UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS

CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA, *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: 3:16-cv-1530-C 3:16-cv-1537-N

MEMORANDUM IN SUPPORT OF DEFENDANTS' CONSOLIDATED OPPOSITION TO PLAINTIFFS' MOTIONS FOR SUMMARY JUDGMENT AND DEFENDANTS' CONSOLDIATED CROSS-MOTION FOR SUMMARY JUDGMENT

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ACRONYMS USED

ACLI	American Council of Life Insurers
APA	Administrative Procedure Act
BIC	Best Interest Contract
DOL	Department of Labor
ERISA	Employee Retirement Income Security Act
FIA	Fixed Indexed Annuity
FIO	Federal Insurance Office
FINRA	Financial Industry Regulatory Authority
IALC	Indexed Annuity Leadership Council
IMO	Independent Marketing Organization
IRA	Individual Retirement Account
IRS	Internal Revenue Service
NAFA	National Association for Fixed Annuities
NAIC	National Association of Insurance Commissioners
NASAA	North American Securities Administrators Association
PTE	Prohibited Transaction Exemption
RIA	Regulatory Impact Analysis for Final Rule and Exemptions
SEC	Securities and Exchange Commission
SIFMA	Securities Industry and Financial Markets Association

INTRODUCTION

The Department of Labor ("DOL") has broad authority under the Employee Retirement Income Security Act ("ERISA") to protect Americans' retirement savings. In exercise of that authority, DOL engaged in an open rulemaking process spanning almost six years that focused on conflicts of interest in the market for retirement investment advice. Based on extensive public comments and evidence gathered during that process, DOL determined that conflicts of interest in that market are widespread and that underperformance associated with such conflicts in the mutual funds segment alone could cost IRA investors between $95 billion and $189 billion over the next 10 years and between $202 billion and $404 billion over the next 20 years. DOL also found that its previous regulation, which set forth a five-part test to qualify as a "fiduciary" under ERISA by virtue of "render[ing] investment advice," had left loopholes, allowing those acting like fiduciaries to disclaim fiduciary status and its attendant responsibilities and restrictions.

To address these threats to Americans' retirement security, DOL promulgated the Conflict of Interest Rule ("the Rule") and related exemptions ("the rulemaking") at issue here. Pursuant to its authority to define terms for purposes of ERISA, DOL refined its definition of a person who "renders investment advice" to better align with the text and purposes of ERISA in light of significant changes in retirement savings and the market for retirement investment advice since its prior rulemaking. Simultaneously, DOL employed its authority to grant exemptions to allow fiduciaries to engage in certain conflicted transactions that would otherwise be prohibited by law. DOL sought to mitigate the inherent conflicts of such transactions by conditioning the exemptions on safeguards so that they would nevertheless be in the interest, and protect the rights, of retirement investors, as statutorily required.

In these cases, three sets of plaintiffs ("Plaintiffs") challenge the rulemaking, but the bases of their challenge are inapposite legal authority and mischaracterizations of the rulemaking. For instance, Plaintiffs would have the Court disregard the functional test Congress

adopted to determine fiduciary status and supplant it with a standard purportedly based on the common law of trusts, despite Congress's express departure from the common law. Similarly, Plaintiffs urge the Court to rely on the distinctions and approach taken in securities laws, rather than looking to ERISA. But it is ERISA, not the common law of trusts or securities laws, that is the source of the rulemaking at issue.

Moreover, Plaintiffs' position rests on their gross mischaracterization of DOL's rulemaking, which begins on the first page of the Chamber of Commerce brief. While Plaintiffs allege that the rulemaking renders "[w]idely-accepted methods of compensation ... prohibited," Chamber Br. 1, DOL, in fact, crafted new exemptions to allow the industry to "continue to receive common forms of compensation that would otherwise be prohibited [by law], subject to appropriate safeguards." AR12.[1] Likewise, rather than establishing "entirely new standards of conduct," Chamber Br. 1, those who qualify as fiduciaries are subject to the fiduciary responsibilities and restrictions included in ERISA when it was passed in 1974, and those who wish to carry out conflicted transactions that would otherwise be prohibited by law are subject to "fiduciary norms and basic standards of fair dealing" that have long governed fiduciary relationships. AR2. And rather than "reconfigur[ing]" "relationships among financial representatives and their customers," or "eras[ing]" "distinctions between salespeople and fiduciary advisers," Chamber Br. 1, the rulemaking recognizes the reality that a bright-line distinction does not exist, and, as a result, retirement investors are relying on investment advice from those who convey they have investors' best interests in mind but nevertheless find ways to disclaim any obligation to act in investors' best interests. AR498 n.412. On and on, each of Plaintiffs' claims is based on faulty premises about what the rulemaking does, and, as a result,

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[1] Citations to the administrative record begin with the prefix "AR," which includes both the initial joint appendix of core rulemaking documents, *see* ECF No. 47, and the supplemental joint appendix to be filed at the conclusion of the briefing. *See* Order, ECF No. 45. Other sources will be filed with this brief and cited as "Defs.' App'x."

their claims find no legal support in the inapposite authority that they cite.

The changes required under the rulemaking will impose costs on those providing investment advice. DOL determined, however, that those transitional costs will be significantly outweighed by enormous benefits to retirement investors. Where Congress delegated to DOL the authority to determine how best to protect Americans' retirement security, and where DOL, consistent with that authority, conducted a thorough analysis and provided a reasoned explanation for its conclusions as to how best to do so, DOL's determination is entitled to deference, and Defendants are entitled to summary judgment on all of Plaintiffs' claims.

STATEMENT OF FACTS

I. REGULATION TO PROTECT RETIREMENT INVESTORS

Congress enacted ERISA in 1974 based on its determination that Americans' retirement savings were not adequately protected to their detriment and that of the country. Pub. L. No. 93-406, 88 Stat. 829, 898 (1974) (codified at 29 U.S.C. §§ 1001, *et seq.*); *see* § 1001(a). Prior to ERISA, "federal involvement in the monitoring of pension funds in this country was minimal." *Sec'y of Labor v. Fitzsimmons*, 805 F.2d 682, 689 (7th Cir. 1986). ERISA's predecessor, the Welfare and Pension Plans Disclosure Act of 1958 ("Disclosure Act"), provided for "only limited disclosure of information and filing of reports for … pension funds. *Id.* And under the Disclosure Act, "the primary responsibility for supervising … pension funds was left to … beneficiaries, reserving to the states the detailed regulations relating to insurance and trusts[.]" *Id.*[2] Congress thus enacted ERISA "after determining that the then present system of regulation was ineffective in monitoring and preventing fraud and other pension fund abuses." *Id.* It replaced the previous system[3] with, *inter alia*, enhanced "disclosure and reporting" requirements,

[2] Internal citations, quotations, and alterations are omitted in this brief unless otherwise indicated.

[3] ERISA repealed the Disclosure Act. Pub. L. No. 93-406, § 111(a), 88 Stat. 829, 851 (1974).

"standards of conduct, responsibility, and obligation for fiduciaries [to] employee benefit plans,"[4] and "appropriate remedies, sanctions, and ready access to the Federal courts." 29 U.S.C. § 1001(b); *see also Tolbert v. RBC Capital Markets Corp.*, 758 F.3d 619, 621 (5th Cir. 2014).

A. Title I of ERISA: Employee Benefit Plans

As part of its effort to safeguard employee benefit plans, their participants, and beneficiaries, Title I of ERISA imposes stringent obligations on individuals who engage in important plan-related activities, *i.e.*, "fiduciar[ies]." 29 U.S.C. § 1104. In defining who qualifies as a "fiduciary" under ERISA, Congress took an "express statutory departure" from the common law understanding of that term, defining "'fiduciary' not in terms of formal trusteeship, but in *functional* terms ... thus expanding the universe of persons subject to fiduciary duties." *Mertens v. Hewitt Assocs.*, 508 U.S. 248, 262 (1993). According to this "artificial definition of 'fiduciary,'" *id.* at 255 n.5, "a person is a fiduciary with respect to a plan" if:

> (i) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets,
>
> (ii) *he renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan*, or has any authority or responsibility to do so, *or*
>
> (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan.

29 U.S.C. § 1002(21)(A) (emphasis added). A "fiduciary" under Title I of ERISA must adhere to duties of loyalty and prudence. *Id.* § 1104. The former requires a fiduciary to "discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries" and for

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[4] An "employee benefit plan" under Title I of ERISA encompasses two subsidiary categories. *See* 29 U.S.C. § 1002(3). "Employee pension benefit plans" provide retirement income to employees and include various types of defined benefit pension plans and defined contribution plans (*e.g.*, 401(k) plans in which participants direct investment of retirement savings in their individual accounts). "Employee welfare benefit plans" provide various other benefits such as payments for medical care, disability, or death. To be covered by Title I of ERISA, the plan must be established or maintained by private sector employers, employee organizations, or by both. *Id.* § 1003(a).

the "exclusive purpose" of providing benefits to participants and beneficiaries and defraying reasonable expenses of plan administration. *Id.* § 1104(a)(1)(A). The latter requires a fiduciary to act "with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims." *Id.* § 1104(a)(1)(B).

As an additional protective measure, Congress prohibited fiduciaries from engaging in specified transactions Congress deemed inherently fraught with conflicts of interest. *Id.* § 1106; *see Lockheed Corp. v. Spink*, 517 U.S. 882, 888 (1996) (Congress's goal was to bar categorically transactions likely to injure a plan and its beneficiaries). In particular, a fiduciary must not "deal with the assets of the plan in his own interest or for his own account" or "receive any consideration for his own personal account from any party dealing with such plan in connection with a transaction involving the assets of the plan." 29 U.S.C. § 1106(b)(1), (3). Given the breadth of the prohibited transaction provisions, Congress enumerated statutory exemptions from some of them. *Id.* § 1108(b). In addition, Congress delegated to the Secretary of Labor ("the Secretary") the authority to grant "conditional or unconditional" administrative exemptions on a class-wide or individual basis, if the Secretary finds that the such an exemption is:

> (1) administratively feasible,
> (2) in the interests of the plan and of its participants and beneficiaries, and
> (3) protective of the rights of participants and beneficiaries of such plan.

Id. § 1108(a). The Secretary, fiduciaries, and plan participants or beneficiaries may bring actions to enforce the fiduciary duty and prohibited transaction provisions. *Id.* § 1132(a)(2), (3), (5).

B. Title II of ERISA: Tax-Favored Retirement Accounts

In Title II of ERISA, Congress amended the Internal Revenue Code ("the Code") to adopt a "fiduciary" definition parallel to that in Title I. 26 U.S.C. § 4975(e)(3). Title II covers most employee benefit plans covered by Title I, as well as other tax-favored retirement and

savings plans (collectively "IRAs").[5] While the Code provisions do not include duties of loyalty and prudence, they do, as in Title I, prohibit fiduciaries and others from engaging in specified conflicted transactions. *Id.* § 4975(c). The Secretary has the authority to grant administrative exemptions from these Code provisions on the same terms as in Title I. *Id.* § 4975(c)(2).[6]

Those who violate the Code's prohibited transaction provisions are subject to excise taxes enforced by the Internal Revenue Service ("IRS"). *Id.* § 4975(a)-(b). IRA holders may also bring state law claims, including breach of contract claims, regarding the transaction or their relationship with the adviser. *See, e.g.*, *Knox v. Vanguard Group, Inc.*, No. 15-13411, 2016 WL 1735812, at *4-6 (D. Mass. May 2, 2016); *Abbit v. ING USA Annuity & Life Ins. Co.*, 999 F. Supp. 2d 1189, 1197-99 (S.D. Cal. 2014).

C. The 1975 Regulation's Interpretation of "Investment Advice"

ERISA also delegated to the Secretary broad authority to "prescribe such regulations as he finds necessary or appropriate to carry out the provisions of [Title I of ERISA]." 29 U.S.C. § 1135. "Among other things, such regulations may define accounting, technical and trade terms used in such provisions." *Id.* Pursuant to that authority, DOL in 1975 issued a regulation stating when a person "renders investment advice for a fee or other compensation" within the meaning of the second prong of the "fiduciary" definition in ERISA. 40 Fed. Reg. 50842 (Oct. 31, 1975) ("the 1975 regulation"). The 1975 regulation was promulgated before 401(k) plans existed and

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[5] Unless otherwise specified, the term "IRA" refers collectively to the plans covered by 26 U.S.C. § 4975(e)(1)(B)-(F), which include individual retirement accounts, health savings accounts, Coverdell education savings accounts, and certain other trusts and plans. While employee benefit plans that are "qualified" under 26 U.S.C. § 401(a) are also encompassed by § 4975, they are not referred to as IRAs in this brief for clarity's sake.

[6] The parallel provisions of Title I of ERISA and § 4975 of the Code led to redundancy. To harmonize their administration and interpretation, President Carter issued Reorganization Plan No. 4 in 1978 ("Reorganization Plan"), which Congress ratified in 1984, Pub. L. No. 98-532, 98 Stat. 2705 (codified at 5 U.S.C. App. 1, 29 U.S.C § 1001 note). Among other things, the Reorganization Plan transferred to DOL the interpretive, rulemaking, and exemptive authority for the fiduciary definition and prohibited transaction provisions that apply to both employer-based plans and IRAs. *See* Reorg. Plan § 102 (transferring "all authority of the Secretary of the Treasury to issue [regulations, rulings, opinions, and exemptions under section 4975 of the Code] ... to the Secretary of Labor").

before IRAs were commonplace. It narrowed the scope of the statutory definition by setting forth a five-part test, under which a person was deemed to "render[] investment advice" when he: (1) renders advice as to the value of securities or other property, or makes recommendations as to the advisability of investing in, purchasing, or selling securities or other property, (2) on a regular basis, (3) pursuant to a mutual agreement, arrangement or understanding, with the plan or a plan fiduciary that (4) the advice will serve as a primary basis for investment decisions with respect to plan assets, and (5) the advice will be individualized based on the particular needs of the plan. *See* 29 C.F.R. § 2510.3–21(c)(1) (2015); 26 C.F.R. § 54.4975-9 (2015) (parallel Code regulation). Under the 1975 regulation, an adviser was an investment advice fiduciary with respect to a particular instance of advice only if he met every element of the five-part test.

D. Regulation of Providers of Investment Advice

Retirement investment advice is governed by several different (but overlapping) regulatory and supervisory regimes, including ERISA, federal securities laws, state insurance regulation, and industry self-regulatory bodies. *See* Regulatory Impact Analysis for Final Rule and Exemptions, April 2016 ("RIA"), AR344-45, 355. ERISA, including the Code provisions, applies to all forms of assets a plan or IRA may hold, including real estate, insurance products, and securities. AR344. Rooted in the common law of trusts (but differing from it in key respects), the focus of ERISA is on the elimination or mitigation of conflicts of interest and adherence to substantive standards of conduct, reflecting legislative judgments on the best way to protect the public interest in certain tax-preferred benefits. *Id.* By contrast, federal securities laws, administered by the Securities and Exchange Commission ("SEC"), apply to transactions involving a narrower category of investments—securities—but a broader class of investor—all clients—not just retirement investors. AR345. The duties imposed on advisers by the SEC stem largely from statutory antifraud provisions. *Id.* As a result, those duties differ in significant respects from those in ERISA and the Code. *Id.* The insurance industry is primarily regulated

by state law, which is influenced by non-binding model standards from the National Association of Insurance Commissioners ("NAIC"),[7] but can deviate in small or large ways. AR352, 355.

Within these regimes are three overlapping groups of professionals providing investment advice to the retirement market today—registered investment advisers, broker-dealers ("brokers"), and insurers and their agents. *See* AR416. A registered investment adviser meets the definition of "investment adviser" in the Investment Advisers Act of 1940 ("the Advisers Act"), 15 U.S.C. § 80b-1 *et seq.*, and generally must register with the SEC. A registered investment adviser has fiduciary duties similar to, but not coextensive with, ERISA duties of loyalty and prudence. AR348-49. Conflicts of interest are generally addressed by disclosure and consent for transactions, unlike ERISA's categorical transaction prohibitions. AR349.

Brokers trade securities on others' behalf and are generally governed by the Exchange Act and SEC rules. 15 U.S.C. § 78c(a)(4); AR347. They are not required to register as investment advisers if their advice is "solely incidental" to the conduct of their business as a broker or dealer and they receive no "special compensation" for advisory services. 15 U.S.C. § 80b-2(a)(11)(C); AR348. In giving investment advice, brokers are generally subject only to a "suitability" standard set by the Financial Industry Regulatory Authority ("FINRA"),[8] which requires a broker to have a reasonable basis to believe that a recommended transaction or investment strategy involving securities is suitable for the customer, based on the customer's investment profile. *See* AR348-49, AR427.

Insurance companies sell annuity contracts as retirement investment options for plan and IRA investors.[9] AR355-57. The NAIC's 2010 Suitability in Annuity Transactions Model

[7] The NAIC is the standard-setting and regulatory support organization created and governed by chief insurance regulators from all 50 states, DC, and five territories. AR352.

[8] FINRA is a self-regulatory organization of the broker industry. It is registered with, and operates under the oversight of, the SEC. *See* AR349-50.

[9] This discussion does not concern immediate annuities or the payout phase of deferred annuities. *See* AR438.
(*footnote continued on next page*)

Regulation ("2010 Model Regulation"), to the extent adopted by states, sets suitability standards for insurers similar in many respects to FINRA suitability requirements for brokers. AR357; AR27896. The NAIC sought to establish a framework under which insurance companies, not just individual agents or brokers, are "responsible for ensuring that the annuity transactions are suitable." AR355, AR68126. To do so, the 2010 Model Regulation requires insurers to develop supervisory systems to ensure their and their agents' compliance with the Model Regulation and suitability requirements. AR27900-01, 2010 Model Regulation § 6(F)(2). This includes establishing reasonable policies and procedures to assess the suitability of each product recommendation. *Id.* A version of the 2010 Model Regulation has been adopted by 35 states and the District of Columbia, but exact requirements vary by state, and one state currently lacks any suitability requirements. AR358; AR27908-14. The Federal Insurance Office ("FIO")[10] has noted that the lack of a uniform standard is particularly concerning for complex annuities: "[a]s unprecedented numbers of seniors reach retirement age with increased longevity, and as life insurers continue to introduce more complex products tailored to consumer demand, the absence of national annuity suitability standards is increasingly problematic." AR14888-89, AR358.

There are generally three types of deferred annuities: declared-rate annuities (also called "traditional fixed annuities"), fixed-indexed annuities ("FIAs"), and variable annuities. *See Am. Equity Inv. Life Ins. Co. v. SEC*, 613 F.3d 166, 168-69 (D.C. Cir. 2009); *see also* AR427-28, AR438-42 (comparison chart). All three types are sold to individual IRA holders, whereas for sales to employee benefit plans—which are generally group annuities rather than individual annuities—declared-rate and variable annuities predominate. AR433, Fig. 3-9. The annuity

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Instead, it focuses on the accumulation phase in which the customer is not receiving a payout.

[10] The Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"), Pub. L. No. 111-203, 124 Stat. 1376 (2010), established FIO in the U.S. Department of the Treasury and vested FIO with certain authorities, including the authority to monitor all aspects of the insurance industry. AR353.

market is concentrated, with the top 20 companies handling about 80% of the assets, and specialized, with the leading companies that sell variable annuities not selling fixed annuities, and vice versa. AR420. The three types differ as follows:

- Declared-rate. These are "contract[s] issued by a life insurance company, under which the purchaser makes a series of premium payments to the insurer in exchange for a series of periodic payments from the insurer to the purchaser at agreed upon later dates." *Am. Equity*, 613 F.3d at 168. Under most state laws, if the annuity is liquidated, the contract holder is guaranteed 87.5% of premiums paid after any fees or other charges. AR440. The insurance company bears the investment risk because it guarantees that the purchaser will earn a minimum rate of interest. AR434-35, AR439. They are subject only to state insurance laws and are not regulated under federal securities laws. *Am. Equity*, 613 F.3d at 168.

- Variable. These are regulated as securities, and purchasers pay premiums that are invested in common stocks and other equities, such that the entire investment risk—as to both principal and interest—is borne by the contract holder and benefit payments vary with the success of the investment. AR427, AR439.

- Fixed-indexed. FIAs are a hybrid. *Am. Equity*, 613 F.3d at 168. While the contract holder's *principal* is guaranteed as in declared-rate annuities, *returns* are not. Instead, returns vary widely based on the performance of a specified index or other external reference. AR439-40. Thus, similar to variable annuities, some of the investment risk of an FIA is borne by the contract holder. *Id.*; AR484. The annual index-linked gains are not simply credited to the investors account, but instead the insurance company can limit how much is credited by deducting fees (called "spreads," "margins" and "administration fees") and crediting only a percentage of the interest-linked gains and imposing interest rate caps or upper limits on returns. AR435, 439. Congress has directed the SEC not to treat FIAs as securities if they satisfy the NAIC suitability standards and other standards set forth in the Dodd-Frank Act.[11]

Annuities are sold through different distribution channels. Variable annuities are most commonly sold by brokers. AR447. Declared-rate annuities are most commonly sold by banks or career insurance agents.[12] *Id.* FIAs are most commonly sold by independent insurance agents (66% in 2014). *Id.* The independent agent channel for declared-rate annuities and FIAs

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[11] The Harkin Amendment to the Dodd-Frank Act, § 989J, establishes rules for FIAs to be exempt securities. *See* Pub. L. No. 111-203, § 989J, 124 Stat. 1376, 1949.

[12] Career agents are those who devote more than 75% of their time to one insurance company's products, and often receive financing, training, and office space from that company. AR417.

generally also involves insurance intermediaries such as independent marketing organizations ("IMOs"), who provide support to independent agents. AR418-19.

II. CHANGES IN THE RETIREMENT INVESTMENT MARKET SINCE 1975

A. Much Investment Advice Today is Rendered by Advisers Who Are Not Subject to Fiduciary Responsibilities Under the 1975 Regulation

Since DOL adopted the 1975 regulation, the retirement savings market has changed profoundly. Then, most pension plans were employer-based defined benefit plans, AR9, where the employee is entitled to a fixed periodic payment upon retirement. *Hughes Aircraft Co. v. Jacobson*, 525 U.S. 432, 439 (1999). The employer typically bears the entire investment risk and must cover any underfunding that may result from the plan's investments. *Id*. These plans have ongoing funding requirements, *see* 29 U.S.C. § 1083; 26 U.S.C. §§ 412, 430, and because they are more likely to be large and actively managed, the financial professionals who provide ongoing investment advice are likely to meet the 1975 regulation's five-part test. *See* AR430.

That paradigm has shifted with the rise in IRAs, created through ERISA in 1974, and 401(k)-type defined contribution plans,[13] created by Congress in the Revenue Act of 1978. Pub. L. No. 95-600, § 135(a), 92 Stat 2763 (1978). A 401(k) plan allows employees to defer taxes by investing part of their salaries for retirement. 26 U.S.C. § 401(k). In late 2015, IRAs held $7.3 trillion, while defined contribution plans (including 401(k)s) held $5.2 trillion, and defined benefit plans held only $2.8 trillion. AR431; *see also* AR504 (share of participation in defined contribution plans grew from 29% to 83% since 1975).[14]

As a result of this shift, plan participants are increasingly responsible for managing their own retirement assets. AR319; AR9. Participants in 401(k) plans have some fiduciary

[13] A defined contribution plan "provides for ... benefits based solely upon the amount contributed to the participant's account, and any income, expenses, gains and losses[.]" 29 U.S.C. § 1002(34).

[14] A 401(k) plan differs from an IRA in that it is set up by the employer or a group of employees. *See* 26 U.S.C. § 401(k). IRAs are individual accounts subject to total control by the account holder. *See* AR413-14.

protection for their investment choices because 401(k) plan fiduciaries are responsible for both selecting investment options and managers and monitoring their performance. AR4; 29 C.F.R. § 2550.404c-1(f)(8), (9). Participants, however, still face many choices, such as deciding how to allocate their assets in their individual accounts and often rely on professional advisers for assistance. AR507-13, 517-20. Employers, including small businesses, may also rely on advisers to help select the investment options for such plans. AR504-06, 516-17.

The role of participants has also increased due to the growth of IRAs. By 2015, more than 40 million households saved for retirement in IRAs (in the narrow sense).[15] AR9; AR431, 500. Most IRA assets derive from rollovers from defined contribution plans, which are expected to approach $2.4 trillion cumulatively from 2016 through 2020. AR319, 416. Most IRA investors consult a financial professional in some capacity regarding their rollover decision, but IRA investors do not have the same protections as 401(k) plan participants. *Id.*

Due in part to these shifts, as well as the application and manipulation of the 1975 regulation's five-part test, much of the retirement investment advice given today is not protected by fiduciary duties and restrictions. For instance, as a result of the "regular basis" requirement in the five-part test, an adviser is not a fiduciary when an investor seeks "specialized advice on a one-time basis, even if the advice concerns the investment of all or substantially all of the assets held in the account (*e.g.*, an annuity purchase or a rollover from a plan to an IRA or from one IRA to another)." AR10. The "regular basis" requirement also means that fiduciary standards may not apply to advice given to a plan fiduciary about a one-time purchase of a group annuity to cover all of a plan's participants for the rest of their lives when a defined benefit plan terminates. *Id.* Investment professionals otherwise frequently avoid fiduciary duties and

[15] This includes the individual retirement accounts encompassed by 26 U.S.C. § 4975(e)(2), and not the other tax-favored accounts for which "IRA" is also used in this brief. *See supra* n.5.

restrictions by marketing their services in ways that suggest they are providing tailored, individualized advice, while concurrently disclaiming fiduciary status under the five-part test by disavowing in fine print a "mutual" understanding that the advice is intended to be used as the "primary basis" for investment decisions. *Id.*; *see also* AR320.

B. Advisers Have Widespread Conflicts of Interest that Harm Retirement Investors

At the same time, compensation arrangements in the retirement investment industry have created incentives for advisers to recommend products that pay them or their firms more money rather than products that are in their clients' best interests. *See* AR337, 444-50 (explaining different forms of conflicted compensation arrangements). Product providers compensated entirely or primarily on a commission basis have a strong incentive to aggressively maximize sales, and when commissions vary depending on the product, the provider has a further incentive to recommend the product paying the highest commission. *See* AR436-37, 450. Incentives created by varying compensation are compounded by arrangements in which an insurer pays agents and brokers a percentage of premiums if they meet certain goals in terms of volume, persistency, and profitability for the insurer. AR438.[16]

Brokers and their representatives often have a financial stake in the investment decisions that IRA investors make according to the representatives' advice and often stand to gain if IRA investors trade more, buy or hold certain mutual funds or other products, or buy securities out of the broker's own inventory. AR444. The attendant conflicts often play out at two levels: variation in the revenue received by the broker, and variable compensation paid by the broker to

[16] The conflicts posed by these compensation practices have been well-documented by regulators and outside groups and acknowledged by the financial services industry. *See* AR449. In an October 2013 report, based on firms' responses to a conflict of interests letter, in-person meetings, and a follow-up compensation questionnaire, FINRA identified conflicts that encourage advisers to meet certain production thresholds to obtain large rewards, favor some products over others to enhance firm revenue or profit, and give preference to proprietary products. AR450. A RAND study prepared for the SEC also identified financial conflicts that advisers often operate under when recommending a transaction to a client. AR446. Financial service providers also affirmed the prevalent use of a wide variety of compensation arrangements with the potential for biased investment advice. AR449 & n.315.

its representatives who render IRA advice. *Id.*

Similar conflicts of interest arise in the context of annuities. Commissions for annuities are generally much higher and are often less transparent than those for mutual funds. *See* AR447. The Indexed Annuity Leadership Council ("IALC"), one of the Plaintiffs here, stated that the typical commission on an FIA sale is "about six to eight percent give or take," AR60668 (Aug. 12, 2015 Hr'g Tr., statement of Jim Poolman); *see also* AR447, compared with an average commission of 1.37% for brokers selling front-end-load mutual funds. *See* AR661.[17] Thus, for example, a $90,000 rollover from a 401(k) to an annuity—the median lump sum distribution for a retiring worker, AR502-03—could provide the agent a commission of as much as $7,200. These problems are further compounded by the use of bonuses given to independent agents or brokers by insurers for meeting certain sales goals. AR447-48.[18] As a result, insurance agents have financial incentives to steer investors toward particular annuity products regardless of whether these products best serve investors. *Id.* And if a customer has an unexpected need for liquidity and chooses to access the annuity's account value, surrender charges and adverse tax consequences may reduce accrued returns or even erode a portion of the premium. AR456, 600.

Individual consumers, who are now the predominate recipients of this advice often, lack the expertise of their advisers and are frequently unaware of the nature and extent of these conflicts. AR325, 421, 443, 447-48, 458-59.[19] Consumers today are also confronted with

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[17] "Loads" are sales fees associated with certain investment products. Investors pay a front-end sales load when they purchase fund shares and a back-end or deferred sales load when they redeem their shares. *See* SEC Fast Answers, Mutual Fund Fees and Expenses, http://www.sec.gov/answers/mffees.htm#salesloads.

[18] *See, e.g.,* AR16242-76 (Cmt. 702, Financial Planning Coalition); AR5316-22, Zeke Faux and Margaret Collins, "Indexed Annuities Obscure Fees as Sellers Earn Trip to Disney," Bloomberg Business (January 20, 2011).

