commercial enterprises.⁸¹ Those entities create account products that meet the required regulatory terms. Employers designate one or more entities to accept the employer’s contributions. In 1996 the Australian government adopted a policy to encourage competition among the funds that could receive superannuation contributions by permitting individuals to have some choice among funds.⁸² The policy of choice was so controversial that legislation to permit choice was not enacted until 2004 and implementation of choice began in mid-2005.⁸³

⁷⁰ See Barbara Waive, *Ownership and Security: Individualised Pensions and Pension Policy in the United Kingdom and the United States*, 10 J. Comp. & Change 328-29 (2006) (discussing US proposals for individual accounts). But, 82 per cent of the schemes designated by employers had not garnered any members as of 2004. *Id.* A new type of scheme, known as personal accounts, is planned for 2012. Barbara Waive, *Personal Provision of Retirement Income in the UK* 9-17 (forthcoming 2009) (forthcoming book chapter, on file with Professor Dana M. Muir).

⁷¹ Waive, *Personal Provision*, *supra* note 70.

⁷² *Id.*

⁷³ Bateman & Piggott, *supra* note 53, at 2.

⁷⁴ Hazel Bateman, *Recent Superannuation Reforms: Choice and Flexibility in Retirement*, 16 Aus. Acctg. Rev. 2, 2 (2006) (noting that public sector funds were more widespread and DB plans predominated); Hazel Bateman, *Regulation of Australian Superannuation*, 36 Aus. Econ Rev. 118, 118-19 (2003) (noting that public sector DB plans date to the mid-nineteenth century). For a case study of the recent insolvency of a DB plan sponsored by a private sector Australian employer, see Shauna Ferris, *Ansett’s Superannuation Fund: A Case Study in Insolvency*, in *Retirement Provision in Scary Markets* 161 (H. Bateman ed. 2007) (analyzing the insolvency of Ansett, an Australian-based airline).

⁷⁵ Bateman, *supra* note 74, at 119.

⁷⁶ Bateman & Piggott, *supra* note 53, at 3.

⁷⁷ See *infra* text accompanying notes 78-80.

⁷⁸ Bateman & Piggott, *supra* note 53; see also Bateman, *supra* note 74, at 120-21.

⁷⁹ Bateman & Piggott, *supra* note 53, at 9.

⁸⁰ OECD, *Private Pensions: A Growing Role* 2, available at <http://www.oecd.org/dataoecd/36/11/38731322.pdf>.

⁸¹ *Id.* at 15-17.

⁸² Gail Pearson, *You’ll Need at Least a Million Dollars’ – The Regulation of Superannuation in Australia*, 5 presented at ALSB Annual Conference, St. Petersburg, FL, 2006 (copy on file with author).

⁸³ *Id.*

Whether one looks at the UK, Australia, or the US, the new standard in work-related retirement plans is increasingly becoming similar to the equivalent of an individual investment or savings account. Figure 2 summarizes pension-related savings vehicles with individual accounts in the US, UK, and Australia. Employers may, or in the US and the UK may not, contribute to the accounts. The details of the accounts vary widely in many details, including whether assets are held in a trust or governed by

Figure 2. Retirement-Specific Accounts with Individual Accounts			
	Employer-based Schemes (ER\$)		Personal Vehicles (IR\$)
	Trust-based	Contract-based	Contract-based
US	<ul style="list-style-type: none"> • 401(K) • Profit-sharing • Etc. 	<ul style="list-style-type: none"> • Simplified Employee Plan, SIMPLE 	IRA, etc.
UK	- Occupational Money Purchase	<ul style="list-style-type: none"> • Group Personal Pension • Stakeholder Pension 	<ul style="list-style-type: none"> • Individual Personal Pension • Stakeholder Pension
Austr.	- Superannuation Account		<ul style="list-style-type: none"> • Self-managed Superannuation Fund

contract, the minimum and maximum annual contributions, and regulation of the distribution of account assets before and after retirement. All of those details are important from the perspective of tax policy, the rights of account holders, and obligations of employers. However, for purposes of considering the ways in which the regulation of DC retirement-specific accounts intersects with the regulation of the financial services industry, it is the individualized nature of the accounts and the relationship between the account holders and those, including employers and financial services firms, who sit on the other side of the equation that is relevant. And, while it is possible that the US paradigm could shift once again to DB entitlements, commentators generally view such a change as highly unlikely.⁸⁴

B. Risks in a DC World for the Accumulation of Retirement Assets

The paradigm shift from DB plans to DC retirement-specific assets has rendered current regulation an outdated solution to a very different set of risks than existed in the 1970s when the Employee Retirement Income Security Act of 1974 (ERISA),⁸⁵ the primary federal statute regulating employer-sponsored retirement-specific accounts, was enacted. Commentators have written extensively on the implications the convergence of work-related retirement plans on a DC model have for the

⁸⁴ See ROGER LOWENSTEIN, WHILE AMERICA AGED 236 (2008) (“[I]t is probably too late to preserve the traditional pension system.”); EDWARD A. ZELINSKY, THE ORIGINS OF THE OWNERSHIP SOCIETY 145 (2007) (“There will be no resurrection of traditional defined benefit pension plans.”); Karen C. Burke & Grayson M.P. McCouch, *Social Security Reform: Lessons from Private Pensions*, 92 CORNELL L. REV. 297, 303 (2007) (“ERISA’s regulatory scheme bears more heavily on defined benefit plans and thus puts them at a comparative disadvantage relative to defined contribution plans”); Edward A. Zelinsky, *The Defined Contribution Paradigm*, 114 YALE L.J. 451, 534 (2004) (“[T]here is today no realistic chance of resuscitating the classic annuity-paying defined benefit plan.”). *But see*, GHILARDUCCI, *supra* note 24, at 101 (“[T]he case for DB pensions has never been stronger.”).

⁸⁵ Employee Retirement Income Security Act of 1974 (ERISA), ERISA §§ 1-4402, 29 U.S.C. §§ 1001-1461 (2000).

adequacy of retirement income.⁸⁶ This section focuses on a different question -- the changes in the risk profile of asset accumulation that have resulted from the movement to a DC model. Unlike in DB plans, individuals, not employers, may choose whether they will participate in a work-related retirement plan. Individuals, not employers, typically choose how to invest the assets. Individuals, not employers, bear the investment risk on the accounts. And, individuals, not employers, decide how the accumulated assets will be distributed in retirement. As recognized by other commentators, the effect of these changes on risk can be categorized as participation risk, investment risk, and longevity risk.⁸⁷ The regulatory challenges created by these risks differ significantly in a DC model from those that existed under the DB plan model in place when Congress enacted ERISA in 1974.

Consider participation risk first. Both the percentage of employees in the US covered by and the number of employees who participated in either a DB or a DC style work-related retirement-specific account dropped between 1999 and 2003. Coverage rates decreased to 46.7 percent in 2003 from 50 percent in 1999.⁸⁸ This decrease is more problematic than is first apparent. Evidence shows that significant numbers of employees covered by (eligible to participate in) DC plans do not choose to contribute and that lower-paid workers are less likely to contribute (participate) as compared to more highly paid workers.⁸⁹ Thus, the shift to DC retirement-specific accounts increases the participation risk for employees because participation depends not only on whether the employer offers a plan but also whether employees choose to contribute.

The shift to DC retirement-specific accounts has also increased the investment risk for employees. Most DC accounts delegate investment choice to employees. Since the benefit an employee receives from such a plan is whatever amount is in that employee's account at retirement or distribution of the assets, the employee bears the investment risk. The result is to shift to employees not just the risk that a particular asset might perform poorly but also the risk that the appropriate holding period for some investments in a diversified portfolio may be longer than an individual employee can tolerate and the capital markets may be weak at the time that an individual employee retires or draws down assets.⁹⁰ DB plans, which typically were adopted with the intent that they would be in place for many years, could at least theoretically spread the risk of a down period in the markets or the risk of assets with long holding periods over the life of the DB plan.⁹¹

Finally, in a DB plan the requirement that the employer fund the plan sufficiently to pay promised benefits combined with the fact that benefits are paid for a retiree's lifetime means that employers bore the longevity risks in those plans. Most DC plans provide that assets will be distributed in a lump sum. Tax regulation requires that minimum distributions occur after a set age. Although nothing prevents the owner of assets held in a DC account to use those assets, either before or after distribution, to purchase an annuity, most retirees choose not to do so. As a result, retirees with DC retirement-specific accounts risk the possibility of outliving their accumulated assets.⁹² This risk is higher for women who statistically have longer life spans than men and tend to accumulate lower levels of assets for retirement.⁹³

⁸⁶ Colleen E. Medill, *Challenging the Four "Truths" of Personal Social Security Accounts: Evidence from the World of 401(k) Plans*, 81 N.C.L. REV. 901 (2003); Susan J. Stabile, *Paternalism Isn't Always a Dirty Word: Can the Law Better Protect Defined Contribution Plan Participants?*, 5 EMPL. RTS. & EMPLOY. POL'Y J. 491 (2001).

⁸⁷ See ZELINSKY, *supra* note 84, at 6-23 (referring to participation risk as funding risk). Professor Zelinsky explains that DB pension recipients are not insulated from all risks. They face reduction in the real value of their pensions through inflation, a possibility of payment default, and backloading, which causes the final years of a worker's career and long service at one employer to be especially important. *Id.* at 23-27.

⁸⁸ GHILARDUCCI, *supra* note 24, at 34.

⁸⁹ *Id.* at 118 (finding that 27% of workers with incomes between \$20,000 and \$39,999 did not contribute to a 401(k) when eligible whereas only 4% of workers earning over \$100,000 did not contribute when eligible).

⁹⁰ See ZELINSKY, *supra* note 84, at 6-13.

⁹¹ Of course, any minimum funding obligations impose requirements on DB plan sponsors, especially in an environment of low interest rates and falling equities markets. See, e.g. Jilian Mincer, *Record Losses Hit Pensions of Big Firms*, WALL ST. J. D7 (Nov. 18, 2008) (stating that the average funding for DB plans of employers referenced in the article fell from 100% at the beginning of the year to 76 percent).

⁹² GHILARDUCCI, *supra* note 24, at 122-25.

⁹³ *Id.* at 49-51.

The UK has experienced a similar shift in risk as the US. As in the US, the UK has seen a shift from DB to DC retirement-specific accounts.⁹⁴ The current voluntary system means UK pension savers face participation risk, as illustrated by the low number of individuals who contribute to stakeholder plans. Individuals in the UK typically have fewer investment choices and usually the account provides for a default investment so the risk in choosing the wrong investment is lower. However, individual account holders still bear the investment risk in the sense that their entitlement is equivalent to the amount accumulated in their retirement-specific account. And, the defined contribution nature of accounts combined with a lack of annuity distributions means that individuals also bear longevity risk. Australia avoids the first of these risks – that of participation – by mandating employer contributions to Superannuation Guarantee accounts. However, even in Australia, individual DC account holders bear both investment and longevity risk.

IV. Risk, Regulation and the Division of Regulatory Authority

This Part considers how current regulation addresses the risks inherent in DC retirement-specific accounts and the problems that result. It begins by examining the allocation of regulatory authority vis-à-vis employer-sponsored retirement-specific accounts and shows that the allocation is a historical artifact attributable to the DB pensions that were the standard at the time of ERISA's enactment. That approach is contrasted to the regulatory oversight of retirement-specific accounts that are not employer sponsored and of generalized investment accounts. For perspective and alternative approaches, the Part compares the regulatory challenges and the distribution of authority in the US to the approaches used in the UK and Australia.

