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

REPLY MEMORANDUM IN SUPPORT OF DEFENDANTS' COMBINED CROSS-MOTIONS FOR SUMMARY JUDGMENT

TABLE OF CONTENTS

TABLE OF CONTENTS i

TABLE OF AUTHORITIES iii

ACRONYMS USED x

INTRODUCTION 1

ARGUMENT 1

I. The Department's Reasonable Interpretation of Fiduciary "Investment Advice" Is Entitled to Deference 1

A. ERISA's Broad Statutory Language Does Not Compel an Interpretation Limited to Relationships Recognized as Fiduciary at Common Law 2

B. DOL Reasonably Defined Fiduciary "Investment Advice" in Conformance with ERISA's Statutory Text, Not the Common Law the Statutory Definition Replaced 4

C. DOL Reasonably Defined Fiduciary "Investment Advice" in Conformance with ERISA's Statutory Text, Not Distinctions Rooted in Securities Laws 7

II. The Department Has Express Statutory Authority to Grant Conditional Exemptions for Tax-Favored Accounts 12

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" 14

IV. DOL's Cost Benefit Analysis Supports its Rulemaking 17

V. The Inclusion of Annuities in the Best Interest Contract Exemption is Reasonable 21

A. DOL Sufficiently Explained its Reasons for Including Variable Annuities and FIAs in the BIC Exemption 21

B. DOL's Rulemaking Appropriately Treats Classes of Products Differently Due to Different Degrees of Conflicts of Interest 23

C. DOL Appropriately Took Existing Annuity Regulation into Account in Determining How to Regulate Variable Annuities and FIAs 24

D. The BIC Exemption is Sufficiently Workable for Annuities 27

E. DOL Provided Adequate Notice and Opportunity to Comment on the Scope of Annuities to be Covered by PTE 84-24 30

VI. Exemptions Requiring that Contracts Allow for Class Action Lawsuits Do Not Violate the Federal Arbitration Act 32

VII. DOL's Rulemaking Is Consistent with the First Amendment 33

A. The Rulemaking is a Valid Regulation of Professional Conduct 34

B. The Rulemaking is a Valid Regulation of Inherently Conflicted Transactions 36

C. The Rulemaking Directly Advances the Government's Interest in Protecting Retirement Investors from Conflicted Investment Advice 39

CONCLUSION 40

TABLE OF AUTHORITIES

CASES

10 Ring Precision, Inc. v. Jones,
722 F.3d 711 (5th Cir. 2013) 32

Accountant's Soc'y of VA v. Bowman,
860 F.2d 602 (4th Cir. 1988) 42

AFL-CIO v. Donovan,
757 F.2d 330 (D.C. Cir. 1985) 14, 16, 17

Alamo Express, Inc. v. ICC,
673 F.2d 852 (5th Cir. 1982) 22

Alexander v. Sandoval,
532 U.S. 275 (2001) 17

Allina Health Servs. v. Sebelius,
746 F.3d 1102 (D.C. Cir. 2014) 37

Am. Equity v. SEC,
613 F.3d 166 (D.C. Cir. 2010) 29

Am. Fed'n of Unions Local 102 Health & Welfare Fund v. Equitable Life Assurance Soc'y,
841 F.2d 658 (5th Cir. 1988) 9, 10

Am. Trucking Assocs. v. ICC,
656 F.2d 1115 (5th Cir. 1981) 16

Associated Builders & Contractors of Texas, Inc. v. NLRB,
826 F.3d 215 (5th Cir. 2016) 21

Astra USA, Inc. v. Santa Clara County, Cal.,
563 U.S. 110 (2011) 17, 18

AT&T Mobility LLC v. Concepcion,
563 U.S. 333 (2011) 38

Austin v. Gen. Am. Life Ins. Co.,
498 F. Supp. 844 (N.D. Ala. 1980) 7

BASF Wyandotte Corp. v. Cottle,
598 F.2d 637 (1st Cir. 1979) 36
Brazos Elect. Power Coop., Inc. v. Sw. Power Admin.,
819 F.2d 537 (5th Cir. 1987) 37

Bowen v. Kendrick,
487 U.S. 589 (1988) 11

Brock v. Self,
632 F. Supp. 1509 (W.D. La. 1986) 11

Burlington N. & Santa Fe Ry. Co. v. White,
548 U.S. 53 (2006) 12, 19

Cent. Hudson Gas & Elec. Corp. v. Pub. Serv. Comm'n of New York,
447 U.S. 557 (1980) 43

Cent. States, Se. & Sw. Areas Pension Fund v. Cent. Transp., Inc.,
472 U.S. 559 (1985) 5

Central & Sw. Servs., Inc. v. EPA,
220 F.3d 683 (5th Cir. 2000) 40

Central & Sw. Servs., Inc. v. EPA,
532 U.S. 1065 (2001) 40

Chemical Mfrs. Ass'n v. EPA,
870 F.2d 177 (5th Cir. 1989) 31, 35

Chevron U.S.A., Inc. v. Nat'l Res. Def. Council,
467 U.S. 837 (1984) 2, 4

City of Arlington v. FCC,
668 F.3d 229 (5th Cir. 2012) 32, 37

Clackamas Gastroenterology Assocs., P.C. v. Wells,
538 U.S. 440 (2003) 4, 5

Conn. Bar Ass'n v. United States,
620 F.3d 81 (2d Cir. 2010) 40

ConocoPhillips Co. v. EPA,
612 F.3d 822 (5th Cir. 2010) 23, 30, 31

CSX Transp., Inc. v. Surface Transp. Bd.,
754 F.3d 1056 (D.C. Cir. 2014) 40

David P. Coldesina, D.D.S. v. Estate of Simper,
407 F.3d 1126 (10th Cir. 2005) 7

Davis v. United Air Lines, Inc.,
575 F. Supp. 677 (E.D.N.Y. 1983) 18

Davis Mountain Trans-Pecos Heritage Ass'n v. FAA,
116 F. App'x 3 (5th Cir. 2004) 18

Ellis v. Rycenga Homes, Inc.,
484 F. Supp. 2d 694 (W.D. Mich. 2007) 7, 9, 10, 11

Encino Motorcars, LLC v. Navarro,
136 S. Ct. 2117 (2016)... 25

Farm King Supply, Inc. Integrated Profit Sharing Plan & Tr. v. Edward D. Jones & Co.,
884 F.2d 288 (7th Cir. 1989) 10

Fin. Planning Ass'n v. SEC,
482 F.3d 481 (D.C. Cir. 2007) 12

Gibson v. Tex. Dep't of Ins.,
700 F.3d 227 (5th Cir. 2012) 40

Grizzle v. Tex. Commerce Bank,
38 S.W. 3d 265 (Tex. App. 2001) 34

Grochowski v. Phoenix Constr.,
318 F.3d 80 (2d Cir. 2003)... 17, 18, 37

Hines v. Alldredge,
783 F.3d 197 (5th Cir. 2015) 40

Hines v. Alldredge,
136 S. Ct. 534 (2015)... 40

Hughes Aircraft Co. v. Jacobson,
525 U.S. 432 (1999)... 7

In re R. M. J.,
455 U.S. 191 (1982)... 40

John Hancock Mut. Life Inc. Co. v. Harris Tr. & Sav. Bank,
510 U.S. 86 (1993)... 6

Kellam v. Servs.,
No. 3:12-cv-352-P, 2013 WL 12093753 (N.D. Tex. May 31, 2013) 2

Kellam v. Metrocare Servs.
560 F. App’x 360 (5th Cir. 2014) 2

King v. Christie,
135 S. Ct. 2048 (2015) 40

King v. Governor of New Jersey,
767 F.3d 216 (2014) 40

Locke v. Shore,
634 F.3d 1185 (11th Cir. 2011) 40

LoPresti v. Terwilliger,
126 F.3d 34 (2d Cir. 1997) 3, 4, 9

Lowe v. General Motors Corp.,
624 F.2d 1373 (5th Cir. 1980) 18

Lowe v. S.E.C.,
472 U.S. 181 (1985) 40

Marathon Oil Co. v. EPA,
830 F.2d 1346 (5th Cir. 1987) 22

Markle Interests, LLC. v. U.S. Fish & Wildlife Serv.,
827 F.3d 452 (5th Cir. 2016) 21, 28

MCI Telecomms. Corp. v. Am. Tel. & Tel. Co.,
512 U.S. 218 (1994) 14, 15

Mertens v. Hewitt Assocs.,
508 U.S. 248 (1993) 1, 5, 6, 7

Michigan v. EPA,
135 S. Ct. 2699 (2015) 21

MM&S Financial, Inc. v. Nat’l Ass’n of Secs. Dealers, Inc.,
364 F.3d 908 (8th Cir. 2004) 17

Moon v. BWX Techs., Inc.,
577 F. App’x 224 (4th Cir. 2014) 3

Moore-King v. Cty. of Chesterfield, Va.,
708 F.3d 560 (4th Cir. 2013) 40

Native Fish Soc. v. Nat'l Marine Fisheries Servs.,
992 F. Supp. 2d 1095 (D. Or. 2014) 37

Nat'l Ass'n for the Advancement of Multijurisdiction Practice v. Lynch,
826 F.3d 191 (4th Cir. 2016) 40

Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Services,
545 U.S. 967 (2005) 3

Nat'l Propane Gas Ass'n v. U.S. Dep't of Transp.,
43 F. Supp. 2d 665 (N.D. Tex. 1999) 24, 25

Nebraska v. EPA,
331 F.3d 995 (D.C. Cir. 2003) 39

Niss v. Nat'l Ass'n of Secs. Dealers, Inc.,
989 F. Supp. 1302 (S.D. Cal. 1997) 17

Ohralik v. Ohio State Bar Ass'n,
436 U.S. 447 (1978) 40

Owner-Operator Indep. Drivers Ass'n, Inc. v. Fed. Motor Carrier Safety Admin.,
494 F.3d 188 (D.C. Cir. 2007) 32

Palma v. Verez Assur., Inc.,
79 F.3d 1453 (5th Cir. 1996) 18

PDK Labs., Inc. v. DEA,
362 F.3d 786 (D.C. Cir. 2004) 27

Pegram v. Herdrich,
530 U.S. 211 (2000) 3, 5, 6

Pickup v. Brown,
740 F.3d 1208 (9th Cir. 2013) 40

Pickup v. Brown,
134 S. Ct. 2871 (2014) 40

Reed v. Town of Gilbert,
135 S. Ct. 2218 (2015) 40

San Luis & Delta-Mendota Water Auth. v. Jewell,
747 F.3d 581 (9th Cir. 2014) 18

Serafine v. Branaman,
810 F.3d 354 (5th Cir. 2016) 40

Srein v. Frankford Trust Co.,
323 F.3d 214 (3d Cir. 2003).. 7

Sugar Cane Growers Co-op. v. Veneman,
289 F.3d 89 (D.C. Cir. 2002) 40

Teledesic LLC v. FCC,
275 F.3d 75 (D.C. Cir. 2001) 18

Tex Tin Corp. v. EPA,
935 F.2d 1321 (D.C. Cir. 1991) 39

Thomas, Head & Greisen Employees Trust v. Buster,
24 F.3d 1114 (9th Cir. 1994) 11, 14

Trinity Indus. v. Occupational Safety & Health Review Comm'n,
111 F. App'x 751 (5th Cir. 2004) 11, 14

Umland v. PLANCO Financial Services, Inc.,
542 F.3d 59 (3d Cir. 2008)... 17, 18, 21

United Steelworkers of Am. v. Schuylkill Metals Corp.,
828 F.2d 314 (5th Cir. 1987) 35

Util. Air Regulatory Grp. v. EPA,
134 S. Ct. 2427 (2014).. 20

Varity Corp. v. Howe,
516 U.S. 489 (1996).. 6, 7

Weaver v. U.S Information Agency,
87 F.3d 1429 (D.C. Cir. 1996) 39

STATUTES

9 U.S.C. § 2.. 38

15 U.S.C. § 80b-2(a)(11) 12

15 U.S.C. § 78s(g)(1).. 18

26 U.S.C. § 3111 .... 15, 16

26 U.S.C. § 4975(c) 14, 15, 16, 21

29 U.S.C. § 186(c)(5) 5

29 U.S.C. § 1002(21)(A) .... passim

29 U.S.C. § 1103(a) 5

29 U.S.C. § 1108(a) 16, 21, 28, 32

29 U.S.C. § 1108(b)(2) 20

Dodd-Frank Wall Street Reform and Consumer Protection Act,
Pub. L. No. 111-203, 124 Stat. 1376 (2010) 29

REGULATIONS

29 C.F.R. § 2510.3-21(a)(1) 9

29 C.F.R. § 2510.3-21(g)(3) 9

Definition of the Term "Fiduciary"
40 Fed. Reg. 50842 (Oct. 31, 1975) 8

Employee Benefit Plans,
41 Fed. Reg. 56760 (Dec. 29, 1976) 8

Amendment to PTE 84-24
71 Fed. Reg. 5887 (Fed. 3, 2006) 19

Investment Advice – Participants & Beneficiaries
76 Fed. Reg. 66136 (Oct. 25, 2011) 23

FINRA Customer Code Rule 12204 33

OTHER AUTHORITY

Dep't of Enforcement v. Charles Schwab & Co.
(FINRA Bd. of Governors Apr. 24, 2014) [Link] 33

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") exercised its express statutory authority to define "fiduciary" for purposes of the Employee Retirement Income Security Act ("ERISA") to better align its regulation to ERISA's statutory text, legislative history and remedial purposes in light of today's marketplace for retirement investment advice. It also provided exemptions that allow those who give fiduciary investment advice to continue to collect common forms of compensation, while ensuring that their advice is in the best interests of retirement investors. Plaintiffs challenge DOL's exercise of authority but do not even attempt to refute that the Rule's fiduciary definition comports with an ordinary understanding of the key statutory text, or that the exemptions DOL adopted will mitigate conflicts of interest inherent in much of the retirement investment advice given to today. The various arguments Plaintiffs advance—from attempts to rollback ERISA standards to the common law ones ERISA replaced to attempts to undermine DOL's extraordinarily thorough cost-benefit analysis—are simply efforts to insulate brokers and insurance agents from fiduciary obligations to provide investment advice in the best interest of retirement investors and be held accountable for that advice. Plaintiffs' claims should be rejected.