[19] *See* AR498 n.412, AR10361-90 (Sept. 15, 2010 joint letter to SEC from AARP, Consumer Federation of America, Certified Financial Planner Board of Standards, Financial Planning Association, National Association of Professional Financial Advisers, Investment Adviser Association, and North American Securities Administrators Association ("NASAA"), transmitting survey results demonstrating that a "vast majority" of U.S. investors support a clear fiduciary standard and reporting that upwards of 60% of surveyed investors incorrectly believe that stockbrokers and insurance agents are already subject to fiduciary duties).

myriad choices of financial products, many of which did not exist or were uncommon in 1975. *See* AR319. Advisers may also market themselves with titles like "financial adviser" or "wealth manager" that imply expertise but that anyone can use. AR416.

Under these circumstances, DOL found that the predictable result is that conflicts bias investment advisers to the detriment of investors. In its RIA, DOL quantified the extent of harm in the IRA market for some mutual funds, finding the impact of conflicts of interest on investment outcomes in that market to be large and negative. *See* AR474-76, Fig. 3-17. A review of the data suggests that IRA holders receiving conflicted investment advice in that market can expect their investments to underperform by an average of one-half to one percent per year over the next 20 years. AR474. This underperformance—in one segment of the market alone—could cost IRA investors between $95 billion and $189 billion over the next 10 years. *Id.* Based on a wide body of evidence, DOL also concluded that the harm is widespread throughout the market. *Id.* Surveys show that insurance professionals themselves believe that agents sometimes act on conflicts of interest at customers' expense. *Id.* 147.

DOL concluded there was specific cause for concern regarding FIAs. As NASAA, an organization representing state securities regulators, noted:

> Equity-indexed annuities are extremely complex investment products that have often been used as instruments of fraud and abuse. For years, they have taken an especially heavy toll on our nation's most vulnerable investors, our senior citizens for whom they are clearly unsuitable.

AR68639. The SEC similarly noted "complaints of abusive sales practices" in the FIA market, including inadequate disclosure to investors and outsized commissions. 74 Fed. Reg. 3138, 3138-39 (Jan. 16, 2009).[20] FINRA has expressed concerns that the sales materials associated

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[20] *See also Brokers' Choice of Am., Inc. v. NBC Universal, Inc.*, 138 F. Supp. 3d 1191, 1195 (D. Colo. 2015) (finding substantially true "the 'gist'" of a *Dateline* program that an "Annuity University" for licensed insurance brokers "teaches insurance agents to scare and mislead seniors into buying unsuitable insurance products").

with FIAs often do not fully and accurately describe the products and could confuse or mislead investors. AR359. Commenters on the rulemaking expressed similar concerns. *See* AR39243-46 (Cmt. 596, Ron A. Rhoades), AR46846-53 (Cmt. 3090, Professor Bullard for Fund Democracy), AR45965-67 (Cmt. 3034, Committee for the Fiduciary Standard).

C. Proposed Rulemaking

2010 Proposal. In an effort to close the gap in the application of fiduciary duties and minimize conflicts of interest in the market for retirement investment advice, DOL published a notice in 2010 proposing to revise the 1975 regulation's definition of an investment advice fiduciary. *See* 75 Fed. Reg. 65263 (Oct. 22, 2010). DOL held a two-day public hearing, received over 300 comment letters, and held more than three dozen meetings with interested parties on the proposed rule. AR12. A number of commenters requested additional analysis of the proposal's expected costs and benefits, AR703, and others asked for new prohibited transaction exemptions to minimize disruption of current compensation practices. *Id.*; *see also* AR321. In light of these comments, and because of the significance of the proposal, DOL decided to withdraw the 2010 proposal. AR699, 727; AR321.

2015 Proposal. After meeting with numerous stakeholders, studying the issues raised by commenters, and producing a more robust preliminary RIA, AR12, AR321, DOL issued a new proposal in 2015. AR699. In addition to revising the definition of who "renders investment advice," DOL responded to commenters' requests by proposing two new prohibited transaction exemptions ("PTEs"), the Best Interest Contract ("BIC") Exemption and the Principal Transactions Exemption, which could be used for a broad range of compensation practices and investment transactions. AR322. DOL also proposed to amend some existing PTEs. *Id.* Both the amendments to existing exemptions and the two new exemptions would condition reliance on adherence to impartial conduct standards, requiring the financial institution and adviser to:

(1) provide advice in the investor's "best interest," a term defined to mirror the

duties of prudence and loyalty in Title I of ERISA, 29 U.S.C. § 1104(a),
(2) avoid misleading statements, and

(3) charge no more than reasonable compensation for the total services provided to the investor.

AR63. With the 2015 proposal, DOL published on its website a preliminary RIA, containing an in-depth economic assessment of the market for retirement investment advice. *See* AR819.

Comments and hearings. DOL initially provided a 75-day comment period on the proposal but extended the comment period by two weeks in response to stakeholder requests. AR13. In August 2015, DOL held a four-day public hearing on the proposal, at which over 75 speakers testified. *Id.* DOL made the proposed regulation, exemptions, public comments, and hearing transcript available on its website. *Id.* In total, DOL received over 3,000 individual comment letters. DOL again held numerous meetings with interested stakeholders. AR323.

D. Final Rulemaking

Definition of "Investment Advice" Fiduciary. After carefully evaluating the extensive record developed on the 2015 proposal, DOL published the final rule on April 8, 2016 ("the Rule"). AR1. The Rule defines "investment advice" in terms of specified "recommendations" to an advice recipient regarding, *inter alia*, "the advisability of acquiring, holding, disposing of, or exchanging," or "the management of," "securities or other investment property," including how the securities should be invested after they are rolled over, transferred, or distributed from a plan. 29 C.F.R. § 2510.3–21(a)(1)(i)-(ii).[21] The Rule further defines a "recommendation" as "a

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[21] Specifically, under the Rule, a person renders fiduciary investment advice with respect to moneys or other property of an employee benefit plan or IRA if such person provides to a plan fiduciary, plan participant or beneficiary, IRA, or IRA owner the following types of advice, for a fee or other compensation, direct or indirect:

(i) A recommendation as to the advisability of acquiring, holding, disposing of, or exchanging, securities or other investment property, or a recommendation as to how securities or other investment property should be invested after the securities or other investment property are rolled over, transferred, or [otherwise] distributed from the plan or IRA;

(ii) A recommendation as to the management of securities or other investment property, including, among other things, recommendations on investment policies or strategies, portfolio composition, selection of other persons to provide investment advice or investment management services, selection of investment account arrangements (e.g., brokerage versus advisory); or

(*footnote continued on next page*)

communication that, based on its content, context, and presentation, would reasonably be viewed as a suggestion that the advice recipient engage in or refrain from taking a particular course of action." § 2510.3–21(b)(1). The definition of a recommendation is based on FINRA's approach to regulating investment advice in the broker context and tracks SEC guidance. AR26-27. Communications that require the adviser to comply with suitability requirements under applicable securities or insurance laws are "recommendations" under the Rule. AR26.

In response to comments on the 2015 proposal, DOL concluded in the Rule that certain categories of advice, including investment education, which had been listed as "carve-outs" in the 2015 proposal, were not investment advice that came within the new definition because they were not recommendations. AR3, AR26. Separately, DOL excluded from the definition three categories of activities that could have been considered "recommendations" because it did not believe Congress intended to cover them as fiduciary relationships: (1) transactions with certain plan fiduciaries who have financial expertise; (2) swap transactions; and (3) certain advice provided by plan sponsor employees. AR3.

<u>BIC Exemption.</u> On the same day it published the Rule, DOL also published the final BIC Exemption.[22] *See* AR58, 81 Fed. Reg. 21002 (Apr. 8, 2016). The exemption provides

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> recommendations with respect to rollovers, transfers, or distributions from a plan or IRA, including whether, in what amounts, in what form, and to what destination such a rollover, transfer, or distribution should be made[.]

AR52 (new 29 C.F.R. § 2510.3–21(a)(1)). In addition, a recommendation described above must be made either directly or indirectly (e.g., through or together with any affiliate) by a person who—

> (i) represents or acknowledges that that it is acting as a fiduciary within the meaning of [ERISA] or the Code;
>
> (ii) renders the advice pursuant to a written or verbal agreement, arrangement, or understanding that the advice is based on the particular investment needs of the advice recipient; or
>
> (iii) directs the advice to a specific advice recipient or recipients regarding the advisability of a particular investment or management decision with respect to securities or other investment property of the plan or IRA.

Id. (new 29 C.F.R. § 2510.3–21(a)(2)).

[22] On July 11, 2016, DOL republished the BIC Exemption with a technical correction to confirm insurers' broad

(*footnote continued on next page*)

broad prohibited transaction relief for a range of compensation practices that ERISA and the Code would otherwise prohibit, so long as advisers and financial institutions adhere to basic fiduciary standards and take certain specified steps to mitigate the impact of conflicts of interest. AR59. In particular, to rely on the exemption, financial institutions must:

- acknowledge fiduciary status with respect to investment advice to the investors;
- adhere to "impartial conduct standards" requiring them to:
  - give advice in the retirement investor's best interest (i.e., prudent advice based on the investment objectives, risk tolerance, financial circumstances, and needs of the investor, without regard to financial or other interests of the adviser or financial institution);
  - charge no more than reasonable compensation; and
  - make no misleading statements about investment transactions, compensation, and conflicts of interest;
- implement policies and procedures reasonably and prudently designed to prevent violations of the impartial conduct standards;
- refrain from giving or using incentives for advisers to act contrary to the customer's best interest; and
- fairly disclose the fees, compensation, and material conflicts of interest associated with their recommendations.

AR63. In the case of fiduciary advice to non-Title I plans and IRAs, these requirements must be contained in a contract between the financial institution and the retirement investor. AR78.

The exemption does not ban differential compensation—such as commissions based on customers' investment decisions—as long as the policies, procedures, and incentive practices viewed as a whole are reasonably and prudently designed to avoid misalignment of the adviser's and investor's interests. AR133, BIC Exemption § II(d)(3). DOL's intent in the exemption was to hold financial institutions and their advisers responsible for adhering to fundamental fiduciary standards, while leaving them the flexibility and discretion to determine how best to satisfy these basic standards in light of the unique attributes of their businesses. AR63.

The final BIC Exemption reflects many changes made in response to comments to make

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eligibility to rely on the exemption, consistent with its intended scope and DOL's analysis in the RIA. *See* AR146.

its conditions less costly and more readily complied with by financial institutions. AR74; *see also* AR567-68 (chart comparing proposed and final BIC Exemptions). Only the financial institution must execute the contract with the investor (electronically or in writing), rather than each of the advisers from whom the investor receives advice, and the contract need not be executed until the recommended investment transaction is made, rather than when advice is first given. AR79-80. The exemption adds a provision that errors or omissions with respect to the disclosure requirements will not result in loss of the exemption if the financial institution acts in good faith and discloses correct information promptly after discovery of the error. AR64.

The final exemption also reduces compliance costs by eliminating and substantially modifying certain data collection and disclosure requirements. Namely, DOL eliminated an extensive data retention requirement that would have required financial institutions to collect and maintain detailed data for six years from the date of the applicable transactions. AR112 (now requiring them to maintain only records necessary to determine whether conditions of the exemption are met). It also eliminated a proposed pre-transaction disclosure that would have required a chart illustrating the total cost of the recommended investment for 1-, 5-, and 10-year periods expressed as a dollar amount. AR64, AR104-05 (now requiring disclosure focusing on financial institution's material conflicts of interest with more specific information to be provided upon request). DOL also eliminated the proposal's annual disclosure requirement and modified the website disclosure by minimizing the specificity of the information required. AR67, AR106.

Many of the changes, including some of those noted above, were made in response to concerns raised by the insurance industry. AR74; *see also* AR599. For instance, DOL revised the "reasonable compensation" standard throughout the exemption to match what is already required under other provisions of ERISA and the Code. AR74. To address concern that certain features of insurance products would be undervalued by this standard, DOL explained that "it is appropriate to consider the value of the guarantees and benefits in assessing the reasonableness

of the arrangement, as well as the value of the services." AR87.

DOL considered and rejected the suggestion that the definition of "financial institution" be expanded to include IMOs. AR123. DOL concluded that the definition, which determines the types of firms that can execute a best interest contract, should be limited to entities that are subject to well-established regulatory conditions and oversight. *Id.* Nevertheless, DOL provided that such entities could apply for an individual exemption and demonstrate "their ability to effectively supervise individual Advisers' compliance with the terms of this exemption." *Id.*[23] Under the BIC Exemption, an insurance company can continue to contract with IMOs or similar organizations to take on the supervisory responsibility required of financial institutions. *See* AR90 (final exemption was designed to allow flexibility so that financial institutions could design oversight procedures "that are effective for their particular business models").

DOL also recognized that insurance is sometimes sold by independent, state-licensed agents who represent multiple insurance companies. DOL required the responsible financial institution under the contract to assume responsibility for ensuring that the advice of such agents adheres to the standards. *See* AR95. Thus, if an insurance company executed the contract with a retirement investor, it would be responsible for adopting appropriate policies and procedures to ensure that the adviser's recommendations were in the investor's best interest and satisfied the other standards set out in the contract. Because the NAIC Model Regulation places the responsibility for establishing a system to oversee suitability on the insurance company, DOL concluded that the exemption was compatible with state insurance regulations. AR74-75. Like the proposal, the final BIC Exemption is available for recommendations on all annuities. AR73.

<u>Principal Transactions Exemption.</u> DOL also published another new exemption, the

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[23] Other IMOs may also rely on any individual exemption that is granted, provided they meet the same conditions. *See* BIC Exemption § VIII(e)(5); AR139.

Principal Transactions Exemption. AR158, 81 Fed. Reg. 21089 (Apr. 8, 2016). This exemption allows investment advice fiduciaries to engage in purchases and sales of certain investments out of their inventory for an employee benefit plan or IRA. *Id.* This primarily occurs in connection with bonds purchased by brokers. The terms of this exemption largely serve as an extension of the BIC Exemption, including its contract requirement, with some modification for the unique circumstances of these transactions. *See* AR202-08.

Amendment of PTE 84-24. Given that the BIC Exemption would be available to all annuities and many other products, DOL proposed to amend an existing exemption, PTE 84-24, 71 Fed. Reg. 5887 (Feb. 3, 2006), which had been available for insurance and annuity contracts. *See* AR785, 80 Fed. Reg. 22010. DOL proposed to revoke relief under this particular exemption for IRA transactions involving the purchase of mutual fund shares, variable annuity contracts, and other annuity contracts that are securities under federal securities laws, while leaving the exemption available for all annuity transactions involving ERISA plans and non-securities annuity transactions involving IRAs. AR788. DOL explained:

> The Department is not certain that the conditions of the Best Interest Contract Exemption, including some of the disclosure requirements, would be readily applicable to insurance and annuity contracts that are not securities, or that the distribution methods and channels of insurance products that are not securities would fit within the exemption's framework. While the Best Interest Contract Exemption will be available for such products, the Department is seeking comment in that proposal on a number of issues related to use of that exemption for such insurance and annuity products.
>
> The Department requests comment on this approach. *In particular, the Department requests comment on whether the proposal* to revoke relief for securities transactions involving IRAs (i.e., annuities that are securities and mutual funds) but leave in place relief for IRA transactions involving insurance and annuity contracts that are not securities *strikes the appropriate balance and is protective of the interests of the IRAs*.

AR790 (emphasis added). Likewise, DOL requested "comment on this approach" in the proposed BIC Exemption:

> In particular, we ask *whether we have drawn the correct lines between insurance and annuity products that are securities and those that are not*, in terms of our decision to continue to allow IRA transactions involving non-security insurance and annuity contracts to occur under the conditions of PTE 84–24 while requiring IRA transactions involving securities to occur under the conditions of this proposed Best Interest Contract Exemption.

AR747 (emphasis added). In response, several comments specifically recommended that FIAs be grouped with annuity contracts in the BIC Exemption.[24] Many commenters—including several of the Plaintiffs and their members—urged that variable annuities and FIAs be treated alike, preferably in PTE 84-24 or in a stand-alone exemption.[25] And both IALC and another group representing FIA providers urged DOL to maintain its proposal to allow advisers involved in FIA transactions to rely on PTE 84-24 and criticized parts of the proposed BIC Exemption.[26]

After carefully considering feedback received in response to its request for comments, DOL determined that PTE 84-24 should be available for the receipt of commissions for IRA and plan transactions only in connection with recommendations involving "fixed rate annuity contracts" as defined in the exemption. AR256, PTE 84-24 § VI(k). The definition does not include variable annuities, FIAs, or similar annuities; as a result, fiduciaries advising on these products can no longer rely on PTE 84-24 but must instead use the BIC Exemption if they wish to be exempted from the prohibited transaction provisions that would otherwise apply. AR227.

DOL explained that it reserved PTE 84-24 for simpler annuities that "provide payments that are the subject of insurance companies' contractual guarantees and that are predictable" and

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[24] *See, e.g.*, AR39096 (Cmt. 577, University of Miami Investor Rights Center) (arguing all annuities should come within the BIC Exemption), AR39272, 45700-01 (Cmts. 596 & 3017, Prof. Ron Rhoades), AR46847-53 (Cmt. 3090, Fund Democracy).

[25] *See, e.g.*, AR37553-54 (Cmt. 336, Voya Financial); AR37791-92 (Cmt. 429, Chamber of Commerce); AR38217-18 (Cmt. 506, SIFMA); AR40114-16 (Cmt. 626 Insured Retirement Inst.); AR41103, 41115-16 (Cmts. 676 & 3098, Nw. Mutual Life Ins. Co.); AR41633-38 (Cmt. 718, Allianz Life. Ins. Co.); AR42430-31 (Cmt. 767, Guardian Life Ins. Co.); AR46745-50 (Cmt. 3083, Jackson Nat'l Life Ins. Co.); AR46891-92 (Cmt. 3092, Prudential); AR60340-41 (Bradford Campbell, Chamber of Commerce at Aug. 11, 2015 Hr'g).

[26] *See, e.g.*, AR42359, 42376, 47030-41 (Cmts. 762 & 3111, NAFA); AR2540-41, 47074-78 (Cmts. 774 & 3124, IALC); *see also* AR60635 (Jim Poolman, IALC at Aug. 12, 2016 Hr'g).

that have "terms that are more understandable to consumers." AR232. By contrast, "[g]iven the complexity, investment risks, and conflicted sales practices associated with [variable annuities and FIAs], the Department ... determined that recommendations to purchase such annuities should be subject to the greater protections of the [BIC] Exemption." AR233. DOL further explained that "[b]oth categories of annuities, variable and indexed annuities, are susceptible to abuse, and [r]etirement [i]nvestors would equally benefit in both cases from the protections of [the BIC Exemption], including the conditions that clearly establish the enforceable standards of fiduciary conduct and fair dealing." AR234. By limiting the application of PTE 84-24, DOL explained that it was creating a level playing field for variable annuities, FIAs, and mutual funds and avoiding a regulatory incentive for advisers to preferentially recommend FIAs. *Id.*

Final Regulatory Impact Analysis. DOL also produced its final RIA of the rulemaking in April 2016. In conducting its analysis, DOL reviewed a wide body of economic evidence including statistical analyses of investor results in conflicted investment channels, experimental studies, government reports documenting abuse, and economic theory on the dangers posed by conflicts of interest. AR899-918, 961, 964. The IRA market in particular is replete with conflicts of interest between advisers and investors. Many investors do not know how much they are paying for advice or whether the advice is of high quality. The public comments and studies DOL reviewed provide persuasive evidence that conflicts of interest bias advisers' recommendations in ways that harm investors, and as a result, investors pay more and earn lower returns than they would in the absence of such conflicts. *See* AR412.

The analysis found that conflicted advice is widespread, causing serious harm to plan and IRA investors, and that disclosing conflicts alone would fail to adequately mitigate the conflicts or remedy the harm. AR324. For example, DOL found that IRA holders receiving conflicted investment advice can expect their investments to underperform by an average of one-half to one percent per year over the next 20 years. AR325. DOL estimated that the underperformance

associated with conflicts of interest—in the mutual funds segment alone—could cost IRA investors between $95 billion and $189 billion over the next 10 years. *Id.* DOL noted that while these expected losses are large, they represent only a portion of what retirement investors stand to lose as a result of adviser conflicts. *See id.*

By extending fiduciary status to more advice and providing flexible and protective exemptions that apply to an array of compensation arrangements, DOL concluded that the rulemaking will mitigate conflicts, support consumer choice, and deliver substantial gains for retirement investors and economic benefits that more than justify the costs. AR323; AR483-94 ("Gains to Investors"). DOL estimated that in the front-end-load mutual fund segment alone, investors could gain between $33 billion and $36 billion over 10 years. AR413, AR483. DOL concluded that these gains alone outweighed all of the expected costs of the rulemaking. AR413, AR484. With regard to annuities in particular, DOL requested data from the industry that it could use to quantify gains to investors in the insurance market, but the industry replied that it did not have such data. AR68906, 69063-66 (Dec. 15, 2011 letter to ACLI and response). Thus, DOL did not have sufficient data to quantify the gains for annuities but expected the rulemaking to create substantial net benefits for retirement investors. AR484. DOL reasoned that conflicts of interest in the annuity market are likely to be more pronounced than in the mutual fund market due to generally higher annuity commissions that are paid to insurance agents, which incentivize them to steer consumers toward certain products that are not in their best interest. *Id.*

Based on the available data and considering cost-saving revisions to the final BIC Exemption, DOL concluded that the total costs to retirement investment advice industry to comply with the rulemaking would be between $10 billion and $31.5 billion over 10 years with a primary estimate of $16.1 billion. AR326, AR535-68. On several occasions, DOL requested data from the regulated community that would allow it to quantify the costs of complying with the rulemaking with even greater precision. AR485, 522. The financial services industry,

namely the Securities Industry and Financial Markets Association ("SIFMA"), and the Financial Services Institute ("FSI"), provided largely unverifiable cost estimates. *See* AR522-26. DOL nevertheless considered this data, along with estimated start-up costs to complying with the rulemaking provided by two insurers, TIAA-CREF and Northwestern Mutual, while noting that SIFMA reports both firms and other insurers as members and could have included their costs in the SIFMA estimates. AR536 n.506, AR553. By giving the industry commenters the benefit of the doubt on their cost estimates, DOL likely considerably overestimated the costs associated with the rulemaking. AR326, AR522-26, AR623, AR634-40. In this way, and by not considering the benefits to consumers of mitigating conflicts of interest with respect to other investment products, or conflicts other than those associated with up-front fees, DOL took an extremely conservative approach in its cost-benefit analysis. *See* AR325.

In response to comments that costs to the insurance industry could be high, DOL attempted to quantify them, even though the industry had not provided much usable data. AR527. Using publicly available sources of information, DOL estimated the number of affected insurance companies and also determined which ones sold certain kinds of annuities. AR420. It also analyzed annuity sales by type of agent, and the role of IMOs and other intermediaries. AR418. It applied the cost data from brokers because insurers will have to perform similar tasks to comply with the rulemaking, even though the products they sell may vary. AR553. It concluded that the total costs for insurers to comply with the Rule and all of the new and amended exemptions, including the BIC Exemption, ranged from $1.1 billion to $1.3 billion over a ten year period. AR554, Fig. 5-11; *see also* AR564-66 (summaries for insurers and others using discount rates and various assumptions).

DOL also analyzed the impact of the rulemaking on affected small businesses as required by the Regulatory Flexibility Act, 5 U.S.C. §§ 601 *et seq*. AR570-74. Treating 99.3% of insurers as small entities based on the Small Business Administration's definition, it analyzed the

costs they would incur and discussed changes made in the rulemaking to reduce costs to large and small firms. AR571-76. It noted the possibility that some small service providers may find that the increased costs associated with ERISA fiduciary status outweigh the benefit of continuing to service the ERISA plan or IRA markets. AR574. DOL did not believe that this outcome would be widespread, however, or result in a diminution of the amount or quality of advice available to small or other retirement investors, as firms would fill the void for those markets. AR574. DOL also noted anecdotal evidence that small entities do not have as many business arrangements that give rise to conflicts of interest. *Id.*

In determining how best to mitigate conflicts in the market for retirement investment advice, DOL considered numerous alternatives. *See* AR578-608. Among them was extending the exclusion for transactions with certain plan fiduciaries who have financial expertise to include smaller plans, participants, and beneficiaries, AR580; basing exemptive relief on disclosure alone, AR584; and allowing FIAs to rely on PTE 84-24, AR598. DOL ultimately concluded, based on all of the data it considered, that none of the alternatives would protect retirement investors as effectively and efficiently as the rulemaking. AR612.

<u>Effective and Applicability Dates.</u> The rulemaking became effective on June 7, 2016 and is applicable beginning on April 10, 2017. In response to comments, DOL also provided an additional transition period, until January 1, 2018, for financial institutions and advisers to attain full compliance with all of the conditions of the new exemptions. AR607-08. During the transition period, financial institutions and advisers will be able to rely on the BIC Exemption and Principal Transactions Exemption subject to more limited conditions. *See, e.g.*, BIC Exemption § IX, AR125, 140. Namely, during that time, they will not be required to enter into the best interest contract or affirmatively warrant that they have adopted and will comply with written policies and procedures reasonably and prudently designed to ensure that advisers adhere to the impartial conduct standards and provide required disclosures. AR140-41.

III. PROCEDURAL HISTORY

In June 2016, Plaintiffs filed in this district three separate complaints challenging the rulemaking. Compl., *Chamber of Commerce v. Perez*, No. 3:16-01476-M (June 1, 2016) ("Chamber" plaintiffs); Compl., *Am. Council of Life Insurers v. Dep't of Labor*, No. 3:16-01530-C (June 8, 2016) ("ACLI" plaintiffs); Compl., *Indexed Annuity Leadership Council v. Perez*, No. 3:16-1537-N (June 8, 2016) ("IALC" plaintiffs).[27] On June 17, 2016, Defendants filed an unopposed motion to consolidate the three cases in this district, ECF No. 37, which the Court granted on June 21, 2016. ECF No. 43. On July 7, 2016, this Court granted the parties' joint motion to establish a schedule for summary judgment proceedings. ECF No. 45.

ARGUMENT

The rulemaking seeks to mitigate inherent conflicts of interest that arise when advisers' compensation is linked to products, like mutual funds or annuities, they recommend to ensure that retirement investors get impartial investment advice. DOL acted well within its authority in promulgating these protections and provided a reasoned explanation for its decision to do so.

"[W]hen a district court reviews a summary judgment motion concerning an agency's action, the court determines not whether the material facts are disputed, but whether the agency properly dealt with the facts." *Garcia for Congress v. FEC*, 22 F. Supp. 3d 655, 658 (N.D. Tex. 2014). This is a "modified standard" to decide "the legal question of whether an agency could reasonably have found the facts as it did." *Triplett v. Fed. Bureau of Prisons*, No. 3:08-1252, 2009 WL 792799, at *7 (N.D. Tex. 2009). Under this standard, for the reasons detailed below, there is no legal basis for Plaintiffs' requested relief, and Defendants are entitled to summary judgment on all of Plaintiffs' claims.

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[27] Two other cases have been filed challenging the Conflict of Interest Rule and/or these exemptions. *See* Compl., *Market Synergy Group, Inc. v. U.S. Dep't of Labor*, No. 5:16-4083 (D. Kan. Jun. 8, 2016); Compl., *Nat'l Ass'n for Fixed Annuities v. Perez*, No. 1:16-1035 (D.D.C. Jun. 2, 2016).

I. THE DEPARTMENT'S INTERPRETATION OF FIDUCIARY "INVESTMENT ADVICE" IS REASONABLE AND ENTITLED TO DEFERENCE

"Filling [statutory] gaps … involves difficult policy choices that agencies are better equipped to make than courts." *Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs.* ("*Brand X*"), 545 U.S. 967, 980 (2005) (citing *Chevron, U.S.A., Inc. v. NRDC*, 467 U.S. 837 (1984)). Accordingly, it is well-established that "ambiguities in statutes within an agency's jurisdiction to administer are delegations of authority to the agency to fill the statutory gap in reasonable fashion." *Id.* And courts "may not disturb an agency rule unless it is arbitrary or capricious in substance, or manifestly contrary to the statute." *Mayo Found. for Med. Educ. & Research v. United States*, 562 U.S. 44, 53 (2011). *Chevron* deference applies, moreover, even where an agency revises its previous interpretation, so long as the agency "display[s] awareness that it is changing position, and show[s] that there are good reasons for the new policy." *Encino Motorcars, LLC v. Navarro*, 136 S. Ct. 2117, 2125-26 (2016).

In enacting ERISA, Congress gave DOL the authority to "prescribe such regulations as ... necessary or appropriate to carry out the [relevant] provisions," including to "define accounting, technical and trade terms used in" the Act. 29 U.S.C. § 1135. Congress also adopted a broad definition of "fiduciary" to allow DOL to "consider varying interpretations and the wisdom of its policy on a continuing basis," *Brand X*, 545 U.S. at 981, to serve ERISA's "broadly protective purposes." *John Hancock Mut. Life Ins. Co. v. Harris Trust & Sav. Bank*, 510 U.S. 86, 96 (1993). In exercise of that discretion, DOL promulgated a reasonable interpretation of fiduciary "investment advice" that comports with the text, history, and purposes of ERISA. That reasonable interpretation is entitled to deference. *Chevron*, 467 U.S. at 837.

