Docket No. 17-3038
Oral Argument Requested

IN THE UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

MARKET SYNERGY GROUP, INC.,
Plaintiff-Appellant,

v.

UNITED STATES DEPARTMENT OF LABOR and R. ALEXANDER ACOSTA, in his official capacity as Secretary of the United States Department of Labor,
Defendants-Appellees.

Appeal from a Decision of the United States District Court for the District of Kansas, Honorable Daniel D. Crabtree, Case No. 5:16-CV-04083

BRIEF OF AMICI CURIAE AARP, AARP FOUNDATION, AMERICANS FOR FINANCIAL REFORM, BETTER MARKETS, CONSUMER FEDERATION OF AMERICA, NATIONAL EMPLOYMENT LAW PROJECT AND PUBLIC INVESTORS ARBITRATION BAR ASSOCIATION IN SUPPORT OF DEFENDANTS-APPELLEES AND URGING AFFIRMANCE

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CORPORATE DISCLOSURE STATEMENTS

Pursuant to Rule 26.1 of the Federal Rules of Appellate Procedure and Rule 26.1 of the Rules of the United States Court of Appeals for the 10th Circuit,

AARP and AARP FOUNDATION hereby certify that the Internal Revenue Service has determined that AARP is organized and operated exclusively for the promotion of social welfare pursuant to Section 501(c)(4) of the Internal Revenue Code and is exempt from income tax. The Internal Revenue Service has determined that AARP Foundation is organized and operated exclusively for charitable purposes pursuant to Section 501(c)(3) of the Internal Revenue Code and is exempt from income tax. AARP and AARP Foundation are also organized and operated as nonprofit corporations under the District of Columbia Nonprofit Corporation Act. Other legal entities related to AARP and AARP Foundation include AARP Services, Inc. and Legal Counsel for the Elderly. Neither AARP nor AARP Foundation has a parent corporation nor issued share or securities.

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NATIONAL EMPLOYMENT LAW PROJECT (NELP) hereby certifies that it is a Section-501(c)(3) non-stock corporation. No corporations or other organizations are affiliated with it or have any other interest in it.

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Dated: September 27, 2017

/s/ Mary Ellen Signorille
Mary Ellen Signorille

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GLOSSARY

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AFR	Americans for Financial Reform
APA	Administrative Procedure Act
BICE	Best Interest Contract Exemption
CFA	Consumer Federation of America
Code	Internal Revenue Code
DOL	Department of Labor
DOL H'rg Tr.	Department of Labor Transcript of Aug. 12, 2015 Proceeding
ERISA	Employee Retirement Income Security Act
FIA	Fixed Index Annuities
Rule	Department of Labor's Fiduciary Rule
FINRA	Financial Industry Regulatory Authority
Gov't Appx.	Appellees' Supplemental Appendix
IALC	Indexed Annuity Leadership Council
IMO	Independent Marketing Organization
IRA	Individual Retirement Account
NAFA	National Association for Fixed Annuities
NAIC	National Association of Insurance Commissioners
NAIFA	National Association of Insurance and Financial Advisors

NELP	National Employment Law Project
NPRM	Notice of Proposed Rulemaking
PIABA	Public Investors Arbitration Bar Association
PTE	Prohibited Transaction Exemption
RIA	Regulatory Impact Analysis
SEC	Securities and Exchange Commission

INTERESTS OF AMICI CURIAE[1]

This brief is filed on behalf of seven nonprofit organizations that are deeply committed to enhancing the quality of advice that millions of Americans receive concerning investments in their retirement accounts.

AARP—with approximately 38 million members—is a nonprofit, nonpartisan organization dedicated to fulfilling the needs and representing the interests of people age fifty and older. AARP fights to protect older people's financial security, health, and well-being. AARP's charitable affiliate, AARP Foundation, creates and advances effective solutions that help low-income individuals fifty and older secure the essentials so that they do not fall into poverty during retirement. Through, among other things, participation as amici curiae in state and federal courts, AARP and AARP Foundation seek to increase the availability, security, equity, and adequacy of pension, health, and other employee benefits that countless members and older individuals receive or may be eligible to receive. A major priority has been to assist Americans in accumulating and effectively managing the assets they will need to supplement Social Security, so that they can maintain an adequate standard of living in retirement.

[1] Amici certify that no party or party's counsel authored this brief in whole or in part, or contributed money that was intended to fund the brief's preparation or submission, and further certifies that no person, other than amici, contributed money intended to prepare or submit this brief. Fed. R. App. P. 29(a)(4)(E). A motion for leave to file this brief has been filed simultaneously with this brief.

Americans for Financial Reform ("AFR") is a nonpartisan, nonprofit coalition of more than 200 consumers, investor, labor, civil rights, business, faith-based, and community groups. *See* AFR, *Coalition Members*, goo.gl/dxAYKT (last visited Sept. 12, 2017). AFR works to lay the foundation for a strong, stable, and ethical financial system—one that serves the economy and the nation as a whole. AFR engages actively in policy issues relating to securities regulation and investor protections.

