Wolters Kluwer

When you have to be right

White Paper

August 4, 2020

Highlights

- **The essential history of Regulation BI**
- **A review of the DOL's proposal to replace the vacated fiduciary rule and related Best Interest Contract exemption**
- **A comparison of the suitability standard, selected legislative and regulatory proposals, and Regulation BI**
- **Detailed explanations of Regulation BI, Form CRS, and SEC interpretations of the broker-dealer exclusion and the investment adviser conduct standard**
- **A preview of what Regulation BI examination and enforcement may look like**
- **Analysis of litigation challenging the validity of Regulation BI**
- **A look ahead at state fiduciary standards and the law of federal preemption**

Inside

Executive summary 1
Introduction: an abridged history of Regulation Best Interest 2
The basics of Regulation BI 17
SEC interpretation of the broker-dealer exclusion from the Advisers Act 21
SEC interpretation of the investment adviser conduct standard 22
Relationship summary on Form CRS 24
Examination and enforcement 31
FINRA rules conformed to Regulation BI 34
Regulation BI litigation 34
The road ahead: state fiduciary standards and preemption 42
Conclusion 47

By *Mark S. Nelson, J.D.*

Regulation Best Interest under the microscope: advising the retail customer past, present, and future

Executive summary

The SEC adopted Regulation Best Interest for the purpose of enhancing the standard of care applicable when broker-dealers provide personalized investment advice about securities to their retail customers. The SEC first proposed Regulation BI in April 2018 and adopted the final version of the regulation on June 5, 2019. Regulation BI became effective September 10, 2019, but firms were not required to comply with the regulation until June 30, 2020. The lag periods between adoption, effectiveness, and compliance were intended to give firms time to update their internal systems to handle the new disclosures mandated by Regulation BI.

A separate SEC rulemaking, adopted on the same day as Regulation BI, addressed the new relationship summary to be filed with the Commission on Form CRS. The relationship summary describes a broker-dealer's and/or investment adviser's customer and client relationships and provides information about conflicts of interest, fees, and other costs. Like Regulation BI, Form CRS became effective on September 10, 2019, but transitional provisions did not require firms' initial Forms CRS to be filed with the Commission until the period May 1, 2020 through June 30, 2020.

The public and federal court debate over Regulation BI centered on divergent interpretations of the SEC's authority under Dodd-Frank Act Section 913, the agency's main source of authority for Regulation BI. The SEC has said that the Dodd-Frank Act gave the agency flexibility to adopt any standard of care for broker-dealers. By contrast, a group of states and a financial planning firm have argued that the SEC, if it adjusted the broker-dealer standard of care at all, was required by the Dodd-Frank Act to adopt a fiduciary standard of care equivalent to the standard applicable to investment advisers. This outcome, the groups argued, is mandated by basic principles of statutory construction that require courts to read Section 913 in its entirety rather than focus on an individual provision within the statute, as the SEC had urged. Those opposed to Regulation BI also asserted that the SEC's "enhanced" standard of care contained in Regulation BI is nothing more than a version of the existing suitability standard.

© 2020 CCH Incorporated and its affiliates. All rights reserved.

In early June 2020, a three-judge panel of the U.S. Court of Appeals for the Second Circuit heard expedited oral argument in the federal case challenging the validity of the SEC's Regulation BI. The possible outcomes included dismissal based on either lack of subject matter jurisdiction or lack of constitutional standing by the petitioners. The court, however, could decide the merits of the case, if it found that it had jurisdiction and at least one of the petitioners had constitutional standing. As a result, there were numerous scenarios under which either the petitioners or the SEC could prevail in part, or entirely. On June 26, 2020, a majority of the three-judge Second Circuit panel held that the investment planning petitioner (but not the state petitioners) had constitutional standing and upheld Regulation BI on the merits. One judge partially dissented because he would have found that all of the petitioners lacked constitutional standing and, thus, would not have addressed the merits of the case (although he agreed with the majority's merits result).

However, another potential source of litigation may arise regarding the several states, such as Massachusetts, which have either adopted, or are on a path to adopt, fiduciary-like standards of care for broker-dealers that purport to be stronger than the standard required by Regulation BI. If such litigation challenging state broker-dealer fiduciary standards were to arise, it is likely that a broker-dealer firm and/or industry group challenging a state regulation would assert that the federal government's Regulation BI preempts the state regulation. The SEC, in adopting Regulation BI, was silent on whether Regulation BI was intended to preempt stronger state regulations. The preemption question likely would come down to how a court would interpret multiple provisions within the National Securities Markets Improvement Act of 1996, which re-aligned the divisions between federal and state securities regulatory authorities.

Moreover, on June 1, 2020, the Department of Labor submitted a proposal titled "Improving Investment Advice for Workers & Retirees Exemption" (RIN 1210-ZA29) to the Office of Management and Budget's Office of Information and Regulatory Affairs for the purpose of regulatory review. It was anticipated that this filing would contain a DOL version of an enhanced standard of care that would harmonize DOL's regulations under the Employee Retirement Income Security Act of 1974 (ERISA) with the SEC's Regulation BI. The DOL has since publicly revealed the text of its proposal to replace the DOL fiduciary standard regulation promulgated by the Obama Administration that was vacated by the Fifth Circuit in March 2018. Even though the SEC's and DOL's regulation of broker-dealers and ERISA fiduciaries with respect to retail customers may be increasingly settled, it remains for the SEC, the DOL, and the Financial Industry Regulatory Authority (FINRA) to police the new regulatory regime on behalf of retail customers.

Introduction: an abridged history of Regulation Best Interest

Regulation Best Interest (Regulation BI) may be best described as the product of a long tug-of-war between political rivals who disagree about whether a new fiduciary standard of conduct for retail investors is needed and, if it is needed, what the content of that standard should be, and whether the Department of Labor (DOL) or the SEC should act first, or act together, to bring such a standard into existence. Dodd-Frank Act Section 913 explicitly authorized Commission rulemaking on the standard of care for broker-dealers, provided any resulting regulation takes into consideration the results of a required study on the topic.

The DOL moves first. The SEC's Dodd-Frank Act-mandated study on investment advisers and broker-dealers was one of a trio of required studies that, in addition to reconsidering the applicability of the fiduciary standard to retail investors, also addressed investment adviser examinations and conflicts of interest at investment banks. The SEC's Dodd-Frank Act Section 913 study concluded that investor confusion over the applicable standards of care could be reduced and that investor protection could be increased if there was a uniform fiduciary standard for broker-dealers and investment advisers when they provide personalized investment advice about securities to retail customers. Such standard would require a broker-dealer to "act in the best interest of the customer without regard to the financial or other interest of the broker, dealer,

© 2020 CCH Incorporated and its affiliates. All rights reserved.

or investment adviser." The study also recommended that the Commission consider whether to harmonize existing regulations that apply when broker-dealers and investment advisers engage in similar activities (e.g., advertising and customer communication, finders and solicitors, licensing, registration, supervision, continuing education, and recordkeeping) (Dodd-Frank Wall Street Reform and Consumer Protection Act, Sections, 913, 914, and 919A, respectively; Study on Investment Advisers and Broker-Dealers, January 2011).

The SEC's Section 913 study produced no Commission proposals during the course of multiple SEC Chairs in the years after enactment of the Dodd-Frank Act. It was former President Barack Obama who eventually made the opening gambit in 2015 by directing the DOL to move forward with a new standard of conduct for ERISA fiduciaries (See, The White House, Office of the Press Secretary, FACT SHEET: Middle Class Economics: Strengthening Retirement Security by Cracking Down on Backdoor Payments and Hidden Fees, February 23, 2015; See also, Definition of the Term "Fiduciary"; Conflict of Interest Rule—Retirement Investment Advice, April 1, 2016, 81 F.R. 20946, April 8, 2016).

The DOL also adopted its best interest contract exemption as an adjunct to the agency's regulation defining "fiduciary." The best interest contract exemption allowed certain persons who provide investment advice to retirement investors to receive compensation that otherwise would be banned to fiduciary advisers to employee benefit plans and IRAs under ERISA and the Internal Revenue Code. Under the best interest contract exemption, a financial institution must affirmatively state in writing that it and the adviser are fiduciaries. A financial institution and its adviser also must affirmatively state they will adhere to impartial conduct standards. But perhaps the key to the best interest contract exemption was its definition of "best interest" to include the requirement that investment advice be provided "without regard" to the financial or other interests of the adviser or financial institution (Best Interest Contract Exemption, Release No. ZRIN 1210–ZA25, April 1, 2016, 81 F.R. 21002, April 8, 2016).

Upon the change of Administrations in 2017, President Donald Trump issued a presidential memorandum directing the Secretary of DOL to "examine" the final fiduciary rule and "prepare an updated economic and legal analysis" of the fiduciary rule. If the Secretary made an affirmative finding that the rule, among other things, hinders access to retirement services or stresses the retirement savings industry, the Secretary must begin a notice and comment rulemaking to either rescind or revise the fiduciary rule (Presidential Documents, Fiduciary Duty Rule, Memorandum for the Secretary of Labor, 82 F.R. 9675, February 3, 2017). The DOL would delay implementation and amend certain provisions of the fiduciary rule while studying its economic and legal bases (See, e.g., 18-Month Extension of Transition Period and Delay of Applicability Dates; Best Interest Contract Exemption (PTE 2016–01); Class Exemption for Principal Transactions in Certain Assets Between Investment Advice Fiduciaries and Employee Benefit Plans and IRAs (PTE 2016–02); Prohibited Transaction Exemption 84–24 for Certain Transactions Involving Insurance Agents and Brokers, Pension Consultants, Insurance Companies, and Investment Company Principal Underwriters (PTE 84–24), 82 F.R. 56545, November 29, 2017).

The SEC's Dodd-Frank Act Section 913 study concluded that investor confusion over the applicable standards of care could be reduced and that investor protection could be increased if there was a uniform fiduciary standard for broker-dealers and investment advisers when they provide personalized investment advice about securities to retail customers.

Meanwhile, in March 2018, a two-judge majority on a Fifth Circuit panel would, over a vigorous dissent, vacate *in toto* the DOL's fiduciary rule (*Chamber of Commerce of the United States of America v. U.S. Department of Labor*, March 15,

© 2020 CCH Incorporated and its affiliates. All rights reserved.

2018, Jones, E.). The majority focused on the DOL's regulation interpreting the definition of "investment advice fiduciary" which, in part, states that a person is a fiduciary if she "renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so."

The majority, although rejecting the Obama Administration's theory that ERISA was inherently ambiguous, nevertheless assumed, *arguendo*, that ERISA was ambiguous in its use of the phrase "investment advice for a fee" and, thus, the DOL's regulation could survive *Chevron* Step 1. However, the majority concluded that the DOL's regulation failed *Chevron* Step 2 because it was not a permissible or reasonable construction of ERISA. The majority reasoned that the DOL regulation departed from the common law of trusts, which ERISA had incorporated; DOL's 1975 regulation, as the majority described it, stated that the "contemporary understanding" was that fiduciary meant an "intimate relationship between adviser and client beyond ordinary buyer-seller interactions."

The dissent noted that the retirement savings industry had in the years after enactment of ERISA shifted from one of traditional pensions to one of 401(k) plans and individual retirement accounts and that the ERISA framework created in the 1970s was not designed to deal with this change in how employees save for retirement. The dissent also disputed many of the majority's theories, including that Congress intended to incorporate the Investment Advisers Act's approach to separating investment advisers from broker-dealers into ERISA.

In the aftermath of the Fifth Circuit's opinion, the Trump Administration's SEC stepped into the void and proposed and adopted Regulation BI. But the DOL would soon re-enter the arena. As of June 1, 2020, the DOL submitted a new proposed fiduciary standard to the Office of Information and Regulatory Affairs (OIRA) for regulatory review. That proposal is titled "Improving Investment Advice for Workers & Retirees Exemption" (RIN 1210-ZA29). Although initially the text of the proposal was not publicly available, the DOL has since formally issued the proposal, which is discussed in more detail below. But before the DOL formally sought to replace the best interest contract exemption, both Congress and the SEC struggled to define how the authority granted to the SEC by the Dodd-Frank Act should be used.

Congressional reaction. The prospect of a stronger fiduciary conduct standard for broker-dealers, especially one promoted first by the DOL, spurred legislative efforts by the then-Republican-led House during the 113th and 114th Congresses to, among other things, delay the DOL from adopting a fiduciary standard until the SEC had first issued a final rule stating the applicable standard. Legislation of this type was sponsored by Rep. Ann Wagner (R-Mo) and Sen. Roy Blunt (R-Mo) and passed the House by votes of 254-166 (113th Congress) and 245-186 (114th Congress) (See, e.g., Retail Investor Protection Act (H.R. 2374; H.R. 1090; S. 2497).

Representative Wagner later introduced a bill during the 115th Congress titled the Protecting Advice for Small Savers (PASS) Act (H.R. 3857) that would have, among other things: (1) repealed the Obama Administration's DOL's final fiduciary regulation; (2) imposed a best interest standard on broker-dealers that was vaguely similar to what would become the SEC's Regulation BI; (3) repealed the SEC's Dodd-Frank Act authority to establish a uniform fiduciary standard of conduct for brokers, dealers, and investment advisers; and (4) preempted related state laws concerning broker-dealers (except for state regulations of non-securities insurance products). The bill's best interest standard also contained numerous references to FINRA's suitability standard regarding key definitions such as "customer's investment profile," "reasonable diligence," and "recommendation." The House Financial Services Committee reported the Wagner bill favorably on a party-line vote of 34-26, but the bill never received a vote by the full House.

The minority Democratic views expressed in the related House FSC report characterized the Wagner bill as just another version of suitability, despite the bill's "best interest" language. But perhaps the minority saved its strongest language for the effect they said the bill would have on efforts by the Obama Administration's DOL to impose a higher standard of care for those who advise retirement savers. Said the minority: "H.R. 3857 is another effort by Republicans to kill the Department of Labor's (DOL) fiduciary rulemaking, which has been partially effective for four months now to finally protect American seniors and retirement savers from conflicted advice about their retirement assets" (See, House Rep. No. 115-894).

© 2020 CCH Incorporated and its affiliates. All rights reserved.

Regulation BI slowly emerges. The demise of the DOL's fiduciary standard opened the door to the SEC to propose, and then adopt, Regulation BI. Before the Commission formally proposed Regulation BI in 2018, multiple SEC chairs had opportunities to address the standard of care for broker-dealers under the SEC's Dodd-Frank Act authorities and, ultimately, did not move forward with such proposals. It would not be until nine years after the Dodd-Frank Act became law that a majority of the Commission would adopt a regulation invoking the authorities contained in Dodd-Frank Act Section 913. Until then, SEC action on what would become Regulation BI slowly emerged.

Former SEC Chairwoman Mary Schapiro, the first SEC chair to begin implementation of the Dodd-Frank Act reforms, first mentioned the uniform fiduciary duty as a topic for SEC staff consideration in November 2010. By February 2011, Schapiro had publicly advocated a uniform fiduciary standard for retail investors:

> I have long believed that retail investors deserve a fiduciary standard of conduct regardless of the title printed on their financial counselor's business card.
>
> We know that the difference between an investment adviser and a broker-dealer is often lost on an investor. What is hard to explain is why there should be a different standard of conduct for the two roles — especially as the once-bright lines between the two professions grow dim and the same or substantially similar services are involved.

Schapiro would reiterate this belief in an April 2011 speech in which she also indicated she would move soon to codify the results of the Section 913 study. In July 2011, Schapiro told lawmakers that "Investment professionals' first duty must be to their clients, and we look forward to implementing the study's recommendations" (referring to the Dodd-Frank Act Section 913 study required to be conducted by the SEC) (See, Mary L. Schapiro, Brodsky Family Lecture at Northwestern University School of Law, November 9, 2010; Mary L. Schapiro, Remarks at the CCOutreach National Seminar, February 8, 2011; Mary L. Schapiro, Remarks before the Society of American Business Editors and Writers, April 8, 2011; Mary L. Schapiro, Testimony before the House Financial Services Committee on "Enhanced Oversight After the Financial Crisis: The Wall Street Reform Act at One Year," July 21, 2011).

In February 2013, SEC Chair Elisse Walter told the Senate Banking Committee that the SEC was considering the recommendations of the Section 913 report and that the agency was preparing a draft document asking for "data specific to the provision of retail financial advice and the regulatory alternatives." During Walter's several months as

The demise of the DOL's fiduciary standard opened the door to the SEC to propose, and then adopt, Regulation BI.

President Obama's designated SEC chair, the SEC also would issue a call for public comment on the appropriate standards of conduct for investment advisers and broker-dealers. But further action on the broker-dealer standard of conduct would have to await Walter's replacement (Elisse B. Walter, Testimony before the Senate banking Committee on "Wall Street Reform: Oversight of Financial Stability and Consumer and Investor Protections," February 14, 2013; Duties of Brokers, Dealers, and Investment Advisers, Release No. 34–69013, March 1, 2013, 78 F.R. 14848, March 7, 2013).

SEC Chair Mary Jo White, in March 2014, nearly a year after becoming chair, said in a speech that the standard for investment advice to retail customers of broker-dealers was an "immediate and high priority" and that she had directed SEC staff to evaluate how best to use the SEC's Dodd-Frank Act Section 913 authority, including by examining whether to recommend a universal fiduciary standard and/or other steps that could be taken in the near term. As for the differences between the standards of conduct for investment advisers and for broker-dealers, White said "[w]henever you have substantially similar services regulated differently, I believe it is necessary to consider carefully whether the regulatory distinctions make sense" (Mary Jo White, Protecting the Retail Investor, March 21, 2014).

© 2020 CCH Incorporated and its affiliates. All rights reserved.

In March 2015, White told lawmakers that SEC staff had "provided technical assistance" to the DOL as it prepared to issue its interpretation of "fiduciary" under ERISA. By June 2015, White had publicly stated a preference for a uniform fiduciary standard: "I believe that broker-dealers and investment advisers should be subject to a uniform fiduciary standard of conduct that requires acting in the best interests of their clients when providing personalized securities advice to retail investors and I have begun to pursue that path with the Commission" (Mary Jo White, Testimony before the House Financial Services Committee on "Examining the SEC's Agenda, Operations and FY 2016 Budget Request," March 24, 2015; Mary Jo White, Remarks Before the SEC Historical Society, June 4, 2015).

The uniform fiduciary standard, however, would become one of several open regulatory questions for the Commission at the end of White's tenure following the change of Administration in January 2017. White was not unique in failing to move the Commission to adopt a uniform fiduciary duty or another standard within the bounds of the Dodd-Frank Act. In fact, three Democrat-appointed SEC chairs in the years following the enactment of the Dodd-Frank Act were unable to achieve such a result—White (Independent), Walter (Democrat) (designated as chair by President Obama), and Schapiro (Independent). Although perhaps no one could have known it with certainty at the time, White's eventual successor, the Republican-appointed Jay Clayton (Independent), would invoke the SEC's Dodd-Frank Act authorities, albeit to impose a standard of conduct for broker-dealers that was purportedly higher than suitability but less than the uniform fiduciary standard authorized by Congress in Dodd-Frank Act Section 913(g).

White would give two significant speeches as her term as chairwoman came to an end in 2017. In the first speech, a few days before President Trump's January 20, 2017 inauguration, White warned of the forces that could jeopardize the SEC's independence, including overly-prescriptive congressional mandates (she cited the Dodd-Frank Act and the Jumpstart Our Business Startups (JOBS) Act) as well as congressional proposals to alter the SEC's rulemaking process (she specifically cited the now-defunct GOP-led CHOICE Act). Both trends, said White, lend themselves to increased political polarization of the Commission (Mary Jo White, "The SEC after the Financial Crisis: Protecting Investors, Preserving Markets," January 17, 2017).

In the second speech, on January 23, 2017, White delivered the keynote address before an audience at the 44th Annual Securities Regulation Institute in Coronado, California, just days after she had left the Commission. White said the SEC "remains a strong, independent agency" and that the uniform fiduciary standard was an issue that requires the Commission to "grapple" with "hard choices," including whether to follow the path of Dodd-Frank Act Section 913 or to address the standard of conduct for broker-dealers via unspecified "other means." As chair, White told Congress that she had concluded such a fiduciary standard should apply to personalized securities advice to retail investors, a view she reiterated in her last appearance before Congress as SEC chair two months earlier. In that appearance, White also had spelled out the issues with which the Commission must "grapple" in considering a uniform fiduciary standard:

> I recognize that this is a complex issue, and that there are significant challenges that will need to be addressed in proposing a uniform fiduciary standard, including how to define the standard, how it would affect current business practices, and the nature of the potential effects on investors, particularly retail investors.

(Mary Jo White, "The SEC in 2017 and the Path Ahead," January 23, 2017; Mary Jo White, Testimony before the House Financial Services Committee on "Examining the SEC's Agenda, Operations, and FY 2018 Budget Request," November 15, 2016).

Regulation BI adopted. Current SEC Chair Jay Clayton, in his first substantive speech as chair, urged the Commission to "bring clarity and consistency" to the standards for investment advisers and broker-dealers given the partial effectiveness, at that time, of the DOL's fiduciary rule. Clayton also expressed a desire for the SEC to work with the DOL to promote the long term interests of Main Street investors. Clayton further noted that he had issued a statement calling for additional public comment on how the SEC should address the standards of conduct for investment advisers and broker-dealers because the last SEC request for such public comment had occurred four years

© 2020 CCH Incorporated and its affiliates. All rights reserved.

earlier on March 1, 2013, at the end of Walter's brief time as chair and shortly before White was confirmed as chair by the Senate. Clayton appeared to imply that the prior public comments may have become outdated. Even at this early stage, however, Clayton suggested that he wanted to preserve for investors a range of choices between the products and services offered by broker-dealers in any regulatory action the SEC might take on the subject: "[a]nd, any action will need to be carefully constructed, so it provides appropriate and meaningful protections but does not result in Main Street investors being deprived of affordable investment advice or products."

