IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS

CHAMBER OF COMMERCE OF THE UNITED STATES, et al., Plaintiffs, v. THOMAS E. PEREZ, SECRETARY OF LABOR, and UNITED STATES DEPARTMENT OF LABOR Defendants.	Civil Action No. 3:16-cv-1476-M Consolidated with: No. 3:16-cv-1530-M No. 3:16-cv-1537-M

BRIEF *AMICUS CURIAE* OF BETTER MARKETS, INC., IN SUPPORT OF THE DEFENDANTS

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Statutes

Other Authorities

IDENTITY AND INTEREST OF BETTER MARKETS[1]

Better Markets, Inc. ("Better Markets") is a nonprofit, nonpartisan organization that promotes the public interest in the financial markets through comment letters, litigation, independent research, and public advocacy. It fights for reforms that create a stronger, safer financial system; promote the economic prosperity of all Americans; and protect individual investors from fraud, abuse, and conflicts of interest. Better Markets has submitted more than 175 comment letters to financial regulators, including the U.S. Department of Labor ("DOL"), advocating for strong implementation of reforms in the securities, commodities, and credit markets. It has also filed numerous *amicus* briefs in federal district and circuit courts, typically in support of agency actions. *See generally* Better Markets, http://www.bettermarkets.com (including archive of briefs).

Better Markets has extensive expertise on the subjects of financial-market regulation, investor protection, and administrative law, including the scope of a regulatory agency's duty to conduct cost-benefit analysis in support of its rulemakings. *See generally* BETTER MARKETS, SETTING THE RECORD STRAIGHT ON COST-BENEFIT ANALYSIS AND FINANCIAL REFORM AT THE SEC (July 30, 2012), http://www.bettermarkets.com/sites/default/files/documents/Setting%20The%20Record%20Straight.pdf. All of these topics are central to this case. Better Markets is also intimately familiar with the provisions of the DOL fiduciary duty rule ("Rule") and the exhaustive rulemaking process that DOL followed to craft it. Better Markets filed two extensive comment letters supporting the Rule. *See* DOL comment letter file on the Rule, https://www.dol.gov/ebsa/regs/cmt-1210-AB32-2.html

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[1] Better Markets states that no party's counsel authored this brief in whole or in part, and further, that no party or party's counsel, and no person or entity other than Better Markets, its members, or its counsel, contributed money that was intended to fund preparing or submitting this brief.

(last visited August 25, 2016). Furthermore, Better Markets testified at DOL's public hearings in August of 2015. *See* DOL Conflict of Interest Proposed Rule Public Hr'g, https://www.dol.gov/ebsa/regs/1210-AB32-2-Hearing.html (last visited August 25, 2016). In addition, Better Markets is a co-founding and steering member of Save Our Retirement, a coalition of almost 100 public-interest, retirement, and labor organizations that has worked for years to support the Rule. *See* Save Our Retirement, Membership List (Sept. 8, 2015), http://saveourretirement.com/2015/09/about-save-our-retirement/. This knowledge and expertise will enable Better Markets to assist this Court in resolving the many issues raised in this critically important case.

Better Markets has a strong interest in the outcome of this case for three reasons. First, it seeks to defend the Rule and thereby ensure that Americans trying to save for a secure and dignified retirement are better protected from adviser conflicts of interest that pervade much of the industry, siphoning away tens of billions of dollars every year in hard-earned savings. The Rule, even with its generous exemptions, enshrines the commonsense principle that all financial advisers who serve retirement savers must put their clients' best interest first, as Congress always intended in the Employee Retirement Income Security Act of 1974 ("ERISA") and the Internal Revenue Code ("Code"). A decision to invalidate the Rule would maintain a status quo that exacts a huge toll on retirement savers. Such a decision would also intensify an already serious retirement crisis in this country. Millions of Americans have far too little saved for retirement. *See* U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-15-419, RETIREMENT SECURITY: MOST HOUSEHOLDS APPROACHING RETIREMENT HAVE LOW RETIREMENT SAVINGS 9 (2015). Americans must at least be able to protect and preserve what savings they have managed to set aside.

Second, Better Markets has an interest in ensuring that the plaintiffs' profound

misinterpretations of ERISA are firmly rejected. If, for example, ERISA is held to be bounded by the securities laws or common-law trust concepts—none of which actually limit the generous breadth of ERISA—then DOL's ability to implement and enforce ERISA's fiduciary duty would be impaired, not only as to the Rule but also as to future regulatory measures that DOL may take to protect retirement savers.

Finally, Better Markets has an interest in defending the DOL's rulemaking process against the plaintiffs' attacks predicated on the Administrative Procedure Act ("APA") and general principles of administrative law. DOL conducted one of the most thorough, deliberative, and accommodating rulemakings in history, spanning nearly six years, including a six-month comment period and four days of public hearings. It culminated in a balanced Rule, a set of carefully crafted exemptions, a 395-page Regulatory Impact Analysis, and extensive commentary. *See* Regulatory Impact Analysis for Final Rule and Exemptions[2] ("RIA") (Apr. 2016), https://www.dol.gov/ebsa/pdf/conflict-of-interest-ria.pdf. The record shows that the DOL considered the appropriate factors, examined the relevant data, and offered rational explanations for the choices it made, all in accordance with applicable precedent. Moreover, contrary to the plaintiffs' contention, DOL had no statutory duty to conduct yet more cost-benefit analysis, nor was DOL required to protect the incumbent distribution model for fixed-indexed annuities ("FIAs") from disruptions under the Rule and the exemptions. If this Court were to find this extraordinary process inadequate, then future attempts by DOL and other agencies to adopt rules in the public interest will become much more vulnerable targets for litigation, based fundamentally on nothing more than the regulated industry's self-serving, unfounded, and ultimately irrelevant

[2] *N.B.*, the RIA is produced in the administrative record at 308–698. For ease of reference, this brief cites to the RIA's original pagination.

claims of harm to their bottom line.

