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

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 Nos. 3:16-cv-1530-M and 3:16-cv-1537-M)

REPLY OF AMERICAN COUNCIL OF LIFE INSURERS, NATIONAL ASSOCIATION OF INSURANCE AND FINANCIAL ADVISORS, AND NORTH TEXAS INSURANCE AND FINANCIAL ADVISORS' ASSOCIATIONS PLAINTIFFS IN SUPPORT OF THEIR MOTION FOR SUMMARY JUDGMENT AND RESPONSE TO DEFENDANTS' CROSS-MOTION FOR SUMMARY JUDGMENT

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INTRODUCTION

The Department's lengthy brief cannot paper over two fatal defects at the Rule's core. ***First***, the Rule's radical expansion of the definition of "investment advice" indefensibly relabels as "fiduciary" routine sales conversations between, for example, insurance agents and customers that lack the critical characteristics of trust and confidence that underlie all traditional fiduciary relationships. The Department effectively concedes this but argues (at 42-43) that it has no obligation to demonstrate that the communications it seeks to regulate as fiduciary "'are *actually* in relationships of trust and confidence.'" In its view, the Department is free to regulate speech as fiduciary—and to prohibit speech that is not fiduciary in nature—at its discretion, provided only that it believes doing so is a good idea.

The Department's interpretation is literally boundless—it claims its power is what it says it is—and far exceeds the Department's statutory authority, as the Chamber Plaintiffs explain. Moreover, as Plaintiffs here explain, this sweeping expansion of the statute's reach violates the First Amendment because it imposes unjustified burdens on truthful commercial speech about annuity products that Plaintiffs' members issue, market, and distribute, dramatically decreasing access by American retirement savers to that vital information and in that way harming the very consumers the Rule purports to help. The Department's dismissive responses—that the Rule raises no First Amendment concerns because it supposedly regulates only "professional conduct" or "false or misleading" commercial speech—are inaccurate, are foreclosed by precedent, and would have devastating consequences for commercial speech protections if accepted. The serious constitutional problems created by the Rule require rejection of the Department's expansive construction of the statute under well-established interpretive principles; if permitted under the statute, the Rule must be struck down under the First Amendment as applied to Plaintiffs' members' truthful, non-misleading commercial speech.

Second, dissatisfied that Congress chose to enforce ERISA Title II through an excise tax administered by the IRS, the Department fashioned an unprecedented enforcement-by-private-lawsuit regime that relies on plaintiffs' lawyers and private citizens to enforce ill-defined standards through breach-of-contract actions. The creation from whole cloth of this decentralized enforcement regime at variance from statutory text and structure, once again, exceeds the Department's statutory authority, as the Chamber Plaintiffs explain.

And the problems with the Rule's "best interest contract" provisions do not stop there. The BICE has particularly severe and unjustifiable consequences for variable and fixed indexed annuities, effects not accounted for by the Department and that require the Rule's vacatur. The Department acknowledged throughout the rulemaking the obvious reality that by being subjected to the BICE, these products would lose market share relative to products placed in the less burdensome PTE 84-24. But the Department placed them in the BICE without first considering the substantial costs to American consumers from decreased access to those products. The Department admits (at 68) it did not give "separate consideration" to the consumer benefits of those annuities, claiming it was not required to do so because it did not intend or expect the Rule to affect access to them. That litigation position—which is disingenuous at best—is inconsistent with the text and structure of the Rule, the Department's own express analysis, and the administrative record. The obvious truth is that the Rule will harm consumers by reducing their access to annuity products that have substantial value for many. The Department's failure to grapple with those harms violated its bedrock duty to consider "the advantages *and* disadvantages of [its] decisions." *Michigan v. EPA*, 135 S. Ct. 2699, 2707 (2015).

In the rulemaking, the Department decided to transform the retirement marketplace into one more to its liking. In doing so, it ran roughshod over constraints the First Amendment, its enabling statute, and the APA place on its authority, and harmed the interests of the retirement savers it wanted to help. For those reasons, and as explained by the Chamber and IALC Plaintiffs, this Court should grant summary judgment and vacate the Rule.

ARGUMENT

I. THE RULE VIOLATES THE FIRST AMENDMENT

The Rule regulates, burdens, and bans truthful commercial speech by Plaintiffs' members about annuity products, and it does so in a manner that discriminates based on speaker, listener, and the Department's judgments regarding the value of the speech at issue. ACLI Br. III. The Rule satisfies neither strict nor intermediate scrutiny; indeed, the Department all but admits it ignored the First Amendment implications of the Rule during the rulemaking. Plaintiffs are therefore entitled to summary judgment on their First Amendment claim.

A. The Department's Threshold Objections Are Unavailing

The Department's opening objections (at 94) to Plaintiffs' First Amendment claim are as unpersuasive as they are undeveloped. ***First***, contrary to a one-sentence assertion, Plaintiffs have not waived their First Amendment claim. In addition to a challenge under the APA, Plaintiffs bring a pre-enforcement First Amendment claim under the Declaratory Judgment Act. Compl. ¶¶ 238, 256. Typical waiver principles do not apply to such claims, *e.g., Weaver v. U.S. Info. Agency*, 87 F.3d 1429, 1434 (D.C. Cir. 1996) (recognizing availability of "pre-enforcement attack" on "regulation restricting … speech"), and reliance on an APA case—*BCCA Appeal Grp. v. EPA*, 355 F.3d 817 (5th Cir. 2003)—is thus misplaced.

Moreover, even with respect to an APA claim, and even if it were possible to waive a *constitutional* objection to an agency rule under the APA (we submit that it is not, *see, e.g., Dawson Farms, LLC v. Farm Serv. Agency*, 504 F.3d 592, 606 (5th Cir. 2007); *Ramirez v. CBP*, 709 F. Supp. 2d 74, 83 (D.D.C. 2010)), "issue exhaustion" is not required unless a statute or regulation requires it or the proceeding below was "sufficiently 'adversarial,'" *Delta Found., Inc. v. United States*, 303 F.3d 551, 560-562 (5th Cir. 2002)—none of which is true here. In any event, multiple commenters, including ACLI, argued that the Rule would chill non-fiduciary sales speech and that less restrictive alternatives could achieve the Department's aims, putting at issue the substance, if not the label, of the First Amendment claim. *E.g.*, AR39737-39739, 51894; *see also* AR37 (noting comments arguing the Rule "violated traditional legal principles that … recognize the right of businesses to market … products and services").