The request for "clarity and consistency" in Clayton's speech regarding the standards of conduct for investment advisers and broker-dealers was layered on top of eight principles Clayton said would guide him as chair: (1) the SEC's tripartite mission: to protect investors; maintain fair, orderly, and efficient markets; and to facilitate capital formation; (2) the long term interests of Main Street investors ("Mr. and Ms. 401(k)"); (3) the existing regime of disclosure, materiality, certain "heightened responsibilities" for some market participants, and antifraud enforcement; (4) the consideration of whether regulatory changes should be evaluated for their incremental and cumulative effects; (5) the evolution and use of technology but also with an eye to compliance costs; (6) a degree of introspection and self-criticism regarding retrospective rule reviews; (7) ensuring the Commission has "a realistic vision" for how rules are implemented and how the SEC will conduct compliance examinations; and (8) ensuring coordination between federal, state, and international securities regulators (Jay Clayton, Remarks at the Economic Club of New York, July 12, 2017).

As mentioned, Clayton had, one month before the Economic Club of New York speech, issued a call for public comments on the role of broker-dealers and investment advisers. That request was prompted by developments, including the Obama Administration's DOL fiduciary regulation, that had occurred since the SEC's Dodd-Frank Act-mandated Section 913 study (Jay Clayton, Public Comments from Retail Investors and Other Interested Parties on Standards of Conduct for Investment Advisers and Broker-Dealers, June 1, 2017).

The SEC proposed Regulation BI in April 2018. Less than one month later, Clayton reiterated that he believed the Commission should ensure through its rulemaking that both the investment adviser and broker-dealer options remain viable for investors—who may wish to choose one or the other or both depending on their personal financial needs—while also "enhance[ing] investor protection." Clayton then described the proposed Regulation BI thus:

> After identifying the problems, and noting that they were interrelated, we settled on an overarching design objective: eliminate, or at least substantially address, the "gaps" or mismatches between investor expectations and understanding, on the one hand, and market and legal realities on the other hand. We then decided to close those gaps from both ends — changing investor understanding and changing market regulation. And, importantly, to make those efforts complementary.

Later in the speech, Clayton suggested that the combination of an enhanced standard of conduct for broker-dealers plus the use of more consistent fiduciary principles throughout the "spectrum of investment advice" could result in "harmonization." Dodd-Frank Act Section 913 used the concept of harmonization in the context of harmonized enforcement (Regulation Best Interest, Release No. 34–83062, April 18, 2018, 83 F.R. 21574, May 9, 2018; Jay Clayton, The Evolving Market for Retail Investment Services and Forward-Looking Regulation — Adding Clarity and Investor Protection while Ensuring Access and Choice, May 2, 2018).

Also in 2018, the Investor as Purchaser Subcommittee of the SEC's Investor Advisory Committee made several recommendations about the SEC's proposed Regulation BI. Specifically, the IAC subcommittee recommended that the SEC: (1) clarify investment advisers' and broker-dealers' obligation to act in their clients' best interest; (2) ensure that the best interest standard covers rollovers and dually-registered firms' account type recommendations; (3) explicitly characterize the best interest standard as a fiduciary duty whose specific obligations may vary depending on the business model to which it is applied; and (4) conduct usability testing of proposed Form CRS before adopting specific disclosure obligations.

© 2020 CCH Incorporated and its affiliates. All rights reserved.

The IAC had previously recommended that the SEC impose a uniform fiduciary duty on broker-dealers when they provide personalized investment advice to retail investors (Recommendation of the Investor as Purchaser Subcommittee Regarding Proposed Regulation Best Interest, Form CRS, and Investment Advisers Act Fiduciary Guidance, November 7, 2018; Recommendation of the Investor Advisory Committee Broker-Dealer Fiduciary Duty, November 22, 2013).

The Commission adopted Regulation BI by a vote of 3-1 on June 5, 2019. The adopting release is thematically consistent with the proposing release, but the adopting release also significantly amended the proposing release by expanding requirements regarding broker-dealers' disclosure obligation, added language to refine the care and conflict of interest obligations, added a compliance obligation, and added a definition of "conflict of interest." The totality of Regulation BI rulemaking consists of four separate documents:

The totality of Regulation BI rulemaking consists of four separate documents: (1) Regulation BI; (2) Form CRS (the relationship summary); (3) an interpretive release regarding the meaning of "solely incidental" within the broker-dealer exclusion from the Investment Advisers Act; and (4) an interpretive release regarding the investment adviser standard of conduct.

(1) Regulation BI; (2) Form CRS (the relationship summary); (3) an interpretive release regarding the meaning of "solely incidental" within the broker-dealer exclusion from the Investment Advisers Act; and (4) an interpretive release regarding the investment adviser standard of conduct. Regulation BI itself divides into four related obligations: (1) a care obligation; (2) a disclosure obligation; (3) a conflicts of interest obligation; and (4) a compliance obligation. Regulation BI became effective September 10, 2019, although compliance was not to be required until June 30, 2020 (Regulation Best Interest: The Broker-Dealer Standard of Conduct, Release No. 34–86031, June 5, 2019, 84 F.R. 33318, 33400, July 12, 2019). Appropriations legislation that passed the House on party lines within a month of the SEC's adoption of Regulation BI would have barred the SEC from implementing Regulation BI and the related interpretive releases, but that legislation stood little chance of advancement in the Senate (See, Section 1003 of H.R. 3351)).

A key concern for the Commission in adopting Regulation BI was to understand how retail investors would use information to be provided in the relationship summary on Form CRS. In fact, Regulation BI itself tends to be highly principles-based in setting the standard for broker-dealer conduct regarding recommendations made to retail customers, while the SEC's supplemental Regulation BI materials and the Form CRS adopting release (the relationship summary) contain most of the details associated with broker-dealers' obligations under Regulation BI. To this end, after the SEC issued its Regulation BI proposing release, the SEC's Office of Investor Advocate commissioned from RAND Corporation two surveys: (1) one regarding the prospect of a uniform fiduciary standard that was separate from the Commission's rulemaking process; and (2) another survey regarding the usability of information that could eventually appear in the relationship summary within Form CRS.

On October 12, 2018, the SEC's Investor Advocate, Rick Fleming, submitted a public comment letter on proposed Regulation BI that contained the text of a report prepared by the SEC's Office of the Investor Advocate (OIAD) and RAND Corporation titled "The Retail Market for Investment Advice." The report noted the long history of "blurred" roles of broker-dealers and investment advisers and the SEC's prior efforts to clarify these roles, such as via the now-vacated 2005 regulation that emphasized whether a broker-dealer received special compensation and provided advice that was solely incidental to its brokerage

© 2020 CCH Incorporated and its affiliates. All rights reserved.

business; the regulation also contained a required disclosure statement that urged customers to ask unspecified questions about their broker's activities that is at least suggestive of the detailed conversation starters contained in Form CRS (See, Certain Broker-Dealers Deemed Not To Be Investment Advisers, Release No. 34-51523, April 12, 2005, 74 F.R. 20424, April 19, 2005; the regulation was vacated by the D.C. Circuit in *Financial Planning Association v. SEC*, March 30, 2007, Rogers, J.).

The OIAD/RAND report addressed the overarching questions of why investors seek professional investment advice and whether investors grasp the differences between the types of financial professionals. The report further noted that two factors may influence investors: (1) financial literacy—the more financially literate an investor is the more likely they will seek professional investment advice and the less likely they are to follow unsolicited advice; and (2) the degree of trust an investor has in an adviser—investors are more likely to follow professional advice if they trust the adviser (e.g., the adviser has a good communication style or holds certain credentials). Both early-stage focus groups and a later survey of 1,816 individuals suggested that investors believe that a financial professional acting in their "best interest" would, among other things, recommend the lowest cost products, consider the investor's personal financial situation, provide ongoing account monitoring, and not sell products that would cause an investor to lose money. The survey also noted: (1) most investors had 401(k)s or IRAs with fewer investors holding direct investments such as stocks; (2) fewer than half of respondents had used a financial professional; (3) more than half of those who did use a financial professional did so for retirement savings purposes and these investors used either an investment adviser or a dually-registered investment adviser/broker-dealer; and (4) most investors understood that brokers are paid in commissions but approximately two-thirds of investors surveyed were unaware that investment advisers get paid based on a customer's assets (Brian Scholl, Office of the Investor Advocate and Angela A. Hung, RAND Corporation, The Retail Market for Investment Advice, 2018).

The second RAND survey asked respondents to comment on a sample relationship summary and was sent to 1,816 individuals who had previously responded to the survey "The Retail Market for Investment Advice;" the response rate was greater than 80 percent. Overall, the RAND survey reported that retail investors viewed the information to be provided in the relationship summary as a positive development. However, prospective retail investors surveyed also expressed some concerns about ease of use of the relationship summary. For one, respondents said the relationship summary was too long, although a sizeable percentage said the length was about right. Respondents also had difficulty understanding sections of the relationship summary addressing costs/fees and conflicts of interest. With respect to conflicts of interest, some respondents thought this section potentially undermined another section that explains the broker-dealer's or investment adviser's obligations to the retail investor. The survey noted that many respondents were unsure of the meaning of the term "fiduciary." When asked about additional questions they could ask of a broker-dealer or investment adviser, respondents generally said they appreciated the questions suggested and would ask them. Still, a sizeable number of respondents said they were somewhat or very uncomfortable in asking questions focused on a broker-dealer's or investment adviser's disciplinary history or qualifications. Clayton observed in the press release announcing the survey results that investors often do not understand the relationships involved in the broker-dealer or adviser relationships and that the SEC would continue to seek to provide investors with information about these key relationships (SEC press release, November 7, 2018; A. Hung, Katherine G. Carman, Jennifer Cerully, Jeff Dominitz, Kathryn Edwards, Investor Testing of Form CRS Relationship Summary, RAND Corporation, November 2018).

The SEC also provided a forum through which individuals could comment on the proposed relationship summary. The results, which were drawn from 93 responses, were published in Appendix C to the adopting release for Form CRS. As with the RAND study, respondents appeared to find the proposed relationship summary useful, although some comments suggested it could be shorter. A question asking about the technical difficulty of the relationship summary calling for a narrative response drew 10 comments asking for a definition or other explanation of the term

© 2020 CCH Incorporated and its affiliates. All rights reserved.

"fiduciary" (See, Form CRS Relationship Summary; Amendments to Form ADV, Release No. 34-86032, June 5, 2019, 84 F.R. 33492, July 12, 2019).

As previously noted, the Commission adopted Regulation BI by a 3-1 vote on June 5, 2019. Regulation BI is effective as of September 10, 2019. However, compliance was not required until June 30, 2020 (Regulation Best Interest: The Broker-Dealer Standard of Conduct, Release No. 34-86031, June 5, 2019, 84 F.R. 33318, July 12, 2019). According to the adopting release, the compliance date was chosen to coordinate implementation of the best interest standard with the relationship summary requirement, adopted in its final form on the same day as was Regulation BI (See, Form CRS Relationship Summary; Amendments to Form ADV, Release Nos. 34-86032, June 5, 2019, 84 F.R. 33492, July 12, 2019).

Clayton's prepared remarks upon the adoption of Regulation BI sought to dispel the several criticisms that would be lodged by the dissenting commissioner and the SEC's Investor Advocate. Clayton spoke of the SEC's leading, but non-exclusive, expertise in the area of investment advisers and broker-dealers but said the Regulation BI package of rules and interpretations was within the SEC's purview. "They are designed to enhance the quality and transparency of the financial professional retail investor relationship, and include two overarching objectives: (1) to bring the required standards of conduct for financial professionals and related mandated disclosures in line with reasonable investor expectations; and (2) to preserve retail investor access (in terms of both choice and cost) to a variety of investment services and products," said Clayton (Jay Clayton, Statement at the Open Meeting on Commission Actions to Enhance and Clarify the Obligations Financial Professionals Owe to our Main Street Investors, June 5, 2019)

Commissioner Hester Peirce suggested that the declining number of broker-dealers was a worrisome trend and that the Commission will need to monitor how Regulation BI works in practice to ensure that it was "properly calibrated" (Hester M. Peirce, Statement at the Open Meeting on Regulation Best Interest and Related Actions, June 5, 2019). Commissioner Elad Roisman said Regulation BI would preserve investor choice versus the 2016 DOL fiduciary regulation, which he said limited investor choice, may have caused some firms to mull dropping smaller customers, raised costs, and increased litigation risks. Roisman acknowledged that Regulation BI also would raise costs for firms but that the regulatory improvements the regulation will bring justify those costs (Elad L. Roisman, Statement at the Open Meeting on Regulation Best Interest, the Interpretation of the Standard of Conduct for Investment Advisers, the Form CRS Relationship Summary, and the Interpretation of "Solely Incidental," June 5, 2019).

Commissioner Robert Jackson, Jr. dissented from the package of reforms contained in the SEC's several Regulation BI releases. For one, Jackson noted that the final investment adviser interpretive release excluded language that was part of the proposing release that would have stated that an investment adviser must put its client's interest first. With respect to Regulation BI, Commissioner Jackson observed that the final rule does not define "best interest" and the rule could allow conflicts to be resolved through only disclosure. As a result, Jackson asserted that the Regulation BI regulatory package will further blur the differences between investment advisers and broker-dealers. Jackson also said the Commission's economic analysis was deficient because it failed to evaluate the choice of not imposing a fiduciary standard on broker-dealers under Dodd-Frank Act Section 913(g).

With respect to state standards of conduct for broker-dealers, Jackson said Regulation BI should be viewed as a "federal floor, not a ceiling." Jackson then asked investors to continue fighting for higher standards of conduct: "In the meantime, I call on all of you who have been so crucial to this effort to keep fighting. Encourage investors to seek out true fiduciary advice from financial professionals who have chosen to hold themselves to higher standards than those we've set today. Keep pushing for meaningful protections in the States who choose to give their citizens the best chance for a safe retirement. And, most importantly, do not stop the critical work of advocating for the financial security of all Americans" (footnote omitted) (Robert J. Jackson Jr., Statement on Final Rules Governing Investment Advice, June 5, 2019).

SEC Investor Advocate Rick Fleming Characterized Regulation BI as an "improvement" over "suitability," but also worried that investors

© 2020 CCH Incorporated and its affiliates. All rights reserved.

could be harmed if the new rule is not aggressively enforced by the Commission. Fleming also objected to the investment adviser interpretive release's handling of conflicts of interest, which he said a recently amended instruction to Form ADV (General instruction 3, to Part 2 of Form ADV) required advisers to "seek to avoid" *and* fully disclose any material conflicts (emphasis in original); Fleming said that a footnote in the Commission's interpretive release (No. 57) elided this change in Form ADV and instead concluded that the standard for adviser conflicts of interest was intended to be the one set forth in Supreme Court precedent, which required only the elimination of conflicts *or* disclosure of them (emphasis in original). The original text of each document stated the following:

- Supreme Court precedent—"The Investment Advisers Act of 1940 thus reflects a congressional recognition "of the delicate fiduciary nature of an investment advisory relationship," as well as a congressional intent to *eliminate, or at least to expose*, all conflicts of interest which might incline an investment adviser—consciously or unconsciously—to render advice which was not disinterested" (See, *SEC v. Capital Gains Research Bureau, Inc.*, 375 US 180 (1963) (emphasis added)).
- Instruction No. 3, General Instructions for Part 2 of Form ADV—"Under federal and state law, you are a fiduciary and must make full disclosure to your *clients* of all material facts relating to the advisory relationship. As a fiduciary, you also must seek to avoid conflicts of interest with your clients, and, at a minimum, make full disclosure of all material conflicts of interest between you and your *clients* that could affect the advisory relationship. This obligation requires that you provide the client with sufficiently specific facts so that the client is able to understand the conflicts of interest you have and the business practices in which you engage, and can give informed consent to such conflicts or practices or reject them. To satisfy this obligation, you therefore may have to disclose to *clients* information not specifically required by Part 2 of Form ADV or in more detail than the brochure items might otherwise require. You may disclose this additional information to *clients* in your *brochure* or by some other means." (See, Amendments to Form ADV, Release No. IA–3060, July 28, 2010, 75 F.R. 49234, 49287-49288, August 12, 2010) (emphasis in original).

Although Fleming's comment above addressed the Commission's interpretation of the standard of conduct for investment advisers, portions of the cited language from *SEC v. Capital Gains Research Bureau, Inc.* appear in Regulation BI's definition of "conflict of interest" (Rick Fleming, Statement Regarding the SEC's Rulemaking Package for Investment Advisers and Broker-Dealers, June 5, 2019)

About one month after the Commission adopted Regulation BI, Clayton provided a more detailed defense of Regulation BI in which he characterized the many criticisms of Regulation BI as "...false, misleading, misguided, and unfortunately, in some cases, [] simply policy preferences disguised as legal critiques." Clayton's defense of Regulation BI can be viewed as addressing three topics: (1) the best interest standard itself; (2) the two interpretive releases accompanying the best interest rulemaking; and (3) the new relationship summary on Form CRS.

First, Clayton noted the four components of Regulation BI (disclosure, care, conflicts, and compliance), while also observing that the new rule will allow the Commission to more efficiently enforce broker-dealer conduct. He countered critics by stating that the conflicts of interest component requires broker-dealers to address conflicts and make recommendations in a client's best interest. Clayton further noted that the new rule is principles-based, thus, obviating the need for a definition of "best interest." Finally, Clayton reiterated that the reason for not imposing certain obligations on broker-dealers (e.g., continuous monitoring of customer accounts) was aimed at preserving retail customers' choice about whether and how to interact with a broker-dealer or an investment adviser; continuous monitoring also would conflict with the Commission's accompanying interpretation of "solely incidental" with respect to activities a broker-dealer may engage in that are incidental to its broker-dealer business and for which it receives no special compensation.

Second, Clayton addressed interpretive issues regarding the investment adviser standard. Clayton asserted that the standard of conduct for

© 2020 CCH Incorporated and its affiliates. All rights reserved.

investment advisers remained the same as the standard applied by the Commission for decades under the Supreme Court's opinion in *SEC v. Capital Gains Research Bureau, Inc*. Clayton also responded to concerns expressed by, for example, SEC Investor Advocate Fleming, that the interpretive release elided the instruction to Form ADV contained in a 2010 revision of the form by the Commission that suggested a stronger conflicts of interest requirement; Clayton said there was "no legal or regulatory basis for this claim."

Clayton also defended the specific words used by the Commission in its investment adviser interpretation regarding whether a client's interests must be put first. Said Clayton:

> Some have taken issue with the words we used in describing the investment adviser's fiduciary duty, that an adviser "not subordinate its clients' interests to its own" or "not place its own interest ahead of its client's interests." They would prefer the formulation that an adviser must "put its client's interest first." I have no qualms with an adviser saying that they "put their client's interest first"—as our Fiduciary Interpretation recognizes, that is a plain English formulation of the legal standard that may be more understandable to retail clients.

Moreover, Clayton emphasized that under Regulation BI, a broker-dealer cannot meet its obligations only through disclosure because regardless of whether a broker-dealer discloses, mitigates, or eliminates a conflict, he or she must also satisfy the other components of the rule, including the care obligation. An investment adviser likewise could not meet his or her duty of care solely through disclosure, although he or she could satisfy the duty of loyalty through disclosure and informed consent.

Third, Clayton sought to counter objections that the new Form CRS relationship summary would not achieve its goal of educating consumers about the differences between broker-dealers and investment advisers. Clayton said the relationship summary requires a prominent link to an SEC resource page and that the SEC plans to conduct an educational campaign to inform investors about Regulation BI and related regulations and interpretations (Jay Clayton, Regulation Best Interest and the Investment Adviser Fiduciary Duty: Two Strong Standards that Protect and Provide Choice for Main Street Investors, July 8, 2019).

Clayton re-commits to June 30, 2020 compliance date. As the June 30, 2020 compliance date for Regulation BI approached, it seemed likely that only federal litigation challenging the validity of the regulation could potentially short-circuit the SEC's efforts to bring Regulation BI to fruition (as discussed below, the Second Circuit would uphold Regulation BI). Meanwhile, Clayton had stated that he did not foresee even the COVID-19 pandemic justifying a delay in the compliance date for Regulation BI. Clayton later reaffirmed his commitment to the June 30, 2020 compliance date. However, in his latest statement on the compliance date, Clayton noted several areas of concern regarding Regulation BI: (1) 401(k) rollovers, especially those that are newly authorized by the Coronavirus Aid, Relief and Economic Security (CARES) Act; (2) high risk products that involve derivatives, are less liquid, and are more volatile; (3) COVID-19-related investments, especially those that may involve pump-and-dump schemes or penny stocks; and (4) structured investment vehicles such as special purpose acquisition corporations, which may appeal to retail investors because of "money back" features but which also may be fraught with conflicts of interest (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, April 2, 2020; Jay Clayton, Confirmation of June 30 Compliance Date for Regulation Best Interest and Form CRS, June 15, 2020).

Renewed DOL proposal. The Trump Administration's DOL, currently headed by Eugene Scalia, the late Supreme Court Justice Antonin Scalia's son and one of the attorneys who represented the U.S. Chamber of Commerce in its law suit that resulted in the Fifth Circuit vacating the Obama Administration DOL's fiduciary regulation, formally issued a new proposal titled "Improving Investment Advice for Workers & Retirees Exemption" (RIN 1210-ZA29). The DOL's latest proposal, however, is designed to align DOL policy with the SEC's Regulation BI. The SEC's Clayton quickly issued a statement

© 2020 CCH Incorporated and its affiliates. All rights reserved.