Better Markets is a nonprofit, nonpartisan organization that promotes the public interest in the financial markets through comment letters, litigation, independent research, and public advocacy. It fights for reforms that create a stronger, safer financial system; promote the economic prosperity of all Americans; and protect individual investors from fraud, abuse, and conflicts of interest. Better Markets has filed hundreds of comment letters with the financial regulators and numerous briefs in federal court advocating for strong implementation of reforms in the securities, commodities, and credit markets. *See generally* Better Markets, goo.gl/sAHdpN (last visited Sept. 12, 2017) (including archive of comment letters and briefs).

Consumer Federation of America ("CFA") is a nonprofit association of more than 250 state, local, and national pro-consumer organizations, founded in 1968 to represent the consumer interest through research, advocacy, and education. More

information about CFA's membership is available at goo.gl/ST7e6W (last visited Sept. 12, 2017). For three decades, CFA has been a leading voice in advocating for stronger protections for individual investors. CFA policy in this area is focused on ensuring that investors have a choice of appropriate investments and service providers, the information necessary to make informed choices, protection against fraud and abuse, and effective recourse when they are the victims of wrongdoing.

The National Employment Law Project ("NELP") is a national nonprofit organization that for more than 45 years has advocated for policies and practices that promote economic opportunity and security for low-wage and unemployed workers. NELP's advocacy includes research, policy development, and litigation, including filing amicus curiae briefs in federal and state courts. To the extent low wageworkers have retirement savings that supplement social security at all, they have small-defined contribution plans or IRAs. These retirement vehicles require low-wage workers to make complex investment decisions that directly affect their quality of life in retirement. For that reason, many seek expert financial advice. Loopholes in prior regulations allowed important categories of financial advisers to operate with damaging conflicts of interest. No group of investors has been hurt more than low-wage workers, who—with their small savings—can least afford to absorb the losses. NELP has a deep understanding of the Rule, having closely followed its development and having participated in the rulemaking proceedings.

The Public Investors Arbitration Bar Association ("PIABA") is an international bar association whose members represent investors in disputes with the securities industry. The mission of PIABA is to promote the interests of the public investor in securities and commodities arbitration by protecting public investors from abuses in the arbitration process; making securities and commodities arbitration as just and fair as systematically possible; and creating a level playing field for the public investor in securities and commodities arbitration. PIABA members represent investors in court and arbitration who have received conflicted advice from investment advisers, securities brokers, and insurance brokers, oftentimes in connection with their retirement accounts, observing firsthand the harm that has resulted from the conflicted advice.

Amici believe that the Department of Labor's ("DOL") Fiduciary Rule ("Rule") protects individuals' retirement accounts and thus promotes retirement security. Amici are intimately familiar with the Rule's provisions and the exhaustive rulemaking process DOL followed to craft it.

INTRODUCTION AND SUMMARY OF ARGUMENT

The regulation of investment advice concerning tax-preferred retirement savings is a straightforward exercise of DOL's core delegated authority under the Employee Retirement Income Security Act ("ERISA") and the Internal Revenue Code ("Code"). Congress authorized DOL to define certain statutory terms related

to the statutes' coverage, including the definition of "investment advice." It also permitted DOL to create conditional exemptions from statutorily prohibited transactions. Over the years, DOL has repeatedly exercised its authority to define terms and create exemptions. The Fiduciary Rule and its related Exemptions are nothing more than a long overdue update of these definitions and exemptions to account for changes in retirement planning and to better advance the statutes' remedial purposes.

DOL's interpretation of the prohibited transaction exemption ("PTE") provisions of ERISA and the Code is, if anything, an even more straightforward application of delegated authority. In shaping the contours of fiduciary standards of care and loyalty under ERISA and the Code, Congress identified certain "prohibited transactions," each of which constitutes a per se breach of fiduciary duty. *See* 29 U.S.C. § 1106; 26 U.S.C. § 4975. But, Congress also delegated to the Secretary of Labor the authority to grant conditional or unconditional exemptions to the prohibited transactions. *See* 29 U.S.C § 1108; 26 U.S.C § 4975. Here, DOL created a conditional exemption known as the Best Interest Contract Exemption ("BICE"), precisely as authorized by Congress.

Appellant second-guesses DOL's decision to condition PTEs involving fixed index annuities ("FIA") on the terms of the BICE, as opposed to those of a less rigorously conditioned exemption available for fixed-rate annuities. DOL provided

fair notice that it was evaluating which PTE would be most appropriate for which type of annuity. DOL also performed a thorough study of the FIA market and determined that conflicts of interest there posed a severe risk to plan participants and beneficiaries, which existing state regulation failed to mitigate. DOL amply justified its decision that FIAs, like variable annuities, should be subject to the enhanced protections of the BICE.

ARGUMENT

I. DOL GAVE FAIR NOTICE THAT IT WAS CONSIDERING INCLUDING FIAS UNDER THE BICE.

At bottom, Appellant's complaint is that DOL should have asked a specific question concerning the placement of FIAs in the PTEs at issue. However, DOL's Notice of Proposed Rulemaking ("NPRM"), the extensive comments, and the hearing testimony conclusively demonstrate that all stakeholders had ample notice that DOL was evaluating which PTE would be most appropriate for FIAs—the BICE or PTE 84-24. Appellant calls this a "switcheroo," but more likely, Appellant simply dropped the ball by not commenting.