A. Congress Adopted a Broad "Fiduciary" Definition, Delegating to DOL the Discretion to Interpret "Investment Advice" to Serve ERISA's Remedial Purposes

"Statutory interpretation … begins with the text." *Ross v. Blake*, 136 S. Ct. 1850, 1856 (2016). Here, ERISA's statutory language demonstrates that Congress cast a wide net in

assigning fiduciary status to persons involved in three separate functions—management, investment advice, and administration—related to retirement plans:

> [A] person is a fiduciary with respect to a plan to the extent (i) he exercises *any* discretionary authority or discretionary control respecting management of such plan or exercises *any* authority or control respecting management or disposition of its assets, (ii) he renders investment advice for a fee or other compensation, direct or indirect, with respect to *any* moneys or other property of such plan, or has *any* authority or responsibility to do so, *or* (iii) he has *any* discretionary authority or discretionary responsibility in the administration of such plan.

29 U.S.C. § 1002(21)(A) (emphasis added); 26 U.S.C. § 4975(e)(3) (largely same). Congress emphasized the intended breadth of the statutory definition by repeating the word "any" in each prong and by including the disjunctive "or." Courts have thus recognized that Congress "commodiously imposed fiduciary standards on persons whose actions affect the amount of benefits retirement plan participants will receive." *John Hancock*, 510 U.S. at 96.[28] Moreover, as Plaintiffs concede, *see* Chamber Br. 14, Congress did not cabin DOL's discretion by providing a precise definition of what it means to "render[] investment advice for a fee or other compensation, direct or indirect." Instead, the plain language is susceptible to multiple reasonable interpretations, and Congress left to DOL the responsibility to further define it.

The definition DOL adopted fits comfortably within an ordinary understanding of the text. A standard dictionary definition of *advice* is "an opinion or recommendation offered as a guide to action, conduct, etc.," and of *investment* is "the investing of money or capital in order to gain profitable returns." *The Random House Dictionary of the English Language* (2d ed. 1987). Consistent with those capacious outer boundaries, the Rule defines "investment advice" in terms of specified "recommendations" to a particular advisee as to, *inter alia*, "the advisability of

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[28] *See also Arizona State Carpenters Pension Tr. Fund v. Citibank (Arizona)*, 125 F.3d 715, 720 (9th Cir. 1997) ("ERISA … requires a broad definition of fiduciary … to be construed liberally."); *Farm King Supply, Inc. Integrated Profit Sharing Plan & Tr. v. Edward D. Jones & Co.*, 884 F.2d 288, 293 (7th Cir. 1989) ("'The broadness of the definition [of fiduciary] is readily apparent.'"); *Donovan v. Mercer*, 747 F.2d 304, 308 (5th Cir. 1984) ("It is clear that Congress intended the definition of "fiduciary" under ERISA to be broadly construed.").

acquiring, holding, disposing of, or exchanging," or "the management of," "securities or other investment property." 29 C.F.R. § 2510.3–21(a)(1)(i)-(ii). The Rule further defines a "recommendation" as "a communication that, based on its content, context, and presentation, would reasonably be viewed as a suggestion that the advisee engage in or refrain from taking a particular course of action." § 2510.3–21(b)(1). And consistent with the statutory language, the Rule limits its application to advice resulting in "compensation" and concerning "property of [a] plan." § 2510.3–21(a). A paid suggestion to an advisee to take a particular course of action with respect to his or her investment property readily comports within an ordinary understanding of what it means to "render[] investment advice for a fee or other compensation, direct or indirect."

B. None of Plaintiffs' Arguments Demonstrates that the Statute Unambiguously Forecloses DOL's Interpretation of "Investment Advice"

Plaintiffs make six primary arguments in contending that DOL's interpretation fails at *Chevron* step one; however, none of them undermine, much less "unambiguously foreclose," DOL's interpretation, as required to meet the "demanding *Chevron* step one standard" to overcome an agency's interpretation. *Brand X*, 545 U.S. at 982-83.

First, Plaintiffs argue that DOL's interpretation is foreclosed by their understanding of the common law of trusts, which they argue limits fiduciary relationships to those with a "special degree of 'trust and confidence.'" Chamber Br. 15. Setting aside whether Plaintiffs' understanding of the common law is correct, Congress did not confine the fiduciary definition to the common law of trusts; instead, as the Supreme Court has recognized, Congress took an "express statutory departure" from the common law understanding of "fiduciary," adopting a "functional" definition, rather than one based on formal trusteeship. *Mertens v. Hewitt Associates*, 508 U.S. 248, 264 (1993). In this way, Congress did not limit fiduciary status to the common law understanding of that term but sought to "expand[] the universe of persons subject to fiduciary duties," *id.* at 262, to effectuate ERISA's protective purposes. *John Hancock*, 510

U.S. at 96; *see also Donovan v. Cunningham*, 716 F.2d 1455, 1464 n.15 (5th Cir. 1983) ("ERISA's modifications of existing trust law include imposition of duties upon a broader class of fiduciaries."); 120 Cong. Rec. 3977, 3983 (1974) (Rep. Perkins) ("The Committee has adopted the view that the definition of fiduciary is of necessity broad.... This is a departure from current judicial precedents but is necessary to the proper protection of these plans." (explaining bill with definition ultimately adopted in conference version of ERISA)).[29]

It is not unusual for Congress to adopt a common law term but define it differently for purposes of a statute, even where the statute elsewhere codifies common law concepts, *see, e.g., Middleburg Volunteer Fire Dep't, Inc. v. McNeil & Co.*, 60 F. Supp. 3d 640, 651 (E.D. Va. 2014) (recognizing important difference in statutory definition of "accord and satisfaction" even where statute largely codified common law doctrine of accord and satisfaction); *Donovan v. Tastee Freeze (Puerto Rico), Inc.*, 520 F. Supp. 899, 902 (D.P.R. 1981) (construing definitions of "employee" and "employer" in the Fair Labor Standards Act without reference to common law principles or test). And where Congress in ERISA explicitly adopted an "artificial definition of 'fiduciary,'" *Mertens*, 508 U.S. at 255 n.5, that departed from the common law understanding of that term, the statutory definition prevails. *Ry. Express Agency, Inc. v. R.R. Ret. Bd.*, 250 F.2d 832, 837 (7th Cir. 1958) ("If there is any real difference between the generally accepted common law tests and the statutory definition, the latter must prevail."); *Hartline v. Sheet Metal Workers' Nat'l Pension Fund*, 134 F. Supp. 2d 1, 10-11 (D.D.C. 2000) ("[I]n determining whether a party

[29] *See also Smith v. Provident Bank*, 170 F.3d 609, 613 (6th Cir. 1999) ("[T]he definition of a fiduciary under ERISA is a functional one, is intended to be broader than the common law definition, and does not turn on formal designations such as who is the trustee."); *Arizona*, 125 F.3d at 720 (ERISA defines fiduciary "not in terms of formal trusteeship, but in functional terms[.]"); *Custer v. Pan Am. Life Ins. Co.*, 12 F.3d 410, 418 n.3 (4th Cir. 1993) (ERISA's definition of fiduciary is "broader than the common law concept of a trustee"); *Ellis v. Rycenga Homes, Inc.*, 484 F. Supp. 2d 694, 703 (W.D. Mich. 2007) ("The definition of a fiduciary under ERISA is a functional one.... It is intended to be broader than the common-law definition and does not turn on formal designations or labels."); *Hunter v. Metro. Life Ins. Co.*, 251 F. Supp. 2d 107, 112–13 (D.D.C. 2003) ("In ERISA, Congress took a functional approach towards defining who would be treated as a fiduciary.").

acts as a fiduciary," the D.C. Circuit "look[s] only to ERISA" not "the common law of trusts." (citing *Systems Council EM–3 v. AT & T Corp.*, 159 F.3d 1376, 1379 (D.C. Cir. 1998)).[30] DOL thus need not have confined its interpretation of fiduciary "investment advice" to those relationships recognized as fiduciary under the common law, and Plaintiffs' proposed reading is contrary to Congress's intent to extend fiduciary status to a broader class of relationships.

Second, Plaintiffs argue that DOL's interpretation is foreclosed because it does not recognize the securities law distinction between investment advisers, who are fiduciaries, and brokers, who are not. *See* Chamber Br. 15-16. The statutory text and legislative history demonstrate that this distinction has no place in ERISA. Tellingly, to create the distinction Plaintiffs identify, Congress in the Advisers Act "define[d] 'investment adviser' broadly *and* create[d] ... a precise exemption for broker-dealers." *Fin. Planning Ass'n v. SEC*, 482 F.3d 481, 489 (D.C. Cir. 2007) (emphasis added); *see* 15 U.S.C. § 80b-2(a)(11).[31] Had Congress intended to adopt the same distinction in ERISA, presumably it would have done so expressly, as it did in the Advisers Act, by including a similar exemption. *See FCC v. NextWave Pers. Commc'ns Inc.*, 537 U.S. 293, 302 (2003) ("[W]here Congress has intended to provide regulatory exceptions to provisions ... it has done so clearly and expressly."). Because there is no such exemption in ERISA, one can presume that Congress did not mean to limit the investment advice prong of the

[30] DOL does not disagree with Plaintiffs that "Congress incorporated principles of trust law into ERISA," or that Congress was "familiar[] with the meaning of 'fiduciary' under the law of trusts." Chamber Br. 17. But as demonstrated above, while Congress incorporated principles of trust law into other parts of ERISA, Congress knowingly and expressly departed from the common law meaning of fiduciary in ERISA. As a result, the judicial gloss Plaintiffs attempt to apply to the fiduciary definition does not stick where Congress "affirmatively act[ed] to change the meaning" of the existing interpretation. *Blitz v. Donovan*, 740 F.2d 1241, 1245 (D.C. Cir. 1984).

[31] The Advisers Act defines an "investment adviser" as "any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities." 15 U.S.C. § 80b–2(a)(11). The definition then goes on to expressly exclude from the definition of "investment adviser" "any broker or dealer whose performance of such services is solely incidental to the conduct of his business as a broker or dealer and who receives no special compensation therefor." *Id.* § 80b–2(a)(11)(C).

fiduciary definition in such a way. *See Burlington N. & Santa Fe Ry. Co. v. White*, 548 U.S. 53, 63 (2006) ("We normally presume that, where words differ …, Congress acts intentionally and purposely in the disparate inclusion or exclusion.").[32] In enacting ERISA, Congress specifically referred to the Advisers Act when it created an exception to the requirement that plan trustees have exclusive authority and control over plan assets. 29 U.S.C. §§ 1002(38)(B), 1103(a)(2). Yet, it did not refer to the Adviser's Act when it defined a fiduciary as someone who renders investment advice for compensation. Thus, while Congress understood this legal backdrop, it chose not to limit fiduciaries in ERISA to those covered by the Advisers Act.[33]

Third, Plaintiffs argue that the "plain meaning of the phrase 'renders investment advice for a fee'" requires a distinction between those paid for "merely selling a product" and those paid to render investment advice. Chamber Br. 17. This argument fails for multiple reasons. To begin, Plaintiffs mischaracterize the Rule by suggesting that it applies fiduciary status to those who merely sell a product. *Id.* It does not. The Rule makes clear that where an individual merely sells a product, and does not render investment advice by way of specified recommendations, he is not a fiduciary under the Rule. AR26 ("[W]hether a 'recommendation' has occurred is a threshold issue and the initial step in determining whether investment advice has occurred."); AR39 ("[I]n the absence of a recommendation, nothing in the [Rule] would make a person an investment advice fiduciary merely by reason of selling a security or investment property to an interested buyer.").[34] Whether a recommendation occurs is an objective inquiry, determined by asking whether, based on its content, context, and presentation,

[32] For this reason, the case law Plaintiffs cite on page 16 of their brief is inapposite, as it relies on the express exclusion from the definition of an "investment adviser" brokers whose advice is "incidental to the conduct of [their] business" as brokers. 15 U.S.C. § 80b–2(a)(11)(C).

[33] Moreover, ERISA's investment advice prong does not single out securities, but instead applies to any investment using "moneys or other property" of a retirement plan. 29 U.S.C. § 1002(21)(A); 26 U.S.C. § 4975(e)(3).

[34] Relatedly, subsection (d) of the 1975 regulation, which is preserved in paragraph (e) of the Rule, continues to provide that a broker dealer is not a fiduciary solely by reason of executing specific orders. 29 CFR 2510.3–21(e).

it reasonably would be viewed as a suggestion to a retirement investor to take a particular course of action with regard to investment property. 29 C.F.R. § 2510.3–21(b)(1). Once a person crosses that line, he is no longer "merely sell[ing] a product"; he is rendering investment advice.

Moreover, while Plaintiffs truncate the relevant clause, *see* Chamber Br. 17, nothing in the broad statutory text—which includes a person who "renders investment advice for a fee *or other compensation, direct or indirect*"—29 U.S.C. § 1002(A)(21)(ii)—indicates that compensation must be paid principally for investment advice, as opposed to for advice rendered in the course of a broader sales transaction. DOL has thus long interpreted that language to include commissions for advice incidental to a sales transaction, *see* 40 Fed. Reg. 50842 (Oct. 31, 1975) (statutory term includes "brokerage commissions, mutual fund sales commissions, and insurance sales commissions"); DOL Advisory Opinion 83–60A (Nov. 21, 1983) (Defs.' App'x 1) (statutory term includes "all fees or compensation incident to the transaction in which investment advice to the plan has been or will be rendered"), and courts have widely agreed. *See Farm King Supply*, 884 F.2d at 291-92 ("those who render investment advice for a fee" include "stock brokers and dealers who recommend certain securities and then participate in the acquisition or disposition of those securities and receive a commission for their services"); *Thomas, Head & Griesen Emps. Trust v. Buster*, 24 F.3d 1114, 1120 (9th Cir. 1994) (commission received on sale of notes to plan meets direct or indirect fee requirement); *Eaves v. Penn*, 587 F.2d 453, 458 (10th Cir. 1978) (investment advice prong "includes … stock brokers or dealers who recommend certain securities and then participate in the acquisition or disposition of those securities and receive a commission for their services."); *Ellis*, 484 F. Supp. 2d at 710 (rejecting as "untenable" broker's argument that it was paid only "commissions for sales, not a fee for investment advice" and that "the advice ... was free"); *Brock v. Self*, 632 F. Supp. 1509, 1520 n.11 (W.D. La. 1986) (sufficient that third-party defendants were "at least indirectly

compensated for the investment advice which they rendered" as part of a "package deal").[35]

In addition, Plaintiffs' own statements contradict their assertion that "[a]n agent who receives a commission on the sale of a product is not paid for 'render[ing] investment advice.'" Chamber Br. 17. ACLI emphasized both during the rulemaking process and in its filings in this case that the significant advisory role insurance agents and brokers play in the course of selling annuities in part justifies the commission they receive:

> [I]nsurers, agents and brokers … must introduce savers and retirees to annuities, help them to understand the value proposition, and educate them on the variety of annuities available with features that can address concerns regarding liquidity, inflation, premature death, etc. Given the need for a high level of education about annuities … it is important that [DOL] recognize that these elements led to the customary compensation practices in place which differ from those that govern the sale of other types of investments or investment advisory and management services.

AR 39731 (Cmt. 621, ACLI). And again:

> Insurance agents and broker-dealers ... help consumers assess whether an annuity is a good choice and, if so, which type of annuity and optional features suit consumers' financial circumstances…. Effectively informing consumers about annuities thus often requires a more involved conversation than is required to sell other financial products. For these reasons, … insurers typically pay a sales commission to compensate agents and broker-dealers for the significant effort involved in learning about, marketing, and selling annuities.

ACLI Br. 4-5. These commissions thus easily fit within the statutory (and identical regulatory) language providing that a fiduciary includes one who renders investment advice "for ... *indirect*" compensation. 29 U.S.C. § 1002(21)(A)(ii); 29 C.F.R. § 2510.3-21(a)(1). In sum, neither the

[35] Plaintiffs selectively quote from inapposite authority in an effort to support the proposition that "[s]imply urging the purchase of [a] products does not make an [insurance company] an ERISA fiduciary with respect to those products." Chamber Br. 18 (citing *Am. Fed'n of Unions Local 102 Health & Welfare Fund v. Equitable Life Assur. Soc. of the U.S.*, 841 F.2d 658, 664 (5th Cir. 1988)). Read in context, it is clear that the Fifth Circuit came to that conclusion by relying on the 1975 regulation's narrower five-part, as it stated that "[m]erely giving advice to self-insure does not make Equitable a fiduciary within the meaning of [§ 1002(21)(A)(ii)] *because the advice was not given on a regular basis pursuant to a mutual agreement for a fee*." *Am. Fed'n of Unions*, 841 F.2d at 664 (emphasis added). As noted, the 1975 regulation required, *inter alia*, that advice be given "on a regular basis" and "pursuant to a mutual agreement." 29 C.F.R. § 2510.3–21(c)(1) (2015); 26 C.F.R. § 54.4975-9 (2015).

statutory language, nor current marketplace realities, supports limiting the fiduciary definition to those paid principally for investment advice, rather than as part of a broader sales transaction.[36]

Fourth, Plaintiffs argue that, unlike DOL's interpretation, the fiduciary definition in ERISA requires advice to be "provided on a regular basis and through an established relationship." Chamber Br. 19. Plaintiffs' argument is based on their assertion that the other two prongs of the fiduciary definition require a "meaningful, substantial, and ongoing relationship." *Id.* This is incorrect. The first and third prongs of the fiduciary definition, like the second, are broad, and deem a person a fiduciary if he has "*any* discretionary authority or discretionary control respecting management of [a] plan" or "*any* discretionary authority or discretionary responsibility in the administration of [a] plan." 29 U.S.C. § 1002(21)(A)(i), (iii). *See, e.g., Bannistor v. Ullman*, 287 F.3d 394, 411 (5th Cir. 2002) ("The definition of 'fiduciary' is phrased broadly: it extends to anyone who exercises 'any' authority or control." (Garza, J., specially concurring) (citing *Am. Fed'n of Unions Local 102*, 841 F.2d at 662)).[37] Moreover, in light of Congress's goal to extend fiduciary status broadly, Plaintiffs' attempt to read into the definition a limitation that does not exist is particularly ill-advised. *See Hardt v. Reliance Standard Life Ins. Co.*, 560 U.S. 242, 252 (2010) (placing a limitation in a statute that is "conspicuously absent more closely resembles inventing a statute rather than interpreting one").[38]

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[36] During the rulemaking, some of Plaintiffs' members and others advocated for a broad "seller's" carve-out from the fiduciary definition. DOL expressly declined to adopt such a broad carve-out and for good reason, as it found that sales and investment advice go hand-in-hand, and the requested carve-out would "run the risk of creating a loophole that … could be used by financial service providers to evade fiduciary responsibility for their advice through ... boilerplate disclaimers." AR36.

[37] Even if the first and third prongs could be read to require an ongoing relationship, as Plaintiffs suggest, the second prong "is different" and need not include such a requirement. *Ellis*, 484 F. Supp. 2d at 711. For example, the first and third prongs focus on authority and control, but that is expressly not required for the second prong. *See id.*, ("Subsection (ii) … is different…. On its face, it requires only that the fiduciary render investment advice for a fee or other compensation, direct or indirect, with respect to plan assets.").

[38] As DOL explained, the regular basis requirement in the five-part test (which Plaintiffs attempt to resuscitate here) served to undermine ERISA's protective purposes because episodic advice can have a significant impact on a retiree's income. *See* AR10 (regular basis requirement has led to highly consequently investment decisions being based on investment advice not subject to fiduciary protections).

Fifth, Plaintiffs contend that in section 913(g) of the Dodd-Frank Act, "Congress prohibited the SEC … from creating a [fiduciary] standard … that banned commissions." Chamber Br. 19. On that basis, Plaintiffs argue that it is "implausible" that Congress would have taken such action "while leaving DOL free to adopt an interpretation with that exact consequence." *Id.* There are many problems with this argument. To begin, DOL's rulemaking does not "ban[] commissions"; instead, it is the long-standing prohibited transaction provisions in ERISA and the Code that prohibit fiduciaries from receiving conflicted commissions. 29 U.S.C. § 1106; 26 U.S.C. § 4975(c). The rulemaking specifically provides *exemptions* from those provisions to *allow* the industry to continue to receive customary forms of compensation, such as commissions. AR46. Moreover, setting aside the fact that § 913(g) of the Dodd-Frank Act evinces an intent to *expand* fiduciary standards, as well as the fact that Congress's direction to the SEC has no bearing on DOL's authority under ERISA, the most fundamental problem with Plaintiffs' argument is that Congress's passage of § 913(g) in 2010 says little to nothing about what Congress intended when it adopted the fiduciary definition in ERISA in 1974. *See Mackey v. Lanier Collection Agency & Serv., Inc.*, 486 U.S. 825, 839 (1988) (noting in the ERISA context that "the opinion of this later Congress as to the meaning of a law enacted 10 years earlier does not control the issue" (citing *United Airlines, Inc. v. McMann*, 434 U.S. 192, 200 n.7 ("'[T]he views of a subsequent Congress form a hazardous basis for inferring the intent of an earlier one.'")).

Sixth, Plaintiffs incorrectly argue that Congress has implicitly "ratified" the 1975 regulation's interpretation of an investment advice fiduciary where it has "amended ERISA many times" without amending the fiduciary definition. Chamber Br. 19. "As a general matter," arguments based on such congressional inaction "deserve little weight in the interpretive process." *Cent. Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 187 (1994). And while courts "have recognized congressional acquiescence to administrative

interpretations of a statute in some situations, [they] have done so with extreme care." *Solid Waste Agency of N. Cook Cty. v. U.S. Army Corps of Eng'rs*, 531 U.S. 159, 169 (2001). Accordingly, where Congress has not "re-enact[ed] a statute without change," *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353, 382 n.66 (1982), or "amended … *the relevant provisions*," *Barnhart v. Walton,* 535 U.S. 212, 220 (2002) (emphasis added), the notion of congressional ratification is of little assistance in interpreting a statute. Plaintiffs point to only one amendment, which merely "adopted a new statutory exemption applicable to investment advice." Chamber Br. 19 (citing Pension Protection Act of 2006, Pub. L. 109-280, 120 Stat. 780 (2006)). Such action is insufficient to show congressional ratification. *Cf. AFL-CIO v. Brock*, 835 F.2d 912, 915 (D.C. Cir. 1987) (requiring "express congressional approval of an administrative interpretation if it is to be viewed as statutorily mandated").

At bottom, Plaintiffs attempt to impose non-textual limits on the fiduciary definition in contravention of Congress's intent to apply fiduciary status broadly to effectuate ERISA's protective purposes and fail to satisfy the demanding standard to overturn DOL's interpretation.

C. DOL's Interpretation of "Investment Advice" is a Reasonable Construction of the Statutory Language that Comports with the Text, History, and Purposes of ERISA

Because Plaintiffs have failed to show that DOL's interpretation is unambiguously foreclosed by the statute, DOL's interpretation is entitled to deference so long as it is reasonable. *Chevron*, 467 U.S. at 843. In light of the text, history, and purposes of ERISA, the Rule's interpretation of "investment advice" easily meets this standard.

As explained, the Rule's definition of "investment advice" in terms of specified "recommendations" to a particular advisee regarding the use of "investment property" that results in compensation to the adviser, 29 C.F.R. § 2510.3-21(a), (b), readily comports with an ordinary understanding of what it means to "render[] investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan." 29

U.S.C. § 1002(21)(A); 26 U.S.C. § 4975(e)(3). Plaintiffs point to nothing in the legislative history that compels a different reading of the statute. *See, e.g.*, H.R. Rep. No. 93-1280 (1974) (Conf. Rep.), as reprinted in 1974 U.S.C.C.A.N. 5038, 5103 (simply stating that the "term 'fiduciary' also includes any person who renders investment advice for a fee").

In addition, DOL's interpretation of "investment advice" serves ERISA's broad remedial purposes by protecting against activities that pose the precise harms Congress enacted the statute to avoid. *See John Hancock*, 510 U.S. at 86 (noting ERISA's "broad purpose of protecting retirement benefits"). Such a "[r]emedial statute[] [is] to be construed liberally," in particular "in an era of increasing individual participation in [the] market." *R&W Tech. Servs. Ltd. v. Commodity Futures Trading Comm'n*, 205 F.3d 165, 173 (5th Cir. 2000); *see also Landry v. Air Line Pilots Ass'n Int'l AFL-CIO*, 892 F.2d 1238, 1251 (5th Cir. 1990) (ERISA is to be given "a liberal construction … in keeping with its remedial purposes"). As DOL explained, most retirement investors today no longer participate in defined benefit plans, "where their employer has both the incentive and fiduciary duty to facilitate sound investment choices"; instead, most now have individual account-based plans for which they make their own choices and rely on advisers in a market where "both good and bad investment choices are myriad and [conflicted] advice ... is commonplace." AR703. The Rule thus aligns the definition of investment advice with today's marketplace realties and ensures, consistent with ERISA's text and congressional intent, that fiduciary status applies to "persons whose actions affect the amount of benefits retirement plan participants will receive." *John Hancock*, 510 U.S. at 96.

None of Plaintiffs' arguments, which largely rely on premises DOL has debunked above, undermines the reasonableness of the Rule's definition.[39] For instance, Plaintiffs attack the

[39] For example, Plaintiffs repeat the argument that the Rule rejects the "statutory" dichotomy between sales and advice. Chamber Br. 22. If the statutory dichotomy were in the *relevant* statute or Plaintiffs had provided some indication that Congress intended to adopt such a dichotomy in ERISA, their argument might be relevant; but a dichotomy recognized in another statute effected by adopting an express exclusion from a statutory definition is

(*footnote continued on next page*)

Rule's definition on the basis that it will extend fiduciary status where there is "[n]o regular contact," "nor any indicator of a relationship of trust and confidence." Chamber Br. 20. Yet, nothing in the statutory text requires that investment advice be provided on a regular basis, and it is Plaintiffs' position that would lead to an unreasonable result. As DOL explained, the "regular basis" requirement in the 1975 regulation no longer aligns with congressional intent in light of today's market realities and could result in fiduciary protections failing to extend to transactions that could have significant consequences for retirement investors. *See* AR10. For example:

> [I]f a small plan hires an investment professional on a one-time basis for an investment recommendation on a large, complex investment, the adviser has no fiduciary obligation to the plan under [the 1975 regulation]. Even if the plan is considering investing all or substantially all of the plan's assets, lacks the specialized expertise necessary to evaluate the complex transaction on its own, and the consultant fully understands the plan's dependence on his professional judgment, the consultant is not a fiduciary because he does not advise the plan on a "regular basis." The plan could be investing hundreds of millions of dollars in plan assets, and it could be the most critical investment decision the plan ever makes, but the adviser would have no fiduciary responsibility under the 1975 regulation. While a consultant who regularly makes less significant investment recommendations to the plan would be a fiduciary if he satisfies the other four prongs of the regulatory test, the onetime consultant on an enormous transaction has no fiduciary responsibility.

Id. Such a result is also at odds with congressional intent, as evidenced by ERISA's broad definition of fiduciary, which was meant to ensure that those having such influence over, and responsibility for, retirement investment decisions are acting in the interest of advisees and held accountable for their advice. *See Woodfork v. Marine Cooks & Stewards Union*, 642 F.2d 966, 969 (5th Cir. 1981) ("One of the purposes of ERISA is to protect ... the interests of participants in employee benefit plans ... by establishing standards of conduct, responsibility, and obligation for fiduciaries of employee benefit plans, and by providing for appropriate remedies….").

Moreover, Plaintiffs' argument that the Rule's definition improperly extends fiduciary

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irrelevant for purposes of interpreting a definition in ERISA, which did not adopt such an exclusion.

status where there is no "indicator of a relationship of trust and confidence," Chamber Br. 20, has it precisely backwards: Congress did not limit fiduciary status to those already in relationships of trust and confidence under the common law; instead, Congress identified those persons whose activities impact Americans' retirement security and artificially *created* a fiduciary relationship. Thus, far from limiting fiduciary status to relationships recognized as fiduciary under pre-existing law, Congress designed the functional definition of fiduciary to address deficiencies in the previous protections for Americans' retirement savings. *See, e.g., Varity Corp. v. Howe*, 516 U.S. 489, 497 (1996) ("ERISA's standards and procedural protections partly reflect a congressional determination that the common law of trusts did not offer completely satisfactory protection."); 120 Cong. Rec. 29928, 29932 (Aug. 22, 1974) (Senator Harrison Williams Jr., introducing ERISA conference report) ("Neither existing State nor Federal law has been effective in preventing or correcting many of … abuses" such as "self-dealing, imprudent investing, and misappropriation of plan funds[.]"); S. Rep. No. 92-1150 (Aug. 18, 1972) (recognizing that federal regulation was needed due to the insufficiencies of the common law of trusts); 120 Cong. Rec. 3977, 3983 (1974) (Rep. Perkins) (broader definition of fiduciary was necessary to the proper protection of employee benefit plans). Plaintiffs' position, which would appear to require a showing that a particular adviser-advisee relationship would constitute a fiduciary relationship under the common law of trusts, would lead to the anomalous result of reverting to pre-existing law from which Congress expressly departed.

For these reasons, there is also no credence to Plaintiffs' argument that DOL's authority "depends on a factual showing that those providing [investment] advice are *actually* in relationships of trust and confidence." IALC Br. 14. The statute applies industry-wide to those who "render[] investment advice," rather than requiring individual showings for different types

of participants in the retirement advice market.[40] And DOL need not assess common law "factors" to "determin[e]" whether a person who renders investment advice would be a fiduciary under the common law, *see* IALC Br. 14-15, given Congress's express adoption of a standard that applies fiduciary status more broadly than the common law. *See supra* Stmt. of Facts § I(A).

