

Public Statement

Confirmation of June 30 Compliance Date for Regulation Best Interest and Form CRS



Chairman Jay Clayton

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New Website Page for Main Street Investors

Need for Increased Care when Recommending 401(k)/IRA Rollovers and Withdrawals, Complex or Risky Products, COVID-Related Investments and SPACs

Background—Confirmation of June 30 Compliance Date

In June 2019, the Commission adopted Regulation Best Interest (“Reg BI”) and Form CRS to enhance significantly the quality and transparency of relationships between broker-dealers and investment advisers (together, “firms”) and retail investors.^[1] The compliance date for Reg BI and Form CRS is June 30, 2020.

Reg BI establishes a new standard of conduct for broker-dealers when making a recommendation of any securities transaction or investment strategy (including account recommendations) to a retail customer. Reg BI and Form CRS, together with the interpretations adopted contemporaneously by the Commission,^[2] will bring the legal requirements and mandated disclosures for firms serving retail investors in line with reasonable investor expectations, while preserving access (in terms of both choice and cost) to a variety of investment services and products.

Over the past twelve months, the Commission and the staff have engaged extensively with broker-dealers, investment advisers, retail investors and other market participants, as well as FINRA and other regulatory partners, regarding the implementation of Reg BI and Form CRS.^[3] In April 2020, based on that engagement, I observed that firms—broker-dealers, investment advisers and “dual hatted” personnel—had made considerable progress in (1) adjusting their business practices, (2) supplementing and modifying their policies and procedures and (3) otherwise aligning their operations and preparing for the requirements of Reg BI and the obligation to file and deliver Form CRS.^[4] I also confirmed my view that the June 30, 2020 compliance date for Reg BI and the Form CRS requirements was appropriate. Engagement with firms and other market participants has continued over the past two months, and we remain committed to assisting firms and other market participants in completing this important effort.^[5] In addition, our work across the Commission over the past several months has strengthened

my view that the effects of the COVID-19 pandemic weigh substantially in favor of implementing the Reg BI and Form CRS requirements as soon as practicable.

New Website Page for Main Street Investors

To help Main Street investors better understand Form CRS and its benefits, the Commission has established a new website page.^[6] This investor-focused resource also provides educational resources and additional tools for investors to assist them in reading and understanding as they begin to navigate Form CRS, and in researching firms and financial professionals.

Areas Where Increased Care May be Necessary When Making Recommendations to Main Street Investors

The COVID-19 pandemic and various related actions have had, and we expect will continue to have, many significant effects on our markets and our Main Street investors. We have witnessed unprecedented stresses and volatility in various areas of our capital markets. These stresses have been met with an array of policy responses.^[7] As a result, the current and future needs and expectations of many of our Main Street investors, as well as the risks they face, have changed significantly. For example, Main Street investors may have greater needs for cash and liquidity as a result of a change in employment or other circumstances.

In addition, we are mindful about the mix of investments and strategies being marketed to Main Street investors, particularly in the context of recent market volatility. It is clear to me that some of the investments and strategies being marketed to Main Street investors are complex and risky, including certain of those that (1) are marketed as responsive to the effects of COVID-19, (2) provide significantly leveraged exposure (and risk) through the use of options, futures and other derivatives or through the use of margin and (3) have complex structures that may not be easily understood by Main Street investors. I am concerned that recommendations of these investments and strategies may not be in the best interest of significant portions of our Main Street investors. Unfortunately, certain other investments, including some marketed as COVID-19-driven, may be simply fraudulent as the Commission has charged in recent enforcement actions.^[8]

Under Reg BI, when making investment recommendations to a retail investor, a broker-dealer cannot put its interests ahead of the interests of its customer. The broker-dealer also is required to take into account investor-specific considerations such as investment horizon, needs and objectives, investment experience and risk tolerance. Similarly, under the Investment Advisers Act (the "Advisers Act"), an investment adviser cannot put its own interests ahead of the interests of its client, and must have a reasonable understanding of the client's objectives, including an understanding of the client's investment profile (including his or her financial situation, level of financial sophistication, investment experience and financial goals).

In meeting their respective obligations under Reg BI and the Advisers Act, broker-dealers and investment advisers should review their operations to be sure they are making recommendations or providing investment advice to retail investors that is in those investors' best interest. In this regard, and without limiting areas where review may be necessary generally, I believe firms should ensure that, particularly under current conditions, focus is being applied in the following areas, to the extent they are included in a firm's recommendation or advice to a retail investor:

- **Rollovers and withdrawals from 401(k) and other plans.** Reg BI's application to recommendations of rollovers of and withdrawals from retirement accounts is one of its most significant enhancements over the status quo.^[9] Recommendations to retail investors to roll-over or transfer assets from one type of account to another, or to take withdrawals from an account, should be approached with care. Firms should be particularly attuned to their regulatory obligations in light of the additional flexibility Congress recently provided investors to take withdrawals from certain accounts.