The NPRM expressly requested comment on different possible treatment of different types of annuities under the Rule. *See* App. Appx., vol. 5, at 1129. This meets the requirement of the Administrative Procedure Act ("APA") that the proposed rulemaking "fairly apprises interested persons of the subjects and issues the agency is considering." *Chem. Mfrs. Ass'n v. EPA*, 870 F.2d 177, 203 (5th Cir.

1989). Thus, "the notice need not specifically identify 'every precise proposal which [the agency] may ultimately adopt as a final rule,'" *id*. (citing *United Steelworkers of Am. v. Schuylkill Metals*, 828 F.2d 314, 317 (5th Cir. 1987)), so long as the final rule is a "logical outgrowth" of the proposal. *See Long Island Care at Home, Ltd. v. Coke*, 551 U.S. 158, 174 (2007) (interpreting "logical outgrowth" as a result that was reasonably foreseeable).

The NPRM expressly requested comment on:

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

See App. Appx., vol. 5, at 1129. As one industry commenter clearly understood, "[t]he [p]roposal specifically request[ed] comment on *which exemption, the BIC Exemption or a revised PTE 84-24, should apply* to different types of annuity products." App. Appx., vol. 7, at 1589 (emphasis added). DOL's express request for comment on the question at issue defeats any challenge to the adequacy of notice.

Stakeholders clearly understood that DOL was contemplating changes to the proposal, specifically which PTE would cover various types of annuities. Many stakeholders used the opportunity to file comments on the placement of FIAs

before and after the hearing. *See infra* nn.3-5. Several industry commenters explicitly supported the proposal to exempt FIAs under PTE 84-24, but not under the BICE. *E.g.*, App. Appx., vol. 7, at 1647[2] ("[W]e believe that the conditions of the Best Interest Contract Exemption (BICE) would be problematic for fixed annuities and would not offer any meaningful additional protections for sales of fixed annuities to IRA holders."); App. Appx., vol. 7, at 1634[3] (detailing objections subjecting FIAs to the BICE). Conversely, other commenters argued that the BICE should not apply to any annuities, including FIAs. *E.g.*, National Association of Insurance and Financial Advisors ("NAIFA"), Comments on Proposed Definition of Fiduciary Investment Advice at 21–24 (July 21, 2015),[4] goo.gl/QCGWQb ("PTE 84-24 should apply to all annuity products sold to all types of investors."); App. Appx., vol. 6, at 1532 ("***PTE 84-24 should continue to be the exemption applicable to all***

[2] IALC re-iterated its positions at the public hearing and in a subsequent comment letter dedicated *entirely* to the issue. *See* DOL Hr'g Tr. 904 (Aug. 12, 2015), goo.gl/yRPc2E; IALC, Comments on Proposed Rulemaking Definition of the Term "Fiduciary" etc. at 4 (Sept. 24, 2015), goo.gl/XASnFJ ("For the reasons discussed below, the new proposed Best Interest Contract Exemption (BICE) would not work in the context of any fixed annuity product, including an FIA.").

[3] *See also* NAFA, Comments on Conflict of Interest Rule etc. at 1–6 (Sept. 24, 2015), goo.gl/wTUz9n (arguing that "PTE 84-24 is the appropriate regulatory exemption for fixed annuities," including FIAs).

[4] *See also* NAIFA, Comments on Proposed Definition of Fiduciary Investment Advice etc. at 5 (Sept. 24, 2015), goo.gl/UkLrLR (stating that the annuity field will be "divided between those who have to comply with the far more onerous BIC exemption and those who can rely on a less burdensome PTE (*e.g.*, PTE 84-24)").

annuities and other insurance products.") (bold and italic emphasis in original); App. Appx., vol. 7, at 1598-1603 (arguing no annuity should be subject to the BICE to ensure a level playing field).

Others disagreed, arguing for a broader application of the BICE, including its application to FIAs. *E.g.*, Gov't Appx. 77 ("recommend[ing] that the BIC exemption apply to the sale of equity indexed annuities . . . ."); App. Appx., vol. 7, at 1673-1679 (arguing that all annuities—whether fixed, indexed, or variable—should be regulated under the BICE because the products raise similar concerns with conflicted compensation, and different standards would permit regulatory arbitrage); Gov't Appx. 20 (arguing that "compensation stemming from all annuities . . . should be permitted only through the Best Interest Contract Exemption."). Appellant's contention that the issue of the placement of FIAs was not in play has no basis in light of the NPRM itself and the comments submitted before and after DOL's hearing.

As the district court recognized, App. Appx., vol. 2, at 424-427 , this robust debate on whether FIAs should be subject to the BICE further demonstrates that the final Rule was the "logical outgrowth" of the proposed rule, *accord*, *Chamber of Commerce of the United States v. Hugler* ("*Chamber*"), 231 F. Supp. 3d 152, 184–86 (N.D. Tex. 2017) (finding it was "reasonably foreseeable" that DOL could put FIAs on the other side of the line); *Nat'l Ass'n for Fixed Annuities v. Perez*

("*NAFA*"), 217 F. Supp. 3d 1, 48 (D.D.C. 2016) (NAFA's reading of the proposed rule as not giving notice "is not tenable"), and, therefore, that DOL's notice was more than sufficient under the APA.

