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

CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA, FINANCIAL SERVICES INSTITUTE, INC., FINANCIAL SERVICES ROUNDTABLE, GREATER IRVING-LAS COLINAS CHAMBER OF COMMERCE, HUMBLE AREA CHAMBER OF COMMERCE DBA LAKE HOUSTON AREA CHAMBER OF COMMERCE, INSURED RETIREMENT INSTITUTE, LUBBOCK CHAMBER OF COMMERCE, SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION, and TEXAS ASSOCIATION OF BUSINESS,

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

CHAMBER OF COMMERCE PLAINTIFFS' REPLY
IN SUPPORT OF THEIR MOTION FOR SUMMARY JUDGMENT
AND
OPPOSITION TO DEFENDANTS' CROSS-MOTION FOR SUMMARY JUDGMENT

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INTRODUCTION

The government amply illustrates the fundamental flaw in the Fiduciary Rule in the first sentence of its brief: Contrary to its assertion, the Department of Labor does *not* have "broad authority under [ERISA] to protect Americans' retirement savings." Dkt. 72-1 at 1. Congress gave DOL regulatory and enforcement authority over *employer-sponsored* retirement plans and virtually *no* authority over retirement savings outside that context. Desiring to regulate all "retirement savings" but lacking that power, DOL leveraged its limited interpretative authority under ERISA and the Internal Revenue Code to impose restrictions that are so impracticable that the financial and insurance industries will have no choice but to either abandon the market or submit themselves to the vast and onerous new regulatory architecture that DOL has erected through its exemptive authority. And by using that authority to exact firms' agreement to legal obligations that it is powerless to impose directly, DOL has seized the power over "retirement savings" that Congress never bestowed on it; shoved aside other regulators, both federal and state; and upended decades of state and federal regulation and law. This unprecedented approach to regulation not only impairs the ability of savers with modest means to plan for a secure retirement, but threatens to create a blueprint for pervasive regulatory excesses that erase the division of responsibility between coequal agencies and federal and state governments.

The Fiduciary Rule is all about Individual Retirement Accounts ("IRAs")—accounts that are not ERISA plans and that are, therefore, beyond DOL's purview apart from its limited authority under the Code, as relevant here, to interpret the statutory definition of "fiduciary" and grant prohibited transaction exemptions consistent with the statute. Tellingly, the supposed harms DOL identifies in its cost-benefit analysis relate primarily to the IRA market; the contract requirement of the Best Interest Contract ("BIC") exemption—the centerpiece of DOL's attempt to compel commitments that it cannot impose—does not apply to ERISA plans; and large ERISA

plans are exempt from the Rule entirely. Thus, the changes the Rule would actually effect are overwhelmingly directed at the very accounts DOL lacks power to regulate.

Each of DOL's arguments in support of its rulemaking is inconsistent with the text of the statutes, controlling precedents, and congressional determinations. The crux of DOL's defense—that its interpretation of "fiduciary" is reasonable because Congress abandoned fiduciary's settled meaning in all respects—conflicts with Supreme Court precedent and canons of statutory construction. Moreover, DOL's interpretation conflicts with ERISA, the Code, and the securities laws in other respects by conflating sales activity with fiduciary advice, resulting in a Rule so unworkable that it cannot be deemed reasonable. DOL also asserts that its exemptive authority is so "open-ended" that it may impose substantive standards of conduct and penalties on service providers to IRAs that Congress did not. But an agency cannot wield a limited grant of authority so as to "effectively . . . introduc[e] . . . a whole new regime of regulation." *MCI Telecommc'ns Corp. v. AT&T Co.*, 512 U.S. 218, 234 (1994). And, the contractual enforcement mechanism created by the BIC exemption does not merely encapsulate existing state law, but provides new rights and remedies in an "end-run" around Congress's purposefully limited design. DOL's other arguments also lack merit.[1]

This Court should reject the Department's impermissible regulatory overreach and hold the agency to its congressionally-prescribed limits, vacating the rulemaking in its entirety.

ARGUMENT

I. The Department Has Adopted An Unreasonable, Arbitrary Interpretation Of "Fiduciary" That Conflicts With The Plain Meaning Of ERISA And The Code

The Department argues that Congress worked a radical change in the law and the English

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[1] Plaintiffs incorporate by reference the arguments in the reply briefs of the IALC and ACLI plaintiffs, including regarding fixed-indexed annuities and the First Amendment.

language when it incorporated the term "fiduciary" into ERISA and the Code, and again when it defined "fiduciary" to include those who "render investment advice for a fee." *See* Dkt. 72-1 at 30-31. According to DOL, Congress jettisoned the historical understanding of what it means to be a fiduciary, as well as the established distinction between an advisory relationship (which is fiduciary) and a sales relationship (which is not). *See id.* at 1-2, 31-46. These arguments are at odds with the statutory text, practical realities, and reasoned decisionmaking.

A. "Fiduciary" Is A Term Of Art That Excludes Broker-Dealers And Other Sales Relationships That Are Improperly Captured By DOL's Rule

When Congress used the term "fiduciary" in ERISA and the Code, it incorporated a central element of trust law: the presence of a relationship of "special intimacy or . . . trust and confidence" between the parties. Dkt. 61 at 14-15. Brokers and other salespersons have never been understood to have a fiduciary relationship and are not paid for providing advice. *Id.* at 14-18. DOL's Rule conflicts with that historical understanding and the limitation it places on the statutes' reach; indeed, DOL makes no secret of the Rule's intent to sweep in relationships that are not marked by ongoing interactions involving heightened trust and confidence. Dkt. 72-1 at 32-33.

Under DOL's boundless interpretation, virtually any purchase recommendation by a broker-dealer or insurance agent makes her a fiduciary, even something as simple as "providing a selective list of securities" and indicating they are "appropriate for [that] investor" without making a "recommendation . . . with respect to any one security." AR 27. An introductory conversation with a broker during which an IRA was suggested as an investment option would be fiduciary "advice," even if the broker's statement was entirely incidental to the ultimate sale. *See id.* at 22-23. Indeed, a *person* need not be involved to form what at common law was the most personal of financial relationships—the triggering "communication" may be "initiated by

. . . a computer software program." *Id.* at 3.[2]

DOL essentially concedes that this unprecedented interpretation of fiduciary is inconsistent with trust law (Dkt. 72-1 at 31), but argues that because Congress departed from the common law of trusts in one respect, it jettisoned the common law in *all* respects, including when it comes to the very nature of a fiduciary relationship. In DOL's view, a term with ancient vintage was emptied of all historical meaning when incorporated in ERISA and the Code. *See id.* at 31-33. Startling, if it were accurate. But it is not.

The Department's argument rests on *Mertens v. Hewitt Associates*, 508 U.S. 248, 262 (1993), in which the Supreme Court described ERISA's definition of "fiduciary" as "functional." Plaintiffs in that case were participants in an employer-sponsored benefit plan who sued the plan's actuarial firm, arguing that the firm should be liable for losses to plan participants because it had "knowingly participated in the plan fiduciaries' breach of their fiduciary duties," even though it was not itself a fiduciary. *Id*. at 250-51. Finding the plaintiffs could not bring an action for money damages against the actuarial firm, the Court noted that "ERISA . . . defines 'fiduciary' not in terms of formal trusteeship, but in *functional* terms of control and authority over the plan . . . thus expanding the universe of persons subject to fiduciary duties." *Id.* at 262. Congress's "express statutory departure," *id.* at 264 (White, J., dissenting), was thus directed at one specific limitation of "traditional trust law": that only those expressly *named* as trustees were subject to fiduciary duties. *Id.* at 262 (majority op.).

To be sure, this broadened the "class of fiduciaries" that had existed under trust law. But neither *Mertens* nor any other authority supports DOL's claim that Congress set the term "fiduciary" wholly adrift from its common law meaning. On the contrary, virtually every case

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[2] The only instance DOL identifies in which a sale is not fiduciary is when a broker-dealer "execut[es] specific orders" without having prompted the customer or identified the securities to be purchased. Dkt. 72-1 at 34 n.34.

