No. 17-10238

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA; FINANCIAL SERVICES INSTITUTE, INCORPORATED; FINANCIAL SERVICES ROUNDTABLE; GREATER IRVING-LAS COLINAS CHAMBER OF COMMERCE; HUMBLE AREA CHAMBER OF COMMERCE, doing business as Lake Houston Chamber of Commerce; INSURED RETIREMENT INSTITUTE; LUBBOCK CHAMBER OF COMMERCE; SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION; TEXAS ASSOCIATION OF BUSINESS,
Plaintiffs-Appellants,

v.

UNITED STATES DEPARTMENT OF LABOR; R. ALEXANDER ACOSTA, SECRETARY, U.S. DEPARTMENT OF LABOR,
Defendants-Appellees.

AMERICAN COUNCIL OF LIFE INSURERS; NATIONAL ASSOCIATION OF INSURANCE AND FINANCIAL ADVISORS; NATIONAL ASSOCIATION OF INSURANCE AND FINANCIAL ADVISORS-TEXAS; NATIONAL ASSOCIATION OF INSURANCE AND FINANCIAL ADVISORS-AMARILLO; NATIONAL ASSOCIATION OF INSURANCE AND FINANCIAL ADVISORS-DALLAS; NATIONAL ASSOCIATION OF INSURANCE AND FINANCIAL ADVISORS-FORT WORTH; NATIONAL ASSOCIATION OF INSURANCE AND FINANCIAL ADVISORS-GREAT SOUTHWEST; NATIONAL ASSOCIATION OF INSURANCE AND FINANCIAL ADVISORS-WICHITA FALLS,
Plaintiffs-Appellants,

v.

UNITED STATES DEPARTMENT OF LABOR; R. ALEXANDER ACOSTA, SECRETARY, U.S. DEPARTMENT OF LABOR,
Defendants-Appellees.

INDEXED ANNUITY LEADERSHIP COUNCIL; LIFE INSURANCE COMPANY OF THE SOUTHWEST; AMERICAN EQUITY INVESTMENT LIFE INSURANCE COMPANY; MIDLAND NATIONAL LIFE INSURANCE COMPANY; NORTH AMERICAN COMPANY FOR LIFE AND HEALTH INSURANCE,
Plaintiffs-Appellants,

v.

R. ALEXANDER ACOSTA, SECRETARY, U.S. DEPARTMENT OF LABOR; UNITED STATES DEPARTMENT OF LABOR,
Defendants-Appellees.

On Appeal from the United States District Court for the Northern District of Texas, Dallas Division, Nos. 3:16-cv-1476, -1530, -1537

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July 20, 2017

CERTIFICATE OF INTERESTED PERSONS

No. 17-10238

CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA; FINANCIAL SERVICES INSTITUTE, INCORPORATED; FINANCIAL SERVICES ROUNDTABLE; GREATER IRVING-LAS COLINAS CHAMBER OF COMMERCE; HUMBLE AREA CHAMBER OF COMMERCE, doing business as Lake Houston Chamber of Commerce; INSURED RETIREMENT INSTITUTE; LUBBOCK CHAMBER OF COMMERCE; SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION; TEXAS ASSOCIATION OF BUSINESS,
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Plaintiffs-Appellants,

v.

R. ALEXANDER ACOSTA, SECRETARY, U.S. DEPARTMENT OF LABOR; UNITED STATES DEPARTMENT OF LABOR,
Defendants-Appellees.

The undersigned counsel of record certifies the following listed persons and entities as described in the fourth sentence of Local Rule 28.2.1 have an interest in the outcome of this case. These representations are made in order that the judges of this court may evaluate possible disqualification or recusal.

Plaintiff-Appellant the Indexed Annuity Leadership Council has no parent corporation and no publicly held corporation owns 10% or more of its stock.

The parent company of Plaintiff-Appellant Life Insurance Company of the Southwest is National Life Insurance Company. No publicly held corporation owns 10% or more of the stock of Life Insurance Company of the Southwest.

Plaintiff-Appellant American Equity Investment Life Insurance Company is wholly owned by its parent company, American Equity Life Holding Company.

Plaintiff-Appellant Midland National Life Insurance Company ("Midland") is wholly owned by Sammons Financial Group, Inc. ("Sammons Financial"); Sammons Financial is wholly owned by Consolidated Investment Services, Inc. ("Consolidated"); and Consolidated is wholly owned by Sammons Enterprises, Inc. ("Sammons Enterprises"). Midland owns Solberg Reinsurance Company, MNL Reinsurance Company and Midland National Services Corporation, LLC. Midland is also otherwise related by common ownership to Sammons Retirement Solutions, Inc. and Sammons Securities, Inc. (which owns Sammons Financial Network, LLC).

Plaintiff-Appellant North American Company for Life and Health Insurance ("North American") is wholly owned by Sammons Financial Group, Inc. ("Sammons Financial"); Sammons Financial is wholly owned by Consolidated Investment Services, Inc. ("Consolidated"); and Consolidated is wholly owned by Sammons Enterprises, Inc. ("Sammons Enterprises"). North American is also otherwise related by common ownership to Sammons Retirement Solutions, Inc. and Sammons Securities, Inc. (which owns Sammons Financial Network, LLC).