Second, facial-challenge principles pose no bar to Plaintiffs' First Amendment claim. The facial/as-applied distinction "goes to the breadth of the remedy employed by the Court," *Citizens United v. FEC*, 558 U.S. 310, 331 (2010), and here Plaintiffs seek relief "as applied" to the truthful commercial speech of Plaintiffs' members, Compl. ¶ 238, not facial invalidation. Furthermore, under the APA, this Court must set aside a rule "contrary to constitutional right," 5 U.S.C. § 706(2)(B), and the Department's failure to tailor the Rule to avoid creating First Amendment problems requires vacatur of the Rule as a whole, *e.g.*, *Nat'l Fed'n of Indep. Bus. v. Per*ez, 2016 WL 3766121, at *46 (N.D. Tex. June 27, 2016) (granting preliminary injunction barring implementation of rule based in part on First Amendment challenge).

B. The Rule Fails Strict Scrutiny

As Plaintiffs have explained, the Rule—with its web of distinctions among products and practices—imposes an array of content discrimination based on speaker, listener, and message. ACLI Br. 11-13. Regardless of the label given to the speech at issue—whether "professional" or "commercial"—the Rule's systematic content-based discrimination demands strict scrutiny.

The Rule is content-based under each of the tests recently clarified by the Supreme Court: it draws facial distinctions, and it ties the level of regulation to the Department's views of the value of the underlying speech and speaker. *Reed v. Town of Gilbert*, 135 S. Ct. 2218, 2227

(2015); ACLI Br. 12-14. Although regulation of truthful commercial speech is subject to at least intermediate scrutiny, *Cent. Hudson Gas & Elec. Corp. v. Pub. Serv. Comm'n*, 447 U.S. 557, 564-566 (1980)—a standard that may also apply to some content-based regulation of broad commercial speech categories if, for example, the regulation is aimed at fraud or illegality in a specific industry—strict scrutiny is proper where, as here, the government accomplishes "further content discrimination" within such broad categories, *R.A.V. v. City of St. Paul*, 505 U.S. 377, 387, 394 n.7 (1992). Thus, in the context of a restriction like the Rule that "burdens disfavored speech by disfavored speakers," the Supreme Court has held that "[c]ommercial speech is no exception" to the First Amendment's disapproval of content discrimination, *Sorrell v. IMS Health Inc.*, 564 U.S. 552, 564-566 (2011); *cf. Retail Dig. Network, LLC v. Appelsmith*, 810 F.3d 638, 648-650 (9th Cir. 2016) ("Our sister circuits have agreed that *Sorrell* requires stricter judicial scrutiny of content-based restrictions on non-misleading commercial speech[.]").

Indeed, as Supreme Court precedent establishes, the Constitution's prohibition on content discrimination is a "distinct … limitation[] … on government regulation of speech," *Reed*, 135 S. Ct. at 2229-2230, which applies to regulation of even otherwise "proscribable speech," *R.A.V.*, 505 U.S. at 387. "[C]ontent discrimination" thus ordinarily requires strict scrutiny, *id.*, because it is the "constitutionally impermissible manner" of regulation—not the type of speech at issue—that is dispositive, *Carey v. Brown*, 447 U.S. 455, 465 (1980).

The Rule cannot survive strict scrutiny. First, there are many narrower alternative approaches *Congress* could have adopted to address perceived conflicts of interest (such as regulating compensation directly), ACLI Br. 14-15, a point the Department ignores. Second, the Rule fails strict scrutiny for the same reasons it fails intermediate scrutiny, as described in Plaintiffs' opening brief and below, *id.* 15-23; *see infra* I.C.3; *cf. Sorrell*, 564 U.S. at 571-572.

The Department does not seriously argue that the Rule satisfies strict scrutiny, with good reason. *See United States v. Playboy Entm't Grp., Inc.*, 529 U.S. 803, 818 (2000) (content-based discrimination is "rare[ly]" permissible). Instead, it argues that the Rule's content-, speaker-, and listener-based distinctions depend only on the level of conflicts of interest and do not trigger strict scrutiny because guarding consumers from "commercial harms" is a content-neutral justification. DOL Br. 101 (citing *Sorrell*, 564 U.S. at 579); *see id.* 102. But, as *Sorrell* itself shows, the "commercial harms" that may permit content-based regulation of commercial speech are only those that arise from "false or misleading speech." *Sorrell*, 564 U.S. at 579. As Plaintiffs previously explained and as they develop further below, the Rule is simply not an antifraud measure, and the Department's conflation of conflicts of interest with fraud upends core First Amendment protections. *See* ACLI Br. 11 n.4; *infra* Part I.C.2.

Finally, the Department resorts (at 102-103) to a parade of horribles, speculating that Plaintiffs' position would require application of strict scrutiny to a host of regimes, such as securities laws, that regulate based on "subject matter." That misses the point. The Rule's focus on "recommendations" regarding certain "content" is relevant to the First Amendment inquiry because it shows the Rule regulates expression. ACLI Br. 11-12. But the Rule is subject to strict scrutiny because it draws myriad content-based lines among messages (imposing many more burdens on speech about some products than speech about others); listeners (imposing many more burdens on speech to listeners the Department deems less sophisticated than speech to listeners the Department deems more sophisticated); and speakers (imposing many more burdens on speech by human speakers than on speech by so-called robo-advisers). *Id.* 12-13. That is "paradigmatic … content-based discrimination." *Reed*, 135 S. Ct. at 2230.

C. The Rule Fails Intermediate Scrutiny

The Rule also abjectly fails intermediate scrutiny, *see* ACLI Br. 15-23; the Department's contrary arguments are unfounded as a matter of law and fact.

1. The Professional Conduct Doctrine Is Inapposite

The Department first attempts (at 95) to avoid First Amendment review entirely on the grounds that the Rule regulates "professional conduct," and that any effect on speech is "incidental." That position is untenable for two independent reasons.

