CARLTON FIELDS

The DOL Fiduciary Rule: Charting a Course, Avoiding Collisions & Potential Litigation

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Q&A on IRA Transactions

Previously, I wrote about potential litigation under the Department of Labor's then proposed fiduciary rule (*see Expect Focus*, Vol. II, 2015). I predicted the following as to sales of index annuities to IRAs if the rule was adopted as proposed:

> "From a litigation perspective, this change to a fiduciary status for the sales agent is substantial and in many cases will afford litigants unhappy with investment results, or the ultimate characteristics of a particular form of annuity, the opportunity to second-guess the original decision applying a significant range of issues."

Over the next several months, we will provide comments and further predictions regarding risks of, and defenses for, potential litigation under the revised, "temporary" DOL rule and its progeny as both the debates and the DOL's review of the rule continue. Given the amount of ink that has been (and continues to be) dedicated to this subject, our observations will assume readers have a sufficient level of understanding, eliminating the need for detailed background on each issue. With that premise, we pose these questions:

> **Q.** Does it make a difference, from a potential litigation perspective, whether a commissioned sale of an annuity to an IRA relies on Prohibited Transaction Exemption (PTE) 84-24 or the best interest contract (BIC) for its exemption? **A.** Probably not. Under either the BIC or PTE 84-24, the sales agent who is now (at least from the DOL's perspective) a fiduciary must adhere to the Impartial Conduct Standards when using either exemption. Those fiduciary standards will apply to the sale and the potential exists for litigation asserting the violation of "fiduciary" duties (more on that below). Of course, depending on the practices adopted by the financial institution (under the BIC) or the sales agent (under 84-24), the nature and content of disclosure will differ. There will likely be some difference due, in part, to the requirements of the exemptions themselves. Under 84-24, there is a requirement to "obtain advance written

authorization" and a "written disclosure" while the requirements for written "Transition Disclosures" originally imposed under the BIC have been removed. Nevertheless, both exemptions require adherence to the Impartial Conduct Standards. The difference in the methods used to achieve such adherence should not alter the nature or results of litigation for breach of a fiduciary duty. A plaintiff's pleadings in some future allegation of a fiduciary breach will not focus on the exemption's status, but rather on the applicable fiduciary standards, which, under the DOL's exemptions, are identical. **Q.** Can we assume that all state courts, when confronted with an IRA sale that is not preempted by or subject to ERISA federal jurisdiction, nor tethered to existing ERISA case law and principles, will nonetheless conclude that the DOL's standards of "Best Interest" must necessarily be followed in determining the boundaries of any "fiduciary duty" assumed by the agent or broker of the sale under state law? Does the creation of this fiduciary duty under the DOL's exemption result in a potential cause of action at all under state law? If so, what state law or duties will be applied if and when a purchaser chooses to attempt to enforce that fiduciary duty in a state court litigation? **A.** It depends. Some (probably the DOL) will say, "Of course the courts will rely on the DOL's articulation of the duties and applicable standards." But, apparently at least some at the DOL thought it necessary, when the BIC exemption was first proposed, to embody those standards in a written contract so that both the sales agent and the IRA purchaser agree as to the standards. The nature and contours of a "fiduciary" duty relationship have traditionally been considered necessarily consensual, and the intent of two parties to such relationships has been crucial to the enforcement of the duty. We know that for many years state courts have routinely concluded that, absent facts to the contrary, the mere sale of insurance/annuities does not create a fiduciary relationship between an insurer or its agent and the insured. Most recently, in a decision refusing to apply fiduciary duties to an agent's sale of insurance and annuity policies, the Pennsylvania Supreme Court held **"a fiduciary duty may arise *in* the context of consumer transactions only if one party cedes decision-making control to the other party,"** noting that **"the superior knowledge or expertise of a party does *not* impose a fiduciary duty on that party or otherwise convert an arms-length transaction into a confidential relationship."** See *Yenchi v. Ameriprise Financial, Inc.*, No. 8 WAP 2016, 2017 WL 2644473, at *8 (Pa. June 20, 2017). Why should state courts conclude otherwise based on an interpretation of a federal statute by the DOL? At least during the transition period, and absent some specific representations as part of the sales transaction, there will be no clear articulation of what standards would apply to this "imposed" fiduciary duty, other than what the DOL claims must be employed to gain the exemption. There is potential for a wide variety of results here. There are 50 state laws governing fiduciary conduct, and numerous variations from state to state on how those standards should be applied. Based on existing precedents, there is a very

> real possibility that state courts will refuse to impose a state law fiduciary duty absent other indicia of a fiduciary relationship during the transaction.

Our next article on this subject will discuss the recent activities raising the possibilities for and implications of, class action waiver and arbitration provisions and review some of the variances among a few selected states regarding the application of the fiduciary principles, discuss potential theories likely to be asserted in a class action context by plaintiff's counsel, and provide readers some suggestions for addressing these potential theories in advance.

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