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Amidst Ongoing Activity in the Courts, A New DOL "Fiduciary Rule" Is in the Works

The Department of Labor ("DOL") is reportedly developing a new proposed "fiduciary rule," a regulatory rule first developed in 1975 that contains a test to determine who qualifies as a fiduciary under ERISA. This development comes as cases in federal courts challenge DOL's existing guidance on when an investment advisor is considered a fiduciary. In one of those cases, DOL recently dropped its appeal of the court's decision striking down part of the guidance.

Background

DOL issued a regulation in 1975 that provides a five-part test to determine who is an ERISA fiduciary in the context of giving investment advice – i.e., the so-called "fiduciary rule." Under one of the parts – called the "regular basis" test – an investment advisor must make investment recommendations to a plan on a regular basis. In 2016, DOL revised its regulation to include advisors who make recommendations to roll over assets from a retirement plan to an IRA within the scope of an ERISA fiduciary. This was a much broader definition of fiduciary than the original 1975 regulation. However, the 2016 rule was struck down by the Fifth Circuit Court of Appeals, which reinstated the five-part test, holding that, by getting rid of the "regular basis" test, the 2016 rule improperly defined fiduciaries as including nearly all financial professionals who do business with ERISA plans and IRA holders, not just those with a relationship of trust and confidence with a client.

Following the Fifth Circuit's ruling, DOL published Prohibited Transaction Exemption ("PTE") 2020-02, which addressed fiduciary investment advice to retirement investors. In FAQs published to answer questions about PTE 2020-02, DOL states that the "regular basis" test could be satisfied for a recommendation to roll plan assets to an IRA, even when it is the first instance of advice. Effectively, an advisor could be considered a fiduciary even with a very limited, first-time interaction with a plan participant. PTE 2020-02 and the FAQs generated new concerns that DOL was – just as it had under the 2016 rule – trying to broaden who would be considered an ERISA fiduciary, and therefore subject to ERISA fiduciary duties.

Court Activity

In the time since PTE 2020-02 went into effect, two major federal lawsuits were filed against DOL, both arguing that DOL essentially tried to improperly implement a new fiduciary rule through PTE 2020-02 and the FAQs that would have the effect of reviving the 2016 rule, even though the Fifth Circuit it struck down. First, the American Securities Association ("ASA") filed a lawsuit in the District Court for the Middle District of Florida. The ASA argued that, under the FAQs discussed above, DOL impermissibly expanded the circumstances under which an investment advisor is subject to fiduciary duties. On February 13, 2023, the Florida district court struck down part of the FAQs. (See RPI 2023-05 for a fuller discussion of this ruling.) Interestingly, on May 15, 2023, DOL dropped its appeal to the Eleventh Circuit Court of Appeals after originally starting the appeals process.

In February 2022, a separate challenge that makes very similar claims to the ASA case was filed by the Federation of Americans for Consumer Choice in the District Court for the Northern District of Texas. That court has yet to make a

decision in the case, but many suspect its decision will be in line with the Florida court's decision.

DOL Officials Weigh In

Government officials have long indicated that DOL intends to develop a new fiduciary rule. Though the timing on the release of a new proposed rule is not completely clear, recent comments by DOL officials seem to indicate that a new rule is coming sooner rather than later. Employee Benefits Security Administration Assistant Secretary Lisa Gomez indicated in May that issuing a new fiduciary rule is a "huge priority" for DOL. Similarly, comments by DOL Acting Secretary Julie Su during her nomination hearing for Secretary of Labor show that DOL is moving forward with a new fiduciary rule proposal. It is unclear how DOL will take into account the Florida court decision – and a potential Texas court decision – when developing the new rule.

Upcoming Regulatory Rule

On June 13, 2023, DOL released its updated regulatory agenda, which states that a proposed rule regarding the definition of fiduciary is being developed at DOL. The agenda projects an August 2023 date for the release of a proposed rule. Typically, the release dates listed on federal agencies' regulatory agendas tend to be very flexible, and often the actual release date is significantly after the projected date. In some cases, a rule listed on the regulatory agenda is never published at all. However, because of the recent activity and comments described above with regard to the fiduciary rule, it seems possible that a proposed rule will be published closer to the projected release date.