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2. Life Insurance Company of the Southwest
3. American Equity Investment Life Insurance Company
4. Midland National Life Insurance Company
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July 20, 2017

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INTRODUCTION

The Department of Labor (DOL) and its *amici* have failed to refute the Indexed Annuity Leadership Council (IALC) plaintiffs' showing that the fiduciary rule is invalid.

DOL nowhere disputes that, when Congress enacted the Employee Retirement Security Act of 1974 (ERISA), the settled common-law meaning of "fiduciary" required a special relationship of trust and confidence—a relationship that did not arise in one-time insurance sales. IALC Br. 19-22. Nor does DOL dispute that this Court must presume that Congress intended to incorporate this meaning when it used the term "fiduciary" in ERISA. Nevertheless, DOL asks the Court to uphold its conclusion—announced for the first time more than 40 years after ERISA's enactment—that the central attribute of a "fiduciary" relationship is irrelevant to fiduciary status under ERISA.

DOL repeatedly claims that this interpretation is entitled to deference under *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984). But the agency simply ignores *Chevron*'s two-step framework, and tries to elide *Chevron*'s first step, in which this Court must construe the statute based on ordinary tools of interpretation, without regard to the agency's views. DOL also ignores the stringent standard this Court must apply to determine whether the presumption of common-law incorporation has been overcome—a standard that cannot

be met with respect to ERISA. Instead, DOL relies on wholly inapposite authority to claim that this interpretive presumption (used to determine a statute's "plain meaning") can be overridden based on market changes that occur decades after ERISA was passed. Proper application of the ordinary rules of construction, however, forecloses DOL's newly-minted interpretation of a common-law term.

DOL also fails to rebut plaintiffs' showing that its treatment of fixed indexed annuities (FIAs) was arbitrary and capricious because it failed to support its conclusion that FIA sales are inflicting "excessive losses" on consumers despite existing regulation. DOL relies heavily on studies of mutual funds, arguing that it was reasonable to extrapolate their results to FIAs. But DOL does not defend the only basis it gave in the rulemaking for this extrapolation—an article that does not even discuss FIAs. DOL does not show that the dynamics that purportedly led to mutual-fund underperformance—underinvestment in fund management, timing errors, and chasing returns—apply to FIAs, which are not actively managed or traded. And without its mutual-fund studies to fall back on, it has no empirical evidence to support its claim that existing regulation is insufficient.

Nor did DOL provide a rational theoretical basis for finding existing regulation inadequate. DOL barely defends the principal basis it gave in the rule—lack of uniformity. And for good reason: DOL does not dispute that almost all FIAs are sold in compliance with the NAIC model rules so that they may qualify for the Harkin

Amendment's exemption from the securities laws, or that an interest in uniformity does not, in any event, support the adoption of a best-interest standard. DOL's bare assertion that a best-interest standard is needed because it is theoretically "stricter" is not a rational basis for finding existing regulation inadequate, particularly in light of Congress's contrary judgment in the Harkin Amendment.

ARGUMENT

I. DOL'S NEW DEFINITION OF A "FIDUCIARY" IS INVALID.

A. DOL's New Definition Of A "Fiduciary" Is Inconsistent With The Plain And Unambiguous Meaning Of ERISA.

DOL insists that *Chevron* deference applies to its interpretation of the term "fiduciary" in ERISA, but it completely ignores *Chevron*'s two-step framework. Under *Chevron*'s first step, a court must apply "ordinary tools of statutory construction" to "determine 'whether Congress has directly spoken to the precise question at issue,'" because "'[i]f the intent of Congress is clear, that is the end of the matter.'" *City of Arlington v. FCC*, 133 S. Ct. 1863, 1868 (2013). Thus, a court does not even reach *Chevron*'s second step—and evaluate the reasonableness of an agency interpretation—unless it concludes that a statutory term remains ambiguous after employing all tools of construction.

This case is properly resolved at *Chevron*'s first step. DOL's attempts to escape this conclusion are unavailing.

1. No deference is owed to DOL's views concerning the statute's plain meaning.

DOL repeatedly refers to *Chevron*, Br. 15-16, 19, 22, 36, but never mentions this Court's duty, in *Chevron* step one, to construe the statute itself. Instead, DOL effectively invites this Court to defer to *the agency's* assessment of ERISA's plain meaning. That invitation should be rejected.

DOL acknowledges the "presumption that Congress intends to incorporate a common-law term's meaning," but claims that *DOL* "reasonably interpreted ERISA's language, structure, and purpose to go beyond the [common law's] trust-and-confidence standard." Br. 25-26. In *Chevron* step one, however, DOL's views are irrelevant. The critical inquiry is whether *Congress* intended to depart from a common-law meaning. And this Court, not DOL, must make that determination. *See Chevron*, 467 U.S. at 842-43 (question of deference arises "[i]f … *the court determines*" that a statute is ambiguous) (emphasis added); *id.* at 843 n.9 ("judiciary is the final authority on issues of statutory construction").