First, even if the "professional conduct" doctrine had ever commanded a majority of the Supreme Court—it has not—it is not implicated here by its terms. That doctrine traces to Justice White's concurrence in *Lowe v. SEC*, 472 U.S. 181 (1985), a case involving authority to regulate investment advisers under the Investment Advisers Act—in other words, to regulate individuals whose business is to offer fiduciary advice for a fee. In that context, Justice White opined the government may sometimes regulate the conduct of true fiduciaries subject to less stringent First Amendment review. *Id.* at 228-229; *see Serafine v. Branaman*, 810 F.3d 354, 360 (5th Cir. 2016) (noting the professional speech doctrine is about regulating "fiduciary relationship[s]").

But even under Justice White's approach, the central problem with the Department's argument—as the Department is forced to acknowledge—is that the Rule is *not* limited to regulating actual fiduciary relationships or expression, but instead purports to *impose* fiduciary obligations on non-fiduciary commercial speech by regulatory fiat. The Department thus claims (at 42) that its statutory authority is not "limit[ed] … to those already in relationships of trust and confidence" but includes the authority to "artificially *create*[]" such relationships out of ordinary sales conversations. That imposition of fiduciary burdens on *non*-fiduciary speech is precisely what is at issue. The Constitution does not permit the government to evade First Amendment scrutiny by burdening non-fiduciary speech through the artifice of classifying that speech as "fiduciary" or "professional." The government "'cannot foreclose the exercise of constitutional rights by mere labels.'" *Bigelow v. Virginia*, 421 U.S. 809, 826 (1975).

In *Lowe*, Justice White himself anticipated and rejected this sort of power grab: "Surely it cannot be said, for example, that if Congress were to declare editorial writers fiduciaries for their readers and establish a licensing scheme under which 'unqualified' writers were forbidden to publish, this Court would be powerless to hold that the legislation violated the First Amendment." *Lowe*, 472 U.S. at 231. That is just what the Rule does here: it "declares" that all recommendations to retirement savers must be made in a fiduciary capacity, or not at all, whether or not those recommendations occur in relationships of "trust or confidence," effectively banning typical commercial sales speech. Under the Rule, an insurance agent may not make a sales presentation to a customer—however truthful the presentation or suitable the product—but may make sales "recommendations" only as a fiduciary. Even if the professional conduct doctrine were to insulate from First Amendment scrutiny regulation of fiduciary expression, it cannot permit insulation by *ipse dixit*. Otherwise, the government could vitiate First Amendment protections by sleight of hand, merely relabeling non-fiduciary speech as "fiduciary."

For that same reason, the Department's refrain (at 98) that the Rule simply "requires a fiduciary to act like a fiduciary," and "is not a restriction on speech," only underscores the signal flaw in the Department's logic. The Rule does far more than force "fiduciar[ies] to act like … fiduciar[ies]": it first *creates* fiduciary duties by transforming garden-variety sales conversations involving retirement savers into fiduciary relationships and thereby requires non-fiduciaries to act under fiduciary obligations or remain silent. Plaintiffs' First Amendment claim is aimed directly at *that* breathtaking expansion of the fiduciary "label" and burdens.[1]

Second, the professional conduct doctrine is also inapposite because, unlike professional

[1] Thus, the Department's assertion that the First Amendment claim, "insofar" as it "challenge[s] the Rule's definition of who constitutes a fiduciary," is "coextensive with [Plaintiffs'] APA challenge," DOL Br. 98 n.106, has it backwards. The First Amendment operates as an independent constraint on both Congress and the Department, and its relevance to the statutory issue is its command that the Department and this Court must construe ERISA to avoid serious constitutional questions. *See Hersh v. U.S. ex rel. Mukasey*, 553 F.3d 743, 753-754 (5th Cir. 2008).

licensing regimes—which are the paradigm of professional conduct regulation, *Lowe*, 472 U.S. at 232 (White, J., concurring) ("generally applicable licensing provisions" do not violate First Amendment); DOL Br. 95, 97 n.103 (admitting the doctrine is "most often" applied to "schemes" "involv[ing] the licensing of professionals")—the Rule is not targeted at "conduct," with merely "incidental" effects on speech. To the contrary, the Rule regulates speech directly and intentionally—"advice" and "recommendations" trigger its regulatory burdens and prohibitions—and the Rule thus by its terms is squarely targeted at speech that "propose[s] a commercial transaction," the very definition of commercial speech. *Edenfield v. Fane*, 507 U.S. 761, 767 (1993). There is nothing "incidental" about that effect. *Cf. Sorrell*, 564 U.S. at 567 (regulation had "more than an incidental burden" where, "on its face and in practical operation," it was triggered by "the content of the speech and the identity of the speaker").

Notwithstanding the Department's apparent view (at 96-97), an insurance agent describing products to a customer, even in a personalized fashion, and facilitating selection of a suitable product is engaged in protected commercial speech. "[P]ersonal solicitation," no less than mass advertising, "is commercial expression to which the protections of the First Amendment apply." *Edenfield*, 507 U.S. at 765. Indeed, in striking down a ban on in-person solicitation by accountants, the Supreme Court has held that such speech has "considerable value"—"allow[ing] a direct and spontaneous communication" in which the seller "has a strong financial incentive to educate the market and stimulate demand for his product," and the buyer is given "an opportunity to explore [the product] in detail" and compare it to "alternatives." *Id.* at 765-766; *Pac. Frontier v. Pleasant Grove City*, 414 F.3d 1221, 1231 n.8 (10th Cir. 2005) ("personal solicitation is imbued with important First Amendment interests"); *cf.* DOL Br. 97 n.103 (suggesting commercial speech protections apply only to "commercial advertising").