"commend[ing]" the DOL proposal and noting the "Commission's constructive and ongoing engagement with the Department" (Jay Clayton, Statement on the Department of Labor's Investment Advice Proposal, June 29, 2020).

The DOL's 2020 proposal would create a class exemption from ERISA and Internal Revenue Code (IRC) provisions regarding prohibited transaction restrictions. As a result, financial institutions and investment professionals would be allowed to receive certain forms of otherwise prohibited compensation and they could engage in riskless principal transactions and other covered principal transactions. However, financial institutions and investment professionals would have to abide by a set of impartial conduct standards when they provide fiduciary investment advice to retirement investors. These fiduciary advisers also would have to comply with disclosure requirements, have written policies and procedures, conduct retrospective reviews (including annual CEO certifications), satisfy eligibility requirements, and maintain records for a period of six years. A press release announcing the proposal also stated that the DOL will implement portions of the Fifth Circuit opinion that vacated the 2016 DOL fiduciary regulation, including the now reinstated "five-part test" and DOL Interpretive Bulletin 96-1 (See, Interpretive Bulletin 96–1; Participant Investment Education, RIN 1210–AA50, May 30, 1996, 61 F.R. 29586, June 11, 1996).

Section II of the proposal is the centerpiece and it would require financial institutions and investment professionals to comply with impartial conduct standards. The first of these standards states that investment advice must, at the time it is provided, be in the retirement investor's best interest. Unlike Regulation BI, although similar to the DOL's 2016 best interest contract standard, the latest DOL proposed fiduciary regulation does define "best interest," both in the applicable impartial conduct standards and in the definition section of the proposed regulation. Thus, "best interest" would mean:

> … the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims, based on the investment objectives, risk tolerance, financial circumstances, and needs of the Retirement Investor, and does not place the financial or other interests of the Investment Professional, Financial Institution or any affiliate, related entity, or other party ahead of the interests of the Retirement Investor, or subordinate the Retirement Investor's interests to their own (Section II(a)(1) and Section V(a)).

One significant difference, however, between the DOL's 2016 best interest contract exemption regulation and its 2020 proposal is the absence of the phrase "without regard" from the 2020 proposal's definition of " best interest." Instead, for the purpose of aligning the 2020 proposal with Regulation BI, the proposal substitutes the concepts of the financial institution or investment professional not putting its own interest ahead of that of the retirement investor or subordinating the retirement investor's interest to that of the financial institution or investment professional. The 2020 proposal's language is nearly identical to language contained in the SEC's interpretation of the duties of investment advisers (See, Commission Interpretation Regarding Standard of Conduct for Investment Advisers, Release No. IA–5248, June 5, 2019, 84 F.R. 33669 July 12, 2019) ("the adviser must, at all times, serve the best interest of its client and not subordinate its client's interest to its own. In other words, the investment adviser cannot place its own interests ahead of the interests of its client").

The DOL's latest proposal, however, is designed to align DOL policy with the SEC's Regulation BI.

The DOL's 2020 proposal also would impose additional impartial conduct standards and other requirements, including:

- *Compensation*—Compensation received by a financial institution or investment professional must not exceed what is reasonable under specified provisions in ERISA and the IRC.

© 2020 CCH Incorporated and its affiliates. All rights reserved.

- *Best execution*—A financial institution or investment professional must, in accord with federal securities laws, seek the best execution of trades reasonably available under the circumstances.
- *Statements about recommended transactions*—A financial institution's or investment professional's statements to a retirement investor about a recommended transaction or other matters must, at the time they are made, not be materially misleading.
- *Disclosures*—A financial institution, before engaging in an exempted transaction, must provide the retirement investor with: (1) a written acknowledgement that the financial institution and its investment professionals are fiduciaries; and (2) a description of the services to be provided and of material conflicts of interest that is accurate and not misleading in all material respects.
- *Policies and procedures*—A financial institution must: (1) have written policies and procedures regarding compliance with the impartial conduct standards; (2) policies and procedures regarding mitigation of conflicts of interest such that those policies and procedures and incentive practices viewed as a whole are prudently designed to avoid misalignments between the interests of the financial institution and its investment professionals and those of the retirement investor; and (3) a financial institution must document the specific reasons why a rollover is in the retirement investor's best interest.
- *Retrospective review*—A financial institution must at least annually conduct a retrospective review that is reasonably designed to assist in detecting and preventing violations of, and achieving compliance with, the impartial conduct standards and the policies and procedures for compliance with the exemption; a written report on the results of the review must be provided to the financial institution's CEO and CCO; the financial institution's CEO must make specified certifications on an annual basis.

Depending on the outcome of the 2020 general election, a re-elected Trump Administration would likely move forward with adoption of a final DOL standard of care to harmonize DOL's approach with the SEC's Regulation BI. However, the DOL's proposal has a short 30-day comment period that will close August 6, 2020, meaning the exemption could be granted well before the end of 2020. If the proposed exemption is granted, the DOL would make the exemption available 60 days after the final exemption is published in the Federal Register. A group of consumer groups has already asked the DOL to extend the comment period to 90 days (Letter from AFL-CIO, et. al. to U.S. Department of Labor, EBSA Office of Exemption Determinations, July 8, 2020; Improving Investment Advice for Workers & Retirees, Release No. ZRIN 1210–ZA29, 85 F.R. 40834, July 7, 2020). However, a newly elected Democratic Administration could use the OIRA process to stop a Trump DOL proposal or a Democrat-controlled DOL and/or SEC could seek to rescind a final DOL fiduciary rule and/or modify Regulation BI via notice and comment rulemaking. Alternatively, a Democratic-controlled White House and Congress could invoke the Congressional Review Act to disapprove a Trump Administration DOL rule that is inconsistent with Democratic policy goals.

The standards and proposals compared: FINRA/DOL/Congress/Regulation BI. As noted in the introductory materials above, one of the major Republican-led legislative proposals, had it been enacted, would have used the term "best interest" while also referring to elements of FINRA's suitability standard. Although there are obvious differences, there also are many similarities between FINRA Rule 2111 (suitability), the Wagner bill, and Regulation BI. The chief difference is that the Wagner bill and Regulation BI (but not FIRNA Rule 2111) use the term "best interest," albeit without defining the term. FINRA, however, has issued a Regulatory Notice that observed that many cases would impose a best interest requirement on broker-dealers, such that a recommendation must be consistent with the customer's best interest. As a result, the FINRA notice states that a broker-dealer could not make a recommendation to a customer that put the broker-dealer's interest ahead of the customer's interest (See, FINRA Regulatory Notice 12-25, May 18, 2012).

The DOL's 2016 best interest contract exemption regulation did define "best interest," as does the DOL's 2020 proposal to align ERISA with Regulation BI. The chief difference, however, between the DOL's 2016 regulation and its 2020 proposal is that the 2016 definition of "best interest" used the phrase "without regard to" and the 2020 proposal's definition does not use this phrase but instead contains language that touches elements of Regulation BI and the SEC's investor adviser

© 2020 CCH Incorporated and its affiliates. All rights reserved.

interpretation. The Commission, in adopting Regulation BI, explained that the phrase “without regard” was not used in order to avoid reducing retail investors’ choices and increasing costs to retail investors. Regulation BI also explained that the best interest standard is an enhanced standard that avoids confusion that may arise from the inherent ambiguities associated with the phrase “without regard.” Elsewhere in the supplemental materials, the Commission explained that, although FINRA guidance and cases refer to a standard “consistent with” a customer’s best interest, Regulation BI requires that a recommendation be “in” a customer’s best interest, suggesting that for purposes of Regulation BI this is not a mere difference in terminology but a stronger standard than the interpretations of FINRA’s suitability requirement (See, Regulation Best Interest: The Broker-Dealer Standard of Conduct, Release No. 34–86031, June 5, 2019, 84 F.R. 33318, 33331-33332, 33373-33374, July 12, 2019).

The following chart compares FINRA Rule 2111 (before it was recently amended to conform to Regulation BI) to the DOL’s best interest contract exemption issued in 2016, the Wagner bill, and Regulation BI for purposes of illustrating the evolution of regulatory policy regarding standards of conduct for investment advice provided to retail investors across the Obama and Trump Administrations:

Broker-dealer standards compared: the evolution of Regulation BI

Topic	FINRA Rule 2111	DOL Best Interest Contract Exemption (2016)	H.R. 3857	Regulation BI
General requirements	A broker-dealer must have a reasonable basis to believe a recommended transaction or investment strategy involving a security is suitable based on the information obtained through reasonable diligence of the broker-dealer to ascertain the customer’s investment profile.	The best interest contract exemption was an adjunct to the DOL’s regulation defining “fiduciary” that allows certain persons who provide investment advice to retirement investors to receive compensation otherwise banned to fiduciary advisers to employee benefit plans and IRAs under ERISA and the IRC.	When a broker-dealer makes a recommendation to a retail customer, the recommendation shall be in the retail customer’s best interest at the time it is made by: (i) reflecting reasonable diligence; and (ii) reflecting the reasonable care, skill, and prudence that a broker-dealer would exercise based on the customer’s investment profile.	A broker-dealer making a recommendation of any securities transaction or investment strategy involving securities must act in the best interest of the retail customer at the time the recommendation is made without placing the broker-dealer’s interest ahead of the interest of the retail customer.
Obligations	1. Reasonable-basis suitability (suitable for some investors). 2. Customer-specific suitability (suitable for particular customer based on investment profile). 3. Quantitative suitability (series of recommended transactions not excessive and unsuitable taken together based on investment profile).	1. Contract required between financial institution and retirement investor. 2. Financial institution affirmatively states in writing that it and the adviser are fiduciaries. 3. Financial institution and adviser affirmatively state they will adhere to impartial conduct standards. 4. Financial institution affirmatively warrants that it: (i) has policies and procedures reasonably and prudently designed to ensure advisers adhere to impartial conduct standards; (ii) has identified, documented, and has measures to prevent material conflicts; and (iii) does not use or rely upon quotas, appraisals, performance or personnel actions, bonuses, contests, special awards, differential compensation.	1. General disclosure obligation (disclose prior to the point of sale to such customer, in a clear and concise manner the: (i) type and scope of services the broker-dealer provides; (ii) the standard of conduct that applies to the relationship; (iii) the types of compensation the broker-dealer receives; and (iv) any material conflict of interest).	1. Disclosure obligation (disclosure of material facts regarding scope and terms of relationship and of material facts relating to conflicts of interest). 2. Care obligation (reasonable basis to believe that the recommendation: (i) could be in the best interest of at least some retail customers; (ii) is in the best interest of a particular retail customer based on the customer’s investment profile; and (iii) a series of recommended transactions is not excessive and is in the retail customer’s best interest when taken together based on the customer’s investment profile).

© 2020 CCH Incorporated and its affiliates. All rights reserved.

Topic	FINRA Rule 2111	DOL Best Interest Contract Exemption (2016)	H.R. 3857	Regulation BI
Obligations (cont'd)		5. State in the contract, among other things, the best interest standard of care. 6. Note: the best interest contract exemption would have been unavailable if a contract contained ineligible provisions (e.g., exculpatory terms or class action waivers).	2. Conflict of interest obligation (A broker-dealer must avoid, disclose, or reasonably manage any material conflict of interest with a retail customer). Note: The bill would refer to FINRA Rule 2111 regarding the definitions of "reasonable diligence" and "recommendation."	3. Conflict of interest obligation (written policies and procedures reasonably designed to, among other things: (i) identify and, at a minimum disclose, conflicts of interest; (ii) identify and mitigate conflicts that incentivize a broker-dealer to put its own interest ahead of the retail customer's interest; and (iii) identify and eliminate any sales contests, sales quotas, bonuses, and non-cash compensation based on sales in a limited time period). 4. Compliance obligation (written policies and procedures reasonably designed to achieve compliance with Regulation BI).
Investment profile	A customer's investment profile (non-exhaustive list) includes the customer's: 1. Age. 2. Other investments. 3. Financial situation and needs. 4. Tax status. 5. Investment objectives. 6. Investment experience. 7. Investment time horizon. 8. Liquidity needs. 9. Risk tolerance. 10. Any other information the customer may disclose.	The definition of "best interest" suggests the outlines of an investment profile (i.e., "investment objectives, risk tolerance, financial circumstances, and needs of the Retirement Investor").	Incorporates FINRA Rule 2111.	A customer's investment profile (non-exhaustive list) includes the customer's: 1. Age. 2. Other investments. 3. Financial situation and needs. 4. Tax status. 5. Investment objectives. 6. Investment experience. 7. Investment time horizon. 8. Liquidity needs. 9. Risk tolerance. 10. Any other information the customer may disclose.
Best interest defined?	No. But FINRA guidance suggests a best interest standard.	"Best interest" means the adviser: "providing the advice act with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims, based on the investment objectives, risk tolerance, financial circumstances, and needs of the Retirement Investor, without regard to the financial or other interests of the Adviser, Financial Institution or any Affiliate, Related Entity, or other party."	No.	No.
Standard of conduct uses "without regard" language?	No.	Yes.	No.	No.

© 2020 CCH Incorporated and its affiliates. All rights reserved.

Topic	FINRA Rule 2111	DOL Best Interest Contract Exemption (2016)	H.R. 3857	Regulation BI
Retail investor defined?	No. But FINRA Rule 2110(a)(6), dealing with communications with the public, defines "retail investor" to mean any person other than an institutional investor, regardless of whether the person has an account with a member.	"Retirement Investor" means: (i) a participant or beneficiary of a plan subject to Title I of ERISA or described in IRC Section 4975(e)(1)(A), with authority to direct the investment of assets in the plan account or to take a distribution, (2) the beneficial owner of an IRA acting on behalf of the IRA, or (3) a retail fiduciary regarding a plan subject to Title I of ERISA or described in IRC Section 4975(e)(1)(A) or IRA.	A natural person or legal entity, or the legal representative of such natural person or legal entity, in each case other than an institutional account, who: (i) receives a recommendation from a broker-dealer; and (ii) implements such recommendation with such broker or dealer primarily for personal, family, retirement, or household purposes.	A natural person, or the legal representative of such natural person, who: (i) receives a recommendation of any securities transaction or investment strategy involving securities from a broker-dealer; and (ii) uses the recommendation primarily for personal, family, or household purposes.

Source: *Financial Industry Regulatory Authority, Inc. Rule 2111 (Suitability) (as adopted before the amendments to be made by FINRA Regulatory Notice 20-18, June 19, 2020); Best Interest Contract Exemption, Release No. ZRIN 1210–ZA25, April 1, 2016, 81 F.R. 21002, April 8, 2016; Protecting Advice for Small Savers (PASS) Act of 2017 (H.R. 3857) and House Report No. 115-894, August 10, 2018; Regulation Best Interest: The Broker-Dealer Standard of Conduct, Release No. 34–86031, June 5, 2019, 84 F.R. 33318, July 12, 2019.*

The basics of Regulation BI

Regulation BI contains the SEC's new standard of conduct for broker-dealers when dealing with personalized advice about securities made to retail investors. In this context, the best interest standard generally enhances the standard of conduct for broker-dealers as compared to the suitability standard. Regulation BI's best interest obligation consists of four related obligations: (1) a disclosure obligation; (2) a care obligation; (3) a conflicts of interest obligation; and (4) a compliance obligation. Regulation BI also works in tandem with the relationship summary requirements contained in new Form CRS. Form CRS prescribes the contents and delivery requirements for the relationship summary that must be delivered to a broker-dealer's retail customers. According to the supplemental materials accompanying Regulation BI, the regulation was adopted under the broad grant of authority in Dodd-Frank Act Section 913(f), rejected a "one size fits all" approach that a uniform fiduciary standard would entail, and does not create a safe harbor (Regulation Best Interest: The Broker-Dealer Standard of Conduct, Release No. 34–86031, June 5, 2019, 84 F.R. 33318, 33329, 33330, 33333, July 12, 2019).

The Commission also issued two related interpretive releases discussing the "solely incidental" exclusion for broker-dealers from the Investment Advisers Act and discussing the investment advisers' fiduciary standard of conduct. To facilitate compliance, the SEC issued a Small Entity Compliance Guide for Regulation BI. Moreover, the SEC's Division of Trading and Markets has issued FAQs regarding Regulation BI and Form CRS and a workflow diagram for the filing of Form CRS. These guidance documents are extensive but it should be remembered that informal guidance states the views of SEC staff and would not be

Regulation BI's best interest obligation consists of four related obligations: (1) a disclosure obligation; (2) a care obligation; (3) a conflicts of interest obligation; and (4) a compliance obligation. Regulation BI also works in tandem with the relationship summary requirements contained in new Form CRS.

© 2020 CCH Incorporated and its affiliates. All rights reserved.

legally binding (Regulation Best Interest: A Small Entity Compliance Guide, last visited July 14, 2020; Frequently Asked Questions on Regulation Best Interest, last visited July 14, 2020; Frequently Asked Questions on Form CRS, last visited July 14, 2020; Relationship Summary Filing Workflow on IARD & Web CRD®, last visited July 14, 2020).

Best interest obligation. Regulation BI states a general best interest obligation that applies to recommendations about securities made to retail customers by broker-dealers and their associated persons. Specifically, a broker-dealer, or natural person associated with a broker-dealer, must, when recommending any securities transaction or investment strategy involving securities (including account recommendations) to a retail customer, act in the retail customer's best interest at the time of making the recommendation without placing the financial or other interest of the broker-dealer (or associated person) making the recommendation ahead of the retail customer's best interest (Exchange Act Rule 15l-1(a)(1), 17 C.F.R. 240.15l-1(a)(1) at ¶25,423A).

This general obligation applies to recommendations made to retail customers. Regulation BI defines "retail customer" to mean a natural person (or that person's legal representative) who receives a recommendation of any securities transaction or investment strategy involving securities from a broker-dealer or associate of a broker-dealer. The definition also states that the retail customer must use the recommendation primarily for personal, family, or household purposes (Exchange Act Rule 15l-1(b)(1), 17 C.F.R. 240.15l-1(b)(1) at ¶25,423A). The supplemental materials to Regulation BI confirm that a retail customer must both *receive* and *use* a recommendation. The word "use" would entail the following: (1) the retail customer opens a brokerage account regardless of whether the broker-dealer receives compensation; (2) the retail customer has an existing account and receives a recommendation regardless of whether the broker-dealer receives compensation; or (3) the broker-dealer has or will receive compensation, even if the retail customer does not have an account at the firm (Regulation Best Interest: The Broker-Dealer Standard of Conduct, Release No. 34–86031, June 5, 2019, 84 F.R. 33318, 33344, July 12, 2019, at ¶82,301).

The supplementary materials accompanying Regulation BI also suggest how the Commission views certain issues that may arise under Regulation BI. For example, costs associated with a recommendation are one factor, but Regulation BI does not require a broker-dealer to recommend the "lowest cost option" (Regulation Best Interest: The Broker-Dealer Standard of Conduct, Release No. 34–86031, June 5, 2019, 84 F.R. 33318, 33326, July 12, 2019). Additional references to the supplemental materials can be found in the discussion below.

Broker-dealers satisfy their best interest obligation by complying with four related obligations regarding: (1) disclosure; (2) care; (3) conflicts of interest; and (4) compliance. Each of these obligations is discussed in more detail below.

Disclosure obligation. The disclosure obligation under Regulation BI requires a broker-dealer to provide a retail customer with full and fair written disclosure of all material facts regarding the scope and terms of the relationship with the retail investor and of all material facts regarding conflicts of interest associated with the recommendation. With respect to material facts regarding the scope and terms of the relationships with the retail investor, Regulation BI specifically mentions two topics for disclosure:

- That the broker-dealer is acting as such regarding the recommendation; material fees and costs applicable to the retail customer's transactions, holdings, and accounts; and the type and scope of services provided to the retail customer (including material limits on securities or investment strategies involving securities that may be recommended)
- All material facts relating to conflicts of interest associated with the recommendation (Exchange Act Rule 15l-1(a)(2)(i), 17 C.F.R. 240.15l-1(a)(2)(i) at ¶25,423A).

The supplemental materials accompanying Regulation BI state that materiality refers to the *Basic, Inc. v. Levinson* standard, as modified for the Regulation BI context; thus, something is material if there is a substantial likelihood that a reasonable retail customer would consider it important. (Regulation Best Interest: The Broker-Dealer Standard of Conduct, Release No. 34–86031, June 5, 2019, 84 F.R. 33318, 33347, July 12, 2019, at ¶82,301).

Care obligation. The care obligation under Regulation BI includes three components: (1) a general care obligation; (2) a care obligation

© 2020 CCH Incorporated and its affiliates. All rights reserved.

specific to a particular retail customer; and (3) a care obligation regarding series of transactions. As a result, a broker-dealer, in making a recommendation, must exercise reasonable diligence, care, and skill regarding the several care obligations.

A broker-dealer must understand the potential risks, rewards, and costs associated with a recommendation and have a reasonable basis to believe that the recommendation *could* be in the best interest of *at least some* retail customers (emphasis added). This general care obligation is paired with a specific care obligation. Thus, a broker-dealer must also have a reasonable basis to believe the recommendation is in the best interest of a particular retail customer based on that customer's investment profile and the potential risks, rewards, and costs associated with the recommendation; furthermore, the recommendation must not place the financial or other interest of the broker-dealer ahead of the retail customer's interest (Exchange Act Rule 15l-1(a)(2)(ii)(A) and (B), 17 C.F.R. 240.15l-1(a)(2)(ii)(A) and (B) at ¶25,423A).

With respect to a series of transactions, a broker-dealer must have a reasonable basis to believe that a series of recommended transactions (even if the retail customer's best interest is viewed in isolation) is: (1) not excessive and is in the retail customer's best interest when taken together in light of the retail customer's investment profile; and (2) does not place the financial or other interest of the broker-dealer ahead of the retail customer's interest (Exchange Act Rule 15l-1(a)(2)(ii)(C), 17 C.F.R. 240.15l-1(a)(2)(ii)(C) at ¶25,423A).