A. Current Allocation of Regulatory Authority

The current US regulatory regime, which applies to all employee benefit plans sponsored by private-sector employers, is found in ERISA. Congress enacted ERISA in 1974 after ten years of debate.⁹⁵ A defining event for pension regulation was Studebaker's closing of its automobile assembly plant in South Bend, Indiana in 1963. Studebaker had sponsored a DB pension plan for its employees but that plan was drastically underfunded when Studebaker failed.⁹⁶ As a result, most employees and retirees received only a small portion of the pensions they expected or nothing at all. The severe economic impact on retirees and workers attracted the attention of law makers.⁹⁷ Eventually, the Senate held subcommittee hearings featuring testimony by workers from a number of companies who did not receive the pensions their employers had promised.⁹⁸

As a result of these unmet worker expectations, much of the congressional focus when enacting ERISA was on ensuring that employers kept the benefit promises they made to their employees.⁹⁹ The statutory mechanisms used to achieve security of DB pension promises included enhanced disclosure requirements, imposition of fiduciary standards, vesting and funding provisions, and private rights of enforcement.¹⁰⁰ Congress was also concerned with the amount and proper use of the tax expenditure for pension plans. Thus, ERISA limits both benefits from and contributions to retirement plans.¹⁰¹

⁹⁴ See *supra* text accompanying notes 68-72.

⁹⁵ JAMES WOOTEN, *THE EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974: A POLITICAL HISTORY*, 1 (2004).

⁹⁶ *Id.* at 51.

⁹⁷ *Id.* at 73-74.

⁹⁸ *Id.* at 168-69.

⁹⁹ *Id.* at 271; see also ERISA § 3, 29 USC. § 1001 (“[I]t is desirable in the interests of employees and their beneficiaries, . . . that minimum standards be provided assuring the equitable character of [pension] plans and their financial soundness.”).

¹⁰⁰ See WOOTEN, *supra* note 95, at 266-67.

¹⁰¹ *Id.* at 267.

Throughout the wrangling over benefits legislation, the DOL and IRS competed to receive regulatory authority over the benefits field.¹⁰² The fight extended to arguments over which subcommittees in the House and Senate had jurisdiction over the proposed legislation.¹⁰³ Congress ultimately resolved the turf battles by, as Rep. John Erlenborn put it, “cut[ting] the baby in half... [and leaving each committee and agency with] half this dead child.”¹⁰⁴

There was little pretense that the division of authority was other than a politically expedient solution. Even at the time, some legislators anticipated the inefficiencies that would result from overlapping jurisdiction.¹⁰⁵ Because Congress’s technical solution was to write many of the statutory provisions into both the labor and the tax sections of the US Code,¹⁰⁶ the IRS and DOL eventually agreed to cede each other authority over specific types of regulation. Under the agreement, the IRS received responsibility for funding, eligibility to participate in plans, and ensuring entitlement to plan funds. The DOL received authority over fiduciary issues, proper disclosure, and claims procedures. Currently the Employee Benefits Security Administration (EBSA), an agency within the DOL, exercises most of the DOL’s responsibilities for oversight of benefit-related issues.¹⁰⁷ The anomalous approach to duplicative legislative provisions continues to this day, as does the agreed upon division of responsibility between the IRS and DOL.¹⁰⁸

Those interested in the reform of financial services oversight will immediately notice that there is no obvious role for the SEC¹⁰⁹ in the regulation of employer-sponsored retirement-specific accounts. Although the SEC is responsible for regulatory implementation of disclosure requirements that govern the release of information by public companies and mutual funds to investors,¹¹⁰ EBSA has authority over the disclosure requirements imposed on employer-sponsored retirement-specific accounts, including on certain of the investments in those accounts.¹¹¹ While the SEC works with self-regulatory organizations such as the Financial Industry Regulatory Authority (FINRA) to set standards for the conduct of broker-dealers and other industry participants who deal directly with investors,¹¹² it is EBSA that oversees the fiduciary obligations of those individuals and entities who interact with employees who invest through employer-sponsored retirement-specific accounts.¹¹³ The scope of the securities fraud provision overseen by the SEC is widely recognized for its breadth in reaching material misrepresentations or omissions connected with the purchase and sale of any security as defined by the federal securities laws.¹¹⁴ In

¹⁰² See *id.* at 154-55 (competing for authority over fiduciary standards); 202 (arguing over which agency could best enforce the legislative standards);

¹⁰³ *Id.* at 194-96 (outlining the jurisdictional problems between the Senate Labor Committee and the Senate Finance Committee); 224-26 (discussing the clash between the House Labor Committee and the House Ways and Means Committee).

¹⁰⁴ *Id.* at 237.

¹⁰⁵ *Id.*

¹⁰⁶ WOOTEN, *supra* note 95. In part this division of authority between a tax regulator and a workplace regulator may exist because US pension policy has long reflected the tension between balancing tax and other incentives for employer sponsorship of pension plans with provisions that protect employees from malfeasance and unfairness.

¹⁰⁷ <http://www.dol.gov/ebsa/>

¹⁰⁸ STANLEY, *supra* note 54, at 39.

¹⁰⁹ In this article, I focus on the lack of a role for the SEC because of the SEC’s authority over many standard investment products; however the same point applies to regulators of insurance products, certificates of deposit and any other form of financial investment held in employment-related retirement-specific accounts.

¹¹⁰ See Corey Ciocchetti, *The Privacy Matrix*, 12 J. TECH. L. & POL’Y 245,331, n.89 (2007) (“The Securities and Exchange Commission (SEC) requires some prospectus documents that must be distributed to potential investors by public companies and mutual funds to possess certain sections drafted in plain English.”).

¹¹¹ See *Fiduciary Regulation for Disclosure in Participant-Directed Individual Account Plans*, 73 Fed. Reg. 43014, 43040 (proposed July 23, 2008) (to be codified at 29 C.F.R. §2550.404a-5(d)(4)(i)) (proposing disclosure standards for certain types of employment-related retirement-specific accounts).

¹¹² See *SEC Gives Regulatory Approval for NASD and NYSE Consolidation* (July 26, 2007), available at <http://www.sec.gov/news/press/2007/2007-151.htm> (noting that “FINRA will operate under SEC oversight.”).

¹¹³ See *Meeting Your Fiduciary Responsibilities*, available at <http://www.dol.gov/ebsa/pdf/fiduciaryresponsibility.pdf>.

¹¹⁴ See Thomas W. Joo, *Legislation and Legitimation: Congress and Insider Trading in the 1980s Summer*, 82 IND. L.J. 575, 608 (2007) (referring to “the broad, generic anti-fraud prohibition of Section 10(b) of the 1934 Act and the similarly broad SEC Rule 10b-5 promulgated thereunder”).

comparison, for employer-sponsored retirement-specific accounts, claims of misrepresentations or omissions fall within ERISA's fiduciary regime and are subject to ERISA's limitations on remedies.¹¹⁵ Another dimension of complexity is added by those accounts, such as IRAs that are retirement-specific accounts but are not employer-sponsored. EBSA has little to no regulatory authority over those accounts. Even though they have much the same tax treatment and share many other characteristics with employer-sponsored retirement-specific accounts, federal regulation treats the non-employer sponsored accounts differently from retirement-specific accounts in plans sponsored by employers.

Concentration of oversight responsibilities at DOL and IRS for employer-sponsored benefit plans was a rational approach when the primary risks to employees were, as was true in DB pension plans, that employers would not keep the promises that they were making of lifetime pension payments. The relationship risks were that an employer would not properly fund a plan, would commit malfeasance with respect to plan assets, or would be dishonest in explaining pension entitlement to employees. The employer's role and actions were the main determinant of whether an employee would receive the pension promised by the employer. As explained above, however, the DB plan is no longer the paradigmatic pension plan and the primary risk faced by employees is no longer that employers will not keep promises of life time pension payments. The methods used to accumulate wealth for retirement have changed but the regulation and division of regulatory responsibility has not.

The UK and Australia have taken quite different fundamental approaches to the regulation of retirement-specific accounts and to the integration of that regulation with oversight of other types of investment activities. Australia, where the employment-related pension system, the Superannuation Guarantee, is relatively new, does not have a workplace regulator as one of its key regulators for the Guarantee. Instead, it divides authority among the Australian Prudential Regulation Authority (APRA), the Australian Securities and Investments Commission (ASIC), and the Australian Taxation Office (ATO).¹¹⁶ ASIC's primary function is to regulate the business activities of all corporate entities in Australia. Included among those corporate entities are the financial entities that are active in providing the investment funds in which superannuation contributions are held and invested.¹¹⁷ In 1998, ASIC assumed responsibility for consumer protection vis-à-vis pension accounts and investments.¹¹⁸ This includes responsibility for disclosure requirements that are intended to provide investors with information necessary to make informed investment choices.¹¹⁹ APRA regulates the financial services sector from a prudential standpoint. As such, it is responsible to ensure prudent management so that the entities offering funds as investment vehicles for superannuation maintain the financial resources to meet their obligations.¹²⁰

Thus, retirement-specific accounts are included in the regulatory authority of ASIC and APRA in a way that does not generally differentiate between those accounts and other, non-retirement specific investment activities. Furthermore, Australia's regulation of superannuation follows the objectives-based approach that Australia applies more generally to financial services regulation.¹²¹ For example, one objective is to ensure that funds maintain sufficient assets to meet their obligations. Supervision of that objective is the task of APRA regardless of whether the financial services entity is holding assets that in the US would constitute A\$, B\$ or R\$.

¹¹⁵ See *id.*

¹¹⁶ Bateman, *supra* note 74, at 122; Leslie Nielson, *Benchmarking Australian Superannuation Regulation and Practice*, 13, available at http://www.aph.gov.au/senate/committee/corporations_cte/completed_inquiries/2004-07/superannuation/library_research_paper.pdf. The ATO regulates Self Managed Superannuation Funds, which are somewhat similar to U.S. Individual Retirement Accounts, in that SMSFs must have fewer than five members and the trustees must be fund beneficiaries.

¹¹⁷ Parliamentary Joint Committee on Corporations and Financial Services, *The Structure and Operation of the Superannuation Industry*, 9 (Aug. 2007) [hereinafter *Superannuation Industry*].

¹¹⁸ *Id.*

¹¹⁹ Nielson, *supra* note 116, at 13-14.

¹²⁰ *Superannuation Industry*, *supra* note 117, at 8.

¹²¹ See BLUEPRINT, *supra* note 5, at 142.

Compare the approach of the UK where the Financial Services Authority (FSA) and The Pensions Regulator (TPR) divide primary regulatory responsibility for pension plan oversight.¹²² The FSA and TPR have entered into a detailed memorandum of understanding that allocates authority between the two entities. At the conceptual level, the memorandum divides authority on the basis of the entities subject to oversight. The FSA, as an integrated part of its mission to “regulate[] the financial services industry in the UK,”¹²³ regulates the financial and insurance firms that advise on the marketing, sale, and provision of personal pensions and annuities. The FSA also has responsibility for improving investor knowledge and understanding of financial products and markets.¹²⁴ This includes the responsibility to improve employees’ understanding of the purchase of pension products through education and disclosure. The FSA heavily regulates disclosures to investors in pension products and provides comparison materials¹²⁵ and decision trees¹²⁶ on its own website.¹²⁷ The TPR’s role is to oversee and provide advice to employers and to trustees of work-based pension plans. In general TPR has responsibility for oversight of and providing advice to employers and to trustees of work-based pension plans. TPR is a public body accountable to the Department for Work and Pensions (DWP).¹²⁸

The specific differences in the way the US, UK, and Australia have assigned regulatory authority for work related pension savings are traceable to differing philosophies on division of that authority. Looking at the division between the IRS and EBSA, the US divides authority according to the types of legal issues that arise in the accounts – what I will call an issue oriented approach. If it is a fiduciary or disclosure issue, it belongs to the EBSA. If it is an issue of plan funding, it belongs to the IRS. The SEC and other financial services regulators are not part of that mix.

At the conceptual level, in the UK the FSA and TPR divide authority on the basis of the entities subject to oversight.¹²⁹ The FSA oversees the relationship between the individual employees who have pension accounts and the financial services firms that administer those accounts and provide the underlying investment products. Australia departs even further from the workplace model of regulation by dividing authority among ASIC, APRA, and ATO, with APRA playing the key role in consumer protection for other than prudential matters. In contrast, the US assigns to EBSA significant regulatory authority over the relationship between the individual employees who have pension accounts and the entities that administer the accounts. For example, disputes over mishandled investment directions are

¹²² HM Revenue & Customs’s role generally is limited to ensuring that the tax expenditure associated with tax-favored retirement-specific accounts remains in check.

¹²³ FSA website, “About the FSA,” <http://www.fsa.gov.uk/Pages/About/What/index.shtml>.