SUMMARY OF ARGUMENT

This case epitomizes one of the most significant and damaging trends in modern administrative law: relentless attempts by members of the regulated industry to invalidate rules designed to protect the American public by holding agencies to extreme standards of cost-benefit analysis that have no basis in law. True to this strategy, the plaintiffs in this case have tried to equate reasoned decisionmaking under the APA with a duty to conduct hyper-quantitative and comparative cost-benefit analysis. *See* IALC Br. 24, ECF No. 56 (claiming that "[t]he obligation to confront and compare the costs and benefits of regulation is an essential aspect of administrative rationality"). And they pair this legal argument with characteristically dire predictions that the Rule will impose "immense" costs, resulting in major disruptions, particularly to the distribution networks for FIAs. Chamber Br. 37, ECF No. 52.

But there is no justification for this dramatic rewriting of the basic principles that govern economic analysis by regulatory agencies. Congress decides, in an agency's organic statute, whether and to what extent an agency must conduct cost-benefit analysis, and, in ERISA, it chose not to impose that duty on the DOL—with good reason. Nothing in the APA, applicable case law, or any other provision of law alters this conclusion. In this case, pursuant to executive orders, the DOL did in fact thoroughly consider the costs and benefits of the Rule, and the law required nothing more rigorous, quantitative, or precise. Moreover, the plaintiffs' exaggerated claims of harm from the Rule are just that—unfounded predictions that are all too easily recruited to defeat important regulatory reforms.

Finally, the plaintiffs' more targeted claims that the Rule irrationally subjects FIAs to the more protective provisions of the Best Interest Contract ("BIC") exemption are unfounded. In reality, given the intense conflicts of interest, significant risks, and troubling sales abuses

associated with FIAs, the DOL had ample grounds for concluding that these annuities warrant treatment under the BIC. In short, the Rule epitomizes reasoned decisionmaking on every level, and the plaintiffs' claims should all be rejected.

ARGUMENT

I. DOL FULFILLED ITS DUTY TO CONSIDER THE ECONOMIC IMPACT OF THE RULE.

One of the plaintiffs' core arguments is that the DOL failed to conduct an adequate cost-benefit analysis to support the Rule. *See, e.g.*, Chamber Br. 38, ECF No. 52 (citing DOL's alleged "failure to properly assess the impact and costs of its action"); *id.* at 35 (faulting DOL for "assigning *no* cost estimate to class action litigation in its cost analysis"); ACLI Br. 30, ECF No. 49 (alleging DOL's failure to "weigh a rule's costs and benefits before adopting it"); IALC Br. 24, ECF No. 56 (citing alleged failure to conduct "a reasonable cost-benefit analysis" for moving FIAs to the BIC exemption). Their strategy has become standard fare among opponents of financial regulation, and it has essentially three elements: Claim that the agency is under a legal obligation to conduct exhaustive cost-benefit analysis where none exists; advance unsupported and grossly exaggerated predictions that the Rule will impose devastating costs on the industry (all while ignoring or downplaying the benefits); and fault the agency for failing to account for—and ultimately protect the industry from—those supposedly dire consequences.

In reality, the DOL was under no legal duty to conduct a quantitative and comparative cost-benefit analysis any more rigorous than its RIA.[3] Moreover, as shown in Section II below, the

[3] The DOL clearly *was* under an obligation to consider costs and benefits pursuant to the terms of various executive orders. But those executive orders are not enforceable in court. *See* Executive Order No. 12,866 § 10, 58 Fed. Reg. 51,735 (Oct. 4, 1993) ("This Executive Order is *intended only to improve the internal management of the Federal Government and does not create any right or benefit, substantive or procedural,*

plaintiffs' inflated cost projections, especially in the insurance field, have no basis; indeed, many are contradicted by public assurances from members of the industry itself that they are preparing to adapt to the Rule.

The DOL amply considered the relevant factors. As demonstrated in its brief, the DOL thoroughly considered all relevant factors, including, pursuant to executive orders, the costs and benefits of the Rule, both qualitatively and, where possible, quantitatively. And it specifically evaluated the impact of the Rule and the BIC on independent marketing organizations ("IMOs") and independent agents that recommend and sell FIAs. *See, e.g.*, RIA 38, 101–05, 131, 144, 238 & n.519, 254, 310–11.[4] The DOL furthermore provided plausible explanations for its decisions that were fully consistent with the "evidence before the agency." *See Motor Vehicle Mfrs. Ass'n of U.S., Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983); *Markle Interests, LLC v. U.S. Fish & Wildlife Serv.*, No. 14-31008, 2016 WL 3568093, at *3 (5th Cir. June 30, 2016).

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enforceable at law or in equity by a party against the United States, its agencies or instrumentalities, its officers or employees, or any other person.") (emphasis added). This explains the plaintiffs' struggle to contrive an enforceable legal basis for their cost-benefit claims. In any event, the DOL's RIA amply fulfilled its obligations under the executive orders. This is plain from the extraordinary thoroughness of the RIA itself, and it was confirmed in the executive branch's internal review process. The proposed and final versions of the Rule were each thoroughly reviewed and approved by the Office of Information and Regulatory Affairs, the agency within the Office of Management and Budget responsible for ensuring that agencies comply with the principles set forth in executive orders, including cost-benefit provisions. *See, e.g.*, Conclusion of EO 12866 Regulatory Review, Office of Information and Regulatory Affairs, http://www.reginfo.gov/public/do/eoDetails?rrid=125915.

[4] The DOL went so far as to retain an outside consultant, Advanced Analytical Consulting Group ("AACG") to analyze studies and comments offered by industry opponents, several of whom are the plaintiffs in this case. *See* Karthik Padmanabhan, et al., Review of Selected Studies and Comments in Response to the Department of Labor's Conflict of Interest 2015 Proposed Rule and Exemptions, Advanced Analytical Consulting Group, Inc. (Mar. 4, 2016), https://www.dol.gov/ebsa/pdf/review-of-selected-studies-and-comments-in-response-to-coi.pdf. AACG found the industry studies and comments to be "lacking in rigor, failing to recognize emerging alternatives to traditional offerings of investment advice, incorrectly equating the benefits of conflicted advice to those of non-conflicted advice, or suffering from logical fallacies." *Id.* at i. AACG concluded that, "None of the studies offer compelling arguments against implementation of the DOL's Conflict of Interest Proposed Rule." *Id.*

Neither the APA nor ERISA nor *Michigan v. EPA* required the DOL to produce an analysis that was any more precise.