The care obligation includes multiple references to a retail customer's investment profile. Regulation BI defines "retail customer investment profile" to mean a non-exhaustive list of personal characteristics, including a retail investor's:

- Age;
- Other investments;
- Financial situation and needs;
- Tax status;
- Investment objectives;
- Investment experience;
- Investment time horizon;
- Liquidity needs;
- Risk tolerance;
- Any other information the retail customer may disclose to the broker-dealer in connection with a recommendation (Exchange Act Rule 15l-1(b)(2), 17 C.F.R. 240.15l-1(b)(2) at ¶25,423A).

With respect to account type recommendations, the supplemental materials accompanying Regulation BI state five factors to be used when determining whether a particular account type is in the particular retail customer's best interest:

- The products and services provided in the account;
- The projected costs to the retail customer;
- Alternative account types available;
- Services requested by the retail customer; and
- The retail customer's investment profile.

If a broker-dealer is dually-registered as an investment adviser, the determination would need to consider both brokerage and advisory account types and the eligibility requirements for these accounts types (e.g., account minimums) (Regulation Best Interest: The Broker-Dealer Standard of Conduct, Release No. 34–86031, June 5, 2019, 84 F.R. 33318, 33382-33383, July 12, 2019, at ¶82,301).

In the case of IRAs, rollovers, and workplace retirement plans, key factors include:

- Fees and expenses;
- Available investment options;
- The ability to take penalty-free withdrawals;
- Application of required minimum distributions;
- Protection from creditors and legal judgments;
- Holdings of employer stock; and
- Special features of the existing account.

These factors are in addition to other factors a broker-dealer may be required to consider in making the required evaluation. (Regulation Best Interest: The Broker-Dealer Standard of Conduct, Release No. 34–86031, June 5, 2019, 84 F.R. 33318, 33383, July 12, 2019, at ¶82,301).

Conflict of interest obligation. Regulation BI requires a broker-dealer to establish, maintain, and enforce written policies and procedures reasonably designed to identify and at a minimum disclose (as part of the disclosure obligation), or eliminate conflicts of interest. "Conflict of interest" means: "an interest that might incline a broker, dealer, or a natural person who is an associated person of a broker or dealer—consciously or unconsciously—to make a recommendation that is not disinterested" (Exchange Act Rule 15l-1(b)(3), 17 C.F.R. 240.15l-1(b)(3) at ¶25,423A). As a result, the conflict of interest disclosure required of a broker-dealer contemplates written policies and procedures that address the following items:

© 2020 CCH Incorporated and its affiliates. All rights reserved.

- Identify and at a minimum disclose, or eliminate, all conflicts of interest associated with recommendations (the disclosure aspect of this requirement refers to the disclosure obligation in Exchange Act Rule 15l-1(a)(2)(i), 17 C.F.R. 240.15l-1(a)(2)(i) at ¶25,423A;
- Identify and mitigate any conflicts of interest associated with recommendations that create an incentive for a natural person associated with a broker-dealer to place the broker-dealer's or the associated person's interest ahead of the interest of the retail customer;
- Identify and disclose material limits placed on the securities or investment strategies involving securities that may be recommended to a retail customer and identify and disclose any conflicts of interest associated with those limits (the disclosure aspect of this requirement refers to the disclosure obligation in Exchange Act Rule 15l-1(a)(2)(i), 17 C.F.R. 240.15l-1(a)(2)(i) at ¶25,423A. Moreover, the broker-dealer must prevent the limits and associated conflicts of interest from causing the broker-dealer or associated person to make recommendations that place the broker-dealer's or associated person's interest ahead of the retail customer's interest. The broker-dealer also must identify and eliminate incentives based on sales of specific securities or specific types of securities within a limited time. Regulation BI specifically targets incentives such as sales contests, sales quotas, bonuses, and non-cash compensation (Exchange Act Rule 15l-1(a)(2)(iii), 17 C.F.R. 240.15l-1(a)(2)(iii) at ¶25,423A).

The supplemental materials accompanying Regulation BI include a non-exhaustive list of potential mitigation methods:

- Avoid compensation thresholds that disproportionately increase compensation through incremental increases in sales;
- Minimize compensation incentives for employees to favor one account type or product over others by establishing differential compensation based on neutral factors;
- Eliminate compensation incentives within comparable product lines by capping the credit that an associated person may receive across mutual funds or other comparable products across providers;
- Implement supervisory procedures to monitor recommendations that are near certain thresholds, involve higher compensating, proprietary, or principal products, or which involve rollovers;
- Adjust compensation for associated persons who fail to adequately manage conflicts; or
- Limit the types of retail customers to whom certain products, transactions, or strategies may be recommended (Regulation Best Interest: The Broker-Dealer Standard of Conduct, Release No. 34–86031, June 5, 2019, 84 F.R. 33318, 33392, July 12, 2019, at ¶82,301)

Lastly, according to the supplemental materials accompanying Regulation BI, sales contests and other non-cash compensation incentives must be eliminated because they pose "too strong of an incentive" for a broker-dealer to put her interest ahead of the interest of a retail customer and, thus, cannot be reasonably mitigated. However, the ban on such practices would not reach broker-dealers' employee benefits or training and educational meetings, if these meetings are not based on the sale of specific securities or type of securities in a limited time frame (Regulation Best Interest: The Broker-Dealer Standard of Conduct, Release No. 34–86031, June 5, 2019, 84 F.R. 33318, 33395-33397, July 12, 2019, at ¶82,301).

Compliance obligation. A final compliance obligation requires that a broker-dealer, in addition to its conflict of interest obligation, establish, maintain, and enforce written policies and procedures that are reasonably designed to achieve compliance with Regulation BI (Exchange Act Rule 15l-1(a)(2)(iv), 17 C.F.R. 240.15l-1(a)(2)(iv) at ¶25,423A).

Recordkeeping requirements. Regulation BI requires a broker-dealer to retain certain records relating to retail customer accounts for at least six years after the earlier of: (1) the date the account was closed; or (2) the date on which the information was collected, provided, replaced, or updated (Exchange Act Rule 17a-4(e)(5), 17 C.F.R. 240.17a-4(e)(5) at ¶26,155). These requirements apply to information governed by Exchange Act Rule 17a-3(a)(17) regarding basic customer information, account records to be sent at prescribed intervals, notice of account changes, and updates to reflect changes in an account's investment objectives (Exchange Act Rule 17a-3(a)(17), 17 C.F.R. 240.17a-3(a)(17) at ¶26,154).

© 2020 CCH Incorporated and its affiliates. All rights reserved.

The recordkeeping requirement also applies to information about a recommendation. As a result, Exchange Act Rule 17a-3(a)(35) requires a broker-dealer to retain information about each retail customer to whom a recommendation of any securities transaction or investment strategy involving securities has or will be provided. Specifically, a broker-dealer must retain a record of all information collected from and provided to a retail customer under Regulation BI. A broker-dealer also must retain a record of the identity of each natural person associated with the broker-dealer who is responsible for the account. However, a retail customer's neglect, refusal, or inability to provide or update information required to be retained by a broker-dealer excuses the broker-dealer from obtaining that information (Exchange Act Rule 17a-3(a)(35), 17 C.F.R. 240.17a-3(a)(35) at ¶26,154).

The supplemental materials accompanying Regulation BI state that the recordkeeping requirements exist to aid broker-dealers in demonstrating their compliance with Regulation BI. The Commission also stated that it did not intend to create comprehensive new recordkeeping requirements and that most broker-dealers should already be familiar with the similar requirements regarding FINRA's suitability standard. Moreover, although best interest determinations are made on a recommendation-by-recommendation basis, the same is not required of broker-dealers' efforts to satisfy the recordkeeping requirements (Regulation Best Interest: The Broker-Dealer Standard of Conduct, Release No. 34–86031, June 5, 2019, 84 F.R. 33318, 33398-33399, July 12, 2019, at ¶82,301).

SEC interpretation of the broker-dealer exclusion from the Advisers Act

The Commission also addressed via an interpretive release several issues that could result in confusion under Regulation BI and the Investment Advisers Act regarding the scope of broker-dealer activities excluded from the Act. Advisers Act Section 202(a)(11) defines "investment adviser" to mean, among other things, any person who is compensated for engaging in the business of advising others about the value of securities. Advisers Act Section 202(a)(11)(C) excludes from this definition any broker-dealer who performs these services in a manner that is "solely incidental" to the conduct of the broker-dealer business and who does not receive "special compensation" for those services; this exclusion is known as the broker-dealer exclusion (Investment Company Act Section 202(a)(11) at ¶56,155).

As a result, the Commission said, in its view, consistent with one federal court's opinion and its own prior interpretations of the "solely incidental" language, the broker-dealer exclusion means the following:

> We interpret the statutory language to mean that a broker-dealer's provision of advice as to the value and characteristics of securities or as to the advisability of transacting in securities is consistent with the solely incidental prong if the advice is provided in connection with and is reasonably related to the broker-dealer's primary business of effecting securities transactions. If a broker-dealer's primary business is giving advice as to the value and characteristics of securities or the advisability of transacting in securities, or if the advisory services are not offered in connection with or are not reasonably related to the broker-dealer's business of effecting securities transactions, the broker-dealer's advisory services are not solely incidental to its business as a broker-dealer (footnotes omitted).

The interpretation further stated that the evaluation of whether a broker-dealer's services are solely incidental to its conduct in effecting securities transactions would require examination of the facts and circumstances, the services offered, and the relationship between the broker-dealer and the customer.

Moreover, the interpretation explained that neither the "quantum" nor the "importance" of a broker-dealer's advice determines applicability of the broker-dealer exclusion. To the contrary, the interpretation stated that a broker-dealer's investment advice that otherwise satisfies the requirements of the broker-dealer exclusion can be "consequential" and "need not be trivial, inconsequential, or infrequent."

—*Investment discretion.* The Commission also considered two scenarios that often arise in

© 2020 CCH Incorporated and its affiliates. All rights reserved.

the advisory context: investment discretion and account monitoring. With respect to investment discretion, the Commission said that unlimited discretion would not be solely incidental because it implies an ongoing advisory relationship.

With respect to temporary or limited discretion, the Commission noted seven previous examples that could be consistent with the broker-dealer exclusion, including: (1) discretion regarding the price or the time at which to execute an order; (2) certain actions to be taken when a customer is unavailable; and (3) exchanging one fund for another fund of the same type. The examples generally involved some degree of specification by the customer about how the broker-dealer should act. According to the interpretation, the seven examples would fall within the broker-dealer exclusion because they are in connection with and reasonably related to a broker-dealer's business of effecting securities transactions and do not imply that investment advice is a broker-dealers' primary business.

The Commission, however, also provided three qualifications about broker-dealers' temporary account discretion: (1) the Commission did not endorse the notion that temporary or limited discretion means "a few months" because such duration could indicate a primarily advisory relationship; (2) the Commission said it would be solely incidental for a broker-dealer to buy or sell securities to satisfy margin requirements or other customer obligations that the customer has specified (the interpretation suggested that collateral calls also might be solely incidental); and (3) the Commission said it would be solely incidental for broker-dealers to sell specific bond or other securities if doing so will permit a customer to realize a tax loss on the original position.

—*Account monitoring*. The Commission's interpretive release also addressed the issue of account monitoring. Typically, the provision by a broker-dealer of account monitoring services would fall within the ambit of the Advisers Act. However, the interpretation said that not all account monitoring activities by broker-dealers necessarily fall within the Advisers Act. The interpretation cited two examples of permissible account monitoring that would be solely incidental and, thus, within the scope of the broker-dealer exclusion. In the first example, a broker-dealer agrees with a customer to provide periodic buy, sell, or hold recommendations. In the second example, the broker-dealer voluntarily (without any agreement with the customer) monitors the customer's account and makes a recommendation to the customer based on the voluntary review; the interpretation noted that without an agreement with the customer, this type of activity would not be account monitoring.

The interpretation, however, further noted both in the main text and in several footnotes (Nos. 68 and 69) that each recommendation made under the two examples would be subject to Regulation BI. Moreover, the interpretation cautioned that a broker-dealer who charges a separate fee for account monitoring would fall within the ambit of the Advisers Act. Likewise, a broker-dealer that provides the limited types of account monitoring suggested by the two examples above must be careful not to receive any special compensation that would cause the activity to fall outside the broker-dealer exclusion.

Lastly, the interpretation suggested that a broker-dealer could seek to mitigate any confusion about the character of any account monitoring it provides by adopting appropriately tailored policies and procedures. Similarly, a dually-registered firm could adopt policies and procedures that clearly explain the differences between account monitoring provided to advisory customers and to brokerage customers (Commission Interpretation Regarding the Solely Incidental Prong of the Broker-Dealer Exclusion from the Definition of Investment Adviser, Release No. IA-5249, June 5, 2019, 84 F.R. 33681, July 12, 2019, at ¶82,304).

SEC interpretation of the investment adviser conduct standard

The SEC's interpretive release discussing the fiduciary obligations of investment advisers addresses three topics: (1) the scope of the duty; (2) the duty of care; and the (3) the duty of loyalty. With respect to the general nature of the adviser's fiduciary duty, the interpretation recited that the duty is grounded in both Investment Advisers Act Section 206's antifraud authorities and the Supreme Court's opinion in *SEC v. Capital Gains Research Bureau, Inc.* and that opinion's reliance on equitable principles that form the basis for common law fraud.

© 2020 CCH Incorporated and its affiliates. All rights reserved.

As a result, an adviser (agent) has both a duty of care and a corresponding duty of loyalty to the client (principal). The interpretation stated the adviser's duty thus: "the adviser must, at all times, serve the best interest of its client and not subordinate its client's interest to its own. In other words, the investment adviser cannot place its own interests ahead of the interests of its client." The adviser's fiduciary duty also is principles-based, non-waivable, and applies to the entirety of the adviser-client relationship, but also must be viewed in light of the agreed scope of the adviser-client relationship.

When Clayton defended Regulation BI and the related interpretations a month after its adoption, he would specifically call attention to the use of "subordinate" and "best interest" in the investment adviser interpretation. According to Clayton, it would be appropriate for an adviser to state that "…they "put their client's interest first." Peirce's earlier statement on the adoption of Regulation BI also would briefly highlight the word "subordinate," albeit for the purpose of noting that the SEC now used the word "subordinate' instead of "subrogate;" the latter term, she said, had been previously misused in the fiduciary context. For example, the supplementary materials to the 2010 amendments to Form ADV in one instance had stated: "[u]nder the Advisers Act, an adviser is a fiduciary whose duty is to serve the best interests of its clients, which includes an obligation not to *subrogate* clients' interests to its own" (emphasis added).

Before discussing the details of the SEC's interpretation of the investment adviser fiduciary duty, Regulation BI's economic analysis section provided a quick textual comparison of key features of the adviser fiduciary duty and the best interest duty for broker-dealers. These features can be compared via the following chart:

Topic	Advisers	Broker-dealers
Fiduciary or other duty	Principles-based; adviser must act in retail client's best interest and must not put own interest ahead of client's interest; applies to entirety of adviser-client relationship.	Principles-based but with a prescriptive set of minimum requirements; broker-dealer must act in retail client's best interest and must not put own interest ahead of client's interest; applies at time of recommendation.
Account monitoring	Ongoing monitoring is part of regulatory regime.	Agreed upon but only to the extent solely incidental to brokerage business.
Conflicts of interest	Full and fair disclosure with client's informed consent.	Broker-dealers must have written policies and procedures.

Source: *Regulation Best Interest: The Broker-Dealer Standard of Conduct, Release No. 34–86031, June 5, 2019, 84 F.R. 33318, 33463, July 12, 2019.*

—*Duty of care*. According to the interpretation, the adviser's duty of care encompasses three elements: (1) the client's best interest; (2) best execution of trades; and (3) ongoing advice and account monitoring. With respect to the best interest obligation, an adviser must understand and make a reasonable inquiry into the client's investment objectives either through the client's investment profile (retail clients) or the investment mandate (institutional clients). In the case of a retail client, the investment profile, which includes the client's financial situation, level of financial sophistication, investment experience, and financial goals, is similar to the more rigorously defined investment profile contained in Regulation BI.

The adviser also must have a reasonable belief that advice provided is in the client's best interest, which depends on the context, such as the portfolio to be managed and the client's investment objectives. An adviser also must reasonably investigate an investment to ensure the investment is not based on materially inaccurate or incomplete information. An adviser, however, could recommend a higher cost investment if doing so is in the client's best interest.

With respect to best execution, the interpretation stated that an adviser has a duty to ensure that a client's total cost or proceeds are the most favorable under the circumstances when the adviser is responsible for choosing broker-dealers to execute trades on a client's behalf. The interpretation further explained that "best qualitative execution," not the lowest cost execution, is the touchstone. Moreover, an adviser

© 2020 CCH Incorporated and its affiliates. All rights reserved.

should periodically and systematically evaluate the execution received for a client.

The duty of care also includes advice and monitoring. The interpretation stated that an adviser should provide advice and monitoring at a frequency that is in the client's best interest in light of the agreed scope of the adviser-client relationship.

—*Duty of loyalty*. The interpretive release states that an adviser's fiduciary duty requires the adviser to not put its own interest ahead of the client's interest. As a result, full and fair disclosure of all material facts to the client is essential, especially when an adviser is dually-registered as a broker-dealer. A dually-registered firm should make written disclosures at the start of a relationship that clearly state when it will act in an advisory capacity and when it will act in a brokerage capacity. A firm's disclosures should also state when advice is limited to products offered via an affiliated broker or adviser.

Moreover, an adviser must eliminate or disclose all conflicts of interest which could incline the adviser (consciously or unconsciously) to render advice that is not disinterested. The interpretive release, however, noted that disclosure and consent alone would not satisfy an adviser's duty to act in the client's best interest. First, the disclosure must be sufficiently specific such that a client can understand it and decide whether or not to consent. Examples of insufficient disclosure include the use of phrases like "other clients" or "may," as in there "may" be a conflict of interest, or if "may" precedes a list of all potential conflicts but the list obscures actual conflicts. These situations would require additional explanation by the adviser. However, "may" could be appropriate if no conflict currently exists and a conflict could arise later.

Second, an adviser must eliminate or fully and fairly disclose conflicts that arise when it allocates investment opportunities to clients. The interpretation noted that conflicts can arise between an adviser and a single client or in a scenario in which an adviser might seek to allocate investment opportunities among many clients.

The interpretive release noted that an adviser can mull the nature and objectives of its relationship with a client and the scope of the adviser-client relationship in making such allocations. An adviser also need not follow any particular method of allocation, although an adviser must not allow its methods to prevent it from providing advice in the client's best interest.

Consent by an advisory client to a relationship after full and fair disclosure of conflicts must be informed. The interpretive release concluded that an adviser could not infer or accept client consent if the adviser was aware, or reasonably should have been aware, that the client did not understand the nature and import of the conflict. But even so, an adviser need not affirmatively determine that the client understood the disclosure or that the client's consent was informed; the purpose of the disclosure is to ensure the client is in a position to understand and provide informed consent (Commission Interpretation Regarding Standard of Conduct for Investment Advisers, Release No. IA-5248, June 5, 2019, 84 F.R. 33669, July 12, 2019, at ¶82,303).

Relationship summary on Form CRS

Form CRS is a disclosure document related to Regulation BI in which a broker-dealer or investment adviser provides important information to a retail investor about the nature of the relationship between the broker-dealer or investment adviser and the retail investor. This information is called the "relationship summary," which Form CRS defines to mean "a written disclosure statement prepared in accordance with these Instructions that you must provide to *retail investors*" (Form CRS, General Instruction 11.D. at ¶57,101). The SEC also has issued a Small Entity Compliance Guide that summarizes the requirements for the relationship summary.

Form CRS is contained in Part 3 of Form ADV. Information to be included in the relationship summary must address the following topics: (1) client/customer relationships and services offered; (2) fees, costs, conflicts of interest, and the applicable standard of conduct; (3) the broker-dealer's or investment adviser's legal or disciplinary history; and (4) how a retail investor may obtain additional information. There are different requirements for filing Form CRS depending on whether the filer is a broker-dealer or an investment adviser. Moreover, Form ADV is the vehicle by which an investment adviser files Form CRS; the following discussion will emphasize

© 2020 CCH Incorporated and its affiliates. All rights reserved.

Form ADV's requirements pertaining to Form CRS only, but readers should also consult Form ADV for more generalized filing requirements for Form ADV (See, Form ADV at ¶57,101).

Filing Form CRS. A broker-dealer must file a current Form CRS with the Commission through the Central Registration Depository (CRD) operated by the Financial Industry Regulatory Authority, Inc. A broker-dealer that has no retail customers is not required to prepare or file Form CRS (Exchange Act Rule 17a-14(b)(1) and 17a-14(b)(2), 17 C.F.R. 240.17a-14(b)(1) and (b)(2); Form CRS, General Instruction 7.A.).

An investment adviser must file a current Form CRS as Part 3 of Form ADV electronically through the Investment Adviser Registration Depository (IARD) absent a hardship exemption. A note to the applicable rule text states that an investment adviser that is not required to deliver Form CRS to any clients is not required to prepare and file Form CRS as part of its Form ADV (Investment Advisers Act Rule 203-1(a)(1) and Note 1 to paragraph (a)(1), 17 C.F.R. 275.203-1(a)(1); Form CRS, General Instruction 7.A.).

A firm that is dually-registered as an investment adviser and a broker-dealer must file Form CRS via both the IARD and the CRD (Form CRS, General Instruction 7.A.(i)).