Nor is the Department correct that Plaintiffs' First Amendment claim would call into question "myriad long-standing state and federal laws pertaining to the conduct of numerous fiduciary relationships." DOL Br. 98. Whatever First Amendment scrutiny applies to licensing and regulating lawyers, doctors, and psychologists has nothing to do with the standard applicable to a restriction like the Rule that flatly prohibits purely commercial speech by mandating that all actually non-fiduciary communications on certain topics bear fiduciary obligations. Besides, even licensed fiduciaries are entitled to normal First Amendment protections for their commercial speech. *See Shapero v. Ky. Bar Ass'n*, 486 U.S. 466, 472 (1988) ("[l]awyer advertising is … constitutionally protected commercial speech").[2]

Third, even if the so-called "professional speech" doctrine applied (it does not), the Rule still would have to survive at least intermediate scrutiny, *see King v. Governor of N.J.*, 767 F.3d 216, 237 (3d Cir. 2014); *Pickup v. Brown*, 740 F.3d 1208, 1227-1229 (9th Cir.), *cert. denied*, 134 S. Ct. 2871 (2014), which it does not, ACLI Br. 15-23; *infra* Part I.C.2.

2. The Rule Is Not An Antifraud Measure Because It Proscribes And Regulates Truthful Commercial Speech

The Department's alternative theory for evading First Amendment review (at 100)—that the Rule only "regulates transactions with the potential to mislead"—fares no better.

At the outset, the Department incorrectly frames the legal standard. The government may outlaw misleading speech, but it cannot ban speech that merely has the "potential" to mislead. *In re R.M.J.*, 455 U.S. 191, 203 (1982). Speech that is "inherently" misleading is proscribable; speech that is only "potentially" so is not, and is subject to at least intermediate scrutiny. *Id.*; *Gibson v. Tex. Dep't of Ins.*, 700 F.3d 227, 235-236 (5th Cir. 2012). To proscribe commercial

[2] The Department's reliance (at 98-100) on *Ohralik v. Ohio State Bar Ass'n*, 436 U.S. 447 (1978), is misplaced. *Ohralik* upheld a ban on in-person solicitation by lawyers due to dangers that, the Supreme Court has since clarified, are "unique" to those circumstances. *Edenfield*, 507 U.S. at 774.

speech, the Department must demonstrate it is "inherently likely to deceive" or "has in fact been deceptive," and could not be presented in a non-deceptive way, *R.M.J.*, 455 U.S. at 202-203; *Gibson*, 700 F.3d at 236—none of which the Department has done here (nor could it).

Equally important, the Department's contention that the Rule is targeted at "misleading" speech—a description it repeatedly invokes (at 95, 97 n.10, 101-102, 106) but never explains—is simply wrong. The Rule is aimed at "conflicts of interest" and "conflicted advice,"AR5, 642, not fraudulent or deceptive speech. The Department itself acknowledges this by contrasting securities laws, which "stem largely from statutory antifraud provisions," DOL Br. 7, with the Rule's focus on "conflicted compensation," *id.* at 80. Existing federal securities laws, SEC regulations, and state laws already prohibit false and misleading statements. The Department deems those laws and regulations insufficient because truthful speech—even suitable recommendations—may serve the economic interests of the speaker, and the Department seeks to allow only speech that exclusively serves a listener's interests. AR38. From this, as well as the Rule's title ("Conflict of Interest Rule") and operative provisions, it is perfectly clear that the Rule is directed at the supposed harms from speech with an economic motive, *even when that speech is truthful*. If speech by someone with an economic interest could be banned as "misleading" with no First Amendment scrutiny, no constitutional protection would remain for commercial speech. That is obviously not the law. *See Sorrell*, 564 U.S. at 567 ("a great deal of vital expression" "results from an economic motive").

Stripped of its lawyers' post-hoc re-characterizations, the Department's concern with conflicted advice is not that it is "inherently likely to deceive," *R.M.J.*, 455 U.S. at 202, but that even well-informed consumers purportedly lack the "skills and knowledge" to act in their own interests on the basis of truthful information, AR452; *see* AR4-5 (claiming that consumers are "bewildered" when faced with complex investment choices). That premise is unsupported by the record. But more fundamentally, as a rationale for regulation of speech, it is categorically foreclosed by the First Amendment, which "assume[s] that [truthful] information is not in itself harmful, that people will perceive their own best interests if only they are well enough informed, and that the best means to that end is to open the channels of communication rather than to close them." *Va. State Bd. of Pharmacy v. Va. Citizens Consumer Council*, 425 U.S. 748, 770 (1976).

3. The Rule Cannot Survive Intermediate Scrutiny

The Department's desire to insulate its Rule from First Amendment scrutiny is understandable. Strict scrutiny is fatal, and under intermediate scrutiny, the Rule must directly advance a substantial government interest and be narrowly tailored. *Cent. Hudson*, 447 U.S. at 565. The Department bears the burden of proof, *Allstate Ins. Co. v. Abbott*, 495 F.3d 151, 168 (5th Cir. 2007), and is entitled to no deference on law or fact, *Porter v. Califano*, 592 F.2d 770, 780 (5th Cir. 1979). The Rule fails each step of intermediate scrutiny: it proceeds from multiple unconstitutional assumptions; it will harm retirement savers by raising the cost of access to information about retirement products; and more narrowly tailored alternatives were clearly available. ACLI Br. 15-23. The Department's responses fall flat.

Citing substantial record evidence, Plaintiffs demonstrated that the Rule's sweeping imposition of fiduciary obligations and the substantial liability risk it created under the BICE will raise the cost of retirement products and impede consumers' access to commercial information about those products. ACLI Br. 18-20; AR39770, 42296. Indeed, this effect is inevitable as a matter of "basic … economics." AR63932. The Department says virtually nothing of substance in response. It curtly asserts that "DOL concluded quite the opposite," and demands deference to that *ipse dixit* based "on DOL's expertise." DOL Br. 107; *see id.* at 62. But agencies' conclusory claims to "expertise" alone cannot justify infringement of constitutional liberties:

"courts should make an independent assessment of a … claim of constitutional right when reviewing agency decisionmaking." *Porter*, 592 F.2d at 780.

The Department's substantive responses are also wholly lacking. Plaintiffs pointed to record evidence demonstrating that the liability risks created by the BICE were substantial, and would have serious economic effects. AR39754-39755, 40230, 40593-40594, 40620. The Department admits (at 61) it did not directly "quantify those alleged costs." But without making such an attempt, the Department obviously lacked any basis for its conclusions about the effects of the Rule on the costs of access to information and products. Nor can it explain why banning truthful sales conversations—a low-cost means by which many consumers gain valuable information about retirement products—will not have the obvious effect of raising the costs of obtaining such information and thereby reducing consumers' access to it. AR63932, 63946.