II. DOL FULFILLED ITS DUTIES UNDER THE APA BY ITS THOROUGH ANALYSIS AND DECISION-MAKING REGARDING THE TREATMENT OF FIXED INDEXED ANNUITIES (FIAS).

The APA's core requirement is that an agency must "examine the relevant data and articulate a satisfactory explanation for its action including a rational connection between the facts found and the choice made." *Encino Motorcars, LLC v. Navarro*, 136 S. Ct. 2117, 2125 (2016) (internal quotation marks omitted). The April 2016 extraordinarily thorough and well-supported Regulatory Impact Analysis for Final Rule and Exemptions, App. Appx., vols. 3-4 ("RIA"), and extensive accompanying analysis removes any doubt that DOL satisfied its obligations under the APA regarding the Rule's treatment of FIAs. This fully satisfied DOL's obligation to engage in reasoned decision-making and to consider the "relevant factors" and the "important aspect[s] of the problem." *Friends of the Bow v. Thompson*, 124 F.3d 1210, 1215 (10th Cir. 1997). Given the inadequacies in the state regulatory framework and the problematic features, sales practices, and compensation incentives associated with FIAs, described below, DOL acted reasonably in concluding that FIAs should be subject to the BICE. The district court correctly found that DOL's determination "about the complexity, risk, and

conflicts of interest associated with recommendations of variable annuity contracts, indexed annuity contracts and similar contracts" was supported by substantial evidence. App. Appx., vol. 2, at 414; *accord*, *Chamber*, 231 F. Supp. 3d at 186-88; *NAFA*, 217 F. Supp. 3d at 49–50.

A. DOL Reasonably Found That FIAs Are Not Benign Financial Products, But Instead Have Conflicts Similar To Variable Annuities.

The RIA provided an extensive analysis of the annuity market. *See* App. Appx., vol. 3, at 707, 779-802, 815-817, 820-824, 828-830, 832-833, 836-838. This included a review of the various products and their features, the distribution of various annuity products, the conflicts of interest that exist in the annuity market, and the harms to retirement savers that can result from those conflicts. While data limitations impeded the specific quantification of the losses that affect retirement savers who invest in annuities, DOL found nonetheless that there is "ample qualitative and in some cases empirical evidence that they occur and are large both in instance and on aggregate." *Id*. at 707. Thus, DOL provided direct evidence, as well as evidence related to mutual funds (which present analogous issues), that conflicts in the annuity market result in material harm to retirement investors and, therefore, demand the enhanced protections that the Rule provides.

The RIA demonstrated that sales-based incentives—across the financial services and insurance industries—drive behavior and encourage and reward

advisers for acting in ways that are detrimental to investors. *See id*. at 820, 829-830. Those incentives and conflicts exist to the same, or even a greater, extent in the annuities market as they do in the mutual fund market. DOL found that:

> various annuity products…involve similar or larger adviser conflicts [as compared to mutual funds], and these conflicts are often equally or more opaque. Many of these same products exhibit similar or greater degrees of complexity, magnifying both investors' need for good advice and their vulnerability to biased advice. As with mutual funds, advisers may steer investors to products that are inferior to, or costlier than, similar available products, or to excessively complex or costly product types when simpler, more affordable product types would be appropriate.

Id. at 707 (relying on Daniel Schwarcz & Peter Siegelman, *Insurance Agents in the 21st Century: The Problem of Biased Advice*, *in* RES. HANDBOOK ON THE ECON. OF INS. LAW 36 (Daniel Schwarcz & Peter Siegelman eds. (2015)) ("*Insurance Agents in the 21st Century*")). The authors of the cited text also consider it appropriate to analogize conflicts in the mutual fund space to conflicts in the insurance space, stating, "[w]hile not exactly on point, this literature is comparatively well developed and involves many of the same basic considerations as are at play in insurance markets." *Insurance Agents in the 21st Century*.[5]

[5] The performance of an investment product is reduced by the amount of commission, fees, and administrative expenses that are charged for that investment product. All else being equal, the higher these costs are, the lower the investment's value will be, regardless of how the costs are charged (whether directly or indirectly, or through a front-end commission, ongoing fee, or back-end surrender charge). *See* Stan Garrison Haithcock, *What Levels of Commission Do Agents Earn on Annuities?*, THE BALANCE (June 25, 2017), goo.gl/Pnj7mj; Patrick J. Collins,

DOL specifically considered the important distinguishing characteristics of fixed-rate annuities,[6] FIAs, and variable annuities; the distribution of these annuity products; the conflicts of interest that exist in the annuity market; and the harms to retirement savers that can result from those conflicts. According to the RIA, "public comments and other evidence demonstrate that these products are particularly complex, beset by adviser conflicts, and vulnerable to abuse." App. Appx., vol. 3, at 706.

