Is (or Isn't) Time Running Out for the Fiduciary Rule?

By Kerry Pechter *Thu, Feb 9, 2017*

Three benefits attorneys told RIJ this week that the DOL's fiduciary rule became effective last June, and that it may be hard to stop the rule--or even delay the April 10 applicability date--without another lengthy review and public comment process.

Time may not be running out on the Department of Labor's fiduciary rule as quickly as first assumed when the Trump administration issued its February 3 memorandum calling for a review of the rule, which requires that advisors on retirement accounts put their clients' interests ahead of profits.

A Dallas federal judge yesterday dismissed industry objections to the DOL rule in an 81-page ruling, after ignoring administration requests to postpone the issuance of her decision. Lawyers also pointed out to *RIJ* this week that the DOL rule has been legally binding since last June, and therefore may not be easily cast aside.

There's still the question of whether the rule's April 10, 2017 "applicability" date will be pushed back. Several ERISA lawyers believe it will be. President Trump's final memorandum on the rule did not specify a delay; it merely said that the DOL would take action to rescind or revise the rule if it "created burdensome legal costs for financial services providers" that might, in turn, be passed along to investors.

The administration seems determined to delay the applicability date while it decides how to confront the rule, however. On February 3, acting DOL secretary Edward Hugler said in a press release, "The DOL will now consider its legal options to delay the applicability of the date as we comply with the President's memorandum." The nominee for Secretary of Labor, Andrew Puzder, hasn't yet been confirmed.

Could the delay be delayed?

But would the administration need to hold a comment period before it could call a time-out on the applicability date? Yes, said Micah Hauptman, financial services counsel at the Consumer Federation of America, in a recent interview with Bloomberg BNA.

A formal rulemaking process would be the "most conservative" way of delaying the rule through regulation, Hauptman said. “That requires saying, ‘We disagree with the findings and the overall rulemaking of the previous administration, and here’s why,’” Hauptman said. “They would have to do it through reasoned decision-making and analysis based on all the relevant facts.”

Hauptman, whose group supports the fiduciary rule, said that a formal rulemaking process would be necessary because the rule is already *in effect*, even if it doesn’t apply until April 10 of this year. The way the law was written, he said, it became effective shortly after it was promulgated in the spring of 2016. The fact that the industry had an extra year to comply would not change that, apparently.

Even “if they’re changing the applicability date, we still think it would require notice and comment, because the rule is already effective,” Hauptman said. “The rule survived a congressional review act challenge and went into effect last June. That’s a widely recognized fact, not my opinion.”

Hauptman pointed to an **announcement** in the Federal Register on April 8, 2016, that the rule became effective on June 7, 2016, and that the applicability date was set for April 10, 2017 as a way to give financial services firms more time to adapt their processes and procedures to comply with the rule, such as creating new training programs and retooling technology for new kinds of reporting.

“The DOL rule has long been effective—no real dispute there,” said Mercer Bullard, a University of Mississippi law professor who gave Congressional testimony in favor of the rule last year. “It’s also hard to imagine a legal avenue by which the implementation date could be moved because that is an amendment to the rule. I certainly hope that the DOL will be sued if it violates the Administrative Procedure Act, but that’s a function who can afford to bring the case.”

“The fact that the rule is effective is very meaningful. This gives the proponents of the survival of the rule a lot of ammunition. This rule went into effect on June 7, 2016. Under the Congressional Review Act, Congress tried to overturn it and couldn’t. But the DOL delayed applicability,” ERISA attorney Marcia Wagner told *RIJ* yesterday.

“This matters because the DOL under the Administrative Procedure Act can’t change the rule without engaging in the regulatory process,” she added. “That can take a year. You have to write the new regulations and get public comment. The public comment has to come back. It’s really a long process. I don’t know how you do that before April 10. That may be why the proposed draft of the [Trump] memorandum had a 180-day delay written into it, but the final draft did not."

A 'slam dunk' to justify rescission?

Others assume that a delay will be announced very soon. The law firm of Drinker Biddle published an alert this week saying, "We expect an announcement, possibly within a matter of days, that steps are being taken to delay the April 10 applicability date… Assuming that the applicability date is delayed, and that the delay survives potential legal challenges, the consequences will be as follows:

- The applicability date will likely be delayed, either immediately or through multiple subsequent steps, for six months or even a year. As a result, service providers to retirement plans and IRAs will likely not need to comply with the Fiduciary Rules on April 10.
- Instead, those service providers will be required to comply with the currently applicable fiduciary regulation and existing prohibited transaction exemptions (the "old" rules).