DOL cites on the departure from the common law is referring solely to the expansion of fiduciary status beyond "named" fiduciaries.[3] And it is black-letter law that where a statute "abrogates the common law in certain respects," courts must nevertheless "presume that Congress retained all other elements of [the common law] that are consistent with the statutory text." *Universal Health Servs., Inc. v. United States*, 136 S. Ct. 1989, 1999 n.2 (2016). *See also, e.g.*, *Neder v. United States*, 527 U.S. 1, 23-25 (1999); *Molzof v. United States*, 502 U.S. 301, 310-11 (1992) (similar).[4]

DOL nowhere attempts to show that the "other elements" of a fiduciary relationship—including a relationship of trust and confidence, characterized by "frequent and personal contact," *Lowe v. SEC*, 472 U.S. 181, 195 (1985)—are incompatible with the text of ERISA or the Code. More to the point, this one change Congress made in the common law understanding of fiduciary cannot justify treating as fiduciaries broker-dealers, sales agents, and others who—at the time ERISA was enacted—were *distinguished from* fiduciaries. *Infra* pp. 12-13. Rather, the weight Congress placed on the "function" of a plan service provider—versus whether the provider is "named" in the trust document—made consideration of the historical function of a fiduciary still more important. The Supreme Court illustrated that three years after *Mertens* in *Varity Corp. v. Howe*, 516 U.S. 489, 502 (1996), where it expressly relied on the common law of trusts to interpret ERISA's "fiduciary" definition. It was appropriate, the Court explained, "to

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[3] *See, e.g.*, *Smith v. Provident Bank*, 170 F.3d 609, 613 (6th Cir. 1999) ("the definition of a fiduciary under ERISA . . . does not turn on formal designations"); *Ariz. State Carpenters Tr. Fund v. Citibank (Ariz.)*, 125 F.3d 715, 718, 720 (9th Cir. 1997) (custodial bank not an ERISA fiduciary because it did not have sufficient "control and authority over the plan" to meet the "functional" definition under ERISA); *Custer v. Pan Am. Life Ins. Co.*, 12 F.3d 410, 418 n.3 (4th Cir. 1993) (fiduciary status not determined merely by who is the "named fiduciary"); *Donovan v. Mercer*, 747 F.2d 304, 308 (5th Cir. 1984) (similar); *Ellis v. Rycenga Homes, Inc.*, 484 F. Supp. 2d 694, 703 (W.D. Mich. 2007) (similar).

[4] DOL also was obligated, but failed, to interpret "fiduciary" consistent with its common law application in order to avoid serious First Amendment concerns. *See* ACLI Reply Part I.

look to the common law, which, over the years, has given to terms such as 'fiduciary' and trust 'administration' a legal meaning to which, we normally presume, Congress meant to refer." *Id.* The Court went on to consider the "ordinary trust law understanding of fiduciary 'administration.'" *Id.*[5]

DOL also strays far from the text of ERISA, the Code, and the established meaning of "fiduciary" when it suggests that fiduciary status should be determined by whether a person's activities "impact" "retirement security." Dkt. 72-1 at 42. Quoting a snippet from *John Hancock Mutual Life Insurance Co. v. Harris Trust & Savings Bank*, 510 U.S. 86, 96 (1993), DOL argues that "fiduciary status applies to 'persons whose actions affect the amount of benefits retirement plan participants will receive.'" Dkt. 72-1 at 40; *see also id.* at 30. This passing statement in *John Hancock* was not meant as a test of fiduciary status—the statutory definition was not even at issue in the case—and the Supreme Court has directly stated that "the threshold question [under ERISA] is not whether the actions of some person . . . adversely affected a plan beneficiary's interest, but whether that person was acting as a fiduciary (that is performing a fiduciary function) when taking the action." *Pegram v. Herdrich*, 530 U.S. 211, 226 (2000). A range of non-fiduciaries can significantly affect a plan, including "parties in interest" who provide plan services or the "settlor" who establishes or amends a plan. *See Harris Trust & Sav. Bank v. Salomon Smith Barney Inc.*, 530 U.S. 238, 242-43 (2000) (firm that "provided broker-dealer services" and "sold interests in several motel properties to [plan] for nearly $21 million" was "nonfiduciary" party-in-interest); *Sys. Council EM-3 v. AT&T Corp.*, 159 F.3d 1376, 1379-80 (D.C. Cir. 1998) (defendant merely acted in a "settlor function[]"). In any event, DOL's

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[5] The common law meaning of "fiduciary" is also consistent with dictionary definitions, which DOL consults in its brief. *See* Dkt. 72-1 at 30. *See, e.g.*, Fiduciary, *Merriam Webster's Collegiate Dictionary* (10th ed. 1993), defining "fiduciary" as (for adjective): "of, relating to, or involving a confidence or trust: as **a:** held or founded in trust or confidence . . . ," and (for noun): "one that holds a fiduciary relation or acts in a fiduciary capacity."

"vague notions of a statute's 'basic purpose' are . . . inadequate to overcome the words of its text regarding the *specific* issue under consideration." *Great-West Life & Annuity Ins. Co. v. Knudson*, 534 U.S. 204, 220 (2002) (internal citation and quotation marks omitted).

DOL also asserts, wrongly, that the second prong of the "fiduciary" definition should not be read in harmony with the first and third prongs (Dkt. 72-1 at 37 n.37). That contention violates the basic canon of construction that "the words of a statute must be read in their context and with a view to their place in the overall statutory scheme." Dkt. 61 at 18 (quoting *Roberts v. Sea-Land Servs., Inc.*, 132 S. Ct. 1350, 1357 (2012)). The statutory structure confirms that Congress intended the defining characteristics of a "fiduciary" under trust law to carry over into the statutes, as the first and third prongs both describe relationships consistent with a traditional fiduciary relationship, involving important decision-making power for the plan. The second prong should be read to require a similarly significant relationship.

The legislative record too confirms Congress's understanding that the defining functions of a "fiduciary" under trust law would carry over into ERISA and the Code. The House Report, for instance, explained that a "fiduciary is one who occupies a position of confidence or trust" and that, for purposes of ERISA, this includes "a person who exercises any power of control, management, or disposition with respect to monies or other property of an employee benefit fund." H.R. Rept. No. 93-533, at 2082 (1973) *as reprinted in* 1974 U.S.C.C.A.N. 4639, 4649 (cited in Dkt. 61 at 17). DOL ignores this statement, instead citing passages confirming that a formal trusteeship is no longer required. *See* Dkt. 72-1 at 32, 42. But as explained above, that does not make the historic *functions* of a fiduciary irrelevant—it heightens their importance.

In short, in using the term "fiduciary" in ERISA and the Code, Congress incorporated a familiar term of art and, with it, its accumulated meaning. *FAA v. Cooper*, 132 S. Ct. 1441, 1449

(2012). DOL itself acknowledged as much on several occasions, recognizing, for instance, that it should avoid "burdening activities that do not implicate relationships of trust," (AR 4), because only some relationships are "appropriately regarded as *fiduciary*" (*id.* at 3 (emphasis added)). Specifically, to qualify as a fiduciary under ERISA and the Code, a party must have an advisory relationship to a plan, not a sales-based relationship: fiduciary and sales relationships are fundamentally different and mutually exclusive, an understanding well established prior to ERISA's enactment. *See infra* pp. 12-13. DOL is wrong to contend that Congress could have used any word in place of "fiduciary" without affecting the reach of ERISA or the Code. *See, e.g.*, *Util. Air Reg. Grp. v. EPA*, 134 S. Ct. 2427, 2439-42 (2014).

To the extent DOL has discretion to remove one element of its original five-part test, doing so increases the other elements' importance in ensuring that the relationship is genuinely "fiduciary." Here, however, DOL unreasonably removed the requirement of advice on a "regular basis" as well as other requirements that serve to ensure the presence of an advisory relationship, including that the parties have a "mutual understanding" that the relationship is fiduciary. Indeed, DOL arbitrarily barred parties from agreeing that a sales-based relationship—to which any advice was wholly incidental—was, in fact, a sales rather than fiduciary relationship.[6]

In short, to faithfully interpret "fiduciary," DOL was obligated to avoid an interpretation that swept in sales-based relationships. DOL not only failed to avoid that error, it zealously pursued it.