The Department likewise fails to show that the Rule is narrowly tailored, or to explain why it bypassed much simpler, more direct, and less disruptive ways of addressing any concerns about conflicts of interest. ACLI Br. 20-23. For example, instead of adopting this sweeping redefinition of "fiduciary" communications and the elaborate enforcement structure of the BICE, the Department could have required agents and broker-dealers to make clear and conspicuous disclosures telling customers whether they are fiduciary advisers or salespeople. *Id.* at 22-23. That approach would have been more tailored; it would have directly addressed any possible role confusion; and it would have allowed consumers to evaluate the information accordingly. *Id.* The Department conceded that disclosure is "critical" to "understanding … the nature of the relationship and the scope of the conflicts of interest," AR105, but rejected such a narrowly tailored approach because it concluded that "disclosure of advisers' conflicts can backfire, leading … consumers to act contrary to [their own] interests," AR459. The Department thus acted based on a counterintuitive assumption that truthful information provided by non-fiduciaries does not further retirement savers' interests and can "even [be] harmful." AR6. The record amply demonstrated otherwise, ACLI Br. 16, but, in any event, that "highly paternalistic" assumption is incompatible with the First Amendment, *Cent. Hudson*, 447 U.S. at 591.

Because the Rule bans truthful commercial speech, regulates in a content-discriminatory manner, and cannot withstand intermediate—much less strict—scrutiny, it is unconstitutional.

II. THE RULE'S TREATMENT OF ANNUITIES IS ARBITRARY AND CAPRICIOUS

The Rule accomplishes a sweeping regulatory intervention into the retirement savings marketplace, one that will drastically reduce consumers' access to annuities and information about annuities—investment products that play a vital role in helping American consumers navigate the various risks facing retirement savers. Yet remarkably, the rulemaking devotes very little attention to annuities or truthful information about those products in facilitating consumers' access to annuities. In light of the superficial "analysis" the Department did offer, the Rule is arbitrary and capricious or contrary to law as applied to annuities.

A. The BICE Is Not "Administratively Feasible" For Annuities

Under ERISA and the Code, the Department may create exemptions, such as the BICE, only if they are "administratively feasible." 29 U.S.C. § 1108(a); 26 U.S.C. § 4975(c)(2). The BICE violates this requirement because it is unworkable for the insurers, agents, and broker-dealers that issue or sell annuities. ACLI Br. 27-29. The Department's responses fall short.

At the outset, the Department labors mightily to evade the feasibility requirement, claiming (at 82) this only requires an exemption to be "feasible for DOL to administer, rather than workable for the industry." It is implausible that Congress would require an agency to consider its own convenience, but not that of regulated parties. And not surprisingly, the Department does not cite a single rule or decision reflecting this "long-standing" interpretation, and is reduced to relying instead on a news report of a speech delivered 40 years ago and a law review note. *See id.* at 82 n.85. In any event, during the rulemaking, the Department operated under a contrary interpretation, purporting to assess whether the Rule would be feasible from the industry's perspective, as commenters argued was required. AR83-84, 88, 174, 241, 244, 272, 296. The Rule must stand or fall based on "the grounds that the agency invoked when it took action," not post-hoc arguments of litigation counsel. *Michigan v. EPA*, 135 S. Ct. 2699, 2710 (2015); *SEC v. Chenery Corp.*, 318 U.S. 80, 92-94 (1943).

On the merits, the Department struggles (at 82-87) to defend the workability of the BICE by addressing each feature in isolation. But it is the combination of the BICE's ill-defined standards with its novel and unpredictable enforcement-by-private-lawsuit regime that makes the BICE infeasible. Unlike the statutory and common-law examples that the Department cites (at 82-84), the BICE's "best interest," "reasonable compensation," and proprietary-sales standards will not be enforced by a single agency capable of providing advance guidance and uniform interpretation, or by a single court able to refine those terms over time into consistently applied rules of conduct. Instead, the Department has elected to embed them in *contracts* to be enforced through *state-law* breach of contract class action litigation in state and federal court.

That creates an intolerable burden for Plaintiffs' members. For example, if a jury in Texas applying Texas law concludes that a compensation practice was reasonable, can agents in California adopt that practice with confidence that a jury applying California contract law will reach the same conclusion? Or if one Missouri court holds that evidence of hindsight market performance is admissible to assess the reasonableness of a prior investment recommendation, how would an insurer assess that risk nationally? The Department does not say, although those were precisely the type of "feasibility" issues the statute obligated the Department to consider.

Making matters worse, the Department now has taken the position in parallel litigation that the IRS too will be making its own "independent determination … [of] whether or not the financial institution sufficiently complied with" the BICE's standards. NAFA Tr. 81-82, 83-84; *see* 26 U.S.C. § 4975(a), (b). A nationwide insurer attempting to comply with the BICE thus must contend with the possibility that the IRS and courts around the country will apply the BICE's open-ended requirements inconsistently. And if the insurer guesses wrong about how even one such forum would rule, it will face potentially staggering liability—liability the Department did not even attempt to quantify. *See* DOL Br. 61. Whether or not it contravenes ERISA's mandate for a "single uniform national scheme," *Gobeille v. Liberty Mut. Ins. Co.*, 136 S. Ct. 936, 947 (2016); *cf.* DOL Br. 84 n.90, the crazy-quilt private enforcement regime that the Department has unleashed can hardly be described as "feasible."

Contrary to the Department's assertions (at 82-83), its "reasonable compensation" standard does not make the Rule predictable here. For decades, the Department has refused to say whether particular arrangements are reasonable on the ground that the question is "inherently factual"—an unhelpful track record spanning more than 200 advisory opinions. *E.g.*, Mr. Leslie J. Miller, 1981 WL 314473, at *2 (DOL Jan. 15, 1981); Advisory Opinion Procedure, 41 Fed. Reg. 36,281, 36,282 (Aug. 27, 1976). Far from illuminating matters, the Department's "guidance regarding relevant factors to consider," DOL Br. 83—assuming courts would even consider themselves bound by the "guidance"—only sows further confusion and potential for inconsistent outcomes. Reasonableness, the Department says, should be "measured by the *market* value of the particular services, rights, and benefits" provided, AR85 (emphasis added), but should not turn on whether compensation is "customary," AR87. "Reasonable compensation" is, in other words, "a market based standard," AR87—except when it is not.