In its analysis, DOL compellingly showed that FIAs share critical features with variable annuities, such as the allocation of investment risk, fees, and guaranteed optional benefits, that make them susceptible to similar conflicts and abuses, features that are not shared by fixed-rate annuities. App. Appx., vol. 3, at 821-822. DOL found that FIAs "are as complex as variable annuities, if not more complex." *Id*. at 820. For example, it found that insurers can transfer investment risks to FIA investors in many complex ways that resemble the transfer of risk to variable annuity investors. *See id*. at 821-822. For example, variable annuities can offer hundreds of subaccounts that expose clients to market risk, typically through

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Annuities and Retirement Income Planning, CFA Institute Research Foundation, 2 (Feb. 2016), goo.gl/fio6jM. Thus, the higher an annuity's commission, the worse the annuity product is likely to be for the investor and, at the same time, the stronger the incentive will be for the adviser to recommend the higher cost, lower value annuity product.

[6] A fixed rate annuity "offers 'a guaranteed level of return that will always provide a guaranteed and predictable level of income.'" *NAFA*, 217 F. Supp. 3d at 8.

mutual fund performance. *See id.* Similarly, FIAs expose clients to investment risk by crediting investors' accounts based on changes in a market index, excluding dividends. They foist risk onto investors in other ways as well, through a combination of complex and obscure factors such as participation rates, interest-rate caps, and spread/margin asset fees. *See id*. Worse, insurance companies generally reserve the power to unilaterally change terms and conditions to lower an FIA investor's effective return, leaving the investor with little or no recourse. These investment-oriented features differentiate FIAs from fixed-rate annuities, which provide guaranteed, specified rates of interest on premiums paid and whose terms and conditions regarding crediting criteria do not vary based on the self-interest of the insurance company.

Tellingly, the comments of insurers in the annuity market themselves support DOL's conclusion that variable annuities and FIAs share similar characteristics. For example, Allianz's comment detailed how the designs of these two products are converging. *See* App. Appx., vol. 7, 1602-1603. The comment described how FIAs can resemble variable annuities and how in fact Allianz Life Insurance Co. offers FIAs that blend features of variable annuities and vice versa, referring to one such product as "a variable annuity with index investment options." *Id*. Jackson National Life Insurance Co. echoed Allianz's comments describing how these product types have converged, stating, "[r]ecent changes to

the structures of fixed indexed annuities (FIAs) and variable annuities . . . have resulted in these products becoming remarkably similar." Gov't Appx. 88.

The shared complexity and opacity of these products fosters a dependence on professional advice, creating an environment in which conflicts of interest are more likely to thrive. The RIA cited to academic research contending that insurance "agents can inefficiently withhold information and distort consumer choices by providing misleading information or operating in their own self-interests." App. Appx., vol. 4, at 853 (citing *Insurance Agents in the 21st Century*). Insurance agents may engage in this conduct without any consequences, according to these researchers, because it is exceedingly difficult for consumers to ascertain the value of insurance products even after purchase. *See id*. Based on these considerations, DOL rightly determined that prudent and impartial advice, important to all investors, is even more crucial in safeguarding the best interests of investors in variable annuities and FIAs. *See* App. Appx., vol. 3, at 821, 838.

Furthermore, a wide range of commenters provided unequivocal feedback that, if variable annuities were subject to the more protective conditions under the BICE and FIAs were subject to the less protective conditions of PTE 84-24, there would be an incentive to shift sales to FIAs without regard to the best interests of the customer. Based on these considerations, DOL properly determined that these products should be subject to similar treatment, and that treatment should be under

the more protective conditions of the BICE. *See* App. Appx., vol. 4, at 982. Indeed, DOL found that:

> the conflicts of interest between insurance agents and consumers are relevant and applicable in the annuity market as well. If anything the potential harm from conflicts of interest would be larger in the annuity market because purchasers of annuities are often older individuals who are less sophisticated in financial matters than purchasers of commercial property-casualty insurance.

App. Appx., vol. 3, at 820.

The RIA collected specific examples of conflicts in the FIA context, including "an insurance broker [who] could be rewarded for steering customers toward insurers whose production goals they are approaching." *See id.* at 830. Moreover, when annuities are considered within the context of the broader range of investment products, a financial professional may have an incentive to recommend an annuity over other alternatives, such as mutual funds, because annuity commissions are often substantially higher than broker-dealers' mutual-fund or securities commissions. *See id.* at 829-830. Conflicts of interest are thus likely more pronounced in the annuity market than in the mutual-fund market. Furthermore, commissions are typically higher for selling more complex and opaque FIAs and variable annuities than simpler, more consumer-friendly fixed-rate annuities, thus increasing the incentives to recommend FIAs and variable annuities. *See* Stan Garrison Haithcock, *What Level of Commission Do Agents Earn on Annuities?*, THE BALANCE (June 25, 2017), goo.gl/Pnj7mj.