The Coronavirus Aid, Relief and Economic Security (CARES) Act allows eligible participants in certain tax-advantaged retirement plans to take early distributions of up to \$100,000 during this calendar year without

being subject to early withdrawal penalties and with an expanded window for paying the income tax they owe on the amounts they withdraw. By waiving early withdrawal penalties and other limitations tied to retirement accounts, Congress provided investors with substantial flexibility to access these plans in order to weather financial hardships related to the pandemic. However, to use that relief effectively, investors must navigate certain rules and make significant spending and investment decisions.

The SEC's Office of Investor Education and Advocacy noted in a recent investor alert that some promoters are recommending that investors take CARES Act withdrawals or otherwise roll-over retirement funds to invest in products they are soliciting.^[10] Firms should recognize that these recommendations are subject to Reg BI and ensure that their policies and procedures meet the requirements of Reg BI, the Advisers Act and Form CRS, as appropriate.^[11]

- **Complex or risky products.** Recommendations or investment advice to retail investors regarding complex or risky products, including significantly leveraged products that rely on derivatives strategies to enhance returns, or those that focus on investments in less liquid and more volatile markets, should be carefully reviewed by firms to ensure that they are in the best interest of retail investors. For example, inverse or leveraged exchange-traded products may not be in the best interest of a retail investor absent an identified, short-term, investor-specific trading objective.^[12]
- **COVID-related investments.** Since the spread of COVID-19 began, some companies have announced new products and services designed to address the health and other effects of the virus. For example, a number of stock promotions have claimed that new products or services of publicly-traded companies can prevent, detect, ameliorate or cure COVID-19, and that the stock of these companies will dramatically increase in value as a result.^[13] Others have presented themselves as able to rapidly manufacture products that may be useful or necessary to slow the disease's spread,^[14] discussed the status of development of drug candidates for potential application to COVID and the ability to expedite regulatory approval of any such treatment,^[15] or discussed the ability to provide testing kits that would allow submission of testing samples from home.^[16] Some of these COVID-related investment promotions have been part of an alleged "pump-and-dump" scheme, and others have been made in connection with penny stocks.^[17] A broker-dealer's recommendation to a retail customer regarding COVID-related investments should be based, among other things, on an understanding of the potential risks, rewards and costs associated with the recommendation.^[18] Similarly, an investment adviser must have a reasonable belief that its advice, including its advice with respect to COVID-related investments, is in the best interest of the client, including a consideration of whether investments are recommended only to those clients who can and are willing to tolerate the risks of those investments and for whom the potential benefits may justify the risks.^[19]
- **SPACs and Other Structured Investment Vehicles.** SPACs, or special purpose acquisition corporations, are created to raise money from investors on the premise that the sponsor of the SPAC will, in the future, identify and acquire another, usually privately-held, company. Before the target company is acquired, the SPAC acts as a pool of capital, and if a target company is not identified during a specific period of time, investors typically receive their money back. These investments may be appropriate for various types of retail investors, including as a component of a diversified portfolio. However, because of this "money back" feature, during times of heightened market volatility, retail investors may view SPACs as a relatively safe investment option, even though the structure and strategy of a SPAC may present complex risks. Those risks may include potential conflicts of interest caused by the compensation structure in itself and in combination with the "money back" feature. Recommendations or investment advice to retail investors regarding an investment in a SPAC or another type of structured investment vehicle should take any such risks into account in determining whether the investment is in a retail investor's best interest.^[20]

As we proceed to the June 30 compliance date for Reg BI and Form CRS, and as the effects of the pandemic on our markets continue, the Commission will continue to focus on the interests of our Main Street investors, and we remain committed to enhancing the quality and transparency of their relationships with their financial professionals.

[1] See Regulation Best Interest, Exchange Act Release No. 86031 (June 5, 2019) (adopting rule 15l-1 under the Exchange Act) (“Reg BI Release”), available [here](#); and Form CRS Relationship Summary; Amendments to Form ADV, Exchange Act Release No. 86032, Advisers Act Release No. 5247 (June 5, 2019) (“Form CRS Release”), available [here](#). Form CRS and its related rules require firms to deliver to retail investors a brief customer or client relationship summary that provides information about the firm. Firms must file their relationship summaries with the Commission.