Additional features of the BICE make it unworkable for the independent agents who currently sell more than two-thirds of all fixed indexed annuities. AR418, 420, 447, 47077. In particular, for independent agents who sell only insurance, the BICE requires the insurer to sign a contract guaranteeing the agent's compliance with the BICE's fiduciary standards. AR139. But because independent agents sell products for multiple insurers, no one insurer possesses the information necessary to make good on that guarantee. *See* IALC Br. 25-26; ACLI Br. 29. The Department responds (at 85-86) that such an insurer "will need to ensure only that recommendations and sales concerning its own products meet the standards." But that is no answer at all. An 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. Thus, complying with the BICE will require insurance companies "to overhaul their primary distribution model for fixed indexed annuities." IALC Br. 26.

The Department now claims (at 86) that it "considered [the independent agent] distribution model throughout its analysis and identified several available options." But the portions of the record the Department cites (at 86-87 & n.92) summarily describe independent agents and IMOs, AR354, 417-420, 447, and they lump agents and IMOs with other regulated entities, AR570, 626-627. They do not show that the Department meaningfully "considered" the unique ways in which the BICE will impede the sale of annuities through independent agents.

The BICE is fundamentally unworkable for variable and fixed indexed annuities, and so violates the statute's "administrative feasibility" requirement.

B. The Department Unlawfully Ignored The Benefits Of Annuities

Plaintiffs' brief explained that the Rule is arbitrary and capricious because the Department failed to account for the harm to American consumers from decreased access to variable and fixed indexed annuities as a result of the Rule. ACLI Br. 29-32. That violated the

Department's duty to "pay[] attention to the advantages *and* disadvantages of agency decisions," *Michigan*, 135 S. Ct. at 2707, and to consider "important aspect[s] of the problem," *Motor Vehicle Mfrs. Ass'n of U.S., Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983).

Remarkably, the Department concedes (at 68) that it did not "quantify reduction in access to [variable and fixed indexed annuities] as a separate consideration," and it does not point anywhere in the record to qualitative consideration of those harms. Instead, the Department defends its failure to consider record evidence of consumer harms from reduced access to variable and fixed indexed annuities on one, and only one, ground: the Department's "goal" was purportedly not "to decrease investors' selection of these types of annuities, *per se*," and the Department had "no reason to expect that variable annuities, FIAs, or any other class of products will lose market share." DOL Br. 67-68. That response fails at each step.

First, even if the Department did not *intend* to steer consumers away from variable annuities, the administrative record established that this would be the Rule's inevitable *effect*, ACLI Br. 27, and the Department was obligated to account for that "important aspect of the problem," *State Farm*, 463 U.S. at 43—which it failed to do.

The Department tries (at 68) to justify ignoring potential consumer harm by claiming that the Rule would depress variable and fixed indexed annuities only if they are "disproportionately recommended on unjustifiable bases." But although the BICE and PTE 84-24 impose the same "reasonable compensation" and "best interest" standards on those recommending retirement products, only the BICE—applied to variable and fixed indexed products but not fixed rate annuities—exposes a seller to "class litigation, and liability and associated reputational risk." AR2. It is the *different liability exposure* created by the Rule, not the elimination of "unjustifiable" recommendations, that will drive sellers to recommend fixed rate annuities over variable and fixed indexed annuities. *See* AR116 (potential liability is a "significant deterrent"). The damage done by that discrimination among products has nothing to do with whether a product is actually best for the customer, and everything to do with which recommendation would carry the most liability risk. The Department ignores that obvious problem.

Second, its text and structure make clear that the Rule, by design, will decrease consumer access to variable and fixed indexed annuities. In the RIA in particular, the Department laid bare its intention to engineer not only the availability of retirement products, but to change consumer decisions in the marketplace. According to the RIA, the Rule is "expected to create benefits in the annuity market … through better matches between consumers and the annuity product." AR484; *see* AR624 (Rule is "intended and expected … to move markets toward a more optimal mix of … financial products"); AR627 (anticipating market share gains for what the Department deems "consumer-friendly insurance products"); ACLI Br. 23-24.

The structure of the Rule also reflects the Department's efforts to remake the market for retirement products. The Rule subjects different annuities to two distinct regimes with markedly different burdens and liability risks. Agents and broker-dealers may sell variable and fixed indexed annuities for a commission only under the BICE, but may sell fixed rate annuities for a commission under PTE 84-24. AR74, 235. Throughout the rulemaking, the Department acknowledged that placing a product or practice in the BICE, rather than in PTE 84-24, would materially alter the market for that product or practice. For example, the Department explained that placing fixed rated annuities "under the terms of PTE 84-24 will *promote access* to these [fixed rate] annuity contracts." AR232 (emphasis added). It also asserted that moving fixed indexed annuities from PTE 84-24 to the BICE was necessary to "avoid[] creating a regulatory incentive to preferentially recommend indexed annuities" over variable annuities or mutual funds.

AR74, 237-238. And it declined to subject robo-advisers to the BICE precisely to avoid "adversely affect[ing] the incentives currently shaping the market for robo-advice." AR114. The Department plainly understood that placing a class of products or services in the BICE would decrease consumer access to and change the costs of those products or services, and on that basis placed products or services into or left them out of the BICE.

For these reasons, the Department cannot now credibly deny that subjecting variable and fixed indexed annuities to the "more stringent" BICE, while leaving fixed rate annuities in the "streamlined" PTE 84-24, AR232-233, 235, will depress the sale of the former and promote the sale of latter. Indeed, in 2015, the Department told the Brookings Institution that "[v]ariable annuities are not the answer for so many people," and predicted that the Rule would steer investors towards "simple investments" that it believes would better "serve[]" "[t]heir needs." Schoeff, *Perez Calls Out Variable Annuities In Argument For DOL Fiduciary Rule*, Investment News (June 24, 2015). Before driving consumers from annuity products, whether deliberately or merely knowingly, it was incumbent on the Department to study the benefits of the products at issue and consider the potential adverse effects of its actions. Its failure to do so was arbitrary and capricious. *See Corrosion Proof Fittings v. EPA*, 947 F.2d 1201, 1223 (5th Cir. 1991); *NorAm Gas Transmission Co. v. FERC*, 148 F.3d 1158, 1164 (D.C. Cir. 1998).