Moreover, DOL found that "the conflicts of interest in the annuity market can be even more detrimental than the mutual fund market." App. Appx., vol. 3, at 829. The RIA detailed how annuities sold on commission, and specifically FIAs, are associated with other product features that are detrimental to retirement savers, including substantial surrender charges that persist for years.[7] DOL provided evidence, for example, that annuities sold by an intermediary who receives a commission more often include surrender charges than annuities sold directly to customers. App. Appx., vol. 3, at 829. Moreover, the RIA further described how commissions in the annuity market create a misaligned incentive system and result in conflicts of interest between financial professionals and consumers. The RIA highlighted that, because many financial professionals are compensated entirely or primarily by commissions resulting from annuity sales, this creates an incentive to aggressively maximize sales of the highest-commission products. *See id.* at 830, 832. Such disadvantageous features of these products exacerbate conflicts of interest, encouraging and rewarding agents for recommending annuity products that are in the financial interest of agents, IMOs, and insurance companies—not

[7] Surrender charges effectively lock up a saver's money and make it costly to reverse the investment decision. *See* App. Appx., vol. 5, at 1149-1150. A survey of available FIAs shows products with surrender periods as long as 16 years and surrender charges as high as 20% of premiums. *See* American Equity Bonus Gold (July 14, 2016), goo.gl/iNuVNE. Surrender fees for the 10 top-selling indexed annuities in 2015 averaged 11% in the first year. *See* Fidelity Viewpoints, *Indexed annuities: Look before you leap* (Sept. 15, 2017), goo.gl/1pLe6K.

the best interest of retirement savers.

Appellant erroneously claims that "[t]he only significant difference between FIAs and fixed declared-rate annuities is the method for computing interest earnings credited" to the policies, Appellant's Brief ("App. Br.") 4, and further argues that this is "a distinction having no bearing on the Department's articulated concerns regarding conflicted sales advice." *Id.* at 41. These claims are false. In reality, an FIA's crediting mechanism creates a conflict of interest that can ultimately harm investors. Because insurance companies can manipulate how much is credited to an investor's account through the imposition of caps, participation rates, and spreads, and can unilaterally change terms and conditions to lower an investor's effective return, *see supra,* insurance companies can impose indirect and opaque costs that ultimately reduce investors' effective returns and transfer investment risk to the investor. But that ability to manipulate and vary effective returns and transfer investment risk to the investor is wholly absent with fixed-rate annuities, which provide guaranteed, specified rates of interest on premiums paid. DOL thus adduced evidence that the conflicts associated with FIAs are more acute than with fixed-rate annuities and, therefore, require stronger protections for retirement savers.

These intense conflicts of interest lead to high-pressure and abusive sales, as the RIA revealed. For example, a study by the Financial Planning Coalition on

older individuals' financial exploitation found that "over half of the [Certified Financial Planner] professional respondents . . . personally had worked with an older client who previously had been subject to unfair, deceptive or abusive practices. Of these, 76 percent reported financial exploitation that involved equity-indexed or variable annuities." App. Appx., vol. 3, at 830.

Given these factors, it was entirely reasonable for DOL to conclude that FIAs should be subject to the more protective exemptive conditions under the BICE and that IMOs should not be treated as financial institutions without first demonstrating they have an adequate supervisory mechanism in place to ensure compliance with the Rule.

B. DOL Reasonably Concluded That FIAs Require Additional Regulation To Protect Consumers From Potential Conflicted Advice.

Appellant erroneously claims that DOL's decision to subject FIAs to the BICE were arbitrary and capricious because DOL did not adequately consider the sufficiency of existing regulation in its decision-making. App. Br. 45–49. The district court agreed with DOL's explanation about the insufficiency of existing regulations given the changes in retirement planning and the investment market, the growth of these plans, and the shift of responsibility from professional plan asset managers to individual investors. App. Appx., vol. 2, at 445-447. The district court found it reasonable to subject FIAs to additional regulation considering

"FIAs are likely to involve complex fee arrangements that make conflicts of interest and other abuses difficult for consumers to discern," *id.*, and the court recognized the need to "protect consumers from [the] potential for conflicted advice," *id.* at 446; *accord, Chamber*, 231 F. Supp. 3d at 188–91; *NAFA*, 217 F. Supp. 3d at 50 (it "crafted the [BIC Exemption] so that it will work with, and compliment [*sic*], state insurance regulations.").

The RIA included a close examination of the fragmented regulatory landscape affecting the distribution of annuities. For example, it reviewed the lack of uniformity with regard to state insurance suitability regulations. *See* App. Appx., vol. 3, at 734-741, 809 (only thirty-five states have adopted the National Association of Insurance Commissioners ("NAIC") model regulation.). And despite Appellant's claim, App. Br. 47, that DOL unreasonably dismissed the state-based regulatory structure, the RIA cited to the Federal Insurance Office's Annual Report on the Insurance Industry, published in September 2015, which stated, "[a]s unprecedented numbers of seniors reach retirement age with increased longevity, and as life insurers continue to introduce more complex products tailored to consumer demand, the absence of national annuity suitability standards is increasingly problematic." App. Appx., vol. 3, at 740.

Even in states that have adopted the Model Suitability Regulation of the NAIC, the regulations do not adequately protect retirement investors against sales-

driven conflicts of interest. State insurance suitability rules resemble FINRA's suitability rules, which apply to broker-dealers' securities sales. *Id.* at 731-733, 737-741, 809. DOL provided compelling evidence that such standards, even after recent updates, provide retirement investors with inadequate protections from sales-driven conflicts of interest in the sale of insurance and securities. *See* App. Appx., vol. 3, at 734-741, 794, 807-809, 828-830, 836-836; vol. 4, at 980-984. Suitability rules allow the sale of the least-suitable among a wide range of "suitable" investments and function more like a "do not defraud" standard than a best-interest standard. Given that mutual funds and annuity contracts are similarly fraught with harmful conflicts of interest based on sales incentives (and that both types of products have been subject to similar regulatory frameworks), DOL appropriately concluded that retirement savers needed the enhanced protections offered under the Rule for both variable annuities and FIAs, along with securities.