ARGUMENT

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

DOL has shown that the Rule, which defines fiduciary investment advice in terms of specified "recommendations" concerning "investment property," comports with an ordinary understanding of the statutory text, which extends fiduciary status to those who "render[] investment advice for a fee or other compensation, direct or indirect."[1] *See* Defs.' Br. 29-32, ECF No. 72-1. Plaintiffs do not dispute this, failing even to analyze the central text, 29 U.S.C. § 1002(21)(A)(ii) ("renders investment advice"). *See* Chamber of Commerce Opp'n 2-16 ("Ch.

[1] "[A] person is a fiduciary with respect to a plan to the extent: ... (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 ...." 29 U.S.C. § 1002(21)(A).

Opp'n"), ECF No. 109; IALC Opp'n 2-7, ECF No. 108. Indeed, Plaintiffs largely ignore Congress's three-pronged statutory definition, urging the Court to rely instead on the common law understanding (as articulated by Plaintiffs) of "fiduciary"—the very term Congress took pains to define. *See* Ch. Opp'n 3; IALC Opp'n 1. Plaintiffs' reasoning is directly at odds with ERISA's text, legislative history, and Supreme Court precedent, all of which demonstrate that Congress displaced the common law with a functional test for fiduciary status to better protect Americans' retirement savings. Defs.' Br. 31-33, 41-42; *Mertens v. Hewitt Assocs.*, 508 U.S. 248, 255 n.5 (majority), 264 (White, J., dissenting) (1993) (Congress adoption of an "artificial definition of 'fiduciary'" was an "express statutory departure" from the common law).[2] In addition, Plaintiffs' claim that the Rule unreasonably includes "[b]rokers and other salespersons," who "are not paid for providing advice," Ch. Opp'n 3; IALC Opp'n 1, relies on a dichotomy between advice and sales that is neither reflected in ERISA nor existent in reality—as shown by ACLI's own statements, confirming that brokers and agents are compensated for the investment advice they give in the course of selling retirement investment products. *See* Defs.' Br. 33-37.

A. ERISA's Broad Statutory Language Does Not Compel an Interpretation Limited to Relationships Recognized as Fiduciary at Common Law

As DOL has shown, Congress adopted a broad definition of "fiduciary" in ERISA, including a person who "renders investment advice for a fee or other compensation, direct or indirect," 29 U.S.C. § 1002(21)(A), and delegated to the agency the authority to interpret who qualifies as an "investment advice" fiduciary. *Id.* § 1135; Defs.' Br. 29-31. Plaintiffs do not dispute this, but IALC nonetheless argues that a showing of a "relationship of trust and confidence," as purportedly required for fiduciary status under the common law, is "compelled by … the statutory text." IALC Opp'n 4.[3] Setting aside whether IALC's interpretation of the common

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

[3] Chamber argues that the Rule's definition is "unreasonable" and "arbitrary," not that it is foreclosed by ERISA's text. Ch. Opp'n 3; *see id.* 2-16. It thus concedes that the Rule should be analyzed under *Chevron* step two, meaning that it is entitled to "controlling weight unless [it is] arbitrary, capricious, or manifestly contrary to the statute." *Chevron U.S.A., Inc. v. Nat'l Res. Def. Council*, 467 U.S. 837, 844 (1984); *Kellam v. Servs.*, 2013 WL 12093753, at

law is correct, ERISA's fiduciary definition nowhere refers to the common law or a relationship of trust and confidence. *See* § 1002(21)(A). And IALC's argument that its interpretation is "compelled by … the statutory text" is unavailing where it is devoid of any analysis of the central text—what it means to "render[] investment advice." *See* IALC Opp'n 1-7.

Further, as explained, Congress found that the common law was not adequately protecting retirement investors and thus expressly departed from it in adopting ERISA's "fiduciary" definition. *See* Defs.' Br. 31-33, 41-42. The principal inquiry for determining whether a person is acting as a fiduciary under ERISA is therefore not whether that person is in a relationship of trust and confidence recognized as fiduciary under the common law, but whether that person is performing one of the three fiduciary functions set forth in § 1002(21)(A). *See Pegram v. Herdrich*, 530 U.S. 211, 226 (2000) ("threshold question" to determine "whether [a] person was acting as a fiduciary" under ERISA is whether that person "was performing a fiduciary function").[4]

IALC's sole argument in support of its position is that the second prong should be read "consistent[ly] with" the other two prongs, which IALC alleges "afford[] such broad powers" that those who wield them are "necessarily those in whom others repose special trust and confidence." IALC Opp'n 4. IALC offers no support for its bare assertion that the first and third prongs, which speak in terms of "any" exercise of authority, control, or responsibility, *see* § 1002(21)(A)(i), (iii), inherently involve "broad powers," or that those who wield them are "necessarily" in positions of trust and confidence. *See* IALC Opp'n 4; Defs.' Br. 29-30, 37. While they might be in positions of trust and confidence, Congress did not require an independent showing of such a relationship to confer fiduciary status. Where IALC fails to analyze the central text and where Congress expressly adopted ERISA's definition to displace the common law because it had proven ineffective, *see* Defs.' Br. 31-32, 41-42, IALC has not shown that its interpretation is consistent

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*3 (N.D. Tex. May 31, 2013) (failure to respond to arguments constitutes abandonment or waiver of issue).

[4] *See also LoPresti v. Terwilliger,* 126 F.3d 34, 40 (2d Cir. 1997) ("Unlike the common law definition under which fiduciary status is determined by virtue of the position a person holds, ERISA's definition is functional.").

with the statutory text, much less that DOL's interpretation is "unambiguously foreclose[d]" by it. *Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs.*, 545 U.S. 967, 983 (2005).

B. DOL Reasonably Defined Fiduciary "Investment Advice" in Conformance with ERISA's Statutory Text, Not the Common Law the Statutory Definition Replaced

Because Plaintiffs have failed to show that DOL's interpretation is foreclosed by the statutory text, that interpretation is entitled to deference so long as it is reasonable. *Chevron*, 467 U.S. at 865. DOL's interpretation easily meets this standard. The Rule, which defines fiduciary "investment advice" in terms of specified "recommendations" concerning "investment property," 29 C.F.R. § 2510.3–21(a)(1)(i)-(ii), comports with an ordinary understanding of the text and is supported by ERISA's legislative history. *See* Defs.' Br. 29-34. And the Rule serves ERISA's remedial purpose by extending fiduciary status, and its attendant duties and restrictions, to the majority of those providing investment advice to retirement investors today. *See id.* 39-41.

Without disputing that the Rule comports with an ordinary understanding of the statutory text, Plaintiffs again invoke their understanding of the common law to challenge the reasonableness of the Rule's definition. *See* Ch. Opp'n 3; *see also* IALC Opp'n 1 (arguing that DOL's interpretation is unreasonable because it would encompass "[b]rokers and other salespersons," who are not in relationships of "special intimacy or . . . trust and confidence"). But their argument rests on the erroneous premise that Congress, in providing a *statutory* definition of "fiduciary" in ERISA, largely "incorporated" the *common law* understanding of who qualifies as a fiduciary. Ch. Opp'n 3. While courts may look to the common law "to fill gaps in statutory text" in the face of "congressional silence," *Clackamas Gastroenterology Assocs., P.C. v. Wells*, 538 U.S. 440, 447 (2003), they do not do so where, as here, Congress did not silently leave a statutory gap, but provided a three-pronged statutory definition. *Id.* (courts may look to the common law "when an *undefined* term has a settled meaning at common law"). If Congress had intended to incorporate the common law understanding of fiduciary status, it knew how to do so. *See Cent. States, Se. & Sw. Areas Pension Fund v. Cent. Transp., Inc.*, 472 U.S. 559, 570 (1985)

(citing, *inter alia*, 29 U.S.C. §§ 1103(a), 186(c)(5) ("[R]ather than explicitly enumerating *all* of the powers and duties of trustees and other fiduciaries, Congress invoked the common law of trusts to define the general scope of their authority and responsibility.")). But while Congress relied on the common law to inform fiduciary *duties*, it did not look to the common law to define fiduciary *status* but made clear that "the definition of fiduciary … is a departure from current judicial precedents but is necessary to the proper protection of … plans." 120 Cong. Rec. 3977, 3983 (1974) (Rep. Perkins). *See* Defs.' Br. 31-33.[5] Accordingly, the Supreme Court has cautioned that "[b]eyond the threshold statement of [fiduciary] responsibility … the analogy between ERISA fiduciary and common law trustee becomes problematic." *Pegram*, 530 U.S. at 225.

Unable to refute the substantial authority showing that Congress, in defining "fiduciary" in ERISA, took an "express statutory departure" from the common law, *Mertens*, 508 U.S. at 262 (White, J., dissenting), Plaintiffs concede as much, *see* Ch. Opp'n 4, but argue that Congress deviated from the common law only by extending fiduciary status beyond "those expressly *named* as trustees." *Id.* There is simply no support for Plaintiffs' cramped interpretation. While *Mertens* noted that ERISA fiduciaries include both named fiduciaries and those who fall within the definition at § 1002(21)(A), it did not conclude or otherwise indicate that ERISA's *only* expansion of fiduciary status was to include unnamed individuals. *See* 508 U.S. at 251-52, 262. And the Supreme Court has recognized numerous ways in which ERISA's fiduciary definition fundamentally departed from the common law. *See, e.g., Pegram*, 530 U.S. at 225 (ERISA fiduciaries can include those with financial interests adverse to beneficiaries, such as employers, plan sponsors, and others who provide benefits to a plan); *Varity Corp. v. Howe*, 516 U.S. 489,

[5] Plaintiffs point to statements in the legislative history that a "fiduciary is one who occupies a position of confidence and trust." *See* Ch. Opp'n 7. Such statements do not show that Congress required an independent showing of a relationship of trust and confidence in order to be a fiduciary under ERISA, nor do they overcome Congress's indication that it sought to depart from the common law and adopted a definition that nowhere refers to trust and confidence. Instead, ERISA's "fiduciary" definition creates such a relationship whether or not the common law would have done so. *See* 120 Cong. Rec. at 3983 (Rep. Perkins) ("It is the clear intention of the Committee that any person with a specific duty imposed on him by this statute be deemed to be a fiduciary").

498 (1996) (ERISA allows a fiduciary to be both an employer and plan administrator).[6]

What's more, Plaintiffs' interpretation begs the question: if Congress expanded fiduciary status to include those who are not named fiduciaries, how does one determine who those fiduciaries are? Plaintiffs would have the Court look to whether the person is in a relationship of trust and confidence, or is carrying out functions, recognized as fiduciary under the common law. *See* Ch. Opp'n 5; IALC Opp'n 2. But the courts have rightly concluded that the relevant inquiry under ERISA is to ask whether a person is carrying out one of the three enumerated functions in the statutory text. *See Pegram*, 530 U.S. at 225-26. Plaintiffs' interpretation would require the Court to determine not only whether a person carried out one of those enumerated activities, but also whether that person and the advisee were in a relationship of trust and confidence recognized as fiduciary under the common law. *See* Ch. Opp'n 3-4; IALC Opp'n 2. Even if Plaintiffs' understanding of the common law were correct, their interpretation imposes additional non-textual requirements to be an ERISA fiduciary, thereby narrowing the class of individuals who could qualify. Such an outcome is inconsistent with ERISA's purpose to "expand the universe of persons subject to fiduciary duties," *Mertens*, 508 U.S. at 262, and therefore, "must give way" to the statute's text and purposes. *Hughes Aircraft Co. v. Jacobson*, 525 U.S. 432, 447 (1999).