Transition rules for filing Form CRS. Transitional rules govern the filing of Form CRS by broker-dealers and investment advisers through the June 30, 2020 compliance date for Regulation BI. As a result, a broker-dealer that is registered with the SEC as a broker-dealer before June 30, 2020 must file its initial Form CRS starting May 1, 2020 but not later than June 30, 2020. A broker-dealer that files a registration application with or has a pending registration application with the SEC on or after June 30, 2020 must comply with the applicable regulations by the date on which its registration application becomes effective (Exchange Act Rule 17a-14(f), 17 C.F.R. 240.17a-14(f) at ¶26,165; Form CRS, General Instruction 7.C.(ii) at ¶57,101).

An investment adviser that is registered or has a pending registration application with the SEC before June 30, 2020 must amend its Form ADV to include its initial Form CRS pursuant to Part 3 of Form ADV starting May 1, 2020 but not later than June 30, 2020. The SEC will reject an initial application filed after June 30, 2020 which omits the relationship summary (Investment Advisers Act Rule 204-1(e), 17 C.F.R. 275.204-1(e) at ¶56,322; Form CRS, General Instruction 7.C.(i) at ¶57,101).

A broker-dealer or investment adviser must, within 30 days of the date on which it is first required to file Form CRS, deliver to each existing customer/client who is a retail investor its current Form CRS. Moreover, the broker-dealer or investment adviser must begin using Form CRS as of the date the firm is first required to file Form CRS in order to satisfy the Form CRS delivery requirement (Exchange Act Rule 17a-14(f), 17 C.F.R. 240.17a-14(f) at ¶26,165; Investment Advisers Act Rule 204-5(e), 17 C.F.R. 275.204-5(e) at ¶56,326; Form CRS, General Instruction 7.C.(iv). at ¶57,101).

Who must deliver a relationship summary? Registered broker-dealers and registered investment advisers must deliver the relationship summary to retail investors. Broker-dealers and investment advisers are those entities registered with the Commission under Exchange Act Section 15 and/or Investment Advisers Act Section 203, respectively. However, if a broker-dealer or investment adviser has no retail investors, that broker-dealer or investment adviser is not required to prepare or file Form CRS. (Exchange Act Rule 17a-14(c), 17 C.F.R. 240.17a-14(c) at ¶26,165; Investment Advisers Act Rule 204-5(b), 17 C.F.R. 275.204-5(b) at ¶56,326).

To whom must the relationship summary be delivered? The relationship summary must be delivered to retail investors. "Retail investor" means "[a] natural person, or the legal representative of such natural person, who seeks to receive or receives services primarily for personal, family or household purposes" (Exchange Act Rule 17a-14(e)(2), 17 C.F.R. 240.17a-14(e)(2) at ¶26,165; Investment Advisers Act Rule 204-5(d)(2), 17 C.F.R. 275.304-5(d)(2) at ¶56,326; Form CRS, General Instruction 11.E. at ¶57,101).

When must Form CRS be delivered? A broker-dealer must deliver Form CRS to each retail investor before or at the earliest of: (1) a recommendation of an account type, securities transaction, or investment strategy involving securities; (2) placing an order for the retail investor; or (3) opening a brokerage account for the retail investor (Exchange Act Rule 17a-14(c)(1), 17 C.F.R. 240.17a-14(c)(1) at ¶26,165; Form CRS, General Instructions 7.B.(ii) and 7.C.(iii). at ¶57,101).

With respect to a broker-dealer's existing retail customers, the broker-dealer must deliver Form

© 2020 CCH Incorporated and its affiliates. All rights reserved.

CRS before or at the time of: (1) opening a new account that is different from the retail investor's existing account; (2) recommending that the retail investor roll over assets from a retirement account into a new or existing account or investment; or (3) recommending or providing a new brokerage service or investment that does not necessarily involve the opening of a new account and would not be held in an existing account (Exchange Act Rule 17a-14(c)(2), 17 C.F.R. 240.17a-14(c)(2) at ¶26,165; Form CRS, General Instruction 9.A. at ¶57,101).

Similarly, an investment adviser must deliver Form CRS to each retail investor before or at the time of entering into an investment advisory contract with the retail investor. Form CRS clarifies that delivery must occur in this time frame even if the agreement with the retail investor is oral (Investment Advisers Act Rule 204-5(b)(1), 17 C.F.R. 275. 204-5(b)(1) at ¶56,326; Form CRS, General Instructions 7.B.(i) and 7.C.(iii). at ¶57,101). With respect to existing clients, an investment adviser must deliver Form CRS before or at the time of: (1) opening a new account that is different from the retail investor's existing account; (2) recommending that a retail investor roll over assets from a retirement account into a new or existing account or investment; or (3) recommending or providing a new investment advisory service or investment that does not necessarily involve the opening of a new account and would not be held in an existing account (Investment Advisers Act Rule 204-5(b)(2), 17 C.F.R. 275.204-5(b)(2) at ¶56,326; Form CRS, General Instruction 9.A. at ¶57,101).

Form CRS clarifies the timing of delivery of the relationship summary by a firm that is registered with the SEC as both a broker-dealer and as an investment adviser. A dual registrant must deliver the relationship summary at the earliest of the times required of broker-dealers or investment advisers (Form CRS, General Instructions 7.B.(iii). at ¶57,101).

Moreover, a broker-dealer or investment adviser must deliver a current Form CRS to each retail investor within 30 days upon request and without charge (Exchange Act Rule 17a-14(c)(5), 17 C.F.R. 240.17a-14(c)(5) at ¶26,165; Investment Advisers Act Rule 204-5(b)(5), 17 C.F.R. 275.204-5(b)(5) at ¶56,326; Form CRS, General Instructions 1.C. and 9.B. at ¶57,101).

Updating the relationship summary. A broker-dealer or investment adviser must amend its Form CRS by following the instructions for amendments contained in Form CRS (Exchange Act Rule 17a-14(b)(3), 17 C.F.R. 240.17a-14(b)(3) at ¶26,165; Investment Advisers Act Rule 204-1(a)(2), 17 C.F.R. 275.204-1(a)(2) at ¶56,322). As a result, a broker-dealer must update its relationship summary within 30 days of any information contained in the relationship summary becoming materially inaccurate. A broker-dealer also must include an exhibit that highlights the most recent changes by marking the revised text or providing a summary of material changes (Form CRS, General Instructions 8.A. and 8.C. at ¶57,101).

Additionally, Form ADV amendments must be filed electronically unless the investment adviser has obtained a continuing hardship exemption, in which case, the investment adviser would mail the completed Part 3 (and other relevant parts) to the SEC via FINRA (Investment Advisers Act Rule 204-1(b), 17 C.F.R. 275.204-1(b) at ¶56,322).

Communicating changes to Form CRS. A broker-dealer or investment adviser must communicate changes to Form CRS to each retail investor who is an existing customer/client within 60 days of when the amendments are required to be made. A broker-dealer or investment adviser must not charge a customer/client for the update. However, communication of changes to Form CRS can be made via an amended relationship summary or via another disclosure delivered to the customer/client (Exchange Act Rule 17a-14(c)(4), 17 C.F.R. 17a-14(c)(4) at ¶26,165; Investment Advisers Act Rule 204-5(b)(4), 275 C.F.R. 204-5(b)(4) at ¶56,326; Form CRS, General Instruction 8.B. at ¶57,101).

Posting Form CRS. A broker-dealer or an investment adviser must post their current Form CRS prominently on their public website (if any) in a location and format that is easily accessible to retail investors (a paper relationship summary must be first among documents delivered). The similar Investment Advisers Act rule, however, does not specify that the website must be a "public" website, as does the equivalent rule for broker-dealers, although the applicable instruction within Form CRS does mention "public website" in the context of both broker-dealers and investment advisers. The instruction also clarifies that the relationship summary and any updates to it may be delivered electronically, consistent with SEC guidance contained in the document titled "Use of Electronic Media by

© 2020 CCH Incorporated and its affiliates. All rights reserved.

Broker-Dealers, Transfer Agents, and Investment Advisers for Delivery of Information." The relationship summary also may be delivered to a retail customer/client in the manner the customer/client requested. If electronic delivery is used, the relationship summary must be presented prominently; if the relationship summary is delivered in paper format, the relationship summary must be the first document in the package of documents (Exchange Act Rule 17a-14(c)(3), 17 C.F.R. 240.17a-14(c)(3) at ¶26,165; Investment Advisers Act Rule 204-5(b)(3), 17 C.F.R. 275.204-5(b)(3) at ¶56,326 Form CRS, General Instructions 10.A., 10.B., 10.C., and 10.D. at ¶57,101).

Other disclosure obligations. The rules pertaining to Form CRS provide that broker-dealers and investment advisers remain subject to any additional disclosure obligations beyond those applicable to Form CRS that they may have under other federal laws or regulations, or under the rules of a self-regulatory organization. The relevant provision for investment advisers also states that investment advisers may have additional obligations under state laws and regulations (Exchange Act Rule 17a-14(d), 17 C.F.R. 240.17a-14(d) at ¶26,165; Investment Advisers Act Rule 204-5(c), 17 C.F.R. 275.204-5(c) at ¶56,326).

What records must be maintained? A broker-dealer must, under Exchange Act Rule 17a-3(a)(24), retain a record of the date each Form CRS was provided to each retail investor. This requirement also applies to any Form CRS provided to a retail investor before an account was opened. Moreover, the records required to be retained under Exchange Act Rule 17a-3(a)(24), plus a copy of each Form CRS, must be retained for a period of at least six years after the record or Form CRS is created (Exchange Act Rule 17a-3(a)(24), 17 C.F.R. 240.17a-3(a)(24) at ¶26,154; Exchange Act Rule 17a-4(e)(10), 17 C.F.R. 240.17a-4(e)(10) at ¶26,155; Form CRS, General Instruction 6.A. at ¶57,101).

An investment adviser must retain: (1) a copy of each Form CRS and any amendment or revision to Form CRS; and (2) a record of the dates that each Form CRS and each amendment or revision to Form CRS given to any client or prospective client who later becomes a client (Investment Advisers Act Rule 204-2(a)(14)(i) at ¶ 56,323; Form CRS, General Instruction 6.A. at ¶57,101).

Contents of the relationship summary. Form CRS includes a set of general instructions that provide information about how to draft the relationship summary in terms of format, writing style, and use of graphics. These instructions also include special considerations for dual registrants. Moreover, Form CRS includes a number of items that state particular requirements for the content to be included in the relationship summary. The several items address a number of topics, including: (1) an introduction with basic information; (2) information about relationships and services; (3) information about fees, costs, conflicts, and the standard of conduct; (4) disciplinary history; and (5) certain additional information (See, Form CRS, General Instruction 1 and Items 1 through 5 at ¶57,101).

Format. Broker-dealers and investment advisers must respond to each item within Form CRS in the order those items appear in the instructions. Disclosures in the relationship summary must be limited to what is called for by the instructions and items within Form CRS. The relationship summary also is subject to page limits:

- Paper format—2 pages.
- Dual registrants with single relationship summary for both advisory and brokerage services (paper format)—4 pages.
- Dual registrants/affiliates with separate relationship summaries for advisory and brokerage services—2 pages for each relationship summary.

The instruction also states that broker-dealers and investment advisers must be reasonable regarding paper size, font size, and margins. Electronically delivered relationship summaries must adhere to the electronic equivalent of the paper format page limits (Form CRS, General Instruction 1. at ¶57,101).

Moreover, both investment advisers and broker-dealers must present their brokerage and investment advisory information with equal prominence and in a manner that clearly distinguishes and facilitates comparison of the two types of services. An investment adviser or broker-dealer also may acknowledge other financial services the firm provides beyond investment advisory or brokerage services, including insurance, banking, retirement services, or investment advice offered under state registration or licensing (Form CRS, General Instructions 5.A., 5.B.(i), and 5.C. at ¶57,101).

© 2020 CCH Incorporated and its affiliates. All rights reserved.

Writing style. The relationship summary should be written using plain English and should consider the retail investor's level of financial experience. In the late 1990s, at a time when plain English in SEC filings was a prominent topic of discussion that resulted in adoption of the Plain English Disclosure regulation, the SEC's Office of Investor Education and Advocacy published a document titled "A Plain English Handbook," which the general instructions to Form CRS suggest broker-dealers and investment advisers may refer to in drafting the relationship summary. Much of the explicit advice on drafting provided in the applicable instruction focuses on common sense drafting techniques, for example, avoiding jargon or legalese (at least without further explanation) and avoiding multiple negatives. Broker-dealers and investment advisers are cautioned to avoid making "exaggerated or unsubstantiated claims," to avoid boilerplate, and to avoid placing undue emphasis on services or investments not available to retail investors.

The instruction also recites the omnipresent securities law admonition that information in the relationship summary must be true and cannot omit material facts necessary to make the disclosures, in light of the circumstances under which they were made, not misleading. Inapt disclosures or conversation starters, though, can be omitted or modified. However, delivery of the relationship summary alone may not be enough to satisfy other legal obligations (Form CRS, General Instruction 2. at ¶57,101).

Graphics. Form CRS encourages the use of graphics (e.g., dual-column charts) to depict information required to be disclosed. A relationship summary that is posted on a firm's website should incorporate online tools that can populate information based on a retail investor's selections. Likewise, a relationship summary posted on a firm's website must include hyperlinks or other means to access referenced information (a paper relationship summary may include URL addresses or Quick Response (QR) codes). Explanatory and supplemental materials must be responsive to the particular item within Form CRS addressed by the information, and a broker-dealer or investment adviser cannot "obscure or impede" the understanding of the information presented (Form CRS, General Instruction 3. at ¶57,101).

Format of conversation starters. The conversation starters required by several items within Form CRS must be displayed using text features that make them more noticeable and prominent versus other discussion text. Additional information regarding services, fees, and conflicts of interest required by items within Form CRS also must be presented in a manner that is more noticeable and prominent versus other discussion text (Form CRS, General Instructions 4.A and 4.C. at ¶57,101).

For broker-dealers and investment advisers that provide only online services or automated investment advisory services without a particular individual available to talk to a retail investor, the firm must provide a page or section on its website that answers each of the conversation starters questions while also providing in the relationship summary a means to access that information. For broker-dealers and investment advisers that provide automated investment advisory or brokerage services and still make a person available to talk to retail investors, that person must be available to discuss the conversation starters with a retail investor (Form CRS, General Instruction 4.B. at ¶57,101).

Special considerations for dual registrants. Form CRS imposes additional requirements regarding the contents of the relationship summary for firms that are dually registered with the SEC as broker-dealers and investment advisers. Form CRS defines "dual registrant" as a firm that is registered with the SEC as both a broker-dealer and an investment adviser and which offers services to retail investors as both a broker-dealer and an investment adviser. Form CRS suggests that a firm which provides one, but not both, types of services to retail investors would not be a dual registrant. As an example, Form CRS posits that a dually registered firm that provides investment advisory services to retail investors but limits its brokerage services to only institutional investors would not be a dual registrant for purposes of Form CRS (Form CRS, General Instruction 11.C. at ¶57,101).

A dual registrant is "encouraged" to prepare a single relationship summary, although a dual registrant may prepare separate relationship summaries for its investment advisory and brokerage services. Regardless of whether a dual registrant prepares a single relationship summary or

© 2020 CCH Incorporated and its affiliates. All rights reserved.

separate relationship summaries, it must present its brokerage and investment advisory information with equal prominence such that its services are clearly distinguished and comparable. For a dual registrant that prepares separate relationship summaries, both must be delivered at the same time and with equal prominence regardless of whether the retail investor qualifies for those services or accounts. Similar requirements apply when a broker-dealer or investment adviser has affiliates or provides certain additional services (Form CRS, General Instruction 5.A. at ¶57,101).

Form CRS also imposes limits on the length of the relationship summary. The relationship summary for a dual registrant with a single, paper relationship summary is limited to four pages; dual registrants/affiliates with separate paper relationship summaries are limited to two pages for each relationship summary. Electronic relationship summaries must adhere to the electronic equivalent of the paper length limits (Form CRS, Instruction 1.C. at ¶57,101).

Form CRS prescribes "conversation starters" or questions a retail investor can ask of a broker-dealer or investment adviser. With respect to a dual registrant, Form CRS requires inclusion of the following conversation starter: "If you are a *dual registrant*, include: 'Given my financial situation, should I choose an investment advisory service? Should I choose a brokerage service? Should I choose both types of services? Why or why not?'" (Form CRS, Item 2.D.(iii). at ¶57,101). Similar requirements apply to disclosures about a broker-dealer's or investment adviser's legal obligations when providing recommendations. For a dual registrant, Form CRS prescribes the following: "If you are a *dual registrant* that prepares a single *relationship summary*, use the heading: 'What are your legal obligations to me when providing recommendations as my broker-dealer or when acting as my investment adviser?'" (Form CRS, Item 3.B. at ¶57,101).

Form CRS also clarifies the timing of delivery of the relationship summary for dual registrants. As a result, a dual registrant must deliver the relationship summary at the earliest of the times required of broker-dealers or investment advisers (Form CRS, General instruction 7.B.(iii). at ¶57,101). For a broker-dealer, delivery is to be made at the earliest of: (1) a recommendation of an account type, securities transaction, or investment strategy involving securities; (2) placing an order for the retail investor; or (3) opening a brokerage account for the retail investor (Exchange Act Rule 17a-14(c)(1), 17 C.F.R. 240.17a-14(c)(1) at ¶ 26,165; Form CRS, General Instruction 7.B.(ii). at ¶57,101). For an investment adviser, delivery must occur before or at the time of entering into an investment advisory contract with the retail investor (similar requirements apply to opening new accounts of a different type, rollovers, and new advisory services or investments that may not involve a new account but are not held in an existing account). Form CRS clarifies that delivery must occur in this time frame even if the agreement with the retail investor is oral (Investment Advisers Act Rule 204-5(b)(1), 17 C.F.R. 275. 204-5(b)(1) at ¶56,326; Form CRS, General Instruction 7.B.(i). at ¶57,101).

Item 1. Item 1 of Form CRS requires the firm to provide basic information, including the date of the relationship summary, which must be displayed prominently in the header or footer on the first page (and in a similar location if the relationship summary is in electronic form). The firm also must provide an introduction in which it states its name and whether it is registered with the SEC as a broker-dealer, an investment adviser, or both. A firm must state that advisory and brokerage services and fees differ and that this fact is important for retail investors to understand. A firm may include references to membership in FINRA or the Securities Investor Protection Corporation. Moreover, the relationship summary must state that retail investors can access free and simple tools on the SEC's website (Investor.gov/CRS) (Form CRS, Item 1. at ¶57,101).

Item 2. Under Item 2 of Form CRS, a broker-dealer or investment adviser must discuss relationships and services under the heading "What investment services and advice can you provide me?" The relationship summary must describe the services offered, such as brokerage, investment advisory services, or both, plus any material limits on these services. The description must also discuss whether the firm provides account monitoring and whether the firm accepts discretionary authority (broker-dealers may, but are not required, to state whether they accept limited discretionary authority). Broker-dealers that offer recommendations should consider whether they are subject to the Investment Advisers Act. A firm also must explain whether it

© 2020 CCH Incorporated and its affiliates. All rights reserved.

makes available advice regarding a limited set of products (e.g., proprietary products) and whether retail investors are subject to account minimums or other requirements. Broker-dealers and investment advisers can include additional information (Form CRS, Items 2.A., 2.B., and 2.C. at ¶57,101).

Item 2 also requires the firm to include five conversation starters. These are specific questions a retail investor can ask of a broker-dealer or investment adviser to obtain further information about the scope of the services offered by the broker-dealer or investment adviser. For example, a retail investor could ask questions about whether to choose a broker-dealer or an investment adviser or both, how the broker-dealer or investment adviser will make recommendations, and what are the broker-dealer's or investment adviser's qualifications. Additional conversation starters are required by other items within Form CRS (Form CRS, Item 2.D. at ¶57,101).

Item 3. Under Item 3 of Form CRS, a broker-dealer or investment adviser must discuss a range of topics under the heading "What fees will I pay?" The item requires a description of principal fees and costs, including the frequency with which they are imposed and any related conflicts they pose, and any additional fees and costs. Broker-dealers are required to describe their transaction-based fees (i.e., more trades generate more fees, which may incentivize the broker-dealer to encourage trading), while investment advisers must discuss ongoing asset-based fees, fixed fees, wrap fees, and other direct fees. The item further requires that the relationship summary include a statement to the effect that a retail investor pays fees regardless of whether an investment gains or loses money and that fees and costs will reduce any gains. Moreover, the relationship summary must include a conversation starter regarding how fees and costs may impact an investment and how a hypothetical amount invested would be impacted by fees and costs: "Help me understand how these fees and costs might affect my investments. If I give you 10,000 to invest, how much will go to fees and costs, and how much will be invested for me?" (Form CRS, Item 3.A. at ¶57,101).

Item 3 further requires a broker-dealer or investment adviser to discuss the applicable legal standard for the particular services offered to a retail investor. The item prescribes the text of headings to be used and other disclosures to be made in the relationship summary. The prescribed language must appear in a heading that varies depending on whether the person is a broker-dealer, investment adviser, or dual registrant. The prescribed language also varies depending upon whether a broker-dealer does or does not make recommendations subject to Regulation BI, and upon whether a dual registrant prepares a single relationship summary and does or does not make recommendations as a broker-dealer subject to Regulation BI. Item 3 also includes a prescribed conversation starter regarding how conflicts of interest may affect a retail investor and how the broker-dealer or investment adviser will handle those conflicts: "How might your conflicts of interest affect me, and how will you address them?" (Form CRS, Item 3.B. at ¶57,101).

A final component of Item 3 requires that a broker-dealer or investment adviser make certain disclosures about how they are compensated under the heading "How do your financial professionals make money?" For one, the relationship summary must summarize any cash and non-cash compensation received and how those payments may raise conflicts of interest. Moreover, the relationship summary must discuss various compensation factors, including pay that is based on the amount of client assets serviced, the time and complexity required to meet a client's needs, products sold, product sales commissions, and revenue earned from advisory services or recommendations (Form CRS, Item 3.C. at ¶57,101).