The APA does not impose a duty to conduct cost-benefit analysis. The plaintiffs contend in effect that reasoned decisionmaking under the APA *entails* a duty to conduct cost-benefit analysis. As framed by IALC, the "obligation to confront and compare the costs and benefits of regulation is an essential aspect of administrative rationality." IALC Br. 24. But this is not the law. The APA's arbitrary-and-capricious standard does *not* require an agency to engage in cost-benefit analysis. *See Vill. of Barrington v. Surface Transp. Bd.*, 636 F.3d 650, 670–71 (D.C. Cir. 2011) (observing there is no authority "for the proposition that the APA's arbitrary and capricious standard alone requires an agency to engage in cost-benefit analysis."). Furthermore, "[t]he APA imposes no general obligation on agencies to produce empirical evidence." *Stilwell v. Office of Thrift Supervision*, 569 F.3d 514, 519 (D.C. Cir. 2009). The APA's core requirement is that an agency must "examine the relevant data and articulate a satisfactory explanation for its action including a 'rational connection between the facts found and the choice made.' " *State Farm*, 463 U.S. at 43. The extraordinarily thorough and well-supported RIA removes any doubt that DOL satisfied its obligations under the APA.

Nor does ERISA impose such an obligation. Ultimately, it is an agency's organic statute that determines whether a court may hold the agency accountable for conducting cost-benefit or economic-impact analysis and the rigor of that analysis. As the Supreme Court has cautioned, an agency's duty to conduct cost-benefit analysis is not to be inferred lightly or without a clear indication from Congress in an agency's organic statute. *See Am. Textile Mfrs. Inst., Inc. v. Donovan*, 452 U.S. 490, 510–12 & n.30 (1981) ("Congress uses specific language when intending that an agency engage in cost-benefit analysis."); *see also Inv. Co. Inst. v. CFTC*, 720 F.3d 370,

379 (D.C. Cir. 2013) ("Where Congress has required 'rigorous, quantitative economic analysis,' it has made that requirement clear in the agency's statute, but it imposed no such requirement here."). Here, the relevant organic statute is ERISA,[5] and in ERISA, Congress chose *not* to impose a cost-benefit analysis obligation on DOL.

That decision should be respected, not just as a matter of law, but on policy grounds as well. There is a growing acknowledgment that at least in the realm of financial regulation, cost-benefit analysis interferes with rather than enhances the regulatory process. *See, e.g.*, Dennis M. Kelleher, *The Dodd-Frank Act Is Working and Will Protect the American People If It Is Not Killed Before Being Fully Implemented*, 20 N.C. BANKING INST. J. 127, 136 (2016) (arguing that myopic cost-benefit analysis prioritizes Wall Street's narrow cost interests above the public interest; drains agency resources; prolongs the rulemaking process; and produce resultss that are incomplete, imprecise, and unreliable); *see also* John C. Coates IV, *Cost-Benefit Analysis of Financial Regulation: Case Studies and Implications*, 124 YALE L.J. 1, 918–19 (2015) (concluding, in a critique of D.C. Circuit decisions on cost-benefit analysis, "[t]he D.C. Circuit presented no evidence that there is any available scientific technique for the SEC to 'assess the economic effects' of the rule along the lines the court seemed to think legally required"). As one court aptly observed in the environmental context, requirements of economic analysis "should not serve as a dilatory device, obstructing the Agency from proceeding with its primary mission of cleaning up the lakes, rivers, and streams of this Nation." *FMC Corp. v. Train*, 539 F.2d 973, 978–79 (4th Cir.

[5] To the extent that DOL is exercising the authority transferred from the Secretary of the Treasury to develop exemptions under § 4975 of the Internal Revenue Code, Treasury is also under no statutory obligation to conduct cost-benefit analysis. *See* 26 U.S.C. § 7805(a).

1976).[6]

Michigan v. EPA is inapposite. Finding no explicit economic analysis requirement in ERISA, the plaintiffs turn to *Michigan v. EPA* for the proposition that a duty to conduct cost-benefit analysis springs from Congress's general delegation of rulemaking authority to DOL. But *Michigan* is inapplicable to this case. The Supreme Court held in *Michigan* that the EPA was required to consider costs when determining whether to regulate certain power-plant emissions, in light of specific environmental statutory provisions and studies focused on cost. In contrast, the DOL's general grant of rulemaking authority covers the entire swath of ERISA, and the notion that Congress thus intended to impose a duty on DOL to conduct cost-benefit analysis for each and every rule is untenable.[7]

The Court was also heavily swayed by the fact that the EPA was dealing with a specific mandate to determine whether to regulate at all: "Agencies have long treated cost as a centrally relevant factor when deciding *whether to regulate*." *Michigan*, 135 S. Ct. at 2707 (emphasis

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[6] A number of cases the plaintiffs cite are inapplicable because they involve very different organic statutes, many in the area of environmental regulation, that impose requirements found nowhere in ERISA. *See* Chamber Br. 37 (citing *Sierra Club v. Sigler*, 695 F.2d 957, 979 (5th Cir. 1983), which involved the National Environmental Policy Act and a variety of specific obligations to consider the impacts of a proposed action); ACLI Br. 32 (citing *Corrosion Proof Fittings v. EPA*, 947 F.2d 1201, 1223 (5th Cir. 1991), which involved the Toxic Controlled Substances Act that, *inter alia*, imposed an affirmative obligation to promulgate the "least burdensome regulation").

[7] Post-*Michigan* decisions confirm that the bedrock principles governing cost-benefit analysis remain intact. *See Lindeen v. SEC*, No. 15-1149, 2016 WL 3254610, at *9 (D.C. Cir. June 14, 2016) ("We do not require the Commission 'to measure the immeasurable' and we do not require it to 'conduct a rigorous, quantitative economic analysis unless the statute explicitly directs it to do so.' "); *but see MetLife, Inc. v. Financial Stability Oversight Council*, No. 15-cv-45, 2016 WL 1391569, *16 (D.D.C. Mar. 30, 2016) (holding that the word "appropriate" may require the evaluation of certain costs). *MetLife* is deeply flawed on multiple grounds, including its treatment of *Michigan*. *See* Br. *Amicus Curiae* of Better Markets, Inc. in Support of the Defendant-Appellant 24–27, *MetLife, Inc. v. Financial Stability Oversight Council*, No. 16-5086 (D.C. Cir. filed June 23, 2016), http://www.bettermarkets.com/resources/better-markets-amicus-brief-metlife-v-fsoc.

added). By contrast, in ERISA, Congress has already made the threshold decision that retirement assets must be protected against conflicts of interest under the strongest possible standards of loyalty and prudence because they are so critical to the "well-being and security of millions of employees and their dependents." 29 U.S.C. § 1001(a).[8] Unlike the EPA in *Michigan,* the DOL is simply tasked with implementing the clear mandate that Congress issued. In light of the foregoing authorities, it is clear that the DOL performed all of the economic analysis in support of the Rule that was required.