[6] To the extent DOL believes that financial representatives improperly cause customers to believe they are entering an advisory, fiduciary-type relationship, the solution is to address those relationships under the existing DOL interpretation, or to adopt a revised interpretation that addresses those circumstances. It does not justify an overbroad Rule.

B. DOL's Interpretation Cannot Be Squared With The Statutory Requirement To "Render Investment Advice For A Fee Or Other Compensation"

On its face and in historical usage, the phrase "render investment advice for a fee or other compensation" refers to someone who provides advice in order to be compensated for it: the preposition "for" indicates that the *purpose* of the compensation is to pay for the advice. *See* For, *Merriam-Webster's Collegiate Dictionary* (10th ed. 1993) (defining "for" as, among other things, "a function word to indicate purpose" or "an intended goal," as in "a grant *for* studying medicine"); Dkt. 61 at 15, 17. DOL distorts the plain language, contending that payment for services other than advice creates fiduciary status. Dkt. 72-1 at 34-35.

DOL's counter-textual arguments do not withstand scrutiny. In ordinary sales interactions, the commission is not paid for recommendations that are made in the course of the transaction (*e.g.*, "you'll like this car's gas mileage"). One of the cases DOL cites, *Farm King Supply, Inc. Integrated Profit Sharing Plan & Trust v. Edward D. Jones & Co.*, 884 F.2d 288, 294 (7th Cir. 1989), makes this very point: The broker there did not provide investment advice under ERISA, but only "offered the plan individualized solicitations much the same way a car dealer solicits particularized interest in its inventory"; this "special attention . . . was obviously provided to foster more sales." The Fifth Circuit has made the same point: "Simply urging the purchase of [the company's] products does not make an insurance company an ERISA fiduciary with respect to those products." *Am. Fed'n of Unions Local 102 Health & Welfare Fund v. Equitable Life Assur. Soc. of U.S.*, 841 F.2d 658, 664 (5th Cir. 1988).[7]

A broker-dealer or insurance agent is not compensated for "advice." A commission is

[7] DOL dismisses the Fifth Circuit's decision as "inapposite authority," claiming that it is based on the old five-part test for fiduciary status that DOL now seeks to replace. Dkt. 72-1 at 36 n.35. That is incorrect. Although the Fifth Circuit observed that "advice to self-insure" does not fit within the five-part test, the court also separately reasoned that "urging the *purchase* of [the company's] products" does not create fiduciary status. 841 F.2d at 664 (emphasis added). That statement is not accompanied by a citation to the five-part test. *Id.*

paid if, and only if, there is a sale, no matter how meticulously the salesperson may have "advised" the consumer. Conversely, a broker will receive a full commission once a sale is made even if she makes only a fleeting "recommendation" or none at all. Someone compensated on this basis is plainly not "render[ing] investment advice for a fee."[8] *Cf.* AR 44.

The different payment models for fiduciaries and salespersons, which were well established when ERISA and the Code were enacted, strongly support the same conclusion. Well before those statutes, a "distinction" had long existed between the "two general forms of compensation" that financial professionals receive in connection with offering investment assistance—commissions, which are earned "for each securities transaction completed," and "a separate advice fee," which is "often a certain percentage of the customer's assets under advisement or supervision[]." *Fin. Planning Ass'n v. SEC*, 482 F.3d 481, 485 (D.C. Cir. 2007). To say that payment for a product, when accompanied by the barest of suggestions, is payment *for* advice sufficient to confer fiduciary status, is to ignore this time-honored distinction that was central to the statutory definition enacted by Congress.

DOL seeks to evade the significance of this statutory language by omitting a key part of it—time and again, it frames the key question as whether "investment advice" has been provided, rather than whether the payment was for advice. But an interpretation of "render investment advice *for a fee*" that fails to address that aspect of the transaction and the statutory language is unreasonable, arbitrary, and capricious. *See Motor Vehicle Mfrs. Ass'n of U.S., Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983).

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[8] DOL contends that commissions qualify as compensation for advice because insurance agents and brokers can "play" an "advisory role." Dkt. 72-1 at 36. But the fact that insurance and financial professionals may sometimes convey information about the products they sell does not mean they are paid *for* advice. Having a knowledgeable salesforce can be a competitive advantage and helpful to consumers, but that does not mean the payment is tendered for anything but the service of matching the buyer with the desired product.

DOL's brief dismisses the distinction between sales and advice as not "relevant" and essentially illusory; "sales and investment advice go hand-in-hand," it says. Dkt. 72-1 at 37 n.36; 40 n.39. But when basing a regulatory program on a statute that inquires whether a person "render[s] investment advice for a fee," it is crucial to ascertain whether *advice* is what is being paid for, rather than something else.[9]

DOL actually awakens to this distinction in a key part of its Rule, where it excludes from its "fiduciary" definition transactions involving plans with at least $50 million in assets. For this exclusion to apply, "the person must not receive a fee or other compensation directly from the plan . . . *for the provision of investment advice (as opposed to other services)*." AR 38; *id.* at 55 (emphasis added). The "other services" referred to here are sales—hence the Department's reference to this exception as the "seller's carve-out." *E.g.*, *id.* at 35, 36, 39. The carve-out thus makes the same inquiry that elsewhere the Department protests is impossible and illusory, seeking—in DOL's words—to determine whether the relationship is a sales relationship or "advisory." "If a plan expressly pays a fee for advice," DOL explained in the rulemaking, "the essence of the relationship is advisory" and, therefore, fiduciary. AR 38. *See also id.* at 3.

Despite recognizing in the seller's carve-out that the "express[] pay[ment] [of] a fee for advice" is the "essence of" an "advisory" relationship, DOL otherwise ignores the settled distinction between advisory and sales relationships. DOL thus honors the sales-advice distinction in the part of the Rule that concerns its core regulatory authority—oversight of large benefit plans—but ignores the distinction when seeking to extend its reach to IRAs, over which it

[9] None of the cases DOL cites grapple with the textual requirement that it is "advice" that must be provided "for a fee or other compensation." *Thomas, Head & Griesen Employees Trust v. Buster*, 24 F.3d 1114, 1120 (9th Cir. 1994), is conclusory, its reasoning consisting of two sentences, one of which is "We disagree." *Ellis v. Rycenga Homes, Inc.*, 484 F. Supp. 2d 694, 710 (W.D. Mich. 2007), is similarly devoid of reasoning. And *Brock v. Self*, 632 F. Supp. 1509, 1520 n.11 (W.D. La. 1986), is not on point because the third-party defendants were compensated for "any and all advice sought to keep the Plan in conformance with ERISA."

has no oversight or enforcement role. That maneuver is critical to the new regulatory requirements DOL places on IRAs, and illustrates that this Rule is not based on a consistent, coherent understanding of what constitutes rendering advice for a fee, but rather on DOL's desire to regulate those who long have been recognized to perform a sales function.

Finally, the Department argues that a salesperson who provides a "suggestion" is covered by the statutory language because the statute refers to "render[ing] investment advice for a fee or other compensation, direct *or indirect*." Dkt. 72-1 at 35 (emphasis added.) Making a sale, DOL suggests, is an *indirect* means of being paid for advice. *Id.* at 35-36. That argument fails as a simple matter of grammar: The word "indirect" refers to whether the "fee or other compensation" is paid directly or indirectly, not to the advice's role in generating the fee. Thus, "indirect" means that a person paid *for* advice can be a fiduciary even if the payment flows from a source other than the plan or advisee. That is precisely how DOL interprets that phrase elsewhere in the rulemaking, including in its definition of "Third-Party Payments," or "indirect" compensation. *See, e.g.*, AR 133 ("The recommended transaction will not cause the Financial Institution . . . to receive, directly or indirectly, compensation for [its] services that is in excess of reasonable compensation"), 134, 137, 103 & 140 (all similar). *And see* 29 C.F.R. § 2550.408b-2(c)(1)(viii)(B) (defining "indirect" compensation as "compensation received from any source other than the covered plan, the plan sponsor, the covered service provider, or an affiliate," such as a "subcontractor").