In a comment circulated to his clients, advisor Philip Chao wrote this week, "We suspect the DOL will soon trigger a delay to the application date of the new law by six months or longer depending on the amount of time the DOL expects to complete the study. In the meantime, the Fiduciary Rule will not become applicable.

"We expect the main portion of the rule to remain intact and the more controversial and administratively cumbersome portion to be revised. Lobbyists will again work overtime to defeat or reshape the Fiduciary Rule."

Once that process begins, according to ERISA attorney Jason C. Roberts of the Pension Resource Institute, it will be a "slam dunk" to show that the rule is inconsistent with Trump administration policies because it fails one of the three tests described in Trump's February 3 memorandum.

That test asks "whether the Fiduciary Duty Rule is likely to cause an increase in litigation, and an increase in the prices that investors and retirees must pay to gain access to retirement services." Roberts believes that it clearly does.

"The path of least resistance may be for the [Trump] DOL to focus on [that issue], he wrote in an essay on LinkedIn, adding that "the bigger question is then what to expect in terms of either a 'proposed rule rescinding or revising' the current regulation and the degree to which either would be determined to be 'appropriate and as consistent with law.'

But Bullard told *RIJ* in an email this week that most of the costs of complying with the rule have already been incurred by financial services firms. In other words, at least part of the horse is out of the barn.

"Changes in the industry over the last year have radically changed the economics of compliance," he wrote, referring to the various internal costs of complying with the rule. "Many have already incurred the cost." [Other changes have] "proved false the industry's claims that brokers would not be able to charge commissions. Many have decided to do exactly that under the rule."

The Administrative Procedures Act

Bullard also suggested that consumer advocacy groups with adequately deep pockets might sue the DOL to prevent the discarding of the rule. "I expect that DOL will be sued if it amends the rule—which would include delaying it—without doing a cost-benefit analysis, and such an analysis would be impossible to complete prior to the implementation date."

Who might sue the DOL? "Any investor advocacy group with the funds to hire counsel, such as Better Markets, unions, or Public Citizen. The grounds would be arbitrary and capricious rulemaking, failure to provide for notice and comment," Bullard added.

At one consumer advocacy group, a lawsuit is currently being discussed. "We are considering all our options, including challenging the Administration in court if it violates procedural requirements," said Barbara Roper, Director of Investor Protection at the Consumer Federation of America.

The grounds for such a suit, Hauptman said and ERISA attorney Marcia Wagner said this week, would be a violation by the Trump administration of the Administrative Procedures Act. "We will be watching whether the Administration violates the Administrative Procedure Act or otherwise violates the law. There are a number of ways this could happen," Hauptman told *RIJ*.

An unstoppable trend

Even without the rule, many believe that the trend toward fee-based advice and toward the web-mediated offering of low-cost, transparent, participant-like services to the mass of rollover IRA clients will continue. Some even think that the DOL rule was merely just a formal endorsement of stronger, technology-driven trends in financial services.

Wagner, in a bulletin this week, conceded that "it is highly unlikely that the DOL Fiduciary Rule and related exemptions such as the Best Interest Contract Exemption (BICE) will survive in their current form, in light of President Trump's clear willingness to dismiss government officials unwilling to conform to his agenda.

But she encouraged her industry clients to assume that the rule will stand, because it's better for them in the long run.

"Even if the DOL concludes that the best course of action is to return to the rules in effect prior to the enactment of the DOL Fiduciary Rule and BICE, it would not necessarily be the best course of action to undo all of the compliance steps that have already been taken," she wrote.

"Some of the actions that have been accelerated by the DOL Fiduciary Rule reflect an industry trend towards an advisory rather than a brokerage based platform. Moreover, the move towards more transparent fee disclosures may reflect new industry standards for 'best practices.' Focusing more narrowly upon compliance issues, transition-period documentation should be retained, although its final form may need to be modified to reflect any future DOL action.

"Finally, it is important to keep in mind that the primary enforcer of violations of the DOL Fiduciary Rule and BICE was to be the private tort bar, rather than the DOL or IRS. Even if BICE is repealed, the tort bar will seek and exploit various causes of action. For example, compensation grids that have the effect, even if unintended, of incentivizing investments in particular funds may be challenged."

Striking a lighter note, Bill Harris, the CEO of robo-advisor Personal Capital, responded to a comment by White House National Economic Council director Gary Cohn that the fiduciary rule is "a bad rule for consumers… [It's] like putting only healthy food on the menu because unhealthy food tastes good but you still shouldn't eat it because you might die younger."

To which Harris, who favors the retention of the DOL rule, replied in a press release, "Encouraging people to die younger is one way to solve our retirement crisis. But we think a better way is to encourage people to save responsibly and invest well, so they're able to live a long life in financial security."