Relying on a case involving the meaning of the term "employee" in the National Labor Relations Act (NLRA), DOL also suggests that its "'construction of [a common-law] term is entitled to considerable deference'" because the task of interpreting the term "fiduciary" has "'been assigned primarily to'" the agency. Br. 25 (quoting *NLRB v. Town & Country Elec., Inc.*, 516 U.S. 85, 94 (1995)). DOL's reli-

ance on this case is misplaced. Under the NLRA, "there is no doubt that … the commonlaw agency test" governs the meaning of "employee." *NLRB v. United Ins. Co. of Am.*, 390 U.S. 254, 256 (1968). Thus, the NLRB is not accorded deference in deciding *whether* the common-law test governs, but in *applying* that test in the "innumerable situations … where it is difficult to say whether a particular individual is an employee," *id.* at 258, including in close cases where the Board's application might depart from the common law "with respect to particular questions," *Town & Country Elec. Inc.*, 516 U.S. at 94 (citing *United Ins. Co. of Am.*, 390 U.S. at 25); *see also FedEx Home Delivery v. NLRB*, 849 F.3d 1123, 1127-28 (D.C. Cir. 2017) (in light of *United Insurance*, the principle that an agency can change its interpretation of an ambiguous statute does not apply to whether the common law determines employee status). Here, DOL does not claim deference to its application of a common-law test of "fiduciary" status to particular facts, but for its decision to jettison that test. Again, however, the issue at *Chevron* step one is whether *Congress* intended to jettison that test.

DOL's authority to prescribe regulations, Br. 23, also does not alter the *Chevron* step one inquiry. First, DOL has authority to issue regulations that "define accounting, technical and trade terms." 29 U.S.C. § 1135. The term "fiduciary," however, is not an "accounting, technical [or] trade ter[m]," but a common-law term with a settled meaning.

Second, and more fundamentally, even broad grants of rulemaking authority do not empower agencies to deviate from the plain meaning of statutes. As the Supreme Court recently explained, courts interpret a "grant of rulemaking authority in light of" *Chevron* and, "[w]here a statute is clear, the agency must follow the statute." *Cuozzo Speed Techs., LLC v. Lee*, 136 S. Ct. 2131, 2142 (2016) (citing *Chevron*). As we show next, proper application of the rules of construction makes clear that Congress intended to retain the hallmark of a fiduciary relationship in ERISA, and thus left no "gap" for DOL to fill or ambiguity for DOL to resolve.

2. Nothing in ERISA requires a departure from the common law's trust-and-confidence standard.

As plaintiffs have explained, IALC Br. 20-22, the presumption of common-law incorporation is strong: to overcome it, DOL must show that ERISA "*dictates*" a departure from the common law, *Nationwide Mut. Ins. Co. v. Darden*, 503 U.S. 318, 322 (1992) (emphasis added), because some aspect of the statute is "incompatible with" the common-law meaning, *Neder v. United States*, 527 U.S. 1, 25 (1999), or reflects an "unequivoca[l] … intent" to abandon it, *NLRB v. Amax Coal Co.*, 453 U.S. 322, 330 (1981). DOL completely ignores these cases and the standard they establish.

DOL cites *Varity Corp. v. Howe*, 516 U.S. 489, 497 (1996), for the proposition that the common law is merely the "starting point" for construing ERISA, Br. 27, then quotes snippets from cases in which the Supreme Court has noted that ERISA's

functional definition of a fiduciary "'expand[ed] the universe of persons subject to fiduciary duties,' … to 'commodiously impose[] fiduciary standards on persons whose actions affect the amount of benefits.'" *Id.* at 20-21 (quoting *Mertens v. Hewitt Assocs.*, 508 U.S. 248, 262 (1993); *John Hancock Mut. Life Ins. Co. v. Harris Trust & Sav. Bank*, 510 U.S. 86, 96 (1993) (brackets added by DOL)). None of these cases, however, abandons or waters down the presumption of common-law incorporation. To the contrary, in *Varity*, the Court cited *Darden* and reiterated its presumption. 516 U.S. at 502. And in the very sentence where it described the common law as a "starting point," the Court went on to explain that a court must consider whether "the language of [ERISA], its structure, or its purposes *require* departing from common-law trust requirements." *Id.* at 497 (emphasis added). Tellingly, DOL cites or quotes parts of this sentence four separate times, Br. 25-28, yet each time it omits the critical phrase "*require* departing from common-law trust requirements."

Mertens and *Varity* also illustrate the kind of statutory evidence that could "require" such a departure—and why such evidence is missing here. In *Mertens*, the Court noted that, under ERISA, fiduciaries include not only "persons named as fiduciaries by a benefit plan, … but also anyone else who exercises discretionary control or authority over the plan's management, administration, or assets." 508 U.S. at 251 (citation omitted). This functional definition is plainly "incompatible with," *Neder*, 527 U.S. at 25, and thus "require[s]" a departure from, *Varity*, 516 U.S. at

497, the common-law rule that "only the trustee had fiduciary duties." *Mertens*, 508 U.S. at 262. Similarly, in *Varity*, the Court recognized that, by permitting employers to serve as plan administrators, ERISA necessarily departed from the common-law rule that prohibited fiduciaries from holding positions that create conflicts of interest with trust beneficiaries. *Varity*, 516 U.S. at 498. *See also Pegram v. Herdrich*, 530 U.S. 211, 225 (2000) (in contrast to common law, ERISA permits fiduciaries to have "financial interests adverse to beneficiaries"). These cases confirm that a departure from the common law is *required*—and the presumption of common-law incorporation is thus overcome—only if some aspect of the statute is "inherently inconsistent" with the common law. DOL quarrels with plaintiffs' reading of *Mertens*.[1] But it never acknowledges the standard for overcoming the presumption of common-law incorporation set forth in *Darden*, 503 U.S. at 522 ("*dictates*" otherwise) (emphasis added), and *Varity*, 516 U.S. at 497 ("*require[s] departing from*") (emphasis added), and it offers no other coherent explanation for the departures recognized in *Mertens*, *Varity*, and *Pegram*.