¹²⁴ See Ian Greenstreet, *Stakeholder Pensions – The Compliance Regime*, 8 PENSIONS 152 (2003). Dispute resolution also is handled differently in the US, UK and Australia. The US leaves dispute resolution to the benefit plan in the first instance with appeals heard primarily in the federal court system. In the UK, three different ombudsman services and The Pensions Advisory Service share responsibility for assisting individuals with pension-related questions, disputes and compensatory rights. Australia is similar to the US in that the benefit plan has the first opportunity and obligation to resolve benefit disputes. Australia differs, however, in that it has established a specific tribunal, the Superannuation Complaints Tribunal (SCT), to hear benefits-related complaints. Only a limited right of appeal exists from the decisions of the SCT.

¹²⁵ See <http://www.fsa.gov.uk/tables/bespoke/Pensions> (providing tables for comparison of both personal pension and stakeholder pension products).

¹²⁶ <http://www.moneymadeclear.fsa.gov.uk/trees>.

¹²⁷ The FSA has, however, declined to require some reporting on the basis that it would be too technical for investors to use. See Financial Services Authority, *Bundled Brokerage and Soft Commission Arrangements for Retail Investment Funds*, 3, available at http://www.fsa.gov.uk/pubs/policy/ps06_05.pdf. (stating its view is some detailed disclosures from fund managers would not be useful to individual fund investors “since most of them would probably find the information too technical to get any benefit from it).

¹²⁸ Although DPW, not TPR, develops pension policy and law in the UK, TPR is widely-recognized as a regulatory body. See Clearance Guidance (“The Pensions Regulator (the ‘regulator’) is the regulatory body for work-based pension schemes in the UK.”) <http://www.thepensionsregulator.gov.uk/guidance/clearance/introduction.aspx>

¹²⁹ This division of authority is detailed in a memorandum of understanding that allocates authority between the two entities. *Memorandum of Understanding Between the Financial Services Authority and the Pensions Regulator* (Apr. 6, 2005, as updated Oct. 2007), available at <http://www.thepensionsregulator.gov.uk/pdf/moufsa.pdf>.

governed by ERISA as fiduciary disputes, and thus are the territory of EBSA.¹³⁰ Similarly, EBSA has responsibility for disclosure requirements regarding benefits statements and such investment-related material as account fees.¹³¹

B. An Operational Analysis of Risk

As DC retirement-specific accounts have become more prevalent,¹³² the risks to employees in their accumulation of retirement wealth have changed. The risks of participation, investment return, and longevity all pose challenges to the ability of individuals to save enough to support themselves in retirement. This subpart analyzes specific examples of ways these risks have affected retirement savings, thereby highlighting the problems posed for substantive regulation and the division of regulatory authority.

1. Choice of Investments

One of the risks associated with DC accounts is investment risk. In DB plans, employers that sponsored the plans typically determined, directly or indirectly, the investment allocation of plan assets. That made sense in a style of plan where the employer also bore the investment risk. In DC plans, however, individuals typically must make their own investment allocation decisions and bear the resulting risk.¹³³ This assumption of risk becomes particularly perilous when individuals make undiversified bets in their account investments, choose the wrong type of retirement-specific account, or need retirement income during a down period in the markets. If employees are given a choice of investments or accounts, the regulatory system must anticipate that not all employees will make efficient choices. The alternative, of course, is a paternalistic system that constrains employees' ability to make investment choices.

a. US - Employer Stock

In the US, legal issues relating to the investment of pension assets in the stock of the plan's sponsoring employer were largely dormant, other than in the context of potential corporate takeovers¹³⁴ and Employee Stock Ownership Plans,¹³⁵ until two events occurred in rapid succession. Those events resulted in large losses in investments held in employer stock in retirement-specific accounts by employees of a variety of companies. The first event was the dramatic drop in the US stock markets after the bursting of the tech bubble in early 2000. The second event was the collapse of Enron Corporation in 2001, which was followed by a surge in governance and accounting scandals at other US companies.

In the employer stock cases, employees alleged wrongdoing against an array of individuals and institutions including the companies sponsoring the plans, individual plan fiduciaries, company directors, and directed trustees. The legal claims brought under ERISA can generally be divided into three

¹³⁰ See *LaRue v. DeWolff, Boberg & Assoc.*, 128 S. Ct. 1020 (2008) (finding that an individual has a cause of action under ERISA for mishandled investments in a retirement-specific account).

¹³¹ See *Fiduciary Regulation for Disclosure in Participant-Directed Individual Account Plans*, 73 Fed. Reg. 43014, 43040 (proposed July 23, 2008) (to be codified at 29 C.F.R. §2550.404a-5(d)(4)(i)) (proposing disclosure standards for certain types of employment-related retirement-specific accounts).

¹³² *Supra* Section III.A.

¹³³ Regulations permit plans to shift the investment risk from the plan sponsor to the individual account holders if minimum regulatory standards are met. For a discussion of the standards and other issues with delegation of investment choice, see Muir, *supra* note 44, at 8-10.

¹³⁴ See Steven J. Aresnault, *Fiduciary Duties of ESOP Trustees Under ERISA in Tender Offers: The Impact of Herman v. NationsBank Trust Company and a Proposal for Reform*, 3 U. PA. J. LAB. & EMP. L. 87, (2000) (discussing the fiduciary tensions inherent in fiduciaries who are high level employees making decisions for both the corporation and the retirement plan during hostile corporate takeover situations).

¹³⁵ Brett McDonnell, *ESOPs' Failures: Fiduciary Duties When Managers of Employee-Owned Companies Vote to Entrench Themselves*, 2000 COLUM. BUS. L. REV. 199 (2000) (discussing fiduciary issues resulting from employer stock held by ESOPs).

categories, all based in fiduciary obligation. As such, EBSA was the agency responsible for providing regulatory oversight and interpretation and it took an active role in some of the litigation.¹³⁶

The employer stock cases serve to illustrate the distinctions drawn in the regulation of employer-sponsored retirement-specific accounts (accounts holding ER\$) compared to generalized investment accounts (accounts holding A\$) and retirement-specific accounts not sponsored by employers (accounts holding IR\$). Assume an employee, Saver, invests \$100 in the stock of Saver's employer, Employer, through Employer's 401(k) (a retirement-specific account holding ER\$)¹³⁷ and another \$100 in the same stock through a brokerage account (a generalized investment account holding A\$). Saver loses most of the investment when the stock's value drops. If Saver then alleges that Employer intentionally misrepresented its business prospects, Saver might bring a lawsuit for fiduciary violation under ERISA for losses in the retirement-specific account but would claim securities fraud under section 10b of the Securities and Exchange Act of 1934¹³⁸ for losses in the generalized investment account. The agency responsible for regulatory oversight of the ERISA claim would be EBSA but the SEC would be responsible for oversight of regulation regarding securities fraud. Similarly, if an investor alleges fraud in a retirement-specific account not sponsored by an employer, EBSA would have no responsibility for oversight. Burdens of proof, the right to sue, and other litigation-related matters can be quite different between ERISA and securities law claims.¹³⁹ Yet, Saver's basic claim is the same in each instance – Employer intentionally misrepresented its business prospects. Perhaps this approach is optimal but the question fragmentation of law and oversight deserves a careful review as part of the reform of financial services regulation.

Another complication arises because of the different approach to regulation in the different types of investment accounts. Saver might claim that Employer's misrepresentation was one of omission. Saver's legal theory might be that the information Employer conveyed was misleading because it left out significant facts and thus what was communicated was misleading. Or, Saver might allege that Employer had information that Employer did not communicate to Saver but, if Saver would have known the information, Saver would not have purchased additional Employer stock or may have sold Employer stock. This scenario raises the question of whether ERISA's general fiduciary provisions require more frequent or more extensive disclosure to employees holding stock in retirement-specific accounts than the securities laws require public companies to make to their shareholders.¹⁴⁰ This question creates another

¹³⁶ For discussion of the typical allegations, see Dana Muir & Cindy Schipani, *The Challenge of Company Stock Transactions for Directors' Duties of Loyalty*, 43 HARV. J. LEGIS. 437, 459-60 (2006). Some cases have settled. See, e.g., Rankin v. Rots, No. 02-CV-71045, 2006 US Dist. LEXIS 45706 (E.D. Mich. June 28, 2006). Others have been dismissed for various reasons, including the unavailability of relief. *In re McKesson HBOC Inc. ERISA Litig.*, 391 F. Supp. 2d 812 (N.D. Cal. 2005). The Fifth Circuit recently granted summary judgment in favor of an employer based upon limitations on the employer's fiduciary duties and ERISA's reflection of policy goals favoring investment in employer stock. *Kirschbaum v. Reliant Energy, Inc.*, No. 06-20157, 2008 US App. LEXIS 9124, at *12, *21-34 (5th Cir. Apr. 25, 2008).

¹³⁷ Commentators have called for limitations or outright bans on the holding of employer stock in DC retirement-specific wrappers. See, e.g., *The Evolving Pension and Investment World After 25 Years of ERISA: Hearing Before the Subcomm. On Employer-Employee Relations of the Comm. on Education and the Workforce*, 106th Cong. 49-50 (2000) (statement of John H. Langbein, Professor, Yale Law School) (arguing for caps on employer stock); Jeffrey Gordon, *What Enron Means for the Management and Control of the Modern Business Corporation: Some Initial Reflections*, 69 U. CHI. L. REV. 1233, 1248-49 (2002) (arguing that the risk profile of undiversified holdings of employer stock may be incompatible with the tax incentives provided to those accounts). The US Congress has considered capping employee account holdings of employer stock but to date has refused to do so. Instead it enacted legislation in 2006 that requires plans to grant 401(k) account holders certain rights to diversify out of employer stock. The scope of those rights depend on whether the employer stock was purchased through employer or employee contributions. Stanley, *supra* note 54, at 208-09.

¹³⁸ 15 U.S.C. §78j(b) (2000).

¹³⁹ Muir & Schipani, *supra* note 136, at 343-51.

¹⁴⁰ The extent that ERISA's fiduciary provisions require disclosure beyond the reporting requirements explicitly set forth in ERISA has been controversial. See Shelby D. Green, *To Disclose or Not to Disclose? That is the Question for the Corporate Fiduciary who is also a Pension Plan Fiduciary Under ERISA: Resolving the Conflict of Duty*, 9 U. PA. J. LAB. & EMP. L. 831 (2007); Andrew S. Hartley, *Making the Case for Mandatory Removal of Imprudent Investment Vehicles: Inside Information Can Make Employer Securities a Bad 401(k) Option*, 5 APPALACHIAN J. L. 99 (2006); Susan J. Stabile, *I Believed My Employer and Didn't Sell My Company Stock: Is There an ERISA (or '34 Act) Remedy for Me?*, 36 CONN. L. REV. 385, 416-17 (2004).

layer of difficulty. If employees who hold stock in employer-sponsored retirement-specific accounts are entitled to superior disclosure as compared to general public shareholders then compliance with the disclosure requirements to the employees would violate the federal securities law prohibition on tipping and insider trading. Similarly, the employees' resulting trades would violate the insider trading rules.

EBSA's position on the insider trading issues has been that the ERISA and federal securities law obligations can be rationalized.¹⁴¹ According to EBSA's view, which has been accepted by a majority of courts,¹⁴² companies must make public disclosures at the earliest time and to the highest standard of disclosure required by either ERISA or the securities laws.¹⁴³

Most of the reporting requirements under the federal securities laws impose quarterly and annual disclosure obligations. Even then, companies have wide latitude in not reporting material facts so long as the omissions do not cause the disclosures that are made to be misleading. So, for example, the securities laws typically would not require a company to report, mid-quarter, a significant decrease in sales or increase in costs. If, however, ERISA imposes an affirmative obligation on fiduciaries to report material information that investors in retirement-specific accounts would find important in making investment decisions, the fiduciaries would have to report the sales or costs information to the employee investors. Then the securities laws would require simultaneous reporting of the information to the public shareholders in order to avoid repercussions for the company and the employee investors under insider trading theories. The result is that implied reporting requirements under a pension law, which is interpreted by EBSA, would effectively require reporting of information by a company to all of its shareholders in numerous situations where the federal securities laws, as interpreted by the SEC, would not otherwise require reporting. EBSA is correct that the two legal requirements can co-exist, but this is an odd way to set public disclosure requirements.¹⁴⁴

The risks of choosing an investment strategy obviously derive from more than disclosure. As noted above, basic finance theory provides that employees who hold stock of their employer concentrate their risk by investing their human capital and financial capital in the same company. Empirical studies suggest that investing in company stock exposes employees to greater risks without commensurately compensating them for that risk.¹⁴⁵ Nor do employees as a general matter seem to benefit from any increased access to information about their company. Research indicates that no correlation exists between employees' elections to invest in company stock in their retirement-specific accounts and later performance of that stock.¹⁴⁶ Wider access to investment advice on such basic investing concepts might help retail investors increase diversification and lower their risks.