Ninth Circuit Rules Disability Insurer was ERISA Fiduciary in Connection with Erroneous Benefit Calculation

A recent ruling by the Ninth Circuit Court of Appeals raises questions about when a benefit calculation – which is typically not a fiduciary act under ERISA – might give rise to a fiduciary violation. Even though the case involved a long-term disability plan benefit, it could have implications for retirement plan benefit calculations as well.

Case Background

In the case before the Ninth Circuit, a participant's long-term disability benefit was higher than it should have been due to a calculation error. On several occasions over a nine-year period, the participant sought verification of the calculation. For example, she asked for income verification as part of her mortgage application process. Each time, the erroneous calculation was confirmed.

Finally, the insurer/plan administrator discovered the error and started the process of recovering the overpayment pursuant to the plan's terms. These

efforts included completely suspending the participant's monthly benefit payments.

The participant sued claiming, among other things, that the insurer/plan administrator had breached its fiduciary duties. The district court dismissed the fiduciary breach claim, ruling that calculating benefits pursuant to a pre-established set of policies and procedures is not a fiduciary act.

Ninth Circuit's Opinion

The Ninth Circuit Court of Appeals reversed the district court on the question of whether the insurer/plan administrator was acting as a fiduciary.

In sum, the Ninth Circuit concluded that even if the insurer/plan administrator's initial calculation was not a fiduciary act, its subsequent actions, which were "central to [the participant's] injury," were discretionary, and therefore fiduciary acts.

Specifically, the Ninth Circuit noted that the following actions taken by the insurer/plan administrator were "well-established fiduciary functions":

- As opposed to the "use of an online mechanism to calculate benefits" at issue in a previous case involving a pension benefit calculation, the Ninth Circuit explained that the insurer/plan administrator provided the participant with "individualized consultations with benefit counselors." These "individualized consultations" apparently were limited to the participant asking for confirmation of her benefit for various personal reasons.
- In some cases, the insurer/plan administrator issued verification letters to lenders upon the participant's request. Citing *Varity v. Howe*, 516 U.S. 489 (1996), the Ninth Circuit said "'conveying information about the likely future of plan benefits' through benefits counselors amounts to a fiduciary act." In *Varity*, in order to induce employees to agree to be transferred to a new spinoff company, an employer intentionally misrepresented the employee benefits that would be provided.
- The insurer/plan administrator "gathered [the participant's] earnings information, and interpreted the [p]lan's terms to determine which benefits and deductions applied." It isn't clear what the insurer/plan administrator did in this context that is materially different from what third-party administrators typically do when they calculate benefits.
- Even though the insurer/plan administrator knew the participant had relied on its repeated confirmation of its benefit calculation to make financial decisions, it decided "to immediately and aggressively collect the overpayment amount after nine years had passed, going as far as to entirely suspend" her benefits. The plan document authorized, but did not require, the insurer/plan administrator to recover overpayments.

Observations

The Ninth Circuit's decision is only the most recent in a long line of cases where courts have struggled with the distinction between fiduciary and non-fiduciary acts under ERISA. It is an inherently fact-specific inquiry that is often complicated by circumstances like those at issue here, where a sympathetic plaintiff is facing financial harm due to a plan error.

Nonetheless, some of the Ninth Circuit's reasoning could raise questions about whether things that in the past have been considered non-fiduciary acts – such as gathering salary and employment data to perform a benefit calculation or

responding to a participant's request for benefit verification – could be viewed differently by courts (at least those within the Ninth Circuit's jurisdiction) going forward.

Recent HHS Settlements Serve as Reminder of HIPAA Requirements

In May, the Department of Health and Human Services' ("HHS") Office for Civil Rights ("OCR") announced two settlements related to violations of the Health Insurance Portability and Accountability Act ("HIPAA"). Both settlements – one dealing with individuals' right to access their information under HIPAA and one concerning a security breach involving Protected Health Information – are reminders that HIPAA violations can come with hefty penalties.

