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How intense will the DOL's fiduciary rule defense be? It depends on the election.

By BRIAN CROCE

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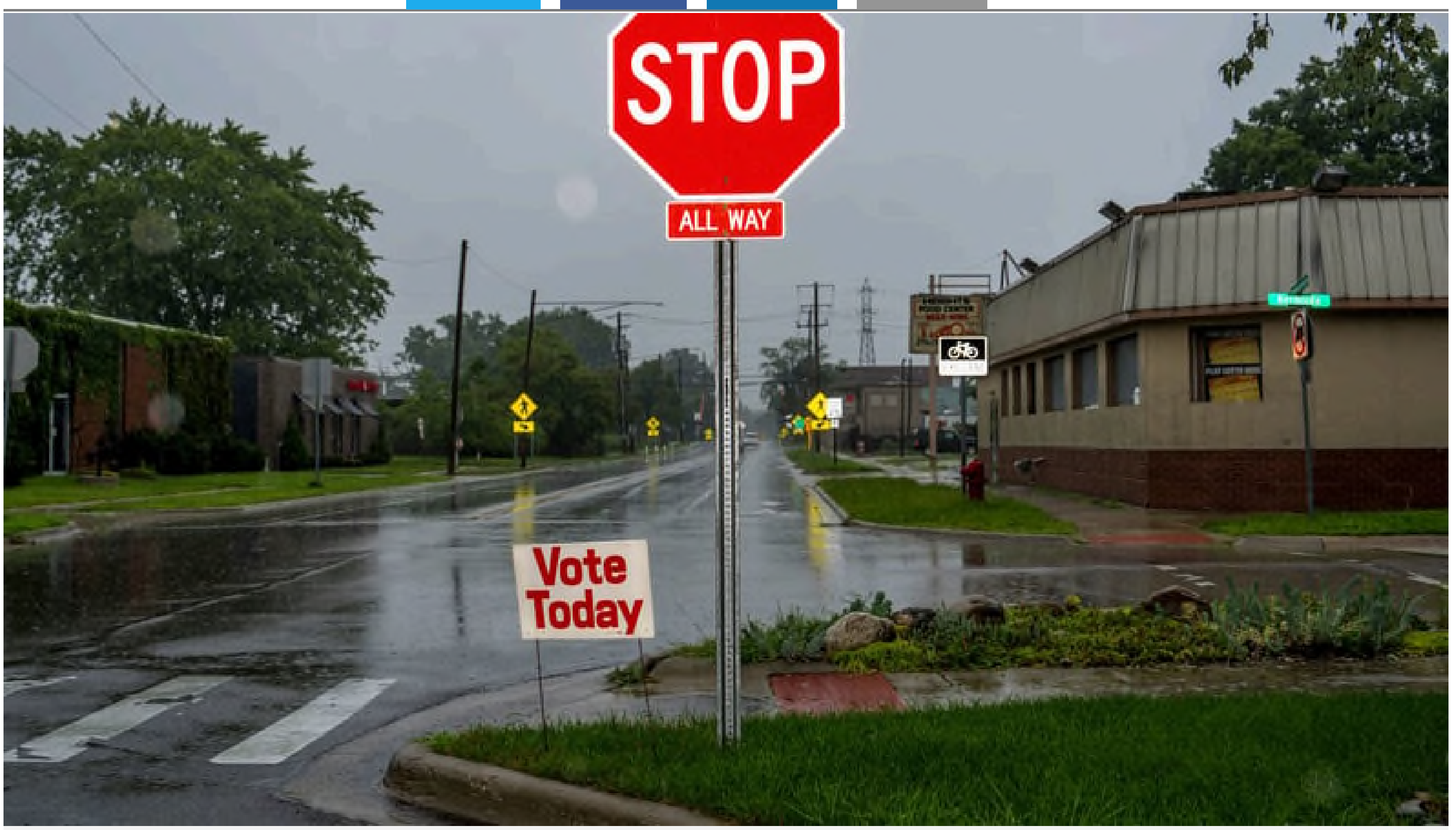

Nic Antaya/Bloomberg

The Department of Labor's fiduciary investment advice rule is facing a tough challenge in court, and the outcome of the presidential election will likely determine how vigorously the department gets to defend its case, legal experts said.