For similar reasons, Plaintiffs are incorrect that ERISA's fiduciary definition does not extend to "[b]rokers and other salespersons" on the theory that "fiduciary and sales relationships are fundamentally different and mutually exclusive." Ch. Opp'n 3, 8. Plaintiffs' view is at odds with the fact that ERISA extends fiduciary status, "regardless of status or title," to individuals "to the extent they are performing one of the functions identified in the definition." *David P. Coldesina, D.D.S. v. Estate of Simper*, 407 F.3d 1126, 1132 (10th Cir. 2005). "Fiduciary status

[6] Plaintiffs' attempt to rely on *Varity* is misplaced. *See* Ch. Opp'n 5-6. To determine whether Varity was acting as a fiduciary, the Court did not evaluate whether it was in a relationship of trust and confidence recognized as fiduciary under the common law; instead, the Court "interpret[ed] the statutory terms which limit the scope of fiduciary activity to discretionary acts of plan 'management' and 'administration.'" *Varity*, 516 U.S. at 502. While the court referenced common law understandings of "administration" when conducting its analysis, it was, at bottom, tethered to the statutory text. Here, Plaintiffs do not conduct a textual analysis of what it means to "render[] investment advice," or even analyze the common law understanding of those terms, and thus are not following *Varity*.

under § 1002(21)(A) is not an all or nothing concept. A court must ask whether a person is a fiduciary with respect to the particular activity in question." *Srein v. Frankford Tr. Co.*, 323 F.3d 214, 221 (3d Cir. 2003). It is thus irrelevant whether an individual is a broker or not or involved in a sale or not. To the extent he "renders investment advice," he is a fiduciary under ERISA, and the Rule is not unreasonable for failing to excise brokers and agents from fiduciary status.[7]

C. DOL Reasonably Defined Fiduciary "Investment Advice" in Conformance with ERISA's Statutory Text, Not Distinctions Rooted in Securities Laws

Plaintiffs next reiterate their argument that the Rule is unreasonable because it applies fiduciary status to those, like brokers and insurance agents, who receive commissions, rather than fees solely for investment advice. *See* Ch. Opp'n 9-13. Nothing in the text—which applies fiduciary status to those "who render[] investment advice for a fee or other compensation, direct or indirect"—suggests that compensation must be paid solely, or even principally, for investment advice. Defs.' Br. 35. DOL has thus long interpreted that broad language to include all compensation incident to a transaction in which investment advice is given. *See id.* And Plaintiffs cannot credibly dispute what ACLI concedes: that brokers and agents *are* compensated for investment advice in the course of selling their products. *Id.* 36-37. In an attempt to support their reading that ERISA applies fiduciary status only to those paid solely for investment advice, Plaintiffs contort the statutory language, isolating the term "for" from the rest of the text and reversing the clause to argue that "the preposition 'for' indicates that the *purpose* of the compensation is to pay for the advice." *Id.* at 9. But the statute does not say that *compensation* is paid "for" rendering investment advice, as Plaintiffs suggest, *see id.*, but that *investment advice* is

[7] Plaintiffs' bare assertion that [b]rokers and other salespersons" have never been understood to be fiduciaries, Ch. Opp'n 3, is incorrect, as fiduciary status under ERISA has always turned on functions, not labels. *See, e.g., Ellis v. Rycenga Homes, Inc.*, 484 F. Supp. 2d 694, 706 (W.D. Mich. 2007) ("[T]he status of an insurer as a fiduciary is not automatic but rather turns upon the provisions of the plan and of the agreement made by the insurer."); *Austin v. Gen. Am. Life Ins. Co.*, 498 F. Supp. 844, 846 (N.D. Ala. 1980) ("[A] stockbroker may clearly be deemed a fiduciary under the alternative test set forth in section 2510.3–21(c)(ii) (B) of the regulation."). Indeed, after ERISA was passed, insurers requested an exemption in order to receive commissions in connection with sales of insurance products, *see* PTE 77-9, 41 Fed. Reg. 56760 (Dec. 29, 1976) (precursor to PTE 84-24), asking, in particular, that "normal sales presentations" and "recommendations" not be considered investment advice under the 1975 regulation. DOL declined, explaining that determinations would need to be made on a case-by-case basis. *Id.* at 56762.

rendered "for" a fee or other compensation. 29 U.S.C. § 1002(21)(A). Thus, even using Plaintiffs' definition, commissions fall under the statute, because brokers and agents undoubtedly give advice "for" the purpose of earning commissions. Further, Plaintiffs' reading would impose a non-statutory limitation—that compensation be "solely" for investment advice—in contravention of Congress's intent to apply fiduciary status broadly and would construe narrowly a definition courts have said should be construed liberally. *See* Defs.' Br. 30 & n.28; *Am. Fed'n of Unions Local 102 Health & Welfare Fund v. Equitable Life Assurance Soc'y,* 841 F.2d 658, 663 (5th Cir. 1988) (giving "fiduciary" "a liberal construction in keeping with the remedial purpose of ERISA"). A natural reading supports DOL's interpretation that a person or affiliated entity must simply receive some form of compensation in connection with or as a result of an investment transaction or service. 29 C.F.R. § 2510.3-21(g)(3);[8] *see Ellis*, 484 F. Supp. 2d at 710 ("the statute … requires only a 'fee or other compensation, direct or indirect,' in exchange for investment advice").[9]

Nor does the case law support Plaintiffs' reading. Indeed, at least three cases have explicitly rejected Plaintiffs' argument while confirming DOL's interpretation that "a fee or other compensation, direct or indirect" encompasses brokerage, mutual fund, and insurance sales commissions. *See* Defs.' Br. 35. Plaintiffs attempt to minimize these cases by contending that they do "not grapple with the textual requirement that it is 'advice' that must be provided 'for a fee or other compensation'" or are "not on point." Ch. Opp'n 11 n.9. That is incorrect. In *Thomas, Head & Greisen Employees Tr. v. Buster*, 24 F.3d 1114 (9th Cir. 1994), the defendant specifically argued that his sales commissions "were not fees for investment advice, but rather represent[ed]

[8] Such a reading is consistent with common definitions of "for." *See The Random House Dictionary of the English Language* (2d ed. 1987) ("in consideration or payment of; in return for"; "in exchange for").

[9] Plaintiffs mischaracterize DOL's position as being that the term "indirect" refers to "the advice's role in generating the fee." Ch. Opp'n 12. Commissions are "indirect" compensation for investment advice where they are paid by firms, not by the investor. *See* Defs.' Br. 34-37. DOL's position that these commissions constitute compensation *for rendering investment advice* is based on the fact that the text does not require compensation to be solely, or even principally, for investment advice, as well as the practical reality, acknowledged by ACLI and other commenters, that sales and investment advice go hand-in-hand, such that commissions are often paid, at least in part, for the investment advice given in the course of selling investment products. *See id.* 36-37, 37 n.36; *see also Ellis*, 484 F. Supp. 2d at 714 (noting that "the line between sales activity on the one hand and advice on the other may be indistinct").

the profit earned by a salesperson." *Id.* at 1120. The Ninth Circuit rejected that interpretation, cautioning that it would "not permit a fiduciary to avoid his responsibilities merely by structuring a financial transaction so as to achieve that goal." *Id.* Likewise, the court in *Ellis* found it "clear that [the defendant] received a fee or other compensation, direct or indirect, for its investment advice within the meaning of ... ERISA." 484 F. Supp. 2d at 710; *id.* (defendant "received a commission at the time each security was purchased, as well as a number of other fees during the life of the relationship"). Reading the statute to "require[] only" that the compensation be "in exchange for investment advice," the court found "untenable" defendant's characterization of his fees "as commissions for sales, not a fee for investment advice." *Id.* And *Brock v. Self*, 632 F. Supp. 1509 (W.D. La. 1986), directly contradicts Plaintiffs' position that compensation must be paid solely for investment advice to qualify as fiduciary investment advice. Despite the fact that there was "no direct evidence … [of] receiving monies or charging a fee for investment advice," the court there found that the third-party defendants "were at least indirectly compensated for the investment advice … they rendered" where "such advice was rendered as part of the package deal." *Id.* at 1520 n.11. Plaintiffs' authority is unavailing as neither of the cases they cite addressed whether commissions qualify as a "fee or other compensation, direct or indirect" under ERISA. *See* Ch. Opp'n 9. And one confirms that the fiduciary definition's second 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." *Farm King Supply, Inc. Integrated Profit Sharing Plan & Tr. v. Edward D. Jones & Co.*, 884 F.2d 288, 293 (7th Cir. 1989). The case law thus belies Plaintiffs' interpretation.[10]

Plaintiffs' continued reliance on the Advisers Act, *see* Ch. Opp'n 12-14, is also unavailing,

[10] Plaintiffs misuse the court's statement in *Am. Fed'n of Unions* that "[s]imply urging the purchase of [the company's] products does not make an insurance company an ERISA fiduciary with respect to those products." Ch. Opp'n 9 & n.7 (quoting 841 F.2d at 664). As explained, *see* Defs.' Br. 36 n.35, the court made this statement in the context of rejecting the company's fiduciary status because it did not meet the requirements of the 1975 regulation's five-part test. *See* 841 F.2d at 664. This statement in no way supports Plaintiffs' position that "a fee or other compensation, direct or indirect" does not include sales commissions, an issue the court did not address.

as DOL has shown that the Act's definition of an investment adviser has no bearing on the appropriate interpretation of ERISA's fiduciary definition. *See* Defs.' Br. 37-38, 45-46.[11] Plaintiffs contend that the distinction in the Advisers Act between fiduciary investment advice and sales performed by broker-dealers was so "clear and long-standing" that "Congress did not need to" explicitly adopt it in ERISA. *Id.* But Plaintiffs' bare assertion that Congress borrowed this distinction in ERISA *sub silentio*, without any reference to the Advisers Act in the fiduciary definition or any indication in the statutory text, is insufficient to overcome the presumption that "where words differ …, Congress acts intentionally and purposefully in the disparate inclusion or exclusion." *Burlington N. & Santa Fe Ry. Co. v. White*, 548 U.S. 53, 62-63 (2006).[12]

Plaintiffs also cannot garner support for their position that sales and advice are distinct from the Rule's exclusion from the fiduciary definition transactions involving sophisticated plans with at least $50 million in assets. AR54. Plaintiffs make much of DOL's choice not to apply this exclusion where the person giving investment advice receives compensation directly from the plan "for the provision of investment advice (as opposed to other services)." Ch. Opp'n 11. But DOL's choice is not focused on sales; it merely serves to ensure that a person does not charge a plan a direct fee for advice and then disclaim fiduciary responsibility. The fact that DOL chose to apply the full scope of the statutory definition where a plan "*expressly* pays a fee for advice," AR38, does not mean that a discrete payment for advice is *required* by the statutory text. *See* AR43-44.

Further, Plaintiffs' own statements, and others from industry, foreclose Plaintiffs' assertion

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[11] Plaintiffs largely abandon their congressional ratification argument, and their tepid assertion that "the sum of congressional actions … demonstrates that Congress expects retirement investors to be serviced by [those] paid on a commission basis," Ch. Opp'n 14 n.10, is a far cry from meeting the standard to demonstrate congressional ratification of the 1975 regulation. *See* Defs.' Br. 38-39. Moreover, the rulemaking does not prohibit commissions, as Plaintiffs continue to suggest, *see* Ch. Opp'n 13-14, but was crafted to allow for them. *See* Defs.' Br. 37-38.

[12] Moreover, whether the Advisers Act recognized a distinction between commissions and separate advice fees, as Plaintiffs suggest, *see* Ch. Opp'n 10 (citing *Fin. Planning Ass'n v. SEC*, 482 F.3d 481, 485 (D.C. Cir. 2007)), is irrelevant here where Congress applied fiduciary status broadly in ERISA to anyone who "renders investment advice for a fee or other compensation, direct or indirect," without distinguishing or otherwise limiting the type of compensation required for fiduciary status. The definition of an investment adviser in the Advisers Act is not parallel to the language in ERISA, in particular on this point, as it refers to "compensation" but does not include the clause in ERISA that compensation can be "direct or indirect." *See* 15 U.S.C. § 80b-2(a)(11).

that "[a] broker-dealer or insurance agent is not compensated for 'advice.'" Ch. Opp'n 9. As DOL explained, Defs.' Br. 36, ACLI concedes as much, asserting during the rulemaking process and in this litigation, that the advisory role brokers and insurance agents play in "help[ing] consumers assess … which type of annuity and optional features suit consumers' financial circumstances" justifies their customary compensation rates. ACLI Br. 4-5, ECF No. 62; *see also* AR39731 (Cmt. 621, ACLI). And ACLI is not alone. Advisors Excel, a nationwide IMO, justified insurers' upfront commissions based on "the amount of work a producer [i.e., insurance agent] devotes to working with a client, explaining options and product features, undertaking the state-required suitability analysis and working on his or her client's behalf to help make the best financial decisions possible." AR51885 (Exemption Cmt. 333). While Plaintiffs attempt to ignore these statements, *see generally* Ch. Opp'n 2-16, they cannot escape what the industry's statements demonstrate: that brokers and agents are compensated for rendering investment advice.

Plaintiffs attempt to avoid this reality by noting that brokers and agent receive commissions only in the event of a sale, "no matter how meticulously the salesperson may have 'advised' the consumer." Ch. Opp'n 10. But the fact that a broker or agent may not be compensated unless he or she finalizes a sale does not mean that the commission paid is not, at least in part, compensation for investment advice rendered during the course of the sale. Plaintiffs' position—that commissions are paid for sales and not the investment advice rendered during the course of a sale, no matter how meticulous the advice, *see id.*—would appear to insulate from fiduciary status brokers and agents who are paid by commissions at the very time consumers are most in need of protection: when they actually follow through on the advice and invest their retirement savings.[13] This anomalous result is at odds with ERISA's purpose to protect retirement investors from

[13] Plaintiffs also attempt to support their position that commissions are paid for sales, and not investment advice, by noting that "a broker will receive a full commission once a sale is made even if she makes only a fleeting 'recommendation' or none at all." Ch. Opp'n 10. But where a broker does not make a recommendation that rises to the level of "a call to action that a reasonable person would believe was a suggestion to make or hold a particular investment or pursue a particular investment strategy … with regard to investment property," the broker will not qualify as an investment advice fiduciary under the Rule. AR27; *see also* Defs.' Br. 34-35.

conflicts of interest that could harm their retirement security and is itself unreasonable.