C. The Rule's Inconsistency With The Securities Laws Further Illustrates That DOL Has Exceeded Its Authority

The Investment Advisers Act of 1940, 15 U.S.C. § 80b-1 *et seq.* (the "Advisers Act" or "Act"), particularly its definition of "investment adviser" and its exclusion of "incidental" advice from that definition, further inform ERISA's definition of "fiduciary" and the "investment

advice" prong. Dkt. 61 at 15-17. DOL claims, however, that this exclusion is irrelevant because Congress did not spell out a similar exclusion in ERISA and the Code. Dkt. 72-1 at 33.

That argument misses the point. The Advisers Act iterates the clear and long-standing distinction between fiduciary investment advice and sales performed by broker-dealers. Dkt. 61 at 15-17. The strong parallels between ERISA's fiduciary definition and the Advisers Act's investment adviser definition (parallels DOL never addresses), as well as the explicit references to the Advisers Act in other parts of ERISA, confirm that Congress legislated against the background of the Act. *Id.* Accordingly, Congress did not need to refer explicitly to the Advisers Act in the investment advice prong of ERISA and the Code to embed, in those new laws, the distinction that the well-known language carried with it from the Act. The cases DOL cites are not to the contrary; one concerned "different words" used in separate sections of the same statute, *Burlington N. & Santa Fe Ry. Co. v. White*, 548 U.S. 53, 62-63 (2006), and the other addressed whether a "subtle" provision in the Bankruptcy Code was intended to "provide regulatory exceptions," *FCC v. NextWave Pers. Commc'ns Inc.*, 537 U.S. 293, 302 (2003).

DOL also rejects the import of the Dodd-Frank Act for the interpretation of fiduciary it has adopted. *See* Dkt. 72-1 at 38. *See also* Dkt. 61 at 19. In Dodd-Frank, Congress directed the SEC to hew to specific considerations in delineating any fiduciary standard that it adopted for broker-dealers, including that receipt of commissions should *not* be a fiduciary violation. *See* Dkt. 61 at 4. DOL dismisses Congress's clear direction on this point by contending that it is the prohibited transaction rules of ERISA and the Code that bar commissions, not the new Rule. *See* Dkt. 72-1 at 38. But DOL adopted its overly expansive definition of fiduciary with the express purpose of triggering the statutes' prohibitions on commissions. Dkt. 61 at 7-8; AR 4-5, 18, 43-44. That objective was directly at odds with Congress's explicit instruction that fiduciary status

should *not* be used to outlaw broker-dealers' receipt of commissions. Dkt. 61 at 9.[10]

DOL also asserts that because Dodd-Frank was enacted after ERISA, it can shed no light on ERISA's meaning. Dkt. 72-1 at 38. That argument ignores "the most rudimentary rule of statutory construction": "courts do not interpret statutes in isolation, but in the context of the *corpus juris* of which they are a part, including later-enacted statutes." *Branch v. Smith*, 538 U.S. 254, 281 (2003) (plurality opinion). *Mackey v. Lanier Collection Agency & Service, Inc.*, 486 U.S. 825, 840 (1988), cited by DOL, noted only that an amendment to the same statute did "not control" its prior meaning. Here, the two statutes must be interpreted in light of one another because both address the conduct standards applicable to broker-dealers and investment advisers.

Finally, in asserting that "disclosure of conflicts 'could be ineffective—or even harmful,'" Dkt. 72-1 at 46 (quoting AR 118), DOL doubles down on the Rule's rejection of the efficacy of disclosure, the very premise of our securities laws. DOL says this is justified because, in ERISA, Congress established a more protective regime for employment retirement assets than it had for securities. *Id.* That argument misstates the context in which DOL disparaged disclosure: DOL was not addressing the obligations that Congress imposes on *those who are* fiduciaries; instead, it was engaged in a policy-based consideration of *who should be deemed* fiduciaries. It makes matters worse that DOL's conclusions in this part of the rulemaking rested merely on the determination that "disclosure *alone*" is ineffective (*id.*; emphasis by DOL), since no one advocated a "disclosure alone" regime, as the extensive protections of the securities laws attest. Finally, the fact that DOL *required* burdensome disclosure once someone *is* a fiduciary merely illustrates the arbitrariness of its prior finding that

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[10] The Department also argues that Congress's acquiescence in the long-standing requirements for the IRA market do not constitute "ratification" of DOL's existing rules (Dkt. 72-1 at 38-39). But the sum of congressional actions in this area, including Dodd-Frank, demonstrates that Congress expects retail investors to be serviced by broker-dealers and insurance representatives who are paid on a commission basis.

disclosures are useless or even harmful.

* * *

The Department's brief emphasizes the supposedly unforeseen changes in employee retirement plans since ERISA was enacted. Even if DOL were correct that "today's marketplace realities" demand a radical change in the law, that would be a warrant for legislative action by Congress, not a license for an agency to contort an existing statute in a manner that conflicts with its text. *See Nat'l Pork Producers Council v. EPA*, 635 F.3d 738, 753 (5th Cir. 2011). For all DOL's talk of unexpected changes in ERISA plans, moreover, the principal "reforms" DOL seeks are with respect to IRAs, which Congress squarely contemplated when it amended the Code and enacted ERISA in 1974: IRAs *were part of that enactment*. Their remarkable success and growth cannot be a basis to interpret the Code to prohibit the commission-based IRA model that contributed to that success, and that was anticipated by Congress.

It is significant, as well, that DOL's new fiduciary definition would not function in the IRA marketplace—it would be utterly unadministrable—if not for the BIC exemption that DOL adopts simultaneously. The exemption, DOL said, is necessary to preserve a "wide variety" of "beneficial" compensation practices, since "serious adverse . . . consequences" could result from "simply banning all commissions" in the IRA marketplace, as DOL's fiduciary interpretation would. AR 59, 118. An interpretation that is not serviceable without titanic "exemptions" is unreasonable, arbitrary, and capricious; indeed, it is no interpretation at all.

Rather, the Department's new Rule is a power grab to regulate IRAs that has no basis in the statutory text and reflects instead DOL's view that today, "social change and legal change and financial change" are best achieved through "regulation" and secondarily through

"litigation."[11] This Rule will affect an enormous portion of the American economy, yet the only authority DOL offers is its role in interpreting "fiduciary." Dkt. 72-1 at 44. That is far from an "express" delegation of authority for DOL to dismantle and reshape the IRA marketplace with profound, and untold, consequences—the precise reason the Supreme Court refused deference in *King v. Burwell*, 135 S. Ct. 2480, 2489 (2015). *See also Whitman v. Am. Trucking Ass'ns*, 531 U.S. 457, 468 (2001). DOL's interpretation is owed no deference.

II. It Was Arbitrary And Capricious For DOL To Use Its Exemptive Authority To Impose Sweeping New Standards Of Conduct That Congress Did Not Authorize

DOL claims that its exemptive authority under ERISA and the Code is "open-ended," restrained only by DOL's capacity to decide whether the conditions it elects to impose meet three broadly-worded statutory requirements. Dkt. 72-1 at 48-49. Thus, DOL contends, its imposition of new substantive standards for IRAs, which mirror those in ERISA but lack a basis in the text of the Code, cannot be arbitrary and capricious. *Id.*

This remarkable proposition—that an agency has virtually unfettered authority to create new substantive obligations—has no basis in ERISA, the Code, or in administrative law. DOL reaches that conclusion only by ignoring the Supreme Court decisions discussed in plaintiffs' opening brief (Dkt. 61 at 24-25), which demonstrate how DOL's limited authority to *exempt* entities from statutory prohibitions (*id.* at 5) cannot be used to *regulate* by imposing new substantive standards that lack a basis in the statute. In *MCI Telecommunications Corp.*, 512 U.S. at 234, the Supreme Court instructed that an agency cannot wield a power to "modify" a statute's requirements in a fashion that would "effectively . . . introduc[e] . . . a whole new regime of regulation." The agency in that case had used regulation to achieve an effective

[11] *Borzi Highlights Changes to ERISA as She, Other Speakers Look Back at Law's 40 Years*, Bloomberg BNA, 41 BPR 1929 (Sept. 9, 2014).