C. The Department Failed Reasonably To Consider The Existing And Robust Regulatory Framework Governing The Sale Of Annuities

Compounding the Department's flawed analysis of annuities, the Department also failed reasonably to consider existing annuity regulation. *See* ACLI Br. 32-35. The Department's account largely came down to nine quantitative studies that purportedly showed the ineffectiveness of those regulations. But those studies prove *nothing* with respect to present-day regulation of annuities because they focused almost exclusively on one type of mutual fund—not annuities—and they relied on data predating significant reforms to the regulatory framework governing retirement products in general and annuities in particular that addressed precisely the concerns the Department seeks to remedy through its Rule. ACLI Br. 33.[3]

The Department now turns somersaults to sidestep these fundamental problems. First, the Department maintains (at 79) that it was appropriate to "extend[]" mutual-fund studies to the annuity marketplace because "conflicts exist in both the mutual fund and annuity markets[.]" But the Department's principal evidence of harm to consumers from such conflicts—the nine quantitative studies—predates FINRA's adoption in 2012 of enhanced suitability requirements governing the sale of securities generally (FINRA Rule 2111), including mutual funds and variable annuities. FINRA Rule 2111 "strengthen[ed], streamline[d] and clarif[ied]" existing consumer protections by codifying and defining the three core suitability obligations: customer-specific, reasonable-basis, and quantitative suitability. *See* FINRA Notice 11-02. It "expanded [the] list of explicit types of information that firms … must attempt to gather and analyze as part of a suitability analysis." *Id.* The rule also for the first time extended suitability consideration to investment strategies involving securities, such as recommendations to hold securities. The studies say nothing about these later, strengthened rules and thus shed no light on the impact of present-day mutual fund regulation, let alone existing annuity rules.

Second, and more fundamentally, in asserting "there is no reason to expect that existing laws governing *insurance* would substantially lower the risk of harm to investors from conflicted compensation observed in the *mutual fund* context," DOL Br. 80 (emphasis added), the Department fails to acknowledge that annuities are governed by a distinct, customized, and

[3] The Department's supposed qualitative "evidence" of harm to annuity purchasers does not make up for the failure of its quantitative analysis. IALC Reply I.B.2. In addition, because the quantitative studies played a central role in the Department's analysis, the conclusion that the Department improperly relied on them requires vacatur of the Rule. *See Nat'l Fuel Gas Supply Corp. v. FERC*, 468 F.3d 831, 839 (D.C. Cir. 2006).

comprehensive regulatory framework that was enhanced in 2010 to account for annuities' unique features. The dated mutual fund studies relied upon by the Department, which focus primarily on investment performance in the historical period 1991 to 2005, do not measure the efficacy of targeted and more rigorous *annuity-specific* rules.

Indeed, these rules already prohibit practices the Department highlights as justification for the Rule. *E.g.*, DOL Br. 85 (noting "impruden[ce]" of illiquid annuity subject to large surrender charge for consumer with few liquid assets). The FINRA rule applicable to deferred variable annuities (FINRA Rule 2330) requires broker-dealers to have a reasonable basis to believe that a recommended transaction comports with the general suitability standard, but it also provides *specific* mandates governing the sale of variable annuities. Broker-dealers must have a reasonable basis to conclude a customer would benefit from the annuity's distinct characteristics, such as tax-deferred growth, annuitization, or a death or living benefit. Moreover, member firms must develop written supervisory policies and procedures and create compliance training programs to ensure that those who effect and review covered deferred variable annuity sales understand their material features. Finally, a registered principal must approve *each* deferred variable annuity sale—a heightened supervisory requirement that does *not* apply to mutual funds.

The recently strengthened 2010 version of the NAIC Model Rule—adopted by 37 States and D.C. while remaining States apply other suitability or consumer-protection standards—creates similar protections.[4] An agent must have reasonable grounds to believe the "consumer would benefit from certain [annuity] features," and from "the particular annuity as a whole." NAIC Model Rule § 6(A)(2)-(3). And issuers must not only develop and implement product-

[4] *See* Heinrich, *State Roundup: State of the State—2015 Year in Review*, Annuity Outlook (Feb. 10, 2016). While the Department objects (at 80) to a "lack of uniformity among state regulation of annuities," it did not identify in the record or otherwise any meaningful differences or gaps in federal and state suitability rules, let alone any resulting harm to consumers.

specific compliance training but also establish processes for reviewing each annuity recommendation to ensure there is a reasonable basis to believe it is suitable—a requirement akin to FINRA's principal review obligation. *Id.* §§ 6(F), 7.

The Department's reliance on out-of-date mutual funds studies accounted for neither the heightened obligations governing the sale of securities in general nor the specific enhancements to FINRA and state suitability rules governing the sale of annuities and thus could not possibly have demonstrated that existing annuity regulation is insufficient. The Department's failure to consider "whether, under the existing regime, sufficient protections existed" renders the Rule arbitrary and capricious. *Am. Equity v. SEC*, 613 F.3d 166, 179 (D.C. Cir. 2010).