It is nevertheless striking that Plaintiffs wish to maintain their ability to disclaim fiduciary status, even in situations where retirement investors *do* rely on them for trusted investment advice. As Plaintiffs acknowledge in a footnote, IALC Br. 18 n.7, a 2010 survey of American investors reported that upwards of 60% of investors incorrectly believe stockbrokers and insurance agents already must comply with fiduciary duties requiring them to put their clients' interests first. *See* AR498 n.412; AR10361 (Sept. 15, 2010 joint letter from AARP, et al., to the SEC). Plaintiffs suggest that their clients' expectations are irrelevant and that advisers should be able to act in self-interested ways so long as they do not "accept" the trust their clients place in them. *See* IALC Br. 18 n.7 (advancing Plaintiffs' interpretation of common law doctrines about mutual acceptance to avoid fiduciary status). ERISA's statutory language imposes no such limitation, and Plaintiffs' suggestion confirms DOL's dissatisfaction with the 1975 regulation under which advisers could take advantage of their unilateral desire to avoid rendering advice in investors' best interests, despite fostering the impression that they are doing so. *See* AR10 (under the five-part test's "mutual understanding" requirement, "[i]nvestment professionals … frequently market [their] services in ways that clearly suggest the provision of

[40] During the rulemaking, DOL specifically rejected the premise that the Rule must limit fiduciary status to those in relationships that "have the hallmarks of a trust relationship," noting that ERISA's text extends fiduciary status to a broader set of relationships. AR45. Thus, DOL did not "concede[] that it can regulate only activities that 'implicate relationships of trust,'" as Plaintiffs suggest, IALC Br. 13, and the statements Plaintiffs cite do not show otherwise, *see id.* at 14 n.4. Most of the cited discussion concerns DOL's reasonable determination that investment advice communications with certain plan fiduciaries who are licensed financial professionals or plan fiduciaries who have at least $50 million under management do not present the same ills that ERISA was enacted to remedy. *See* AR3 (both parties "understand they are acting at arm's length," and "neither party expects that recommendations will necessarily be based on the buyer's best interests, or that the buyer will rely on them as such"). This exclusion of certain arms-length transactions does not undermine the statutory breadth or DOL's interpretation.

tailored or individualized advice, while … disclaiming in fine print the requisite 'mutual' understanding that the advice will be used as a primary basis for investment decisions").

Plaintiffs next argue that the Rule's definition is not entitled to deference because it would allow DOL to regulate "a far broader range of the U.S. economy" than allowed for by the "modest authority" Congress gave DOL in ERISA and the Code. Chamber Br. 21. This argument flounders where it begins because Plaintiffs themselves concede that DOL's authority extends to defining the term "fiduciary" in ERISA and the Code. *See* Chamber Br. 23-24 (stating that DOL's "interpretive authority" includes "the Code's definition of 'fiduciary'"); *see also* 29 U.S.C. § 1135; Reorg. Plan § 102. Thus Plaintiffs' analogy to *King v. Burwell*, 135 S. Ct. 2480 (2015), is misplaced because Congress "expressly," *id.* at 2489, gave DOL the relevant interpretive authority. *See also Johnson v. Buckley*, 356 F.3d 1067, 1073 (9th Cir. 2004) ("not[ing] the broad authority of both the Secretary of Labor and the Secretary of the Treasury to promulgate regulations governing ERISA"); *Guidry v. Sheet Metal Workers Int'l Ass'n, Local No. 9*, 10 F.3d 700, 708 (10th Cir. 1993), *rev'd in part on other grounds*, 39 F.3d 1078 (10th Cir. 1994) (en banc) (same). Because that is the case, there is no merit to Plaintiffs' contention that DOL has exceeded its authority by entrenching on the jurisdiction of the SEC. *See* Chamber Br. 23. Indeed, the SEC has consistently recognized DOL's authority to define fiduciary investment advice for purposes of ERISA, noting "that advisers entering into performance fee arrangements with employee benefit plans covered by the [ERISA] are subject to the fiduciary responsibility and prohibited transaction provisions of ERISA." SEC, Exemption to Allow Investment Advisers to Charge Fees, 63 Fed. Reg. 39022, 39024 n.14 (July 21, 1998).

Nor is there merit to Plaintiffs' argument that DOL "failed to justify changing the regulatory treatment of those who provide advice incidental to sales of fixed annuities." IALC Br. 18. The Supreme Court recently stated that "[a]gencies are free to change their existing policies as long as they provide a reasoned explanation for the change." *Encino Motorcars*, 136

S. Ct. at 2125. Here, unlike the situation in *Encino Motorcars*, where the Court found the agency had provided "barely any explanation," DOL provided a detailed explanation for revising its definition of "investment advice." DOL explained that the 1975 regulation's five-part test needed to be revised because it was allowing persons acting as fiduciaries to avoid fiduciary responsibilities. *See, e.g.,* AR4-7; *see also supra* Stmt. of Facts § II(A). Even if the annuity industry "structured their compensation arrangements and distributions channels" in reliance on the previous definition, IALC Br. 18, DOL is entitled to change that definition where it concluded that it is necessary to protect retirement investors. Moreover, DOL accounted for such reliance interests by specifically providing means for the industry to continue to collect their preferred forms of compensation and to fit into the new structure, so long as they could do so consistently with the interests of retirement investors. *See infra* Arg. § V(C).[41] This thorough consideration and explanation more than satisfies the standard set forth in *Encino*.

Lastly, there is no merit to Plaintiffs' argument that the Rule "defie[s] congressional intent" by "reject[ing] … the disclosure regime established by Congress under the securities laws." Chamber Br. 22. ERISA serves different purposes and, thus, sets up a very different regime than the securities laws. Indeed, while Congress recognized the value of disclosures, one of the primary motivations for the passage of ERISA was Congress's finding that existing requirements, which relied heavily on disclosures, were insufficient to adequately protect retirement investors from conflicts of interest and needed to be augmented by the imposition of fiduciary responsibilities and restrictions. *See supra* Stmt. of Facts § I; H.R. Rep. No. 93-533, *as reprinted in* 1974 U.S.C.C.A.N. 4639, 4642 at 11 (1973) ("Experience … has demonstrated the

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[41] As explicated below, DOL also thoroughly explained why the risks, complexities, and conflicts of interest justified amending PTE 84-24 and requiring conflicted FIA transactions to proceed under the BIC Exemption. *See infra* Arg. § V(A)(1). DOL also specifically analyzed the costs and other impacts of its determination on the annuity industry, *see* AR522-69, made changes to the BIC Exemption to minimize those impacts, and determined that the benefits of the rulemaking greatly outweighed the remaining costs to the industry. AR58-59.

inadequacy of the … Disclosure Act in regulating the private pension system for the purpose of protecting rights and benefits due to workers. It is weak in its limited disclosure requirements and wholly lacking in substantive fiduciary standards."); *see also* S. Rep. No. 93-127 (1973) (same). ERISA reflected congressional judgment that retirement investments merit special protection given their importance to the "well-being and security of millions of employees and their dependents," their "preferential Federal tax treatment," and their importance to commerce and the "stability of employment." *See* 29 U.S.C. § 1001(a). Thus, while ERISA includes disclosure requirements, it also requires far more, including "standards of conduct, responsibility, and obligation for fiduciaries" and "provid[es] for appropriate remedies, sanctions, and ready access to the Federal courts." *See* §§ 1001(b), 1104, 1106, 1132.

The rulemaking accords with Congress's approach, with disclosures an important part of the rulemaking. *See* AR105 (disclosures "provide basic information that is critical to [investors'] understanding of the nature of the relationship and the scope of the conflicts of interest"); *see also* AR63 (requiring those who render investment advice to "[a]cknowledge fiduciary status with respect to [that] investment advice" and "[f]airly disclose the fees, compensation, and Material Conflicts of Interest, associated with their recommendations"). But in light of evidence that disclosure of conflicts "could be ineffective—or even harmful," AR118, DOL rejected a disclosure-only regime, explaining that "[d]isclosure *alone* has proven ineffective to mitigate conflicts in advice." *Id.* (emphasis added). Far from "def[ying] congressional intent," Chamber Br. 22, DOL's approach to disclosures precisely accords with it.

Given DOL's reasonable interpretation of fiduciary investment advice and Plaintiffs' failure to undermine the reasonableness of that interpretation, DOL's interpretation is entitled to deference, and Defendants are entitled to summary judgment on Plaintiffs' first claim.

II. THE DEPARTMENT HAS EXPRESS STATUTORY AUTHORITY TO GRANT CONDITIONAL EXEMPTIONS FOR TAX-FAVORED ACCOUNTS

Where "[t]he Secretary is expressly delegated the authority to grant [an] exemption and is required to make certain other determinations in order to do so[,] ... [t]hat grant and those determinations have legislative effect, are thus entitled to great deference under the 'arbitrary and capricious' standard." *AFL-CIO v. Donovan*, 757 F.2d 330, 343 (D.C. Cir. 1985). DOL's determination to grant the BIC Exemption on the condition that fiduciaries who seek to rely on it act in the best interest of their retirement investors easily meets this standard.

Congress in ERISA sought to protect Americans' retirement savings by prohibiting fiduciaries to employee benefit plans and IRAs from engaging in specified transactions that Congress deemed so fraught with conflicts of interest that it prohibited them altogether. *See* 29 U.S.C. § 1106; 26 U.S.C. § 4975(c); *Donovan*, 716 F.2d at 1464-65 ("The object of [the prohibited transaction provisions] was to make illegal per se the types of transactions that experience had shown to entail a high potential for abuse.").[42] Congress also delegated to the Secretary broad authority to grant "conditional or unconditional" administrative exemptions to the prohibited transaction restrictions, if the Secretary makes findings that any such exemption is "(1) administratively feasible, (2) in the interests of the plan and of its participants and beneficiaries, and (3) protective of the rights of participants and beneficiaries of such plan." 29 U.S.C. § 1108(a); 26 U.S.C. § 4975(c)(2). As explained above, *see supra* n.6, pursuant to the Reorganization Plan, DOL's exemption authority applies to the prohibited transaction restrictions in both Title I of ERISA and the Code. *See* 5 U.S.C. App. 1, § 102.

Pursuant to this broad delegation of authority, and upon making the requisite findings, *see* AR76, DOL granted the BIC Exemption, which includes a requirement that fiduciaries

[42] *See also Chao v. Hall Holding Co.*, 285 F.3d 415, 441 n.12 (6th Cir. 2002) (collecting cases and commentary in support of the proposition that the object of the prohibited transaction provisions "was to make illegal per se the types of transactions that experience had shown to entail a high potential for abuse").

adhere to impartial conduct standards if they wish to engage in otherwise prohibited transactions. *See* AR63. DOL granted the BIC Exemption after an extensive notice-and-comment period and after conducting a thorough regulatory impact analysis that concluded that conflicts of interest in the market for retirement investment advice are widespread and could cost retirement investors tens to hundreds of billions of dollars over the next ten years. *See id.* Based on these findings, and in accordance with its statutory mandate to protect retirement investors in the case of prohibited transactions, DOL determined that it was appropriate to condition utilization of the BIC Exemption on adherence to impartial conduct standards to prevent advisers from acting on conflicts of interest to the detriment of retirement investors. *See* AR82.

As DOL explained, the impartial conduct standards constitute "baseline standards of fundamental fair dealing that must be present when fiduciaries make conflicted investment recommendations to Retirement Investors" because the standards "are necessary to ensure that Advisers' recommendations reflect the best interest of their Retirement Investor customers, rather than the conflicting financial interests of the Advisers and their Financial Institutions." AR116. Given Congress's broad delegation of authority to DOL to grant "conditional or unconditional" administrative exemptions based on its findings that an exemption serves the interests, and protects the rights, of retirement investors, DOL's determination to condition utilization of the BIC Exemption on compliance with "baseline standards of fundamental fair dealing," *id.*, is entirely reasonable and "entitled to great deference." *AFL-CIO*, 757 F.2d at 343.

Plaintiffs challenge DOL's decision to condition use of the BIC Exemption on adherence to the best interest standard, arguing that DOL's exemption authority is "limited"—indeed, so limited that DOL has "no authority to … regulate … fiduciaries or plans under the Code." Chamber Br. 24. Such a narrow reading of DOL's open-ended authority to grant administrative exemptions is contrary to the statutory text and case law. DOL has broad authority to exempt "any disqualified person or transaction … from all or part of the [prohibited transaction]

restrictions" so long as the Secretary makes the three requisite statutory findings. *See* 26 U.S.C. § 4975(c)(2). In similar contexts, courts have found that such language "conspicuously confers upon the [agency] broad [exemption] authority," *Chamber of Commerce of U.S. v. SEC*, 412 F.3d 133, 138-39 (D.C. Cir. 2005) (interpreting provision permitting exemption "if and to the extent … necessary or appropriate in the public interest and consistent with the protection of investors and the purposes ... of this subchapter"), and "very broad discretion." *Nat'l Small Shipments Traffic Conf., Inc. v. Civ. Aeronautics Bd.*, 618 F.2d 819, 827-28 (D.C. Cir. 1980) (interpreting provision allowing Board to exempt "any person or class of persons" from "any provision" of statute "if it finds that the exemption is consistent with the public interest").

Despite DOL's broad authority to grant administrative exemptions, Plaintiffs argue that DOL's exemption authority is limited to "*reduc[ing]* regulatory burdens" but does not include the authority to "*impose* … new obligations" or "otherwise regulate … fiduciaries or plans under the Code." Chamber Br. 23, 25. But DOL is not, in fact, imposing new obligations on fiduciaries; instead, it is requiring them to adhere to conditions when they engage in transactions that would otherwise be prohibited altogether. Plaintiffs' interpretation would impose limits on DOL's exemption authority that are not in the statutory text—in contravention of Congress's broad grant of authority and discretion to DOL—and would read the word "conditional" out of the text altogether. In delegating to DOL the authority to grant "conditional or unconditional" administrative exemptions, *see* 26 U.S.C. § 4975(c), Congress foresaw that DOL may need to require adherence to certain conditions in order to make the requisite statutory findings. DOL has thus long granted conditional administrative exemptions,[43] and Plaintiffs point to no case law questioning DOL's authority to do so.

[43] *See, e.g.,* PTE 93-33, 58 Fed. Reg. 31053 (May 28, 1993), as amended at 59 Fed. Reg. 22686 (May 2, 1994) and at 64 Fed. Reg. 11044 (March 8, 1999); PTE 97-11, 62 Fed. Reg. 5855 (Feb. 7, 1997), as amended at 64 Fed. Reg. 11042 (Mar. 8, 1999); PTE 91-55, 56 Fed. Reg. 49209 (Sept. 27, 1991), as corrected at 56 Fed. Reg. 50729 (Oct. 8, 1991).

Moreover, DOL was well within its authority to require adherence to this particular condition—satisfaction of the best interest standard—for fiduciaries seeking to rely on the BIC Exemption to engage in transactions otherwise prohibited by Congress. Plaintiffs suggest that such a condition is somehow foreclosed by the fact that Congress did not impose the duties of prudence and loyalty encompassed by the best interest standard on those who qualify as fiduciaries under the Code. *See* Chamber Br. 25. But DOL has not disturbed Congress's structural choices under ERISA or the Code. The rulemaking does not impose independent obligations on fiduciaries outside of the context of prohibited transactions. Instead, the rulemaking simply specifies the conditions for fiduciaries when they seek to engage in transactions *otherwise prohibited by Congress*, in accordance with Congress's directive to grant such exemptions only if they can be crafted to protect retirement investors. *See* AR116.

Far from prohibiting DOL from conditioning an exemption on adherence to fiduciary standards, Congress left to DOL the discretion to use its expertise and to weigh competing policy concerns over time to determine how best to protect IRA investors in the case of conflicted transactions.[44] DOL's solution—requiring fiduciaries to IRAs to act in the best interest of investors—is entirely consistent with the statutory prerequisites that the exemption serve the interests and protect the rights of retirement investors. *See* 26 U.S.C. § 4975(c)(2). There is nothing unreasonable or impliedly prohibited about DOL's drawing on long-standing fiduciary duties that Congress used in related contexts in order to protect IRA investors in the case of conflicted transactions.[45] As such, DOL's determination is entitled to deference, *see AFL-CIO*,

[44] *See, e.g., Aurora Packing Co. v. NLRB*, 904 F.2d 73, 76 n.1 (D.C. Cir. 1990) (*Chevron* presumes Congress delegated authority in part because of an agency's expertise and in part because of an agency's inherent policy role).

[45] Moreover, as DOL explained, the use of such "principles-based conditions, which are rooted in the law of trust and agency, have the breadth and flexibility necessary to apply to a large range of investment and compensation practices, while ensuring that Advisers put the interests of Retirement Investors first." AR63.

757 F.2d at 343, and Defendants are entitled to summary judgment on Plaintiffs' second claim.[46]

III. THE DEPARTMENT'S PROVISION, IN A CONDITIONAL ADMINISTRATIVE EXEMPTION, FOR CONTRACT TERMS THAT COULD BE ENFORCEABLE UNDER STATE LAW DOES NOT "CREATE A PRIVATE RIGHT OF ACTION"

Plaintiffs claim that the BIC and Principal Transactions Exemptions improperly "create a private cause of action" by conditioning relief from otherwise prohibited transactions on contract requirements aimed at insulating IRA holders from conflicts of interest.[47] *See* Chamber Br. 29; ACLI Br. 9.[48] But Plaintiffs mischaracterize what DOL has done. Under the terms of the exemptions, a fiduciary adviser cannot engage in an otherwise prohibited transaction unless the financial institution responsible for overseeing the adviser commits in writing to adhere to the impartial conduct standards, provides basic disclosures, and promises to implement procedures to ensure compliance with the impartial conduct standards and avoid financial incentives to violate those standards. A contract executed under the exemptions will expose the firm and adviser only to pre-existing causes of action.

Because DOL has not, in fact, created any new private right of action, the limits courts

[46] Plaintiffs also appear to claim that DOL exceeded its authority in the BIC Exemption because their members, they say, cannot alter their fee structures and so will need to rely on the BIC Exemption to engage in conflicted transactions. As discussed below, *see infra* Arg. VI(A), Plaintiffs have not demonstrated through their unsupported allegations that their members could not alter their compensation structures to avoid prohibited transactions, and DOL reasonably expected that the industry would—and could—innovate. *See* AR634-40. In any event, DOL granted the BIC Exemption precisely to allow for the continued use of certain compensation practices. AR59. Plaintiffs' assertion that they will be unable to alter their compensation practices and therefore will be required to adhere to the conditions of the BIC Exemption does not undermine DOL's authority to grant it.

[47] Separately, even though the BIC Exemption has no contract requirement for transactions involving *employee benefit plans*, *see* AR135, Plaintiffs also appear to claim that its provisions applicable to these plans somehow violate the APA by enabling suits "for breach of [exemption] requirements that go well beyond ERISA's fiduciary conduct standards and statutory exemptions." Chamber Br. 28. This undeveloped theory does not raise *Sandoval* issues because it is clear that any suit for plan transactions will proceed under the express remedies Congress provided in the statute. *See* 29 U.S.C. § 1132(a)(2), (3); AR64, 98.

[48] More than 30 times, ACLI cites its complaint as evidence in support of its motion. *See, e.g.*, ACLI Br. 9. But a party's own complaint that is signed only by counsel and not under penalty of perjury cannot support a summary judgment motion. *See King v. Dogan*, 31 F.3d 344, 346 (5th Cir. 1994); *Tate v. Starks*, 444 F. App'x 720, 726 (5th Cir. 2011). This is especially so in a record review case, which is limited to the record before the agency. *See Medina Cty. Envtl. Action Ass'n v. Surface Transp. Bd.*, 602 F.3d 687, 706 (5th Cir. 2010). Accordingly, DOL does not address any arguments and evidence contained only in ACLI's 105 page complaint but not contained in its brief.

have recognized under which a private right of action may be inferred by the judicial or executive branches have nothing to do with this case. *See Alexander v. Sandoval*, 532 U.S. 275, 286 (2001) ("[P]rivate rights of action to enforce federal law must be created by Congress."); *Mertens*, 508 U.S. at 254 (ERISA provides a "detailed enforcement scheme," and the Supreme Court is generally "unwilling[] to infer causes of action in the ERISA context"). These principles are irrelevant here because DOL has neither "created" a private right nor required an "action to enforce federal law." *Sandoval*, 532 U.S. at 286.

DOL has not expanded the scope of ERISA's causes of action beyond those expressly provided for in 29 U.S.C. § 1132, created any new private causes of action under the Code, or created any other cause of action under any other law. *See* AR116, 195 ("[T]his exemption does not create a cause of action for ... IRA owners to directly enforce the prohibited transaction provisions of ERISA and the Code in a federal or state-law contract action."). Instead, DOL has simply specified the minimum contract terms for a financial institution and adviser to qualify for two exemptions for IRA transactions. *See supra* Stmt. of Facts § II(D).[49]

There is a significant difference between conditioning an exemption on minimum contract terms, and creating or inferring a new cause of action that was not authorized by courts or legislatures. While DOL has imposed minimum contract terms, it does not have the authority to create a state law cause of action to enforce that contract. Plaintiffs certainly do not purport to

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[49] As relevant, a qualifying BIC Exemption contract:

- Must state that the financial institution and adviser are fiduciaries with respect to investment advice provided under the contract;
- Must state that the financial institution and adviser will adhere to the impartial conduct standards;
- Must disclose various items, including the types of compensation they expect to receive from third parties;
- May include individual arbitration agreements (with certain limits);
- May restrict punitive damages if permissible under other law; and
- Must not waive or qualify the investor's ability to participate in a class action or other representative action in court.

See BIC Exemption § II(a)-(f), AR132-35. The Principal Transactions Exemption's requirements are similar. *See* Principal Transactions Exemption § II(a)-(f), AR202-05.

explain how DOL could "create" a state law cause of action. Parties are free to enter into a contract pursuant to the BIC or Principal Transactions Exemptions, and if they do so, they can avoid violation of the prohibited transaction rules and thereby reduce the advisers' exposure to liability under ERISA and the Code. To the extent, however, parties wish to enforce the contract terms, they will have to rely on existing causes of action under state contract or other laws, not new causes of action created by DOL. The only actions available under ERISA are those specified by ERISA and private parties cannot bring an action for violation of the Code provisions relating to IRAs.[50]

Moreover, because the relevant transactions already involve contracts enforceable under state or other law, it is sensible for DOL to focus on the terms of the contractual relationship between the parties in fashioning a protective exemption. *See, e.g.*, AR46171 (Cmt. 3050, ACLI) ("Insurers are familiar with the idea of an enforceable contract between a financial institution and its customer. All annuity owners have contractual rights enforceable against the insurer and recourse to state insurance departments and state courts.").[51] Given that such contract claims are not novel, the contract terms required to meet the exemptions do not make financial institutions subject to "whole new enforcement mechanisms," Chamber Br. 29, let alone new federal causes of action.[52]

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[50] Plaintiffs gain no support for their position by arguing that DOL has "paint[ed] financial professionals into a corner where they have no choice but to accept the exemption's terms." Chamber Br. 29. This is both inaccurate and irrelevant. DOL explained that financial professionals have a number of ways to change their compensation to avoid conflicts, such that recourse to the exemptions is unnecessary. *See* AR638. Regardless, it is not the rulemaking but ERISA and the Code that prohibit their conflicted transactions. *See supra* Arg. § I.

[51] As Plaintiffs acknowledge, annuities have long been subject to state court litigation (sometimes federal litigation on diversity grounds). *See, e.g.*, *Miller v. Nationwide Life Ins. Co.*, 448 F. App'x 423, 426-34 (5th Cir. 2011); *Knox*, 2016 WL 1735812, at *4-6; *Abbit*, 999 F. Supp. 2d at 1197-99; *Orr v. Mfrs. Life Ins. Co. of N. Am.*, No. 3:98-0165, 1998 WL 614651, at *1-4 (N.D. Tex. Sept. 8, 1998). In addition to annuities, the sales of other retirement investment products encompassed by the prohibited transaction provisions, *see* 26 U.S.C. § 4975(c)(1), are also contracts. *See, e.g.*, *Williams v. Bank of Am., N.A.*, 602 F. App'x 187, 188-89 (5th Cir. 2015) (elements of contract under Texas law); *Meisler v. Smith*, 814 F.2d 1075, 1078-79 (5th Cir. 1987) (addressing suits over broker contracts).

[52] Indeed, ACLI suggested an alternative exemption "that would require a fiduciary and/or the fiduciary's employer or an affiliate ... to provide retirement savers with a written enforceable commitment that, in providing investment

(*footnote continued on next page*)

Failing to show that DOL has violated *Sandoval*, Plaintiffs repeat the argument, debunked above, *see supra* Arg. § II, that DOL's exemption authority cannot involve setting additional conditions for regulated entities. *See* Chamber Br. 30 (claiming DOL has authority "only ... to *exempt* parties from regulatory burdens"). Here, DOL is well within its authority to dictate the terms of a "conditional" exemption, which reasonably includes consideration of what contractual terms would meet the statutory criteria for an exemption. *See, e.g.*, 26 U.S.C. § 4975(c)(2). DOL explained its actions on that basis, determining "that the contract requirement ... serves a critical protective function." AR116, AR195; *see also* AR116 (potential "liability ... [for] fail[ure] to provide advice that is prudent or otherwise in violation of the standards ... [is] a significant deterrent to violations of important conditions under an exemption that accommodates a wide variety of potentially dangerous compensation practices").

Plaintiffs nevertheless argue that DOL's condition-setting authority cannot be used in a way that could augment potential liability. They point to nothing in the text of ERISA or the Code that compels this conclusion, nor any case law questioning the use of similar exemption authority. Indeed, precluding DOL from granting exemptions on conditions that could lead to liability under other regulatory schemes could dramatically reduce DOL's ability to craft sensible conditions and make it much more difficult for the agency to grant exemptions at all.[53] Far afield from *Sandoval*, Plaintiffs rely on vague generalities and two inapplicable cases. The exemptions

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guidance and advice, the financial professional will act in the saver's best interest." AR46172 (Cmt. 3050, ACLI).

[53] For instance, because financial products are regulated by a variety of state and federal bodies, it would be difficult for DOL to avoid setting conditions that affect potential liability. If, for example, DOL imposed a disclosure requirement on a party regulated by the SEC or state insurance departments, or required a firm to make certain representations to a plan or IRA customer about fees or performance, the content and accuracy of the disclosure could likely be subject to claims under state or federal securities, insurance, or consumer protection laws. If it imposed a licensing requirement or limited eligibility for an exemption to particular categories of institutions, such as banks or insurance companies, it could effectively expose persons wishing to rely on the exemptions to actions under those regulatory regimes. Conversely, as the Supreme Court has expressly recognized and approved, state regulatory actions can affect claims available under federal law. *See UNUM v. Ward*, 526 U.S. 358, 377 (1999) (noting that a saved state insurance law may be enforced as a plan term in an ERISA claim for benefits).

here are not contrary to the plain text, as in *Loving v. IRS*, 742 F.3d 1013 (D.C. Cir. 2014),[54] and DOL has not stretched its general rulemaking authority beyond plausible limits, as in *Contender Farms, LLP v. USDA*, 779 F.3d 258 (5th Cir. 2015).[55] DOL instead has exercised the specific authority delegated by Congress to set conditions for administrative exemptions that meet statutory criteria. *See* 29 U.S.C. § 1108(a); 26 U.S.C. § 4975(c)(2).

For all the reasons above, Plaintiffs' cannot show that Congress intended to preclude contract provisions in the administrative exemptions. Indeed, with some regularity, federal agencies require private contracts for regulated entities. *See, e.g.*, 14 C.F.R. § 212.3(c) (regulating charter flight providers by requiring written contracts with specific terms to be signed prior to the operation of a flight).[56] As the citations demonstrate, contrary to Plaintiffs' position, it is not novel for federal regulations to specify terms for private contracts, and other ERISA

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[54] *Loving* concluded that "tax-return preparers" do not fall within the statutory term "representatives of persons." *Id.* at 1016-22 (finding the plain meaning of the statutory term dispositive, with support from five other considerations). From *Loving*'s discussion "find[ing] at least some significance in the fact that multiple Congresses have acted as if Section 330 did not ... cover tax-return preparers," Plaintiffs single out the observation that IRS's view "would effectively gut Congress's carefully articulated existing system for regulating tax-return preparers," because the statutory "provisions specific to tax-return preparers" and "corresponding civil penalties" "all ... would have been unnecessary." *Id.* at 1020. By contrast here, DOL has express authority to craft exemptions, and Congress's separate imposition of excise taxes on entities engaging in prohibited transactions, *see* 26 U.S.C. § 4975(a)-(b), is not undermined or made redundant by an exemption containing a contract requirement.

[55] In *Contender Farms*, the court rejected, on plain language grounds, an agency's argument relying on a specific provision that authorized it to impose "requirements," concluding that the agency could not include conditions that fell outside the scope of that provision—*i.e.*, that did not "relate to whether 'persons' are 'qualified' to inspect horses for evidence of soring." 779 F.3d at 272 (quoting 15 U.S.C. § 1823(c)). By contrast, here, the conditions DOL imposed relate directly to the statutory criteria. And in the section relied on by Plaintiffs, Chamber Br. 29-30, the court rejected an agency argument based on general authority to issue rules "deem[ed] necessary to carry out the provisions of this chapter," 779 F.3d at 273 (quoting 15 U.S.C. § 1828), because the agency had "addresse[d] an area that is plainly outside [its] statutory authority." *Id.* at 272.