"elimination of [a] crucial provision of the statute for 40% of a major sector of the industry," causing "a fundamental revision of the statute." *Id.* at 231. Here too, DOL has acted to fundamentally transform the Code through the BIC exemption, but its action is even more audacious: DOL uses its exemptive authority not to eliminate regulatory burdens, but to introduce "a whole new regime of regulation," *id.* at 234, imposing standards of conduct on service providers to IRAs that replicate the duties Congress imposed only in ERISA. *See* Dkt. 102 at 16 (DOL has "created a regulatory framework"). It is implausible that Congress—which "does not . . . hide elephants in mouseholes," *Whitman*, 531 U.S. at 468—buried in DOL's exemptive authority the power to ordain that virtually the entire IRA market operates on improper payments, and to impose on service providers in that market the duties of loyalty and prudence that Congress purposely omitted from the Code. *See Util. Air*, 134 S. Ct. at 2442-43.[12]

DOL offers no answer to the controlling authority cited in plaintiffs' opening brief. It cites two out-of-circuit cases, neither of which supports its contention that its exemptive authority is so "open-ended" and lacking in principled limitations that it can be the basis for erecting a whole new regulatory framework.[13] DOL objects that plaintiffs would place "limits on DOL's exemption authority that are not in the statutory text" by precluding DOL from "impos[ing]"—through conditions to the BIC exemption—"the duties of prudence and loyalty" that "Congress did not impose" itself. Dkt. 72-1 at 49-50. That objection gets it backwards. It is

[12] The fact DOL has any role at all with respect to IRAs is merely the result of an administrative reorganization in 1978. *See* Dkt. 72-1 at 6 n.6. A change undertaken for administrative simplicity and efficiency is an especially unlikely, implausible source for the exceptional power DOL now claims.

[13] In *Chamber of Commerce v. SEC*, 412 F.3d 133, 139 (D.C. Cir. 2005), the court upheld the SEC's exemption only because its purpose was not "beyond that of the statute" authorizing it, and the exemption was consistent with the "means the Congress used" to effect the statute's purpose. And in *Nat'l Small Shipments Traffic Conf., Inc. v. Civ. Aeronautics Bd.*, 618 F.2d 819, 827-28 (D.C. Cir. 1980), the court upheld an exemption because it was authorized by "the plain language of the statute." That exemption did what exemptions ordinarily do: reduce regulatory requirements. DOL's "exemption" does the opposite; it constructs an entirely new framework of requirements, which are nowhere authorized in the plain language of ERISA or the Code, and DOL's "means" include creating private liability that is inconsistent with the statutory penalties.

the agency that seeks to erase statutory limits on its authority. Plaintiffs do not dispute that DOL has authority to grant "conditional or unconditional" exemptions. *See id.* at 47, 49 & n.43. But an action that "effectively incorporate[s]" into the Code the ERISA duties of loyalty and care—and thereby establishes a regulatory scheme that is contrary to the Code (Dkt. 61 at 23-24)—is incompatible with the limited nature of an exemptive authority.[14]

The Department's Rule also goes further than the statute permits, and further than any agency in any case DOL cites, by attaching not merely new *conditions* through its exemptive authority, but new *consequences*. Ordinarily when a condition is attached to an exemption, the failure to satisfy the condition means the exemption is lost and the statutory duties and penalties snap back into place. But under this new Rule, when a financial institution enters a "Best Interest Contract," and falls short of its requirements, the institution not only loses the exemption, but also becomes subject to suit for breach of the contract. The BIC exemption thereby imposes new non-statutory penalties, and produces arbitrary and capricious results: Under DOL's new regime, if a service provider to an IRA declined to enter a BIC and received an unreasonable commission, then it would be subject to the statutory excise tax. But if that same firm *did* sign a BIC, it would be subject to a private right of action and potentially class action litigation, on top of the excise tax. DOL offers no reason why the penalties Congress devised are sufficient to address conflicts of interest outside of the BIC, but—under the BIC—those same (or lesser) conflicts necessitate a private right of action for damages.

The Department argues that it has not regulated through its exemptive authority because

[14] The previous DOL exemptions cited in footnote 43 of DOL's brief merely illustrate that the conditions DOL has imposed in the past are different in kind than here. PTE 97-11 contains conditions such as that "[t]he services offered under the relationship brokerage arrangement must be of the type that the broker-dealer itself could offer consistent with all applicable federal and state laws regulating broker-dealers." 64 Fed. Reg. 11,042, 11,043. PTE 91-55 requires, among other things, a "written confirmation statement" identifying the basic facts of the transaction. 56 Fed. Reg. 49,209, 49,211.

the affected firms can simply change to a fee-based compensation model, thereby "avoiding prohibited transactions" and the need to submit to the BIC exemption. Dkt. 72-1 at 51 n.46; *see also* AR 117. But significant record evidence shows that as a result of the Rule, service providers to IRAs often will have no choice but to use the BIC exemption because of the superiority of the transaction-based compensation model in many circumstances. Dkt. 61 at 26-27. DOL ignores this evidence. Even more striking, however, is that DOL's litigation position is flatly contradicted by its own repeated statements in the rulemaking that a fee-based account would be improper for a significant part of the market, particularly customers with small accounts who trade infrequently.[15] For those customers, DOL declared, a fee-based account would be "abusive conduct"—meaning that the financial representative would be obligated to use a transaction-based compensation model and, accordingly, adhere to the requirements of the BIC. *See* Dkt. 61 at 27 (citing AR 67-68 n.18); AR 611 n.573. *See also* AR 59, 118. Similarly, in the rulemaking DOL declined the suggestion of some commenters to "sunset" the BIC exemption, citing its "concern[s] . . . about the disruptive impact of simply barring all conflicts after 5 years, *assuming that were even possible*, and about the potential impact that such *dramatic action* would have on the availability of advice." AR 119 (emphases added).

Those statements constitute powerful, unrefuted evidence that DOL has adopted an overbroad, unadministrable definition of fiduciary precisely so it may channel service providers into the BIC exemption and subject them to burdens that Congress has not. That is why a senior Labor Department official cautioned financial institutions that they should not be "looking for ways out of the [BIC] contract requirement." Mark Schoeff Jr., *Despite lawsuits, DOL is working with advisers to help implement fiduciary rule*, InvestmentNews (July 5, 2016).

[15] *See* AR 36438-40 (for year 2010, approximately 50% of IRA accounts contained assets of $25,000 or less and had on average 3 to 5 trades per account for that year).

Finally, even if DOL were correct that its exemptive authority is broader than plaintiffs contend, the standards of conduct imposed here would still be "arbitrary and capricious." DOL asserts that these standards "are necessary to ensure that Advisers' recommendations reflect the best interest of their Retirement Investor customers." Dkt. 72-1 at 48 (quoting AR 116). But DOL cites nothing in the record for this beyond its own *ipse dixit*, *see id.*, and there is no discernable stopping point to the discretionary judgments DOL claims to be empowered to make. Today, it renders verdicts on the merits of arbitration, punitive damages, and class actions. Tomorrow, if this is permissible, the door is wide open for DOL to use its exemptive authority to decide what causes of action firms should promise contractually to their customers; how much a truly effective compliance officer must be paid; or whether—in some other context—punitive damages or treble damages should in fact be necessary for exemption. This is not the system of government the Framers designed, or what Congress enacted in the Tax Code.