[1] DOL deems plaintiffs' reading of *Mertens* "cramped" because the Court "did not mention written trust documents … in the relevant discussion." Br. 27. But the Court referred to persons "*named* as fiduciaries" in benefit plans, *Mertens*, 508 U.S. at 251 (emphasis added), and contrasted ERISA's functional definition with "*formal* trusteeship," *id.* at 262 (emphasis added)—both clear references to the formalities of a written trust.

Nothing in the "investment advice" prong of ERISA's fiduciary definition, moreover, is inherently inconsistent with the common law's trust-and-confidence standard. Indeed, DOL has never made any showing to the contrary. It simply recites dictionary definitions of the words "advice" and "investment." Br. 19-20. Those definitions, however, are not "incompatible with," *Neder*, 527 U.S. at 25, the conclusion that such advice must be provided in a relationship of trust and confidence. *See* IALC Br. 22.

Congress could have departed from the common law by defining "fiduciary" to include persons who "render *any* investment advice for a fee." That definition would sweep in all persons who provide any investment advice for a fee, whether or not they do so in a relationship of trust and confidence. But Congress did not include persons who "render *any* investment advice for a fee," despite its conspicuous use of the word "any" in the other two prongs of the definition. Congress' differential use of the word "any" in the other definitional prongs underscores that it did not jettison the common-law trust-and-confidence standard. *Id*. at 23-24. *See also* Chamber Op. Br. 36-38 (commissions are not paid for rendering investment advice in any event).

Nor is DOL correct in claiming that this common-law standard cannot be reconciled with the text of the other definitional prongs, DOL Br. 27, which include persons who exercise any discretionary authority with respect to plan management

or plan administration, and any control or authority over management or disposition of plan assets. 29 U.S.C. § 1002(21)(A)(i)&(iii). The broad authority described in these prongs epitomizes the powers that trustees exercise in relationships of trust and confidence.[2]

ERISA's legislative history confirms this. The Senate Report explains that a

> fiduciary is one who occupies a position of confidence or trust. As defined by the [Act], a fiduciary is a person who exercises any power of control, management or disposition with respect to monies or other property of an employee benefit fund, or who has authority or responsibility to do so.

S. Rep. No. 93-127 at 28-29. The second sentence does not "distinguish[h]" the trust-and-confidence standard from ERISA's control-or-authority definition, DOL Br. 28; it identifies the latter as an application of that standard. DOL likewise misconstrues the import of Congress's concerns about the applicability of traditional trust law to certain plans and whether trust law adequately protected retirement investors "ill-equipped" to safeguard their rights. *Id.* at 28-29. The first concern arose because some plans "do not use the trust form as their mode of funding," S. Rep. No. 93-127

[2] The Restatement (Second) of Trusts, extant when ERISA was enacted, provided that trustees could exercise powers conferred by the trust and all powers "necessary or appropriate to carry out" its purposes, § 186(b). For those entrusted with the care and management of property, this was an "extensive" grant, *id., cmt. d*, that included the power to incur expenses and to lease or sell property absent express prohibitions in the trust documents themselves, *see id.* §§ 188-190.

at 29—a concern Congress addressed by departing from trust-law formalities. Congress addressed the second concern by "allowing ready access to both detailed information about the plan and to the courts," and by specifying "standards … [to] measure the fiduciary's conduct." *Id.* These measures thus supplemented the trust-and-confidence standard; they did not eliminate it.[3]

3. Post-enactment changes in the marketplace cannot establish that ERISA's "purpose" requires a departure from the common law.

Unable to show that the text, structure, or history of ERISA is incompatible with the common-law trust-and-confidence standard, DOL claims that changes in the market since ERISA was enacted, particularly the greater reliance of retirement savers on products sold outside fiduciary relationships, creates an inconsistency with ERISA's purposes "sufficient to displace the common law." Br. 28; *see also id.* at 21-22. This claim is demonstrably incorrect.

[3] DOL also looks outside ERISA for evidence that Congress departed from the common law. Noting that Congress excluded incidental advice from the Investment Advisers Act but not ERISA, DOL claims that this difference "arguably" shows that Congress intended to include such advice in ERISA. Br. 34-35. But DOL nowhere addresses plaintiffs' showings that (1) negative inferences cannot be drawn from different language in different statutes and (2) Congress needed to limit "investment advice" in the Advisers Act because it did not define such advisers as "fiduciaries," and thus did not incorporate the common-law limitations that it incorporated into ERISA. *See* IALC Br. 29-30; *see also Darden*, 503 U.S. at 326 ("textual asymmetry between" ERISA and the Fair Labor Standards Act "precludes reliance on FLSA cases when construing ERISA's concept of 'employee'").