Item 4. Under Item 4 of Form CRS, a broker-dealer or investment adviser must state whether or not they disclose or are required to disclose disciplinary history under the heading "Do you or your financial professionals have legal or disciplinary history?" If the answer is "Yes," then, with certain exceptions, the broker-dealer or investment adviser must disclose legal or disciplinary information contained in Form ADV, Form BD, or Forms U4, U5, or U6. Even if a broker-dealer or investment adviser does not disclose or is not required to disclose disciplinary history, the broker-dealer or investment adviser must still refer a retail investor to a search tool on the SEC's website (Investor.gov/CRS) where the retail investor can research the broker-dealer or investment adviser. Moreover, the broker-dealer or investment adviser must include a conversation starter in its relationship summary regarding whether

© 2020 CCH Incorporated and its affiliates. All rights reserved.

the broker-dealer or investment adviser has a disciplinary history and what type of conduct was involved (Form CRS, Item 4. at ¶57,101).

Item 5. Item 5 of Form CRS requires a broker-dealer or investment adviser to provide basic contact information so that a retail investor can obtain additional information about the firm's brokerage or investment advisory services and request a copy of the relationship summary; this information must be prominently displayed at the end of the relationship summary. The broker-dealer or investment advisor also must provide a telephone number so retail investors can request current information and copies of the relationship summary. Lastly, the relationship summary must include conversation starters regarding who is the retail investor's primary contact at the broker-dealer or investment adviser, whether that person is a representative of a broker-dealer or investment adviser, and who the retail investor can contact to voice concerns about that person's conduct (Form CRS, Item 5. at ¶57,101).

Examination and enforcement

What might examination and enforcement of Regulation BI look like after the June 30, 2020 compliance date passes? The supplemental materials accompanying Regulation BI provide some indication of what compliance with the regulation might look like. The SEC's Office of Compliance Inspections and Examinations (OCIE) also issued two Risk Alerts on April 7, 2020 that offer at least a partial look forward at Regulation BI compliance examinations and enforcement. Both Risk Alerts emphasize firms' good faith efforts to comply with Regulation BI and Form CRS.

Scienter, safe harbor, and waiver. The supplemental materials accompanying Regulation BI confirm that scienter need not be shown to establish a violation of Regulation BI. Similarly, Regulation BI does not create a safe harbor because each of the component obligations is mandatory such that non-compliance with any one of them would violate the general best interest obligation contained in Regulation BI. Similarly, Regulation BI would not alter other broker-dealer obligations under federal securities laws, including application of the SEC's general antifraud authorities. Moreover, a broker-dealer cannot waive compliance with Regulation BI, nor could a retail customer agree to waive the protections afforded by Regulation BI (Regulation Best Interest: The Broker-Dealer Standard of Conduct, Release No. 34–86031, June 5, 2019, 84 F.R. 33318, 33327, 33333, July 12, 2019, at ¶82,301).

The supplemental materials accompanying Regulation BI confirm that scienter need not be shown to establish a violation of Regulation BI.

Regulation BI examinations. OCIE stated in its Regulation BI Risk Alert that examinations of firms' compliance with Regulation BI were likely to occur during the first year of formal compliance with the regulation. The overall focus of these examinations, OCIE stated, would be on two items: (1) Does the firm have policies and procedures reasonably designed to achieve compliance? and (2) Has the firm made reasonable progress in implementing these policies and procedures? (OCIE Risk Alert, Examinations that Focus on Compliance with Regulation Best Interest, April 7, 2020)

OCIE also stated that examinations would specifically target firms' documentation regarding the four Regulation BI obligations of disclosure, care, conflicts of interest, and compliance. With respect to disclosure, OCIE said it will examine the scope and terms of relationships, including the capacity in which recommendations are made. Document requests could address a range of topics, including fee schedules, how registered personnel are compensated, account monitoring, material limits on accounts and services, and lists of proprietary products sold to customers.

Examinations of the care obligation could target a variety of sources of information about retail investors' profiles, firms' processes for forming a reasonable basis to believe a recommendation is in a retail customer's best interest, how firms make recommendations for rollovers and other significant investment decisions, and how firms make recommendations for risky or more costly products.

© 2020 CCH Incorporated and its affiliates. All rights reserved.

OCIE stated it will examine a firm's policies and procedures regarding the conflicts of interest obligation by considering whether these documents address incentives that may place a firm's interest ahead of a customer's interest, including conflicts related to material limits on securities or investment strategies, and the elimination of specific types of conflicts (e.g., sales contests).

Lastly, OCIE stated that examinations of Regulation BI issues will address the compliance obligation. Document requests could target firms' policies and procedures regarding controls, remediation of non-compliance, and training. Moreover, OCIE emphasized that Regulation BI examinations will be risk-based, although OCIE could address additional topics as needed. OCIE also included in the Risk Alert an appendix that contains a sample list of information that may be requested by OCIE.

Form CRS examinations. OCIE also issued a Form CRS Risk Alert in which it said it plans to examine firms regarding compliance with the requirements of the Form CRS relationship summary. As with Regulation BI compliance examinations, initial examinations of Form CRS will focus on whether firms have made a good faith effort to comply with Form CRS. OCIE specifically directed firms seeking additional compliance information to the Form CRS adopting release and to the related Small Entity Compliance Guide (OCIE Risk Alert, Examinations that Focus on Compliance with Form CRS, April 7, 2020).

According to the supplemental materials contained in Regulation BI, the regulation does not create a new private right of action or right of rescission.

Moreover, OCIE stated that it will focus on several specific topics. With respect to delivery and filing, OCIE will examine if firms have filed Form CRS with the Commission and posted the relationship summary on their public websites. OCIE also will examine firms' handling of key dates, such as initial delivery to their existing retail customers by July 30, 2020, and delivery to new retail customers (a footnote to the Form CRS Risk Alert explained that the July 30, 2020 date was calculated to be 30 days after the June 30, 2020 compliance date for purposes of delivering Form CRS within 30 days of the date on which a firm must file Form CRS with the Commission).

OCIE also will examine the content of firms' Forms CRS. As a result, OCIE will look for completeness and whether the information contained in the form is true and correct. Key topics will include firms' descriptions of relationships and services, descriptions of fees and other costs, and descriptions of conflicts of interest.

Finally, OCIE will examine firms' Forms CRS for the use of plain English, whether firms make timely updates to their Forms CRS, and whether firms have policies and procedures to govern their delivery and recordkeeping obligations.

On July 27, 2020, the SEC's staff Standards of Conduct Implementation Committee, established at the time Regulation BI and related releases were adopted, issued a public statement that, while not singling out a particular type of Form CRS disclosure that had been reviewed and found problematic, nevertheless suggested that completeness and clarity might be issues for some firms. "The relationship summaries reviewed to date generally reflect effort by firms to meet the content and format requirements of Form CRS, and the Committee's initial reviews have identified good examples of simple, clear disclosures. At the same time, the Committee's initial reviews have identified examples that may lack certain disclosures or could be clearer or otherwise improved," said the committee statement (Statement by the Staff Standards of Conduct Implementation Committee Regarding New Form CRS Disclosures, July 27, 2020).

FINRA statement regarding OCIE risk alerts. FINRA issued a statement confirming that it will take the same approach as OCIE to initial enforcement of Regulation BI and Form CRS. According to FINRA, Regulation BI-related enforcement will be an "iterative process" aimed initially at ensuring broker-dealers' good faith efforts to comply with Regulation BI and Form CRS. FINRA, however, noted that it was prepared to work with firms regarding compliance, especially in light of the ongoing COVID-19 pandemic. Still, FINRA said that it could take enforcement action if it were to

© 2020 CCH Incorporated and its affiliates. All rights reserved.

observe "customer harm or conduct that would have violated current standards (e.g., suitability)" (FINRA Statement on SEC's OCIE Risk Alerts for Reg BI and Form CRS, April 08, 2020).

Private enforcement. According to the supplemental materials contained in Regulation BI, the regulation does not create a new private right of action or right of rescission. The Commission stated that it did not intend to create such rights. The Commission also noted that Regulation BI is in addition to other obligations broker-dealers may have under other provisions within the federal securities laws and related regulations (Regulation Best Interest: The Broker-Dealer Standard of Conduct, Release No. 34–86031, June 5, 2019, 84 F.R. 33318, 33327, July 12, 2019).

With respect to implied private rights of action more generally, courts typically have looked to the U.S. Supreme Court's decision in *Cort v. Ash*, which stated several factors to be considered regarding whether Congress intended for a statute to be privately enforced. The *Cort* factors, however, have been severely criticized by some justices in later decisions and, thus, it may be more challenging under current practice to persuade a court to imply a private right of action (See, Kristin E. Hickman & Richard J. Pierce, Jr., Administrative Law Treatise Sixth Edition, §20.8 (discussing *Cannon v. University of Chicago* and its progeny regarding how some justices would significantly limit the reach of *Cort v. Ash*).

In the securities law setting, many federal statutes do not explicitly provide for a private right of action, although some more generalized antifraud and anti-manipulation provisions do allow for private lawsuits. Even in the absence of a private right of action specific to Regulation BI, retail customers might be able to invoke these antifraud and anti-manipulation provisions to hold broker-dealers accountable. However, despite several fairly recent Supreme Court decisions upholding the private right of action under Exchange Act Section 10(b) and Rule 10b-5, the court also has expressed a reluctance to further extend this private right of action. Moreover, the recent trend in the Supreme Court is to focus more on the statutory text rather than legislative history in determining whether Congress intended to create a private right of action. As a result, the absence of express language in Dodd-Frank Act Section 913, the primary, but not the only statutory authority relied on by the SEC in promulgating Regulation BI, to create an explicit private right of action would likely impair efforts by retail investors to persuade courts to imply such a right of action (See, Fanto, Gross, and Poser, Broker-Dealer Law and Regulation, §18.02[C][2] (discussing when the federal securities laws allow an express private right of action, an implied private right of action, and no private right of action)).

Likewise, the Commission said in the adopting release for Form CRS that Form CRS was not intended to create a private right of action. Specifically, the Commission noted that it added the phrase " in light of the circumstances under which they were made" to the phrase "the relationship summary may not omit any material facts necessary in order to make the disclosures … not misleading" in order to clarify that the content a firm includes or does not include in its relationship summary should be viewed in the context of the relationship summary being a summary. The additional language also would be consistent with other Commission statements regarding the need for firms to not make misleading statements in their filings. Elsewhere in the adopting release, the Commission observed that one public comment on Form CRS had asked the Commission to include language stating that Form CRS was not intended to create a private right of action. The commenter was concerned that a requirement that firms disclose the applicable standard of conduct in the relationship summary might create an implied contractual right that could lead to a private right of action (Form CRS Relationship Summary; Amendments to Form ADV, June 5, 2019, 84 F.R. 33492, 33504, 33530, July 12, 2019).

Exchange Act Section 18, however, allows for private suits against any person who makes a statement in a document filed with the Commission that was at the time and in the light of the circumstances under which it was made false or misleading with respect to any material fact. The plaintiff must not have known the statement was false or misleading. But a plaintiff who relied on the statement and bought or sold a security at a price that was affected by the statement may obtain damages. The defendant may assert the defense that they acted in good faith and without knowledge the statement was false or misleading. The cause of action must be brought within one year of the discovery of facts

© 2020 CCH Incorporated and its affiliates. All rights reserved.

constituting the cause of action, but not more than three years after the cause of action accrued. Section 18 may be invoked against broker-dealers, although a broker-dealer's liability under the section would arise for reasons other than their status as a broker-dealer (See, Fanto, Gross, and Poser, Broker-Dealer Law and Regulation, §18.02[B], n. 63).

FINRA rules conformed to Regulation BI

FINRA has updated its rulebook to conform its rules to the SEC's Regulation BI. The amendments render FINRA Rule 2111 on suitability inapplicable whenever a broker-dealers' customer's account would be subject to Regulation BI. The amendments also revise FIRNA Rule 2310 (direct participation programs), Rule 2320 (variable contracts of an insurance company), Rule 2341 (investment company securities), and Rule 5110 (corporate financing), to provide that permitted non-cash payments received by (or made by) members must be consistent with Regulation BI, although such payments remain limited to certain specified circumstances (e.g., gifts not exceeding $100 per person annually). FINRA said the SEC had approved the amendments and that the amendments become effective on June 30, 2020, the same date on which compliance with Regulation BI began (FINRA Regulatory Notice 20-18, June 19, 2020).

Regulation BI litigation

Thus far, only two legal challenges to Regulation BI have been brought in federal court and both assert that the final regulation exceeds the SEC's authority and violates the Administrative Procedure Act because the final regulation is arbitrary and capricious. These cases, however, do not raise the question of federal preemption, which likely would be raised in a court challenge to a state fiduciary standard for broker-dealers that is stronger than the standard contained in Regulation BI.

In one case, the state of New York took the lead in challenging the validity of Regulation BI on behalf of six other states, California, Connecticut, Delaware, Maine, New Mexico, Oregon, plus the District of Columbia. The other case was brought by XY Planning Network, LLC (XYPN), a network of financial planners who are registered investment advisers and, thus, subject to the fiduciary standard contained in the Investment Advisers Act, but otherwise compete for business with broker-dealers who are subject to a lesser standard of conduct.

The states and XYPN argued that the broker-dealer business model has evolved, in large part because of modern technology, to one that emphasizes investment advice to the exclusion of more traditional, and now less profitable, broker-dealer order execution services. As a result, they argued that the current suitability standard of conduct for broker-dealers is no longer valid, at least in the context of personalized investment advice about securities provided to retail customers. Collectively, the petitioners believe that Regulation BI, even though it raises the standard of conduct for broker dealers, is just as confusing to retail investors as the suitability standard and that Regulation BI falls short of what is required by the Dodd-Frank Act (State Brief; State Reply Brief; XYPN Brief; XYPN Reply Brief). The SEC countered by relying heavily on its theory of a broad discretionary grant of authority under the Dodd-Frank Act to set a standard of conduct for broker-dealers (SEC Brief).

Jurisdiction. New York and XYPN initially filed their lawsuits in the U.S. District Court for the Southern District of New York, but soon afterwards, filed a petition for review of Regulation BI in the Second Circuit. The district court, on its own motion, had dismissed the complaints for lack of subject matter jurisdiction. In the Second Circuit, New York, XYPN, and the SEC focused their briefs and oral arguments on Article III standing and statutory construction of Dodd-Frank Act Section 913.

Although the question of whether the U.S. District Court for the Southern District of New York or the Second Circuit properly had jurisdiction of the cases was not addressed at oral argument, the state petitioners, in their main brief, disputed that any of the statutory provisions cited by the SEC authorized Regulation BI and, thus, the federal securities laws did not confer exclusive jurisdiction in the federal appeals courts. The following discussion reviews the jurisdictional issues in this case because similar issues have arisen in previous challenges to SEC rulemaking under the Dodd-Frank Act.

© 2020 CCH Incorporated and its affiliates. All rights reserved.

With respect to jurisdiction, the SEC argued that the Second Circuit is the proper locus of the case under Exchange Act Section 25(b)(1), which lists numerous provisions from which persons adversely affected by a rule can appeal directly to an appropriate federal appeals court via a petition for review. Specifically, the SEC cited Exchange Act Sections 15(c)(6) (broker-dealers must abide by SEC regulations) and 17(a) (recordkeeping rules for broker-dealers).

The state petitioners' brief questioned the SEC's theory of why the case should be brought directly in the Second Circuit rather than in the district court. Specifically, the state petitioners disputed the SEC's assertion that district court jurisdiction is inapt because the SEC partially relied on Exchange Act sections listed in Exchange Act Section 25(b)(1), which specifies the types of rules that can be directly appealed to a federal appeals court, as part of the SEC's authority for adopting Regulation BI.

XYPN's brief asserted that venue was proper in the Second Circuit because the firm resides within, and has its principal place of business within, the Second Circuit. As a result, XYPN, unlike the state petitioners, did not seriously contest the Second Circuit's jurisdiction over the petition for review.

The district court, on its own motion, dismissed both the state petitioners' and investment adviser lawsuits against the SEC in September 2019 because the court lacked subject matter jurisdiction. The district court observed that a court can consider whether it has jurisdiction at any time and that the default venue for challenging a federal agency rule is the district court, unless a direct review statute requires the challenge to be brought in a federal appeals court (direct review is a common procedure because it can avoid duplication of effort, but statutes do not always provide for direct review). The state petitioners' brief, however, noted that the court said its dismissal was without prejudice and that the cases could be refiled in the district court if the Second Circuit were to determine that it lacked jurisdiction and did not transfer the cases to the district court.

Petitions for review of SEC regulations issued pursuant to the Dodd-Frank Act have previously run into hurdles regarding jurisdiction. Cases in this context typically involve a petitioner that is trying to bootstrap its petition into the federal appellate courts despite the lack of statutory support for appellate jurisdiction. Although there is at least some basis that direct review of Regulation BI in the U.S. Court of Appeals is proper, two cases reaching the opposite conclusion regarding two different SEC regulations provide examples of the range of arguments petitioners make when seeking direct appellate review of SEC rules.

In a case challenging the SEC's resource extraction issuers rule, the petitioners simultaneously filed petitions for review in the U.S. District Court and the U.S. Court of Appeals for the District of Columbia. The D.C. Circuit ultimately dismissed the petition for review filed there without prejudice and without transferring the case (the petition already had been filed in the district court) because the specific Exchange Act section that was the basis for the resource extraction issuers rule was not listed in Exchange Act Section 25(b)(1). By way of background, Exchange Act Section 25(b)(1) provides for direct appeal to the U.S. Courts of Appeal for "rule[s]" based on specified Exchange Act sections; by comparison, Exchange Act Section 25(a) provides for direct review by federal appellate courts regarding "final order[s]." In its decision, the unanimous D.C. Circuit panel also rejected the petitioner's arguments that circuit precedent regarding the Investment Advisers Act should apply (interpreting "orders" to mean "orders" and "rules"), that Congress's failure to update Exchange Act Section 25(b)(1) created an ambiguity that augured in favor of appellate jurisdiction, and that review in the district court would be duplicative because the district court would rule based on the administrative record instead of conducting fact finding.

Likewise, in a subsequent case challenging the SEC's credit risk retention rule, another unanimous D.C. Circuit panel transferred the case to the district court because it lacked jurisdiction. In that case, the panel rejected the petitioners' assertion that a broad array of federal statutes justified direct review in the appellate court and instead reasoned that the "joint" nature of the regulation (it was promulgated by the SEC and multiple banking regulators), coupled with the lack of any Congressional update to include the specific Exchange Act section in Exchange Act Section 25(b)(1), deprived the D.C. Circuit of jurisdiction.

© 2020 CCH Incorporated and its affiliates. All rights reserved.

Article III standing. The state petitioners explained in their main brief that Article III standing exists for them because they could lose more than $97 million in in tax revenues on investors' gains from securities transactions. The state petitioners also asserted that reduced investment returns in retirement accounts could require them to expend greater amounts on state aid to the elderly.

During oral argument, Ester Murdukhayeva, Assistant Solicitor General, State of New York, addressed standing for the first time during rebuttal. She said if one assumes the states win on the merits, then the SEC would have to impose a fiduciary standard of conduct on broker-dealers. In other words, the relevant comparison for standing purposes is between the congressional mandate (impose a fiduciary standard) and what the SEC actually did (Regulation BI falls short of a fiduciary standard of conduct) and not the status quo ante (broker-dealers adhere to the suitability standard of conduct). With respect to the injury prong of constitutional standing, Murdukhayeva said the state petitioners could lose tax revenues if Regulation BI stands. Murdukhayeva also urged the panel to focus on the existence of an injury rather than the magnitude of that injury.

For XYPN, Article III standing was predicated on competitor standing. Here, XYPN asserted that one of its network members was injured because its broker-dealer rivals can offer "identical or nearly identical" services without being subject to a true fiduciary standard. As a result, XYPN claims injury from broker-dealers pursuing their own interests when dealing with their clients (petitioners cannot do this) and by broker-dealers describing their standard of care using the term "best interests" without having to distinguish themselves from investment advisers. XYPN asserted that its injury is traceable to the SEC's adoption of final Regulation BI. Lastly, XYPN said the court can redress such an injury in a decision favorable to XYPN because the SEC would be more likely to issue a new rule for broker-dealers that either complies with the mandate contained in Dodd-Frank Act Section 913(g) or a new rule that resolves any confusion about the term "best interests."

Deepak Gupta, of Gupta Wessler PLLC, represented XYPN at oral argument. One of the judges sought clarification that the key to Gupta's argument on behalf of XYPN was that even if Regulation BI imposes more stringent rules on the investment adviser petitioners' competitors, there would still be ongoing confusion about what the broker-dealer standard of conduct is. Gupta replied that was correct, but that regulations can do different things and it was not necessary for XYPN to show that the entire regulation favored its competitors because all the investment adviser petitioners had to do was identify an injury traced to the regulation that arises from competing in the same marketplace as the firm's competitors.

The SEC's brief noted that the state petitioners never discussed causation and standing, placing all of their emphasis on injury in fact. According to the SEC, the state petitioners did not show that Regulation BI increased the alleged harm of conflicted advice; rather, Regulation BI imposed greater requirements on broker-dealers than the current suitability standard does. With respect to causation, the SEC said the state petitioners' claims about lost tax revenues are too speculative. Moreover, the SEC said a favorable decision by the court would not redress the state petitioners' claims because such a decision would once again subject broker-dealers to the existing suitability standard, not the fiduciary standard the state petitioners claim the SEC must impose on broker-dealers. Lastly, the SEC said the state petitioners failed to consider the possibility that they will lose tax revenues if the SEC imposes a fiduciary standard on broker-dealers, some of which might quit the market altogether.