III. The BIC Exemption Unlawfully Creates A Private Right Of Action And Is An Unreasonable, Arbitrary Exercise Of DOL's Exemptive Authority

The Department has admitted that while Congress did not impose duties of loyalty and care on service providers to IRAs, the Department "effectively incorporate[d]" those duties from ERISA by making them terms of the Best Interest Contract that service providers must enter. AR 84. DOL also has admitted that "the contractual requirement" in the BIC exemption "creates a mechanism for investors to enforce their rights" under the exemption, even though "[u]nlike participants and beneficiaries in plans covered by Title I of ERISA, IRA owners and participants and beneficiaries in non-ERISA plans do not have an independent statutory right to bring suit against fiduciaries for violation of the prohibited transaction rules." AR 77; *see also id.* at 89. Time and again in the rulemaking, DOL emphasized the importance that the BIC contract be an "*enforceable* commitment," *id.* at 65 (emphasis added). This "enforceability" and the

accompanying "potential for liability," DOL said, were "critical" to the regulatory framework it was creating, *id.* at 77, indeed, they were a "central goal[]" "of this regulatory project," *id.* at 89. *Accord id.* at 76 ("enforceable right" "critical"); 77 (right of action "critical"); 97 (importance of creating "risk of liability"). *See also* AR 368, 458, 460, 483 (right of action intended to "police" compliance). Throughout this rulemaking, DOL rendered judgments of an essentially legislative character about such matters as the best forum for resolving disputes and the appropriate penalties. Despite all this, DOL claims that it did not "create[] any new private causes of action" because contract actions are creatures of state law. Dkt. 72-1 at 51-52.

This sleight-of-hand is an "impermissible 'end run,'" (*Grochowski v. Phoenix Constr.*, 318 F.3d 80, 86 (2d Cir. 2003)) around the Code and the limits it places on DOL's authority, as well as around the Supreme Court's decision in *Alexander v. Sandoval*, 532 U.S. 275 (2001). The exemption gives IRA owners legal recourse they indisputably lack under the Code: the ability to sue for breach of fiduciary duties and for breach of a prohibited transaction exemption. DOL's regulations, not state law, create the compulsion to enter into the BIC; dictate the terms it must contain; and prescribe the remedies that must be available. Through these means, DOL has sought to regulate IRA markets and further its policy goals by writing federal regulatory requirements into privately-enforceable contracts. All of this conflicts with *Sandoval*'s holding that "private rights of action to enforce federal law must be created by Congress." *Id.* at 286.

It is a distinction without a difference that DOL created its new enforceable rights through an essentially compulsory contract, rather than through a provision authorizing suit in the Rule itself. If the agency in *Sandoval*, rather than "promulgat[ing] a regulation forbidding funding recipients" from adopting practices that have a disparate impact, 532 U.S. at 278, had required recipients to enter a contract in which they agreed not to use such practices, the result

would have been the same—there is no basis in the rationale of *Sandoval* for forbidding the former but not the latter. The fact that DOL has no enforcement power with respect to IRAs—and is therefore using the BIC as an end-run in this respect, too—only makes matters worse than in *Sandoval*. DOL has bootstrapped its way into judging matters reserved for Congress, including the standards of conduct that apply, the damages available if those standards are violated, and critical procedural questions such as whether to allow class actions. *See* AR 134.

Just five years ago, the Supreme Court unanimously rejected an attempt to use contract law to import a private right of action into a statutory framework where Congress had provided none. In *Astra USA, Inc. v. Santa Clara County, California*, 563 U.S. 110 (2011), drug manufacturers entered agreements with the government as a way of opting in to a federal drug rebate program. Customers of the drug manufacturers alleged they were being charged prices that exceeded those allowed by the agreement, and sued as third party beneficiaries. In rejecting the claim, the Court explained: "The absence of a private right to enforce the statutory ceiling price obligations would be rendered meaningless if [customers] could overcome that obstacle by suing to enforce the contract's ceiling price obligations instead." *Id.* at 118. Allowing such a bypass made "scant sense." *Id.* at 114.

Other decisions are to similar effect. In *Umland v. PLANCO Financial Services, Inc.*, 542 F.3d 59, 66-67 (3d Cir. 2008), the Third Circuit affirmed dismissal of a breach-of-contract case in which plaintiff contended that some of the contract terms incorporated requirements of the Federal Insurance Contributions Act ("FICA"), which does not provide for private enforcement. The complaint, the court explained, "attempt[ed] to use state common law to circumvent the absence of a private right of action under FICA"; this was impermissible because it "contradict[ed] Congress's decision not to include expressly a private right of action." *Id.*

And in *MM&S Financial, Inc. v. NASD, Inc.*, 364 F.3d 908, 910 (8th Cir. 2004), the Eighth Circuit rejected plaintiff's argument that it could bring a breach-of-contract claim for violation of the rules of a self-regulatory organization. "Given Congress's grant of exclusive jurisdiction to federal courts to hear all claims for breach of duties created under the Exchange Act, we doubt Congress intended to allow MM&S to avoid Congress's decision not to provide an express right of action and pursue instead a common-law breach of contract claim." *Id.* at 911. These cases fully put to rest the argument that because the BIC exemption will be enforced through contract actions, DOL has not created a private right of action.[16]

Even if DOL's tactic of creating private claims by prescribing contract terms distinguished this case from *Sandoval* (and it does not), the Rule would nonetheless be arbitrary and capricious under the APA and unreasonable under step two of *Chevron*. Here, Congress has constructed a framework of requirements and penalties related to IRAs, and DOL's Rule fundamentally transforms that structure by inventing new standards of conduct and liabilities that depart from the Code. *Supra* Part II. Such an overhaul of Congress's design flouts the separation of powers embodied in the Constitution and cannot be deemed a "reasonable" construction of the law. *See Util. Air*, 134 S. Ct. at 2446.

In its effort to find other regulations that remotely resemble what it has done here, DOL merely confirms how extraordinary the BIC cause of action is. *See* Dkt. 72-1 at 55-56 & nn.56-57. Two of the regulations DOL cites are other DOL exemptive rules. One merely requires that qualified professional asset managers ("QPAMs"), who already must be fiduciaries under the exemption, acknowledge their fiduciary status in writing in order to engage in certain

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[16] DOL's Rule differs from cases such as *Lowe v. General Motors Corp.*, 624 F.2d 1373, 1379 (5th Cir. 1980), in that the very existence of the contract to be sued upon, its terms, and its enforceability are all the product of agency action. By contrast, *Lowe* merely involved the truism that "violation of a Federal law or regulation can be evidence of negligence." *Id.*

transactions. 75 Fed. Reg. 38,837, 38,843. This creates no new legal exposure, because neither the rule nor its adopting release refers to the "enforceability" of the QPAM statement, much less that "enforceability" and "liability" are "critical" to the regulation. *Cf. supra* p. 21. The other exemption requires a "written loan agreement" (which is already likely to exist, unlike the BIC) that describes the terms of a loan involving securities that are plan assets, ensuring that persons who are already fiduciaries do not engage in certain lending activity without appropriate precautions. 71 Fed. Reg. 63,786, 63,796. Once again, neither the rule nor its adopting release characterizes "liability" or "enforceability" as a central "goal." Finally, in neither exemption is the consequence of noncompliance anything other than what Congress prescribed, *i.e.*, the exemption is lost and the statutory consequences of a prohibited transaction apply.

The other regulations DOL cites are also entirely different than the "regulatory project" of the BIC exemption, requiring, for example, that some transactions insured by the government set forth basic details such as "unit price," or permitting broadband licensees to negotiate "alternative" private arrangements with third parties.[17] None of these contracts was designed to manufacture new footing for private litigation, or to impose extensive standards of care and conduct. And of course, these regulations concerned conduct that the agencies were authorized to regulate directly, whereas here DOL uses a contract to institute standards that it cannot directly impose, and to foster lawsuits that DOL itself cannot bring.

In sum, DOL cannot establish by direct regulation liabilities that Congress did not create

[17] *See* 7 C.F.R. §§ 1493.20, 1493.70 (setting minimum contract standards for sales insured by the government, such as inclusion of terms specifying delivery period, unit price, payment terms); 47 C.F.R. § 24.238(c) (allowing broadband providers to negotiate "alternative out of band emission limit[s]" with other parties in certain geographical areas); 14 C.F.R. § 212.3(c) ("[c]ontracts to perform charter flights must be in writing" and those contracts "shall include" two basic terms); 7 C.F.R. § 1499.11(g) (requiring participants in government-funded program to "enter into a written contract with each provider of goods, services or construction work that requires the provider to maintain adequate records . . . and to submit periodic reports to the participant").

in the Code; doing so through the backdoor with forcible contracts is no more lawful.