At bottom, Plaintiffs urge the Court to adopt a seller's carve-out that the agency specifically rejected as contrary to ERISA's purposes, *see* Defs.' Br. 37 n.36; AR35-36, and to exempt brokers and agents from fiduciary status based on their use of the customary forms of compensation that DOL crafted the rulemaking to permit at the industry's request, *see* AR858, 934. But a fiduciary should not be permitted "to avoid his responsibilities merely by structuring a financial transaction so as to achieve that goal." *Thomas, Head*, 24 F.3d at 1120. Where the statute's functional definition does not turn on whether an individual is a broker or insurance agent and speaks in broad but general terms of compensation, there is no basis upon which Plaintiffs can do so.

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

Plaintiffs next argue that DOL exceeded its statutory authority by requiring fiduciaries who engage in conflicted transactions to adhere to impartial conduct standards. Ch. Opp'n 16. To succeed on their claim, Plaintiffs must show that DOL's determination to do so is "arbitrary and capricious." *AFL-CIO v. Donovan*, 757 F.2d 330, 343 (D.C. Cir. 1985). Because the impartial conduct standards require such fiduciaries to give advice that is "in the Best Interest of the Retirement Investor," AR140—in perfect keeping with the statutory requirement that exemptions be "in the interests of" retirement investors, 26 U.S.C. § 4975(c)(2)—Plaintiffs cannot do so.

The weakness of Plaintiffs' position is evidenced by their reliance on *MCI Telecomms. Corp. v. Am. Tele. & Tele. Co.*, 512 U.S. 218 (1994). *See* Ch. Opp'n 16. There, the Court held that the agency exceeded its statutory authority to "modify" rate-filing requirements where it "eliminate[ed]" the requirements for 40% of the industry altogether. *MCI*, 512 U.S. at 232. The agency's interpretation was at odds with the statutory text, which every dictionary, save one, defined in terms of incremental or limited change—not complete elimination. *Id.* at 226.

Plaintiffs argue that as in *MCI*, "DOL has acted to fundamentally transform the Code through the BICE." Ch. Opp'n 17. But unlike in *MCI*, where the agency acted contrary to the

statutory text, DOL, in requiring adherence to a best interest standard, acted in concert with it. *Compare* BIC Exemption § IX(d)(1)(i) (requiring advice "in the Best Interest of the Retirement Investor"), *with* 26 U.S.C. § 4975(c)(2) (allowing exemptions only if "in the interests of" retirement investors). And Plaintiffs' assertion that the BIC Exemption "fundamentally transform[s] the Code," cannot be squared with their concessions that the Code's "broadly-worded statutory requirements," authorize DOL to grant "conditional" exemptions. Ch. Opp'n 17-18.

Plaintiffs' argument that the BIC Exemption "is contrary to the Code," *id.*, boils down to their view that because Congress did not impose the duties of prudence and loyalty on fiduciaries to IRAs, DOL cannot require adherence to those same duties as a condition of exemptive relief when fiduciaries to IRAs seek to engage in conflicted transactions. *See id.* Plaintiffs are not comparing apples to apples. DOL did not impose fiduciary duties on fiduciaries to IRAs by virtue of their qualifying as fiduciaries. *See* Defs.' Br. 49-50. There is therefore no inconsistency between the legislative choice in Title I and DOL's treatment of fiduciaries to IRAs under Title II. *See id.* Moreover, by prohibiting conflicted transactions for fiduciaries, Congress created a "no conflict" default and gave DOL the authority to determine under what conditions a fiduciary could be relieved from that default rule while continuing to protect retirement investors in the course of such conflicted transactions. *See* 26 U.S.C. § 4975(c). Thus, DOL did not require adherence to fiduciary duties in the face of congressional silence, as Plaintiffs suggest, but in exercise of Congress's "broadly-worded," Ch. Opp'n 16, authorization to grant exemptions that serve the interests, and protect the rights, of retirement investors. *See* Defs.' Br. 49-50; 26 U.S.C. § 4975(c). That Congress employed those same duties to protect investors in Title I plans supports DOL's finding that conditioning exemptions on adherence to such duties meets the statutory requirements.

In resisting that conclusion, Plaintiffs contend that "there is no discernible stopping point to the discretionary judgments DOL claims to be empowered to make." Ch. Opp'n 20. But the discretionary decision DOL made was merely to require those who seek to engage in transactions that would otherwise be statutorily prohibited to adhere to "baseline standards of fundamental fair

dealing" and to commit to abide by those standards in an enforceable agreement. AR116. Congress expressly gave DOL that discretionary authority, subject only to "three broadly-worded statutory requirements." Ch. Opp'n 16. And principles of administrative law dictate that DOL's determination pursuant to that authority is entitled to deference unless it is arbitrary and capricious. *Am. Trucking Assocs. v. ICC*, 656 F.2d 1115, 1127 (5th Cir. 1981) (in reviewing agency's exemption decision, the court's "task" is to determine whether that decision was "arbitrary and capricious"). Plaintiffs' mere disagreement with the authority Congress gave to DOL, or the way in which DOL exercised that authority, is not a legal basis for overturning DOL's reasoned decision to require those who engage in conflicted transactions to give advice in the best interest of retirement investors when that decision is grounded in the statutory text.

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"

In exercising its authority to craft a "conditional ... exemption," DOL determined that specifying minimum contract terms for conflicted IRA transactions was important to satisfy the statutory requirement that the exemption be "administratively feasible" for the agency, and in the "interests of" and "protective of the rights of" retirement investors. 29 U.S.C. § 1108(a); 26 U.S.C. § 4975(c); *see* AR116, 195. These conclusions are entitled to "great deference," *AFL-CIO*, 757 F.2d at 343, and neither of Plaintiffs' theories is sufficient to overcome that deferential standard.

First, Plaintiffs' attempt to extend *Alexander v. Sandoval*, 532 U.S. 275 (2001), is unavailing because *Sandoval* and its progeny stand for the proposition that a private cause of action may be inferred by a court only upon a showing of congressional intent. *See Sandoval*, 532 U.S. at 286. But DOL has not created a private cause of action; instead, it has specified terms for contracts enforceable under existing state law. AR195; Defs.' Br. 52-54. Plaintiffs acknowledge that IRA transactions are already subject to state contract claims, *see, e.g.*, AR46171 (Cmt. 3050, ACLI), and do not cite any case in which the *Sandoval* line of cases has been applied to limit an agency's express authority to craft conditions for exemptions. There is nothing improper about

"writing federal regulatory requirements into privately-enforceable contracts." Ch. Reply 21. Indeed, agencies specify terms for private contracts with some regularity. Defs.' Br. 55 & n.56.[14]

Plaintiffs cobble together cases rejecting efforts by individuals to enforce agency contracts to which they are not parties[15] and to directly enforce federal law in the guise of contract claims.[16] Here, because only enforcement by contracting parties is at issue, little can be learned from cases dealing with unique considerations related to enforcement of contracts by third parties. *See Astra USA*, 563 U.S. at 119 n.4.[17] Nor are the contract claims here merely disguised attempts to enforce federal statutes. *Cf. Umland*, 542 F.3d at 67 (refusing to "read FICA's provisions into every employment contract"); *Astra USA*, 563 U.S. at 118 (agreements at issue "simply incorporate statutory obligations"). Instead, *Astra USA* suggests the contract terms here—as an exercise of agency discretion rather than repetition of statutory requirements, AR16, 195—are appropriate. *See* 563 U.S. at 118 (suggesting *Sandoval* might not prohibit suits involving violations of an "independent substantive obligation arising only" from the contract not from the statute). As the Fifth Circuit has recognized, that federal law plays a role in liability does not create a federal cause

[14] Plaintiffs seek to distinguish DOL's examples of other regulations on various grounds, including that they "concerned conduct that the agencies were authorized to regulate directly, whereas here DOL uses a contract to institute standards that it cannot directly impose." Ch. Reply 24. This is no distinction because DOL does have direct authority to impose the standards as conditions of the exemption—even without a contract. *See supra* Arg. § II, V(B).

[15] *See Astra USA, Inc. v. Santa Clara Cty.,* 563 U.S. 110, 118 (2011) (rejecting a "third-party suit to enforce an HHS-drug manufacturer agreement"); *Grochowski v. Phoenix Constr.*, 318 F.3d 80, 85 (2d Cir. 2003) (rejecting "state-law claims for breach of contract as third party beneficiaries of the contracts"); *see also MM&S Fin., Inc. v. Nat'l Ass'n of Secs. Dealers, Inc.*, 364 F.3d 908, 910 (8th Cir. 2004) (rejecting challenge to industry self-regulator's acceptance of arbitration claims, relying on another third-party beneficiary case, *Niss v. Nat'l Ass'n of Secs. Dealers, Inc.*, 989 F. Supp. 1302, 1308 (S.D. Cal. 1997)).

[16] *See Astra USA*, 563 U.S. at 118 (claim at issue "is in essence a suit to enforce the statute itself"); *Umland v. PLANCO Fin. Servs., Inc.*, 542 F.3d 59, 66-67 (3d Cir. 2008) (rejecting employee's attempt to challenge her employer's Social Security tax withholdings by interpreting the federal statute, 26 U.S.C. § 3111, as an implied term of her employment contract); *MM&S Fin.*, 364 F.3d at 910 (rejecting "[a]ny attempt ... to bypass the Exchange Act by asserting a private breach of contract claim for violations of [15 U.S.C. §] 78s(g)(1)" where Exchange Act provided exclusive jurisdiction for breach of duties created by that Act); *Grochowski*, 318 F.3d at 86 ("At bottom, the plaintiffs' state-law claims are indirect attempts at privately enforcing ... the [Davis-Bacon Act].").

[17] "Whether a contracting agency may authorize third-party suits to enforce a Government contract is not at issue in this case. We can infer no such authorization where a contract ... fails to demonstrate any intent to allow beneficiaries to en-force those terms." *Id.* Intent of the contracting parties is the key question. *See Palma v. Verex Assurance, Inc.*, 79 F.3d 1453, 1457 (5th Cir. 1996); *Davis v. United Air Lines, Inc.,* 575 F. Supp. 677, 680 (E.D.N.Y. 1983).

of action problem. *See Lowe v. Gen. Motors Corp.*, 624 F.2d 1373, 1379 (5th Cir. 1980).

Plaintiffs' second theory also fails. While they claim that it is arbitrary and capricious for the exemption conditions to involve "new consequences," Ch. Reply 18, 23, it is hard to imagine conditions that DOL could impose as part of an exemption for financial transactions that would not have potential liability implications under other laws. For example, even Plaintiffs' preferred approach of requiring specified disclosures would implicate claims under the securities laws (which are disclosure-based regimes) and potentially under state insurance and consumer protection laws. Moreover, in claiming agencies may specify a contract term only if it "creates no new legal exposure," Ch. Reply 24, Plaintiffs do not respond to DOL's explanation of the only two cases they cite in support of this theory. *See* Defs.' Br. 53. DOL has shown that its specification of minimum contract terms falls within its authority, *id.* 54-55, and is directly tied to the statutory criteria and circumstances on which the exemption is based. *See* AR78, 89, 97, 116.[18]

It is reasonable for DOL to condition an exemption for inherently conflicted transactions on an "up-front commitment to act as a fiduciary." AR605. The BIC Exemption addresses advice in the "retail market"—*i.e.*, when the adviser is dealing directly with retirement investors. BIC Ex. §§ I(b), VIII(o) (AR132, 140); *see also* AR59, 68-70. In that context, some of the conditions DOL traditionally uses to protect the investor are unavailable. For example, as explained in agency testimony sixteen years ago (highlighted by Plaintiffs for other purposes), DOL "typically require[s] the utilization of independent fiduciaries to represent the interests of plans in transactions in which the plan's ... fiduciaries have interests that may conflict with their fiduciary duties." ECF No. 73 at 42; *see, e.g.*, 71 Fed. Reg. 5887, 5889 (Feb. 3, 2006) (PTE 84-24 § V(b) requiring independent fiduciary with no stake in transaction to approve the conflicted transaction). But where the adviser is dealing directly with retirement investors, no disinterested fiduciary of the investor is generally available to sign off on a transaction. AR341-42, 376, 380. Accordingly,

[18] Plaintiffs attempt to buttress their argument by claiming that they have no choice but to employ the BIC Exemption. Ch. Reply 18, 25. This is incorrect because it is possible to provide investment advice without conflicted compensation. *See infra* Arg. § VI. It is also irrelevant to the *Sandoval* and authority claim.

DOL imposed conditions on the relevant financial institution and adviser that would be sufficient to ameliorate the conflict of interest. *See, e.g.*, AR733. Among these conditions are contractual commitments designed to incentivize the financial institution and adviser to "carefully police conflicts of interest to ensure that the conflicts ... do not taint the advice." AR368; *see also* AR78.

DOL found the "contract provides an administrable way of ensuring adherence" to broad protective standards that can be applied across the industry, which freed DOL from adopting "highly prescriptive conditions applicable only to tightly-specified investments and compensation structures." AR78; *see also* AR89, 97, 116. Plaintiffs do not dispute that the possibility of liability is a "significant deterrent." AR116. And the contractual commitment is appropriately limited to its exemptive purpose. It is required only to enter an otherwise prohibited transaction. *See* AR88 ("compliance with the exemption's conditions is necessary only with respect to transactions that otherwise would constitute prohibited transactions"). And because the relevant transactions already involve private contracts, augmentation of those contracts with additional minimum terms is a common sense and reasonable approach. *See* Defs.' Br. 52-54. Accordingly, the BIC Exemption's contract requirement is a measured application of all three prongs of the statutory standard for exemptions. *See* 29 U.S.C. § 1108(a); 26 U.S.C. § 4975(c)(2).

