The Asset Management Industry
SERVING INDIVIDUAL INVESTORS
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Two Courts Stay Effective Date of DOL Fiduciary Rulemaking

[35794]

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TO: ICI Members
Pension Committee
Pension Operations Advisory Committee SUBJECTS: Pension
Tax RE: Two Courts Stay Effective Date of DOL Fiduciary Rulemaking

Two courts have granted stays in lawsuits against the Department of Labor (DOL) regarding its regulatory package on fiduciary investment advice ("2024 Fiduciary Rulemaking").[1] On July 25, 2024, the US District Court for the Eastern District of Texas in a lawsuit brought by the Federation of Americans for Consumer Choice (FACC) granted a stay (until further order of the court) of the effective date of DOL's revised definition of an investment advice fiduciary (Definition) and amended prohibited transaction exemption (PTE) 84-24.[2] The following day, July 26, 2024, the US District Court for the Northern District of Texas in a separate lawsuit brought by the American Council of Life Insurers (ACLI) and other parties granted a stay (for the pendency of the lawsuit and any appeal) of the effective date of DOL's entire 2024 Fiduciary Rulemaking (including PTE 2020-02).[3] Both decisions are attached.

As a consequence of these two decisions, the entire 2024 Fiduciary Rulemaking is on hold as to all parties (not just the parties to the lawsuits) until the resolution of the ACLI lawsuit, and the Definition and PTE 84-24 will remain on hold if the FACC lawsuit is later resolved (or the FACC stay is lifted by the FACC court)—unless either stay is successfully appealed. It is worth noting that both courts expressed significant doubts as to DOL's chances of successfully defending the rulemaking. Pending ultimate resolution of the lawsuits, the regulatory landscape effectively is reset to where it was before the 2024 fiduciary rulemaking. The 5-part test is the operative test for whether a party is an investment advice fiduciary.[4] Moreover, PTE 2020-02 and the various other PTEs that parties have long used continue to be available for advice in their pre-amendment form. However, this also means that certain favorable changes to PTE 2020-02, such as the expanded relief for principal trades and extension to robo-advice, will not take effect for now.

We provide more detail below on the stay orders.

FACC v. DOL Lawsuit

Background

On May 2, 2024, FACC along with several Texas independent insurance agents filed suit against DOL in federal court in the Eastern District of Texas. The plaintiffs are insurance agents who sell annuities and other products to clients rolling assets over from an employer-provided retirement plan, such as a 401(k) plan, to an IRA. The plaintiffs allege that DOL exceeded its authority under ERISA, the Internal Revenue Code (Code), and the Administrative Procedures Act (APA) in promulgating the Definition and PTE 84-24, and that the Definition and PTE 84-24 violate the APA because they are contrary to law and are arbitrary, capricious, and irreconcilable with the text of ERISA and the Code. Plaintiffs argue that the Definition and PTE 84-24 conflict with ERISA by imposing ERISA fiduciary status on them merely for complying with state insurance laws when dealing with a participant in an ERISA plan or with an IRA owner. Plaintiffs sought a stay of the effective date of the Definition and of PTE 84-24, or alternatively a preliminary injunction enjoying DOL from enforcing the Definition and PTE 84-24 while the lawsuit proceeds.

Order Granting Stay

The court in its order granting a stay found (for purposes of granting a stay) that the Definition and PTE 84-24 are contrary to the Fifth Circuit's 2018 decision in Chamber of Commerce v. DOL which vacated DOL's 2016 fiduciary rulemaking.[5] The court characterized DOL's argument as essentially asserting that Chamber is wrong. However, as the court observed, this is an argument to be considered by the en banc Fifth Circuit or the US Supreme Court—and not by the District Court, which is bound by Chamber as it is part of the Fifth Circuit.[6]

Looking to the four factors for granting equitable relief under the APA, namely the plaintiffs' likelihood of success on the merits, the threat of irreparable harm without a stay, whether other parties would be irreparably harmed by a stay, and the public interest; the court found for the plaintiffs in all instances. The court found that the plaintiffs are likely to succeed on the merits of their claim, and that "Defendants are wrong" in asserting that the Definition and PTE 84-24 are narrower in scope than the vacated 2016 fiduciary rulemaking and also are consistent with the Chamber court's conclusion that ERISA is only intended to reach advice relationships involving "trust and confidence." The court reached this conclusion in light of the US Supreme Court's recent Loper Bright decision, which rejected Chevron deference; rather, a court should no longer defer to an agency's interpretation of a statute and instead should decide for itself whether a law means what an agency says it means.[7] The court's conclusion also was informed by the concept that a statute's meaning is fixed at the time the statute is enacted.[8] Congress looked to the common-law definition of fiduciary status when enacting ERISA.