[56] *See, e.g.*, 7 C.F.R. § 1493.20 (USDA's Export Credit Guarantee Program defines "Firm Export Sales Contract" by requiring that the "written evidence of sale ... must, at a minimum, document the following information" constituting nine mandatory terms and one optional one); 7 C.F.R. § 1499.11(g) (specifying that contracts with service providers entered into by participants in USDA's Food for Progress Program must "require[] the provider to maintain adequate records" and "to submit periodic reports to the participant"); 14 C.F.R. § 212.3(c), (e) (specifying that the charter flight contract must be signed both by the carrier and the charterer, that payment must be made in advance, that escrow or surety information be included, and that the surety is released if a claim is not filed within 60 days of cancellation); 47 C.F.R. § 24.238(c) (specifying the parties to a private contract for alternative emissions limits under FCC broadband license—"all affected licensees and applicants").

exemptions have required written agreements with implications for private enforcement.[57] Because DOL has not created a new cause of action, it has not improperly exercised "legislative judgment," Chamber Br. 30, in crafting appropriate exemptions in order to satisfy statutory criteria. *Cf. Whitman v. Am. Trucking Ass'ns*, 531 U.S. 457, 472 (2001) (noting that a "statute [can] delegate[] legislative power to the agency" so long as Congress "lay[s] down by legislative act an intelligible principle to which the [agency] ... is directed to conform").

In sum, DOL has exercised its broad delegated authority to craft administrative exemptions that serve the interests of retirement investors by specifying minimum contract terms for conflicted transactions that already involve contracts enforceable under state law. It did not "create" a cause of action but acted well within its statutory authority. As such, Defendants are entitled to summary judgment on this claim.

IV. DOL'S COST BENEFIT ANALYSIS SUPPORTS ITS RULEMAKING

While Plaintiffs argue that DOL overstated the benefits and underestimated the costs associated with its rulemaking, DOL's thorough and reasonable analysis demonstrates the opposite. This claim is reviewed under the APA's "highly deferential" arbitrary and capricious standard. *ConocoPhillips Co. v. EPA*, 612 F.3d 822, 840 (5th Cir. 2010).[58]

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[57] *See* 75 Fed. Reg. 38837, 38843 (July 6, 2010) (PTE 84-14 conditioning exemption on "acknowledge[ment] in a written management agreement that [the independent fiduciary] is a fiduciary with respect to each plan that has retained [it]"); 71 Fed. Reg. 63786, 63796 (Oct. 31, 2006) (PTE 2006-16 conditioning exemption on "written loan agreement" that includes term stating "that the plan has a continuing security interest in ... the collateral," term addressing the identity of the currency for payments (unless the parties agree that it will be disclosed in the loan confirmation), and term addressing the plan's rights in the event the loan is terminated and the borrower fails to return the borrowed securities within the required timeframe).

[58] Defendants note that the APA, standing alone, does not require a detailed cost-benefit analysis. *See Entergy Corp. v. Riverkeeper, Inc.*, 556 U.S. 208, 224 (2009) (upholding agency choice to seek "only to avoid extreme disparities between costs and benefits"); *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."); *Vill. of Barrington v. Surface Transp. Bd.*, 636 F.3d 650, 670-71 (D.C. Cir. 2011) (rejecting argument that "the APA's arbitrary and capricious standard alone requires an agency to engage in cost-benefit analysis"). While the Supreme Court recently noted that "reasonable regulation ordinarily requires paying attention to the advantages and the disadvantages of agency decisions," *Michigan v. EPA*, 135 S. Ct. 2699 (2015), it did not require the agency "to conduct a formal cost-benefit analysis," leaving it up to the agency "to decide (as always, within the limits of reasonable interpretation) how to account for cost." *Id.* at 2711; *see also Markle Interests, LLC v. U.S. Fish &*

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Review under the arbitrary-and-capricious standard is "extremely limited." *Markle Interests*, 2016 WL 3568093, at *3. Courts apply "a presumption that the agency's decision is valid," which is the plaintiff's burden to overcome. *La. Pub. Serv. Comm'n v. FERC*, 761 F.3d 540, 558 (5th Cir. 2014). The Court must "uphold an agency's action if its reasons and policy choices satisfy minimum standards of rationality." *10 Ring Precision, Inc. v. Jones*, 722 F.3d 711, 723 (5th Cir. 2013). It "need only find a rational explanation for *how* the [agency] reached its decision." *Associated Builders & Contractors of Texas, Inc. v. NLRB*, No. 15-50497, _ F.3d _, 2016 WL 3228174, at *6 (5th Cir. June 10, 2016). By contrast, to fail this standard, an agency must have:

> relied on factors which Congress had not intended it to consider, entirely failed to consider an important aspect of the problem, offered an explanation for its decision that runs counter to the evidence before the agency, or is so implausible that it could not be ascribed to a difference in view or the product of agency expertise.

Markle Interests, 2016 WL 3568093, at *3.

Plaintiffs have not carried their burden to overcome the presumption of validity or to show that DOL's analysis fell below minimum standards of rationality. To the contrary, DOL's detailed analysis demonstrates that its conclusions are well-supported.

A. DOL Relied on Sufficient Evidence that the Rulemaking Would Confer a Substantial Benefit on Retirement Investors by Mitigating Conflicts of Interest in Retirement Investment Advice

Plaintiffs mischaracterize DOL's analysis in claiming that DOL "relied on a single factor" to conclude that the rulemaking would substantially benefit retirement investors. Chamber Br. 34. DOL collected, examined, and relied on a wide body of evidence, both empirical and qualitative, to conclude that conflicted advice about mutual funds, annuities, and other retirement investments inflicts significant harm on retirement investors. *See, e.g.*, AR421-

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Wildlife Serv., No. 14-31008, _ F.3d _, 2016 WL 3568093, at *13 (5th Cir. June 30, 3016).

28, 443-83, 508-13, 614-19, 692-98. Moreover, DOL relied on a group of nine studies to generate a *quantitative* estimate of the ongoing cost of conflicted advice in the mutual fund segment of the IRA market, *see* AR474-479, that were broadly consistent with the much larger body of empirical and qualitative evidence. DOL *also* relied on a single, high quality empirical study of front-end load mutual funds—the Christofferson, Evans, and Musto ("CEM") study—to generate a quantitative estimate of certain gains to investors because this study provided the best available quantitative data for this purpose, AR485-94, 656-80, and because the study's results were consistent with both the related literature on mutual fund performance and the broader literature on conflicts of interest. AR479. Given the breadth and robustness of the broader empirical and qualitative evidence, DOL's *qualitative* conclusions appropriately extend beyond such mutual funds to annuities and other investments that are subject to advisory conflicts. *See also infra* Arg. § V(B).

Contrary to Plaintiffs' insinuation, DOL did not rely on the CEM study to show that conflicted advice is pervasive in the market—ample other evidence served that purpose. *See, e.g.*, AR486 (noting that its quantitative estimates "are largely consistent with the estimates presented in Section 3.2.4 reflecting a large body of academic literature, comments ..., and testimony at the DOL hearing in August 2015"). Instead, the study simply provided the best means to quantify a specific subset of gains to investors, AR494 ("[T]he quantified gains pertain only to the 13 percent of all IRA assets that are invested in front-end-load mutual funds, and only to the subset of conflicts associated with front-end loads."), which standing alone was sufficient to outweigh estimated industry costs. AR 326, 642-643.

All of the criticisms Plaintiffs level against this study were raised during the rulemaking and were addressed by DOL in its RIA. First, the claim that the study "used performance data on certain unrepresentative funds," Chamber Br. 34, was raised in a comment, *see* AR42284-86 (Cmt. 749, Inv. Co. Inst. ("ICI")), to which the CEM study's authors responded. *See* AR45297

(Cmt. 2766, Susan Cristofferson, Richard Evans). DOL also responded in the RIA, addressing ICI's concerns and concluded that the data was representativeness. *See* AR479-82, 666-68. Second, the period covered by the data, 1993-2009, was not "cherry-picked" by DOL, Chamber Br. 34, but was the period used in the study. AR663. The period was reasonable, containing nearly two full market cycles, including a large boom period (1993-2000) and a recovery (2003-2007).[59] Furthermore, DOL confirmed that the results were not idiosyncratic by conducting an analysis of mutual fund performance over the period 1980-2015. *See* AR646-55. DOL's review of the available literature and public comments led it to conclude that the harm to retirement investors from conflicts of interest in the market for advice is not limited to the 1993-2009 period or any other period covered by particular studies. *See* AR477-78. Third, DOL's methodology—basing product performance on the year the product was purchased—matched the study's methodology and the available data. *See* AR485 & n.384; AR662-64. While Plaintiffs claim that "actual holding periods [for the products], or even ... a full market cycle" should have been used, Chamber Br. 34, the study included two full market cycles, and the available evidence indicates that data from actual holding periods, if it had been available, most likely would have shown even greater losses because advisers' conflicts appear likely to make market timing problems worse. AR472, 477, 632-34. Fourth, while Plaintiffs challenge "spreading small marginal benefits across the trillions of dollars in retirement savings," Chamber Br. 35, DOL's application of an estimated effect to the relevant population is standard procedure in cost-benefit analyses. *See, e.g.*, SCM Network, *Int'l Standard Cost Model*, 9 [Link] (Defs.' App'x 3) (cost is "multiplied by the size of the affected population").[60] Finally, contrary to the claim that DOL

[59] *See* Morningstar, Ibbotson SBBI, 2015 Classic Yearbook: Market Results for Stocks, Bonds, Bills, and Inflation 1926-2014, 37 & Graph 2-1 (appended as Defs.' App'x 2); *see also id.* 41-44, Tables 2-2, 2-3. The Court can take judicial notice of these background facts. *See Dine Citizens Against Ruining Our Envir't v. Jewell*, No. 15-0209, 2015 WL 4997207, at *5 n.4 (D.N.M. Aug. 14, 2015).

[60] Plaintiffs' claim that DOL "manipulated the 'law of large numbers'" is incoherent. *See* Chamber Br. 34, 37. The "law of large numbers" is a statistical theorem regarding the tendency of an average of results to be closer to the
(*footnote continued on next page*)

"ignored studies ... that refuted its flawed estimates," Chamber Br. 34, DOL directly responded to ICI's analysis, among others. AR479-82, 616-18.

In sum, DOL had adequate grounds to conclude that conflicts of interest are pervasive, and its quantification of the gains to investors in one market segment is both robust and illustrative of additional gains reasonably expected in other segments. Where, as here, an agency "considers the factors and articulates a rational relationship between the facts found and the choice made and gives at least minimal consideration to relevant facts contained in the record, it is not the role of the court to weigh the evidence pro and con." *Associated Builders & Contractors*, 2016 WL 328174, at *9.

B. DOL Did Not Underestimate the Rulemaking's Costs For the Industry or Retirement Investors

DOL adopted the conservative position of using the affected industry's own estimates of its quantifiable compliance costs, even though these costs were likely overstated. AR525-26. Plaintiffs claim the estimates do not go far enough, suggesting that DOL "focus[ed] on firms' direct compliance costs to the exclusion of virtually all other direct and indirect consequences." Chamber Br. 35. This is inaccurate. DOL specifically examined the "secondary market effects," including the impact of the rulemaking on small investors. *See* AR623-40, 682-88. While Plaintiffs' core argument is that these effects should be quantified, DOL is not obligated to numerically quantify every cost. *See, e.g.*, *ConocoPhillips*, 612 F.3d at 840 (rejecting claim that agency's "failure to estimate benefits for specific new facility locations renders the process arbitrary or capricious," especially where plaintiff "provided no more detailed data during rule making").[61]

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expected value as the number of trials increases. *See* https://www.britannica.com/science/law-of-large-numbers. Plaintiffs do not explain how this in any way relates to DOL's analysis.

[61] None of the cases cited by Plaintiffs is to the contrary. While Plaintiffs try to create a higher standard, such as "properly considering *all* related costs," Chamber Br. 37 (emphasis original), in reality an agency is only held to "minimum standards of rationality," *10 Ring Precision*, 722 F.3d at 723, such that it may not "entirely fail[] to

(*footnote continued on next page*)

Plaintiffs single out only one cost to the industry that was allegedly unaccounted for—"the costs of … class action lawsuits." Chamber Br. 35. Plaintiffs substantially overstate this issue. For starters, DOL did quantify at least a portion of this cost by accounting for increased fiduciary liability insurance premiums. *See* AR555-58.[62] Moreover, investment advisers and related firms are already subject to litigation, including class actions, regarding their marketing, advice, and transactions. *See, e.g.*, AR98 n.72 (noting FINRA and SEC rules); AR448 & n.314 (noting high profile class actions involving variable and fixed annuities). Nor should litigation costs be considered as costs of the rulemaking to the extent firms are found liable for violating the impartial conduct standards or other contract conditions. Accordingly, DOL gave due consideration to the issue, and it was not arbitrary and capricious for DOL not to further quantify these alleged costs.

Separately, Plaintiffs claim that DOL "ignored the costs to individuals whom the Rule will deprive of assistance." Chamber Br. 36. But DOL considered this issue and concluded, based on the evidence, that "quality, affordable advisory services will be amply available to small plans and investors under the final rule and exemptions." AR628; AR628-34. In support of their position, Plaintiffs cherry-pick some information about the United Kingdom's ("UK") transition to a fee-based compensation model that is not fully representative. Chamber Br. 36.

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consider an important aspect of the problem." *Markle Interests*, 2016 WL 3568093, at *3. Plaintiffs generally rely on statutes requiring specific considerations that are not present here. *See Bus. Roundtable v. SEC*, 647 F.3d 1144, 1148 (D.C. Cir. 2011) (addressing SEC's "unique obligation to consider the effect of a new rule upon efficiency, competition, and capital formation" under the Exchange Act); *Corrosion Proof Fittings v. EPA*, 947 F.2d 1201, 1214-15 (5th Cir. 1991) (addressing agency burden under Toxic Substances Control Act, which included considering "the environmental, economic, and social impact of any action" and "using the least burdensome requirements"); *Sierra Club v. Sigler*, 695 F.2d 957, 978 (5th Cir. 1983) (addressing National Environmental Policy Act, which mandates a broad analysis of "the economic, technical, and environmental costs and benefits of a particular action"). In particular, *Sigler* does not require quantifying all costs. Instead, it simply rejected an agency's attempt to "cite possible benefits ... yet avoid citation of accompanying costs." 695 F.2d at 979.

[62] DOL also requested that the industry provide supplemental data, *see, e.g.*, AR64361 (Aug. 26, 2015 letter to Financial Services Inst.), but the industry did not quantify litigation costs, leaving DOL unable to provide a more precise accounting of these costs. *See, e.g.*, AR46068 (Cmt. 3036 Financial Services Inst.) ("Because of the extreme uncertainties surrounding litigation risk, we did not attempt to quantify it in our survey").

Whether the UK's project has been successful and its implications for the U.S. was hotly debated throughout the rulemaking. *See* AR405-09. DOL considered the matter carefully, AR394-408, and concluded that "the UK experience supports a finding that strong protections against advisory conflicts are warranted and can produce substantial benefits for consumers." AR408. Nonetheless, DOL found the UK's project to be distinct in relevant ways. For example, it banned commissions entirely for all investment advice, whereas DOL has merely set conditions for receiving such conflicted payments for retirement accounts. *See id.* Also, the UK has a much lower ratio of advisers per person than the U.S. *See* AR408 (noting that the U.S. has "almost 4 times what the UK had even before the RDR was passed").[63] Given these differences, the UK transition does not show that the rulemaking is likely to decrease access for small investors. AR408.

Plaintiffs' argument that the value of advice to consumers should be added to the cost side of the ledger would only make sense if the rulemaking will, on balance, reduce consumers' access to such advice. Because DOL concluded otherwise, and Plaintiffs have not shown that DOL's conclusion is unreasonable, the general value of investment advice does not need to be treated as a cost of the rulemaking, and Plaintiffs' efforts to bolster evidence that investment advice is valuable are irrelevant. Plus, their arguments have additional defects. First, Plaintiffs suggest that DOL has contradicted its earlier estimates that investors stand to gain from increased

[63] The UK "advice gap" for small investors upon which Plaintiffs rely, *see* Chamber Br. 36; AR68907, is a "trend [that] existed independent of the RDR" and may have been exacerbated by aspects of the RDR that are not mirrored in DOL's rulemaking. *See* AR408. DOL considered the report on which Plaintiffs rely, *see* AR403-04; AR68907, and other facts cast doubt on this "advice gap." *See, e.g.*, AR402 & n.176 (noting that a UK study found "most retail investment advisers continue to serve clients with savings and investments between £20,000 and £75,000 and a third service clients with less than £20,000"); *see also* AR69000-01, FCA Survey of Firms Providing Financial Advice (April 2016) (stating that "32% of firms expected to grow their number of advisers over the next year," the "majority of firms planned to use more technology, particularly in customer communications and to increase efficiency and reduce the costs of the advice process," and a "relatively small proportion of firms (11% or less) expected that, over the next year, they would increase their mass-market, low-cost advice proposition or the provision of generic advice").

access to impartial fiduciary advice under statutory exemption 29 U.S.C. § 1108(b)(14). *See* 76 Fed. Reg. 66,136 (Oct. 25, 2011). This criticism was raised and addressed in the rulemaking. AR631. While Plaintiffs accuse DOL of "*ex post facto* recharacterization of these earlier statements," Chamber Br. 37, DOL's position has not changed. The 2011 regulation pertained only to fiduciary advice provided pursuant to a particular exemption that included very strong consumer protections.[64] While Plaintiffs suggest that DOL's 2011 analysis attributed benefits to non-fiduciary advice, to the contrary, DOL's 2011 analysis consistently pointed to evidence that absent strong consumer protections, advisory conflicts could taint fiduciary advice and harm IRA investors. *See* AR631; 76 Fed. Reg. at 66156 ("[A]bsent adequate protections, conflicts themselves may be more costly to participants than a general prohibition against them."). Second, Plaintiffs claim that DOL should have factored in the possibility that brokers add value by preventing clients from selling funds after a downturn. Chamber Br. 37 (citing Cmt. 3075, Economists Inc.). DOL examined the relevant comment, noted that it lacked empirical support, and concluded that broker incentives toward "more frequent and larger trades" might prevent a net benefit "over the course of a market cycle." AR632-34. Again, this does not contradict DOL's earlier observation that good advice can protect investors in a downturn, *see* 76 Fed. Reg. 66153-54, because the 2011 analysis only concerned "quality fiduciary advice." *See id.* 66156.

In sum, DOL's cost-benefit analysis did not improperly exclude Plaintiffs' proffered harms to consumers because DOL reasonably concluded that these harms would not materialize.

C. DOL's Quantitative Analysis Supported its Reasonable Conclusion that the Benefits of the Rulemaking Would Justify its Costs

Applying conservative assumptions throughout the RIA likely to overstate costs and

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[64] Among other things, this exemption generally requires that either the advisers' fees are level (effectively barring agent commissions), or that the advice is formulated by a computer algorithm that is independently certified to be unbiased. *See* 29 U.S.C. § 1108(g)(2)(A).

understate gains, DOL demonstrated that the rulemaking is consistent with the aims of ERISA. *See* AR329. As discussed, DOL relied on a wide body of evidence to conclude that conflicted advice imposes a substantial burden on retirement investors, and that mitigation of those conflicts would substantially benefit investors. *See supra* Arg. § IV(A). DOL also examined and quantified, to the extent feasible, the costs associated with the rulemaking. *See supra* Arg. § IV(B). DOL's analysis reasonably relied on both qualitative and quantitative evidence, with the weightiest evidence on the qualitative side due to the difficulty in empirically assessing the implications of conflicts of interest where compensation and incentives are opaque and the data was not produced by the industry. *See* AR325. Moreover, its careful consideration of the various criticisms and additional proposed costs raised during by public comments demonstrate that DOL has not "failed to consider an important aspect of the problem" or provided "an explanation for its decision that runs counter to the evidence before the agency." *Markle Interests*, 2016 WL 3568093, at *3.

Plaintiffs ask the Court to consider the quantitative aspects of DOL's analysis in isolation. Chamber Br. 37. This would be inappropriate because DOL's conclusions do not depend on a strict comparison of the quantified benefits versus the quantified costs. Moreover, an agency need not—indeed cannot—base its every action upon empirical data; depending upon the nature of the problem, an agency may be entitled to make "a forecast of the direction in which future public interest lies" based on "deductions based on the expert knowledge of the agency." *FCC v. Nat'l Citizens Comm. for Broad.,* 436 U.S. 775, 813-14 (1978); *see also Melcher v. FCC*, 134 F.3d 1143, 1158 (D.C. Cir. 1998).

Nevertheless, for the Court's convenience and to aid in this explanation, DOL's quantitative analysis, which provides both low and high ranges for the estimates to account for uncertainties, can be summarized as follows:

Table 1. Summary of Quantitative Estimates for Cost Benefit Analysis (in billions)	10 year horizon		20 year horizon	
	Low	High	Low	High
1. Partial investor losses absent rulemaking (only broker-sold mutual funds for IRAs - AR478, 679)	$94.7	$189.3	$201.9	$403.9
2. Partial gains to investors from rulemaking (only front-end load mutual funds for IRAs - AR491)	$32.5	$35.9	$66.4	$75.5
3. Compliance costs from rulemaking (market-wide costs - AR565-66, Figs. 5-13, -14, -15)	$10.0	$31.5	$16.2	$49.1
3.1 Included cost for exclusion of FIAs from PTE 84-24 (AR602)	$0.34	$0.38		

As discussed above, the quantified investor losses and gains (lines 1 and 2) are conservative in numerous ways: (i) the methodology of the estimates, (ii) being derived *exclusively* from the mutual fund sector of the IRA market,[65] (iii) reflecting only one type of loss that conflicts of interest cause, and not other losses, such as those from market timing errors, (iv) reflecting losses and gains only for IRA investors, not including employee benefit plans, and (v) not accounting for potential gains from raising adviser conduct standards. *See* AR324-25, 494; *supra* Arg. § IV(A). The total gains to retirement investors thus are likely to be substantially larger than these particular, quantified gains alone. *See* AR 326. By comparison, the quantified cost estimates (line 3) involve the entire industry's compliance costs and are conservative because they are derived from the industry's own estimates, which DOL concluded are likely to overstate costs. *See supra* Arg. § IV(B).

Plaintiffs argue that the net results of DOL's quantitative analysis support their arguments that the costs outweigh the benefits of the rulemaking. Chamber Br. 37. They are wrong for numerous reasons. They argue that "modest adjustments to [DOL's] projections" would turn the quantitative estimates net negative, and that they have established additional costs that would tip the balance. *Id.* As discussed above, none of their proposed costs require additional

[65] The losses on line 1 involve only mutual funds sold to IRAs by brokers, which make up roughly 22% of the IRA market. AR478, 679. The gains on line 2 involve only front-end load mutual funds sold to IRAs, which make up roughly 8-12% of the IRA market. AR491.

quantification. *See infra* Arg § IV(C). But even if they could identify some cost that would require "modest" adjustment to the quantitative projections, it would not tip the balance. First, Plaintiffs' characterization of the difference between the quantified estimates as a "net benefit" is inaccurate. Such an argument completely ignores all of the unquantified benefits of the rulemaking expressly laid out by DOL in the RIA and supported on qualitative grounds. As discussed above, DOL quantified only a small fraction of the gains from the rulemaking due to data limitations. Second, the quantified costs and benefits are mismatched—the costs are derived from the industry's own market-wide estimates, while the gains are limited to the small fraction of IRA assets invested in front-end load mutual funds. AR494. Third, even if costs marginally exceeded DOL's low-end estimate of investor gains in the short term, as Plaintiffs ask the Court to imagine, *see* Chamber Br. 37 (comparing the high end cost estimate to the low end gain estimate at the ten year mark), they would be unlikely to do so in the long term. Industry costs are front-loaded due to compliance adjustment, but investor gains are back-loaded due to the long-term consequences of better investments. *See* AR326, 491. Finally, focus on the high end of the cost range is unwarranted, as DOL concluded that the most reasonable estimate of costs was $16.1 billion. AR522, 564. Accordingly, based on a holistic view of the evidence, a small overlap between the quantified costs and quantified benefits would not justify the conclusion that the rulemaking produced a net loss. Instead, DOL has demonstrated that the rulemaking will produce substantial gains for investors.

An agency's "factual findings are conclusive if supported by substantial evidence." *El Paso Elec. Co. v. FERC*, No. 14-60822, _ F.3d _, 2016 WL 4191137, at *5 (5th Cir. Aug. 8, 2016). DOL has amply satisfied this standard. *See Knapp v. USDA*, 796 F.3d 445, 453-54 (5th Cir. 2015) ("Substantial evidence is more than a scintilla, less than a preponderance, and is such relevant evidence as a reasonable mind might accept as adequate to support a conclusion.").

D. DOL Weighed the Costs and Benefits of Excluding Variable Annuities and FIAs from PTE 84-24

Plaintiffs also challenge DOL's cost-benefit analysis of the inclusion of variable annuities and FIAs only under the BIC Exemption rather than also under PTE 84-24. *See* ACLI Br. 29-32; IALC Br. 24-28.[66] DOL considered the costs for fiduciaries rendering advice regarding variable annuities and FIAs, and quantified insurers compliance costs. *See* AR528-29, 553-54, 598-606.

Plaintiffs claim that DOL's goal "was to steer consumers away from" variable annuities and FIAs and, therefore, that DOL was obligated to consider the costs of reducing investors' access to variable annuities and FIAs. ACLI Br. 30-31; *see also* IALC Br. 27. As usual, Plaintiffs' premise is mistaken and, thus, so is their conclusion. DOL does not doubt that annuities, including variable annuities and FIAs, can be appropriate financial products for retirement investors. *See* AR324 ("These products ... can play a beneficial and important role in retirement preparation."). Nor is DOL's goal to decrease investors' selection of these types of annuities, *per se*. *See* AR624 (DOL "aim[s] to mitigate harms from advisory conflicts without unduly advantaging or disadvantaging any business model"). Instead, DOL seeks to ensure that these annuities—like other classes of financial products—are recommended to IRAs and plan participants only when they would be in retirement investors' best interests and where financial institutions will be held accountable if they violate that standard. In that context, DOL stated:

> Financial products promoted by conflicted advisers likewise enjoy an inefficiently large market share, diverting resources to the products manufacturers (and possibly to manufacturers' profit) from uses more beneficial to investors. The final rule and exemptions are intended and expected to mitigate these economic inefficiencies and to move markets toward a more optimal mix of advisory

[66] ACLI assumes that DOL's general authority statute, 29 U.S.C. § 1135, provides the basis for its decisions regarding these exemptions. ACLI Br. 30. This is incorrect. DOL has specific authority to grant administrative exemptions, and therefore need not rely on its general authority. *See* 29 U.S.C. § 1108(a); 26 U.S.C. § 4975(c)(2). Because DOL's exemptive authority does not include terms requiring cost benefit analysis, DOL's exemption analysis is not controlled by *Michigan v. EPA*, 135 S. Ct. 2699, 2707 (2015) (applying statute requiring agency to determine regulation was "appropriate and necessary"). Regardless, DOL's analysis considered the relevant costs and benefits of its exemptions and satisfied the relevant APA standards. *See generally* Arg. § IV.

services and financial products.

AR624. DOL aims to ferret out mismatched recommendations of products that are not in the individual investors' best interests. AR627-28. This will be a function, not of consumer access to certain products, but of the quality of the recommendations upon which consumers act. For the reasons discussed below, Plaintiffs cannot show that industry compliance with the BIC Exemption or avoidance of conflicted compensation will meaningfully limit investors' options for annuity purchases. *See infra* Arg. § V(C). Accordingly, there is no reason to expect that variable annuities, FIAs, or any other class of products will lose market share—unless that class of products is disproportionately recommended on unjustifiable bases. Thus, DOL was entirely reasonable in declining to quantify reduction in access to these products as a separate consideration.[67]

Plaintiffs also argue that DOL failed to estimate costs for insurance companies "to overhaul their primary distribution model for [FIAs]." IALC Br. 26. For the reasons discussed below, Plaintiffs have not shown that it will be necessary to dismantle the independent agent distribution model. *See infra* Arg. § V(C). DOL concluded that the "insurance companies and distributors of insurance products" could comply with the BIC Exemption. *See* AR599; *see also infra* Arg. § V(C).[68]

Plaintiffs also claim that DOL failed to show that revoking PTE 84-24 for FIAs "would produce benefits commensurate to its conceded costs." IALC Br. 27. DOL estimated that this action could cost insurers between $34 and $37.8 million over the next ten years for the twelve

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[67] The notion that investors might have to pay more for certain products, IALC Br. 27, adds nothing to the cost-benefit analysis because, even if it is presumed that the industry passes all of its costs on to the consumer (and there are market reasons to expect that is unlikely), consumers would still benefit on net. *See* AR324-26. This is especially the case if Plaintiffs merely mean pay more *up front*, without considering the opaque costs already built into the structural scheme and of which many consumers are unaware. *See* AR436-37, 445, 454-56, 458, 615, 634.