IV. DOL'S COST BENEFIT ANALYSIS SUPPORTS ITS RULEMAKING

DOL has demonstrated that it 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 and justifies the rulemaking. Defs.' Br. 57-69. It "pa[id] attention to the advantages and the disadvantages" of the rulemaking, *Michigan v. EPA*, 135 S. Ct. 2699 (2015), and amply satisfied the APA by providing a "rational explanation for how the [agency] reached its decision." *Associated Builders & Contractors of Tex., Inc. v. NLRB*, 826 F.3d 215, 225 (5th Cir. 2016). By contrast, Plaintiffs have not carried their burden to demonstrate that DOL "entirely failed to consider an important aspect of the problem." *Markle Interests, LLC. v. U.S. Fish & Wildlife Serv.*, 827 F.3d 452, 460 (5th Cir. 2016).

In reply, Plaintiffs do not directly challenge DOL's demonstration that it relied on substantial evidence in concluding that the rulemaking would confer substantial benefits on retirement investors by mitigating conflicts of interest in retirement investment advice. *See* Defs.' Br. 57-60. Nor do they continue to press their misguided attempt to have the Court consider the quantitative evidence in isolation rather than looking at the costs and benefits as a whole. *See id.* 63-66. The five arguments they do press are not meritorious.

First, Plaintiffs argue that DOL failed to appropriately consider "negative effects on savers with limited means." Ch. Reply 26-27. DOL demonstrated that it carefully examined this issue and concluded that advisory services would remain "amply available to small plans and investors." Defs.' Br. 61-62 (quoting AR628); AR69-70, 628-34. Chamber disputes DOL's conclusion that a claim about the benefits provided by brokers in a July 2015 comment lacks empirical support. Ch. Reply 27. DOL explained that this comment's underlying analysis was hypothetical not empirical and suffered from other problems. AR632-34 & n.601; Defs.' Br. 63. While Plaintiffs may disagree with DOL's conclusion, they cannot argue that DOL failed to consider it.[19] *See Marathon Oil Co. v. EPA*, 830 F.2d 1346, 1355 (5th Cir. 1987) (upholding agency action where it could "readily discern" that agency "considered and rejected the mixing zones methodologies proposed by [plaintiff]"); *Alamo Express, Inc. v. ICC*, 673 F.2d 852, 859 (5th Cir. 1982) (holding that it "is not the function of this court to reweigh the evidence" where agency "considered [plaintiff's] evidence and found it unpersuasive").

Second, in light of DOL's demonstration that it did consider the cost of class action litigation, Defs.' Br. 61; AR555-58, Plaintiffs' allegations have narrowed to three details—that firms may be less able to mitigate litigation costs by requiring arbitration and prohibiting class actions, the cost of settling meritless class actions, and that fear of liability might lead firms to

[19] Chamber also introduces two recent articles about two firms' choices allegedly driven by the rulemaking. *See* Ch. Reply 27 n.19. The investment advice industry is dynamic and even before the rulemaking, market participants have been entering and leaving various portions of the market. *See* AR625; AR67048-49. These choices by two firms do not undermine DOL's conclusion that small savers will have ample access to advice.

provide fewer services. Ch. Reply. 27. But the increased fiduciary liability insurance premiums that DOL quantified may include the cost of settling cases. *See* AR555-58. And Plaintiffs overstate the extent to which the availability of class actions creates novel issues—at least for all transactions within FINRA's scope, the BIC Exemption's class action provision does not change the status quo. *See* AR98; *see also infra* Arg. § VI (discussing FINRA Rule). DOL concluded that class actions provide a net benefit by ensuring that there would be a remedy for particularly egregious wrongs and incentivizing good conduct. AR99. DOL's consideration satisfies the APA. *See, e.g.*, *ConocoPhillips Co. v. EPA*, 612 F.3d 822, 840 (5th Cir. 2010) ("under the 'highly deferential' standard of review mandated here, we are unpersuaded that the EPA's failure to estimate benefits for specific new facility locations renders the process arbitrary or capricious").

Third, DOL explained that Plaintiffs' claim that the value of advice to consumers should be added to the ledger as a cost is mistaken because the agency reasonably concluded that the rulemaking would not reduce consumers' access to advice. Defs.' Br. 62; AR131, 623-27. Without attempting to refute DOL's showing, Chamber continues to press DOL's alleged inconsistency with its 2011 cost benefit analysis in implementing a statutory exemption. Ch. Reply 27. This notion is both irrelevant and incorrect as previously discussed. Defs.' Br. 63. *See Davis Mountain Trans-Pecos Heritage Ass'n v. FAA*, 116 F. App'x 3, 15 (5th Cir. 2004) (holding that where agency reached "non-arbitrary conclusion that adverse effects ... were unlikely," the agency's "limited discussion of measures to mitigate those effects [was] reasonable").

Fourth, Plaintiffs claim that DOL failed to consider the cost to independent marketing organizations ("IMOs") and agents selling FIAs. DOL concluded that "distributors of insurance products" could comply with the BIC Exemption, AR599; Defs.' Br. 86-87. And DOL's estimate of compliance cost for insurers—based on the financial industry's own estimates—inherently included costs for insurers to help other entities in the market comply or if insurers did not fill this role, the costs incurred by those entities that would fill that role. *See, e.g.*, AR599. Accordingly, costs for the independent distribution channel to comply are included in the estimate of insurer

costs. Since each aspect of the industry can be expected to adopt a cost-efficient distribution model, costs for the independent channel should not significantly exceed the calculated costs to insurers. AR622. Regardless, DOL need not quantify costs for which it does not have reliable data, Defs.' Br. 68 n.68, and DOL reasonably concluded in light of all the evidence that the benefit to annuity investors outweighed the costs of the rulemaking. *See* AR602. *Cf. Nat'l Propane Gas Ass'n v. U.S. Dep't of Transp.*, 43 F. Supp. 2d 665, 677 (N.D. Tex. 1999) ("The court will not substitute its judgment for that of the agency, especially when the agency is called upon to weigh the costs and benefits of alternative policies, since such cost-benefit analyses epitomize the types of decisions that are most appropriately entrusted to the expertise of an agency.").

Finally, Plaintiffs claim that DOL failed to account for the alleged harm to consumers from decreased access to variable annuities and FIAs. ACLI Reply 17-20; IALC Reply 17-18. As DOL has demonstrated, the premise that access to these annuities will decrease is simply mistaken. Defs.' Br. 67-68.[20] The rulemaking does not decrease *access* to any class of product, but rather appropriately protects the interests of retirement investors by requiring all classes of products to meet objective standards. AR63. As DOL explained, its rulemaking aims to ferret out mismatched recommendations of products that are not in the investors' best interest. Defs.' Br. 68; AR627-28. Even if the rulemaking may result in decreased *recommendations* of certain products or even classes of products that cannot objectively meet the impartial conduct standards, a drop in recommendations is not equivalent to a loss of access. *Id.*; AR64-65.[21]

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[20] Similarly, IALC points to only one record source for the notion that the BIC Exemption would raise the cost of FIAs. IALC Reply 17 (citing Cmt. 785, Americans for Annuity Protection). The comment, which merely asserts that requiring insurance agents to *live up to fiduciary duties* would increase costs, *see* AR42626, does not support the point.

[21] ACLI speculates that "different liability exposure" will "drive sellers to recommend fixed rate annuities over" other annuities. ACLI Reply 18-19. ACLI is arguing that the adviser will act on a conflict, steering customers to products with lesser consumer protections in order to avoid perceived liability exposure. If true, this problem would be worse if FIAs were to be covered by PTE 84-24, since, in that case, advisers presumably would steer customers to FIAs rather than to mutual funds. *See* AR74, 234, 237-78 (excluding FIAs from PTE 84-24 in part to prevent such harmful self-dealing). And DOL concluded that investors will continue to have access to lifetime income products and the market will determine which products are most successful. AR232, 624.

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

In the face of Plaintiffs' claim that the rulemaking "remarkably ... devotes very little attention to annuities," ACLI Reply 14, DOL has demonstrated that it considered the relevant issues and explained the reasons for its treatment of annuities in the BIC Exemption and PTE 84-24. Defs.' Br. 69-92. Accordingly, DOL has exceeded the "minimal level of analysis" required to satisfy the APA by providing an "explanation ... clear enough that its path may reasonably be discerned." *Encino Motorcars, LLC v. Navarro*, 136 S. Ct. 2117, 2125 (2016).

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

DOL explained its reasons for covering variable annuities and FIAs in the BIC Exemption, both in the rulemaking and its brief. Defs.' Br. 70-74. ACLI largely abandons this line of reasoning as to variable annuities. IALC, however, persists in challenging DOL's disposition of FIAs. IALC Reply 18-20. DOL rationally determined, after reviewing all the evidence, that FIAs should be treated like variable annuities and most other products when conflicted fiduciary investment advisers recommend FIAs to retirement investors—due to FIAs' complexity, AR73-74, 325, 435, 439-42, 454-56, 598, 600, greater risk, AR73-74, 439, 447, 600,[22] opaque compensation, AR325, 437, 441-42, 458, inconsistent regulation, AR74-75, 355, 357-59, 601, and the need for a level playing field with variable annuities and mutual funds. AR74, 237-38, 434. Taken together, these considerations amply justify applying the additional protections and structural safeguards for the investors found in the BIC Exemption. Defs.' Br. 71-73.

IALC's separate argument that FIAs and declared rate annuities are functionally "identical," IALC Br. 28, is defeated by the parties' agreement that the method for crediting gains

[22] While declared rate annuities bear the risk that gains will not keep up with inflation or with other investment options, IALC Reply 19, that does not make risk a meaningless or irrelevant consideration for DOL when determining the appropriate exemption to apply. In the context of advisory conflicts of interest, it is relevant how likely the retail investor is to understand the relevant risk or instead by at the mercy of the adviser. Here, for example, declared rate annuity gains almost never fall to zero for a year, while FIA gains typically will be zero in years where the relevant index declines. *Cf.* AR439. So, the risk of gains lagging inflation or the available risk-free rate is larger for FIAs than for declared rate annuities.

is the primary distinguishing feature between the products. *Id.* 29; Defs.' Br. 73. As DOL explained, the crediting method for FIAs introduces several levels of complexity—the choice of an index,[23] the choice of a formula to determine how gains are measured,[24] and the fact that insurers use several different methods to limit how much of the gains are credited.[25] Defs.' Br. 10, 73; AR435, 439-40, 600. This complexity amplifies the potential harms from inherent conflicts of interest in the annuity market by making the investor more "acutely dependent" on the adviser because the costs and risks of such investments are harder to assess, AR439, and provides a sufficient basis, standing alone, to distinguish FIAs from declared rate annuities. Defs.' Br. 73-74.[26] Moreover, there are other relevant differences between the products, including higher commissions on FIAs, AR46849, 46851, and offering complex guaranteed living benefit riders that carry additional fees and commissions, AR442, AR67023. Defs.' Br. 74. Accordingly, DOL's distinction between the products is far from arbitrary.

Next IALC argues that DOL has not justified the need for the "incremental requirements of the BIC exemption, over and above the protections of the enhanced 84-24 exemption and state law" for FIA transactions. IALC Reply 14-15. In fact, numerous considerations are woven throughout DOL's rulemaking record. For example, while higher commissions may be justified in certain circumstances, AR618, they provide incentives for conflicted fiduciary advisers to recommend certain products over others. AR436-38, 447-50. The BIC Exemption, by requiring the insurer and its affiliates to adopt procedures to mitigate improper incentives, becomes more

[23] Although a majority of FIAs use the S&P 500, other indices have been gaining ground, with many branching out into hybrid indices or nontraditional ones such as volatility control or gold. *See* AR439; AR66940.

[24] There are several methods for determining changes to the index, such as point-to-point, annual reset, and high or low watermarks, each of which come with trade-offs the investor needs to understand. *See* AR439 & n.298.

[25] Insurers use at least three different methods to offset their risk from period to period, cover expenses (including commissions), and earn a profit—caps, participation rates, and spreads. *See* AR439, 237-38, 600; AR33656-57.

[26] Unlike the totality of the circumstances analysis at issue in *PDK Labs. Inc. v. DEA*, 362 F.3d 786, 799 (D.C. Cir. 2004), DOL's rulemaking clearly demonstrates that relative complexity was the key distinction between the products. AR600; *see also* AR74, 234. Accordingly, IALC's quibbling with some of the other factors DOL considered is not sufficient to invalidate the rulemaking. *See PDK Labs.*, 362 F.3d at 799 (remand inappropriate if agency's "mistake did not affect the outcome").

essential the higher the commissions and the more complex the products. Similarly, the greater the investor's need to lean advisers' recommendations, the more it is incumbent that advisers have a "powerful incentive" to follow the impartial conduct standards. AR447. Thus, contrary to Plaintiffs' assertion, DOL has sufficiently explained why it placed FIAs in the BIC Exemption.

Finally, Plaintiffs are wrong to suggest that an agency needs to justify every consequence of a rulemaking. *See San Luis & Delta-Mendota Water Auth. v. Jewell*, 747 F.3d 581 (9th Cir. 2014) ("We do not require agencies to analyze every potential consequence of every choice they make[.]"). Even if one consequence of placing other annuities in the BIC Exemption was to "creat[e] a regulatory incentive" to recommend declared rate annuities, IALC Reply 19-20, that is a mere byproduct of more important decisions—to ensure that variable annuity and FIA transactions are sufficiently protective (and a level playing field among those annuities and mutual funds) and to ensure access to guaranteed retirement income by preserving PTE 84-24 for simpler, more understandable declared rate annuities. *See* AR74, 234, 237-38. It is enough that DOL was aware of this possible consequence but considered other factors more important. *See Teledesic LLC v. FCC*, 275 F.3d 75, 86 (D.C. Cir. 2001) (rejecting argument that agency discriminated in favor of incumbents because the result was "the legitimate byproduct" of an important process).