The court found that DOL not only considered various comments concerning the state regulatory systems, but also met with the NAIC and reviewed model state insurance laws.[8] App. Appx., vol. 2, at 447. The court found that DOL

[8] The district court also rejected Appellant's argument that the DOL has the same obligation as the SEC does "to consider or determine whether an action is necessary or appropriate in the public interest . . . [and for] the protection of investors [and] whether the action will promote efficiency, competition, and capital formation." App. Appx., vol. 2, at 446 (quoting *Am. Equity Inv. Life Ins. Co. v. SEC*, 613 F.3d 166, 176-77 (D.C. Cir. 2010) (citing 15 U.S.C. § 77b(b))). The court found that "American Equity Investment has no persuasive value here"

agreed with comments urging enhanced retirement investor protection because "IRA owners need greater protections when investing in index annuities precisely because such products are not regulated securities." *Id.*

Consequently, the court found that DOL's rulemaking was supported by substantial evidence and did not violate the APA. App. Appx., vol. 2, at 438-439.

C. DOL Considered The Rule's Effects On Consumer Access And Reasonably Determined The Need To Protect Consumers From Conflicted Investment Advice Outweighed Any Such Possible Effects.

Although Appellant claims that DOL failed to consider the Rule's effects on both the distribution network for FIAs and consumer access to financial planning, App. Br. 49-53, in fact, DOL did exactly that, but reasonably rejected such effects as a justification for a lighter regulatory approach to FIAs. *See* App. Appx., vol. 4, at 877, 1005-1022. The district court was able to discern DOL's path in recognizing "the effects that the final rule would have on the industry's players but concluded that the need to protect consumers from conflicted investment advice outweighed those concerns," and found DOL's decision to be reasonable. App. Appx., vol. 2, at 454; *accord*, *Chamber*, 231 F. Supp. 3d at 192-193; *NAFA*, 217 F. Supp. 3d at 51–55. DOL analyzed the Rule's effects on various market participants, the products they sell, and how these effects, in turn, would affect

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because Appellant cited no "similar statutory" prerequisite cabining DOL's authority. *Id.* Nor could Appellant cite such a prerequisite in ERISA or the Code; there is none.

consumers. *See, e.g.*, App. Appx., vol. 3, at 736, 799-809, 842; vol. 4, at 936 & n.519, 952, 1008-1009. This fully satisfied DOL's obligation to engage in reasoned decision making and to consider the "relevant factors" and the "important aspect[s] of the problem." On balance, DOL determined that the industry's claims were overblown and that, while the Rule "may pose a particular challenge" to those businesses, including some insurers and mutual fund companies, "whose commission and other compensation structures have been highly variable and laden with more acute conflicts of interest," any temporary frictions in these markets "would be justified by the rule's intended long-term effects of greater market efficiency and a distributional outcome that favors retirement investors over the financial industry." *Id.* at 1006-1007. DOL reasoned that:

> Investors whose advisers and product providers are so affected also may experience some amount of disruption as markets adjust, and may incur some costs to find, acquire, and adjust to new services and products from the same or different vendors. These same investors, however, absent this final regulation and exemptions, would likely have been the most adversely affected by adviser conflicts, and therefore may stand to gain the most from reform, notwithstanding near-term disruptions.

Id. at 1007. DOL further explained that, "the same frictions that present challenges for some businesses may enhance opportunities for others," as new market

competition would promote innovation in both product lines and business models.[9] *Id*.

Appellant's real grievance here is not that DOL failed to consider the costs and benefits of the Rule—by any measure, it clearly did—but that DOL failed to guarantee the continued viability and profitability of Appellant's preferred distribution model. But DOL has no duty to ensure that a particular business model survives regulation if that business model violates ERISA and cannot meet the exemptive conditions that are necessary for the protection of retirement savers. On the contrary, DOL has an affirmative duty to implement Congress's statutory mandates by eliminating such business practices or conditioning them on compliance with sufficiently protective conditions.

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[9] This innovation has already begun. Many companies that offer FIAs have or will supplement their existing menu of commission-based products with new fee-based alternatives. *E.g.*, Cyril Tuohy, *DOL Rule Will Lead To Simplification Of Many Retirement Products*, INSURANCENEWSNET.COM (Sept. 27, 2016), goo.gl/yCUgBx; Press Release, Allianz, *Allianz Life Launches New Retirement Foundation ADV Annuity* (Feb.7, 2017), goo.gl/N9ryPp; Press Release, Nationwide, *Nationwide Announces Its First Fee-based Fixed Indexed Annuity* (July 11, 2017), goo.gl/P7r2ic; Press Release, Great American Life Insurance Company, *Great American Life's Fee-Based Annuity Now Available Through Commonwealth Financial Network* (March 1, 2017), goo.gl/gJEJFG; Press Release, Lincoln Financial Group, *Lincoln Financial Group Broadens Its Suite of Guaranteed Lifetime Income Solutions with New Fee-Based Options* (Feb.13, 2017), goo.gl/UFgVoz; Press Release, Pacific Life, *Pacific Life's New Fixed Indexed Annuity with Simple Interest-Crediting Options and Shorter Withdrawal Charge Schedules* (July 17, 2017), goo.gl/qTv5VY; Press Release, Symetra, *Symetra Introduces New Fee-Based Fixed Indexed Annuities—Symetra Advisory Edge and Symetra Advisory Income Edge* (July 24, 2017), goo.gl/cHnbT2.