The court also rejected DOL's interpretation of the language of ERISA section 3(21), which states (in relevant part) that to be an investment advice fiduciary one must "render[] investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or ha[ve] any authority or responsibility to do so…" (emphasis added). The court found that the Definition improperly equates receiving a fee or other compensation that would not have been paid but for the recommended transaction as a fee or other compensation under section 3(21). The court found that this interpretation ignores the requirement in ERISA that the fee be paid for advice—and not for a sale—in order for a professional to be an investment advice fiduciary under ERISA.[9] As Chamber

held, section 3(21) uses terms from the financial services industry and recognizes the distinction between investment advisers who are paid for their advice, on the one hand, and stockbroker and insurance agents who are compensated only for completing sales.[10] Recommending a product (as stockbrokers and insurance agents may do as part of a sale) is not enough—the fee must be for the advice, and not for the sale.

The Definition and PTE 84-24 also fail to pass muster in treating one-time recommendations to roll over assets from an ERISA Title I plan to an ERISA Title II plan (i.e., an IRA) as fiduciary investment advice. Looking to Chamber, the court observed that contrary to DOL's assertions, its regulatory authority under Title II is limited. Among other things, Title II does not authorize DOL to supervise financial service providers to IRAs or create public or private rights of action for violations of Title II, and it does not subject fiduciaries to Title II plans (i.e., IRAs) to duties of loyalty or prudence. In expanding the Definition to cover IRA service providers and then imposing Title I fiduciary duties on them as a condition of receiving commissions, the Definition and PTE 84-24 exceed DOL's statutory authority.

DOL also acted arbitrarily and capriciously in amending PTE 84-24. Among other things, notwithstanding DOL's protestations to the contrary, the court found that the amendments to PTE 84-24 create a new private right of action for retirement investors as against advisors, brokers, and agents. The imposition of impartial conduct standards on these parties as part of PTE 84-24 impose on them "novel and extensive duties and liabilities" that expose them to breach of fiduciary duty liability and the same private rights of action impermissibly included in the 2016 fiduciary rulemaking.[11]

Plaintiffs would be irreparably harmed were a stay not granted, while DOL would not be so harmed were a stay granted. As such, the public interest would be served through the grant of a stay. The court did not evaluate the veracity of plaintiffs' alleged irreparable injury claims, as DOL did not challenge these assertions. Additionally, because plaintiffs alleged significant and concrete harms were a stay not granted, while the DOL's claimed harms are—as the court found—"less substantial and vaguely defined—and are based on a clear misreading of ERISA and Chamber," the balance of equities favors granting a stay. Moreover, because the Definition and PTE 84-24 likely violate the law and exceed the scope of DOL's authority, the public interest is served by granting a stay

The court also determined that a global stay, as opposed to one limited to the parties to the action, was warranted. The Definition and PTE 84-24 likely are unlawful as to other similarly situated parties in the same manner as they are for the plaintiffs. Additionally, DOL in promulgating the Definition and PTE 84-24 stated that it was seeking to establish a uniform definition of fiduciary investment advice. The interconnected nature of the financial services industry further argued for relief not only for plaintiffs but also for their partners and counterparties.

ACLI v. DOL Lawsuit

Background

ACLI and eight other parties[12] filed suit against DOL in the Northern District of Texas on May 24, 2024. In addition to arguing that the entire 2024 Fiduciary Rulemaking is contrary to law and arbitrary and capricious under the APA, the plaintiffs also assert that the 2024 Fiduciary Rulemaking violates the First Amendment as it applies to truthful commercial speech by financial salespersons by imposing unjustified content-based burdens on sales speech and by unlawfully compelling speech. Plaintiffs also allege, among other things, that

DOL's expansion of fiduciary status is contrary to law and exceeds DOL's statutory jurisdiction in that it redefines all sales speech as fiduciary speech, transforms one-time commercial transactions into fiduciary relationships, precludes parties from structuring their relationships as non-fiduciary through clear contractual language, embodies a standard that is an unlawful end-run around the Chamber decision, conflicts with ERISA's requirement that there be advice for a fee, and ignores the differences in DOL's authority over Title I versus Title II plans.

Order Granting Stay

The court granted the plaintiffs' motion for a stay and denied their motion for a preliminary injunction (which would be unnecessary due to the stay of the effective date). As noted above, unlike the FACC Stay—which applies only to the definition of an investment advice fiduciary and PTE 84-24—the ACLI Stay applies to all aspects of the 2024 Fiduciary Rulemaking. As a threshold matter, the court "agree[d] with and fully incorporate[d]" the FACC court's analysis as part of its decision. Among other things, the court echoed the FACC court's criticism of DOL for largely ignoring the Fifth Circuit's 2018 decision in Chamber, describing DOL's arguments as "nothing more than an attempt to relitigate the Chamber decision."[13]

The court evaluated the same four factors as the FACC court for granting equitable relief under the APA, focusing on the aspects of the 2024 Fiduciary Rulemaking not addressed by the FACC court—the amendments to PTEs 2020-02, 75-1, 77-4, 80-83, 83-1, and 86-128.