B. DOL's Rulemaking Appropriately Treats Classes of Products Differently Due to Different Degrees of Conflicts of Interest

ACLI has not shown that DOL lacks authority to treat classes of products differently. It complains that DOL grouped variable annuities and FIAs with almost all other retirement investment products while leaving a narrow exemption available for declared rate annuities. ACLI Reply 24. Hyperbole about a "radical market intervention" and an "attempt to engineer the market for retirement products," *id.*, do not undermine the fact that DOL has authority to grant exemptions at a level as granular as a single transaction. *See* 29 U.S.C. § 1108(a). While DOL could have entirely revoked PTE 84-24, it adequately explained its reasonable grounds for retaining it for declared rate annuities while making the BIC Exemption available for variable annuities and FIAs.

See Defs.' Br. 73-74. The APA requires no more. *See Markle Interests*, 827 F.3d at 460.

ACLI agrees that DOL can distinguish between products on the basis of conflicts of interest. ACLI Reply 25. DOL did precisely that. *See* Defs.' Br. 73-74. DOL explained how the complexity of variable annuities and FIAs heighten the conflicts of interest by making the investor highly dependent on the advice received. *See id.* But ACLI asks the Court to disregard that factor and instead rule that relative investment risk was an improper consideration. ACLI Reply 25. But risk is also correlated to conflicts of interest, especially where the potential for higher rewards is part of the sales pitch and investors may not be fully aware of the downside risks. *See* AR435, 441-42, 600. And here, it was a supporting, not dispositive factor. *See* Defs.' Br. 73-74.

ACLI's entire argument is built on the idea that DOL has tagged certain annuities as "disfavored products," ACLI Reply 24, even though these annuities are treated the same as almost all other products in the retirement investment market. DOL has explained that it is not targeting these annuities, but instead protecting retirement investors by encouraging advisory structures with fewer and better managed conflicts. Defs.' Br. 78; AR624. ACLI's focus on a few cherry-picked phrases out of context to speculate about the agency's intent does not undermine the reasonable distinctions DOL has amply demonstrated. *See* Defs.' Br. 77-78.[27]

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

Plaintiffs do not show that DOL failed to consider existing annuity regulation, but instead merely dispute the reasonableness of DOL's conclusions. As they acknowledge, DOL found that "notwithstanding existing [regulatory] protections, there is convincing evidence that advice conflicts are inflicting losses on IRA investors." AR426-27; ACLI Br. 32. Accordingly, DOL did examine "whether, under the existing regime, sufficient protections existed." *Am. Equity v. SEC*,

[27] Indeed, ACLI builds its argument around DOL's observation that PTE 84-24 will "promote access" to declared rate annuities, AR232, 238; *see* ACLI Reply 19, 24, but ignore the fact that the BIC Exemption too is designed to promote access to retirement investment products. *See, e.g.*, AR58 ("designed to promote the provision of investment advice that is in the best interest of retail investors"); AR68 ("This exemption is designed to promote the provision of investment advice to retail investors that is in their Best Interest and untainted by conflicts of interest.").

613 F.3d 166, 179 (D.C. Cir. 2010). Nevertheless, Plaintiffs ask the Court to second-guess DOL review of the evidence. That is not this Court's role. *Markle Interests*, 827 F.3d at 460.

As an initial matter, while IALC makes much of the Harkin Amendment, IALC Reply 13-14; Ch. Reply 29, it has little relevance here. Congress created a safe harbor directing the SEC to treat FIAs and other insurance or annuity contracts as exempt securities under the Securities Act of 1933 if the insurer met certain conditions, including NAIC's 2010 Model Suitability Regulation. *See* AR358; Pub. L. No. 111-203, § 989J, 124 Stat. 1376, 1949.[28] But this limited exemption from federal securities registration says nothing about ERISA. *See id.* It certainly is not, as Plaintiffs would have it, a Congressional determination that state regulation is sufficient to address fiduciary conflicts of interest. DOL used its broad regulatory power to ensure that the ERISA fiduciary and prohibited transaction rules work in harmony for all retirement investors, regardless whether they are investing in securities, insurance products that are not securities, or other types of investments.

Further, Plaintiffs cannot show that the conflicts do not exist. Instead, they seek to undermine the compelling evidence that the conflicts are substantial in three ways, claiming that nothing can be learned about annuity sales by extrapolation from mutual fund sales, that nothing can be learned from data preceding the latest regulatory developments in 2010 or 2012, and that a supplemental analysis through 2015 was improper. ACLI Reply 20-23. Courts have long acknowledged that agencies are not required to collect perfect data before regulating, but instead have to exercise their judgment on the basis of the available evidence. *See ConocoPhillips*, 612 F.3d at 841 ("the agency is well within its discretion to regulate on the basis of available information rather than to await the development of information in the future"); *id.* at 842 ("the agency must make do with the available information."). Here, mutual funds and annuities are

[28] Plaintiffs' evidence does not support their blanket assertion that "virtually all fixed indexed annuities are sold in compliance with the Harkin Amendment." IALC Reply 13. IALC's opening brief relied on two comments—NAFA's Cmt. 762, AR42362 n.6 (asserting that insurers "that operate on a nationwide basis have adopted internal policies and protocols that meet or exceed the state or model requirements") and IALC's Cmt. 774, AR42538 (stating only that almost all FIAs are sold under requirements "substantially similar" to the NAIC Model Regulation). *See* IALC Br. 4. Plus, because the SEC is not currently regulating FIAs, insurers have no need to employ the safe harbor. *See* AR358.

comparable in relevant ways—agents are compensated for both with upfront commissions (or "loads") that vary based on the specific product sold, AR444, 447; and both are subject to regulations requiring disclosures and that the recommendations be suitable. AR349, 357. Accordingly, DOL reasonably extrapolated from the substantial evidence of harmful conflicts of interest in the sale of mutual funds to the likelihood of similar conflicts for annuities. *See* Defs.' Br. 79-80. ACLI singles out only one regulatory requirement that applies to annuities but not mutual funds—supervisory approval of each transaction as suitable. ACLI Br. 22-23. But DOL was aware of this distinction, *see* AR350, and ACLI identifies no reason to expect it to substantially alter the conflicts of interest. As DOL noted, FINRA and NAIC suitability is both a less rigorous standard than the fiduciary duty of prudence and does not require acting in the investor's best interest, thus permitting recommendations to be based on the highest return for the agent or broker. *See* AR83-84. Moreover, DOL found that numerous additional pieces of evidence supported the conclusion that conflicts of interest were a problem in the annuity market. *See* Defs.' Br. 79-80.[29] Accordingly, DOL did not "assume[] on the basis of scant record evidence that state laws were insufficient," Ch. Reply 29 n.20; instead its careful analysis demonstrates that it could appropriately extrapolate from the mutual fund and other data to the annuity market.[30] *See* *ConocoPhillips*, 612 F.3d at 841-42 ("defer[ring] to agency's evaluation of the specific ... studies" even though plaintiffs argued it was "highly arbitrary" for agency to find studies comparable).

Nor is it appropriate to write off all empirical analysis prior to 2010 or 2012. While FINRA and the NAIC strengthened their standards then, *see* AR350, 357, they did not fundamentally

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[29] Indeed, a recent academic survey concluded that "although 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; *see also id.* AR31682 (concluding after review of the harms to consumers identified in other markets, including mutual funds, that while "it is possible that these problems are much less prevalent in insurance markets in the US," "we do not think this is likely, given that neither regulation nor competition is stronger for insurance agents than other types of financial intermediaries").

[30] For the same reasons IALC's criticism of DOL's consideration of state regulation is misplaced. Contrary to IALC's claim that DOL "did not, for example, cite evidence that significant numbers of retirement savers who purchase suitable fixed indexed annuities are nevertheless harmed by them," IALC Reply 12, that is exactly what the analogous mutual fund studies indicate. *See* Defs.' Br. 57-59, 79-81.

restructure the existing regime. *See* AR601. Other regulators continued to express concern. *See* AR435, 456, 600 (2011 SEC alert, 2012 FINRA alert). Nor do Plaintiffs explain how any of the implemented changes would ameliorate the sort of conflicts on which DOL's empirical analysis focused. Reports since 2010 indicated that these conflicts remained. *See* AR450; AR41495 (Cmt. 702, Financial Planning Coalition); AR41538, 41541-42, 46166 (Cmts. 706 & 3049, NASAA).

Finally, DOL did not abuse the notice-and-comment process when it supplemented an analysis with additional data. An agency need not rely on only the precise data included with its notice. *See Chemical Mfrs. Ass'n*, 870 F.2d at 201-02 (finding no notice problem where agency "in response to industry criticisms, updated and expanded one of several data sources"). Here DOL disclosed the core studies on which it relied with its notice, AR474-77, and the supplementation merely applied the same basic methodology to a new data set in order to test some commenters' concerns. *See* AR646, 919-20.[31] This is consistent with *Chemical Mfrs. Ass'n* and unlike the case upon which ACLI relies where the agency "fail[ed] to provide an opportunity for comment on the model's methodology" which was "unquestionably among the most critical factual material that was used to support the agency's position." *Owner-Operator Indep. Drivers Ass'n, Inc. v. Fed. Motor Carrier Safety Admin.*, 494 F.3d 188, 199 (D.C. Cir. 2007).

D. The BIC Exemption is Sufficiently Workable for Annuities

The Court should assess the parties' workability arguments in light of the arbitrary and capricious standard—DOL is entitled to prevail unless "its reasons and policy choices" fall below "minimum standards of rationality." *10 Ring Precision, Inc. v. Jones*, 722 F.3d 711, 723 (5th Cir. 2013). *See also City of Arlington v. FCC*, 668 F.3d 229, 261 (5th Cir. 2012) ("Whether the [agency's] decision in this case was ideal, or even necessary, is irrelevant to the question of whether it was arbitrary and capricious "so long as the agency gave at least minimal consideration to the relevant facts as contained in the record"). As an initial matter, Plaintiffs are incorrect that

[31] ACLI criticizes the methodology for "not directly examin[ing] annuity purchases," ACLI Reply 23 n.5, but as previously explained, Defs.' Br. 59, it was not possible to follow specific purchases, and DOL was able to draw robust conclusions by comparing returns for broker sold mutual funds versus their direct-sold counterparts. *Id.* 78-79.

DOL's obligation to find an exemption "administratively feasible" before adopting it, 29 U.S.C. § 1108(a), focuses on "convenience" for the industry. ACLI Reply 14-15. DOL has shown that the plain language and the purpose of the provision focus on feasibility for the agencies administering the exemptions. Defs.' Br. 82 & n.85.[32] Regardless, DOL did consider the workability of the BIC Exemption for annuities and does not agree that the exemption is "fundamentally unworkable" for annuities. ACLI Br. 17; *see, e.g.*, AR64, 74, 554, 567-68, 626-27.

Plaintiffs now claim the central workability problem is the possibility of differing state court interpretations of the same contract terms in class actions. ACLI Reply 15-16. DOL considered the role of litigation, especially as compared to arbitration, and concluded that "the judicial system ensures that disputes ... will be resolved through a well-established framework characterized by impartiality, transparency, and adherence to precedent. The results and reasoning of court decisions serve as a guide for the consistent application of that law in future cases involving other Retirement Investors and Financial Institutions." AR99; *see also* AR78, 88-90, 97. Plaintiffs identify no reason that state courts, in applying long-recognized principles like reasonable compensation and the duties of prudence and loyalty, are likely to diverge widely. *See* Defs.' Br. 84 (pointing out that federal litigation has addressed these issues for decades). Nor do Plaintiffs establish that state courts are ill-equipped to interpret contracts or consider DOL interpretation and guidance regarding the exemption.[33]

Plaintiffs also claim that the BIC Exemption is not workable for independent agents because "[a]n insurer logically cannot guarantee it has created no improper incentives without knowing what other products an agent sells or what commissions the agent receives from others."

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[32] Plaintiffs claim that their expansive interpretation of "administratively feasible" should be adopted because it was shared by some commenters and DOL did not directly reject it in the Rulemaking. ACLI Reply 14-15. But DOL did focus on its own administrative feasibility. *See, e.g.*, AR78 ("The contract provides an administrable way of ensuring adherence to fiduciary standards[.]"); AR170 (same).

[33] Moreover, Plaintiffs' claim that one mistake would result in staggering liability, ACLI Reply 16, is overstated. The BIC Exemption provides relief for good faith mistakes as to disclosures. *See* AR78, 102-03; Defs.' Br. 84. Class action standards provide relevant structure and guard against abuse. AR99. And at the end of the day, requiring an insurer to return the amount of an overcharge after a finding of liability, serves the public interest. See AR78, 99.

ACLI Reply 17.[34] But they do not dispute that insurers have access to detailed information on commission rates for products on the market, including quarterly reports. *See, e.g.*, AR66971-67002, 67018-23. While this information may be retrospective, perfect knowledge is not required for an insurer to appropriately police its own transactions. *See* AR92 (procedures need not "guarantee perfection"). With appropriate knowledge of the industry and how their own products stack up, they can develop procedures and review their own incentives to meet the best interest standard—to serve the straightforward purpose that the recommendation is one that a prudent, informed adviser, adhering to professional standards of care and acting without a conflict, would be comfortable making. *See* AR83-85; *see also* AR 86 (suggesting parties wanting additional assurances could seek "impartial review of their fee structures to safeguard against abuse").