Regulation affects the availability of investment advice across the full range of an investor's accounts. In the US, investment advisors are subject to EBSA regulation for advice given regarding assets held in employer-sponsored retirement-specific accounts (ER\$) and to regulation by the SEC for advice provided regarding assets held in other retirement-specific and generalized investment accounts

¹⁴¹ See, e.g. *Bendaoud v. Hodgson*, 578 F. Supp. 2d 257, 278 (D. Mass. 2008).

¹⁴² Not all courts have agreed. One court granted summary judgment to the defendants, suggesting that if the employer would have disclosed otherwise non-public information about the company to employees holding employer stock in their 401(k) accounts then the employer would have violated securities laws. The court refused to interpret ERISA as requiring pension plan sponsors to violate the federal securities laws *In re McKesson HBOC Inc. ERISA Litigation*, No. C00-20030 RMW, 2002 US Dist. LEXIS 19473, at *24 (N.D. Cal. Sept. 30, 2002) (stating that "fiduciaries are not obligated to violate the securities laws in order to satisfy their fiduciary duties."); see also *Kirschbaum*, 2008 US App. LEXIS 9124, at *33-34 (referring to the potential of a securities law violation as a factor weighing against fiduciary liability).

¹⁴³ See, e.g., *Rankin v. Rots*, 278 F. Supp. 2d 853, 873 (E.D. Mich. 2003), *settled*, No. 02-CV-71045, 2006 US Dist. LEXIS 45706 (E.D. Mich. June 28, 2006); *In re WorldCom Litig.*, 263 F. Supp. 2d 745, 766-67 (S.D.N.Y. 2003); *Enron Corp. Sec., Derivative & ERISA Litig.*, 284 F. Supp. 2d 511, 563-67 (S.D. Tex. 2003).

¹⁴⁴ See *Mark Casciari & Ian Morrison, Should the Securities Exchange Act be the Sole Federal Remedy for an ERISA Fiduciary Misrepresentation of the Value of Public Employer Stock?*, 39 J. MARSHALL L. REV., 637 (2006) (arguing that the federal securities laws should provide the sole federal remedy for misrepresentation and omission claims associated with stock held in a 401(k)).

¹⁴⁵ See Lisa Meulbroek, *Company Stock in Pension Plans: How Costly Is It?*, 48 J.L. & ECON. 444 (2005).

¹⁴⁶ Richard H. Thaler & Cass R. Sunstein, *NUDGE: IMPROVING DECISIONS ABOUT HEALTH, WEALTH, AND HAPPINESS* 127 (2008).

(A\$, B\$, and IR\$). In some respects, the ERISA standards, being fiduciary-based, are the harsher of the two standards. As a result, it is a frequent practice for investment advisors to provide advice across the entire spectrum of an individual's financial planning needs with the sole exclusion of employer-sponsored retirement-specific investment accounts.¹⁴⁷ The outcome of the omission of retirement-specific assets is likely to be a lack of an integrated investment strategy.

The problem in the US remains, though perhaps to a lesser extent, even after statutory changes in 2006, which were intended to expand 401(k) participants' access to investment advice.¹⁴⁸ Rather than eliminate differences in the standards governing advice or allocate authority to a single regulator, the legislative changes authorized advice to 401(k) plan account holders if the advisors meet specific standards. Of particular importance under the legislation is the structure of advisory fees and disclosure of conflicts of interest.¹⁴⁹ The legislation improved access to investment advice but failed to address the underlying structural issue of regulatory fragmentation.

b. UK - Misselling

As discussed above,¹⁵⁰ the UK experimented as early as 1988 with giving individuals the right to opt out of certain government or employer-based retirement-specific accounts and instead to establish personal pensions. In some senses the choice of personal pensions gave individuals power over investments because they were able to choose any authorized financial services vendor to provide the personal pensions. The choice, also, though was one of participation. Individuals could choose what type of account, the government-sponsored scheme, the employer-sponsored scheme, or the personal pension, they preferred.

From the standpoint of demand, personal pensions were an immediate success. Financial services firms established commissioned sales programs and aggressively advertised their products. The marketing worked and individuals opened personal pensions at rates that far exceeded projections.¹⁵¹

When analyzed from the perspective of asset accumulation for retirement, however, an entirely different story on personal pensions emerges. Reports began to surface that sales of personal pensions were not complying with the relevant regulatory standards. In 1992 the Securities and Investments Board (SIB) reviewed a sample of the records associated with personal pension sales and found that only nine per cent substantially complied with regulatory rules.¹⁵² As a result of its concern, the SIB commissioned a study of industry practices. That study found “widespread regulatory compliance failure”¹⁵³

Ultimately regulators required financial services firms that had sold personal pensions and independent financial advisors who provided advice to purchasers to undertake a two-part review process intended to identify misselling that occurred between April 1988 and June 1994. The priority phase covered older purchasers who were at or near retirement. Phase two extended to younger purchasers, who typically were younger than 50. As of June 2002, FSA estimated that the pensions industry would pay out £11.8 billion (approximately \$20.1 billion at the current exchange ratio) after reviewing the records of 1.7 million customers.¹⁵⁴

¹⁴⁷ See, e.g. *id* at 12, 45 (finding that 73% of recent mutual fund investors obtained advice from professional advisors prior to investing but that the survey excluded investments made through employer-sponsored retirement plans).

¹⁴⁸ See *supra* text accompanying notes 42-45.

¹⁴⁹ In mid-2008, EBSA issued proposed regulations that would implement new standards for investment advice. Investment Advice--Participants and Beneficiaries, 73 Fed. Reg. 49895 (Aug. 22, 2008).

¹⁵⁰ See *supra* text accompanying note 69.

¹⁵¹ See *supra* text accompanying note 70.

¹⁵² Richard Nobles & Julia Black, *The Privatization Process: Pensions Mis-selling – The Lessons for Regulating Privatised Social Security*, 64 BROOKLYN LAW REVIEW 933, 939 (1998). The SIB was one of a number of entities later combined to form the FSA.

¹⁵³ Marina Milner & Keith Syrett, *Personal Pensions and the Financial Services Authority: New Chapter or Same Old Story?*, 51 N. Ir. Legal. Q. 141, 142 (2000).

¹⁵⁴ Financial Services Authority, *11.8 billion compensation for pensions and FSAVC reviews*, June 27, 2002.

Professors Black and Nobles chastise the regulators for failing, until the 1992 SIB audit, to focus their regulatory efforts on personal pensions as a product line. The regulators allegedly suffered from a lack of expertise with personal pensions, which constituted a new line of products. Instead of watching for patterns of problematic activity in personal pensions, the regulators established review processes that tended to focus on the behavior of particular financial services firms. According to Professors Black and Nobles, the regulators emphasized reviews of the activities of internal firm controls. As a result, the regulators missed the problems that existed across the financial services industry in the marketing and sale of personal pension accounts. Both the government inquiry and Nobles and Black concluded that the incentives for aggressive sales created by the commission salary structures for salespeople were at the heart of the industry-wide misselling.¹⁵⁵ During the misselling period, responsibility was divided among three regulators. The UK later transitioned to a single regulatory financial system with the FSA as regulator.¹⁵⁶

c. Australia – A “Bad” Investment

Australians received the right in 2005 to direct the investment of assets in their retirement-specific accounts.¹⁵⁷ To date, individual investment directions have not generated a great deal of reported controversy. One recent case, however, illustrates how the Australian system addresses an investor’s claim that his money was improperly invested. In the case, the investor, Mr. Wallace, alleged that the trustee of his account did not follow his verbal direction to convert the investments in his account from “high risk, high tech” shares to a more “secure portfolio.”¹⁵⁸ Between the time that the trustee allegedly should have implemented the direction in March 2000 and February 2001 Mr. Wallace’s account lost its entire value of over Australian \$380,000.¹⁵⁹

The claim was initially heard by the Australian Superannuation Complaints Tribunal (Tribunal), a specialized tribunal authorized to hear benefits-related disputes. In a decision later reversed on other grounds,¹⁶⁰ the Tribunal found in favor of Mr. Wallace. Its decision, though, was not based on the trustee’s failure to follow Mr. Wallace’s purported investment direction. Instead, the Tribunal considered whether the trustee breached its legal duty in adopting the initial investment strategy, which permitted a pensioner aged 70 to invest nearly his entire retirement-specific account in highly speculative stock. The Tribunal found that trustees have an obligation to ensure that the investment strategy is correctly formulated for the individual circumstances of the investor.¹⁶¹ In Mr. Wallace’s circumstances the original aggressive investment strategy was considered too aggressive. Although Australian case law is limited, the *Wallace* case indicates that Australia takes a significantly more paternalistic approach to the selection of investments for retirement-specific accounts than does the US.

¹⁵⁵ *Id.* at 947-951; Select Committee on Treasury, House of Commons, Ninth Report: The Mis-selling of Personal Pensions 3 (1998).

¹⁵⁶ Financial Services Authority, *About FSA: History*, March 21, 2005 available at <http://www.fsa.gov.uk/Pages/About/Who/History/index.shtml>.

¹⁵⁷ *Supra* text accompanying notes 82-83.

¹⁵⁸ *Perpetual Trustees Australia Ltd. V. Wallace* FCA 527, BC200702612 (2007).

¹⁵⁹ *Id.*

¹⁶⁰ The Tribunal’s jurisdiction is conferred by the Complaints Act, which the court interpreted as confining the Tribunal’s jurisdiction to the review of discretionary decisions. The real issue in the context of the appeal was whether the respondent’s claim was a claim against the Fund or a claim against the Trustee. If it was a claim against the Fund, then the discretion was involved and the exercise of that discretion by the Trustee was within the Tribunal’s jurisdiction of review. The court ruled in this case, however, that the claim was against the Trustee (not against the Fund) since there were no true assets left in the Fund by the time the claim was made in 2004. Thus, the Tribunal had no jurisdiction under the Complaints Act to address the complaint. *Perpetual Trustees Australia Limited*, FCA 527.

¹⁶¹ *Id.*

2. Account Fees

Along with the rates of contributions and return on investment, account and investment fees fundamentally impact the accumulation of assets in all types of investment accounts. In the world of traditional economic theory and perfect markets, one would expect rational investors and fiduciaries to consider fees as a factor in the selection of investment products and account services.¹⁶² Behavioral economics, however, has offered a number of possible explanations for how and why traditional economic theory breaks down in situations involving decision making and have focused particular efforts on retirement-specific accounts.¹⁶³

The UK anticipated the problem of inefficiently high account fees when it established stakeholder pensions. At the time they were first made available for investment in 2001 the UK capped stakeholder scheme charges at 1.0 per cent per year. Effective in 2005 the UK increased the cap to 1.5 per cent a year for the first 10 years of a customer account. Thereafter the account fee cap drops back to 1.0 per cent.¹⁶⁴

In the UK a recent study of fees charged by stakeholder plan default funds implies that the regulatory caps have had a significant impact on account fees. Expectations based on general fee data would lead to the expectation that the approximately fifty per cent of default funds which utilize a passive investment style would have lower fees than the default funds that consist of actively managed funds. The actual modal investment fee however is 1.0 per cent across both active and passive default funds. It appears from this data that, in practice, the fee cap has been established as a floor for stakeholder scheme fees. The mean charge of passive default funds is 20 basis points lower than the mean for active default funds, which is somewhat more in accordance with expectations. And a number of other factors may impact the fees charged, including the level of services provided by the scheme and the size of the employee population at a particular workplace.¹⁶⁵ But, the point remains that available data indicate that regulation has had an impact on account fees.