The court stated that "[p]laintiffs are virtually certain to succeed on the merits,"[14] and that Chamber "unambiguously forecloses all of Defendants' arguments."[15] The court forcefully rejected DOL's assertion that fiduciary status under ERISA is a functional definition, characterizing DOL's arguments on this point as "devoid of merit." Rather, ERISA restricts an investment advice fiduciary to a common law understanding of the term; "DOL may not regulate beyond this common law standard."[16]

The court expanded on the FACC court's discussion of a substantial threat of irreparable harm, detailing some of the costs plaintiffs allege. As in the FACC suit, DOL did not dispute plaintiffs' demonstrated irreparable injury. The court nonetheless noted that many of plaintiffs' costs are not recoverable, such as costs to overhaul supervision systems to comply with PTE 84-24, training, and needed technology upgrades. In noting that DOL did "not "sufficiently identify any countervailing hardship" to argue against a stay, the court observed that "the six years from the vacatur of the 2016 Rule to now do not demonstrate a newly pressing need for the Rule to take effect immediately."[17]

As did the FACC court, the court declined to limit relief to the parties to the lawsuit, observing among other things the interconnected nature of the retirement advice industry and DOL's goal of establishing a uniform definition for all parties providing investment advice to retirement investors under Title I and Title II. As the 2024 Fiduciary Rulemaking "is almost certainly unlawful for a broad class of investment professional in the industry," a stay not limited to the parties to the action makes sense.[18] The court also rejected a potential remand of the 2024 Fiduciary Rulemaking to DOL. The court found that remand would be both inefficient and a potential waste of judicial resources in light of the court's finding that plaintiffs are "virtually certain to succeed on their claims that the Rule exceeds DOL's statutory authority."[19]

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Notes

[1] For a summary of the 2024 Fiduciary Rulemaking Package, see ICI Memorandum no. 35699, dated May 3, 2024, available at https://www.ici.org/memo35699.

[2] *Federation of Americans for Consumer Choice* v. DOL, No. 6:24-cv-163-JDK, Order on Motion for Stay (E.D. Tx. July 25, 2024) ("FACC Stay"). For a discussion of this lawsuit, see ICI Memorandum no. 35730, dated June 3, 2024, available at https://www.ici.org/memo35730.

[3] *ACLI v. DOL*, No. 4:24-cv-00482-O, Order on Motion for Stay and Preliminary Injunction (N.D. Tx July 26, 2024) ("ACLI Stay"). For a discussion of this lawsuit, see ICI Memorandum no. 35730, dated June 3, 2024, available at https://www.ici.org/memo35730

[4] As a reminder, two federal courts have issued rulings in recent years interpreting the 5-part test in the context of rollover recommendations, disagreeing with DOL interpretations set forth in the preamble to PTE 2020-02 and associated FAQ guidance. For a discussion of those rulings, see ICI Memorandum no. 35053, dated March 1, 2023, available at https://www.ici.org/memo35053.

[5] Chamber of Commerce v. DOL, 885 F.3d 360 (5th Cir. 2018) ("Chamber"). See ICI Memorandum no. 31137, dated March 16, 2018, available at https://www.ici.org/memo31137.

[6] FACC Stay, Slip Op. p.2.

[7] Loper Bright Enters. v. Raimondo, 144 S. Ct. 2244, 2262 (2024) (overruling Chevron U.S.A. Inc. v. Nat. Res. Def. Council, Inc., 467 U.S. 837 (1984)).

[8] FACC Stay, Slip Op. p.23 (citing Loper Bright and other cases).

[9] FACC Stay, Slip Op. p.27.

[10] Id.

[11] See FACC Stay, Slip Op. p.35.

[12] The eight other original plaintiffs, all of whom are Texas-based or national associations that represent life insurance companies, insurance agents, brokers, and distributors who issue, market, and sell insurance and securities products, including annuities, to retirement savers, are the National Association of Insurance and Financial Advisors (NAIFA)-Fort Worth, NAIFA-Dallas, NAIFA-Pineywoods of East Texas, NAIFA-Texas, NAIFA, the National Association for Fixed Annuities, the Insured Retirement Institute, and Finseca. On July 1, 2024, the court granted the Financial Services Institute and Securities Industry and Financial Markets Association's motion to intervene as plaintiffs.

[13] ACLI Stay, Slip Op. p.9.

[14] Id. p.7.

[15] Id. p.9.

[16] Id. p.9.

[17] Id. p.14.

[18] Id. p.15.

[19] Id. p.16.