Plaintiffs also challenge the reasonable compensation standard, which one of them recommended. *See* Defs.' Br. 83 n.86. They complain that DOL's longstanding standard, which relies on the facts and circumstances involved, has not been subject to advisory opinions. ACLI Reply 16. But with decades of cases under ERISA, *see* Defs.' Br. 83 n.89, and more applying similar standards under the trust law, *see, e.g.*, *Grizzle v. Tex. Commerce Bank*, 38 S.W. 3d 265, 281 (Tex. App. 2001) ("[S]elf-dealing means the trustee used the advantage of its position to gain any benefit for the trustee, other than reasonable compensation[.]"), *overruled on other grounds*, 96 S.W. 3d 240 (Tex. 2002), the standard is far from indeterminate. Nor can Plaintiffs contort DOL's guidance into a contradiction. As DOL explained, although this is a market-based standard, if there are, for example, hidden fees or fraud, or the services are not rendered or are wholly unnecessary, the fee might be unreasonable even if it is in line with market benchmarks. *See* AR87. But so long as the adviser fairly discloses the fees, performs the work, and does not saddle the customer with unnecessary services, it may charge fees within a reasonable market range.

[34] Similarly, IALC posited a situation where an insurer provides a commission 1% higher than a competitor's superior product. IALC Reply 16. It would violate the best interest standard to recommend an objectively worse product to get a higher commission. AR83. Accordingly, the insurer would need to make sure via robust procedures and review of its incentives and those of any affiliates that the recommendation is not made on the basis of the higher commission.

Finally, Plaintiffs claim DOL failed to consider "the unique ways in which the BIC [Exemption] will impede the sale of annuities through independent agents." ACLI Reply 17; *see also* IALC Reply 17. While Plaintiffs' meaning is not readily apparent, the record is clear that DOL was well aware of the independent distribution channel and made room for industry participants to make a variety of choices regarding how to proceed. Defs.' Br. 85-86 & n.92. A number of these choices would leave the distribution channel largely unchanged, while others would be more transformative. *Id.* Regardless, DOL concluded that investors would retain ample access to investment advice. AR328, 628. Accordingly, DOL has satisfied its rulemaking obligations under the APA. *See Markle Interests*, 827 F.3d at 460.

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

DOL provided adequate notice regarding several possible conclusions regarding annuities, including its ultimate decisions. Defs.' Br. 87-92. The notice requirement is satisfied if it "fairly apprises interested persons of the subjects and issues the agency is considering" and it need not "specifically identify every precise proposal which the agency may ultimately adopt." *Chemical Mfrs. Ass'n v. EPA*, 870 F.2d 177, 203 (5th Cir. 1989).

Notices for the BIC Exemption and PTE 84-24 included a two part proposal—(i) to "revoke relief" under PTE 84-24 for variable annuities and (ii) to "leave in place relief" for FIAs and declared rate annuities. AR790. It then made clear that both aspects of the proposal were subject to comment and possible change by inquiring whether it had "drawn the correct lines between [types of] insurance and annuity products," AR747, and whether the proposal "strikes the appropriate balance." AR790. This readily satisfies the logical outgrowth standard. *See, e.g.*, *United Steelworkers of Am. v. Schuylkill Metals Corp.*, 828 F.2d 314, 317-18 (5th Cir. 1987).

IALC first argues that because DOL used the word "determined," the treatment of annuities other than variable annuities was settled and off the table. IALC Reply 22. Plaintiffs' theory is contradicted, not only by the line-drawing language described above, but also by the fact that DOL:

- described both aspects jointly as its "proposal," *id.*, and "approach," AR747;
- explained it tentatively retained a separate exemption for FIAs and declared rate annuities because of uncertainty whether "some of the disclosure requirements ... or [] the distribution methods and channels" for those products would fit the BIC Exemption's framework, AR790; *see also* AR747;
- inquired whether the proposal was "sufficiently protective of the rights of IRAs," AR 790, which flags the possibility that more limitations could be appropriate; and
- invited responses to a set of questions regarding those disclosure requirements and distribution channels so that DOL could "evaluate our approach." AR747.

IALC also argues that notice was lacking because the ultimate distinction between FIAs and declared rate annuities was not discussed and because the complexity criterion was not offered as a distinguishing feature. IALC Reply 22. But the three types of annuities are well known, AR356, 418, making the line-drawing inquiry a clear indication that DOL might ultimately group them differently and on different grounds—precisely what DOL's questions were designed to explore.[35]

Plaintiffs cannot undo the plain text of the notice by speculating that more comments would have been received if the industry expected that DOL would go the other way. IALC Reply 22-23. IALC itself commented on the line-drawing question and offered several reasons it believed "the conditions of the [BIC] Exemption ... would be problematic for fixed annuities." *See* AR42541 (Cmt. 774). They "cannot now complain because they misread the regulatory waters, incorrectly anticipated how [the agency] would react to their criticisms, and, consequently, submitted comments that left some things unsaid." *BASF Wyandotte Corp. v. Cottle*, 598 F.2d 637, 643 (1st Cir. 1979). As DOL noted, numerous comments from the variable annuity industry pointed out similarities between their products and FIAs, and DOL followed their recommendations in part by determining to treat FIAs and variable annuities the same way. Defs.'

[35] DOL does not rely on the meetings with industry member near the end of the comment period in which DOL's likely disposition of FIAs was discussed for the adequacy of its notice. *See* Defs.' Br. 90. But these meetings and the resulting feedback, including Cmt. 3111 and 3124, do support the fact that any procedural defect would be at most harmless error because DOL considered the objections that Plaintiffs make. *See City of Arlington*, 668 F.3d at 243.

Br. 23 & n.25. And plaintiff SIFMA urged DOL to abandon the proposed securities law distinction, which is what DOL did. *Id.* 90.[36] Accordingly, because "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), DOL satisfies the logical outgrowth standard.[37] Finally, the harmless error standard applies to both Plaintiffs' notice theories, and they have not carried their burden. *See City of Arlington*, 668 F.3d at 243 (requiring "party asserting error to demonstrate prejudice").

VI. EXEMPTIONS REQUIRING THAT CONTRACTS ALLOW FOR CLASS ACTION LAWSUITS DO NOT VIOLATE THE FEDERAL ARBITRATION ACT

The BIC and Principal Transactions Exemptions permit binding arbitration of individual claims but require the contract between the financial institution and the investor to preserve the investor's right to bring or participate in a class action. *See* AR98-99, 134, 151. The class action provision does not violate the Federal Arbitration Act ("FAA"): it is consistent with the text of the FAA and does not interfere with its purposes, including to ensure the enforceability of written arbitration agreements. Further, the FAA does not restrict DOL's authority to set conditions for any exemptions it grants in order to protect retirement investors. Defs.' Br. 92-94.

It is undisputed that the class action provision is consistent with the text of the FAA because it does not render any "written provision" providing for arbitration invalid, revocable, or unenforceable. 9 U.S.C. § 2. Indeed, if a financial institution or adviser were to engage in a conflicted IRA transaction without a contract including the class action provision, the institution would be subject to excise taxes under the Code, but the arbitration provision would remain valid, irrevocable, and enforceable. The provision therefore does not interfere with the FAA's "principal

[36] Plaintiffs' attempt to show surprise through news reports after the final exemption was issued similarly fails. IALC Reply 24. It does not undermine the adequacy of notice because there is a significant difference between surprise at a result chosen and surprise that the choice was on the table. *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.").

[37] Similarly, ACLI's claim that it lacked notice that group annuities would proceed under the BIC Exemption also fails. Defs.' Br. 91. Because group annuities are sold to ERISA plans, not IRAs, the contract provision does not apply, AR78, and because FIAs are seldom sold as group annuities, Plaintiffs' distribution channel concerns are irrelevant. Defs.' Br. 91 n.100. It is not clear what relevant information ACLI believes it should have added.

purpose." *AT&T Mobility LLC* v. *Concepcion*, 563 U.S. 333, 342 (2011).

Rather than grapple with this fact, Chamber merely reiterates its disagreement with DOL that "institutions and advisers remain free to invoke and enforce arbitration provisions," Defs.' Br. 93, based on its incorrect view that conflicted compensation arrangements are the only feasible approach to many accounts. Ch. Opp'n 25. In doing so, Chamber ignores the numerous options available to firms that DOL has identified, *see* AR634-40; Defs.' Br. 93-94 (*e.g.,* use of conflict-free robo-advisers, hourly or flat fees, salary-based compensation models), and takes DOL's statements about certain fee arrangements out of context. *See* Ch. Opp'n 19 (citing AR 67-68 n.18; AR 611 n.573). Although DOL has acknowledged that a fee based on a percentage of assets may be inappropriate in some circumstances, AR611 n.573, this does not mean that a conflicted compensation structure is therefore the only alternative. *See* Defs.' Br. 93-94; AR634-40.

In any event, DOL has exercised its broad discretion to craft exemptions in a constrained way by adopting a class action provision that parallels that in the FINRA Customer Code. Under Rule 12204 of that Code, which has been in effect since 1992, individual arbitration is allowed, but class actions cannot be prohibited. *See Dep't of Enforcement v. Charles Schwab & Co.* (FINRA Bd. of Governors Apr. 24, 2014) [Link] (upholding Rule 12204 against, *inter alia*, FAA-based challenge). For many transactions, therefore, the class action provision does not change the status quo. *See* AR98. And as with Rule 12204, the FAA does not override DOL's congressionally-granted authority to require adherence to the class action provision in order to protect retirement investors. *See Dep't of Enforcement*, at *19 (FAA does not override SEC's authority under the Exchange Act to design rules "to protect investors and the public interest").

VII. DOL'S RULEMAKING IS CONSISTENT WITH THE FIRST AMENDMENT

As DOL has shown, there are two independent reasons the Court need not reach Plaintiffs' First Amendment claim at all. Defs.' Br. 94. First, Plaintiffs cannot bring a claim for the first time in court when they had every opportunity but chose not to raise it during the rulemaking process. *Trinity Indus. v. Occupational Safety & Health Review Comm'n*, 111 F. App'x 751 (5th Cir. 2004)

("As a general rule, … courts will not consider questions of law which were neither presented to nor passed on by the agency."). This includes constitutional challenges to a regulation. *See id.* (citing *Nebraska v. EPA*, 331 F.3d 995 (D.C. Cir. 2003)). Further, because "[a]n objection must be made with sufficient specificity reasonably to alert the agency," *Tex Tin Corp. v. EPA*, 935 F.2d 1321, 1323 (D.C. Cir. 1991), Plaintiffs' general comments regarding regulation of their products' marketing was not sufficient notice of their free speech claim. *See* ACLI Opp'n 4.[38]

Plaintiffs' free speech claim also fails because they have not alleged there is "no set of circumstances" under which the rulemaking would be valid under the First Amendment, as they must to succeed on a facial claim. Defs.' Br. 94. Plaintiffs attempt to recast their claim, *see* ACLI Opp'n 4, but theirs is not an as-applied challenge, as they do not argue that the particularities of their speech are protected from an otherwise valid law. *See Bowen v. Kendrick*, 487 U.S. 589, 601 (1988) (differentiating a challenge to a statute "on its face" and to an "otherwise valid statute" as-applied to particular circumstances). And the remedy they seek—"vacatur of the Rule as a whole," ACLI Opp'n 4—goes well beyond their own speech. *See* Ch. Compl. ¶ 200; ACLI Compl. ¶ 238.

A. The Rulemaking is a Valid Regulation of Professional Conduct

Even if Plaintiffs' First Amendment claim could survive these threshold issues, it fails because the rulemaking is a valid regulation of professional conduct. Under the professional speech doctrine, the "regulation of the practice of a profession, even though that regulation may have an incidental impact on speech, does not violate the [First Amendment]. *Hines v. Alldredge*, 783 F.3d 197, 201 (5th Cir.) (citing *Lowe v. SEC*, 472 U.S. 181, 231-32 (1985) (White, J., concurring)), *cert. denied,* 136 S. Ct. 534 (2015). The professional speech doctrine applies where a regulation governs a speaker "providing personalized advice in a private setting to a paying client," as opposed to a speaker "engag[ing] in public discussion and commentary." *Moore-King v. Cty. of Chesterfield*, 708 F.3d 560, 569 (4th Cir. 2013); *accord Serafine v. Branaman*, 810 F.3d

[38] Nor does *Weaver v. U.S Information Agency*, 87 F.3d 1429 (D.C. Cir. 1996), stand for a contrary proposition where a Declaratory Judgment Act claim is included. *See* ACLI Opp'n 3. *Weaver* did not involve an agency rulemaking at all, but addressed exhaustion requirements under the Civil Service Reform Act. 87 F.3d at 1434.

354, 360 (5th Cir. 2016). As shown, the rulemaking is a paradigmatic regulation of "personalized advice in a private setting to a paying client," and is thus a valid regulation of professional conduct under the professional speech doctrine. *See* Defs.' Br. 96-97, 96 n.102.

In response, Plaintiffs concede that regulations are "subject to less stringent First Amendment review" where the professional speech doctrine applies. ACLI Opp'n 7.[39] They also do not dispute DOL's showing that the rulemaking regulates such personalized advice. *See id.* 7-10. Plaintiffs nonetheless argue that the professional speech doctrine does not apply here because the Rule impermissibly applies fiduciary status to non-fiduciaries and requires them "to act under fiduciary obligations or remain silent." *Id.* at 8. Their position fails for at least two key reasons.