Moreover, the SEC said XYPN lacked standing because Regulation BI imposes greater burdens on broker-dealers, not fewer burdens. On a related note, the SEC said XYPN cannot show that if the SEC imposed a fiduciary standard on broker-dealers, broker-dealers would then choose to become investment advisers and join XYPN's network as members. The SEC further asserted that Regulation BI's disclosure obligation and the relationship summary (not at issue in the case) would address the investment adviser petitioners' worries that retail investors will be confused about investment advisers and broker-dealers. XYPN, the SEC said, cannot show causation for reasons similar to those the SEC asserted against the state petitioners. Lastly, the SEC said redressability was lacking regarding XYPN because there is no statutory requirement that the SEC do anything that would benefit XYPN, if they win their case.

© 2020 CCH Incorporated and its affiliates. All rights reserved.

At oral argument Jeffrey Berger, Senior Litigation Counsel for the SEC, urged the court to skip the merits of the case and instead dismiss the case for lack of constitutional standing. Berger said the state petitioners and XYPN premised their cases on the SEC doing nothing, but that approach upends their case on the issue of redressability because, if the SEC does nothing to enhance the broker-dealer standard of conduct, the states and the investment adviser petitioners would be hurt even more because broker-dealers would continue to operate under the old suitability standard. Berger also disputed that the petitioners could show causation because Regulation BI imposes more requirements on broker-dealers and the injuries asserted (for states lost tax revenues and for the investment adviser petitioners competitive harm) are too conjectural.

Interpreting Dodd-Frank Act Section 913. The main difference between how the state petitioners and XYPN on the one hand, and the SEC on the other, interpret Dodd-Frank Act Section 913 comes down to whether they see the statute's language as a series of steps in a process leading to rulemaking or as a choice between two or more rulemaking options. The following subsections describe these opposing approaches to construing Section 913 in greater detail.

—*State petitioners' merits argument.* The state petitioners and XYPN argued in their briefs that Dodd-Frank Act Section 913, the provision authorizing the SEC to impose a fiduciary standard on broker-dealers, should be interpreted as a series of steps in a process that leads to such standard for broker-dealers. That is, the SEC must conduct a study on broker-dealers and retail investors (Section 913(b)), the study is subject to certain considerations (Section 913(c)), the SEC must seek public comment on the report on the study (Sections 913(d) and (e)), then the SEC may "commence" a rulemaking (Section 913(f)), and, lastly, the SEC must give substance to the rulemaking by adopting a fiduciary standard that is equal to the standard for investment advisers (Section 913(g)).

The state petitioners argued that the SEC's Regulation BI ignored the mandate set forth in Dodd-Frank Act Section 913 by adopting a final regulation that is contrary to and in excess of SEC authority. Specifically, the word "may" as used in Section 913 did not give the SEC flexibility about whether or not to adopt a fiduciary standard for broker-dealers with respect to personalized investment advice about securities to retail customers but instead posed for the SEC a choice of subjecting broker-dealers to only the Investment Advisers Act's fiduciary standard or the entirety of the Investment Advisers Act. Put another way, Congress did not authorize the SEC to not impose a fiduciary standard on broker-dealers providing personalized investment advice about securities to retail investors.

The state petitioners also argued that the SEC's interpretation of "solely incidental" under the Investment Advisers Act sweeps too broadly and should not receive judicial deference under either *Chevron* (permissible or reasonable construction of an ambiguous statute) or *Skidmore* (a lesser type of deference granted to the extent a court is persuaded by the agency's interpretation). Said the state petitioners; "Yet, so long as a broker-dealer retains some vestige of its order execution services, the Commission's 'solely incidental' interpretation would exempt any investment advice from the protections of the Advisers Act and Section 913. In effect, the Commission would allow broker-dealers to evade regulation when it is their provision of brokerage services, rather than their investment advice, that is truly 'incidental' to their main business."

Murdukhayeva made similar arguments during oral argument before the Second Circuit. One judge noted that if the SEC had done nothing, the status quo (the suitability standard) would have continued, but if the states win this lawsuit, then the standard of conduct goes back to suitability. Murdukhayeva said that once the SEC makes a predicate finding that factually determines broker-dealers no longer provide incidental advice, then the SEC must impose a fiduciary standard under either the Investment Advisers Act or Dodd Frank Act Section 913(g). Under Section 913(g) broker-dealers would retain some flexibility regarding the sale of proprietary products, the receipt of commission- or fee-based compensation, and in being relieved of any continuing duty of care or loyalty (i.e., account monitoring) after providing personalized investment advice about securities to a retail customer.

But Murdukhayeva emphasized that the Investment Advisers Act is both the default standard and an independent source of SEC authority. One judge asked if the Dodd-Frank Act is irrelevant.

© 2020 CCH Incorporated and its affiliates. All rights reserved.

Murdukhayeva answered that the Dodd-Frank Act is material to the case because it reinforces the Investment Advisers Act approach. Murdukhayeva also said that the presence of "may" in Section 913(f) did not give the SEC wide latitude to adopt a standard of conduct for broker-dealers and that the Investment Advisers Act must be read alongside the Dodd-Frank Act.

That reply prompted a judge to ask what "may" actually refers to. Here, Murdukhayeva replied that "may" as used in Section 913(f) refers to the considerations the SEC must address in the congressionally required study of the broker-dealer industry (See Sections 913(c)(9) and (10)), including applying the Investment Advisers Act standard of conduct to broker-dealers wholesale, whether to impose a fiduciary duty on broker-dealers under Section 913(g), and whether to recommend to Congress that the broker-dealer exclusion be eliminated from the Investment Advisers Act definition of "investment adviser" (See Investment Advisers Act Section 202(a)(11)). The panel's questioning appeared to be directed at understanding if the SEC can invoke "may" in Section 913(f) as a discretionary basis to impose any standard of conduct it deems appropriate. Murdukhayeva closed this segment of the argument by noting that the SEC's Section 913 study never mentioned Section 913(f). In fact, the study recommended that the SEC use its authority under Section 913(g) to impose a uniform fiduciary standard for broker dealers.

—XYPN's merits argument. XYPN's brief largely tracked the arguments made by the state petitioners. XYPN argued that the SEC's Regulation BI exceeded the agency's Dodd-Frank Act authority by not reading Sections 913(f) and 913(g) together as providing authority for the SEC to regulate the standard of conduct for broker-dealers and that that standard be the same as the standard for investment advisers. In other words, the SEC could retain the existing suitability standard for broker-dealers or it could adopt a fiduciary standard for broker-dealers, but the SEC could not adopt a standard different from what the Dodd-Frank Act prescribed. According to XYPN, Section 913(f) is "procedural" only and does not provide the SEC with information about the standard of conduct, which instead is provided by Section 913(g). Moreover, the investment adviser petitioners argued that Regulation BI disregards the "without regard" language of Section 913(g)(1), that is, to "act in the best interest of the customer *without regard* to the financial or other interest of the broker, dealer, or investment adviser providing the advice" (emphasis added).

As an aside, XYPN's brief cited the Supreme Court's opinion in *King v. Burwell* for the proposition that the several components of Section 913 must be read in context. In *King v. Burwell*, the Supreme Court interpreted the Affordable Care Act's separate, and seemingly irreconcilable, provisions dealing with tax credits, and found a way to construe the provisions based on their context within the ACA to uphold portions of the ACA. Here, XYPN quoted the operative language from *King v. Burwell*: "courts 'must read the words in their context and with a view to their place in the overall statutory scheme.'" *King v. Burwell* previously was cited in the SEC whistleblower case the Supreme Court decided several years ago, in which the justices reversed the Ninth Circuit's finding that the Dodd-Frank Act's definition of an SEC "whistleblower" applied to the anti-retaliatory provisions contained elsewhere in the whistleblower statute. The dissenting judge in the Ninth Circuit decision was especially critical of that court's use of *King v. Burwell*: "In my view, we should quarantine *King* and its potentially dangerous shapeshifting nature to the specific facts of that case to avoid jurisprudential disruption on a cellular level." *King v. Burwell* may have played a role in the Ninth Circuit's whistleblower decision, but the Supreme Court never cited the case in reaching its holding that the plain language of the Dodd-Frank Act's SEC whistleblower provision required a whistleblower to report directly to the SEC in order to invoke the Dodd-Frank Act's anti-retaliatory provisions. Neither the state petitioners nor the SEC cited *King v. Burwell* in their briefs in the Regulation BI case, and the Second Circuit panel did not mention the case at oral argument.

Gupta, on behalf of XYPN, conceded at oral argument the Second Circuit panel's observation that the SEC could have done nothing. But Gupta added that if the SEC chooses to act, it must abide by a floor; that is, the requirement in Section 913(h) that the SEC harmonize enforcement of broker-dealer and investment adviser standards of conduct. According to Gupta, however, the SEC

© 2020 CCH Incorporated and its affiliates. All rights reserved.

"doubled down" on the existing confusion about the broker-dealer standard of conduct by adopting Regulation BI. One of the arguments both the state petitioners and XYPN made in their briefs was that while Regulation BI technically raised the standard of conduct for broker-dealers, it does so in a way that further confuses broker-dealers with investment advisers by referring to "best interest," which is undefined in Regulation BI and can have different meanings under Regulation BI and the Investment Advisers Act.

Gupta also reiterated to the Second Circuit panel the process theory of the case, in which Section 913 represents a series of steps toward adoption of a fiduciary standard for broker-dealers. Moreover, Gupta sought to counter the SEC's theory of a broad grant of regulatory discretion under Section 913(f). Gupta posited that when Congress indicates by statute that an agency has authority to adopt regulations, it tends to use words like "promulgate" or "provide," rather than the word "commence" in Section 913(f).

—*SEC's merits argument.* With respect to the substantive claims, the SEC responded that Dodd-Frank Act Section 913 authorized the SEC to pursue either of two paths via separate discretionary grants of rulemaking authority. The SEC argued that, under the first path, Section 913(f) provides that the agency "may" engage in rulemaking to address the standards of care for broker-dealers and investment advisers regarding personalized investment advice about securities to retail customers. In promulgating rules, the SEC must consider the staff study mandated by Section 913. The SEC argued that, under the second path, the agency "may" engage in rulemaking to require a broker-dealer providing personalized investment advice about securities to a retail customer to abide by the standard of conduct specified in Investment Advisers Act Section 211 which, as amended, further provides that the standard of conduct must be no less stringent than the standard applicable to investment advisers under Investment Advisers Act Sections 206(1) and (2). Sections 206(1) and (2) are antifraud provisions that have been held by courts to impose fiduciary duties on investment advisers (See e.g., *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 194 (1963)).

As a result, the SEC argued that it could choose between the two regulatory paths or choose to follow neither path, that is, to not further regulate the standard of care for broker-dealers. Moreover, the SEC argued that Regulation BI was not arbitrary and capricious because it preserves a lower cost option for retail investors versus potentially more costly investment advisers (the SEC asserted the DOL's fiduciary standard that was vacated by the Fifth Circuit increased costs to investors with some firms considering leaving the business altogether because of the DOL rule, but that these "trends" had eased after the Fifth Circuit vacated the DOL rule). The SEC also disputed the assertion by the states and investment adviser petitioners that Regulation BI is functionally equivalent to FINRA's suitability standard for broker-dealers and that Regulation BI creates gaps between the standards for broker-dealers and advisers.

Berger, arguing for the SEC, began the portion of his oral argument dealing with statutory construction by noting how both sides seemed to agree that the plain text of the statute should resolve the case. Berger, however, rejected the petitioners' theory of Section 913 being procedural in character and instead reiterated that Section 913(f) contains "classic discretionary language" in the form of the word "may." One of the judges then asked about the purpose served by Section 913(g). Berger replied that Section 913(g) has two purposes: (1) ensure the SEC can impose a fiduciary standard if the required study recommends against such standard; and (2) decrease the likelihood of a legal challenge to SEC rulemaking based on the broker-dealer exclusion contained in the Investment Advisers Act.

Berger also said that Section 913(g) provides "guardrails" if the SEC adopts a fiduciary standard for broker-dealers because it requires the agency to preserve some aspects of the broker-dealer business model (i.e., regarding commissions/fees, proprietary products, and no need for account monitoring). Berger added that within Section 913, subsections (f) and (g) do not cross-reference each other, the use of "shall" and "may" in Section 913 was the product of a legislative compromise over the House and Senate versions of what would become Section 913, and that Congress had the opportunity to eliminate the broker-dealer exclusion and chose not to eliminate the provision.

Lastly, the SEC disputed that a fiduciary standard must not allow a fiduciary to consider its own financial interest. Said the SEC's brief: "The text of the rule—which petitioners barely

© 2020 CCH Incorporated and its affiliates. All rights reserved.

discuss—provides that a broker-dealer 'shall act in the best interest of the retail customer at the time the recommendation is made, without placing [its own interests] ahead of the interest of the retail customer.' Broker-dealers can satisfy this general obligation only by complying with four component obligations: the Disclosure, Care, Conflict of Interest, and Compliance Obligations" (citations omitted). XYPN had observed in its brief that a broker-dealer operating under Regulation BI could consider its own financial interest as long as it does not put its own interest "ahead of" the customer's interest. According to XYPN, Regulation BI's language contrasts with Section 913(g), which requires a broker-dealer to act "without regard" to their own financial interest.

On June 26, 2020, the Second Circuit issued its opinion in the federal court challenge to Regulation BI and provided the SEC the green light the agency needed to fully implement Regulation BI.

—*Congressional amici.* Current and former Democratic members of Congress, including the Dodd-Frank Act's namesakes, former Sen. Chris Dodd (D-Conn) and former Rep. Barney Frank (D-Mass), argued that the SEC's interpretation of Section 913 was wrong. According to the Democratic members of Congress, the state and investment adviser petitioners are correct in understanding Section 913 to present a series of steps leading to a fiduciary standard of conduct for both broker-dealers and investment advisers that harmonizes gaps in existing law as found by the study required by Section 913. Moreover, the Democratic members of Congress argued that Sections 913(f) and 913(g) must be read together; thus, Section 913(f) authorizes the SEC to "commence a rulemaking," while Section 913(g) provides the substances of that rulemaking and further authorizes the SEC to "promulgate rules." Any other interpretation would render Section 913(g) superfluous (Brief of Current and Former Members of Congress as Amici Curiae in Support of Petitioners, January 3, 2020).

Current and former Republican members of Congress, including Rep. Ann Wagner (R-Mo), the author of a "best interest" bill, submitted an amicus brief in support of the SEC. According to the Republican amici, Section 913(f) functions as a "dimmer switch" instead of a "circuit breaker." As a result, Section 913(f) is typical of a Congressional grant of rulemaking discretion and does not pose "a binary choice between imposing either a single duty on all investment professionals or doing nothing at all." The Republican amici further cited as support for their view the use of the plural "standards" in Section 913(f) (apparently suggestive of a non-binary choice) and the reference from Section 913(c)(14) back to the SEC's authority in Section 913(f). Moreover, the Republican amici also argued that Section 913(g) was included in the Dodd-Frank Act to remove any ambiguity about the SEC's ability to impose a fiduciary standard of conduct on broker-dealers given the existence of the statutory broker-dealer exclusion contained in the Investment Advisers Act, if the SEC opted to impose such a duty. Said the Republican amici: "Subsection 913(g) thus sets a new outer bound on the SEC's authority, but it is part of a broader statutory scheme, not a standalone directive to adopt a particular substantive rule." (Brief of Representatives Ann Wagner, Andy Barr, J. French Hill, Blaine Luetkemeyer, and Senator Tom Cotton as Amici Curiae in Support of Respondents, March 10, 2020).

Second Circuit opinion. On June 26, 2020, the Second Circuit issued its opinion in the federal court challenge to Regulation BI and provided the SEC the green light the agency needed to fully implement Regulation BI. The majority found that the investment adviser petitioner had Article III standing to sue the SEC but the state petitioners did not. Because the investment adviser petitioner had standing, the majority then addressed the merits of the case and upheld Regulation BI over the petitioners' Administrative Procedure Act challenge. One judge partially dissented because he would have found that the investment adviser petitioners also lacked constitutional standing. As a result, the Second Circuit denied the petitions for review and, thus, cleared the way for Regulation BI to be fully implemented (*XY Planning Network, LLC v. SEC*, June 26, 2020, Park, M.).

© 2020 CCH Incorporated and its affiliates. All rights reserved.

—*Article III standing*. The majority found that XYPN member Ford Financial Solutions, LLC had Article III standing to challenge Regulation BI based on the doctrine of competitor standing, which posits that standing can exist when an agency permits more competition against a firm. The majority explained that Ford Financial Solutions' principal had attested that the firm would be less able to distinguish its investment adviser business, which is subject to a fiduciary standard of conduct, from other firms that, under Regulation BI, will be able to state that they too serve their customer's best interests. As a result, Ford Financial Solutions would have to lower its prices or devote more resources to maintaining its sales levels. Thus, the majority said Ford Financial Solutions had demonstrated via "economic logic" and "actual market experience" why Regulation BI would hurt their business. In a footnote, the majority distinguished similar cases where the facts were more speculative.

With respect to the state petitioners, however, the majority found Article III standing was lacking because there was no direct link between Regulation BI and their tax revenues. The majority explained that the states' theory of Article III standing ultimately was too speculative because tax revenues depend on multiple variables and the state petitioners did not adequately address the potential loss of revenues that could occur from imposition of a fiduciary standard of conduct on broker-dealers, which the majority said could result in less investor choice or a different fee structure for investors' accounts.

—*Majority credits SEC interpretation of Section 913*. With respect to the merits, the key issue was how to interpret Dodd-Frank Act Section 913. The SEC asserted broad authority to fashion broker-dealer standards of conduct under the permissive ("may") language of Section 913(f). The investment adviser petitioners argued that the SEC, if it acted on broker-dealer standards of conduct, had to impose a fiduciary standard because otherwise Section 913(g), which authorizes the SEC to impose such standard, would be superfluous.

According to the majority, Sections 913(f) and 913(g) are separate sources of rulemaking authority as demonstrated by both sections' use of the word "may." The majority said this view is bolstered by the "necessary and appropriate" language contained in Section 913(f), which states in part: "... as *necessary or appropriate* in the public interest and for the protection of retail customers (and such other customers as the Commission may by rule provide), to *address* the legal or regulatory standards of care for brokers, dealers, investment advisers..." (full quotation from statute provided instead of partial quotation in court opinion but with emphasis as shown in court opinion). As a result, the SEC could opt to refrain from adopting any rule under Section 913, or it could adopt rules under either Section 913(f) or Section 913(g).

The majority further explained that the inclusion of Section 913(g) was intended to counter the argument that the Investment Adviser Act's broker-dealer exclusion deprived the SEC of authority to impose a fiduciary standard of conduct on broker-dealers. Previously, the SEC had attempted rulemaking in this area but the D.C. Circuit vacated the rule because of the broker-dealer exclusion (See, *Financial Planning Association v. SEC*, March 30, 2007, Rogers, J.). The majority, while doubting the need to resort to legislative history, observed in a footnote that the final version of Section 913 included both the House and Senate versions of SEC rulemaking authority but with revised language to make both grants of authority permissive rather than mandatory.

Lastly, the majority rejected the investment adviser petitioners' argument that Section 913, read in its entirety, is a procedure statute that details a number of steps to be taken in order for the SEC to impose a fiduciary standard of conduct on broker-dealers. The majority explained that such reading would mean that the substantive portions of Section 913(f) that come after the broad grant of rulemaking authority are superfluous.

—*Regulation BI not arbitrary and capricious*. The majority rejected the investment adviser petitioners' claim that Regulation BI is arbitrary and capricious. Said the court: "At bottom, Petitioners' preference for a uniform fiduciary standard instead of a best-interest obligation is a policy quarrel dressed up as an APA claim."

First, with respect to the SEC's interpretation of the broker-dealer exclusion, the majority noted that Regulation BI rarely mentioned the interpretation and, thus, the investment adviser petitioners' assertion that Regulation BI ultimately relied on that interpretation was inaccurate, not to mention the interpretation was something which they did not, and could not have, challenged.

© 2020 CCH Incorporated and its affiliates. All rights reserved.

Second, the majority rejected the investment adviser petitioners' argument that Regulation BI elided the issue of consumer confusion. The majority said the SEC weighed reduced consumer confusion from a fiduciary standard of conduct against the possibility broker-dealers subject to such standard might leave the industry or would otherwise incur increased compliance costs they would pass along to investors. The majority also concluded that the SEC's view was supported by substantial evidence.

—*Partial dissenting opinion.* Judge Sullivan wrote a separate opinion in which he agreed that the state petitioners lacked Article III standing and in which he agreed with the majority's conclusion about the merits of the case. The judge, however, dissented, in part, because he believed the investment adviser petitioners also lacked Article III standing. As a result, Judge Sullivan would have dismissed both sets of petitions without reaching the merits of the case.

Judge Sullivan first posited that the investment adviser petitioner could not show that its competitive injury was caused by or traceable to Regulation BI. The judge explained that the alleged competitive harm pre-dated Regulation BI and actually conferred an even greater advantage to broker-dealers than Regulation BI.

Judge Sullivan also objected to the majority's reliance on the investment adviser petitioners' marketing-based theory of Article III standing. The investment adviser petitioners argued that, under Regulation BI, they will be less able to distinguish their services, which are subject to a fiduciary standard, from services offered by broker-dealers, who would have to adhere to an enhanced standard of conduct but which is still lower than a fiduciary standard of conduct. According to Judge Sullivan, a marketing-based theory of Article III standing potentially lacks any limiting principle because virtually any petitioner could assert that their chosen marketing strategy will be impaired by a government regulation.