IV. DOL's Class Waiver Ban Violates The FAA And Is Arbitrary And Capricious

In "remedying" Congress's "failure" to extend ERISA's fiduciary standards and private rights of action to the Code, DOL also mandated that claimants must be allowed to bring their fiduciary breach claims as class actions in court; only individual claims may be freely arbitrated. In thus going a step farther than ERISA—which permits arbitration agreements with class action waivers—and imposing yet another requirement with no footing in the Code, DOL was arbitrary and capricious and violated the Federal Arbitration Act ("FAA"), which prohibits States, private parties, or agencies "from conditioning the enforceability of certain arbitration agreements" on the presence or absence of certain terms. *See* Dkt. 61 at 31-33.

DOL defends its action by arguing that parties "remain free to invoke and enforce" class waiver provisions, only they must not operate in a way that requires an exemption. Dkt. 72-1 at 93. But as explained above, the record evidence and DOL itself have confirmed that the same transaction-based fee model that necessitates an exemption is the only permissible model for many accounts. *Supra* Part II (DOL insisting that it would be "abusive"—and therefore a fiduciary breach—not to use a transaction-based compensation model for some accounts). By DOL's own account, firms serving low-trading customers who do not need ongoing monitoring or assistance will be obligated to enter into contracts that allow class action litigation in court.

As for the supposed "options" for avoiding prohibited transactions: the evidence DOL identifies largely consists of DOL's assumptions that "there is ample room for innovation and market adaptation" (AR 638) and suppositions about "robo-advice providers," who DOL admits "have not been tested in a bear market" (AR 637). None addresses DOL's assertion that a fee-based model is inappropriate in many circumstances. *Supra* pp. 18-19.

The sort of Hobson's choice presented by DOL's Rule is coercive, as the courts have

recognized. *See* Dkt. 61 at 32-33. The Department attempts to distinguish *NFIB v. Sebelius*, 132 S. Ct. 2566 (2012), and *South Dakota v. Dole*, 483 U.S. 203 (1987), by claiming that "DOL has express authority to directly regulate" and "the burden on Plaintiffs' members . . . pale[s] in comparison to the inducements found to be coercive" in those decisions. *See* Dkt. 72-1 at 94 n.101. But DOL does not have authority to impose regulatory requirements on IRAs (*supra* Part II) and as just shown, ceasing to serve a large portion of the IRA market—thereby preserving the ability to arbitrate—is not a genuine, voluntary choice for plaintiffs' members.[18]

For that reason, DOL's Rule impairs parties' ability to agree to arbitrate—and to agree to the subject and terms of arbitration—in a manner that "interferes with fundamental attributes of arbitration," *AT&T Mobility LLC v. Concepcion*, 563 U.S. 333, 344-45 (2011), and impairs parties' ability to "structure their arbitration agreements as they see fit," *Volt Info. Scis., Inc. v. Bd. of Trs. of Leland Stanford Jr. Univ.*, 489 U.S. 468, 479 (1989). It also impermissibly interferes with the FAA's "design[] to promote arbitration," *Concepcion*, 563 U.S. at 345, no less than would a state law that gave regulated entities the "choice" between arbitrating their disputes on the one hand, and, on the other, obtaining necessary licenses and privileges for their business.

V. The Department's Flawed Cost-Benefit Analysis Cannot Justify Its Actions

The Department engages in a lengthy defense of its cost-benefit analysis, *see* Dkt. 72-1 at 56-69, but continues to rely on one-sided evidence and conclusory assertions that fail to support its analysis. Three points in particular illustrate the arbitrariness of DOL's assessment of the costs and benefits of this Rule, and therefore, of the justification for adopting the Rule.

First, DOL dismisses the Rule's negative effects on savers with limited means. *See* Dkt.

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[18] *Amicus* American Association for Justice is thus wrong to contend that DOL's Rule "does not affect the enforceability of agreements." Dkt. 103 at 13. Further, dictating the terms of future agreements is no more consistent with the FAA than gutting agreements that have already been executed.

72-1 at 61-62. For example, DOL says the benefits that brokers provide to clients during a bear market lack "empirical support," *id.* at 63, but rulemaking evidence based on a Vanguard study showed that the "market timing" benefits provided by human advisers were substantial, Dkt. 61 at 37 (citing AR 632, 26179). Notably, Edward Jones and State Farm recently announced that to adhere to the Rule, they are ceasing to sell certain products to retirement savers.[19]

Second, DOL continues to dismiss the daunting costs of exposure to class action lawsuits. DOL claims that firms are already subject to class action litigation (Dkt. 72-1 at 61), but this ignores the fact that many firms—including insurers—currently mitigate those costs through agreements to arbitrate on an individual basis rather than litigate on a class basis. The "increased fiduciary liability insurance premiums" cited by DOL do not specifically address costs from *class actions*, as opposed to litigation generally. *See* AR 555-58. And while DOL asserts that the costs of successful class actions should not be considered, Dkt. 72-1 at 61, that does not excuse ignoring the costs of class actions altogether. Those costs include settling meritless cases because of the risk presented by even a low chance of a class wide damage award, and valuable services being withheld because of fear of liability. *See* Dkt. 61 at 35. This fear was one of just three aspects of the "advice gap" that the UK examined in its recent report, yet DOL entirely ignored this cost of class actions. *See* Financial Conduct Authority, *Financial Advice Market Review Final Report* at 4 (March 2016).

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[19] *See Why State Farm agents are getting out of the investment game*, Crain's Chicago Business (Sept. 3, 2016); *Watch Out, Retirement Savers, Your Choices Are Poised to Shrink*, Wall Street J. (Aug. 18, 2016). These actions by Edward Jones and State Farm refute the assurances of *amicus* Financial Planning Coalition that the Rule will not "close off middle-income investors from obtaining professional financial guidance." Dkt. 102 at 7. Moreover, the experience of the Coalition's members is not representative for at least two reasons. First, the Coalition's fiduciary standard is markedly different than the burdens and liability imposed by DOL's Rule. *Cf.* Dkt. 102 at 6. Second, its members provide financial planning services comparable to the fiduciary advisory services regulated by the Advisers Act; they are not similarly situated to broker-dealers and insurance agents. This case is not the first time the Coalition's members have taken to court to seek to increase regulatory burdens on their competitors, including broker-dealers. *See Fin. Planning Ass'n v. SEC*, 482 F.3d 481 (D.C. Cir. 2007).

Third, DOL continues to misconstrue its statements in a 2011 rulemaking where it noted the significant monetary benefits of financial assistance obtained by retirement savers. DOL contends that its "2011 analysis consistently pointed to evidence that . . . advisory conflicts could taint fiduciary advice and harm IRA investors." Dkt. 72-1 at 63. But that contention fails to address how the 2011 estimate supposedly pertains "only to fiduciary advice," when, as plaintiffs observed, the 2011 regulation clearly attributes benefits to non-fiduciary activities regularly performed by brokers that do not involve alleged conflicts, such as "helping savers avoid excess taxes." *See* Dkt. 61 at 36 (citation omitted). Having based adoption of the Rule in part on the assertion that investment assistance is not necessarily helpful, and that therefore a reduction in assistance is not necessarily adverse, DOL cannot now protest that this is a judgment the Court need not reach. Rather, an error on this point invalidates the Rule as a whole. *See Nat'l Fuel Gas Supply v. FERC*, 468 F.3d 831, 839-40 (D.C. Cir. 2006).

VI. DOL's Regulation Of Fixed-Indexed Annuities Is Arbitrary, Capricious, And Contrary To Congress's Intent

DOL's use of the Rule to regulate fixed-indexed annuities is emblematic of its disregard for the constraints imposed by Congress, and for the role that other regulators play in protecting retirement investments. After the D.C. Circuit struck down an SEC rule attempting to regulate fixed-indexed annuities as securities (*see Am. Equity Inv. Life Ins. Co. v. SEC*, 613 F.3d 166, 167, 179 (D.C. Cir. 2009)), the "Harkin Amendment" to Dodd-Frank prohibited the SEC from regulating these annuities provided that they satisfy certain state regulatory requirements. *See* Dodd-Frank Act, § 989J. Despite this clear intent that fixed-indexed annuities be governed by appropriate state regulations, DOL nonetheless assumed, without any basis or meaningful analysis in the rulemaking (*see* AR 672-75), that state regulation was inadequate.