Fees also have been of great interest in Australia. In 2002, Professor Ian Ramsay prepared a report for ASIC evaluating fee reporting in the product disclosure statements provided to individuals to make investment decisions and in periodic reporting of account returns to investors.¹⁶⁶ Professor Ramsay recommended increasing the standardization of fee discussions and definitions, including specific recommendations for various types of fees.¹⁶⁷ Subsequently, ASIC published model fee disclosures for product disclosure statements, regulatory changes required increased and standardized fee reporting,¹⁶⁸ and ASIC's website now hosts a tool that enables investors to compare fees and other factors about

¹⁶² See John A. Turner, *A Behavioral Economics Perspective on 401(k) Fee Disclosure*, 2008 Newsletter of ABA Employee Benefits Committee, available at <http://www.abanet.org/labor/ebcomm/newsletter/08/spring/ebc-spring-08.shtml>. Evidence does indicate that mutual fund investors tend to invest in stock mutual funds with lower than average expense ratios. 2008 Investment Company Fact Book, 60-61, available at http://www.ici.org/stats/res/2008_factbook.pdf.

¹⁶³ See, e.g., Richard H. Thaler & Cass R. Sunstein, NUDGE: IMPROVING DECISIONS ABOUT HEALTH, WEALTH, AND HAPPINESS 123-27 (2008); Shlomo Benartzi & Richard H. Thaler, *Naïve Diversification Strategies in Defined Contribution Savings Plans*, AM. ECON. REV. 79 (Mar. 2001); Shlomo Benartzi & Richard H. Thaler, *Risk Aversion or Myopia? Choices in Repeated Gambles and Retirement Investments*, 45 MGMT. SCI. 364 (1999).

¹⁶⁴ Alistair Byrne, et. al, *Default Funds in UK Defined-Contribution Plans*, 63 FIN. ANAL. J. 40, 48 (2007).

¹⁶⁵ *Id.*

¹⁶⁶ Ian Ramsay, *Disclosure of Fees and Charges in Managed Investments: Review of Current Australian Requirements and Options for Reform*, Report for ASIC (2002), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=931576.

¹⁶⁷ *Id.* at 7-16.

¹⁶⁸ See

<http://www.fido.asic.gov.au/fido/fido.nsf/byheadline/Superannuation+fund+comparison+worksheet?openDocument>

¹⁶⁸ See Nigel Finch, *Issues Relating to Fee Disclosure in Australian Investment and Superannuation Funds*, 20-21 (2005, updated 2008) (noting that 29 funds reported fees after the model was issued that they had not previously reported), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=862946

competing superannuation funds.¹⁶⁹ Research indicates that the changes have increased the transparency of fee reporting.¹⁷⁰ The increased requirements, however, have been criticized on the basis that they are too detailed and technical for typical investors,¹⁷¹ and the sheer number of funds in the Australian market arguably contributes to the difficulties of market participants in monitoring fees.¹⁷²

To date the US has failed to adopt legislation directly addressing 401(k) account fees. This author was a member of the 2004 EBSA Advisory Council working group that studied the disclosure of account fees in 401(k) accounts. The working group published a report, which included both factual findings regarding failings in current fee disclosures and recommendations intended to enhance fee disclosure. The issue was widely recognized as a concern. After evaluating a variety of problems with current methods of disclosing, or failing to disclose, fees in 401(k) plans, one commentator observed that “[t]he disclosure of fees paid by 401(k) participants currently is closer to what behavioral economics would prescribe for hiding information than it is to clear, informative disclosure.”¹⁷³ A separate reporting requirement applies to IRAs under IRS regulations, which set forth very general fee reporting requirements.¹⁷⁴

In 2006 plan sponsors were forced to pay attention to the fees question after a number of lawsuits were filed alleging that 401(k) plan fee structures violate ERISA’s general fiduciary requirements. Some of the suits claim that plan fiduciaries violated their ERISA obligations by failing to understand or capture for the plan fees paid by one plan service provider (such as a mutual fund) to another service provider (such as a record keeper).¹⁷⁵ Suits also have presented claims that plan fiduciaries failed to appropriately consider the fees charged by plan investment alternatives and, thus, did not make prudent selections of available investment options.¹⁷⁶

3. Default Investments

There are a variety of routes through which individuals with employer-sponsored retirement-specific accounts may have their account assets allocated to a default investment. Default investments raise both of the issues just analyzed – selection of the investment vehicle and the amount of plan fees. If an employee’s assets are invested into a default investment vehicle, someone had to choose what that vehicle would be. And the fees associated with that vehicle will affect the employee’s investment returns.

In the US, the terms of a 401(k) plan may include automatic enrollment. If an employer adopts automatic enrollment, new employees are enrolled automatically in the 401(k) plan unless they affirmatively opt out of the plan. Research and experience indicates that such automatic enrollment features help overcome employee inertia and thereby increase the take-up rate for 401(k) plans.¹⁷⁷ Plans with automatic enrollment, though, need to determine a default investment for the contributions of those employees who are enrolled under the automatic feature. Similarly where an employee enrolls in a

¹⁶⁹ See

<http://www.fido.asic.gov.au/fido/fido.nsf/byheadline/Superannuation+fund+comparison+worksheet?openDocument>

¹⁷⁰ See Finch, *supra* note 168, at 20 (noting that 29 funds reported fees after the model was issued that they had not previously reported).

¹⁷¹ *Id.* at 21.

¹⁷² See Nigel Finch, *The Trouble with MER: The Disclosure of Fees and Charges in Australian Superannuation and Investment Funds*, 4 J LAW & FINCL. MGMT. 32, 33 (2005) (stating that a 2005 report found 1.5 times as many investment funds in Australia as there were companies listed on the Australian Stock Exchange).

¹⁷³ Turner, *supra* note 162.

¹⁷⁴ See Treas. Reg. 1.408-6 (requiring reporting of sales fees and charges against IRA accounts).

¹⁷⁵ See, e.g., Spano v. The Boeing Co., 2007 US Dist. LEXIS 28774, at *2-3 (S.D. Ill. Apr. 17, 2007).

¹⁷⁶ See, e.g., Hecker v. Deere & Co., Nos. 07-3605 & 08-1224, 2009 U.S. App. LEXIS 2950 (7th Cir. Feb. 12, 2009).

¹⁷⁷ See Matthew Venhorst, *Helping Individual Investors Do What They Know is Right The Save More for Retirement Act of 2005*, 13 CONN. INS. L.J. 113 (2006) (discussing the proposed “SMART” plan).

401(k) plan or transfers funds from another plan but does not select among available investment options, the plan must default contributions to an investment vehicle.

Although issues associated with default investments had been observable in 401(k) plans since those plans became popular, EBSA did not issue guidance on default fund selection until October 2007. Prior to that guidance, survey data showed that forty-five per cent of US 401(k) plans provided for a stable-value fund or money-market fund as the default.¹⁷⁸ The goal of selecting stable-value or money-market funds as default funds tends to be the preservation of capital as opposed to investment growth. Prior to the 2008 market downturn, such conservative default investments were heavily criticized particularly for younger investors.¹⁷⁹ The 2007 guidance, in the form of regulations issued by EBSA, established a safe harbor protecting an employer from liability if the employer selects a default fund that possesses the characteristics of what EBSA terms a Qualified Default Investment Alternative (QDIA). An employer may, however, at its own risk designate a fund that is not a QDIA as a default fund. With the exception of investments that pre-date the regulation and investments during the first 120 days of an employee's participation in a 401(k) plan, a QDIA must consist of a mix of investments that take into account either the characteristics of the individual account holder or of a group of employees.

An example of the use of default investments in the UK occurs in employer-selected stakeholder schemes. In order to meet the minimum requirements of a stakeholder scheme, the employer must designate a default investment vehicle.¹⁸⁰ In the UK, a recent study of the stakeholder pension plan schemes registered as of December 2006 found that the default funds offered in those schemes are less uniform than one might expect. The study reviewed default funds selected by financial services firms that developed stakeholder pension products. When an employer chooses a particular stakeholder scheme, that employer has the option of designating a default fund that is different from the default fund selected by the financial services firm. The data indicate, however, that most employers accept the default option suggested by the financial firm that packaged the stakeholder pension product.¹⁸¹

Among the registered stakeholder pension products, the default funds were almost evenly split between actively and passively managed funds. A few default funds were styled as UK equity funds but the majority were evenly divided between global equity funds and balanced funds. It is difficult to rationalize these significant differences in the types of funds chosen by financial services firms as default funds. A firm that markets a given stakeholder scheme typically markets that scheme to a wide variety of employers with various employee demographics. Perhaps the financial services firms do not agree on the appropriate type of default fund for the average individual who opens a stakeholder pension account. Or the firms may not be in agreement over the typical earnings, other investment holdings, risk tolerances and other characteristics of the average individual account holder.¹⁸² In the absence of specific rationales for the difference in the types of default funds chosen, however, some of those selections must be less than optimal.

In addition to its requirement that stakeholder schemes establish a default fund, in 2005 the UK began to require that every stakeholder default fund utilize a life-cycle profile. By ensuring that years remaining to retirement age is a consideration in the structure of a default portfolio, the requirement addresses some of the concern over the variance in default funds. Implementation of the life-cycle requirement is not totally uniform across stakeholder schemes but the vast majority of the schemes begin increasing the per centage of bonds and cash held in a portfolio between 5 and 10 years prior to retirement.¹⁸³

In recent years, Australia has increasingly increased choice in superannuation accounts including choice of fund and choice of investments within a particular fund.¹⁸⁴ Research indicates though that most

¹⁷⁸ Watson Wyatt, *Watson Wyatt's Survey on Default Investments and the DOL's Proposed Regulations*, INSIDER, table 5 (2006).

¹⁷⁹ *Id.*

¹⁸⁰ Belinda Benney, *Legal Issues for Defined Contribution Schemes When Selecting Investments*, 10 PENSIONS 50, 52 (2004).

¹⁸¹ Byrne, *supra* note 164, at 42.

¹⁸² *Id.* at 42-43.

¹⁸³ *Id.* at 42-45.

¹⁸⁴ Bateman, *supra* note 74, at 4.

Australians leave their superannuation assets in the default fund.¹⁸⁵ Another study indicates that Australian's loss aversion with respect to their superannuation accounts is likely to discourage investors from choosing other than the default investment.¹⁸⁶

V. Regulatory Reform – Strategies for Addressing Risk in Retirement-Specific Accounts

The *Blueprint* approach to reform of the regulation that governs the US financial services sector concentrates on reorganizing responsibilities among existing and newly created federal agencies.¹⁸⁷ Much of the focus, as it should be, is on the operation of the financial markets.¹⁸⁸ Other ideas, at least in the *Blueprint*, are to decrease the jurisdiction of the SEC and create a new regulator of business conduct. Similarly, the *Blueprint* calls for creation of a prudential regulator and for federalization of some insurance regulation that is now the province of state regulators.¹⁸⁹ In assigning responsibilities and in eventually developing the substantive regulation to be overseen by the SEC, the new business conduct regulator, and new prudential financial regulator, policymakers must determine the role these regulators will have with respect to retirement-specific accounts, particularly those accounts that are part of employer-sponsored plans. Effective regulation also will need to recognize the risks associated with retirement-specific accounts and the relationship of those risks with generalized investment accounts.

The *Blueprint* identifies regulation of the relationship between financial institutions and financial services customers as the province of the new business conduct regulator. That regulation would have two functions in governing the relationship between institutions and customers. Its first role would be to regulate disclosure practices. Second, it would regulate the institutions' conduct of business practices.¹⁹⁰

In thinking about why – or if -- financial products and the entities that develop, market, sell, and trade those products should be regulated at all, some economists have suggested two roles for regulation. One role is to circumscribe the conduct of business to ensure fairness and appropriate disclosure.¹⁹¹ The second role is to ensure the financial system and the financial actors are fiscally sound.¹⁹² Professor Hazel Bateman takes a slightly different perspective in explaining the need for regulation in the area of financial services. She focuses on three causes of market failures in the financial services area, all of which apply in the context of retirement-specific accounts. Those causes are information asymmetry, externalities, and market power. In the Australian context, the mandatory nature of participation in the superannuation accounts comprises another factor supporting the need for regulation.¹⁹³ This Part considers the issues associated with disclosure and business practices before discussing two competing principles that should be considered in any reform of the regulation of US investment-specific accounts.