First, whether or not the Rule permissibly defines fiduciary status (it does) is not determinative of whether the professional speech doctrine applies, and, consequently, whether the rulemaking is permissible under the First Amendment. Instead, the relevant inquiry is whether a regulation governs personalized advice, as opposed to public discourse. *See Serafine*, 810 F.3d at 360. Plaintiffs do not dispute that the rulemaking is limited to regulating the former, *see* ACLI Opp'n 3-14, and, thus, cannot refute that the professional speech doctrine applies here.

Second, despite the numerous laws and regulations governing fiduciary relationships, Plaintiffs do not point to one case holding that requiring a fiduciary "to act under fiduciary obligations," ACLI Opp'n 8, violates the First Amendment. Plaintiffs attempt to dismiss this fact

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[39] The Supreme Court has held that regulations of "business transaction[s] in which speech is an essential but subordinate component" are subject to a "lower[] … level of … judicial scrutiny." *Ohralik v. Ohio State Bar Ass'n*, 436 U.S. 447, 457 (1978). The majority of courts to have addressed the issue have thus applied a deferential standard of review to regulations of professional conduct. *See Nat'l Ass'n for the Advancement of Multijurisdiction Practice v. Lynch*, 826 F.3d 191, 196 (4th Cir. 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"); *Hines*, 783 F.3d at 201 ("[R]egulation of the practice of a profession, even though [it] may have an incidental impact on speech, does not violate the Constitution."); *Pickup v. Brown*, 740 F.3d 1208, 1229 (9th Cir.) (lowest level of First Amendment protection applied to "regulation of professional *conduct,* where the state's power is great, even though such regulation may have an incidental effect on speech"); *Locke v. Shore*, 634 F.3d 1185, 1191 (11th Cir. 2011) (license requirement [that] "governs 'occupational conduct, and not a substantial amount of protected speech,' … does not implicate constitutionally protected activity under the First Amendment"). Only the Third Circuit has applied intermediate scrutiny to a regulation of professional speech. *King v. Gov'r of N.J.*, 767 F.3d 216, 234 (2014).

by asserting that First Amendment standards that apply to regulations of lawyers, doctors, and psychologists have "nothing to do with the standard applicable to" the Rule, based on their assertion that the Rule "flatly prohibits" speech "by mandating that … non-fiduciary communications … bear fiduciary obligations." *Id.* at 9. Despite Plaintiffs' contortion, requiring adherence to fiduciary obligations does not equate to "flatly prohibit[ing]" speech. And because brokers and insurance agents, like doctors, lawyers, and psychologists, "take[] the affairs of the client personally in hand and purport[] to exercise judgment on behalf of the client," the professional speech doctrine permits regulation of such persons' conduct, even if it has an incidental effect on speech. *Moore-King*, 708 F.3d at 569; *see also Hines*, 783 F.3d at 201.[40]

Plaintiffs argue that because a recommendation "trigger[s]" fiduciary obligations under the Rule, the Rule "is not targeted at 'conduct' with merely 'incidental' effects on speech," but "regulates speech directly." ACLI Opp'n 9. Plaintiffs conflate the threshold requirement for the Rule's application, and what the Rule actually does once applied. While giving a "recommendation" concerning "investment property" is the threshold requirement for fiduciary status, the Rule does not directly regulate fiduciaries' speech once triggered: it neither prohibits, nor requires, particular recommendations; it requires simply that in giving advice, fiduciaries satisfy duties of prudence and loyalty. The Rule does not violate the First Amendment simply because it governs a transaction that involves speech. *Lowe*, 472 U.S. at 228-29 ("[P]ower to regulate the professions is not lost whenever the practice of a profession entails speech.").

B. The Rulemaking is a Valid Regulation of Inherently Conflicted Transactions

Even if the rulemaking could be said to regulate commercial speech, as opposed to professional conduct, it survives the low level of scrutiny that would apply to it. *See* Defs.' Br. 100 (citing *Accountant's Soc'y of Va. v. Bowman*, 860 F.2d 602, 605 (4th Cir. 1988) (commercial

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[40] Plaintiffs attempt to rely on Justice White's statement that Congress could not "declare editorial writers fiduciaries" and then "forbid[] [them] to publish." *Lowe*, 472 U.S. at 231; ACLI Opp'n 8. But unlike Justice White's example, which posited a regulation of both the most typical form of "engag[ing] in public discussion and commentary," *Moore-King*, 708 F.3d at 569, and a complete prohibition on speech, the rulemaking regulates personalized advice, *see* Defs.' Br. 96-97, and requires only that in rendering such advice, fiduciaries adhere to longstanding fiduciary duties.

speech "falls outside the protection of the first amendment[] if the communication is false, deceptive or misleading")). As explained in DOL's opening brief, the rulemaking is aimed at eliminating the effect of conflicts by proscribing misleading statements about investment transactions, compensation, and conflicts of interest and requiring fiduciaries to give advice in the best interest of retirement investors. *Id.* (citing AR63).[41] Plaintiffs concede that DOL may proscribe misleading speech. ACLI Opp'n 10. And whatever test is used, advice that is *not* in investors' best interest "fall[s] outside of the First Amendment's protection" because it is both "inherently likely to deceive" and it "has in fact been deceptive." *Gibson v. Tex. Dep't of Ins.—Div. of Workers' Comp.*, 700 F.3d 227, 236 (5th Cir. 2012); *see* Defs.' Br. 104. As DOL has explained, retirement investors often lack the financial expertise of those giving them investment advice and, as a result, often rely on such advisers for trusted advice. *See* AR4; Defs.' Br. 43; IALC Br. 18 n.7 (recognizing that evidence suggests 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); AR498 n.412, 10361. At the same time, investors are often "unable to assess the quality of the expert's advice or guard against conflicts of interest" because "[m]ost have no idea how advisers are compensated for selling them products," "are bewildered by complex choices that require substantial financial expertise[,] and welcome advice that appears to be free, without knowing that the adviser is compensated through indirect third-party payments creating conflicts of interest or that opaque fees over the life of the investment will reduce their returns." AR4. Under such circumstances, where investors both believe that the investment advice given to them is in their best interest and are in a position to rely on it, they are likely to be deceived by advice that is, in fact, not in their best interest. And the rulemaking amply

[41] While Plaintiffs might be confused about the source of these limitations, *see* ACLI Opp'n 11, the BIC Exemption requires a financial institution seeking to rely on the exemption to commit that: (i) it, along with its advisors, will "provide investment advice that is, at the time of the recommendation, in the Best Interest of the Retirement Investor," and (ii) that "[s]tatements by the Financial Institution and its Advisers to the Retirement Investor about the recommended transaction, fees and compensation, Material Conflicts of Interest, and any other matters relevant to a Retirement Investor's investment decisions, will not be materially misleading at the time they are made." AR133.

demonstrates that due to conflicted investment advice, investors have, in fact, been deceived to their detriment. AR8 (conflicted advice is widespread, causing serious harm to plan and IRA investors); AR443-50 (same); AR461-65 (advisers act on their conflicts); AR465-79 (adviser conflicts harm IRA investors). By simply repeating their mantra that the rulemaking regulates "truthful, non-misleading commercial speech," ACLI Opp'n 1, Plaintiffs fail to show how advice that is not in their customers' best interest could "be presented in a way that is not deceptive," *In re R. M. J.*, 455 U.S. 191, 203 (1982), and fail to refute that the rulemaking is targeted at misleading statements and deceptive advice and is thus subject to a very low level of scrutiny, if it falls within the ambit of First Amendment protection at all. *See* Defs.' Br. 100-01.[42]

Plaintiffs' contrary position that strict scrutiny should apply to such speech is unavailing. In support of their argument that the rulemaking is an impermissible content-based regulation of commercial speech, Plaintiffs rely on a case involving a town sign ordinance that has no application here. *See* ACLI Opp'n 4. In *Reed*, the Court struck down as an impermissible content-based regulation of commercial speech an ordinance that treated signs differently depending on whether they were "[d]irectional signs," "[p]olitical signs," or "[i]deological signs." *Reed v. Town of Gilbert*, 135 S. Ct. 2218, 2227 (2015). By contrast, the rulemaking does not regulate advice differently based on the message conveyed but applies the same standard to all recommendations—that they be in the best interest of the retirement investor. AR63.[43]

[42] Plaintiffs' argument that the Rule is not targeted at misleading speech because it is aimed "at 'conflicts of interest' and 'conflicted advice,'" ACLI Opp'n 11, misses the point. The goal of the rulemaking is to reduce conflicts of interest to better protect Americans' retirement security, but in striving to do so, the only speech the rulemaking arguably regulates is misleading statements and advice that is inherently likely to deceive, if not downright deceptive, because of the conflicts inherent in the transactions it regulates. ERISA, which Plaintiffs do not challenge, prohibits such conflicted transactions, which would include the speech component of such transactions, unless subject to an exemption, precisely because Congress found that they were likely to deceive and otherwise harm retirement investors.

[43] Plaintiffs argue that the rulemaking "impos[es] many more burdens on speech about some products than speech about others." ACLI Opp'n 6. The primary difference between the BIC and Principal Transactions Exemptions and other exemptions, however, is that to rely on the former two, financial institutions must enter into a contract. While Plaintiffs have obscured precisely what aspect of the rulemaking they challenge on First Amendment grounds, they have not alleged that the contract requirement impermissibly regulates speech. Nor could they. *See Conn. Bar Ass'n v. United States*, 620 F.3d 81, 101 (2d Cir. 2010) (provision of federal statute compelling debt relief agencies to execute written contracts with their bankruptcy clients satisfies rational basis review).

Moreover, the distinctions in the rulemaking that Plaintiffs identify, *see* ACLI Opp'n 101, do not trigger strict scrutiny because they are based on the neutral justification of protecting consumers from commercial harms. *See* Defs.' Br. 101-02. Those distinctions also do not trigger strict scrutiny because they were made for the very reason the entire class of speech at issue is afforded less First Amendment protection: because of the varying degrees to which they are likely to mislead and harm consumers. *See id.* at 102. As the Third Circuit recently held in a similar context, distinctions due to evidence that a "particular form of [advice] is ineffective and potentially harmful to clients" are permissible, as they are based on the same "reason professional speech receives diminished protection under the First Amendment—i.e., because of the State's longstanding authority to protect its citizens from ineffective or harmful professional practices." *King*, 767 F.3d at 236-37. Plaintiffs do not even address, much less refute, this point, *see* ACLI Opp'n 3-14, but it is fatal to their position that strict scrutiny applies here.

C. The Rulemaking Directly Advances the Government's Interest in Protecting Retirement Investors from Conflicted Investment Advice

Finally, even if the Court were to determine that the rulemaking regulates non-misleading commercial speech, the rulemaking meets the intermediate level of review that would apply. *See* Defs.' Br. 103-07. First, the rulemaking will "directly advance" the Government's "substantial interest" by reducing adviser conflicts with a benefit to retirement investors totaling more than $30 billion over ten years—in one segment of the market alone. *See id.* 104-05. In response, Plaintiffs simply reiterate their view that the rulemaking will reduce access to investment advice and allege that DOL failed to respond to this point, *see* ACLI Opp'n 12 (citing Defs.' Br. 62, 107), but they ignore DOL's detailed discussion of the issue, *see* Defs.' Br. 60-63, 107, and the evidence cited therein showing that DOL directly considered the rulemaking's impact on small investors, *see id.* at 60, and had a substantial basis for concluding that "quality, affordable advisory services will be amply available to small plans and investors" under the rulemaking. *Id.* at 61 (citing AR628-34). Plaintiffs otherwise rely on the alleged "substantial" "liability risks created by the BICE," ACLI

Opp'n 13, without acknowledging the offsetting restoration of harm done to investors that the liability represents. While this part of the liability was not quantified in the analysis, neither was this gain to the investor. Defs.' Br. 61-66, 65 n.65.

Second, by adopting a flexible principles-based approach, *see* AR57, AR322, AR359-61, considering numerous alternatives to that approach, and making responsive accommodations to the industry, the rulemaking is "not more extensive than … necessary to serve" the Government's substantial interest. *See* Defs.' Br. 105-07.[44] Plaintiffs criticize DOL's approach, arguing that it should have "regulat[ed] compensation directly" or required "disclosures telling customers whether they are fiduciary advisers or salespeople," *id.* at 11. But directly regulating compensation would have been *more extensive* than requiring advisers to collect no more than "reasonable compensation," *see, e.g.,* AR57, and DOL considered a disclosure-based approach but concluded that disclosures alone would not adequately protect retirement investors from conflicted advice. *See* Defs.' Br. 3-4, 45-46, 80, 105-108, 108 n.112.[45] By contrast, DOL's principles-based approach will directly advance the Government's interest in protecting retirement investors in tax-favored accounts from conflicted advice without being more prescriptive than necessary. *See id.* 104-05.

CONCLUSION

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

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[44] Under intermediate scrutiny, the rulemaking need not be "narrowly tailored," ACLI Opp'n 12, as under strict scrutiny, or "the least restrictive method for achieving the government's goal." *Gibson*, 700 F.3d at 237.

[45] In blindly pressing a disclosures-based approach, Plaintiffs attempt to ignore DOL's showing that not only DOL, but Congress in ERISA, found disclosures insufficient to protect retirement investors from conflicts and thus would not have served the Government's interests in the rulemaking. Defs.' Br. 3-4, 45-46, 80, 105-108, 108 n.112.

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Respectfully submitted,

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CERTIFICATE OF SERVICE

On October 7, 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 electronically or by another manner authorized by Federal Rule of Civil Procedure 5(b)(2).

/s/ Galen N. Thorp
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