

Press Release

SEC Adopts Rules and Interpretations to Enhance Protections and Preserve Choice for Retail Investors in Their Relationships With Financial Professionals

FOR IMMEDIATE RELEASE

2019-89

Washington D.C., June 5, 2019 — The Securities and Exchange Commission today voted to adopt a package of rulemakings and interpretations designed to enhance the quality and transparency of retail investors' relationships with investment advisers and broker-dealers, bringing the legal requirements and mandated disclosures in line with reasonable investor expectations, while preserving access (in terms of choice and cost) to a variety of investment services and products. Specifically, these actions include new Regulation Best Interest, the new Form CRS Relationship Summary, and two separate interpretations under the Investment Advisers Act of 1940.

Individually and collectively, these actions are designed to enhance and clarify the standards of conduct applicable to broker-dealers and investment advisers, help retail investors better understand and compare the services offered and make an informed choice of the relationship best suited to their needs and circumstances, and foster greater consistency in the level of protections provided by each regime, particularly at the point in time that a recommendation is made.

"The rules and interpretations we are adopting today address issues that the Commission has been actively considering for nearly two decades," said SEC Chairman Jay Clayton. "Our staff, working collaboratively across all of our Divisions and many of our Offices, has leveraged its decades of experience and expertise in considering these issues. I believe that the exceptional work of the SEC staff, including their careful evaluation of the feedback we received, will benefit retail investors and our markets for years to come. This rulemaking package will bring the legal requirements and mandated disclosures for broker-dealers and investment advisers in line with reasonable investor expectations, while simultaneously preserving retail investors' access to a range of products and services at a reasonable cost."

Under Regulation Best Interest, broker-dealers will be required to act in the best interest of a retail customer when making a recommendation of any securities transaction or investment strategy involving securities to a retail customer. Regulation Best Interest will enhance the broker-dealer standard of conduct beyond existing suitability obligations and make it clear that a broker-dealer may not put its financial interests ahead of the interests of a retail customer when making recommendations.

The Form CRS Relationship Summary will require registered investment advisers and broker-dealers to provide retail investors with simple, easy-to-understand information about the nature of their relationship with their financial professional. While facilitating layered disclosure, the format of the relationship summary allows for comparability among the two different types of firms in a way that is distinct from other required disclosures. Form CRS will also include a link to a dedicated page on the Commission's investor education website, [Investor.gov](https://www.investor.gov), which offers educational information about broker-dealers and investment advisers, and other materials.

The Commission also issued an interpretation to reaffirm and, in some cases, clarify the Commission's views of the fiduciary duty that investment advisers owe to their clients under the Advisers Act. The interpretation reflects how the Commission and its staff have applied and enforced the law in this area, and inspected for compliance, for decades. By highlighting principles relevant to the fiduciary duty, investment advisers and their clients will have greater clarity about advisers' legal obligations.

Finally, the Commission issued an interpretation of the "solely incidental" prong of the broker-dealer exclusion under the Advisers Act, which is intended to more clearly delineate when a broker-dealer's performance of advisory activities causes it to become an investment adviser within the meaning of the Advisers Act. This interpretation confirms and clarifies the Commission's position, and illustrates the application in practice in connection with exercising investment discretion over customer accounts and account monitoring.

Regulation Best Interest and Form CRS will become effective 60 days after they are published in the Federal Register, and will include a transition period until June 30, 2020 to give firms sufficient time to come into compliance. Our interpretations under the Advisers Act will become effective upon publication in the Federal Register.

The Commission recognizes that these new rules will require various market participants to make changes to their operations, including to mandatory disclosures, marketing materials and compliance systems. In order to assist firms with planning for compliance with these new rules, the Commission is establishing an inter-Divisional Standards of Conduct Implementation Committee. We encourage firms to actively engage with this committee as questions arise in planning for implementation. You may send your questions by email to: IABDQuestions@sec.gov.

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FACT SHEET

SEC Open Meeting June 5, 2019

The Commission adopted a package of new rules and amendments and interpretations to enhance the quality of retail investors' relationships with broker-dealers and investment advisers. The rulemaking package is designed to enhance investor protections while preserving retail investor access and choice in: (1) the type of professional with whom they work, (2) the services they receive, and (3) how they pay for these services.

The new rules will enhance the standard of conduct that broker-dealers owe to their customers and align the standard of conduct with retail customers' reasonable expectations. The rules will also provide additional transparency and clarity for retail investors through enhanced disclosures designed to help them understand who they are dealing with, and why that matters. The interpretations reaffirm, and in some cases clarify, the standard of conduct that investment advisers owe to their clients and clarify the scope of the services a broker-dealer can provide consistent with the statutory definition of investment adviser.

With the adoption of this package, regardless of whether a retail investor chooses a broker-dealer or an investment adviser (or both), the retail investor will be entitled to a recommendation (from a broker-dealer) or advice (from an investment adviser) that is in the best interest of the retail investor and that does not place the interests of the firm or the financial professional ahead of the interests of the retail investor.