Apparently recognizing the insufficiency of its own analysis prior to and during the comment period, the Department in promulgating the final Rule discussed an economic analysis it conducted after the comment period had closed concerning performance of certain mutual funds between 1980 and 2015. DOL Br. 81. That last-minute analysis changes nothing. For one, the Department "commit[ted] serious procedural error" in supplementing the administrative record with this new analysis, without providing an opportunity to comment. *Owner-Operator Indep. Drivers Ass'n, Inc. v. Fed. Motor Carrier Safety Admin.*, 494 F.3d 188, 199 (D.C. Cir. 2007) (internal quotation marks omitted). In any event, *mutual-fund* performance from 1980-2015 still says nothing about whether extant *annuity* regulation sufficiently protects consumers.[5]

III. THE RULE UNLAWFULLY DISCRIMINATES AMONG RETIREMENTS PRODUCTS

The Department's efforts to promote and discriminate against particular retirement products exceeded its statutory authority. Agencies are "limited in authority by legislative

[5] The Department points out (at 68) that "DOL updated the CEM study with data through 2015 and found no meaningful difference between the original data and the more recent period." But that is irrelevant: Neither the initial study nor the authors' more recent data examine retirement product purchases following implementation of more stringent FINRA and state suitability rules. And updated information about the market-share of certain mutual funds cannot show whether existing annuity regulations sufficiently guard against conflicts of interest.

enactment," *Cent. Forwarding, Inc. v. ICC*, 698 F.2d 1266, 1285 (5th Cir. 1983), and nothing in ERISA or the Code gives the Department authority to favor and disfavor products in that manner, *see* ACLI Br. IV. The Department's defense of its radical market intervention fails.

The Department first insists (at 77) that it "does not seek to restrict access to any specific product." But, as explained above, that description of the Rule is implausible. The Rule erects a hierarchy among different products, imposing markedly greater burdens on products the Department believes carry more "investment risk" (variable and fixed indexed annuities) and lesser burdens on products the Department wishes to "promote" because it considers them a "better match[]" for consumers (fixed rate annuities). AR232, 484.

This treatment cannot be justified by invoking statutory authority to exempt "'class[es] of fiduciaries or transactions'" from prohibited-transaction rules, DOL Br. 74, or the Department's practice of exempting "particular investment products or transactions," *id.* at 75. Not one of the examples cited by the Department vaguely resembles what the Department did here. In the Rule, the Department created two different regulatory regimes: the BICE and PTE 84-24. The former imposes onerous conditions and the possibility of staggering liability for covered products, while the latter is "streamlined," imposes no such litigation risk, and in these ways is meant to "promote" market share of covered products. The Department placed disfavored products (variable and fixed indexed annuities) in the BICE, knowing that the burdens of the BICE would mean less information about them would reach consumers, while it placed favored products (fixed rated annuities) in PTE 84-24 with the expectation that consumers' access to those products would be improved. That deliberate attempt to engineer the market for retirement products based on the Department's judgment of which are best for consumers is unprecedented and pushes the Rule well beyond the Department's statutory limits. ACLI Br. 24-25.

In addition, the Department's statutory exemption authority allows it to differentiate among classes of products only based upon "'factors which Congress had … intended it to consider.'" *Nat'l Ass'n of Home Builders v. Defenders of Wildlife*, 551 U.S. 644, 658 (2007); *see Massachusetts v. EPA*, 549 U.S. 497, 533 (2007). Here, the prohibited transaction rules are targeted at one particular evil: conflicts of interest. *See, e.g.*, AR62 (29 U.S.C. § 1106(b) "impose[s] on fiduciaries of plans and IRAs a duty not to act on conflicts of interest"); *Nat'l Sec. Sys., Inc. v. Iola*, 700 F.3d 65, 81-82 (3d Cir. 2012) (29 U.S.C. § 1106(b) is aimed at "conflict-of-interest and self-dealing concerns"). Thus, to justify creating different exemptions for subsets of similar products, the Department must point to differences in their potential conflicts of interest that make it appropriate to subject the products to different regulatory conditions.

The Department overstepped that limited statutory role by relying heavily on a factor—"investment risk"—unrelated to conflicts of interest. Explaining why it elected to regulate fixed rate annuities under PTE 84-24, the Department touted, among other things, the lower "investment risk" associated with those products. AR232, 234-235. By contrast, it emphasized, also among other factors, the "significant investment risk" associated with variable annuities, AR232, and stated that fixed indexed annuities likewise involve greater "exposure to investment risks" than fixed rate annuities, AR439. The risk of uncertain returns from a retirement product (that is, "investment risk") bears no logical nexus to conflicted advice—a product with high "investment risk" could be sold with no commission, for example—and the Department was not free to bootstrap its statutory authority over conflicts of interest to disfavor retirement products it deemed to have too much uncertainty for consumers in expected return. That choice should be made by consumers in the marketplace. *See* ACLI Br. 26.

The Department suggests (at 75) it can differentially regulate products because the statute empowers it to "protect investors." But that misconstrues the statute. The Department's exemption authority requires the Secretary to certify that an exemption will be "in the interests of the plan" and "protective of the rights of participants and beneficiaries." 29 U.S.C. § 1108(a)(2)-(3). Those serve as a *check* on the Department's authority; they do not give it boundless authority to craft exemptions based on its "independent judgment" about which products best match consumers' needs. *Modernizing ERISA To Promote Retirement Security: Hearing Before the Subcomm. on Emp'r-Emp. Relations of the H. Comm. on Educ. and the Workforce*,106th Cong. 37 (2000) (statement of Leslie Kramerich, Acting Assistant Secretary of Labor for Pension and Welfare Benefits, U.S. Department of Labor).

IV. THE DEPARTMENT VIOLATED APA NOTICE REQUIREMENTS

For the reasons discussed by IALC and incorporated here, the Court should also vacate the Rule because the Department violated the APA's notice and comment requirements by excluding group and fixed indexed annuities from PTE 84-24 without sufficient notice. *See* IALC Br. III; IALC Reply III; ACLI Br. VI. Plaintiffs add one point here: the Department's errors were hardly harmless. That certain groups may have been made aware of these changes at the last minute does not cure the defect, *MCI Telecomms. Corp. v. FCC*, 57 F.3d 1136, 1143 (D.C. Cir. 1995), and ACLI and NAIFA would have submitted comments explaining why selling group annuities and fixed indexed annuities under the BICE is infeasible, *see* ACLI Br. 33. The Department asserts it was aware of these issues, DOL Br. 91, but it nowhere meaningfully grapples with them in the record, *see supra* p. 17.

CONCLUSION

The Court should vacate the Rule or, in the alternative, declare the Rule unconstitutional as applied to the truthful commercial speech of Plaintiffs' members.

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Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on this 16th day of September, 2016, I electronically transmitted the foregoing document to the Clerk's Office using the CM/ECF System, which will send a notice of filing to all counsel of record.

s/ David W. Ogden
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