DOL cites no case in which any court has concluded that ERISA's purpose overrides a common-law rule. *Varity* certainly did not—it relied on the common law to interpret "fiduciary" and "administration" in ERISA. 516 U.S. at 502-07. In *Darden*, a case DOL simply ignores, the Court *rejected* the government's claim that Congress "must have intended a modified common-law definition" of the term "employee" because it would advance "the Act's 'remedial purposes.'" 503 U.S. at 325. And in *Mertens*, the Court refused to rely on ERISA's "purpose" to overcome the statute's text. 508 U.S. at 261-62.

Instead, DOL cites *United States v. Guidry*, 456 F.3d 493 (5th Cir. 2006), a wildly inapposite case that did not involve ERISA and serves only to underscore the impropriety of DOL's argument. *Guidry* involved the meaning of the term "kidnap" in a federal sentence-enhancement statute. In construing that term, this Court relied heavily on the Supreme Court's decision in *Taylor v. United States*, 495 U.S. 575 (1990), which construed the term "burglary" in a similar sentence-enhancement law. In both cases, the presumption of common-law incorporation was overcome by a factor not present here. As the Supreme Court explained in *Taylor*, the "problem" with presuming that Congress intended to incorporate "the 'classic' common-law definition" of burglary was that, by the time Congress enacted the federal sentence-enhancement statute in 1986, "the contemporary understanding of 'burglary' ha[d]

diverged a long way from its commonlaw roots." *Id.* at 593. As a consequence, "construing 'burglary' to mean common-law burglary would come close to *nullifying* that term's effect in the statute, because few of the crimes now generally recognized as burglaries would fall within the common-law definition." *Id.* at 594 (emphasis added). This Court confronted the same problem in *Guidry*: the meaning of "kidnapping" had also "evolved." *Guidry*, 456 F.3d at 509. Accordingly, this Court relied on the same reasoning to reject the common-law definition of "kidnapping." *See id.* at 510 (quoting the foregoing sentence from *Taylor* and substituting the word "kidnapping" for the words "burglary" and "burglaries").

The rationale of these cases is wholly inapplicable here. DOL has made no showing that, when ERISA was enacted in 1974, the understanding of "fiduciary" had "diverged a long way from its commonlaw roots." *Taylor*, 495 U.S. at 593. To the contrary, DOL does not dispute that the common-law meaning of "fiduciary" has long required a relationship of trust and confidence, and cases decided both before and after ERISA was passed recognized that one-time insurance sales do not create fiduciary relationships absent unusual circumstances. *See* IALC Br. 21-22 n.2. Construing "fiduciary" in accordance with its common-law meaning, therefore, would not have frustrated ERISA's purposes in 1974 or nullified the term's effect in the statute. Indeed, this is why the regulation DOL adopted in 1975 (and maintained for

four decades) reflected the trust-and-confidence requirement and excluded one-time, arm's-length sales. *Id.* at 25-26.

What DOL is really arguing is that the presumption of common-law incorporation can be overcome, not because of any evolution in the understanding of a *legal term* that occurred *before* enactment of a statute that incorporates that term, but because of changes in the *marketplace* that occurred *after* the statute was enacted. This argument cannot be correct. The presumption is used to determine a statute's "plain" meaning, and that meaning is necessarily fixed and permanent. DOL believes that the common law's trust-and-confidence requirement does not serve the interests of some retirement savers today. But that belief is a basis for urging Congress to amend the statute. It is not a basis for concluding that the plain meaning of "fiduciary" is different today than it was in 1974, or that the enacting Congress did not intend to incorporate the term "fiduciary's" common-law meaning.

B. DOL's Interpretation Is Unreasonable.

Even if the Court reaches *Chevron* step two—and it should not—DOL's interpretation is unreasonable because it is inconsistent with the agency's own recognition that ERISA incorporates the trust-and-confidence standard, and with Congress's intent in two other statutes. IALC Br. 31-35.

Although DOL carved out certain transactions because they "do not implicate relationships of trust," ROA.325, it claims that this was not "why [it] created" the

carve-out, Br. 29. Instead, DOL claims, it excluded transactions where "'neither party expects that recommendations will necessarily be based on the buyer's best interests.'" *Id.* (quoting ROA.356). But the reason that parties in arm's-length transactions do not expect recommendations to be based on a best-interest standard is *because* they are not in relationships of trust and confidence. The carve-outs thus rest on a recognition that ERISA requires a fiduciary to be in such a relationship, yet DOL dispensed with that requirement for other transactions. This "interpretive gerrymande[r]" is impermissible. *Michigan v. EPA*, 135 S. Ct. 2699, 2708 (2015).

Similarly, DOL dismisses the relevance of the Advisers Act and the Harkin Amendment because they are securities laws that impose disclosure obligations on all advisers regardless of the nature of their clients, whereas ERISA imposes different obligations on advisers to retirement savers. Br. 34-35. The mere fact that ERISA has a narrower focus, however, does not explain why Congress's decision to forgo regulation of advice incidental to one-time sales in the Adviser's Act has no pertinence to deciding whether Congress would want to regulate the same type of advice when provided to retirement savers. And DOL's purported distinction of the Harkin Amendment—that it concerns the treatment of "*all* fixed-indexed-annuity transactions," while ERISA protects "retirement investors' interests," *id*. at 35-36—is particularly facile, since virtually all FIAs are sold for retirement-related purposes, whether or not they are governed by ERISA. It is an "unreasonable interpretation of