II. THE PLAINTIFFS' DIRE COST PREDICTIONS ARE UNSUPPORTED AND INCREDIBLE.

The plaintiffs' allegations framed around cost-benefit analysis are premised largely on predictions that the Rule and the BIC will impose huge costs on advisers. *See, e.g.*, Chamber Br. 35 (claiming class actions threaten "potentially enormous liability"). Much of the argument hinges more specifically on the insistence that the Rule and the BIC are unworkable and will cause major disruptions in the distribution network for FIAs, to the detriment of the IMOs and independent agents that currently dominate that market. *See id.* at 39 (claiming that "independent agents, many of which are small businesses or sole proprietorships, will be unable to satisfy the BIC exemption and will be forced to exit the fixed-indexed annuity market"); ACLI Br. 29 (claiming that the BIC is "unworkable" and will force issuers to make decisions that "drastically interfere with that widely used distribution model"); IALC Br. 25 (asserting that the BIC exemption "is wholly unworkable for fixed indexed annuities in light of their primary distribution channel—independent insurance

[8] Even if *Michigan* were somehow read to require DOL to consider the costs and benefits of its Rule, DOL more than fulfilled that task in the RIA. The obligation to "consider" factors confers wide discretion upon an agency. *See Sec'y of Agric. v. Cent. Roig Refining Co.*, 338 U.S. 604, 611 (1950); *see also Center for Auto Safety v. Peck*, 751 F.2d 1336, 1342 (D.C. Cir. 1985) (judicial deference is especially appropriate "when the agency is called upon to weigh the costs and benefits of alternative policies"). The Court in *Michigan* affirmed this principle. *See Michigan*, 135 S. Ct. at 2707 (it is for EPA to decide how to account for cost, and assigning monetary values is not required).

agents" and that "[s]ubjecting fixed indexed annuities to the BIC exemption will . . . [impose] massive costs in insurers, independent marketing organizations (IMOs), and independent agents"); IALC Br. 26 ("If forced to comply with the BIC exemption, therefore, insurance companies will have to overhaul their primary distribution model for fixed indexed annuities.").

As a threshold matter, the plaintiffs' contention that the DOL had an obligation to ensure that the BIC exemption was "workable" is simply wrong, and it upends DOL's fundamental role. In fact, DOL has no duty to ensure that a particular business model survives regulation if that business model is fraught with conflicts of interest, violates ERISA, and cannot tailor its operations to meet the exemptive conditions that are necessary for the protection of retirement savers. On the contrary, DOL has an affirmative duty to implement Congress's statutory mandates by eliminating such business practices or conditioning them on compliance with safeguards that it deems necessary in its broad discretion. *See* 29 U.S.C. § 1108.

It is true that ERISA and the Code require that the DOL make certain findings before creating exemptions, including a finding that the exemptions are "administratively feasible." 29 U.S.C. § 1108; 26 U.S.C. § 4975(c)(2). But that phrase refers to the *agency*'s capacity to administer the rule, not an assessment of whether the rule is too burdensome, costly, or otherwise "workable" for industry. *See, e.g.*, Bill Schmidheiser, *ERISA's Prohibited Transaction Restrictions: Policies and Problems*, 4 J. CORP. L. 377, 405 (1978) (" 'Administratively feasible' means feasible for the Departments to administer, given the Departments' resources and the nature of the transaction sought to be exempted."); *see also, e.g.*, Proposed Exemptions from Certain Prohibited Transaction Restrictions, 80 Fed. Reg. 44,708 (July 27, 2015) ("The Applicant represents that the requested exemption is administratively feasible because the Sale is a one-time transaction for cash, which will not require continuous or future monitoring by the Department.").

Unless DOL has the ability to effectively administer a PTE, it cannot ensure compliance with its terms and therefore cannot protect plans, participants, and beneficiaries as Congress intended. Canons of statutory construction support this reading. Two of the three criteria for exemptions set forth in § 1108 aim to protect the plans and their participants and beneficiaries. It would be anomalous to read the third criterion, "administratively feasible," as a sudden expression of Congressional concern about the burdens an *exemption* might impose on the regulated industry. Such a reading would offend "[t]he commonsense canon of *noscitur a sociis,* which counsels that a word is given more precise content by the neighboring words with which it is associated." *United States v. Williams*, 553 U.S. 285, 294 (2008).

In any event, the Rule will not have the ruinous impact that the plaintiffs predict. Their estimates of harm are not credible on their face, as they typify biased and unsubstantiated projections, lacking the authority of independent experts. In fact, the plaintiffs' claims are precisely the type of sky-is-falling exaggerations that the financial-services industry has launched against new regulation for almost a century. The pattern has been repeated with each new effort to strengthen financial regulation, including the federal securities laws, deposit insurance, the Glass-Steagall Act, mutual-fund reform, and others. *See, e.g.*, Marcus Baram, *The Bankers Who Cried Wolf: Wall Street's History of Hyperbole About Regulation*, THE HUFFINGTON POST (June 21, 2011, 6:56 PM), http://www.huffingtonpost.com/2011/06/21/wall-street-history-hyperbole-regulation_n_881775.html; Paul G. Mahoney, *The Origins of the Blue-Sky Laws: A Test of Competing Hypotheses*, 46 J.L. & ECON. 229, 249 (2003) ("In the 5 years following adoption of [the most stringent type of blue sky law statute], bank profits increased on average by nearly 5 percentage points . . . ."); *see also* John Heltman, *Mortgage Rules Not Chilling Market as Feared, Data Shows*, AMERICAN BANKER (Sept. 24, 2015), http://www.americanbanker.com/news/law-

regulation/mortgage-rules-not-chilling-market-as-feared-data-shows-1076899-1.html (belying claims that new mortgage underwriting standards would "cripple credit availability" and spur banks to "quit the business entirely"); Comment of Fin. Planning Coal., (July 5, 2013) (application of fiduciary standard to fee-based accounts did not cause predicted "parade of horribles"), https://www.sec.gov/comments/4-606/4606-3126.pdf. In each case, the imagined harm from regulation failed to materialize. The plaintiffs' claims must be similarly discounted.

