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Department of Labor May Be Saying *Au Revoir* to BIC Exemption's Restrictions on Arbitration

On July 3, 2017, in a brief filed before the United States Court of Appeals for the Fifth Circuit (the "Fifth Circuit"), the Department of Labor ("DOL") and Department of Justice ("DOJ") announced that the Government would no longer defend the restrictions on arbitration in the Best Interest Contract Exemption ("BIC Exemption"), and opined that the conditions should be vacated and severed from the exemption. The move marks a stunning shift in the DOL's defense of its fiduciary rulemaking, which—up until now—has been vigorous and marked by a string of litigation victories.[1]

Background

While the BIC Exemption permits requiring investors to submit to binding arbitration for individual disputes with Advisers or Financial Institutions, the BIC Exemption requires that the contract preserve the right to bring or participate in class action litigation. In the preamble to the BIC Exemption, the DOL went to great lengths to describe its concerns and rationale for preserving the avenue for class action litigation. Specifically, the DOL opined that "[t]he ability to bar investors from bringing or participating in [class action lawsuits] would undermine important investor rights and incentives for Advisers to act in accordance with the Best Interest standard," and noted that "courts impose significant hurdles for bringing class actions, but where investors can surmount these hurdles, class actions are particularly well suited for addressing systemic breaches."[2]

The DOL further noted that "the judicial system ensures that disputes involving numerous retirement investors and systemic issues will be resolved through a well-established framework characterized by impartiality, transparency, and adherence to precedent," and that "court decisions serve as a guide for the consistent application of that law in future cases involving other Retirement Investors and Financial Institutions."[3]

In issuing the BIC Exemption, the DOL stressed its view that the conditions prohibiting waivers for class action litigation (and requiring investors to submit to arbitration for such claims) were consistent with the Federal Arbitration Act ("FAA"), a statute that generally recognizes the enforceability of arbitration agreements. At that time, the DOL noted that the conditions were "fully consistent with the FAA" because they did not "purport to render an arbitration provision in a contract between a Financial Institution and a Retirement

[1] For a recap of the litigation relating to the DOL's fiduciary rulemaking, *see Fiduciary Rule Survives Challenge in Texas*, Groom Law Group Benefits Brief (February 9, 2017), available at http://www.groom.com/resources-1109.html.
[2] 81 Fed. Reg. 21,002, 21,043 (April 8, 2016).
[3] *Id.*

Investor invalid, revocable, or unenforceable."[4] Instead, the DOL argued, "Financial Institutions and Advisers remain free to invoke and enforce arbitration provisions, including provisions that waive or qualify the right to bring a class action or any representative action in court" but would simply not meet the conditions for exemptive relief by doing so.[5]

Notably, while noting that it was "confident that its approach in the exemption does not violate the FAA," the DOL recognized the possibility that the anti-arbitration conditions could be found to be in conflict with the FAA.[6] In this regard, the BIC Exemption provides that the anti-arbitration conditions could be severed from the exemption without otherwise affecting the validity of the exemption. Specifically, Section II(f)(4) of the BIC Exemption provides that "[i]n the event that the provision on pre-dispute arbitration agreements for class or representative claims . . . is ruled invalid by a court of competent jurisdiction, this provision shall not be a condition of this exemption . . . but all other terms of the exemption shall remain in effect."

Trump Administration Signals Support for Arbitration and Restricting Class Action Litigation

The Government's announcement in its Fifth Circuit brief that it will no longer defend the BIC Exemption's anti-arbitration conditions demonstrates a significant shift by the Trump Administration toward favoring arbitration and limiting class action litigation. In its brief, the Government justified its new position as being based on a similar position reversal in a case before the Supreme Court, *NLRB v. Murphy Oil USA, Inc.* ("Murphy Oil"), Nos. 16-285, 16-300, and 16-307 (U.S. June 16, 2017). The *Murphy Oil* case concerns whether arbitration agreements precluding individual employees from asserting work-related claims in class action litigation violate the employees' rights under the National Labor Relations Act ("NLRA").

In an amicus brief filed before the Supreme Court on June 16, 2017, the Trump Administration argued that courts "must enforce agreements to arbitrate federal claims unless the FAA's mandate has been overridden by a contrary congressional command or unless enforcing the parties' agreement would deprive the plaintiff of a substantive federal right."[7] Notably, this position directly conflicts with the National Labor Relation Board's previous position (in that same litigation) that mandatory arbitration violates rights under the NLRA.

In addition to citing the Trump Administration's new position in *Murphy Oil*, the Government's Fifth Circuit brief also justified its new position based on the "savings clause" reserved in the text of the BIC Exemption regarding possible invalidation of the anti-arbitration conditions. In this regard, the brief notes that "DOL clearly indicated that it would have adopted the BIC Exemption even if the exemption's anti-arbitration condition is severed," and that thus "invalidation of the anti-arbitration condition does not justify invalidation of the BIC Exemption or of the fiduciary rule as a whole."[8]

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[4] *Id. at* 21,044.
[5] *Id.*
[6] *Id.*
[7] Brief for the United States as *Amicus Curiae* Supporting Petitioners in Nos. 16-285 and 16-300 and Supporting Respondents in No. 16-307, p. 9, *NLRB v. Murphy Oil* (U.S. June 16, 2017).
[8] Brief for Appellees, R. Alexander Acosta, Secretary, U.S. Department of Labor and U.S. Department of Labor, *Chamber of Commerce v. United States Department of Labor*, pp. 60, 64, No. 17-10238 (5th Cir. 2017).

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New Developments

The Government's new position regarding the BIC Exemption's anti-arbitration conditions directly impacts at least one lawsuit involving the BIC Exemption, *Thrivent Financial for Lutherans v. R. Alexander Acosta and U.S. Department of Labor*, a case pending before the District Court of Minnesota. Significantly, as stated in a July 5, 2017 letter from the plaintiffs to the court (the "Thrivent Letter"), the Government's new position signifies that "DOL has abandoned the arguments that it previously made . . . and DOL thus acknowledges that the legal contentions made . . . in opposition to Thrivent's summary judgment motion are not warranted by existing law."

Subsequently, in a letter to the court dated July 14, 2017 (the "DOL Letter"), the DOL requested that the court stay the litigation. Alternatively, the DOL stated that it "would not oppose this Court's granting summary judgment to Plaintiff vacating BIC Exemption § II(f)(2) as applied to arbitration agreements entered into by Thrivent Financial." However, it is unclear whether this letter has any procedural effect on the litigation.

Indeed, on July 17, 2017, Thrivent filed a motion with the court objecting to the DOL's submission of its requests through a letter rather than a formal motion. On July 18, 2017, the court ordered the DOL to file a formal motion by July 27, 2017.

Our Thoughts

To say the least, these recent developments indicate a substantial shift in the Government's view of arbitration as a method to efficiently resolve disputes. Further, the Government's new position raises the question whether the DOL will remove the restrictions in Section II(f)(2) of the BIC Exemption regarding restrictions/waivers of investor rights to class or representative litigation.

At first blush, it is not clear whether the new litigation position will require the DOL to make this change. Notably, the BIC Exemption states that the conditions can be severed from the exemption if they are "ruled invalid by a court of competent jurisdiction." As a court has not yet actually ruled on the conditions, it is unclear whether the conditions can be said to be "severed" based solely on the Government's new position without any court rulings. Further, even if such a ruling occurs, Secretary of Labor Acosta may remove the anti-arbitration provision from the BIC Exemption, but only after a public notice and comment process.

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