Congress's intent," *Texas v. United States*, 497 F.3d 491, 509 (5th Cir. 2007), to attach fiduciary duties to the same kinds of incidental sales recommendations that Congress excluded from fiduciary treatment elsewhere, and to do so for the very retirement products that Congress exempted from federal regulation.[4]

II. DOL'S TREATMENT OF FIXED INDEXED ANNUITIES WAS ARBITRARY AND CAPRICIOUS.

In addition, DOL's treatment of FIAs was arbitrary and capricious because DOL failed (1) to give a reasoned explanation for finding that existing state regulation of FIA sales is insufficient to protect consumers or (2) to back up its empirical claim that FIA sales are causing significant consumer harms despite these existing regulations. IALC Br. 35-52.[5]

In response, DOL argues that it "was not required to assess the efficacy of state law" because ERISA does not expressly impose such a requirement. Br. 54. But as plaintiffs explained, the Administrative Procedure Act (APA) required DOL

[4] Moreover, contrary to DOL's claim, Br. 35, a later enacted law can be relevant to determining congressional intent for purposes of the *Chevron* step two inquiry. *Texas*, 497 F.3d at 504.

[5] DOL incorrectly characterizes this argument as attacking only its decision to require FIAs "to satisfy the BIC Exemption rather than the amended PTE 84-24." DOL Br. 49. In fact, plaintiffs' arbitrary-and-capricious challenge attacks both the basis for subjecting FIA sales to fiduciary regulation at all and—*a fortiori*—the basis for revoking the 84-24 exemption for FIAs. *See* IALC Br. 51-52.

to assess the sufficiency of existing regulation. IALC Br. 36-38. DOL does not dispute that the adequacy of existing regulation was a "relevant and significant" issue raised by commenters, *Del. Dep't of Nat. Res. & Envtl. Control v. EPA*, 785 F.3d 1, 15 (D.C. Cir. 2015), and an "important aspect of the problem," *Motor Vehicle Mfrs. Ass'n of U.S., Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983). Nor could it: imposing a costly and transformative new rule to address a problem that is adequately addressed by existing law would be manifestly arbitrary and capricious. *See Michigan*, 135 S. Ct. at 2707 ("reasonable regulation ordinarily requires paying attention to the advantages *and* the disadvantages of agency decisions"). In any event, having considered the sufficiency of existing regulation "with no assertion that it was not required to do so," DOL's consideration of that issue is subject to the APA's reasoned decisionmaking requirement, regardless of whether DOL was statutorily required to undertake the analysis. *See Am. Equity Inv. Life Ins. Co. v. SEC*, 613 F.3d 166, 177 (D.C. Cir. 2010); IALC Br. 38 n.7.

Thus, the issue before the Court is whether, in concluding that existing regulation is insufficient to prevent commission-based FIA sales from "inflicting excessive losses on investors," ROA.733, DOL "examine[d] the relevant data and articulate[d] a satisfactory explanation for its action including a rational connection between the facts found and the choice made," *State Farm*, 463 U.S. at 43. This stand-

ard of review, while deferential, is not toothless: the Court must undertake a "searching and careful" review of the agency's reasoning and evidence, *Citizens to Preserve Overton Park, Inc. v. Volpe*, 401 U.S. 402, 416 (1971), and may not uphold the agency's action "upon a ground not set forth by [the agency] itself," *S.D. ex rel. Dickson v. Hood*, 391 F.3d 581, 601 (5th Cir. 2004).

DOL relied on theoretical and empirical rationales for concluding that existing FIA regulation is insufficient. Because DOL relied heavily on both rationales and did not do so in the alternative, the rules must be vacated if either one is deficient. *See Nat'l Fuel Gas Supply Corp. v. FERC*, 468 F.3d 831, 839 (D.C. Cir. 2006). In fact, neither rationale comports with the APA's "scheme of reasoned decisionmaking." *Id.*

A. DOL Failed To Support Its Claim That FIA Sales Are Inflicting Consumer Harms Despite Existing Regulation.

DOL's showing of purported consumer harms rests on studies of mutual funds purporting to show that conflicted compensation harms mutual-fund investors. ROA.795-802. And the lynchpin of its defense of its treatment of FIAs is its claim that "it was reasonable for DOL to extrapolate data from the mutual-funds market to the fixed-indexed-annuities market." Br. 57. In fact, DOL provided no sound basis for that extrapolation, and its post-hoc arguments on appeal fare no better.

As plaintiffs showed, IALC Br. 46, the *only* basis that DOL provided *in the rulemaking proceeding* for extrapolating from mutual-fund studies to FIAs was its

citation, on page 795 of the ROA, of a single article by Evans and Fahlenbrach for the proposition that "insurance products also are likely to be subject to underperformance due to conflicts," ROA.795. But the Evans and Fahlenbrach article *does not even discuss FIAs*. DOL repeatedly cites page 795 of the ROA in its brief to this Court, but nowhere confronts the fact that the only explanation it provided for its extrapolation from mutual-fund studies was an article that is *silent* on FIAs. This alone is dispositive, because the rules can be upheld only "on the rationale set forth by the agency," and not based on "[p]ost-hoc explanations … by appellate counsel." *Hood*, 391 F.3d at 601.