A. Disclosure

Whether assets are held in retirement-specific accounts or in generalized investment accounts, disclosure occurs at two levels. Both levels can be seen as addressing information asymmetries, which

¹⁸⁵ See *id.* at 5.

¹⁸⁶ See Tim Frey et. al., *Will Investors Change Their Superannuation Fund Given the Choice?*, 47 ACCTG. & FIN. 267 (2007).

¹⁸⁷ BLUEPRINT, *supra* note 5, at 137-38.

¹⁸⁸ *Id.* at 137.

¹⁸⁹ BLUEPRINT, *supra* note 5, at 4.

¹⁹⁰ *Id.* at 170. The business conduct regulator would have a third function as well, chartering and licensing providers of financial products and services. *Id.*

¹⁹¹ Jim Stewart, *Financial Regulation in Ireland: Should the Regulator be the Central Bank?*, 9 J. FIN. REG. & COMPL. 42, 44-45 (2001). But see Roberta Romano, *Empowering Investors: A Market Approach to Securities Regulation*, 107 YALE L.J. 2359 (1998) (suggesting that securities issues be allowed to choose their regulatory regime, including the level of required disclosure).

¹⁹² Stewart, *supra* note 191, at 44-45.

¹⁹³ Bateman, *supra* note 74, at 120-21.

are pervasive in capital markets.¹⁹⁴ One level of disclosure applies to the investment product – for example, a specific mutual fund, the stock of a particular company, or a certificate of deposit – that the investor purchases. All retail investors, regardless of the type of account in which they hold assets, arguably require access to basic information about investment products, including the risk profiles, fees, and returns associated with those investments.¹⁹⁵ Second, the investors arguably require access to information that would enable them to understand the terms of the accounts that will hold the investments. For generalized investment accounts that may be a brokerage account (A\$) or a bank account (B\$). For retirement-specific accounts, terms of 401(k) plans are set by an employer (for ER\$) or a financial services firm will have set terms of a product unrelated to employment such as an IRA (for IR\$).

1. Disclosure Regarding Investment Products

Responsibility for implementing disclosure requirements for investment products in the US has been fragmented both within the realm of generalized investment accounts, a fragmentation the *Blueprint* recognizes,¹⁹⁶ and between those accounts and retirement-specific accounts as well as between employer-sponsored retirement-specific accounts (such as 401ks) and individually-established retirement-specific accounts (such as IRAs), fragmentations the *Blueprint* does not explicitly recognize. The *Blueprint* is specific in establishing a goal to consolidate responsibility for disclosure requirements for generalized investment accounts. However, it is not clear whether it intends that consolidation to include responsibility for the disclosure requirements over retirement-specific accounts. Such a consolidation would represent a significant departure over the current approach.

Mutual funds provide the best example of the current divergence in regulatory responsibility and substance. As noted above, in 2007 twenty-four percent of mutual fund investments were held in a DC retirement-specific account.¹⁹⁷ The SEC has primary responsibility for the regulation of mutual funds, with its powers over mutual funds derived from the Investment Company Act.¹⁹⁸ In 1998 the SEC adopted a simplified form of disclosure for use by mutual funds, the profile prospectus or fund profile, which the SEC hoped would make basic information about specific mutual funds more accessible to investors.¹⁹⁹ That simplified disclosure was available to mutual funds purchased through generalized investment accounts. In addition, the SEC announced when it permitted the simplified disclosure that it expected information in that format to be particularly useful to individuals saving in retirement-specific accounts.²⁰⁰ The result, however, has been characterized as “an abysmal failure . . . in the retirement plan market.”²⁰¹ That lack of success probably occurred, at least in part, because EBSA never explicitly approved the profile prospectus for use in the most popular types of employer-sponsored retirement-specific accounts, those where employers delegate investment choice and responsibility to their employees.²⁰²

¹⁹⁴ *See id.*

¹⁹⁵ There has been considerable scholarly debate about the value of disclosure to retail investors. *See, e.g.* Stephen J. Choi & A.C. Pritchard, *Behavioral Economics and the SEC*, 56 STAN. L. REV. 1 (2003) (suggesting that the inefficient behaviors identified by behavioral economics decrease the value of information); Jill E. Fisch & Hillary A. Sale, *The Securities Analyst as Agent: Rethinking the Regulation of Analysts*, 88 IOWA L. REV. 1035 (2003) (identifying conflicts of interest that inhibit the independence of securities analysts); Romano, *supra* note 191 (arguing that investors could choose an efficient amount of disclosure if markets allowed ‘competition’ on that basis); Cynthia A. Williams, *The Securities and Exchange Commission and Corporate Social Transparency*, 112 HARV. L. REV. 1197, 1311 n.3 (1998) (recognizing that while mandatory disclosure has a long history in US securities regulation, “aspects of it are still controversial”).

¹⁹⁶ BLUEPRINT, *supra* note 5, at 170 (“Currently, various federal, state, and SROs supervising banking, insurance, futures, and securities activities have responsibility for promulgating and implementing consumer disclosure regulations and standards.”).

¹⁹⁷ *Supra* text accompanying note 40.

¹⁹⁸ Investment Company Act of 1940, [17 C.F.R. § 270.2a-7 \(2001\)](#).

¹⁹⁹ [63 Fed. Reg. 13,968 \(1998\)](#) (to be codified at 17 C.F.R. pts. 230 & 270).

²⁰⁰ *Mutual Fund Regulation in the Next Millennium Symposium Panels: II. Disclosure*, 44 N.Y.L. SCH. L. REV. 463, 470 (2001).

²⁰¹ *Id.*

²⁰² *Id.* at 470-71.

In November 2007 the SEC began another effort to simplify mutual fund disclosures, again with the hope of making disclosures more useful to investors. This time the SEC decided in favor of implementing what it refers to as short-form prospectuses. This shorter, more focused, version of the full prospectus would meet the securities law requirement that a prospectus be delivered prior to or contemporaneous with a mutual fund investment.²⁰³ The SEC made clear, by permitting specific legending that would refer to DC retirement-specific accounts,²⁰⁴ that it hoped the short-form prospectuses would be used to inform investors who considered buying mutual funds in those accounts. That action put the ball in EBSA's court to approve, ignore, or modify the use of short form prospectuses in DC retirement-specific accounts.

In July 2008, EBSA responded when it issued proposed regulations, which address a variety of disclosure issues that had been simmering for some time. Those proposed regulations eliminate the former requirement that investors who purchase mutual funds through retirement-specific accounts receive a prospectus prior to making the investment, a requirement that was widely ignored.²⁰⁵ However, rather than requiring delivery of the short-form prospectus developed by the SEC as is necessary for generalized investment accounts, the proposed regulations would require a prospectus to be supplied only when a retirement-specific account investor requests one.²⁰⁶ As part of this prospectus-on-request requirement, the EBSA-proposed regulation states that a prospectus "(or any short form or summary prospectus, the form of which has been approved by the [SEC])"²⁰⁷ must be provided. This implies that that a short-form prospectus would only need to be provided to an investor who specifically requests the short-form.

It appears, then, that the SEC and EBSA disagree about the value of a simplified mutual fund disclosure document. The SEC requires disclosure for all mutual fund sales. EBSA requires disclosure only if the investor requests a prospectus. As a result, if the individual from our earlier example, Saver, purchases mutual funds through a standard brokerage account or directly from a mutual fund, SEC guidance requires that Saver receive a short-form prospectus. If Saver buys the same mutual fund through a retirement-specific account, Saver will not automatically receive a prospectus. Rather, Saver has the right to request a prospectus or short-form prospectus, assuming, of course, that Saver knows to make the request and understands the difference between a full prospectus and a short-form prospectus.

From a coordination standpoint, the proposed EBSA regulations are an improvement over past practice in that the proposed regulations explicitly accept forms of prospectus that are approved by the SEC. It has, however, taken 10 years from the implementation of the SEC's fund profile to get to the point where EBSA formally accepts through regulation an SEC summary form of prospectus.²⁰⁸ And, differences in delivery requirements remain. Perhaps these differences in prospectus delivery requirements between retirement-specific and generalized investment accounts serve an important policy function. However, what that policy might be is not clear on the face of the regulations or in statements by the regulators. Nor, does the difference in requirements between the two types of accounts appear to be the product of coordination and agreement between the SEC and EBSA.

The difference in prospectus delivery requirements is only one recent example of the differences between disclosure requirements in investor accounts regulated by EBSA as compared to those regulated by the SEC. EBSA requires that information about investment options be presented in a particular,

²⁰³ Enhanced Disclosure and New Prospectus Delivery Option for Registered Open-End Management Investment Companies, 72 Fed. Reg. 67790, 67815 (proposed Nov. 30, 2007) (to be codified at 17 CFR pts. 230, 232, 239, and 274).

²⁰⁴ 72 Fed. Reg. at 67815.

²⁰⁵ Pete Swisher, *Death to the Prospectus Requirement! The New 401(k) Participant Disclosure Rules*, 8 (2008), available at http://www.401khelpcenter.com/pdf/Death_to_the_Prospectus_Requirement.pdf.

²⁰⁶ Fiduciary Regulation for Disclosure in Participant-Directed Individual Account Plans, 73 Fed. Reg. 43014, 43040 (proposed July 23, 2008) (to be codified at 29 C.F.R. pt. 2550.404a-5(d)(4)(i)).

²⁰⁷ *Id.*

²⁰⁸ EBSA had technically permitted the use of the most recent profile prospectus, however, the consensus of lawyers was to advise plan fiduciaries not to rely on dissemination of profile prospectuses. See *Fiduciary Guidance Counsel* (Mar. 2008) ("Even if a retirement plan's fiduciary is completely confident that the profile prospectus is the "most recent prospectus", a cautious person shouldn't rely on this strained interpretation.").

tabular format.²⁰⁹ As explained above, the amount and disclosure of investment account fees has troubled policy makers in the UK and Australia as well as the US. In 2008 EBSA issued proposed regulations detailing new account fee disclosure requirements in retirement-specific accounts.²¹⁰ At the same time, but not necessarily in tandem, the SEC has been working on regulation of account fee disclosure in generalized investment accounts.²¹¹ The IRS has not revised its regulation of IRA reporting for fee disclosures.²¹² Similarly, disclosures of conflicts of interest by investment advisors and other advisor regulation differ depending on whether the account under advisement is an employer-sponsored retirement-specific account or a generalized investment account.²¹³

These examples of tensions between the disclosure requirements imposed by securities law on the marketing and sale of investments on the one hand and the disclosures imposed by ERISA are not intended to be all inclusive.²¹⁴ Instead, the point is that the fragmentation of responsibility for setting disclosure standards has led to inconsistencies and likely to inefficiencies. If the restructuring of financial services regulation results in the formation of a new business conduct regulator then careful attention should be given to the way authority for disclosure and other regulation related to the sale and purchase of investment products is divided or coordinated between that regulator and EBSA.

2. Disclosure Regarding Investment Assets

Differences in regulators and in substantive regulation also occur at the level of disclosure of the account terms (as compared to disclosure of the terms of the investment product). Although regulatory responsibility for setting the terms of employer-sponsored retirement-specific accounts – terms that are found in the benefit plan established by employers – is divided between the IRS and EBSA, EBSA has authority over the disclosure of those plan terms. Those disclosures have not tended to be particularly problematic either from the standpoint of their substantive content or in regulatory overlap. Substantively, the employee investors must receive information on the terms governing the accounts, such as how much they can save in these plans, whether the employer makes any contributions, whether account holders have access to the funds prior to retirement or other separation, and process-related concerns such as how account holders change investments or elect to receive their funds when the plan distributes their account assets. Certainly, errors and even malfeasance may occur in making these disclosures,²¹⁵ but there are no indications of widespread systemic problems. An exception has been the recent attention, and litigation, over disclosure of account-level fees. EBSA has addressed that fee reporting in the proposed regulations on fee disclosure, which are discussed above.²¹⁶

In the realm of generalized investment accounts, regulatory responsibility for oversight of disclosure of the account terms is splintered as it is with respect to products disclosure.²¹⁷ It appears that the *Blueprint* would also consolidate regulatory authority over this level of disclosure under the authority of the new business conduct regulator.²¹⁸ The *Blueprint* defines one of the key roles of the business conduct regulator as being the development of “adequate disclosures for all types of financial products

²⁰⁹ See Fiduciary Regulation for Disclosure in Participant-Directed Individual Account Plans, 73 Fed. Reg. 43014, 43040 (proposed July 23, 2008) (to be codified at 29 C.F.R. pt. 2550.404a-5(d)(4)(i)).