Contrary to the plaintiffs' warnings, mounting evidence indicates that the FIA industry will readily adapt to the Rule and its exemptions. Insurance companies and IMOs are already fashioning solutions to the challenges of operating under the BIC, including the development of new distribution networks, and they appear confident in their ability to navigate changes. This evidence comes from multiple sources, including IMOs and experts who follow trends in the FIA markets:

- Advisors Excel (an IMO) stated that it has "worked with consultants and law firms to begin preparing the necessary systems to ensure *complete compliance* with the rule, including evaluation of mechanisms to establish Advisors Excel as a financial institution. Rest assured, AE will be prepared for implementation *well in advance of critical dates* and will ensure the financial professionals who work with us are provided with all the tools necessary to comply with the rule." Advisors Excel, DOL Fiduciary Rule (July 2016), http://aeleadstheway.com/wp-content/uploads/2016/07/DOL-Fiduciary-STANCE-2.pdf (emphases added).

- CreativeOne (an insurance wholesaler that assists agents) has "formed an internal, 10-person task force of actuaries, attorneys, compliance, executives, sales and marketing representatives ready to navigate [advisors] through any changes." Chris Conroy, *CreativeOne: Your Resource for Proposed DOL Fiduciary Changes*, CREATIVEEDGE MAG (Apr. 5, 2016), http://www.creativeedgemag.com/creativeone-resource-proposed-dol-fiduciary-changes/.

- Fig Marketing (an IMO that supports agents) "has established a DOL steering committee and is advancing technology and sales and compliance processes to create efficiencies to assist our institutional and retail advisor clients to be successful in any industry environment." Nick Voelker, *The Fiduciary Rule Battle Moves to the Courts!*, FIG CORPORATE BLOG (June 3, 2016), http://www.figblueprint.com/tag/fiduciary-rule/.

Broader surveys yield similar results. An April 2016 article canvassed responses from top executives at a number of IMOs who were asked to share their thoughts on the impact that the Rule would have on their businesses:

- Michael Kalen is the President and CEO of the Futurity First Financial Corporation, a distribution organization with a producer network of over 2,500 independent agents, 15 agencies, and 14 broker-dealer firms. Kalen reported that "some of the tenets of the revised rule like 'ensure objectivity at the point of sale' and 'transparency' are good for the consumer and will be good for business in the long run. We are educating our producers and beginning to develop platform tools they will need to meet these standards if and when they are implemented."

- W. Andrew (Andy) Unkefer is the President of Unkefer & Associates, which is a national annuity and life insurance marketing organization involved in product design and national sales distribution, largely serving independent agents. Unkefer reported that while his company is "contributing to the fight and rallying our agents to participate on two fronts," at the same time they are "preparing to create a fiduciary structure capable of serving our agents, agencies and other marketing firms so they can fully comply with the rule if it prevails."

Brian Anderson, *2016 FMO Executive Outlook, Part I: The M&A Climate, Planning for the DOL Fiduciary Rule, Other Key Challenges*, INSURANCEFORUMS.COM (Apr. 6, 2016), http://ifn.insurance-forums.net/annuities/twenty-sixteen-fmo-executive-outlook-part-one/. Still others have expressed the same confidence that the FIA industry will adapt and even improve:

- Annexus, an independent insurance-product design and distribution company, which comprises a network of 17 IMOs and accounts for more than $4 billion in FIA sales, plans to establish an affiliated broker-dealer through which to sell FIAs. David Rauch, COO and General Counsel at Annexus, stated that it is "full speed ahead" for the firm and that he expects "there are more independent industry players like us who are contemplating the same thing." Greg Iacurci, *Indexed Annuity Distributors Weigh Launching B-Ds Due to DOL Fiduciary Rule*, INVETSMENT NEWS (June 23, 2016), http://www.investmentnews.com/article/20160623/FREE/160629957/indexed-annuity-distributors-weigh-launching-b-ds-due-to-dol.

- Other commentators predict that the Rule will actually strengthen the market for annuities by incentivizing the industry to make them better for investors. Michael Kitces, *Why The DoL Fiduciary Rule Won't Kill Annuities, It Will Make Them Stronger!*, KITCES.COM (Apr. 21, 2016), https://www.kitces.com/blog/why-dol-fiduciary-wont-kill-annuities-it-will-make-them-stronger/.

These examples belie the plaintiffs' insistence that the Rule will inflict catastrophic costs and burdens on IMOs, independent agents, and the FIA marketplace as a whole.[9]

III. THE DOL'S DECISION TO BRING FIAS UNDER THE BIC WAS THE PRODUCT OF REASONED DECISIONMAKING.

Much of the plaintiffs' case is aimed at the DOL's decision to bring FIAs under the BIC. *See, e.g.*, IALC Br. 21–28; ACLI Br. 23–32; Chamber Br. 38–39. IALC in particular alleges that the DOL "drew an arbitrary and unjustified distinction between FIAs and other fixed annuities." IALC Br. 28. But contrary to the plaintiffs' claim, the DOL's carefully considered approach "was the product of reasoned decision making" under the APA, in accordance with the principles set forth in *State Farm*.

As part of the rulemaking, the DOL assembled and published an extensive analysis of the annuity market, including an examination of the important distinguishing characteristics of fixed-rate annuities, FIAs, and variable annuities; the distribution of these annuity products; the conflicts of interest that exist in the annuity market; and the harms to retirement savers that can result from those conflicts. The DOL compellingly showed that FIAs share critical features with variable annuities that make them susceptible to similar conflicts and abuses, features that are not shared by fixed-rate annuities. The RIA also examined the fragmented regulatory landscape governing

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[9] The plaintiffs also make the perfunctory claim that retirement savers will suffer harm under the Rule because it will restrict their access to annuities, described as "enormously valuable to consumers." ACLI Br. 27; *See also, e.g., id.* at 30 (taking it as given that American consumers "will lose access" to annuities); IALC Br. 26 (positing "the substantial costs to retirement savers that will result from the Department's revocation of the 84-24 exemption for fixed indexed annuities"). These assertions deserve no weight. First, the plaintiffs do not establish that FIAs actually benefit investors, and in fact, the record in this case points in just the opposite direction. *See* discussion in Section III, *infra*. The RIA convincingly establishes that FIAs have many problematic features, and that conflicts of interest—which are especially powerful among independent agents selling FIAs—can result in bad financial advice and bad outcomes for investors. Second, the plaintiffs actually make no effort to show that the overall supply of annuities for investors will be reduced by the Rule. Rather, their principal concern appears to be that some insurance market participants will lose their *share* of the FIA business to others, such as broker-dealers.