Unable to defend its rationale in the rulemaking proceeding, DOL recycles the district court's assertion that the agency reasonably extrapolated from mutual funds to FIAs because both are "'subject to disclosure and suitability requirements, and agents selling both products are compensated with upfront commissions that depend on the product sold.'" DOL Br. 57 (quoting ROA.9924). But DOL cites no page of the record where *it* articulated this theory, and as plaintiffs pointed out—with no response from DOL—"this theory cannot be found on the pages the [district] court cited" either. IALC Br. 46. Those pages do not assert that the results from mutual-fund studies can be reliably extended to FIAs without regard to the obvious differences between the two products simply because both are sold on commission and are subject to similar regulatory requirements.

Nor has DOL shown that the dynamics that supposedly explain the underperformance of mutual funds sold on commission apply to FIAs. DOL pointed to studies asserting that mutual funds that pay commissions to brokers may consequently underinvest in fund management, for example because they are "more likely to outsource portfolio management and less likely to hire asset managers with superior educational backgrounds." ROA.986; *see also* ROA.788, 810, 985. But FIAs are not actively managed funds; their performance is tied to the performance of a market index like the S&P 500. Similarly, DOL asserted that "adviser conflicts inflict additional losses … by prompting IRA investors to trade more frequently, which will increase transaction costs and multiply opportunities for chasing returns and committing timing errors." ROA.795; *see also* ROA.790. But FIAs are "buy and hold" products that do not involve trading by the owner, and so this "pat[h] through which conflicted advice can be harmful to IRA investors," ROA.790, also does not apply to FIAs.

DOL's only answer is to double down on post-hoc rationalization by arguing that these distinctions—which DOL did not discuss in the rulemaking proceeding—are irrelevant because they "d[o] not negate advisers' incentive to recommend, at the outset of a transaction, that investors purchase an annuity that maximizes the advisers' financial interest at the customers' expense." Br. 59. But this is just another way of saying that commissions may create conflicts of interest for insurance agents; it

does not address the critical question: whether such conflicts *cause* significant harm to FIA buyers despite existing suitability protections. Because DOL identified no basis for believing that the causal mechanisms that purportedly link brokerage commissions to consumer harms in the mutual-fund market apply to FIAs, DOL could not rationally assume that the same type or degree of harms are likely to result from commission-based FIA sales.[6]

Because DOL's extrapolation from mutual funds to FIAs was unsupported and unreasonable, the rules must be vacated as applied to FIAs, regardless of DOL's other purported "evidence" concerning annuities. *See Nat'l Fuel*, 468 F.3d at 839. In all events, plaintiffs showed that DOL's other "evidence" is inapposite because it involves other products and markets that are not subject to suitability standards, or predates the enhancement of suitability standards in 2010. IALC Br. 48-50.[7] In response, DOL simply argues that it "reasonably declined to rely on plaintiffs' assessment of those standards' effectiveness." Br. 61. Yet DOL ignores the fact that one

[6] This is so regardless of whether commissions on FIAs are "larger and less transparent" than mutual-fund brokerage commissions. DOL Br. 56. This might affect an agent's incentive or ability to act on a conflict, but it says nothing about whether recommendations of suitable FIAs cause significant consumer harms.

[7] In yet another example, DOL cites a FINRA notice *from 2005* expressing concern that sales materials associated with FIAs did not fully describe them and could be confusing, Br. 53 (citing ROA.680), while ignoring the robust disclosure requirements embodied in the recent NAIC suitability and disclosure rules, *see* ROA.6032-33 § 6.A(1); ROA.4215-17 § 5.

of the very studies it relied on acknowledged that suitability rules can "meaningfully mitigate" the risk of self-interested advice, ROA.6086, and that studies in other countries "are not necessarily applicable to the U.S. market, where competitive and regulatory structures may be quite different," ROA.6077. And, in the end, DOL's only empirical basis for deeming suitability rules ineffective was that they purportedly "proved insufficient to protect mutual fund consumers from the harms of conflicts." Br. 60. Thus, without the mutual-fund studies to fall back on, DOL has no response to plaintiffs' showing that DOL's other "evidence" is irrelevant.[8]

Finally, as plaintiffs have explained, IALC Br. 47-48, and DOL nowhere rebuts, the agency cannot fall back on the purported lack of "available information" as to whether commission-based FIA sales are causing significant consumer harms despite existing regulation, Br. 57. DOL staked the rule in significant part on its affirmative claim that existing regulation has failed to prevent conflicts of interest from

[8] Contrary to the claim of one of DOL's *amici*, a 2015 study DOL cited in the rulemaking proceeding does not show that FIAs sold on commission are more likely to have detrimental product features. AARP Br. 23 n.8 (citing ROA.768). The study DOL cited refers to direct sales of fixed annuity contracts (which includes FIAs) and identifies the percentage of contracts that "had surrender charges in effect as of the end of Q2 2015." ROA.10826. Because surrender-charge periods lapse, however, the fact that 44 percent of these contracts sold directly had surrender charges in effect in 2015 does not establish that the other 56 percent (or any subset of that figure) were sold without surrender charges. The study does not identify the percentage of FIAs that never had a surrender charge, much less do so by distribution channel.

inflicting excessive consumer losses, but it failed to substantiate that claim with regard to FIAs. "Professing that [a rule] ameliorates a real industry problem but then citing no evidence demonstrating that there is in fact an industry problem is not reasoned decisionmaking." *Nat'l Fuel*, 468 F.3d at 843-44. DOL's post-hoc effort to "explai[n] away the *absence* of such evidence merely underscores the need to vacate." *Id.* at 844.