Right of Access Settlement

On May 8, 2023, OCR announced a settlement with a licensed counselor providing psychotherapy services in Pittsburgh. The settlement involved a potential violation of the "right of access" provision under HIPAA's Privacy Rule. Under that provision, "covered entities" (i.e., health plans and most health care providers) must provide individuals, upon request, with access to their Protected Health Information ("PHI"). This includes the right to inspect or obtain a copy of the PHI. The Privacy Rule also requires covered entities to respond to these requests in a timely manner – generally, no later than 30 calendar days after receiving the request. Parents, as the personal representatives of their minor children, have a right to access their minor children's medical records.

In 2017, OCR received a complaint stating that the counselor's office, which is a covered entity under HIPAA, failed to provide an individual with access to his minor children's PHI. OCR provided direction to the counselor on the right of access rules and then closed the complaint. The following year, OCR received another complaint from the same individual concerning the counselor's continued noncompliance. OCR then launched an investigation and reached a settlement with the counselor. As part of the settlement agreement, the counselor must respond to the right of access request without delay, implement a corrective plan to revise its policies for access to PHI, and pay $15,000.

Privacy of PHI Settlement

On May 16, 2023, OCR announced another settlement with the Arkansas-based business MedEvolve, Inc., which provides software services to health care entities covered by HIPAA. The settlement involved a potential violation of HIPAA's Privacy, Security and Breach Notification Rules. Under the Privacy Rule, covered entities and their "business associates" must take safeguards to protect individual's PHI and must abide by certain limits on the use and disclosure of PHI absent an individual's prior authorization. (A business associate is a person or entity that performs certain functions or activities that involve the use or disclosure of PHI on behalf of, or provides services to, a covered entity.) The

Security Rule establishes standards to protect individuals' electronic PHI that is created, received, used, or maintained by a covered entity. Under the Breach Notification Rule, covered entities and business associates must notify HHS and any affected individuals when a breach of unsecured PHI has occurred. Business associates are generally required to comply with the Security Rule and some provisions of the Privacy and Breach Notification Rules.

In 2018, OCR began investigating a report that an unsecured MedEvolve server containing electronic PHI – such as the names of patients, billing addresses, and some Social Security numbers – was openly accessible on the internet. MedEvolve is a business associate which provides practice management, revenue cycle management, and practice analytics software services to health care covered entities. According to OCR, MedEvolve failed to properly assess the risks and vulnerabilities of the electronic PHI it was responsible for. As a result of its errors, over 230,000 people had their PHI exposed on the internet. In addition, OCR found that MedEvolve failed to enter into a business associate agreement with its subcontractor that handled PHI, as required by HIPAA. As part of the settlement, MedEvolve agreed to pay $350,000, conduct a risk analysis to determine vulnerabilities to electronic data, and develop and implement a risk management plan to address security risks.

Big Picture

It is crucial that covered entities and business associates remain HIPAA-compliant with respect to the Privacy Rule, the Security Rule, and the Breach Notification Rule, or they too could be subject to an OCR investigation. In its announcement of the settlement with MedEvolve, OCR emphasized that hacking and IT incidents were the most frequent type of large breach that was reported to OCR in all of 2022. With cybersecurity threats becoming more common, covered entities and business associates should take extra care to implement cyber safeguards.

From a plan sponsor perspective, it is important to keep in mind the complexity of HIPAA rule applicability. For example, employers that have self-insured plans are not considered covered entities themselves, but the plan itself is a covered entity. This dichotomy creates the danger of PHI falling through the cracks if proper HIPAA-compliant procedures are not put into place.

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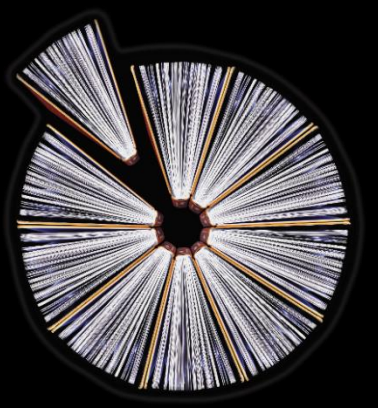

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