²¹⁰ 73 Fed. Reg. 43014.

²¹¹ 72 Fed. Reg. 67790.

²¹² See Treas. Reg. 1.408-6 (requiring reporting of sales fees and charges against IRA accounts).

²¹³ See *supra* text accompanying note 147.

²¹⁴ For example see *supra* text accompany notes 137-39 for discussion of overlapping claims regarding employer stock.

²¹⁵ See, e.g. [Pell v. E. I. DuPont De Nemours & Co.](#), 539 F.3d 292; (3rd Cir. 2008) (finding miscalculations of benefits entitlement); [Burstein v. Ret. Account Plan for Emples. of Allegheny Health Educ. & Research Found.](#), 334 F.3d 365 (3rd Cir. 2003) (reinstating claim for benefits based on inconsistent disclosures).

²¹⁶ See *supra* text accompanying notes 205-07.

²¹⁷ See Swisher, *supra* note 205, at 2.

²¹⁸ See BLUEPRINT, *supra* note 5, at 170.

and services.”²¹⁹ It specifically recognizes the wide dispersion of existing authority over disclosures and indicates that consolidation of the regulatory oversight could increase the uniformity in disclosure approaches.²²⁰ This would have the benefit of rationalizing those disclosures so that investors can compare types of accounts as well as types of investment products.

B. “Business Practices” and Retirement-specific Accounts

In addition to authority over disclosure standards, the *Blueprint* would grant the business conduct regulator oversight responsibility for the substantive conduct of business practices. This responsibility would include regulation of the sales and marketing of financial products. Presumably, this authority also would extend to account maintenance and administration. Currently, as is true of the regulation of disclosure, that authority is splintered among a variety of regulators depending on the particular financial product in question. The stated goal of consolidation of regulatory authority over the business practices of financial institutions is, as with other areas of consolidation, “greater consistency.”²²¹

EBSA currently has regulatory responsibility over all fiduciary activities connected with retirement-specific accounts and ERISA’s definition of fiduciary is unusually broad. Still, competitive sales and marketing of investment products directly to investors in employer-sponsored retirement-specific accounts has not been extensive in the US. Certainly, the US has not experienced widespread problems of the type that occurred in the UK in the misselling scandal. Instead, sales and marketing of investment products has typically focused on the employers that sponsor DC plans because those employers choose the investment options that are made available to the individual employees. Employers typically select a limited menu of mutual funds from one or a small number of fund families. Thus, the marketing competition among financial services firms occurs in the environment of the employer’s decision making. In recently proposed regulations, EBSA made clear that it believes that employers’ selection and ongoing monitoring of investment products constitutes a fiduciary function and is within EBSA’s oversight responsibility.²²² Employers have argued that their role in selecting an investment menu is part of their plan adoption role and, thus, not a fiduciary function. This controversy has yet to be resolved.²²³

Another subset of business practice concerns, however, occurs in the administration of retirement-specific accounts. The potential for problems varies depending on an assortment of factors such as the type of entities responsible for processing transactions and the type of investment. It appears that the business practices regulator would receive authority over all of these activities for generalized investment accounts. Currently, EBSA has regulatory responsibility and ERISA governs these activities in retirement-specific accounts. Here again, the fragmented regulatory approach produces outcomes dependent on whether investments are made in retirement-specific accounts or in generalized investment accounts.

Consider, for example, a situation where our hypothetical investor, Saver, directs the proper entity to liquidate one investment product and move the assets into another product. Assume the entity negligently or intentionally fails to follow Saver’s direction, creating a loss of \$150,000 to Saver.²²⁴ If this were to occur in a standard brokerage account, currently Saver would pursue a claim through the

²¹⁹ *Id.* at 170. Regulation of the disclosure obligations of companies about the companies themselves, as compared to about financial products offered by the companies, would be the province of the corporate finance regulator. This authority would include the oversight currently done by the SEC over corporate disclosure, corporate governance and auditing. Publicly held financial services firms would be subject to the same disclosure, governance, and auditing requirements as other publicly held companies. *Id.* at 145.

²²⁰ *Id.*

²²¹ *Id.* at 170; see also Swisher, *supra* note 205, at 2.

²²² 73 Fed. Reg. 43014.

²²³ See *Hecker v. Deere & Co.*, Nos. 07-3605 & 08-1224, 2009 U.S. App. LEXIS 2950, at *29 (Feb. 12, 2009) (noting that Deere may not be a fiduciary regarding the selection of the investments offered in its plan).

²²⁴ The facts are loosely drawn from *LaRue v. DeWolff, Boberg & Assoc.*, 128 S. Ct. 1020 (2008).

securities industry self-regulatory organization, FINRA, which sponsors mediation and arbitration programs to address such disputes. The SEC has oversight over FINRA and could pursue widespread problems using its own authority. It appears that self-regulatory organizations such as FINRA would continue to play a role in a reformed financial services regulatory framework and would be overseen by the business practices regulator. In comparison, the investor's ERISA claim is a complicated one. Until 2008 there was a question of whether an investor had any rights to bring a fiduciary breach claim for such losses to the retirement-specific account. The Supreme Court resolved that question in the affirmative.²²⁵ The fiduciary standards and remedies, however, remain governed by ERISA and are under the regulatory jurisdiction of EBSA.²²⁶ As a result, the investor's recovery to the plan account may be limited and there may be no other remedial options.²²⁷

C. Principles for Rationalizing Regulation of Retirement-Specific Accounts

The movement to DC retirement-specific accounts and the resulting tensions in the regulation of those accounts as compared to generalized investment accounts means that decisions on allocation of regulatory authority and substantive regulation over retirement-specific accounts must be made as part of any broad reform of the US system of oversight of the financial services sector. To ignore that sector of the investment universe would be to fail to acknowledge the importance of those assets in the broader system of investment and financial services and to leave their regulation in the ERISA framework, which was devised in a very different financial and plan era and results in regulatory overlap. However, to sweep the regulation of retirement-specific accounts wholly into a reformed financial services regulatory system as though those accounts are for all purposes the equivalent of other intermediated retail investments would be to ignore the specialized dimensions of those accounts. As it moves forward, two basic principles can help guide reform in a way that supports the accumulation of retirement wealth. Inherent tension exists, however, between those basic principles, which will require reformers to balance two competing values.

1. Coordination

Coordination is one guidepost that encompasses principles important to efficient and effective regulatory oversight. For example, coordination of the reporting and disclosure regulations that push investment performance information to retail investors, whether those investors hold assets in retirement-specific accounts or in generalized-investment accounts, enhances efficiency for both financial services firms and investors. Coordinated requirements allow firms to minimize costs associated with either complying directly with multiple disclosure regimes or trying to ensure that a single set of disclosures meets the minimum standards of each applicable set of requirements. For investors, coordination minimizes confusion that may result from receiving significantly different communications for different categories of investment accounts. Other areas where coordination should reduce inefficiencies include communications regarding purchases, fees, marketing, and methods of resolution for some claims.

Coordination can minimize the costs of multiple agencies devoting resources to identical issues. It also can reduce the number of touch points that a financial services firm has with regulators. Development of regulatory expertise is also supported by consolidation of regulatory function. For example, a regulator can leverage its experience in dealing with risk mitigation across similar products and types of investors. Consider the risks associated with failing to credit an account for an investment. Those risks are substantially similar in an investment account regardless of whether it is a DC retirement-

²²⁵ *Id.*

²²⁶ *See id.*

²²⁷ *See* Colleen E. Medill, *Resolving the Judicial Paradox of "Equitable" Relief Under ERISA Section 502(A)(3)*, 39 J. Marshall L. Rev. 827, 849-52 (2006).

specific account or a generalized investment account. In an employer-sponsored account, the employer must ensure that its contributions and any employee contributions are properly forwarded to the appropriate plan agent. The result is that there is some additional risk at that level in employer-sponsored plans. But, otherwise, the accounts share similar characteristics. There is no reason to believe that mechanisms intended to ensure recognition of investment deposits or execution of investment instructions are substantially different in the context of retirement-specific accounts than they are with respect to other investment products.

Coordination of investment advice may provide similar benefits. A single regulator provides one touch point or, if regulation continues to be split between federal and state securities regulators, at one type of touch point. For investors, this may enable more wholistic advice as investment advice may be more likely to be provided across all of an investor's assets rather than isolating employer-related retirement specific account holdings.

Coordination should minimize the opportunity for financial services firms to inappropriately exploit regulatory differences between types of accounts. For example, if fees are capped or required to be disclosed in different ways in one set of accounts, that may permit an opportunistic financial services firm to inappropriately exploit the differences by offering different financial products in those accounts as compared to other accounts. In some instances, different product terms may be appropriate because of account sizes, numbers, and other efficiencies. A regulator that has authority over the products regardless of the wrapper holding the products may be best placed to ensure informed regulatory distinctions.

Another perspective on coordination, though, is to look at coordination across the employer and employee relationship. Here, the touch points that may matter are the touch points of an employer when dealing with workplace regulators, or the touch points that an employee faces when trying to resolve work-related compensation disputes. The consequences for employers and employees may increase the value of coordination across the workplace regulators.

It is even less clear at the level of account disclosure than it is at the level of investment product disclosure whether EBSA's current role should be assigned to or coordinated with a business conduct regulator as part of the redistribution of responsibility for financial services regulation.

2. Specialization

As important as coordination is, the value gained through coordination may not outweigh the alternative of specialized, more focused regulation. A counter force to the values associated with coordination can be found within the underlying policies reflected in tax incentives, which are intended to increase the number of Americans who save for their retirement and how much they save. In the past, for example, the goal of increasing long term savings has resulted in restrictions on the early withdrawal of retirement-specific account assets. On the other hand, the policy that the tax incentive is intended to benefit the saver's retirement, not the saver's estate, has led to minimum distribution requirements to reduce the use of those accounts as estate accumulation devices. These retirement-specific account requirements tend to operate at the plan level rather than at the investment level. As such, they are part of the set of rules that wraps around retirement-specific accounts and governs the eligibility of those accounts for tax-favored treatment.

Some commentators have argued that the tax support and policy goals inherent in retirement accounts mean it is appropriate for those accounts to be treated more paternalistically from a regulatory perspective than non retirement-specific accounts are treated.²²⁸ Similarly, as discussed above, Professors Nobles and Black argue that one factor in the misselling scandal in the UK was the failure of the relevant regulators, all of which had responsibility for aspects of investments and financial services firms, to focus on the unique issues associated with personal pensions.²²⁹ The gist of this concern is that regulators

²²⁸ See Dana M. Muir, *The US Culture of Employee Ownership and 401(k) Plans*, 14 ELDER L.J. 1, 17 (2006).

²²⁹ Nobles & Black, *supra* note 152, at 948-49.

without particular expertise in the nuances of retirement-specific accounts will miss risks that are specific to those accounts and to the goal of building wealth for retirement.