DOL barely acknowledges this congressional action in its brief. *See* Dkt. 72-1 at 10 n.11.

Instead, DOL defends its treatment of fixed-indexed annuities by relying on the SEC rule that was invalidated (*id.* at 15), and on the court decision that invalidated it, which said in a *dictum* that it was "reasonable" for the SEC "to treat variable annuities and FIAs the same for purposes of securities laws." *Id.* at 72 (citing *Am. Equity*, 613 F.3d at 172-73). What DOL fails to acknowledge, however, is the court's *holding* that the SEC had arbitrarily concluded that federal regulation was superior to existing state regulation, 613 F.3d at 178-79, and that Congress went a step further in the Harkin Amendment and barred the SEC from ever regulating fixed-indexed annuities again, so long as those state regulatory requirements were satisfied.[20]

DOL also lacks a cogent defense of its failure to account in the rulemaking for the independent marketing organizations ("IMOs") that play a central role in distributing FIAs, but which do not qualify for the BIC exemption and consequently have no plausible means for complying with the Rule. *See* Dkt. 72-1 at 86. DOL suggests that IMOs could apply on an *ad hoc*, case-by-case basis for an exemption, despite the fact that there is no guarantee DOL would grant such an exemption; and DOL contends that an insurance company could simply delegate its oversight responsibilities to an IMO, even though the insurance company would remain liable and has no incentive to take on the risk of claims that it failed to properly oversee the IMO. *Id.* DOL's "solutions" confirm that DOL failed to adequately consider this aspect of the market and that its resulting rulemaking was arbitrary and capricious.

VII. The Appropriate Remedy Is To Vacate All Of The Rules

The APA provides that "reviewing court[s] *shall* . . . hold unlawful and *set aside* agency

[20] DOL attempts to minimize *American Equity*'s holding by arguing that the SEC's error in appraising state protections was made in the context of assessing the rule's effects on "efficiency, competition, and capital formation." Dkt. 72-1 at 72 n.72. In fact, DOL's error is similar, but worse: DOL also assumed on the basis of scant record evidence that state laws were insufficient, but did so after Congress had intervened to approve the adequacy of state regulatory protections. *See* Dkt. 1 ¶ 104 (quoting 15 U.S.C. § 78o(n)(2)).

action" that is arbitrary, capricious, or contrary to law. 5 U.S.C. § 706(2) (emphases added); *see also Checkosky v. SEC*, 23 F.3d 452, 490 (D.C. Cir. 1994) (Randolph, J., concurring). This Court should therefore vacate the Rule and related exemptions and reject DOL's request for remand without vacatur, *see* Dkt. 72-1 at 109. *But see Cent. & S. W. Servs., Inc. v. EPA*, 220 F.3d 683, 692 (5th Cir. 2000).

Even if remand without vacatur were a lawful disposition under the APA, it would not be appropriate here. *See Allied-Signal, Inc. v. U.S. Nuclear Regulatory Comm'n*, 988 F.2d 146, 150-51 (D.C. Cir. 1993). The entire rulemaking here rests on an erroneous interpretation of "fiduciary" and a fundamental misconception of the extent of DOL's authority; these are significant legal errors, not minor errors in reasoning that can be rectified on remand.[21] *See* Dkt. 61 at 27. Further, the consequences of vacatur would be minimal because the Rule and exemptions will not take effect for many months. *See Am. Equity*, 613 F.3d at 179.

The Court should decline DOL's suggestion to simply sever any invalid provisions (Dkt. 72-1 at 109), as the Rule and exemptions all rest upon the improper interpretation of "fiduciary" and other *ultra vires* actions. By DOL's own admission, moreover, the BIC exemption and its private right of action were "critical" to the decision to adopt the Rule and the assessment of its purported benefits, Dkt. 72-1 at 54, and vacating them alone would leave firms with no relief from the Rule's prohibition of commissions, with serious adverse consequences for investors.

CONCLUSION

For the reasons stated in this and plaintiffs' opening briefs, plaintiffs respectfully request that their motion for summary judgment be granted, and DOL's cross-motion be denied.

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[21] This case is thus distinguishable from *Cent. & S. W. Servs.*, 220 F.3d at 692, where the Fifth Circuit remanded because EPA "fail[ed] to explain" its refusal to grant a variance for an industry. Fundamental legal errors are treated differently. *See Am. Forest & Paper Ass'n v. EPA*, 137 F.3d 291, 294 (5th Cir. 1998).

Respectfully submitted,

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s/ Eugene Scalia

James C. Ho, Texas Bar No. 24052766
Russell H. Falconer, Texas Bar No. 24069695
GIBSON, DUNN & CRUTCHER LLP
2100 McKinney Avenue
Suite 110
Dallas, TX 75291
Telephone: (214) 698-3264
Facsimile: (214) 571-2917
jho@gibsondunn.com
rfalconer@gibsondunn.com

Eugene Scalia*
Jason J. Mendro*
Paul Blankenstein*
Rachel E. Mondl*
Gibson, Dunn & Crutcher LLP
1050 Connecticut Avenue, N.W.
Washington, D.C. 20036
Telephone: (202) 955-8500
Facsimile: (202) 467-0539
escalia@gibsondunn.com
jmendro@gibsondunn.com
pblankenstein@gibsondunn.com
rmondl@gibsondunn.com

Counsel for Plaintiffs Chamber of Commerce of the United States of America, Financial Services Institute, Inc., Financial Services Roundtable, Greater Irving-Las Colinas Chamber of Commerce, Humble Area Chamber of Commerce DBA Lake Houston Area Chamber of Commerce, Insured Retirement Institute, Lubbock Chamber of Commerce, Securities Industry and Financial Markets Association, and Texas Association of Business

* Admitted *pro hac vice*

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Steven P. Lehotsky*
U.S. CHAMBER LITIGATION CENTER
1615 H Street, N.W.
Washington, DC 20062
Telephone: (202) 463-5337
Facsimile: (202) 463-5346
slehotsky@uschamber.com

Counsel for Plaintiff Chamber of Commerce of the United States of America

J. Lee Covington II*
INSURED RETIREMENT INSTITUTE
1100 Vermont Avenue, N.W.
Washington, DC 20005
Telephone: (202) 469-3000
Facsimile: (202) 469-3030
lcovington@irionline.org

Counsel for Plaintiff Insured Retirement Institute

David T. Bellaire*
Robin Traxler*
FINANCIAL SERVICES INSTITUTE, INC.
607 14th Street, N.W.
Suite 750
Washington, DC 20005
Telephone: (888) 373-1840
Facsimile: (770) 980-8481
david.bellaire@financialservices.org
robin.traxler@financialservices.org

Counsel for Plaintiff Financial Services Institute, Inc.

Kevin Carroll*
Ira D. Hammerman*
SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION
1101 New York Avenue, N.W.
8th Floor
Washington, DC 20005
Telephone: (202) 962-7300
Facsimile: (202) 962-7305
kcarroll@sifma.org
ihammerman@sifma.org

Counsel for Plaintiff Securities Industry and Financial Markets Association

Kevin Richard Foster*
Felicia Smith*
FINANCIAL SERVICES ROUNDTABLE
600 13th Street, N.W.
Suite 400
Washington, DC 20005
Telephone: (202) 289-4322
Facsimile: (202) 589-2526
richard.foster@FSRoundtable.org
felicia.smith@FSRoundtable.org

Counsel for Plaintiff Financial Services Roundtable

* Admitted *pro hac vice*

CERTIFICATE OF SERVICE

The undersigned hereby certifies that on September 16, 2016, the foregoing document was electronically submitted with the clerk of the court for the United States District Court, Northern District of Texas, using the electronic case file system of the court. I hereby certify that I have served all counsel of record electronically or by another manner authorized by Federal Rule of Civil Procedure 5(b)(2).

s/ Eugene Scalia
Eugene Scalia*