[68] Moreover, even if some insurers may overhaul their distribution models, Plaintiffs offered DOL no means to empirically quantify those costs. *Cf. Bus. Roundtable*, 647 F.3d at 1150 (relying on fact that "empirical evidence ... was readily available" in rejecting agency failure to quantify cost).

insurers most likely to be affected.[69] *See* AR602. But DOL had no means to specifically quantify the investor gains in the FIA segment of the annuity market. DOL had asked the industry to provide relevant data, but industry sources indicated that this data "would be prohibitively expensive to compile or obtain." AR485 & n.385; AR68906, 69063-66. And insurer expenses and agent compensation are opaque. *See* AR454-56. The industry should not be able to criticize a rulemaking for failure to analyze information unobtainable except from the industry itself. *See FCC v. Fox Television Stations, Inc.*, 556 U.S. 502, 519-20 (2009) ("It is one thing to set aside agency action under the [APA] because of failure to adduce empirical data that can readily be obtained. It is something else to insist upon obtaining the unobtainable."). Here, DOL established that conflicts of interest are a particular concern for this class of products and, in light of the general evidence regarding the consequences of conflicted advice, are sure to negatively impact retirement investors. *See infra*, Arg § V(A)(1). And in light of the evidence discussed below, it was reasonable for DOL to conclude that investor gains from the protections of the BIC Exemption exceeded the cost to the industry. *See Melcher*, 134 F.3d at 1158.

V. THE INCLUSION OF ANNUITIES IN THE BEST INTEREST CONTRACT EXEMPTION IS REASONABLE

DOL designed the BIC Exemption to serve as a general purpose exemption for almost all prohibited transactions involving conflicted compensation in the "retail market." AR59, 233. DOL gave annuities significant consideration, in part due to the vulnerability of annuity purchasers, who "tend to be at or near retirement age, when individuals are older and have the most assets at stake." AR425. While DOL expressed uncertainty in its 2015 proposal as to whether annuities could comply with the terms of the exemption (particularly those annuities not

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[69] This cost estimate addressed the life insurers DOL was able to specifically identify as selling FIAs and not variable annuities. Most of the compliance costs estimated were large fixed costs incurred the first time the BIC was triggered. Therefore, DOL's cost quantification for this regulatory alternative focused on those firms that DOL could expect would not have had to use the BIC but for the shift of FIAs from 84-24 to the BIC. *See* AR602.

already required to comply with securities laws), it sought comment on that issue and adapted the exemption in numerous ways to accommodate the relevant concerns. AR73-75, 747, 785. Accordingly, DOL ultimately decided that conflicted transactions involving variable annuities and FIAs should be required to rely on the BIC Exemption—the same as most other prohibited transactions in the retail market—and that PTE 84-24 would remain available for only the simplest annuities. AR74, 232-33. DOL's action must be upheld where it "examined the pertinent evidence, considered the relevant factors, and articulated a reasonable explanation for how it reached its decision." *Associated Builders & Contractors*, 2016 WL 3228174, at *2.

A. DOL Sufficiently Explained its Reasons for Including Variable Annuities and FIAs in the BIC Exemption

1. Considerations of complexity, risk, conflicts of interest, and a level playing field justified including variable annuities and FIAs in the BIC Exemption

In light of the complexities, risks, and conflicts of interest associated with variable annuities and FIAs, DOL concluded that the best way to protect retirement investors in the case of conflicted transactions involving those annuities was to include them alongside mutual funds and other classes of products in the BIC Exemption. AR73-75. Because variable annuities are regulated as securities and are sold by brokers and registered investment advisers, it is sensible for them to be treated the same as mutual funds and other similar products. *See* AR356-57, 418. Moreover, variable annuities "place[] all the investment risks on the annuitant," *SEC v. Variable Annuity Life Ins. Co.*, 359 U.S. 65, 71 (1959), and are subject to the same, if not greater, potential conflicts of interest as mutual funds. *See* AR443-50. Variable annuities often carry larger commissions than mutual funds, providing an incentive to sell more of them, and the costs associated with them are more opaque. AR445, 447. Some advisers sell variable annuities that are proprietary products created by their employers, creating even more conflict issues. *Id.* Accordingly, DOL was well justified in applying the same protective conditions of the BIC

Exemption to variable annuities as it did to mutual funds and most other classes of products.

DOL also demonstrated that its decision to treat FIAs the same as variable annuities and similar products was well supported by "significant concerns about [FIAs'] complexity, risk, and conflicts of interest," along with a desire to ensure a level playing field among these annuities and mutual funds. *See* AR237-38. Like variable annuities, FIAs "are complex products requiring careful consideration of their terms and risks," and DOL concluded that customers can easily misunderstand, overestimate, or underestimate the significance of many of the products' terms and attributes. AR74; AR73 (quoting FINRA publication stating that FIAs "are anything but easy to understand"); *see also* AR435, 439, 454-56 (describing the complex features of FIAs and the multiple variables to consider in choosing one).[70] Furthermore, any index-linked gains are generally not fully credited to the investor, which instead depends on the particular features of the FIA, such as participation rates, interest rate caps, and the rules regarding interest compounding. AR598. Given these and other complexities, retirement investors "are acutely dependent on sound advice that is untainted by the conflicts of interest posed by Advisers' incentives to secure the annuity purchase, which can be quite substantial." AR74.

As for risk, the D.C. Circuit has recognized, "[i]n FIAs, as in securities, there is a variability in the potential return that results in a risk to the purchaser." *Am. Equity*, 613 F.3d at 174; *see also* AR439; *Brokers' Choice of Am., Inc. v. NBC Universal, Inc.*, 757 F.3d 1125, 1132 n.4 (10th Cir. 2014) (noting that due to caps on maximum interest earned and fees, it is "common

[70] Specifically, DOL explained that an investor would need to understand (AR74):

> surrender terms and charges; interest rate caps; the particular market index or indexes to which the annuity is linked; the scope of any downside risk; associated administrative and other charges; the insurer's authority to revise terms and charges over the life of the investment; the specific methodology used to compute the index-linked interest rate; and any optional benefits that may be offered, such as living benefits and death benefits. In operation, the index-linked interest rate can be affected by participation rates; spread, margin or asset fees; interest rate caps; the particular method for determining the change in the relevant index over the annuity's period (annual, high water mark, or point-to-point); and the method for calculating interest earned during the annuity's term (e.g., simple or compounded interest).

for an annuitant's yields to be somewhat lower than expected"). Principal can be lost if the annuity is cancelled early, due to surrender charges and tax consequences, *see* AR73-74, both of which can be substantial.[71] This makes purchasing an annuity product costly to reverse. AR447.

In addition to the complexity and risks involved in FIA purchases, there are inherent conflicts of interest. *See supra* Stmt. of Facts § II(B). Compensation amounts are tied to the advice given, incentivizing agents to sell particular products. And while the complexity of these products render investors particularly reliant on agents' advice, opaque compensation arrangements often leave investors unaware that agents may be steering them toward higher commission products that may not be in their best interest. *See* AR325, 437, 458; *see also* AR234 (noting concern that FIAs, in particular, "have often been used as instruments of fraud and abuse"). For all of these reasons, DOL reasonably concluded that the "stringent anti-conflict policies and procedures" of the BIC Exemption would be more appropriate for variable annuities and FIAs to protect retirement investors. AR234; AR238 (exemption's contractual commitment to adhere to the impartial conduct standards, adoption of anti-conflict procedures, and disclosures "are necessary to address dangerous conflicts present in transactions involving these products").

Moreover, DOL reasoned that treating variable annuities, FIAs, and mutual funds the same under the rulemaking would ensure a level playing field and "avoid[] creating a regulatory incentive to preferentially recommend indexed annuities" based on the reduced level of regulation, rather than the interests of retirement investors. AR74. DOL's rationale is supported by *American Equity*, in which the D.C. Circuit found it reasonable to treat variable annuities and FIAs the same for purposes of securities laws. 613 F.3d at 172-76.[72] The court noted that FIAs

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[71] *See* AR66942, 66968, Wink's Sales & Market Report, 4th Quarter, 2014 (the most common surrender period is ten years, but higher periods are still relatively common); AR42536 (Cmt. 774, IALC) (acknowledging that "[m]ost products sold today" have surrender periods of up to ten years and surrender charges up to ten percent, implicitly acknowledging that some products have higher rates).

[72] On separate grounds, the D.C. Circuit struck down the SEC rule for failure to sufficiently analyze "efficiency, competition, and capital formation." *See id.* at 179. That Securities Act requirement does not apply here.

are "hybrid financial product[s]" that, like variable annuities, "involve considerations of investment not present in the conventional contract of insurance," including risk to the purchaser and "appeal ... not on the usual insurance basis of stability and security but on the prospect of growth through sound investment management." *Id.* at 168, 174. Indeed, variable annuities and FIAs are in direct competition. *See* AR434 ("[FIA] sales are rapidly gaining market share compared to variable annuity sales").[73] Thus, for this reason too, it was reasonable for DOL to require conflicted transactions involving both FIAs and variable annuities to proceed under the BIC Exemption.

2. *DOL's distinction between declared-rate annuities and FIAs is well justified and entitled to deference*

IALC argues that DOL's decision to leave declared-rate annuities in PTE 84-24, while requiring FIA transactions to proceed under the BIC Exemption, is arbitrary because FIAs "are identical" to declared-rate annuities "in almost all respects." IALC Br. 28. IALC acknowledges, however, that FIAs differ from declared-rate annuities in the manner interest is determined and credited. *Id.* 29. This difference is highly significant because the many variations and crediting options for FIAs give rise to great complexity, *see* AR600 ("[FIAs] are anything but easy to understand.... Because of the variety and complexity of the methods used to credit interest, investors will find it difficult to compare one [FIA] to another."), and may cause investors to be left with impressions—from marketing or otherwise—that do not match the reality. *See id.* ("Investors can all too easily overestimate the value of these contracts, misunderstand the linkage between the contract value and the index performance, underestimate the costs of the contract, and overestimate the scope of their protection from downside risk (or wrongly believe they have

[73] Commenters also suggested that, to some extent, variable annuities and FIAs are converging in design. *See* AR41637-38 (Cmt. 718, Allianz Life Ins. Co.) (describing various combination products that include characteristics of both variable and FIAs); AR46747 (Cmt. 3083, Jackson Nat'l Life Ins. Co.) ("these products [have] becom[e] remarkably similar").

no risk of loss).”). Thus, even aspects of FIAs that are similar to those of declared-rate annuities—such as surrender terms and minimum nonforfeiture provisions—take on added significance given the complexity of the product and the effect those aspects can have on their growth-without-risk appeal.

Plaintiffs also overstate the similarities between the products. *See* AR440-42 (chart comparing features of annuities). In addition to the undisputable greater risk involved with FIAs, commissions are typically higher for FIAs than for declared rate annuities. *See* AR447; AR46846 (Cmt. 3090, Fund Democracy). And FIAs, like variable annuities and unlike most declared-rate annuities, are generally sold with guaranteed living benefit riders, which come in several types, involve extra cost, and “because of their variability and complexity may not be fully understood by the consumer.” AR435, 441-42. Taken together, DOL had ample grounds to distinguish between them in its exemptions. *Cf. Westar Energy, Inc. v. FERC*, 473 F.3d 1239, 1241 (D.C. Cir. 2007) (agency should “point to a relevant distinction between the two cases”).

3. DOL’s rulemaking appropriately treats classes of products differently due to the varying degrees of risk they pose to investors

Plaintiffs mistakenly contend that in providing for immediate annuities and declared-rate deferred annuities in PTE 84-24 and other annuities in the BIC Exemption, DOL improperly attempted to “regulate retirement products themselves.” ACLI Br. 23. And Plaintiffs erroneously assert that DOL intends this choice to “impair access to” FIAs and variable annuities. *Id.* 24. This argument fails for numerous reasons.

First, DOL has abundant authority to craft exemptions for a “class” of products that are tailored to the attributes of specific investment products or transactions as it has done here. 29 U.S.C. § 1108(a) (giving DOL the authority to exempt a “class of fiduciaries or transactions”); 26 U.S.C. § 4975(c) (largely same). Shortly before ERISA’s prohibited transaction provisions went into effect, *see* 29 U.S.C. § 1114(c)(4), DOL granted a class exemption allowing plans to

purchase insurance or annuity contracts or mutual funds from insurance agents or brokers who received a commission. *See* 42 Fed. Reg. 32395 (June 24, 1977) (predecessor to PTE 84-24). Since then, DOL has provided numerous exemptions for particular investment products or transactions.[74] Plaintiffs would be content with PTE 84-24 if it singled out annuities from mutual funds but claim that DOL lacks authority to look behind the "annuity" label and find relevant distinctions among types of annuities. ACLI Br. 23. This notion would be similar to claiming that DOL cannot look behind the "securities" label and craft an exemption specifically for mutual funds, as has long been the case.[75] Such a limitation on DOL's exemption authority cannot be squared with the statutory text, which provides DOL broad flexibility to craft conditional exemptions that protect investors in the case of otherwise prohibited transactions. *See* 29 U.S.C. § 1108(a) (DOL may grant "conditional" exemptions, of "*any* fiduciary or transaction, or class of fiduciaries or transactions" from "*all or part* of the restrictions," upon finding the exemption is "in the interests of" and "protect[s] the rights of" investors); 26 U.S.C. § 4975(c) (largely same).[76] Indeed, it is difficult to imagine how DOL could make the requisite findings without assessing the conflicts associated with the particular types of products involved in the transactions that are the subject of the exemptions. Here, DOL has merely applied different standards to widely-recognized categories of annuities based on the different risks they pose to consumers. *See supra* Arg. § V(A)(1). This is not a case where an agency has "treat[ed]

[74] *See, e.g.*, PTE 2004-07, 69 Fed. Reg. 23220 (Apr. 28, 2004) (real estate investment trusts); PTE 94-20, 59 Fed. Reg. 8022 (Feb. 17, 1994) (foreign exchange transactions); PTE 91-55, 56 Fed. Reg. 49209 (Sept. 27, 1991) (American eagle coins); PTE 75-1, 40 Fed. Reg. 50845 (Oct. 31, 1975) (broker-dealers and banks), as amended 71 Fed. Reg. 5883 (Feb. 3, 2006), and as amended, 81 Fed. Reg. 21208 (Apr. 8, 2016)).

[75] *See, e.g.*, PTE 77-4, 42 Fed. Reg. 18732 (Apr. 8, 1977) (providing exemption for mutual funds, but not other securities), as amended at 81 Fed. Reg. 21208 (Apr. 8, 2016).

[76] *FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120 (2000), cited by Plaintiffs, ACLI Br. 24, is not on point. The Court in that case found that the FDA did not have the authority to regulate tobacco because the FDA had consistently taken the position that it did not have such authority, and Congress had declined to adopt a number of bills granting FDA such authority. *See* 529 U.S. at 143, 161. By contrast, ERISA gave DOL express authority to grant conditional administrative exemptions, and DOL has consistently exercised that authority.

like cases differently." *Eagle Broad. Grp., Ltd. v. FCC*, 563 F.3d 543, 551 (D.C. Cir. 2009). And thus, DOL neither exceeded its authority nor acted unreasonably. *See Brown & Williamson*, 710 F.2d at 1176 ("Agencies must be able to distinguish … among products on the market which subject the public to varying degrees of risk."); *Ranchers Cattlemen Action Legal Fund United Stockgrowers of Am. v. USDA*, 499 F.3d 1108, 1120 (9th Cir. 2007) (no APA violation where "the agency … justified its different treatment" of products based on the different risks they presented).

Second, the mere fact that retirement products are also regulated under other legal regimes, such as securities law and state insurance law, does not curtail DOL's exemption authority, which reaches all investment products for which employee benefit plan and IRA moneys will be used. *See, e.g.,* 29 U.S.C. § 1002(21)(A) (reaching investment advice with "respect to any moneys or other property" of a plan); § 1106(a)(1)(A), (D), (E) (listing prohibited transactions, including the "sale ... of *any property* between a plan and a party in interest"; the "transfer to ... a party in interest, of *any assets* of the plan"; and the "acquisition, on behalf of the plan, of *any* employer *security* or employer real property in violation of" § 1107(a) (emphasis added)); AR344. By granting authority to exempt transactions involving securities, insurance, or other investment products, Congress expressly contemplated that DOL's exemptions will encompass fiduciaries in these markets.[77] Recognizing the reality that those who render investment advice—like those in many other industries—are subject to other governing authorities, *see* AR346, DOL coordinated with the SEC staff, state insurance regulators, and the NAIC to ensure that the rulemaking is harmonized to the fullest extent possible with securities

[77] DOL has thus granted numerous exemptions that pertain to securities and insurance products, including those that address insurance company general accounts, *see* PTE 95-60, 60 Fed. Reg. 35925 (July 12, 1995); insurance company pooled separate accounts, *see* PTE 90-1, 55 Fed. Reg. 2891 (Jan. 29, 1990); the execution of securities transactions, *see* PTE 86-128, 51 Fed. Reg. 41686 (Nov. 18, 1986), as amended 67 Fed. Reg. 64137 (Oct. 17, 2002), 81 Fed. Reg. 21181 (April 8, 2016); life insurance, health insurance or annuity contracts that fund employee benefit plans, *see* PTE 79-41, 44 Fed. Reg. 46365 (Aug. 7, 1979).

and insurance regimes. *See* AR14-15; AR74-75. The fact that the transactions regulated by the exemptions involve persons or products that also fall within the jurisdiction of other regulators, *see* ACLI Br. 23, does not curtail DOL's authority to regulate them for ERISA's distinct purposes. *See, e.g., Uselton v. Commercial Lovelace Motor Freight, Inc.*, 940 F.2d 564, 585 (10th Cir. 1991) (discussing with approval the overlap of ERISA and securities regulation).

Third, DOL does not seek to restrict access to any specific product, but instead seeks to serve Congress's goal to prohibit all conflicted transactions except to the extent the harms to retirement investors can be sufficiently mitigated. *See* AR70 (BIC Exemption "does not limit the types of investments that can be recommended by Advisers and Financial Institutions"). Thus, the rulemaking does not "pick and choose retirement products for American consumers," ACLI Br. 24, or regulate the design or manufacture of investment products. *See* AR627. Rather, it requires only that in recommending any one product, investment advice fiduciaries adhere to professional standards of prudence and put the interests of the retirement investor in the driver's seat, rather than those of the adviser or other parties. AR71 ("It is not [DOL]'s intent to foreclose fiduciaries ... from recommending [any securities and other investment products] if they prudently determine that they are the right investments for the particular customer and circumstances."); AR85. Contrary to Plaintiffs' characterizations, *see* ACLI Br. at 24-25, this is fully consistent with ERISA and DOL precedent. Plaintiffs' selective quotation of DOL congressional testimony—explaining that DOL "does not sit in independent judgment regarding ... the investment proposals themselves"—is entirely consistent with DOL's actions here. *See Modernizing ERISA to Promote Retirement Security: Hearing Before the H. Subcomm. on Employer-Employee Relations of the H. Comm. on Educ. and the Workforce*, 106th Cong. 42 (2000) (Leslie Kramerich, Acting Assistant Secretary of Labor) (Defs.' App'x 4). At that hearing, DOL elaborated that "the merits of the transaction are important and are among the various factors considered in the [exemption] application process," and that "we expect the

transaction to be structured to ameliorate potential conflicts of interest." *Id.*[78] These are the very considerations that animated DOL's choices pertaining to PTE 84-24 and the BIC Exemption. *See* AR73-75, 232-35. Moreover, the rulemaking's goal to move the market for retirement investment products toward advisory structures with fewer conflicts of interest, *see, e.g.*, AR624, is not invidious discrimination against FIAs or variable annuities as classes of products, as Plaintiffs suggest, ACLI Br. 23-24, but an attempt to ensure that those engaging in any transactions involving specific types of products minimize their conflicts of interest. *See* AR598-602.

B. DOL Appropriately Took Existing Annuity Regulation into Account in Determining How to Regulate Variable Annuities and FIAs

Plaintiffs also argue that DOL failed "to determine whether, under the existing regime, sufficient protections [already] exist" for annuities. ACLI Br. 32 (quoting *Am. Equity*, 613 F.3d at 179). To the contrary, DOL did extensively consider both existing securities regulation relevant to variable annuities and the state insurance regulation relevant to all annuities, and concluded that its consumer protections were not sufficient. *See* AR344-63, 421, 426-28.

As Plaintiffs acknowledge, DOL concluded that "notwithstanding existing [regulatory] protections, there is convincing evidence that advice conflicts are inflicting losses on IRA investors." ACLI Br. 32 (quoting AR426-27, 475-76). But they argue that because the studies on which DOL relied primarily involved mutual funds, DOL "offered no reasoned explanation" for extrapolating from these studies to insurance products. ACLI Br. 33. The record demonstrates otherwise. The CEM study on which DOL's quantitative benefits are based isolated how conflicts of interest embedded in front-end loads—*i.e.*, commissions, *see* AR444—

[78] *See also id.* at 8 ("It is important to keep in mind there are strong policy considerations in assuring that any advice provided to participants is informed and unbiased. Conflicted advice can result in participants paying higher fees and making inappropriate investment decisions."); *id.* (noting that "new relationships that have developed between old and new players in the financial marketplace .... complicates [DOL's] job of identifying conflicts and the potential for risk or abuse").

paid to brokers in the mutual fund market bias their advice in ways that are harmful to consumers. *See* AR469, 488-89.[79] Because such conflicts exist in both the mutual fund and annuity markets, *see* AR454, DOL reasonably extended its analysis to the annuity market where the commissions are larger and less transparent and products are more complex, leaving consumers more vulnerable to bad advice. *See* AR437-39, 447-48, 474. Such analogies are appropriate. *Cf. Nat'l Small Shipments Traffic Conf.*, 618 F.2d at 831 ("Whether … air taxis are fully representative of the whole industry" it was "appropriate for the Board to look to the[ir] experience … to predict the impact of the proposal on other carriers" because "the air taxis have operated in the type of competitive setting that the exemption is designed to promote").

Moreover, DOL found additional support for concluding that the annuity market is influenced by substantial conflicts of interest in insurance-related studies that could be applied by analogy—such as one demonstrating that contingent commissions "align the insurance agent or broker's incentive with the insurance company, not with the consumer," AR438,[80] and a field experiment study of life insurance sales in India (whose compensation structures are similar to those in the U.S.) showing that insurance agents systematically recommended more expensive products, especially for less sophisticated clients. AR464-65.[81] Not least, DOL noted surveys showing that insurers identified conflicts of interest and failure to recommend products that meet

[79] While DOL also discussed other harms stemming from conflicts of interest, such as frequent trades or timing errors, these are not the harms the CEM study quantified. Accordingly, Plaintiffs' attempt to distinguish FIAs from mutual funds on these ground are unavailing. *See* IALC Br. 19.

[80] "Contingent commissions" are an "arrangement in which an insurance agent or broker receives a percentage of the premiums realized by the insurer, if the agent of broker meets certain goals" set by the insurer. AR438. While the studies involved such commissions in the commercial property-casualty insurance market, similar arrangements exist for annuities. *See id.*

[81] The very article on which IALC relies for its observation that existing empirical studies regarding insurance had produced "few robust conclusions." IALC Br. 19-20 (citing IALC App. 175); AR31679, goes on to support DOL's analysis: "[A]lthough insurance-specific evidence is ultimately quite limited, we conclude that the extant empirical literature considered as a whole, suggests that the problem of biased advice by insurance agents is likely to be significant." AR31677; IALC App. 171.

investors' needs as the field's most significant ethics problems, AR463-64,[82] and state regulators' observations regarding abuses. *See, e.g.*, AR41538 (Cmt. 706, NASAA) ("Rollovers and account transfers are an area where state securities regulators routinely see abuse, such as in cases where an investor is advised to liquidate a well-balanced portfolio in exchange for an over-concentration in a high-fee product."). Indeed, Plaintiffs point to no evidence exonerating annuity markets of conflicts of interest or suggesting that such conflicts do not harm annuity investors. Accordingly, taking the RIA together as a whole, DOL provided a reasoned explanation for concluding that conflicted compensation harms annuity investors, *see* AR474, and this conclusion does not "run[] counter to the evidence before the agency." *Markle Interests*, 2016 WL 3568093, at *3.

The existing regulatory regimes for insurance products do not undermine these conclusions. Both the sale of mutual funds by brokers and the sale of annuities by insurers are governed by regimes that primarily rely on disclosure and suitability requirements. *See* AR427 (noting that state insurance rules "often resemble an NAIC model, which in turn resembles the FINRA model"). Accordingly, there is no reason to expect that existing laws governing insurance would substantially lower the risk of harm to investors from conflicted compensation observed in the mutual fund context. Indeed, DOL specifically examined disclosure and suitability standards and concluded that they provided insufficient protections. *See* AR427, 465, 585, 587. And state insurance laws—and their enforcement—vary significantly, with only 35 states having adopted some version of the 2010 NAIC Model Regulation. AR358, 427, 601; AR27908-14. As DOL explained, the lack of uniformity among states "create[s] uneven protections and confusion for consumers" and "that differences in standards between the states

[82] Plaintiffs criticize the surveys from 1990, 1995, and 2003 as being outdated. See IALC Br. 20. Even if this data is less dispositive than newer information would be, Plaintiffs have not justified entirely disregarding it. DOL concluded that the consistency in the surveys "suggest structural and cultural issues deeply embedded in the insurance business model." AR464.

provide opportunities for arbitrage, if not a race to the bottom." AR601.

Plaintiffs also argue that nine empirical studies on which DOL relied to conclude that conflicted compensation harms investors, *see* AR474-77, should be disregarded because they involved data from before 2010, and the NAIC and FINRA subsequently strengthened their model rules. *See* ACLI Br. 32-33. But Plaintiffs ignored that DOL updated the CEM study with data through 2015 and found no meaningful difference between the original data and the more recent period. *See* AR646-47. Similarly, DOL reviewed data for the period 2008-2014 submitted by a commenter and concluded that this did not change its conclusions. AR479-82, AR649 n.624. Regardless, as valuable as the NAIC and FINRA improvements may be for consumers in some respects, they do not fundamentally change the limitations that come with a disclosure and suitability regime, and DOL reasonably concluded that they were not sufficient safeguards to address ERISA's priorities for the protection of retirement investments.[83] *See, e.g.*, AR41538 (Cmt. 706, NASAA).[84] Contrary to Plaintiffs' claims, DOL has "made a reasonable effort to ensure that appropriate data was relied upon" in reaching its conclusions. *Resolute Forest Products, Inc. v. USDA*, No. 2016 WL 2885869, at *19 (D.C. Cir. May 17, 2016).

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[83] Plaintiffs cite decreased complaint data in an attempt to show that NAIC's 2010 Model Regulation had dramatically improved the regulatory landscape. *See* ACLI Br. 34 (quoting AR47392, Cmt. 61, ASH Brokerage, which in turn cited Linda Koco, *FIA Complaints Rise Unexpectedly*, www.insurancenewsnet.com (Mar. 11, 2015) [Link] (Defs.' App'x 5). The information to which they point exclusively relates to FIAs, not variable annuities. Moreover, it shows that FIA complaints increased in 2014 after declining for several years. *See* Defs.' App'x 5. Regardless, this complaint data is not a reliable guide to the scope of the problem for at least three reasons: 1) for complex products such as these, many consumers may remain unaware that a transactions was not in their best interest, AR445, 456, and 2) the information is drawn from the NAIC's Complaint Database System, which is underinclusive because it depends on voluntary submissions of complaints "deemed confirmed" by state insurance departments, *see, e.g.*, NAIC Closed Confirmed Consumer Complaints by Coverage Type (July 25, 2016) [Link] (Defs.' App'x 6), and 3) information relied on in the public comment appears to focus only "equity indexed" coverage code, even though far more complaints are reported under the more general "annuity" code. *See id.* at 3.

[84] IALC argues that DOL failed to explain why state regulation plus the protections offered by PTE 84-24 are not sufficient "to prevent any abusive sales practices associated with [FIAs]." IALC Br. 24. But as discussed above, DOL did explain why it concluded it was important to provide for FIAs in the BIC Exemption. *See supra* Arg. § V(A)(1)-(2); AR598-602. And as discussed in this section, nothing about existing state regulation undermined DOL's conclusion.

C. The BIC Exemption is Sufficiently Workable for Annuities

ACLI argues that DOL could not properly find that the BIC Exemption is "administratively feasible" for annuities. ACLI Br. 27. This argument is misplaced. DOL has satisfied its statutory requirements, *see* 29 U.S.C. § 1108(a); 26 U.S.C. § 4975(c)(2), by affirmatively finding that the exemption is administratively feasible. *See* AR59 ("[T]he Department has determined that the exemption is administratively feasible[.]"); see also AR65, 76, 101, 117, 131. Moreover, this requirement has long been construed to require consideration of whether an exemption is feasible for DOL to administer, rather than workable for the industry.[85] Plaintiffs' assumption to the contrary is completely unsupported and contrary to the plain language of the standard, which suggests that the term refers to feasibility for the *administrative* agency—not the regulated industry.

Even though workability for the industry is not a statutory criterion (much less for every single entity in the retirement investment marketplace), DOL did not "entirely fail to consider" this aspect of the problem. *Markle Interests*, 2016 WL 3568093, at *3. DOL considered the issues Plaintiffs claim make the BIC Exemption unworkable—and even provided solutions to address many of them. AR567-68; *see supra* Stmt. of Facts § II(D). Accordingly, there is no APA basis for Plaintiffs' contention that the BIC Exemption is unworkable.