FIAs, concluding that it does not provide sufficient protections for retirement savers. According to the RIA, "public comments and other evidence demonstrate that these products are particularly complex, beset by adviser conflicts, and vulnerable to abuse." RIA 8. While data limitations impeded quantification of the losses that affect retirement savers, the DOL found nonetheless that there is "ample qualitative and in some cases empirical evidence that they occur and are large both in instance and on aggregate." *Id.* at 9. Based on these and other considerations, the DOL properly determined that these products should be subject to similar treatment, and that treatment should be under the more protective conditions of the BIC. *See id.* at 284. The DOL's RIA and extensive accompanying commentary clearly satisfied and exceeded the agency's obligation to examine the relevant data and articulate a satisfactory explanation for its action.

FIAs share important characteristics with variable annuities. The DOL analyzed the various annuity products that are marketed and sold to retirement savers, including variable, fixed-indexed, and fixed-rate annuities. It compared and contrasted the different features of these annuities with respect to allocation of investment risk, fees, and guaranteed optional benefits. The DOL specifically drew parallels between variable annuities and FIAs. For example, it found that "similar to variable annuities, the returns of fixed-indexed annuities can vary widely, which results in a risk to investors." *Id.* at 123. It also found that insurers can transfer investment risks to FIA investors in ways that resemble the transfer of risk to variable annuity investors. *See id*. For example, variable annuities can offer hundreds of subaccounts that expose clients to market risk, typically through mutual fund performance. *See id*. Similarly, FIAs expose clients to investment risk by crediting investors' accounts based on changes in a market index, excluding dividends. They foist risk onto investors in other ways as well, through a combination of complex and obscure factors such as participation rates, interest-rate caps, and spread/margin asset fees. *See id.* at 123–24.

Worse, insurance companies generally reserve the power to unilaterally change terms and conditions to lower an FIA investor's effective return, leaving the investor with little or no recourse. These investment-oriented features differentiate FIAs from fixed-rate annuities, which provide guaranteed, specified rates of interest and whose terms and conditions regarding crediting criteria do not vary based on the self-interest of the insurance company.

Stakeholders' comments supported the DOL's conclusion that variable annuities and FIAs share similar characteristics. For example, Allianz's comment detailed how the designs of these two products are converging. It described how FIAs can resemble variable annuities and how in fact Allianz Life Insurance Co. offers FIAs that blend features of variable annuities and vice versa, referring to one such product as "a variable annuity with index investment options." Comment of Allianz Life Ins. Co. of N.A. 22 (July 21, 2015), https://www.dol.gov/ebsa/pdf/1210-AB32-2-00718.pdf: *see also* Comment of Jackson Nat'l Life Ins. Co. 3 (Sept. 24, 2015), https://www.dol.gov/ebsa/pdf/1210-AB32-2-03083.pdf. ("Recent changes to the structures of [FIAs] and variable annuities . . . have resulted in these products becoming remarkably similar.")

The distribution patterns for annuity products provide evidence of conflicts. The DOL also provided data on the recent share of annuity sales by distribution channel and product type. *See* RIA 102–04. Those statistics show that the type of distribution channel largely dictates what products are sold, calling into question the extent to which investors' needs and circumstances determine those sales. For example, the main product sold by independent broker-dealers is the variable annuity (representing 23% of all annuity sales in the market), as compared to the fixed-rate annuity (representing 1% of all annuity sales) and the FIA (representing 3% of all annuity sales). *See id*. By contrast, the main product sold by independent agents is FIAs (representing 15% of all annuity sales), as compared to the variable annuity (representing a negligible amount of all

annuity sales) and the fixed-rate annuity (representing 3% of all annuity sales). *See id*. The stark contrast between these figures makes it highly unlikely that they can be explained by differences among the consumers who seek services from these two types of advisers.

In reality, an investor who seeks advice from an independent agent will in all likelihood receive a recommendation to purchase an FIA regardless of whether that product is actually in his or her best interest, just as an investor who seeks advice from a broker-dealer would likely receive a recommendation to purchase a variable annuity regardless of the merits. The sales figures are especially revealing for fixed-rate annuities. Personal-finance writers, without a financial bias toward any particular product, generally view fixed-rate annuities as offering the best deal for investors. *See, e.g.*, Kimberly Lankford, *Deferred Income Annuities Offer Predictability*, KIPLINGER'S RETIREMENT REPORT (Aug. 2013), http://www.kiplinger.com/article/retirement/T003-C000-S004-deferred-income-annuities-offer-predictability.html; Karen Hube, *The Best Annuities*, BARRON'S (June 20, 2015), http://www.barrons.com/articles/the-best-annuities-1434769209. Yet fixed-rate annuities are the least likely to be sold regardless of sales channel, further evidence that retirement savers are not being sold the products that are in their best interest.

The DOL also chronicled the relatively recent changes in annuity sales within the IRA market. Its statistics show a precipitous decline in sales and market share of fixed-rate annuities, which were once dominant. They also show a recent decline in variable annuity sales, while at the same time FIA sales have hit record levels, causing the DOL to infer that the recent gains in the sales of FIAs have come at the expense of variable annuities. *See* RIA 41, 117–18. Given the central role financial professionals play in recommending annuity products, these sales trends suggest that the incentives for financial professionals to recommend FIAs and variable annuities

are considerably stronger than the incentives to recommend fixed-rate annuities. These factors necessitate stronger safeguards to ensure retirement savers who purchase FIAs and variable annuities are adequately protected.

Powerful conflicts of interest influence the sale of FIAs. The RIA further described how commissions in the annuity market create intense conflicts of interest between financial professionals and consumers. The RIA highlighted that, because many financial professionals are compensated entirely or primarily by commissions resulting from annuity sales, they have an incentive to aggressively maximize sales of the highest-commission products. *See id.* at 132, 134.