In reality, DOL made very generous accommodations to the FIA industry by allowing commission-based compensation in the sale of FIAs to continue notwithstanding ERISA's prohibitions. Although the BICE requires a Financial Institution[10] to take on a critical supervisory role to ensure that advisers are complying with the exemption's conditions, and the Rule does not deem IMOs as Financial Institutions, the DOL did provide several paths for IMOs and other insurance intermediaries to satisfy the conditions of the BICE. For example, they can seek to become Financial Institutions after providing evidence to DOL that they are willing and able to effectively exercise supervisory authority over their advisers or the advisers they contract with, thus ensuring their adherence to the Impartial Conduct Standards.[11] Alternatively, they can acquire or contract with an entity that already qualifies as a Financial Institution and is willing to take on that critical supervisory role to ensure compliance with the exemption's conditions. Several

[10] The BICE defines a "Financial Institution" as an entity that employs or retains the Adviser and is registered as an investment adviser under the Investment Advisers Act of 1940 or under the state laws in which the adviser maintains its principal office and place of business; or is a bank or similar financial institution supervised by federal or state laws or a savings association. Best Interest Contract Exemption; Correction, 81 Fed. Reg. 44,773, 44,783 (July 11, 2016) (to be codified at 29 C.F.R. pt. 2550) , goo.gl/VzyQ2C.

[11] Impartial Conduct Standards are defined as "fundamental obligations of fair dealing and fiduciary conduct, and include obligations to act in the customer's best interest, avoid misleading statements, and receive no more than reasonable compensation." Definition of the Term ''Fiduciary''; Conflict of Interest Rule—Retirement Investment Advice, 81 Fed. Reg. 20,946, 20,991 (Apr. 8, 2016) (to be codified at 29 C.F.R. pts. 2509, 2510, and 2550), goo.gl/aifpbV.

IMOs have done just that. Annexus launched a Broker-Dealer. *See* Greg Iacurci, *Indexed annuity distributors weigh launching B-Ds due to DOL fiduciary rule*, INVESTMENT NEWS (June 23, 2016), goo.gl/UBSUi2 (detailing that distribution networks representing independent insurance agents have plans to launch broker-dealers to continue selling FIAs in retirement accounts under the Rule). Similarly, AmeriLife launched a Registered Investment Adviser, "so that producers would have another qualified financial institution to do business through." *See* Warren S. Hersch, *AmeriLife Faces DOL Rule With Two-Track Strategy*, THINKADVISOR (Apr. 14, 2017), goo.gl/qgtD8X. And the Ohlson Group has "engaged one of the leading Financial Institutions in the industry" to take on a supervisory role. Press Release, *Ohlson Group to introduce AssessBest, the advisor's answer to DOL/Fiduciary Rule*, INSURANCENEWSNET.COM, goo.gl/iC6YQA. Indeed, the most innovative and compliance-minded firms are demonstrating that compliance is, in fact, possible. Consequently, DOL was not required to go to further extremes to protect the FIA industry.

CONCLUSION

For the foregoing reasons, the Court should affirm the district court's decision in all respects.

Dated: September 27, 2017

Sincerely,

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CERTIFICATE OF COMPLIANCE

This brief complies with type-volume limitation of Fed. R. App. P. 32(a)(7)(B) because this brief contains 6,295 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

This brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because this brief has been prepared in a proportionally spaced typeface using Microsoft Word 2010 in 14 point font.

Dated: September 27, 2017

/s/ Mary Ellen Signorille
Mary Ellen Signorille

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Pursuant to this Court's MC/ECF User's Manual, I hereby certify that: (i) all required privacy redactions have been made; (ii) the hard copies that have been submitted to the Clerk's Office are exact copies of the ECF filing; and (iii) the ECF submission was scanned for viruses with the most recent version of Symantec Endpoint Protection and, according to that commercial virus scanning program, is free of viruses.

Dated: September 27, 2017

Respectfully submitted,

/s/ Mary Ellen Signorille
Mary Ellen Signorille

CERTIFICATE OF SERVICE

I hereby certify that on September 27, 2017, the foregoing Brief of Amici Curiae AARP, AARP Foundation, Americans for Financial Reform, Better Markets, Consumer Federation of America, National Employment Law Project and Public Investors Arbitration Bar Association in Support of Defendants-Appellees was electronically filed with the Clerk of the Court for the United States Court of Appeals for the Tenth Circuit using the appellate CM/ECF system. I certify that all participants in the case are registered CM/ECF users and that service will be accomplished by the CM/ECF system.

Dated: September 27, 2017

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