The road ahead: state fiduciary standards and preemption

What does the future of broker-dealer regulation at the state level hold now that Regulation BI has been upheld by a federal appeals court? It seems likely that at least some other states will follow the lead of Massachusetts and enact laws that enable their securities regulators to adopt fiduciary standards. Some states may adopt stronger standards than others, while some may shape their fiduciary standard to at least partially conform to Regulation BI. That, however, does not mean state fiduciary standards will not face legal challenges based on the theory that Regulation BI preempts such state standards. Still, the success or failure of a legal challenge asserting that Regulation BI preempts state fiduciary standards for broker-dealers will depend on many factors, such as whether a state standard in fact conflicts with Regulation BI within the U.S. Supreme Court's evolving preemption doctrine.

Massachusetts issues final regulation. Massachusetts adopted a fiduciary standard for broker-dealers on February 21, 2020, that became effective on March 6, 2020, but which will not be enforced until September 1, 2020. The fiduciary standard is housed primarily in 950 CMR 207 of the Code of Massachusetts Regulations (Amended regulatory text; Adopting Release, Amendments to Standard of Conduct Applicable to Broker-Dealers and Agents – 950 MASS. CODE REGS. 12.200, February 21, 2020; Massachusetts Fiduciary Conduct Standard for Broker-Dealers and Agents Frequently Asked Questions & Answers;).

Under the amended Massachusetts regulations, the failure to observe the fiduciary standard would constitute a dishonest or unethical practice under 950 CMR 12.204. The fiduciary duty regulation, 950 CMR 207(1), further defines the scope of what constitutes unethical or dishonest conduct or practices by providing a non-exclusive list of such broker-dealer behaviors in the fiduciary context, including: (1) failure to adhere to the fiduciary duty when making recommendations, opening of or transferring of assets to an account, or buying or selling securities; and (2) failure to adhere to the fiduciary duty when the broker-dealer: (a) exercises discretion over a customer's account (an exception covers actions that solely relate to the time and/or price for order execution); (b) when a fiduciary duty exists by contract; and (c) when the broker-dealer is contractually required to provide account monitoring.

The Massachusetts regulation also provides for how a broker-dealer meets their duty to

© 2020 CCH Incorporated and its affiliates. All rights reserved.

act with the utmost care and loyalty to their customer. The duty of care may be satisfied by "us[ing] the care, skill, prudence, and diligence that a person acting in a like capacity and familiar with such matters would use, taking into consideration all of the relevant facts and circumstances." A broker-dealer also must make a reasonable inquiry into the following: (1) the risks, costs, and conflicts regarding all recommendations made and investment advice given; (2) the customer's investment objectives, risk tolerance, financial situation, and needs; and (3) any other relevant information.

A broker-dealer satisfies their duty of loyalty by: (1) disclosing all material conflicts of interest; (2) avoiding, eliminating, and mitigating conflicts of interest; and (3) making recommendations and providing investment advice without regard to the financial or any other interest other than the interest of the customer. The regulation further provides that disclosure alone will not satisfy the duty of loyalty. Moreover, a broker-dealer is presumed to have breached the duty of loyalty if she makes a recommendation in connection with a sales contest.

With respect to conflicts of interest, the adopting release made two significant points:

- "The Division revised this portion of the Regulations from that which was in the Proposal to clarify that not all conflicts must be avoided. Likewise, not all conflicts must be eliminated. Accordingly, conflicts that arguably could be avoided or eliminated do not need to be if it would not be reasonable for a broker-dealer or agent to do so."
- "In certain situations, conflicts of interest must be avoided or eliminated. In other situations, conflicts may exist, but must be mitigated and disclosed. In no case will disclosing a conflict of interest, without more, satisfy a broker-dealer's or agent's duty of loyalty."

The final version of the Massachusetts regulation includes some adjustments made after regulators reviewed public comments submitted on the proposed version. For example, references to persons who already are subject to a fiduciary duty were removed. The adopting release also clarified that although the duty exists when incidental advice is given, the duty is not ongoing unless the broker-dealer exercises discretion over a customer's account or has a contractual fiduciary or account monitoring duty. Lastly, 950 CMR 12.204 provides that the suitability standard applies when the fiduciary duty is inapplicable.

Other state proposals. In addition to Massachusetts, at least five other states have or will propose versions of a fiduciary standard for broker-dealers and/or investment advisers. Some of these states follow the Massachusetts example, while some, like Oklahoma, focus on investment advisers instead of broker-dealers. As with Massachusetts, many of these proposals, if adopted, could eventually face litigation over whether Regulation BI preempts them. The following is a survey of the landscape of broker-dealer/investment adviser fiduciary proposals in the small number of states that have attempted such reforms during the last several years:

—*Nevada.* In 2017, Nevada enacted a law (SB 383) that imposed a statutory fiduciary duty on broker-dealers and investment advisers. Nevada regulators have since proposed regulations that further define the statutory fiduciary duty. Broker-dealers, for example, could invoke an episodic fiduciary duty exemption that would limit the fiduciary duty to the provision of specific invest9ment advice without generally creating an ongoing duty unless required by law.

—*New Jersey.* In 2019, New Jersey proposed a fiduciary standard similar in structure to the one later adopted by Massachusetts. The North American Securities Administrators Association expressed support for the proposal. A group of securities industry associations jointly commented that the proposal should either be paused or revised to, among other things, clarify differences between the proposed rule and the rule summary, which are potentially unclear about whether the fiduciary duty for broker-dealers (as opposed to dually-registered broker-dealers/investment advisers) is episodic or ongoing. The U.S. Chamber of Commerce's Center for Capital Markets Competitiveness and the New Jersey Chamber of Commerce likewise urged a significant re-write, cited the likelihood of a preemption challenge, and touted the adequacy of Regulation BI.

—*Maryland.* Legislation introduced in Maryland in early 2019 (SB 786; HB 1127) would have imposed a fiduciary duty on broker-dealers

© 2020 CCH Incorporated and its affiliates. All rights reserved.

and investment advisers to act in a customer's best interest and without regard to the financial or other interest of the person or firm providing the advice. The Maryland Securities Commissioner would have had authority to adopt implementing regulations. The Senate version of the legislation, however, received an unfavorable report from the state Senate Finance Committee shortly after introduction.

—*Oklahoma.* In early 2020, the Oklahoma Department of Securities proposed a fiduciary standard of care for investment advisers. The proposed rule largely tracks the Massachusetts regulation for broker dealers and uses similar "without regard" language. The proposal has been submitted to the Oklahoma Secretary of State's Office of Administrative Rules.

—*Iowa.* The Iowa Insurance Division in May 2020 adopted a best interest standard of care for annuity agents that draws from a model regulation developed by the National Association of Insurance Commissioners and which seeks to harmonize state rules with the SEC's Regulation BI. The Iowa rule was published in the Iowa Administrative Bulletin on June 3, 2020 and becomes effective on July 8, 2020. Iowa Insurance Commissioner Doug Ommen, who also oversees state securities regulations, said in a press release that due to the COVID-19 pandemic a similar best interest rule for securities firms would likely not be proposed until later during the summer of 2020.

Does Regulation BI preempt state fiduciary standards? The U.S. Constitution's Supremacy Clause provides the starting point for analyzing whether a federal law preempts a state law: "This Constitution, and the Laws of the United States which shall be made in Pursuance thereof ... shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any state to the Contrary notwithstanding" (U.S. Const., Art. VI, Cl. 2). From here, preemption may occur for three basic reasons: (1) federal law expressly preempts a state law; (2) the federal government has occupied some field that states may not enter by enacting their own laws; or (3) state law conflicts with federal law. The Supreme Court also has said that the "categories of preemption are not 'rigidly distinct.'" Congressional purpose remains the critical factor in evaluating federal and state laws under all modes of preemption (*See*, *Crosby v. National Foreign Trade Council*, 520 U.S. 363 (2000)).

—*Express and implied preemption.* Express preemption would require some explicit showing in a statute of Congressional intent to displace state laws. Examples of statutory language that can indicate possible express preemption are phrases such as "related to," "covering," and "in addition to, or different than" (See, Congressional Research Service, Federal Preemption: A Legal Primer, July 23, 2019).

Field preemption, one type of implied preemption, would require the government to define the field it claims to have occupied. In general, courts begin preemption analysis with a presumption against preemption. The Supreme Court has noted that, in cases asserting field preemption in areas that sates have traditionally been present, it is assumed that state police powers would not be preempted absent a "clear and manifest" Congressional purpose (*Wyeth v. Levine*, 555 U.S. 555 (2009); But see, Congressional Research Service, Federal Preemption: A Legal Primer, July 23, 2019 at 3-6 (discussing the impact of textualism in recent Supreme Court preemption opinions)).

In a somewhat more recent case, Justice Kagan noted in a concurring opinion that a key Supreme Court precedent on field preemption might not apply the same way if that case had been decided in modern times and, thus, suggested that the court today might be less accommodating to extremely broad theories of field preemption. Said Justice Kagan: "The *Napier* Court concluded that Congress had 'manifest[ed] the intention to occupy the entire field of regulating locomotive equipment,' based on nothing more than a statute granting regulatory authority over that subject matter to a federal agency. Under our more recent cases, Congress must do much more to oust all of state law from a field. *See, e. g., New York State Dept. of Social Servs. v. Dublino*, 413 U. S. 405, 415 (1973) (rejecting preemption even though Congress had enacted a 'detailed' and 'comprehensive' regulatory scheme). Viewed through the lens of modern preemption law, *Napier* is an anachronism." To what extent is Justice Kagan's observation limited to the specific context of railroad cases and to what extent does it cast a longer shadow more generally over field preemption? (*See*, *Kurns v. Railroad Friction Products Corp.*, 565 U.S. 625 (2012) (Kagan, J., concurring)).

© 2020 CCH Incorporated and its affiliates. All rights reserved.

An even more recent case exposed divisions among six of the justices on the current Supreme Court and may suggest the emerging influence of textualism on preemption doctrine. A fractured majority agreed, overall, that federal law did not preempt some state laws that ban uranium mining. Writing for only three justices, Justice Gorsuch, joined by Justices Thomas and Kavanaugh, opined that in evaluating claims of field preemption it is inappropriate to examine state legislative motives because doing so could inhibit state legislative debate, decrease transparency of the legislative process, and could result in burdensome litigation seeking to discover state legislators' motives. Justice Ginsburg, joined by Justices Sotomayor and Kagan, concurred in the judgment and countered that Justice Gorsuch's views on legislative motive were unnecessary to decide the case. Justice Ginsburg also disagreed with Justice Gorsuch's suggestion that obstacle preemption could be eliminated. It is doubtful that this exchange between the justices has settled anything regarding the court's overall preemption doctrine, but it does exemplify how the several preemption theories may evolve over time (*See, Virginia Uranium, Inc. v. Warren*, Slip. Op. (2019).

Implied preemption also may occur where a state law conflicts with a federal law either because it presents an obstacle to the federal law or because compliance with both the state and federal law is impossible. With respect to obstacle preemption, it has been said that federal law preempts a state law where the "challenged state law stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress" (See, *Crosby* (internal punctuation and quotations omitted)). With respect to the inability to comply with both federal and state law, the Supreme Court has observed that impossibility is not only a "demanding defense" but that "the possibility of impossibility [is] not enough" (citations omitted) (*See, Merck Sharp & Dohme Corp. v. Albrecht*, Slip. Op. (2019)).

—*Key NSMIA provisions.* NSMIA includes a number of provisions that amended the Exchange Act to limit and/or preserve state laws and regulations of broker-dealers and investment advisers. A few of these provisions appear to expressly preempt some types of state laws and regulations for broker-dealers, but do not necessarily touch upon all possible state laws and regulations pertaining to broker-dealers. Other NSMIA provisions appear to expressly preserve state authorities, especially regarding states' general antifraud enforcement authorities. Yet another NSMIA amendment to the Exchange Act contained in NSMIA's Title I on broker-dealers implies that state laws and regulations are permitted to the extent they are not specifically prohibited by the Exchange Act or otherwise in conflict with the Exchange Act or related regulations.

The following language from NSMIA likely would provide the starting point for any court analysis of whether Regulation BI preempts similar state fiduciary standards for broker-dealers and investment advisers (See, National Securities Markets Improvement Act of 1996, Pub. L. No. 104-290):

- NSMIA Section 102(a) [Securities Act Section 18(c)(1)]—Consistent with this section, the securities commission (or any agency or office performing like functions) of any State shall retain jurisdiction under the laws of such State to investigate and bring enforcement actions, in connection with securities or securities transactions (A) With respect to—(i) Fraud or deceit; or (ii) Unlawful conduct by a broker, dealer.

Note: *The original NSMIA language has been retained, although the text has been rearranged slightly and now includes references to funding portals and crowdfunding transactions per the Jumpstart Our Business Startups (JOBS) Act of 2012.*

- NSMIA Section 103(a) [Exchange Act Section 15(i)(1)]—No law, rule, regulation, or order, or other administrative action of any state or political subdivision thereof shall establish capital, custody, margin, financial responsibility, making and keeping records, bonding, or financial or operational reporting requirements for brokers, dealers, municipal securities dealers, government securities brokers, or government securities dealers that differ from, or are in addition to, the requirements in those areas established under this title.
- NSMIA Section 103(a) [Exchange Act Section 15(i)(3)]—No law, rule, regulation, or order, or other administrative action of any state or political subdivision thereof may prohibit an associated

© 2020 CCH Incorporated and its affiliates. All rights reserved.

person of a broker or dealer from effecting a [described de minimis] transaction

Note: *NSMIA placed the above Section 103(a) text in Exchange Act Section 15(h), but later amendments to the Exchange Act moved this text to its current location in Exchange Act Section 15(i). Moreover, Exchange Act Section 15(i)(2), added by Section 305(d)(1) of the Jumpstart Our Business Startups (JOBS) Act of 2012, purports to preempt state laws, rules, regulations, or administrative actions regarding a registered funding portal "with respect to its business as such," although this language would not apply to state "examination and enforcement" of a funding portal that "is not in addition to or different from the requirements for registered funding portals established by the Commission."*

- NSMIA Section 103(b) [Exchange Act Section 28(a)—Except as otherwise specifically provided in this title, nothing in this title shall affect the jurisdiction of the securities commission (or any agency or officer performing like functions) of any State over any security or any person insofar as it does not conflict with the provisions of this title or the rules and regulations under this title.
- NSMIA Sections 102 and 307—Section 102 amended Securities Act Section 18(c)(2) to allow states to require notice filings. Section 307 is an uncodified provision in NSMIA that similarly preserves states' authority to require notice filings and to collect certain fees regarding investment advisers.

—*A brief analysis.* As we approach the 86th anniversary of the Exchange Act, perhaps no securities law question has been more fraught with interpretive challenges than that of whether Regulation BI would preempt state laws and regulations purporting to impose a stronger fiduciary standard on broker-dealers. Within the constellation of the Supreme Court's preemption cases, it is somewhat rare for a case to address multiple statutory provisions, some of which expressly preempt state laws and others that expressly preserve certain state laws, and for both sets of provisions to potentially overlap.

The analysis naturally begins with an examination of the SEC's Congressional statutory mandate. NSMIA amended the Exchange Act to expressly prohibit state broker-dealer laws dealing with "capital, custody, margin, financial responsibility, making and keeping records, bonding, or financial or operational reporting requirements … that differ from, or are in addition to, the requirements in those areas established under this title" (i.e. Title I of the Exchange Act). How broadly should these terms, such as "financial responsibility," be read?

NSMIA provided that states "shall retain jurisdiction under the laws of such State to investigate and bring enforcement actions, in connection with securities or securities transactions (A) With respect to—(i) Fraud or deceit; or (ii) Unlawful conduct by a broker, dealer." How broadly should this provision be read? Does it contemplate a state fiduciary standard for broker-dealers?

Moreover, there is the question of how to interpret any state law alleged to be preempted by Regulation BI. Does the text of the state law or regulation in fact conflict with Regulation BI? For example, is it sufficient for a state law or regulation to couch its fiduciary standard in the language of enforcement authorities preserved to the states under NSMIA by labeling the failure of a broker-dealer to abide by a fiduciary standard of care as a dishonest or unethical act or practice? What impact might the emerging textualist viewpoint among a small group of Supreme Court justices have on such analysis and will the court continue to at least sometimes evaluate Congressional and state legislative motives?

At present, Massachusetts is the only state to have adopted a final regulation that potentially conflicts with Regulation BI. Other states have indicated an intention to follow Massachusetts in spirit, but it is unlikely that every state that eventually adopts a similar standard will use the same language as Massachusetts. In the end, the answer to the question of whether Regulation BI preempts state laws and regulations that impose a higher standard of care on broker-dealers than has the SEC is likely more complex, than any potential litigants are willing to admit.

—*Absence of SEC pronouncement on preemption.* The SEC opted to not make a statement in the final version of Regulation BI regarding the potential preemptive effect of the regulation

© 2020 CCH Incorporated and its affiliates. All rights reserved.

on state laws. The SEC, however, did state the following in the supplemental materials accompanying Regulation BI: “We note that the preemptive effect of Regulation Best Interest on any state law governing the relationship between regulated entities and their customers would be determined in future judicial proceedings based on the specific language and effect of that state law.” The only other significant reference to preemption in the adopting release occurred in the economic analysis section (footnote 1163), in which the SEC stated that it had “concluded that we cannot analyze the economic effects of the possible preemption of state law at this point because the factors that will shape those judicial determinations are too speculative.” By contrast, the SEC’s Regulation BI proposing release did not mention preemption.

According to Supreme Court precedent, if a federal preemption challenge was made to a state fiduciary standard based on Regulation BI, it might not matter that the SEC’s adopting release did not make a broader statement on the potential preemptive effect of Regulation BI. In the *Wyeth* case mentioned above, the Supreme Court rejected a pharmaceutical company’s obstacle preemption theory that was, in part, premised on an FDA statement in a regulatory preamble expressing the view that the regulation was intended to preempt similar state laws that could upset the FDA’s ability to evaluate drugs. “In such cases, the Court has performed its own conflict determination, relying on the substance of state and federal law and not on agency proclamations of pre-emption,” wrote Justice Stevens for the majority. The court did note that Congress can authorize an agency to adopt regulations that do have preemptive effect regarding contrary state laws. The court also observed that an agency possesses expertise and that the court might accord *Skidmore* deference to an agency pronouncement on whether state laws are an obstacle to a federal regulatory regime based on the “thoroughness, consistency, and persuasiveness” of the agency’s statement.

SIFMA and NASAA both commented to the SEC on the Regulation BI preemption issue in the months immediately before the SEC issued its adopting release. SIFMA urged the SEC to issue detailed preemption guidance. “The purpose of doing so would be to highlight that NSMIA preempts states from regulating federally registered RIAs and from imposing books and records requirements on BDs that differ from, or are in addition to, federal requirements,” wrote Kevin M. Carroll, SIFMA’s Managing Director & Associate General Counsel. A. Valerie Mirko, NASAA’s General Counsel, countered via footnote with a comparatively streamlined text for the SEC to include in the adopting release: “These rules are not intended to – and they do not – preempt any state law, rule, regulation or order not otherwise preempted by federal law.”

Conclusion

The Second Circuit gave the green light for the SEC to move forward with full implementation of Regulation BI. The broad policy objectives to be achieved via Regulation BI’s standards of conduct, in combination with the detailed disclosures required by Form CRS and the guidance provided in two interpretive releases, present a complex set of regulations and guidance for firms to comply with and for the investing public to comprehend. Even with Regulation BI now in place, a future Commission could still engage in notice and comment rulemaking to adopt a uniform fiduciary standard of conduct under its Dodd-Frank Act Section 913(g) authorities, something the second Circuit’s opinion upholding Regulation BI does not rule out.

The SEC’s OCIE also has announced its plans to conduct initial examinations of firms’ compliance with Regulation BI. The launch of Regulation BI during a global pandemic and related economic downturn may require firms and investors alike to navigate challenges in addition to Regulation BI’s complexity. Perhaps the success or failure of Regulation BI ultimately rests upon the degree to which the SEC is able to educate the investing public and the degree to which the agency polices compliance with the regulation. Clayton, in a July 23, 2020 interview with CNBC, warned of a recent inflow of retail investor funds into riskier short-term trading of stocks. Clayton also urged market participants to “heed[]” the SEC’s new guidance, alluding to Regulation BI and Form CRS. A few days after Clayton spoke, the SEC’s staff Standards of Conduct Implementation Committee, established at the time Regulation BI

© 2020 CCH Incorporated and its affiliates. All rights reserved.

was adopted, said in a public statement that it had conducted initial reviews of filed Forms CRS and that firms could do a better job regarding the completeness and clarity of their Forms CRS.

Moreover, firms may eventually need to prepare to comply with the DOL's latest fiduciary proposal, if and when, the final version is adopted. Lastly, Massachusetts has adopted final regulations implementing its own version of a fiduciary standard for broker-dealers. It remains to be seen if small concessions Massachusetts made in adopting its final regulation after receiving public comments will be enough to avoid litigation over whether federal securities laws preempt state standards of conduct that purport to be stronger than the standard contained in Regulation BI.

Wolters Kluwer Legal & Regulatory, U.S. delivers expert content and solutions in the areas of law, corporate compliance, health compliance, reimbursement, and legal education. Serving customers worldwide, our portfolio includes products under the Aspen Publishers, CCH Incorporated, Kluwer Law International, ftwilliam.com and MediRegs names.

This publication is designed to provide accurate and authoritative information in regard to its subject matter. The publication is provided with the understanding that Wolters Kluwer Legal & Regulatory, U.S., and the author(s) are not engaged in rending legal or other professional services. If legal advice or other professional assistance is required, the services of a professional should be engaged.

© 2020 CCH Incorporated and its affiliates. All rights reserved.