Moreover, when annuities are considered within the context of the broader range of investment products, a financial professional may have an incentive to recommend an annuity over other alternatives, such as mutual funds, because annuity commissions are often higher than broker-dealers' mutual-fund or securities commissions. *See id.* at 131.[10] Conflicts of interest are thus likely more pronounced in the annuity market than in the mutual-fund market. Furthermore, commissions are typically higher for more complex and opaque FIAs and variable annuities than simpler, more consumer-friendly fixed-rate annuities, thus increasing the incentives to recommend FIAs and variable annuities. *See, e.g.*, *How Do Annuity Commissions Get Paid to the Agent?*, ANNUITY123 (May 16, 2013), http://blog.annuity123.com/how-do-annuity-commissions-get-paid-to-the-agent/; Hersh Stern, *Annuity Commissions and Fees*, IMMEDIATE ANNUITIES (July 8, 2016), https://www.immediateannuities.com/annuity-commissions/; Stan Haithcock, *Debunking Conventional Annuity Wisdom*, MARKETWATCH (Apr. 1, 2014), http://www.marketwatch.com/story/debunking-conventional-annuity-wisdom-2014-04-01.

[10] Jim Poolman, executive director of plaintiff Indexed Annuity Leadership Council, testified at the DOL hearing that commissions on FIAs are "6 to 8 percent, give or take." DOL Hr'g Tr. 937 (Aug. 12, 2015), https://www.dol.gov/ebsa/pdf/1210-AB32-2-HearingTranscript3.pdf.

In fact, sale agents are heavily incentivized to sell FIAs. For example, Insurance Agency Marketing Services advertises that it provides agents the "highest commission levels in the industry." IAMServices, Annuity, http://www.iamsinc.com/annuity/ (last visited Aug. 25, 2016). It further advertises on its "Incentives" page that top producers receive trips to the Fairmont Empress Victoria, British Columbia, and the Four Seasons at Mandalay Bay. An agent qualifies for the Four Seasons trip, for example, by selling $1,250,000 of Athene Premium between November 1, 2015 and December 31, 2016. IAMServices, Incentives, http://www.iamsinc.com/incentives/ (last visited Aug. 25, 2016). InsurMark, advertises this enticement for agents: "COLD CASH, GREAT TRIPS, JUICY PERKS." InsurMark, Rewards, http://www.insurmark.net/agentrewards/ (last visited Aug. 25, 2016). And Magellan Financial, has advertised trips to the Hard Rock Resort and Casino, Punta Cana, in the Dominican Republic, and free iPads for meeting certain production requirements. *See* Examples of Incentives for Annuity Brokers 3–4, Sen. Warren, http://www.warren.senate.gov/files/documents/AnnuityExamples.pdf.; Capmar Ins. Servs., Reward Yourself with Our Capmar Incentive Program!, http://www.capmar.com/rewards/ (last visited Aug. 25, 2016).

These incentive programs that IMOs administer exacerbate conflicts of interest, encouraging and rewarding agents for recommending annuity products that are in the agents', IMOs', and insurance companies' financial interest—not retirement savers' best interest. Given these factors, it was entirely reasonable for the DOL to conclude that FIAs should be subject to the more protective exemptive conditions under the BIC and that IMOs should not be treated as financial institutions without first demonstrating they have an adequate supervisory mechanism in

place to ensure compliance with the Rule.[11]

Conflicts of interest give rise to other detrimental features of FIAs. The RIA detailed how annuities sold on commission, and specifically FIAs, are associated with other product features that are detrimental to retirement savers, including substantial surrender charges that persist for years. Surrender charges effectively lock up a saver's money and make it costly to reverse the investment decision. An SEC Investor Alert, for example, explains that "You can lose money buying an equity-indexed annuity, especially if you need to cancel your annuity early." SEC Investor Bulletin: Indexed Annuities (Apr. 2011), https://www.sec.gov/investor/alerts/secindexedannuities.pdf.

A survey of available FIAs shows products with surrender periods as long as 16 years and surrender charges as high as 20% of premiums. *See* American Equity Bonus Gold (July 14, 2016), https://www.aiponline.net/elink/carrier/Rates/AEIRates.pdf (last visited Aug. 25, 2016); *see also*, *e.g.*, Athene Performance Elite 15 Prod. Details 1, http://www.annuity1.com/as_palette/docs/Athene/Athene_PE_15_ProductDetails.pdf (15-year surrender period, surrender charge up to 15%) (last visited Aug. 25, 2016). Indeed, market research shows that surrender fees for the ten top-selling indexed annuities averaged 11.25% in the first year, as of 2015. *See* Fid., Indexed Annuities: Look Before You Leap (July 13, 2016), https://www.fidelity.com/viewpoints/retirement/considering-indexed-annuities (last visited Aug.

[11] The conflicts of interest that drive the sale of annuities are intensified by the complexity and opacity of these products, which foster a dependence on professional advice and creates an environment in which conflicts of interest are more likely to thrive. The RIA cited to academic research indicating that insurance "agents can inefficiently withhold information and distort consumer choices by providing misleading information or operating in their own self-interests." RIA 155. Insurance agents may engage in this conduct without consequence, according to these researchers, because it is exceedingly difficult for consumers to ascertain the value of insurance products even after purchase. *See id.* Based on these findings, the DOL rightly determined that prudent and impartial advice, important to all investors, is even more crucial in safeguarding investors' best interests in variable annuities and FIAs. *See id.* at 123, 140.

25, 2016). The existence of a product with such disadvantageous features proves that the insurance company and the agents selling it are not reliably acting in customers' best interests.

Several commentators have linked FIAs' hefty surrender charges to the lofty commissions that these products pay to encourage and reward financial professionals for selling them:

> In fact, the whole purpose of surrender charges on annuities is simply to ensure that when an insurance agent is paid a commission upfront, the annuity funds will remain invested long enough with the ongoing interest rate spread extracted from the investor return to allow the insurance company to recover that commission cost from the investor (or else he/she pays a surrender charge to make up the difference!).

Michael Kitces, *The Myth Of "Free" No-Expense Fixed Or Equity Indexed Annuities*, KITCES.COM (Mar. 18, 2015), https://www.kitces.com/blog/the-myth-of-free-no-expense-fixed-or-equity-indexed-annuities-interest-rate-spread-is-still-a-cost/. This structure explains why annuities sold by an intermediary who receives a commission more often include surrender charges than annuities sold directly to customers. *See* RIA 131. It also shows the connection between conflicted incentives and the resulting harm to retirement savers.