B. DOL Failed To Give A Rational Explanation For Finding That Existing Regulation Is Insufficient To Protect FIA Buyers.

Independently, the rules must be vacated because DOL failed to provide a rational explanation for its assertion that existing regulation of FIAs is inadequate. IALC Br. 38-44. DOL devotes much of its response to reciting at length the conditions that give rise to the risks of FIAs: their relative complexity, their various terms and risks, the information gap between agents and consumers, and the potentially misaligned incentives created by commissions. This shows that FIA sales should be regulated to protect consumers. It does not provide a rational basis to conclude that existing state suitability and disclosure rules, which are designed to address these very conditions, are inadequate and that costly new federal regulation is needed.

DOL has little to say about its actual rationale for finding state regulation inadequate. The agency, for example, relied heavily on the asserted lack of uniformity in state regulation. *E.g.*, ROA.679, 748, 777, 922. But this rationale is deficient for multiple reasons: (1) it does not establish that any state's regulation is inadequate,

(2) it ignores the fact—not disputed by the agency—that almost all FIAs are sold in compliance with requirements that are substantially similar to the NAIC model rules in order to qualify for the Harkin Amendment's safe harbor from securities regulation, and (3) it does not in any event justify the adoption of a best-interest standard as opposed to a suitability standard. IALC Br. 41-42. DOL's two passing references to its uniformity rationale, Br. 55, 56, respond to none of these points. The deficiency of this rationale alone renders the rules infirm. *See Am. Equity*, 613 F.3d at 177-78 (holding that the SEC's reliance on an interest in clarifying the regulatory status of FIAs was arbitrary and capricious).

DOL also has no persuasive response to plaintiffs' showing that it failed to give meaningful consideration or weight to Congress's judgment in the Harkin Amendment that the NAIC suitability rules are sufficient to protect consumers. IALC Br. 43. DOL argues that it "discussed this provision," Br. 61, but it merely acknowledged the Harkin Amendment's existence and described its terms; it never *explained* why Congress's judgment embodied in that provision does not apply equally here. The agency now seeks to fill that gap by arguing that its rules target only a "subset" of the transactions governed by the securities laws. *Id.*; *see id.* at 35-36. But this is another impermissible post-hoc rationalization, and an unpersuasive one at that. *See supra*, p. 15. DOL itself relied heavily on purported "concerns" expressed by securities regulators. *E.g.*, ROA.555, 777, 921. It cannot now contend

that Congress's resolution of those very concerns is irrelevant simply because the securities laws apply to a broader category of transactions than ERISA.

Nor is there any merit to the claim that DOL's treatment of FIAs is justified by the need to "creat[e] a level playing field" between FIAs and mutual funds and to "avoi[d] creating a regulatory incentive to preferentially recommend [FIAs]." Br. 50-51. This rationale has nothing to do with the adequacy of existing regulation. It elides critical differences between mutual funds and FIAs. *See supra*, p. 20. And it arbitrarily ignores the regulatory incentive to preferentially recommend fixed-rate annuities created by DOL's decision to revoke the 84-24 exemption for FIAs.

At bottom, DOL's theoretical rationale boils down to its observation that a suitability standard might in theory allow an agent to act on a conflict of interest by recommending an FIA that is suitable for the customer but less beneficial than another FIA that offers the agent a lower commission. ROA.671, 733, 747-48, 768. But as plaintiffs pointed out, again without any response from the agency, "DOL did not explain how likely it is that higher commissions will attach to suitable but less beneficial products, or why it is reasonable to assume that the magnitude of any difference between two suitable products is so significant that the resulting consumer harm warrants federal regulation." IALC Br. 40. Particularly in the absence of any empirical evidence of consumer harms resulting from recommendations of suitable-

but-suboptimal FIAs, *see supra* § II.A, and given DOL's extensive reliance on alleged consumer harms resulting from sales of *unsuitable* products, *see* IALC Br. 40, the theoretical difference between a best-interest standard and a suitability standard is not a rational basis to reject the adequacy of existing suitability rules—the very same rules that Congress, in recent legislation enacted in response to the very same concerns cited by DOL, deemed adequate to protect consumers.[9]

[9] The theoretical difference between a best-interest standard and a suitability standard clearly does not support DOL's decision to revoke the 84-24 exemption for FIAs, since the amended 84-24 exemption imposes a best-interest standard. IALC Br. 51.

CONCLUSION

For the foregoing reasons, and those set forth in the IALC plaintiffs' opening brief, the fiduciary rules should be set aside in their entirety. Alternatively, the rules' application to FIAs, or at a minimum, the revocation of the 84-24 exemption for FIAs, should be set aside as arbitrary and capricious.

July 20, 2017

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on the 20th day of July, 2017, an electronic copy of the foregoing brief was filed with the Clerk of Court for the United States Court of Appeals for the Fifth Circuit using the appellate CM/ECF system, and that service will be accomplished by the appellate CM/ECF system.

Dated: July 20, 2017

/s/ Joseph R. Guerra

JOSEPH R. GUERRA

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