First, ACLI argues that the BIC Exemption is unworkable because DOL did not provide sufficient guidance regarding what constitutes "reasonable compensation." *See* ACLI Br. 27-28. However, far from incorporating an unknown standard, DOL, at the suggestion of several

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[85] *See* 91 Pens. & Ben. Rep. (BNA) A-4 (June 21, 1976) (Defs.' App'x 7) (DOL statement at American Bar Association event characterizing "administratively feasible" to "involve[] consideration of the resources of the Department and the Internal Revenue Service in relation to the amount of monitoring by the agencies that the exemption would require"); Bill Schmidheiser, Note, ERISA's Prohibited Transaction Restrictions: Policies and Problems, 4 J. Corp. L. 377, 405 (1979) (citing Exhibit B for proposition that criterion "means feasible for the Departments to administer, given the Departments' resources and the nature of the transaction sought to be exempted").

commenters,[86] relied on the same standard in one of the core statutory exemptions, applicable to all service providers, that Congress included when ERISA was passed. *See* 29 U.S.C. § 1108(b)(2).[87] The standard, as DOL explained, is applicable to fiduciaries under the common law of agency and trusts, and, since 1977, has applied to insurance transactions under PTE 84-24 and its predecessor exemption.[88] Here, DOL provided guidance regarding relevant factors to consider. *See* AR85. And the same standard has been applied by numerous courts in similar contexts showing that the longstanding and widely used provision is eminently workable.[89]

Second, Plaintiffs argue that the "best interest" standard is too vague. ACLI Br. 27-28. The best interest standard incorporates the longstanding fiduciary duties of prudence and loyalty. AR133; BIC Exemption § II(c)(1). These duties are "deeply rooted in ERISA and the common law of agency and trusts." AR82. DOL has described the standards at length, *see* AR82-85, and their application to various contexts. *See, e.g.*, AR87, 94, 111, 115. Plaintiffs do not even

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[86] *See* AR 38126 (Cmt 506, SIFMA); AR39161 (Cmt. 584, Invesco Ltd.); AR41130 (Cmt. 676, Northwestern Mut. Life. Ins. Co.); AR41286 (Cmt. 687, Prudential Financial, Inc.); *cf.* AR40843-45 (Cmt. 660, Consumer Federal of Am.) (relying on DOL's interpretation of § 1108(b)(2)).

[87] Under this exemption, a fiduciary may enter a contract with "a party in interest" for "services necessary for the establishment or operation of the plan" so long as "no more than reasonable compensation is paid therefor." *Id.* DOL's longstanding regulation implementing this provision states that "[g]enerally, whether compensation is reasonable ... depends on the particular facts and circumstances." 29 C.F.R. § 2550.408c-2(b)(1); 42 Fed. Reg. 32389, 32393 (June 24, 1977).

[88] *See* 71 Fed. Reg. 5887, 5889 (Feb. 3, 2006) ("The combined total of all fees, commissions and other consideration received by the insurance agent or broker, ... [in] connection with the purchase of insurance or annuity contracts ... issued by an investment company is not in excess of 'reasonable compensation' within the contemplation of section 408(b)(2) and 408(c)(2) of the Act and sections 4975(d)(2) and 4975(d)(10) of the Code."); 49 Fed. Reg. 13208, 13211 (Apr. 3, 1984) (adoption of PTE 84-24); 42 Fed. Reg. 32395, 32398 (Jun. 24, 1977) (PTE 84-24's predecessor).

[89] *Compare N.Y. State Teamsters Health & Hosp. Fund v. Centrus Pharmacy Sols.*, 235 F. Supp. 2d 123, 129 (N.D.N.Y. 2002) (holding that claim processing fees were reasonable under "the facts and circumstances of this case"); *with Chao v. Graf*, No. 01-0698, 2002 WL 1611122, at *13 (D. Nev. Feb. 1, 2002) (granting preliminary injunction based in part on finding that fees for marketing services were likely excessive and therefore unreasonable). *See also, e.g.*, *Guardsmark, Inc. v. BlueCross & BlueShield of Tenn.*, 169 F. Supp. 2d 794, 803 (W.D. Tenn. 2001) (defendant received unreasonable compensation by overcharging for administrative and run-out fees and wrongfully overpaying claims); *I.B.E.W. Local 1448 Health & Welfare Fund v. Thorndyke Int'l, Inc.*, No. 97-cv-5718, 1998 WL 764753, at *4 (E.D. Pa. Oct. 26, 1998) (determining that 7% "finders fee" paid to party in interest who helped set up employee benefit plan was "reasonable compensation"); *Kouba v. Joyce*, No. 83-C-451, 1987 WL 33370, at *6 n.22 (N.D. Ill. Dec. 31, 1987) (upholding contingency fee arrangement for litigation based on "the facts and circumstances as they appeared to the contracting parties at the time the agreement was entered").

attempt to show that these "well-known standards," AR125, are unworkable.

Third, Plaintiffs argue that the availability of private litigation over violation of the impartial conduct standards gives rise to "unforeseeable" and "potentially staggering, liability." ACLI Br. 28. Plaintiffs' allegations are speculative and unsupported. DOL considered the issue, and determined that the possibility of litigation incentivizes compliance, and that several features of the final exemption "should temper concerns about the risk of excessive litigation," including provisions permitting arbitration of individual claims and contractual waiver of claims for rescission or punitive damages. *See* AR77-78. Fiduciaries selling annuities to employee benefit plans have been subject to the duties of prudence and loyalty from ERISA's inception. *See* 29 U.S.C. § 1104(a)(1)(A), (B). And those using the § 1108(b)(2) exemption or PTE 84-24 have been subject to the reasonable compensation standard for about 40 years. All of these standards have been subject to private enforcement, *see* 29 U.S.C. § 1132(a)(2), (3), yet Plaintiffs point to no evidence that their application has been unworkable.[90] Regardless, where DOL has merely borrowed statutory standards in appropriately analogous contexts, it is unclear why some level of burden on the industry to qualify for an exemption would be unjustified when consistent with the burdens Congress directly imposed on the industry for other purposes.

Fourth, Plaintiffs argue that, despite DOL's express provision for the sale of an insurer's own "proprietary products," *see* AR136-37, BIC Exemption § IV, brokers and insurance agents will be unwilling to sell them due to a lack of "clear guidance about how to avoid liability." ACLI Br. 29. DOL did provide guidance regarding the sale of proprietary products, including a checklist in the exemption's preamble. *See* AR108-11. It also made clear that the prudence standard "does not impose an unattainable obligation ... to somehow identify the single 'best'

[90] Contrary to Plaintiffs' claim, state law litigation regarding *IRA transactions*—which has always been available—does not conflict with ERISA's provision of a "single uniform national scheme" regarding *employee benefit plans*, for which ERISA preempts most state law claims. *See Gobeille v. Liberty Mut. Ins. Co.*, 136 S. Ct. 936, 947 (2016).

investment ... out of all the investments in the national or international marketplace, assuming such advice were even possible." AR85. Plaintiffs single out only one issue of concern—DOL's warning that an adviser may not always find something to recommend. AR111. DOL explained that if the limited menu of proprietary products "does not offer an investment that meets the prudence and loyalty standards with respect to that particular customer," then the adviser may not recommend a product from that menu. *Id.* For example, it may be imprudent to recommend an annuity to a customer that has few liquid assets and needs immediate access to those assets. In that circumstance, an adviser could not justify a recommendation to buy an illiquid annuity subject to large surrender charges merely because that's the only type of product offered by the firm or adviser . *Id.* This is not a vague source of liability, but common sense.[91]

Fifth, Plaintiffs claim it is "impossible for the insurance company to comply" with the financial institution supervisory responsibilities for independent agents. Chamber Br. 38-39; *see also* IALC Br. 25. These claims are based on a misunderstanding of the impartial conduct standards and the supervisory structure of the BIC Exemption. An insurer supervising an agent will not need to supervise the sale of other companies' products, but will need to ensure only that recommendations and sales concerning its own products meet the standards. *See, e.g.*, AR133, BIC Exemption § II(d)(3) (financial institution's obligations extend to its own practices and those of "any Affiliate or Related Entity," not unrelated competitors); AR85; *cf.* AR27900, NAIC Model Regulation § 6(F)(3) (insurer not required to include in its system of supervision a producer's recommendations of products other than annuities offered by the insurer). In discussing the circumstances "when more than one Financial Institution is involved in the sale,"

[91] IALC expects that where the insurance company signs the contract, an independent agent's sale of that company's product would fall under the proprietary product provision. IALC Br. 39. This is mistaken. This provision will not be directly applicable to insurers working with independent agents unless the financial institution "limits Advisers' investment recommendations, in whole or part, based on whether the investments are Proprietary Products." AR136, BIC Exemption § IV(b). Regardless, IALC appears to think such a requirement would be unfair, but does not identify any reason this makes the exemption unworkable.

DOL explained that the signing financial institution is responsible for incentives associated with that transaction—such as incentives offered by the product manufacturer even when the signing financial institution is a broker or registered investment adviser. *See* AR123. While Plaintiffs misread this preamble discussion, *see* IALC Br. 25, context makes clear that only the incentives of affiliates and related entities present a concern.

Finally, Plaintiffs claim that insurance companies will be unable to maintain the independent agent distribution model through which FIAs are commonly sold. *See* IALC Br. 25; ACLI Br. 29; Chamber Br. 39. Contrary to Plaintiffs' claims, DOL acknowledged and considered this distribution model throughout its analysis and identified several available options.[92] Sixty percent of insurance agents are also registered to handle securities, *see* AR419, and the broker or registered investment adviser with which they are affiliated could serve as the financial institution. *See* AR139, BIC Exemption § VIII(e). A third party, such as an IMO, could take on much or all of the insurance company's oversight work even where the insurance company signs the contract. *See* AR90 (leaving flexibility for firms to design oversight procedures "effective for their particular business model"). Alternatively, IMOs or others may seek exemptions to become "financial institutions" separately charged with duties under the BIC Exemption—and several IMOs have already submitted applications. BIC Exemption § VIII(c)(5) (permitting entities to apply for an individual exemption, and creating a mechanism for other entities that meet the same conditions to rely on the new exemption). Plaintiffs have

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[92] *See* AR354 (discussing independent agents); *id.* 417-20 (describing agents and market intermediaries, including observation that insurers in FIA market "heavily rely on independent insurance agents"); *id.* 421 ("The type of products and the distribution channels are intertwined[.]"); *id.* 447 (chart of sales by distribution channel); *id.* 460 (discussing "potential conflicts affecting insurance intermediaries"); *id.* 554 & n.519 (acknowledging that "[i]ndependent insurance agents could also be affected" and that some of their costs could be encompassed in the calculation of insurer costs); *id.* 570 ("[s]mall service providers affected by this rule include ... insurance companies and agents, ... and others providing investment advice to plan and IRA investors"); *id.* 626-27 (discussing choices IMOs and independent agents will face). *See also* AR123 (BIC Exemption discussing IMOs in context of financial institution definition); AR246 (stating intent not to disrupt payment of commissions thru intermediaries).

not shown that even insurance-only agents will be unable to find a place in the revised system. And even if some fraction of such agents choose to exit the market or take another role,[93] DOL provided reasonable grounds to conclude that this will not cause a large reduction in available advisers or impair investors' access to advice. *See* AR131, AR623-27.

In sum, having examined the relevant evidence and factors regarding the ability of annuity providers to comply with the BIC Exemption, and articulating a reasoned explanation for its decision, DOL satisfied the APA requirements. *Associated Builders & Contractors*, 2016 WL 3228174, at *2.

D. DOL Provided Adequate Notice and Opportunity to Comment on the Scope of Annuities to be Covered by PTE 84-24

Plaintiffs' final APA claim is that changes DOL made to the final amendment to PTE 84-24 could not reasonably have been anticipated by the regulated industry and therefore were not a "logical outgrowth" of the proposed exemption. Chamber Br. 39; ACLI Br. 28-29; IALC Br. 31-34. Because DOL provided adequate notice for its actions, this claim fails.

"The APA notice requirement is satisfied if the notice fairly apprises interested persons of the subjects and issues the agency is considering; the notice need not specifically identify every precise proposal which the agency may ultimately adopt as a final rule." *Chemical Mfrs. Ass'n v. EPA*, 870 F.2d 177, 203 (5th Cir. 1989); 5 U.S.C. § 553(b)(3). "A final rule is a logical outgrowth [of the proposed rule] if affected parties should have anticipated that the relevant modification was possible." *Allina Health Servs. v. Sebelius*, 746 F.3d 1102, 1107 (D.C. Cir. 2014). The public "need not have an opportunity to comment on every bit of information influencing an agency's decision." *Texas v. Lyng*, 868 F.2d 795, 800 (5th Cir. 1989). "[C]ourts

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[93] Such market adjustments happen even without new regulation. AR625 (noting that these "markets ... are highly dynamic. They are characterized by innovation in both product lines and business models, and by large ongoing shifts in labor and other resources across product and service vendors and business models"); *see, e.g.*, AR67048-49 (Wink's Sales & Market Report 2014 (listing more than 60 companies that exited, entered, or reentered FIA market).

must proceed with caution before deeming a Final Rule too attenuated from the Proposed Rule, lest [they] supplant the agency's role in the nation's regulatory scheme." *ConocoPhillips*, 612 F.3d at 834.

Here, DOL's decision to require FIA transactions to rely on the BIC Exemption, rather than PTE 84-24, for exemptive relief, grew logically from its 2015 proposal. Importantly, as proposed, the BIC Exemption applied to all annuity transactions. And DOL's notices raised questions about the line to be drawn between variable annuities and other types of annuities for purposes of distinguishing transactions that would be required to use the more protective BIC Exemption and those that could continue to use PTE 84-24 as amended. *See supra* Stmt. of Facts § II(D). DOL both invited comment on whether its proposal had "drawn the correct lines between insurance and annuity products that are securities and those that are not," AR747, and queried whether its decision to "leave in place relief for IRA transactions involving insurance and annuity contracts that are not securities strikes the appropriate balance and is protective of the interests of IRAs." AR790. These statements made clear that DOL was considering whether the proposed categorizations were protective enough of IRA investors and that, based on the comments elicited, it could decide to put FIA transactions on the other side of the proposed line.

Circuit precedent demonstrates that these statements provided adequate notice for purposes of the APA. For example, the Fifth Circuit held that a final rule's "comprehensive definition of 'earnings' was a logical outgrowth of DOL's OSHA rulemaking proceedings," rejecting appellees' argument that, because the definition itself was not in the proposal, they lacked notice that "premium payments" would be included. *United Steelworkers of Am., AFL-CIO-CLC v. Schuylkill Metals Corp.*, 828 F.2d 314, 317-18 (5th Cir. 1987). The court relied on the fact that DOL "requested comments regarding 'what should be the appropriate scope of the [Medical Removal Protection benefits] provision,'" concluding that this, along with more general information, "more than adequately sufficed to apprise fairly an interested party that

there was an issue regarding the breadth of MRP benefits." *Id.* at 318. The court therefore concluded that DOL needed to do no more to "apprise fairly interested parties[,] such as these sophisticated industry members who had challenged the ... standard along every step of the road." *Id.* Here, DOL provided notice that was more than adequate under this standard.

In *United Steelworkers*, the Circuit also found support for adequate notice in the fact that "[a]t least one party ... saw fit to comment on precisely this issue" and "other parties provided extensive comments" on related general concerns, demonstrating that "it was readily apparent to interested parties that the scope of MRP benefits was in dispute." 828 F.2d at 318. The same is true here. Plaintiff IALC's comment, among others, acknowledged that DOL "has inquired in its preamble about whether it has struck the right balance" and offered responses. AR42541 (Cmt. 774, IALC) (concluding "we believe that the conditions of the [BIC] Exemption ... would be problematic for fixed annuities").[94] As noted above, *supra* Stmt. of Facts § II(D), numerous commenters, including a number of Plaintiffs or their members, anticipated the possibility of a different outcome than in the proposal. DOL's final determination that variable annuities and FIAs should be grouped together under only the BIC Exemption is plainly within the logical outgrowth standard. *See Chemical Mfrs. Ass'n*, 870 F.2d at 221 (upholding rule that "was a 'logical outgrowth' ... of petitioners' own comments in particular"); *Brazos Elect. Power Coop., Inc. v. Sw. Power Admin.,* 819 F.2d 537, 543 (5th Cir. 1987) ("That [plaintiff] might have been surprised or disappointed by a particular allocation provides no basis for claiming a statutorily deficient notice of rulemaking.").

Plaintiffs' primary objection is that DOL's shift "from a 'treatment as securities' rationale to a 'complexity' rationale" deprived them of an opportunity to meaningfully comment. IALC

[94] *See also, e.g.*, AR41624 (Cmt. 718, Allianz Life Ins. Co.) ("The Proposal specifically requests comment on which exemption, the BIC Exemption, or a revised PTE 84-24, should apply to different types of annuity products."); AR42376 n.15 (Cmt. 762, NAFA) (noting "that the Department invites public input regarding whether the conditions of the proposed [BIC] Exemption ... would be inapplicable to nonsecurity annuities").

Br. 32. But DOL's action is entirely dissimilar to the "surprise switcheroo[s]" Plaintiffs cite. *Id.* 32-33.[95] By comparison, Plaintiffs dispute only the rationale for the line DOL ultimately drew for "subjects and issues" of which Plaintiffs had ample notice. *Chemical Mfrs. Ass'n*, 870 F.2d at 203. Indeed, abandoning the securities distinction was consistent with the comment of at least one Plaintiff. *See, e.g.,* AR38217-18 (Cmt. 506 App'x 6, SIFMA) (urging DOL to abandon distinction based on securities to avoid uncertainty regarding which exemption would apply); *see also* AR42376 (Cmt. 762, NAFA) (suggesting that DOL's proposed distinction was ambiguous and seeking clarification).

Plaintiffs also argue that their discovery in meetings near the end of the comment period that DOL was strongly leaning toward grouping FIAs with variable annuities in the BIC Exemption proves lack of notice. IALC Br. 33-34. There is nothing improper about such meetings. *Tex. Office of Public Utility Counsel v. FCC*, 265 F.3d 313, 327 (5th Cir. 2001). And here, the meetings demonstrate DOL's diligence in discussing its tentative conclusion (in light of all the comments received) with market participants to receive additional feedback before the comment period closed. While Plaintiffs profess surprise, the proposed exemption was "simply a proposal," and the changes to it here were "reasonably foreseeable." *Long Island Care at Home, Ltd. v. Coke*, 551 U.S. 158, 174-75 (2007).[96]

Finally, Plaintiffs argue that they lacked notice that PTE 84-24 would not be available for

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[95] *Envtl. Integrity Project v. EPA*, 425 F.3d 992, 996-97 (D.C. Cir. 2005) (rejecting agency's "decision to repudiate its proposed interpretation and adopt its inverse"); *Int'l Union, United Mine Workers of Am. v. Mine Safety & Health Admin.*, 407 F.3d 1250, 1259-60 (D.C. Cir. 2005) (rejecting switch from proposed minimum air velocity standard to maximum standard); *Nat'l Mining Ass'n v. Mine Safety & Health Admin.*, 116 F.3d 520, 531 (D.C. Cir. 1997) (rejecting change to *when* pre-shift examinations must occur, where proposal had only discussed "*how* pre-shift examinations would be conducted"); *Kooritzky v. Reich*, 17 F.3d 1509, 1513 (D.C. Cir. 1994) (rejecting rule abolishing substitution because the proposal "contains nothing, not the merest hint, to suggest that the Department might tighten its existing practice of allowing substitution").

[96] *See also United Steelworkers*, 828 F.2d at 317 ("[T]he rule is not required to remain frozen in its original vestigial form."); *Kooritzky*, 17 F.3d at 1513 (agencies are "free to adjust or abandon their proposals in light of public comments or internal agency reconsideration without having to start another round of rulemaking" so long as they have "alerted interested parties to the possibility of ... a rule different than the one proposed").

variable annuity sales to employee benefit plans, ACLI Br. 33, because the proposed revision to PTE 84-24 excluded variable annuity sales to IRAs but not such sales to employee benefit plans. *See* AR793. This argument fails on the same grounds as the first notice argument because the DOL proposal explained its tentative reason for singling out IRAs,[97] and then stated "[t]he Department requests comment on this approach." *See* AR790 (inquiring "whether the proposal to revoke relief for securities transactions involving IRAs ... strikes the appropriate balance and is protective of the interests of the IRAs"). Accordingly, the public had ample opportunity to comment on how plan and IRA sales should be treated under PTE 84-24 and the BIC Exemption—and did.[98] Regardless, Plaintiffs give little attention to this issue, presumably because even if the notice had been inadequate, it would amount to at most harmless error.[99] ACLI states that its supplemental comment would have addressed distribution channel issues for FIAs, *see* ACLI Br. 36, but this is an issue of which DOL was already aware, *see* AR790, which commenters had raised in the context of individual annuities, *see* AR42541 (Cmt. 774, IALC); AR47077-78 (Cmt. 3124, IALC), and which DOL addressed by revising the BIC Exemption.[100] *See supra* Arg. § V(C). Under such circumstances, any notice defect—if there were any—would be harmless. *See City of Arlington*, 668 F.3d at 243-45 (finding harmless error where "comments

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[97] *See* AR789 ("IRA owners generally do not benefit from the protections afforded by the fiduciary duties owed by plan sponsors to their employee benefit plans" making it "critical that their interests are protected by appropriate conditions" and the BIC Exemption "was designed for IRA owners and other investors that rely on fiduciary investment advisers in the retail market").

[98] *See* AR42553-54 (Cmt. 767, Guardian Life Ins. Co.) (noting that annuities that are not securities "are typically fixed annuities and some group variable annuities that are exempt from the securities laws"); AR39745-46 (Cmt. 621, Am. Council of Life Ins.) (stating that revenues to the insurer for group annuity recommendations would not fall within the definition of "insurance commission" in the proposed amendment to PTE 84-24).

[99] The APA specifically provides for judicial consideration of harmless error. *See* 5 U.S.C. § 706 ("[D]ue account shall be taken of the rule of prejudicial error."); *Shinseki v. Sanders*, 556 U.S. 396, 406 (2009) (describing § 706 as an "administrative law ... harmless error rule"). It is plaintiff's burden to show prejudice from the error. *See City of Arlington, Tex. v. FCC*, 668 F.3d 229, 243 (5th Cir. 2012).

[100] Moreover, FIAs are seldom sold as group annuities to plans, *see* AR433, Fig. 3-9, so it is not clear why distribution channel issues unique to FIAs, but not variable annuities, would be relevant.

raised the very issues now raised before this court, and the [agency] addressed those issues in its [decision]" because "when a party's claims were considered, even if notice was inadequate, the challenging party may not have been prejudiced").

VI. PLAINTIFFS' NON-APA CLAIMS FAIL

A. The Contract Requirements in the BIC Exemption and Principal Transactions Exemption Do Not Violate the Federal Arbitration Act

DOL allows the contracts under the BIC Exemption and the Principal Transactions Exemption to provide for binding arbitration of individual claims. *See* AR98-99; AR151. But DOL requires the contract between the financial institution and the investor to preserve the investor's right to bring or participate in a class action. *See* AR134, BIC Exemption § II(f)(2); AR151. Plaintiffs challenge this condition, alleging that it violates the Federal Arbitration Act ("FAA"). *See* Chamber Br. 31. Plaintiffs' claim should be denied because these exemptions are consistent with the statutory text and do not interfere with the FAA's principal purpose—to ensure the enforcement of written arbitration agreements. Nor does the FAA restrict DOL's authority to impose conditions on any exemptions it grants from the prohibited transaction restrictions.

Section 2 of the FAA provides that "[a] written provision in any ... contract … to settle by arbitration a controversy thereafter arising out of such contract … shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. The FAA was meant to reverse "widespread judicial hostility to arbitration agreements," putting them on an equal footing with other contracts. *See AT&T Mobility LLC* v. *Concepcion*, 563 U.S. 333, 342 (2011) ("The principal purpose of the FAA is to ensure that private arbitration agreements are enforced according to their terms.").

Here, the condition at issue does not interfere with the FAA's "principal purpose." *Id.* The preservation condition does not purport to render any "written provision" providing for

arbitration invalid, revocable, or unenforceable. Nor does it prohibit class action waivers. Both institutions and advisers remain free to invoke and enforce arbitration provisions, including those that waive or qualify the right to bring a class action in court. Instead, such a contract simply does not meet the conditions for relief from the prohibited transaction restrictions in ERISA and the Code. As a result, the financial institution and adviser would remain fully obligated under Title I of ERISA and the Code to refrain from engaging in prohibited transactions.

As explained above, *see supra* Stmt. of Facts § I(B), DOL has broad discretion to craft exemptions so long as they are administratively feasible, in the interests of retirement investors, and protective of their rights. Here, DOL concluded that the enforcement rights and protections associated with class action litigation are important to ensure adherence to the impartial conduct standards and other anti-conflict provisions of the exemptions. AR77. If a financial institution enters into a contract requiring binding arbitration of class claims, the rulemaking does not invalidate the provision, but rather requires that the financial institution fully comply with statutory provisions prohibiting conflicted fiduciary transactions in its dealings with investors. The FAA does not limit DOL's express discretionary authority over exemptions, nor entitle parties that enter into arbitration agreements to a pass from the prohibited transaction rules.

In response, Plaintiffs contend they cannot service "certain accounts … using a fee-based compensation model," and thus are being "coerc[ed]" to rely on an exemption with the contract restriction to provide investment advice to retirement investors. Chamber Br. 26, 33. But Plaintiffs' unsupported assertions are not evidence sufficient to withstand summary judgment. *Walker v. FFVA Mut. Ins. Co.*, 603 F. App'x 324, 325 (5th Cir. 2015) (summary judgment "may not be thwarted by conclus[ory] allegations, unsupported assertions, or presentation of only a scintilla of evidence"). And DOL pointed to many ways that the industry can innovate to come into compliance with the rulemaking and avoid prohibited transactions. *See* AR634-40. In regard to fees, in particular, DOL noted that "there is ample room for innovation and market

adaptation on the way advisers are compensated." AR638. "As consumers gain awareness that advice was never 'free,' demand is likely to grow not only for asset-based fee arrangements, but also for hourly or flat fee arrangements." *Id.* "Advisory firms may compensate advisers less by commission and more by salary or via rewards tied to customer acquisition or satisfaction." *Id.* In light of these options, it is simply not the case that Plaintiffs' members have no choice but to engage in conflicted transactions and rely on the BIC Exemption.[101]

As the class action preservation condition does not interfere with contract enforcement, it does not violate the FAA, and Defendants are entitled to summary judgment on this claim.

B. DOL's Rulemaking Is Consistent with the First Amendment

For a variety of reasons, Plaintiffs' First Amendment claim is baseless, even aside from the fact that they did not so much as intimate during the rulemaking process their current claim that the rulemaking violates their free speech rights. *See BCCA Appeal Grp. v. EPA*, 355 F.3d 817, 828-29 (5th Cir. 2003) ("Generally, in considering a petition for review from a final agency order, this court will not consider questions of law which were neither presented to nor passed on by the agency."). They also wholly fail to show that there are "no set of circumstances" under which the rulemaking would be valid under the First Amendment, as they must when bringing a facial challenge. *United States v. Richards*, 755 F.3d 269, 273 (5th Cir. 2014) ("To succeed in a typical facial attack [a plaintiff must] establish that no set of circumstances exists under which [the statute] would be valid, or that the statute lacks any plainly legitimate sweep.").

[101] In addition, the cases Plaintiffs cite in support of their coercion argument are completely dissimilar. *See* Chamber Br. 32-33. Both *Nat'l Fed'n of Indep. Bus. v. Sebelius*, 132 S. Ct. 2566 (2012) and *South Dakota v. Dole*, 483 U.S. 203 (1987), involved Spending Clause challenges and addressed whether Congress improperly used federal funding to compel states to enact or administer a federal program in contravention of principles of federalism. They are of no use here, where DOL has express authority to directly regulate the private transactions at issue. To the extent the cases are even comparable here, the burden on Plaintiffs' members to alter their compensation structures or comply with the conditions of the BIC Exemption pale in comparison to the inducements found to be coercive in *Nat'l Fed'n of Indep. Bus*. 132 S. Ct. 2607 (allowing Secretary to withhold "*all* further [Medicaid] payments ... to the State if she determines that the State is out of compliance with any Medicaid requirement).

Even if Plaintiffs' First Amendment claim could survive these threshold issues, Plaintiffs' claim nonetheless fails. For starters, Plaintiffs appear to go out of their way to obfuscate precisely which aspect of the rulemaking they challenge on First Amendment grounds. *See generally* ACLI Br. 10-23 (referring generally to "the Rule" and elsewhere the Rule's "terms and conditions"). Moreover, their challenge is based on their mischaracterization of the rulemaking as a content-based restriction on commercial speech, even though the rulemaking is no such thing. The Rule refines the fiduciary definition for purposes of ERISA, such that those who fall within the definition must conduct themselves in accordance with fiduciary standards that have never been understood to run afoul of the First Amendment. The exemptions accommodate these fiduciaries by allowing them to engage in transactions that would otherwise be prohibited by law. None of this constitutes a regulation of speech prohibited by the First Amendment.

Furthermore, because the rulemaking is intended to combat misleading advice in the context of inherently conflicted transactions in which financial services professionals engage, any incidental effect the rulemaking may have on speech is subject, at most, to rational basis review. Viewed under that standard—or even if the more exacting standard of intermediate scrutiny were to apply—Plaintiffs' First Amendment claim cannot succeed. Given the Government's undisputed substantial interest in protecting retirement investors from being misled and harmed by conflicted investment advice, and the DOL's use of long-standing and commonsense means to combat such conflicts, the rulemaking easily meets that standard.