On a related front, research by behavioral economists shows that establishing retirement-specific accounts in which employees participate by default are effective in increasing savings in those accounts. For example, automatically enrolling new employees in these accounts, automatically deducting contributions to the accounts from their wages, and investing the assets in particular financial products all can positively affect the accumulation of retirement assets.²³⁰ In 2006 Congress amended ERISA to remove barriers to the use of these types of default provisions and to encourage their implementation.²³¹ Automatic participation and investment account terms do not have a clear parallel in generalized investment accounts. In addition, whether employer-sponsored retirement-specific accounts incorporate the use of those mechanisms is a decision made by employers. Thus, there may be little coordination in this area to be gained by consolidating the regulation under a consumer protection regulator and specialization gains to be had by continuing to assign the regulatory authority to EBSA

More generally, the US system of retirement wealth accumulation is so fragile that it is important that regulatory reform, as it is put in that well-worn phrase, do no harm. The policy ramifications, which are unique to retirement-specific accounts, and relational considerations, may point to EBSA as the regulator of choice, particularly at the level of plan terms. Through their regulation of benefit plans, EBSA and the IRS share responsibility for setting the terms of retirement-specific accounts. Arguably, given EBSA's expertise in allowable plan terms it would be best positioned to set disclosure requirements for those terms.

3. Comparative Experience

Experience in the UK and Australia illustrates the difficulty in achieving an optimal division of regulatory authority over retirement-specific accounts. Each country addressed the allocation of regulatory authority within the context of its approach to financial services regulation. The UK's single regulator model, which assigns the FSA authority over financial services and products currently accommodates the existence of TPR, which has authority to advise and oversee employers that sponsor of work-based pension plans and the trustees of those plans. Australia's objective's-based system assigns regulatory authority in a way closest to that proposed by the *Blueprint*, so that a single regulator (APRA) has responsibility for all prudential regulation and another has responsibility for consumer protection (ASIC). However, both the UK and Australia have struggled with concerns of inefficiencies due to overlapping regulatory authority and gaps in oversight.

In early 2007, the UK commissioned an external study of its pension regulatory system.²³² A large part of the study's mandate was to review the allocation of authority among regulators to ensure efficiency and to identify "conflicts of interest, gaps or unhelpful overlaps in functions."²³³ The review considered the possibility of merging the TPR into the FSA even though the TPR had been in existence only two years at the time of the review.²³⁴ Ultimately the study recommended increased efforts intended to maximize coordination between the TPR and FSA.²³⁵ It also recommended continued observance of the boundaries between the two entities, recognizing that as financial products and regulatory changes affect retirement-specific accounts, it would be important to reevaluate the division of regulatory

²³⁰ Choi, James J., et al. *For Better or For Worse: Default Effects and 401(k) Savings Behavior* Working Paper No. 8651. National Bureau of Economic Research (2001); Cass R. Sunstein, *Boundedly Rational Borrowing*, 73 U. Chi. L. Rev. 249, 256-57 (2006).

²³¹ Pension Protection Act of 2006, § 902, adding 26 U.S.C. §§ 401(k)(13), 401(m)(12), & 414(w).

²³² Paul Thornton, *A Review of Pensions Institutions: An Independent Report to the Department for Work and Pensions* 9 (June 2007), available at <http://www.dwp.gov.uk/pensionsreform/pdfs/InstitutionalReviewFinalreport180507.pdf>

²³³ *Id.*

²³⁴ *Id.* at 37.

²³⁵ *Id.* at 62-62.

authority.²³⁶ That study, however, did not put an end to calls from the financial services firms to merge the FSA and TPR.²³⁷

Australia has undertaken similar reviews, which have resulted in recommendations intended to decrease redundant regulation. In June 2006, the parliamentary Joint Committee on Corporations and Financial Services undertook a study of a variety of pension-related issues, including a benchmarking of Australia's practices against those of other nations and the relevance of APRA's standards.²³⁸ A research paper written at the request of the Parliamentary Joint Committee focused on benchmarking and addressed regulatory overlaps.²³⁹ That report cited concerns resulting from insufficient cooperation and coordination between APRA and ASIC.²⁴⁰ The Parliamentary Joint Committee ultimately recommended a report be undertaken on "the issue of overlapping, inconsistent and conflicting requirements of superannuation funds from a number of regulators."²⁴¹ To date there is no record of such a study.

For disclosure matters, the UK and Australia have generally attempted to resolve the tension between consistency and specialized workplace expertise in favor of consistency, with Australia moving further than the UK in this direction. Both countries have increasingly consolidated authority for regulation of disclosure to investors. In the UK, the FSA has responsibility for ensuring that investors understand financial products and markets but TPR retains some role in disclosures during the accumulation phase of a workplace-related retirement-specific account.²⁴² In Australia, ASIC regulates sales practices and related disclosures by the financial services sector to investors regardless of whether the investments are held in retirement-specific accounts or in generalized investment accounts.²⁴³ One significant difference, though, among the US, UK and Australian pension systems is the amount of discretion that employers have over plan terms. Australia, which mandates a minimum employer contribution level, gives employers the least discretion. The US, which does not require any employer to offer either a DB or DC pension plan, gives employers the most discretion. That increased discretion may affect the balance between the importance of consistency and specialized workplace expertise in assigning regulatory authority.

Similarly, the UK and Australia have consolidated regulatory authority over the business practices of financial services firms using the same principles each country used for assignment of regulatory oversight of disclosure. In the UK, the FSA has regulatory responsibility for the administration of investment accounts, including retirement-specific accounts.²⁴⁴ TPR, however, retains some authority over employment-based pensions because of its focus on the employer's role in pension provision.

The UK consolidation of authority extends to complaint resolution. Investors make their complaints about the administration of investments to the Financial Ombudsman Services (FOS). According to the MOU between the FOS and the PO, "FOS deals with complaints and disputes which predominantly concern the sale and/or marketing of both personal and occupational pensions."²⁴⁵ Compare the US, where FINRA's dispute resolution system applies to complaints against broker-dealers associated with generalized investment accounts and complaints about problems such as execution of

²³⁶ *Id.* at 37.

²³⁷ *See Standard Life calling for single pension regulator*, Money Marketing, Apr. 12, 2007, at p. 13.

²³⁸ *Superannuation Industry*, *supra* note 117, at vii.

²³⁹ Nielson, *supra* note 116.

²⁴⁰ *Id.* at 87. Similarly, concerns were expressed about the interactions of both ASIC and APRA with the ATO. *Id.*

²⁴¹ *Superannuation Industry*, *supra* note 117, at xxiii.

²⁴² *See supra* text accompanying note 122-28.

²⁴³ *See supra* text accompanying note 117-20.

²⁴⁴ <http://www.thepensionsregulator.gov.uk/pdf/moufsa.pdf>; *see also The Governance of Work-based Pension Schemes*, at 42 ("From April 2007 the establishment, operation and winding up of all personal pension schemes are activities regulated by the FSA."), *available at* <http://www.thepensionsregulator.gov.uk/pdf/discussionPaperGovernance.pdf>.

²⁴⁵ An exception that might be considered the regulation of account administration might be the fees charged to accounts. The relevant MOU confers regulatory jurisdiction on TPR for "compliance with the charge cap." <http://www.thepensionsregulator.gov.uk/pdf/moufsa.pdf> p. 4.

buy/sell orders in employer-sponsored retirement-specific accounts are brought as lawsuits in the federal court system.

Australia confers regulatory authority over the administration of all individualized investment accounts on the ASIC. This is part of ASIC's very broad authority, which extends over all corporate entities in Australia including those entities involved in the provision of products and services to investors in retirement-specific accounts. ASIC's responsibilities include prevention of "misleading or deceptive and unconscionable conduct in relation to [retirement investment] products and advice."²⁴⁶ Australia also has established a system of complaint resolution that is unique to benefit related disputes.

As noted above, the level of employer intermediation in retirement-specific accounts distinguishes the US approach from the situation in Australia. Both the UK and US have traditions of pension programs being embedded in the workplace. In that context the employer's retirement-specific account actions are a dimension of the employer-employee relationship. If the sponsorship of those plans becomes too onerous, in a system of voluntary plan sponsorship employers may shift away from DC plans or stop sponsoring plans that contain retirement accounts. Most commentators think that the increase in regulation of DB plans was a factor in the decrease in sponsorship of DB plans.²⁴⁷ Unless, reform of regulation of financial services firms is coupled with reform of the US's voluntary DC system,²⁴⁸ the risk of decreased employer sponsorship must be considered as reform moves forward. The amount of employer intermediation, however, is much higher in DB retirement-specific plans, where the employer makes investment and other risk-related decisions than in DC retirement-specific account plans where those decisions are made by employees.²⁴⁹

Finally workplace-based retirement-specific account schemes in the US have traditionally been used by employers as workplace management tools. In industries where workforce stability was important, DB plans were implemented to increase employee retention. When workforce reductions were required, those same DB plans could provide early retirement programs to ease the impact on employees of the reduction in force. DC retirement-specific accounts provide fewer workplace management tools because they are transferrable among employers and the benefits are not back loaded in the way DB benefits typically are. However, employers still may view those plans as ways to differentiate themselves and attract workers, enhancing their willingness to sponsor such plans. Those circumstances increase the value of specialization by a workplace regulator, such as EBSA, particularly at the account level as opposed to the level of investment products.

VI. Conclusion

The distress in US financial markets, bankruptcies of premier financial services firms, and the congressional rescue packages will reinforce calls for reform of the regulatory framework for the financial services industry. The Treasury Department presented a thoughtful and reasonably comprehensive multi-step plan in its *Blueprint*. Although reform will not be enacted without lengthy debate over the input of many thoughtful proposals, the *Blueprint* provides a framework to begin the discussion of how pension policy and regulation interacts with regulation of the financial services industry. It is essential that as the debate on regulatory reform moves forward policy makers recognize the symbiotic relationship among these areas.

Increasingly, Americans rely on DC retirement-specific accounts, such as 401k accounts, to accumulate assets for retirement. Although they receive favorable tax treatment, those accounts share

²⁴⁶ Parliamentary Joint Committee on Corporations and Financial Services, *The Structure and Operation of the Superannuation Industry*, 9 (Aug. 2007) [hereinafter *Superannuation Industry*].

²⁴⁷ See *supra* text accompanying note 56.

²⁴⁸ Doug Halonen, *401(k) Plans Could be Facing a Total Revamp*, PENSIONS & INVESTMENTS (Oct. 27, 2008), available at <http://www.pionline.com/apps/pbcs.dll/article?AID=/20081027/PRINTSUB/310279971/1005> (outlining proposal to reform the regulation and offering of 401(k) accounts).

²⁴⁹ See *supra* text accompanying note 90-92.

many similarities with investment accounts that are not specific to retirement savings, such as brokerage accounts and bank savings accounts. In each type of account, the individual investor is likely to decide whether to save at all and what investments to make. In each type of account, the individual investor probably will have a variety of opportunities to access the account assets. This is a dramatic difference from the past, when DB retirement plans provided a monthly pension check and were viewed as very different from generic investment accounts.

Although to individual investors, investment accounts of different types, including retirement-specific accounts, are becoming increasingly similar, regulation continues to differentiate among the types of accounts. The *Blueprint* does not explicitly address the regulatory distinctions currently drawn among the various types of accounts and it is impossible to predict how any final reform package will treat retirement-specific account regulation. However, one often discussed reform principle is the consolidation of authority necessary to achieve a specific goal, such as investor protection. The belief is that consolidation would enhance efficiencies, prevent financial products from exploiting regulatory gaps and inconsistencies, and make it easier for investors to compare financial products.

Careful consolidation, though, must be given to any reform of regulation over retirement-specific accounts. Assets held in retirement-specific accounts in the US are a large portion of the total assets under investment in the US. At the same time it is questionable whether those assets will be sufficient to provide retirement security to many Americans. Certainly, DC retirement-specific accounts suffered severe losses during the 2008 economic downturn. It is fair to ask whether proposed reform would better protect retirement-specific accounts in a future downturn. It also is necessary to recognize the intermediary role played by employers and tax policy.

The experience of Australia and the UK illustrates just how difficult these decisions are. Each country took a different path to the assignment of regulatory authority over retirement accounts and the implementation of financial industry participants. Both countries continue to struggle with concerns over regulatory overlaps and regulatory gaps. And, both confront the question of adequacy of retirement assets especially after the 2008 market declines.

There can be no doubt, though, that the fates of capital markets and retirement wealth are intertwined. As the US moves forward with regulatory reform over the financial services industry, the country should not miss this opportunity to ensure that the regulatory structure best supports both the capital markets and working Americans who hope for a financially secure retirement.