Abuses in the sale of FIAs are a serious regulatory concern. These intense conflicts of interest lead to high-pressure and abusive sales practices, as the RIA revealed. For example, a study by the Financial Planning Coalition on senior financial exploitation found that "over half of the [Certified Financial Planner] professional respondents . . . personally had worked with an older client who previously had been subject to unfair, deceptive or abusive practices. Of these, 76 percent reported financial exploitation that involved equity-indexed or variable annuities." RIA 142.

There are more examples of the pervasive conflicts of interest surrounding FIAs than the DOL could possibly have chronicled. For example, in an undercover special, Dateline NBC highlighted advisers' scare tactics, such as making prospective clients think their money is unsafe

in FDIC-insured accounts, downplaying huge surrender charges, and claiming that annuities never lose money. *See* Dateline NBC, Tricks of the Trade (Apr. 23, 2008), *viewable at* http://www.nbcnews.com/id/24095230/ns/dateline_nbc/t/tricks-trade/; *see also Brokers' Choice of Am., Inc. v. NBC Universal, Inc.*, 138 F. Supp. 3d 1191, 1199–1215 (D. Colo. 2015) (finding Dateline broadcast to be substantially true in granting motion to dismiss defamation action).

In addition, state regulators have expressed particular concern after observing an increase in aggressive and misleading advertising by producers and IMOs. Kansas's Insurance Department has observed third-party marketing entities engaging in "misleading, deceptive, and/or incomplete information intended for the general public in what appear to be bait and switch sales tactics." Sandy Praeger, Kan. Comm'r of Ins., Bulletin No. 2014-1 at 1 (May 22, 2014), http://www.ksinsurance.org/department/legalissues/bulletins/2014-1.pdf. Iowa's Insurance Division observed some IMOs "aggressively promoting indexed annuities in potentially deceptive manners." Nick Gerhart, Iowa Ins. Comm'r, Bulletin No. 14-02 at 1 (Sept. 15, 2014), http://www.iid.state.ia.us/sites/default/files/commissioners_bulletins/2014/09/15/insurance_marketing_organizations_pdf_14661.pdf. And statistics compiled by the North American Securities Administrators Association ("NASAA") indicate that annuities are involved in a third of all cases in which senior citizens were subjected to securities fraud or abuse. *See* Comment of NASAA (Sept. 10, 2008), http://www.nasaa.org/wp-content/uploads/2011/07/29-NASAA_Comment_Letter_on_SEC_Proposed_Rule_151A.pdf.

FIAs perform poorly given their design. One way of understanding the true cost of FIAs is to compare the amount those products credit to an investor's account with the returns that an investor could have received elsewhere while taking comparable risks. Several studies have done just that. For example, an illustration by Fidelity shows that an investor would be considerably

worse off purchasing an FIA as compared with a portfolio that is 90% invested in ten-year zero-coupon Treasuries and 10% percent invested in the S&P 500 index. *See* Fidelity, Indexed Annuities: Look Before You Leap. Starting with $100,000, the average ending balance of the Treasury/S&P 500 portfolio would be about $10,000 higher over 56 simulated rolling 10-year periods beginning with 1951-1960 and ending with 2006-2015. *See id.*

Another analysis examined the historical returns of four types of FIAs and 13 specific contracts for the period from 1957 (the beginning of the S&P 500 Index) to 2008. *See* William Reichenstein, *Financial Analysis of Equity-Indexed Annuities*, 18 FIN. SERVS. REV. 291 (2009) (FIAs underperformed the market on a risk-adjusted basis by at least 1.73% per year, with an average underperformance of about 2.9% per year), http://www.cfapubs.org/doi/full/10.2469/dig.v40.n4.21. The analysis concluded that, by virtue of contract design, FIAs will inevitably fail to match the returns available on competitive market-based assets of comparable risk.

Dr. Craig McCann of the Securities Litigation and Consulting Group has done extensive research on FIAs, which has led him to similar conclusions:

> [T]he equity-indexed annuities produce lower returns than US Treasury securities despite being illiquid and exposing investors to stock and bond market risk. This is a recurring theme in equity-indexed annuities. There is an enormous amount of complexity designed into the product but ultimately the complexity is a smoke screen designed and managed to provide investors with substantially the same miniscule returns regardless of which index option is chosen. The resulting investor returns equal the returns on a bond portfolio less a 2.5%-3.0% annual expense ratio.

Craig J. McCann, *An Economic Analysis of Equity-Indexed Annuities* (Sept. 10, 2008), http://slcg.com/pdf/workingpapers/EIA%20White%20Paper.pdf.

Inadequate state insurance regulation. The RIA also included a close examination of the regulatory landscape affecting the distribution of annuities. For example, it reviewed the lack of

uniformity with regard to state insurance suitability regulations. *See* RIA 39, 42, 111. Even in states that have adopted the Model Suitability Regulation of the National Association of Insurance Commissioners, the regulations do not adequately protect retirement investors against sales-driven conflicts of interest. State insurance suitability rules resemble FINRA's suitability rules, which apply to broker-dealers' securities sales. There is compelling evidence that such standards provide retirement investors with inadequate protections from sales-driven conflicts of interest in both contexts. *See id.* at 36–42, 111, 138, 140, 285. Suitability rules allow the sale of the least-suitable among a wide range of "suitable" investments and function more like a "do not defraud" standard than a best-interest standard. This helps to explain why products with highly disadvantageous features can be sold as "suitable" even though they clearly are not in the investor's best interest.

Given these inadequacies in the state regulatory framework, along with the problematic features, sales practices, and compensation incentives associated with FIAs, the DOL acted reasonably in concluding that FIAs should be subject to the BIC, incorporating the conditions it deemed necessary to protect investors from conflicts of interest arising from continued commission-based sales.

CONCLUSION

For the foregoing reasons, the Court is respectfully urged to rule in favor of the defendants and dismiss all of the plaintiffs' claims.

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Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of this *Brief Amicus Curiae of Better Markets, Inc., in Support of the Defendants* was served this 26th day of August 2016, upon counsel for all parties via the Court's CM/ECF electronic filing system.

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