1. The Rule regulates commercial conduct within a fiduciary relationship, and any incidental effect on speech does not violate the First Amendment

"The Supreme Court has long held that 'the First Amendment does not prevent restrictions directed at commerce or conduct from imposing incidental burdens on speech.'" *Hines v. Alldredge*, 783 F.3d 197, 201 (5th Cir.) (quoting *Sorrell v. IMS Health Inc.*, 564 U.S. 552, 567 (2011)). "Pursuant to this principle, there is a robust line of doctrine concluding that

state regulation of the practice of a profession, even though that regulation may have an incidental impact on speech, does not violate the Constitution." *Id.* (citing *Lowe v. SEC*, 472 U.S. 181, 231-32 (1985) (White, J., concurring)).

To determine whether the regulation of professional conduct has only a permissible, incidental effect on speech, courts look to whether "the speaker is providing personalized advice in a private setting to a paying client or instead engages in public discussion and commentary." *Moore-King v. Cty. of Chesterfield, Va.*, 708 F.3d 560, 569 (4th Cir. 2013); *accord Serafine v. Branaman*, 810 F.3d 354, 359 (5th Cir. 2016) (citing *Lowe v. SEC*, 472 U.S. at 232 (White, J., concurring) (distinguishing regulation of professional conduct that consists of personalized advice to a paying client in a private setting and restrictions on protected speech that involves public discussion and commentary)). "Professional speech analysis applies in the former context—where a speaker takes the affairs of a client personally in hand and purports to exercise judgment on behalf of the client in the light of the client's individual needs and circumstances,'"—but not in the latter, which involves public discourse. *Moore-King*, 708 F.3d at 569; *accord Serafine*, 810 F.3d at 359. Regulation of such conduct does not abridge free speech, so long as "any inhibition … is merely the incidental effect of observing an otherwise legitimate regulation." *Underhill Assocs. v. Bradshaw,* 674 F.2d 293, 296 (4th Cir. 1982).

The rulemaking at issue fits comfortably within these parameters. The Rule applies to personalized investment advice to a paying client,[102] and, as ACLI's own brief makes clear, to advisers like Plaintiffs' members, who "take[] the affairs of a client personally in hand and

[102] *See* 29 C.F.R. § 2510.3-21(a)(1)(2)(i)-(iii) (limiting a "recommendation" to one made by an actor who: "(i) [r]epresents or acknowledges that it is acting as a fiduciary within the meaning of the Act or the Code; (ii) [r]enders the advice pursuant to a written or verbal agreement, arrangement, or understanding that the advice is based on the *particular investment needs of the advice recipient*; or (iii) [d]irects the advice to a *specific advice recipient or recipients* regarding the advisability of a *particular investment or management decision* with respect to securities or other investment property of the plan or IRA."); § 2510.3-21(a)(1) (limiting fiduciary status to a person who provides advice "for a fee or other compensation, direct or indirect," mirroring the statutory language, *see* 29 U.S.C. § 1002(21)(A)(ii)).

purport[] to exercise judgment on behalf of the client in the light of the client's individual needs and circumstances." *Accountant's Soc'y of Va. v. Bowman*, 860 F.2d at 602, 604 (4th Cir. 1988). *See* ACLI Br. 4-5 (explaining that insurance agents "help consumers assess whether an annuity is a good choice and, if so, which type of annuity and optional features suits consumers' financial circumstances").[103] Furthermore, the Rule explicitly states that the definition of fiduciary investment advice does not include general communications to the public that could be viewed as commercial speech.[104] *Commodity Trend Serv., Inc. v. Commodity Futures Trading Comm'n*, 149 F.3d 679, 684 (7th Cir. 1998) (explaining that "[c]ommercial advertising constitutes paradigmatic commercial speech under the Supreme Court's standard because its fundamental purpose is to propose an economic transaction"). The Rule thus operates as a regulation of professional conduct, and the exemptions, which aim to mitigate conflicts in investment advice, have at most an incidental effect on speech. As such, the rulemaking is subject to a very low level of scrutiny, if it falls within the ambit of the First Amendment at all. *Lowe*, 472 U.S. at 228 (White, J., concurring) (regulations of professional conduct "are constitutional if they have a rational connection with the applicant's fitness or capacity to practice the profession"); *see also*

[103] The fact that the professional speech doctrine has been applied most often in the context of state and federal schemes that involve the licensing of professionals to enter into a profession, *see, e.g., Serafine*, 810 F.3d 354; *Conn. Bar Ass'n v. United States*, 620 F.3d 81, 96–97 (2d Cir. 2010), does not undermine its applicability here. The rulemaking, which involves determining when a professional renders investment advice so as to qualify as a fiduciary under Title I of ERISA and the Code, is more analogous to cases analyzing the regulation of professional conduct than to those involving the regulation of commercial speech, the paradigmatic example of which is commercial advertising, to which the rulemaking does not apply. The Fourth Circuit recently recognized, in the context of rejecting a First Amendment challenge to county regulations of fortune tellers, that the "proper analytical framework" in such cases is that of professional speech, rather than commercial speech. *See Moore-King*, 708 F.3d at 567-68 (recognizing that "[t]he parameters of commercial speech, typically defined as that which 'does no more than propose a commercial transaction,' … are difficult to identify outside the realm of advertising"). The Government thus advocates that approach here. In any event, whether analyzed as professional speech or as a regulation of misleading commercial speech, the rulemaking should be afforded a deferential standard of review.

[104] *See id.* § 2510.3-21(b)(2)(iii) (excluding from definition of "recommendation" any "general communications that a reasonable person would not view as an investment recommendation, including general circulation newsletters, commentary in publicly broadcast talk shows, remarks and presentations in widely attended speeches and conferences, research or news reports prepared for general distribution, general marketing materials, general market data, including data on market performance, market indices, or trading volumes, price quotes, performance reports, or prospectuses").

Accountant's Soc'y. of Va., 860 F.2d at 604 (applying a standard akin to rational basis); *Locke v. Shore*, 634 F.3d 1185, 1191 (11th Cir. 2011) (holding that regulation of professionals' personalized speech with clients governs "occupational conduct, … not a substantial amount of protected speech, [and] … does not implicate constitutionally protected activity under the First Amendment"); *Moore-King*, 708 F.3d at 570 (declining to "delineate the precise boundaries of permissible occupational regulation" but upholding professional regulation where "legislature may reasonably determine that additional regulatory requirements are necessary"); *but see, e.g.*, *King v. Governor of N.J.*, 767 F.3d 216, 234 (3d Cir. 2014), *cert. denied sub nom. King v. Christie*, 135 S. Ct. 2048, 191 L. Ed. 2d 955 (2015) ("We believe that commercial and professional speech share important qualities and, thus, that intermediate scrutiny is the appropriate standard of review for prohibitions aimed at either category.").[105]

Plaintiffs attempt to recast the rulemaking as a prohibition on protected speech by repeatedly arguing that under the Rule, "[s]alespersons now may speak as a fiduciary, or not at all." ACLI Br. 8; *see id.* 11, 22. But this supposed Hobson's choice does not even present a First Amendment question; that the rulemaking requires a fiduciary to act like a fiduciary is not a restriction on speech.[106] Were it otherwise, myriad long-standing state and federal laws pertaining to the conduct of numerous fiduciary relationships, such as those applying to doctors, lawyers, and psychologists, would be subject to strict scrutiny insofar as they involve the use of speech. Such an approach has been explicitly rejected. *See Ohralik v. Ohio State Bar Ass'n*, 436 U.S. 447, 457 (1978) (regulation of "business transaction in which speech is an essential but

[105] Even if the Court were to determine that an intermediate level of scrutiny were to apply to Plaintiffs' First Amendment challenge to the rulemaking, as explained below, the rulemaking would survive that intermediate standard of review.

[106] And insofar as Plaintiffs challenge the Rule's definition of who constitutes a fiduciary by virtue of rendering investment advice, that contention is coextensive with their APA challenge to the definition and should be rejected for the same reasons. *See supra* Arg. § I.

subordinate component" held subject to "lower[] … level of … judicial scrutiny"); *Nat'l Ass'n for the Advancement of Multijurisdiction Practice v. Lynch*, No. 15-1982, 2016 WL 3361558, at *2 (4th Cir. June 17, 2016) (upholding regulation of lawyers "providing personalized advice in a private setting to a paying client" as "speech … incidental to the conduct of the profession," in which case "the First Amendment does not come into play"). That such a result would be absurd is underscored by the fact that Plaintiffs do not challenge the statutory responsibilities and restrictions applied to fiduciaries under Title I of ERISA and the Code. Nevertheless, the consequence of Plaintiffs' position would be to call into question those provisions on First Amendment grounds.

Plaintiffs also incorrectly suggest that the Rule prohibits their members from talking about annuities outside of a fiduciary relationship. *See* ACLI Br. 11 (asserting that "[u]nder the Rule … a broker-dealer is prohibited from saying 'you should consider buying a variable annuity from my company,' unless that broker-dealer assumes fiduciary status"). That is not the case. Instead, consistent with the professional speech doctrine, which recognizes that "[o]utside the fiduciary relationship between client and [fiduciary], speech is granted ordinary First Amendment protection," *Serafine*, 810 F.3d at 360, the rulemaking regulates only commercial conduct that occurs within a fiduciary relationship. Outside of those parameters, Plaintiffs' members can continue to have conversations about retirement products and market their services without becoming fiduciaries under the Rule. *See* AR31 (explaining that "one would not become a fiduciary merely by providing information on standard financial and investment concepts, such as diversification, risk and return, tax deferred investments; historic differences in rates of return between different asset classes (*e.g.,* equities, bonds, cash); effects of inflation; estimating future retirement needs and investment time horizons; assessing risk tolerance; or general strategies for managing assets in retirement"). It is only once "the adviser … cross[es] the line to recommending a specific investment or investment strategy," *id.*, and advisers are compensated

for their services, that their conduct comes within the rulemaking, which is the "proper sphere of economic and professional regulation." *Ohralik*, 436 U.S. at 459; *id.* (upholding rule where it did "not prohibit a lawyer from giving unsolicited legal advice; it proscribe[d] the acceptance of employment resulting from such advice").

2. The rulemaking regulates transactions with the potential to mislead

To the extent the rulemaking regulates commercial speech (as opposed to professional conduct) at all, it is subject at most to a very low level of scrutiny, as it regulates transactions that have inherent potential to mislead. "Commercial speech is … afforded lesser protection under the Constitution than other forms of speech." *Ford Motor Co. v. Tex. Dep't of Transp.*, 264 F.3d 493, 505 (5th Cir. 2001) (citing *Florida Bar v. Went For It, Inc.,* 515 U.S. 618, 623 (1995) ("Commercial speech enjoys a limited measure of protection, commensurate with its subordinate position in the scale of First Amendment values, and is subject to modes of regulation that might be impermissible in the realm of noncommercial expression."))). It typically receives only an intermediate level of scrutiny. *Cent. Hudson Gas & Elec. Corp. v. Pub. Serv. Comm'n of N.Y.*, 447 U.S. 557, 573 (1980). However, as a threshold matter, "[f]or commercial speech to come within [the protection of the First Amendment], it at least must … not be misleading." *Id.*; *accord Accountant's Soc'y. of Va.*, 860 F.2d at 605 ("Notwithstanding the initial classification of a communication as commercial speech, it falls outside the protection of the first amendment, if the communication is false, deceptive or misleading.").

Plaintiffs characterize the rulemaking as applying to "truthful commercial speech," ACLI Br. 10, and claim it violates the First Amendment by "prohibit[ing] 'recommendations' about retirement products … unless [the Rule's] onerous terms and conditions are satisfied," *id.* at 11. However, the terms and conditions of the exemptions apply only when Plaintiffs' members are engaged in transactions Congress deemed so fraught with conflicts of interest that it prohibited them altogether. *See supra* Stmt. of Facts § I(A)-(B). To the extent the exemptions regulate

speech within those transactions at all, the only advice they limit would consist of suggestions that retirement investors take actions with respect to their investment property that are *not* in their best interest and misleading statements about investment transactions, compensation, and conflicts of interest. *See* AR63.[107] Such statements, with their potential to mislead retirement investors, do not even fall within the ambit of First Amendment protection. *See Cent. Hudson*, 447 U.S. at 563-64 (government may prohibit communication "more likely to deceive the public than to inform it").

Rather than a regulation of transactions with the inherent potential to mislead, Plaintiffs contend that the rulemaking is a content-based restriction on speech subject to strict scrutiny. *See* ACLI Br. 10-14. That is incorrect. Plaintiffs' position is based on its argument that the Rule impermissibly distinguishes between "speakers (human v. robo-advisers), listeners (sophisticated v. unsophisticated), and subject matters (favored v. disfavored retirement products)." *Id.* 11 n.4; *id.* 11-13. In each case, however, the rulemaking treats speakers, listeners, and subject matters differently, not because it "disfavor[s] … particular messages about retirement products," as Plaintiffs suggest, *id.* 13, but because DOL determined that the potential for conflicts of interest and for consumers to be misled differed in degree such that differential treatment was justified.[108] "[P]rotecting consumers from 'commercial harms'" is a "neutral justification" for any "content-based restrictions." *Sorrell*, 564 U.S. at 579 (explicitly contemplating that harm of

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[107] The BIC Exemption also requires certain disclosures, including disclosure of fiduciary status, fees, compensation, and material conflicts of interest. AR63. Plaintiffs do not challenge the disclosure requirements on First Amendment grounds. *See generally* ACLI Br. 10-23.

[108] *See* AR114 (permitting robo-advice to proceed under exemptions other than the BIC Exemption because "the marketplace for robo-advice is still evolving in ways that both appear to avoid conflicts of interest that would violate the prohibited transaction rules and minimize cost"); AR118 (applying fiduciary status to advisers to individual investors and small plans but not to advisers to independent fiduciaries with financial expertise because in most cases, the former "are not financial experts, are unaware of the magnitude and impact of conflicts of interest, and are unable effectively to assess the quality of the advice they receive"); AR36; *supra* Arg. V(A)(1) (explaining that differences in complexity, risk, and conflicts of interest between declared rate annuities and FIAs and variable annuities justified their differential treatment under the rulemaking).

misleading consumers is one such "neutral justification" for content-based restrictions).

Moreover, as Plaintiffs concede, "[w]hen the basis for the content discrimination consists entirely of the very reason the entire class of speech at issue is proscribable," strict scrutiny does not apply because "no significant danger of idea or viewpoint discrimination exists." *R.A.V. v. City of St. Paul, Minn.*, 505 U.S. 377, 388 (1992). "Such a reason, having been adjudged neutral enough to support exclusion of the entire class of speech from First Amendment protection, is also neutral enough to form the basis of distinction within the class." *Id.* Here, where bad advice and misleading statements are wholly proscribable because they are misleading, the rulemaking does not run afoul of the First Amendment where it makes content-based distinctions for the very same reason. Accordingly, where the rulemaking aims at protecting consumers from misleading practices, it is subject to "less than strict review," *44 Liquormart, Inc. v. Rhode Island*, 517 U.S. 484, 501 (1996), if it falls within the ambit of the First Amendment at all.

That strict scrutiny should not apply here is further evidenced by the fact that Plaintiffs' position has no limiting principle. Plaintiffs' argue that "[t]ying the level of regulation to the product discussed is obviously content-based," and thereby subject to strict scrutiny. ACLI Br. 13. If Plaintiffs' position were adopted, it would subject to strict scrutiny a host of statutory schemes and regulatory decision-making that have been upheld as permissible regulation. *See, e.g., Conn. Bar Ass'n*, 620 F.3d at 96 (upholding under rational basis review provisions of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 that prohibited debt relief agencies from advising their clients to incur more debt in contemplation of bankruptcy and required such agencies to provide assisted persons with certain notices, to execute a written contract with such persons, and to include certain language in their advertisements). Indeed, Plaintiffs contend that, like "recommendations," "investment advice" is a subject matter distinction that requires strict scrutiny. ACLI Br. at 12. But if that were the case, ERISA's fiduciary definition itself (which Plaintiffs do not challenge), along with securities laws that

regulate investment advisers, would be subject to strict scrutiny. Such a position would be untenable and has been explicitly rejected by the courts. *See Ohralik*, 436 U.S. at 456 (listing among the "[n]umerous examples … of communications that are regulated without offending the First Amendment" "the exchange of information about securities" and "corporate proxy statements"); *SEC v. Wall St. Pub. Inst., Inc.*, 851 F.2d 365, 373 (D.C. Cir. 1988) ("If speech employed directly or indirectly to sell securities were totally protected, any regulation of the securities market would be infeasible—and that result has long since been rejected." (citing *Paris Adult Theatre I v. Slaton,* 413 U.S. 49, 61-62 (1973), and cases cited)). Applying strict scrutiny to regulations of this sort would cripple the Government's ability to address consumer needs and put into the hands of the courts, rather than the elected branches, the ability to determine the best means to do so. The First Amendment does not compel such a radical result. *See Ohralik*, 436 U.S. at 456 ("[T]he State does not lose its power to regulate commercial activity deemed harmful to the public whenever speech is a component of that activity.").

3. The rulemaking directly advances the Government's substantial interest in protecting retirement investors from conflicted investment advice

For the aforementioned reasons, whether analyzed as a regulation of professional conduct or of transactions with inherent potential to mislead, Plaintiffs' First Amendment claim should be subject to no more than rational basis review. Nevertheless, even if the Court were to determine that the rulemaking regulates commercial speech that is not inherently misleading, the rulemaking would survive the higher level of review that applies to such regulations.

Under the Supreme Court's test for commercial speech, if the communication is neither misleading nor related to unlawful activity, then the government must show: a "substantial" government interest; that the regulation "directly advances" the asserted interest; and that the regulation is "not more extensive than is necessary to serve that interest." *Gibson v. Tex. Dep't of Ins.—Div. of Workers' Comp.*, 700 F.3d 227, 234 (5th Cir. 2012) (citing *Cent. Hudson*, 447

U.S. at 563). "The chosen regulation does not need to be the least restrictive method for achieving the government's goal." *Id.* at 237.

That the Government has a substantial interest in protecting retirement investors from conflicted investment advice that threatens their retirement security is obvious and undisputed. *See United States v. Wenger*, 427 F.3d 840, 848–51 (10th Cir. 2005) ("It is undisputed that the government has an interest in protecting consumers from being misled." (quoting *Illinois, ex rel. Madigan v. Telemarketing Assocs.,* 538 U.S. 600, 612 (2003)); ACLI Br. 15 ("Protecting American retirement consumers is undoubtedly a substantial interest.").[109]

In addition, the rulemaking directly advances that interest without being more extensive than necessary. DOL relied on considerable evidence that conflicts of interest and confusion in the market for retirement investment advice are widespread, causing serious harm to retirement investors. AR642 (summary of scope of conflicts); *see also* AR443-51 (discussing conflicts among brokers and insurance agents in particular). It also found that loopholes in the 1975 regulation's fiduciary definition allowed those who render retirement investment advice to disclaim fiduciary status, even as they suggest to consumers that they are rendering expert financial assistance upon which investors can and should rely. AR35.

To ameliorate these problems, DOL revised the 1975 regulation's definition of fiduciary investment advice to better align with ERISA's statutory text, history, and purposes, *see supra* Arg. § I(A), and to ensure that fiduciary responsibilities and restrictions apply to those Congress intended to be fiduciaries in order to protect retirement investors from conflicted investment advice. In conjunction with the revised definition, DOL crafted administrative exemptions that continue to protect retirement investors even in the case of conflicted transactions by, *inter alia*,

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[109] The Supreme Court has also recognized that states have a compelling interest in the regulation of the practice of professions. *Goldfarb v. Va. State Bar*, 421 U.S. 773, 792 (1975).

requiring investment advice fiduciaries to adhere to impartial conduct standards, to take certain steps to minimize the impact of conflicts of interest, and, in the case of the BIC and Principal Transactions Exemptions, to enter into enforceable agreements to ensure adherence to the exemptions' conditions. *See* AR63 (bulleted summary of the conditions of BIC Exemption). As a result of these regulatory changes, DOL estimates investors will see cost savings and efficiency benefits from the mitigation or elimination of adviser conflicts totaling more than $30 billion over 10 years in one segment of the market alone. AR412-413.

While taking these steps to directly advance the Government's interest in protecting retirement investors from conflicts of interest, DOL also went to great lengths to ensure that the rulemaking was no more extensive than necessary to do so. For example, "[r]ather than create a set of highly prescriptive transaction-specific exemptions," DOL crafted the BIC Exemption, to "flexibly accommodate[] a wide range of compensation practices," AR58, and allow financial institutions and advisers "the flexibility and discretion necessary to determine how best to satisfy the exemption's standards in light of the unique attributes of their business." AR59.

That the rulemaking's flexible, yet protective, approach is no more extensive than necessary is underscored by DOL's consideration of multiple alternatives to the Rule and exemptions during the rulemaking process, as well as the modifications DOL made to the Rule and exemptions in response to comments it received throughout the rulemaking process. As reflected in the RIA, DOL considered numerous alternatives to the approach it took in the rulemaking (including some of those proposed by Plaintiffs' members), but ultimately determined that none of the alternatives would protect retirement investors as efficiently and effectively as the rulemaking. *See* AR578-612. DOL specifically considered the alternative of basing exemptive relief on disclosure alone, *see* AR584-87, but, after thoroughly reviewing the academic research in this area, concluded that "disclosure of adviser conflicts can backfire," *see* AR585, and that relying solely on disclosures "would be ineffective,… would yield little to no

investor gains[,] [and] would fail to justify its compliance cost." *See id.* 587.

DOL also significantly modified the Rule and exemptions in response to comments it received throughout the rulemaking process to make them less costly for the industry while continuing to serve the needs of retirement investors. *See supra* Stmt. of Facts § II(D). DOL determined that the changes would further minimize any potential negative impact on small investors' access to affordable advice. AR65. In this way, the rulemaking serves the Government's substantial interest in mitigating conflicts of interest to the benefit of investors, while being no more extensive than necessary to maintain consumer choice. *See* AR570.

Plaintiffs contend that the rulemaking does not advance the Government's substantial interest in protecting Americans' retirement savings "because it proceeds from an unconstitutional premise" that the Government should shield consumers from "truthful, non-misleading commercial information about retirement products." ACLI Br. 15. But it is Plaintiffs who proceed from the faulty premise. The rulemaking does not seek to prevent retirement investors from receiving truthful, non-misleading information but simply requires financial institutions and advisers to give advice that is in the best interest of retirement investors, *see* AR63, a standard that has long governed fiduciary relationships. AR82 ("The Impartial Conduct Standards represent fundamental obligations of fair dealing and fiduciary conduct … deeply rooted in ERISA and the common law of agency and trusts."). And it seeks to shield investors only from recommendations that are *not* in their best interest and other misleading information. These restrictions do not run afoul of the First Amendment. *See Cent. Hudson*, 447 U.S. at 563-64. Otherwise, the rulemaking is aimed at ensuring that retirement investors are fully informed by requiring advisers to "[a]cknowledge fiduciary status with respect to investment advice" and "[f]airly disclose the fees, compensation, and Material Conflicts of Interest, associated with their recommendations." *Id.* Plaintiffs again latch onto DOL's statement in the rulemaking that "some research suggests" that disclosure of conflicts "could be ineffective—or even harmful."

AR118. As explained above, that statement was made in the context of DOL explaining that, based on academic research results, "[d]isclosure *alone* has proven ineffective to mitigate conflicts in advice." *Id.* (emphasis added). Disclosures are thus only part of the rulemaking, but they are a necessary part, as DOL determined that they "provide basic information that is critical to [investors'] understanding of the nature of the relationship and the scope of the conflicts of interest." AR105.

Plaintiffs otherwise argue that the rulemaking does not directly advance the Government's substantial interest in protecting retirement investors from conflicted advice because the rulemaking will "harm, not help" retirement investors by decreasing their access to affordable investment advice. ACLI Br. 18. For the reasons set forth above, *see supra* Stmt. of Facts IV(B), DOL concluded quite the opposite. After completing a nearly six-year notice-and-comment process and conducting an extensive regulatory impact analysis, which includes thorough analysis of the position of small investors without the rulemaking, as well as the effect of the rulemaking on them, *see* AR628-34, DOL concluded that small investors were not being well served by the financial industry and that the rulemaking will enhance the welfare of the small investors by "nudg[ing] the investment advice market's evolution toward greater efficiency," and by "reflecting better informed matches between customers and advisers." AR634. As explained above, Plaintiffs provide no reason to undermine DOL's conclusions, in particular in light of DOL's expertise in this area.[110]

Based on the foregoing, whether Plaintiffs' First Amendment claim is about conduct and not speech at all, or is subject to rational basis review or intermediate scrutiny, DOL is entitled to summary judgment because the rulemaking serves the Government's substantial interest in

[110] Plaintiffs repeat here their contention that the rulemaking will "effectively ban[]" conversations about retirement investment products. As explained above, *see supra* Arg. VI(B)(1), that is not the case.

protecting retirement investors from conflicts of interest while being no more extensive than necessary to do so.

Finally, while DOL maintains that the rulemaking is in no case subject to strict scrutiny, DOL notes that Plaintiffs' arguments that the rulemaking does not meet that standard because it is not narrowly tailored are without merit. First, Plaintiffs contend that the rulemaking is not narrowly tailored because DOL adopted an overly broad definition of an investment advice fiduciary. *See* ACLI Br. 21. This argument is co-extensive with Plaintiffs' first claim and should be rejected for the same reasons. *See supra* Arg. § I.[111] Second, Plaintiffs argue that the rulemaking is not narrowly tailored because it could have relied on the less restrictive alternative of "clear and simple disclosures." ACLI Br. 17. DOL has shown that disclosures alone would not be "at least as effective in achieving" the Government's purpose. *Am. Civil Liberties Union v. Mukasey*, 534 F.3d 181, 198 (3d Cir. 2008).[112] That this is so is underscored by the fact that Congress determined as much when it enacted ERISA to supplant the previous regime, which relied on disclosures and was found to be ineffective at protecting retirement investors. *See supra* Stmt. of Facts § I. Plaintiffs' repetitious arguments thus do nothing to undermine DOL's showing that the rulemaking directly advances the Government's substantial interest in protecting retirement investors from conflicts of interest and is no more extensive than necessary to do so.

[111] Moreover, to the extent Plaintiffs assert that a regulation can never define a term generally while providing exceptions or exemptions, they are flatly wrong. Agencies promulgate definitions with exceptions—and courts uphold those definitions with exceptions—regularly. *See, e.g.*, *Conn. Bar Ass'n*, 620 F.3d at 86 (upholding in context of a First Amendment claim the Bankruptcy Abuse Prevention and Consumer Protection Act's definition of "debt relief agency," which excluded at least five separate categories of persons or entities); *Household Credit Servs., Inc. v. Pfennig*, 541 U.S. 232, 242-45 (2004) (upholding Federal Reserve Board's interpretation "finance charge" that "specifically excludes" eight types of charges).

[112] As discussed at length in the RIA, available academic and empirical evidence strongly suggests that disclosure alone would be ineffective at mitigating conflicts in financial advice. AR584. Indeed, several brokerage firms acknowledged that "investors rarely read these disclosures … [F]or many investors, the fact that they were given disclosures was seen as meaningless." *Id.* Moreover, investment advice is "needed in the first place because people cannot rely solely on disclosures." AR587.

For all of these reasons, there is no merit to Plaintiffs' First Amendment claim, and DOL is entitled to summary judgment on this claim.

VII. THE APPROPRIATE REMEDY, IF ANY, SHOULD BE DETERMINED AFTER THE CONTOURS OF THE COURT'S MERITS RULING ARE CLEAR.

Plaintiffs have attacked the Rule and various exemptions on numerous grounds. DOL has demonstrated that it is entitled to summary judgment on every claim. But, in the unlikely event that the Court concludes that some aspect of the rulemaking falls short as a procedural matter or otherwise, the Court should either remand to DOL without vacatur or provide an opportunity for the parties to briefly address appropriate remedies, including severability. Here, for most grounds on which any adverse ruling could be based, DOL "may well be able to justify its decision[s]" on remand, and "it would be disruptive to vacate a rule that applies to other members of the regulated community" and to DOL's efforts to protect retirement investors from significant ongoing harm due to conflicts of interest. *Central & Sw. Servs., Inc. v. EPA*, 220 F.3d 683, 692 (5th Cir. 2000), *cert. denied*, 532 U.S. 1065 (2001). Moreover, given the many variations of what could be upheld and struck down, it would be difficult to fully address these issues in the abstract. As a general matter, DOL intends that any invalidated provision of the rulemaking be severed, if feasible, to preserve its many other important benefits. *See, e.g.*, AR101 ("[T]he Department intends that invalidated provisions of the rule and exemption may be severed when the remainder of the rule and exemptions can function sensibly without them."); *see also Conservation Law Found. v. Pritzker*, 37 F. Supp. 3d 254, 271 (D.D.C. 2014) (where "offending portions of the Framework and rule are isolated and severable, the Court vacates them only in part"). Application of these general principles to the particular contours of any adverse decision by the Court can best be addressed in light of the Court's actual ruling.

CONCLUSION

For the foregoing reasons, Defendants are entitled to summary judgment on all claims, and the Court should deny Plaintiffs' motions for summary judgment.

Dated: August 19, 2016

Respectfully submitted,

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CERTIFICATE OF SERVICE

On August 19, 2016, I electronically submitted the foregoing document with the clerk of court for the U.S. District Court, Northern District of Texas, using the electronic case filing system of the court. I hereby certify that I have served all parties to the three actions—Case Nos. 3:16-cv-01476-M, 3:16-cv-01530-C, 3:16-cv-1537-N—electronically or by another manner authorized by Federal Rule of Civil Procedure 5(b)(2).

/s/ Galen N. Thorp
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