"If Donald Trump is elected president, it is entirely possible that there would be a repeat of what occurred in 2018," said Marcia S. Wagner, founder and managing partner of The Wagner Law Group.

Wagner was referencing a lawsuit brought against a 2016 Obama-era rule that broadened the definition of a person or entity taking on fiduciary responsibilities and replaced the five-part test that determines when someone is an investment advice fiduciary under ERISA. The 2016 rule, which swept up virtually any recommendation to a retirement investor, was struck down in 2018 by a three-judge panel at the 5th U.S. Circuit Court of Appeals in New Orleans.

The Trump administration, which took office in January 2017, allowed the Justice Department to defend the rule before the 5th Circuit in July 2017 oral arguments, but after the panel ruled against the Labor Department the following year, the administration elected not to appeal the decision and the fiduciary rule died.

In April, under the Biden administration, the Labor Department finalized the Retirement Security Rule, which, among other things, changed the five-part test so that one-time advice, such as rollovers to IRAs or annuity purchases, must be in an investor's best interest.

Department officials have said the rule is needed to better protect retirement savers and is more narrowly tailored than the 2016 rule.

Insurance and annuity groups disagree and have challenged the rule in two separate lawsuits. Two District Court judges in July each favored the plaintiffs' arguments and stopped implementation of the rule, which was slated to take effect in September.

In legal filings last month, the department said it would appeal the two District Court rulings in the 5th Circuit.

What a Trump administration would do

Michael L. Hadley, a partner at Davis & Harman, said the legal process could take years to play out as the two sides could appeal a decision they don't like all the way to the Supreme Court.

If the 5th Circuit upholds the department's authority to adopt the Retirement Security Rule, the parties challenging the rule would seek review by the Supreme Court but a Trump administration's Department of Labor might not seek to defend its statutory authority, according to Wagner.

Moreover, Hadley agrees that if Trump wins a second term, his administration wouldn't appeal any decision that goes against the department and may even cease its defense before a decision is rendered or arguments are heard.

"Our view is that a Trump administration is likely to take a very similar approach to the fiduciary rule that was taken during the first Trump administration," he said. "They would not continue to fight the litigation and would address the fallout through FAQs and a revision to the prohibited transaction exemption."

Under the Trump administration in 2020, the department issued PTE 2020-02, an exemption that permits investment advice fiduciaries to receive compensation for more types of guidance that are otherwise prohibited under ERISA, like rollover recommendations, so long as they comply with the exemption's conditions, which include care and loyalty obligations and conflict-of-interest mitigation.

The newly released Retirement Security Rule amended PTE 2020-02 and PTE 84-24, an exemption that impacts independent insurance agents making recommendations, such as annuities sales.

If the 5th Circuit rules against the department, a second Trump administration would likely be of the view that the guidance presented in PTE 2020-02 was sufficient, Wagner said.

What a Harris administration would do

On the flip side, if Vice President Kamala Harris were to win, her administration would seek reconsideration of an adverse 5th Circuit decision, and if the request for rehearing were denied, then it would seek review by the Supreme Court, Wagner said.

Similarly, Hadley added, “I would assume a Harris administration would seek to defend the rule until ran out of opportunities to do so.”

If a court vacates the rule and a Harris administration is out of avenues to appeal, Hadley said it would likely continue its efforts to apply the rule’s standards in some way, depending on the constraints handed down by the court’s decision. In that case, a Harris administration could issue further guidance, like frequently asked questions, step up enforcement in the area, or even take another shot at amending the regulation in a way they think is consistent with whatever the courts say, according to Hadley.

“Our assumption is there’s a good likelihood a Harris administration would continue to push these efforts,” he added.

If the 5th Circuit or Supreme Court invalidate the rule, Wagner said she doubts that a Harris administration or future Democratic administration would make another attempt to draft a rule defining investment advice fiduciaries.

“The only way to achieve the objectives sought by the Department of Labor in the Retirement Security Rule may be by congressional legislation, and regardless of who is the victor in the presidential election, it is unlikely that such legislation could be enacted in a closely divided Congress,” Wagner said.

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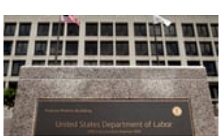

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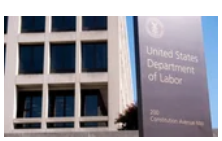

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