Proposal's Highlights

Regulation Best Interest

Regulation Best Interest imposes a new standard of conduct specifically for broker-dealers that substantially enhances the broker-dealer standard of conduct beyond existing suitability obligations. The standard of conduct draws from key fiduciary principles and cannot be satisfied through disclosure alone. It provides specific requirements to address certain aspects of the relationships between broker-dealers and their retail customers, including certain conflicts related to compensation.

When making a recommendation of a securities transaction or an investment strategy involving securities, a broker-dealer must act in the retail customer's best interest and cannot place its own interests ahead of the customer's interests. Regulation Best Interest, in an enhancement from the proposal, applies to account recommendations, including recommendations to roll over or transfer assets in a workplace retirement plan account to an IRA, and recommendations to take a plan distribution. It also applies to implicit "recommendations to hold" that result from agreed-upon account monitoring.

Regulation Best Interest includes the following components:

- *Disclosure Obligation:* Broker-dealers must disclose material facts about the relationship and recommendations, including specific disclosures about the capacity in which the broker is acting, fees, the type and scope of services provided, conflicts, limitations on services and products, and whether the broker-dealer provides monitoring services.
- *Care Obligation:* A broker-dealer must exercise reasonable diligence, care and skill when making a recommendation to a retail customer. The broker-dealer must understand potential risks, rewards, and costs associated with the recommendation. The broker-dealer must then consider these factors in light of the retail customer's investment profile and make a recommendation is in the retail customer's best interest. The final regulation, which is an enhancement from the proposal, explicitly requires the broker-dealer to consider the costs of the recommendation.
- *Conflict of Interest Obligation:* The broker-dealer must establish, maintain, and enforce written policies and procedures reasonably designed to identify and at a minimum disclose or eliminate conflicts of interest. This obligation, which is an enhancement from the proposal, specifically requires policies and procedures to:
 - Mitigate conflicts that create an incentive for the firm's financial professionals to place their interest or the interests of the firm ahead of the retail customer's interest;
 - Prevent material limitations on offerings, such as a limited product menu or offering only proprietary products, from causing the firm or its financial professional to place his or her interest or the interests of the firm ahead of the retail customer's interest; and
 - Eliminate sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sale of specific securities or specific types of securities within a limited period of time.
- *Compliance Obligation:* In an enhancement from the proposal, broker-dealers must establish, maintain and enforce policies and procedures reasonably designed to achieve compliance with Regulation Best Interest as a whole.

Form CRS Relationship Summary

Investment advisers and broker-dealers will be required to deliver a relationship summary to retail investors at the beginning of their relationship. Firms will summarize information about services, fees and costs, conflicts of interest, legal standard of conduct, and whether or not the firm and its financial professionals have disciplinary history. The relationship summary will have a standardized question-and-answer format to promote comparison by retail investors in a way that is distinct from existing disclosures. The relationship summary will permit the use of layered disclosure so that investors can more easily access additional information from the firm about these topics. It also will highlight the Commission's investor education website, Investor.gov, which offers the investing public educational information, including a series of educational videos designed to provide ordinary investors with some basic information about broker-dealers and investment advisers.

Investment Adviser Interpretation

An investment adviser owes a fiduciary duty to its clients under the Advisers Act—a duty that is established by and enforceable through the Advisers Act. This duty is principles-based and applies to the entire relationship between an investment adviser and its client. The final interpretation reaffirms, and in some cases clarifies, certain aspects of the federal fiduciary duty that an investment adviser owes to its clients.

Solely Incidental Interpretation

The broker-dealer exclusion under the Advisers Act excludes from the definition of investment adviser—and thus from the application of the Advisers Act—a broker or dealer whose performance of advisory services is solely incidental to the conduct of his business as a broker or dealer and who receives no special compensation for those services. The interpretation confirms and clarifies the Commission’s interpretation of the “solely incidental” prong of the broker-dealer exclusion of the Advisers Act. Specifically, the final interpretation states that a broker-dealer’s advice as to the value and characteristics of securities or as to the advisability of transacting in securities falls within the “solely incidental” prong of this exclusion if the advice is provided in connection with and is reasonably related to the broker-dealer’s primary business of effecting securities transactions.

What’s Next?

The rules, forms, and interpretations will be published on the Commission’s website and in the Federal Register. The rules and forms will be effective 60 days from publication in the Federal Register and the interpretations will be effective upon publication in the Federal Register.

By June 30, 2020, registered broker-dealers must begin complying with Regulation Best Interest and broker-dealers and investment advisers registered with the Commission will be required to prepare, deliver to retail investors, and file a relationship summary.

In order to assist firms with planning for compliance with these new rules, the Commission is establishing an inter-Divisional Standards of Conduct Implementation Committee, comprised of representatives from our Division of Investment Management, Division of Trading and Markets, Division of Economic and Risk Analysis, Office of Compliance Inspections and Examinations, and Office of the General Counsel. We encourage firms to actively engage with this committee as questions arise in planning for implementation. You may send your questions by email to IABDQuestions@sec.gov.

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