[2] Along with adopting Regulation Best Interest and Form CRS, the Commission also provided interpretations: (1) reaffirming and in some cases clarifying standards of conduct for investment advisers, and (2) regarding when a broker-dealer’s advisory services are solely incidental to the conduct of the business of a broker or dealer. See Commission Interpretation Regarding Standard of Conduct for Investment Advisers, Advisers Act Release No. 5248 (June 5, 2019) (“Fiduciary Interpretation”), available [here](#); Commission Interpretation Regarding the Solely Incidental Prong of the Broker-Dealer Exclusion to the Definition of Investment Adviser, Advisers Act Release No. 5249 (June 5, 2019), available [here](#). These interpretations are currently effective.

[3] See, e.g., staff responses to frequently asked questions on Reg BI, *available here* <https://www.sec.gov/tm/faq-regulation-best-interest>; staff responses to frequently asked questions on Form CRS, *available here* <https://www.sec.gov/investment/form-crs-faq>.

[4] See SEC Chairman Jay Clayton, “Investors Remain Front of Mind at the SEC: Approach to Allocation of Resources, Oversight and Rulemaking; Implementation of Regulation Best Interest and Form CRS” (Apr. 2, 2020), *available at* <https://www.sec.gov/news/public-statement/statement-clayton-investors-rbi-form-crs>.

[5] In April 2020, the staff also noted that during the initial period following the compliance date, SEC examiners will be focusing on whether firms have made a good faith effort to implement policies and procedures reasonably designed to comply with Reg BI, while also providing an opportunity to work with firms on compliance and other questions. In this regard, the staff of the Office of Compliance Inspections and Examinations has issued various Risk Alerts, which are available [here](#) and [here](#).

In addition, the Commission and its staff have provided a number of other resources to assist firms in understanding the new requirements and working toward implementation:

- A dedicated SEC mailbox for firms and others to submit questions: IABDquestions@sec.gov.
- A Small Entity Compliance Guide on Regulation Best Interest, available [here](#).
- A Spotlight Page for relevant materials, including releases, comment letters, speeches, press releases and transcripts, available [here](#).

[6] See <https://www.investor.gov/home/welcome-investor-gov-crs>.

[7] See, e.g., SEC Chairman Jay Clayton, “Remarks to the Financial Stability Oversight Council” (May 14, 2020), *available at* <https://www.sec.gov/news/speech/clayton-remarks-financial-stability-oversight-council-051420>.

[8] See, e.g., SEC Press Release, “SEC Charges Companies and CEO for Misleading COVID-19 Claims” (May 14, 2020), *available at* <https://www.sec.gov/news/press-release/2020-111>; SEC Press Release, “SEC Charges Company and CEO for COVID-19 Scam” (Apr. 28, 2020), *available at* <https://www.sec.gov/news/press-release/2020-97>.

[9] This enhancement aligns broker-dealer obligations with the fiduciary duty applicable to investment advisers. See Fiduciary Interpretation (reaffirming that an investment adviser’s fiduciary duty applies to all investment advice provided to clients, including advice about whether to roll over assets from one account (e.g., a retirement account) into a new or existing account that the adviser or an affiliate of the adviser manages).

[10] See *COVID-19 Related Early Withdrawals from Retirement Accounts – Be Careful of Fraudsters and other Bad Actors Targeting Your Retirement Savings* (June 3, 2020), *available at* <https://www.investor.gov/introduction-investing/general-resources/news-alerts/alerts-bulletins/investor-bulletins/covid-19>.

[11] See Reg BI Release; Fiduciary Interpretation.

[12] See Reg BI Release; Fiduciary Interpretation. These products may be highly complex financial instruments that are designed to achieve their stated objectives on a daily basis and, accordingly, may not be in the best interest of a retail investor seeking a long-term investment strategy.

[13] See, e.g., *Frauds Targeting Main Street Investors -- Investor Alert* (updated June 5, 2020), available at: https://www.sec.gov/oiea/investor-alerts-and-bulletins/ia_frauds; and *Look Out for Coronavirus-Related Investment Scams -- Investor Alert* (updated June 5, 2020), available at https://www.sec.gov/oiea/investor-alerts-and-bulletins/ia_coronavirus.

[14] See, e.g., <https://www.sec.gov/litigation/suspensions/2020/34-88952.pdf>.

[15] See, e.g., <https://www.sec.gov/litigation/suspensions/2020/34-88800-o.pdf>.

[16] See, e.g., <https://www.sec.gov/litigation/suspensions/2020/34-88620-o.pdf>.

[17] See, e.g., SEC Press Release, "SEC Charges California Trader Engaged in Manipulative Trading Scheme Involving COVID-19 Claims" (June 9, 2020), available at <https://www.sec.gov/news/press-release/2020-128>.

[18] See Reg BI Release.

[19] See Fiduciary Interpretation.

[20] See Reg BI Release; Fiduciary Interpretation.