

## SEC and FINRA Provide Reg. BI and Form CRS Guidance as the Implementation Date Approaches

By **Ethan L. Silver**, **Lauren A. Schwartz**, and **Alexander D. Zozos**

### What You Need To Know:

- The implementation date for Reg. BI and Form CRS remains June 30, 2020.
- The SEC's initial compliance review will be focused on "good-faith efforts." Firms should make good faith efforts to implement policies and procedures reasonably designed to achieve compliance with Reg. BI.
- Examinations for compliance with Form CRS will focus on delivery and filing, content, formatting, and updates.

*In an ongoing informational series, Taking Action—Reg. BI, Lowenstein Sandler LLP will provide updates and guidance to broker-dealers, investment advisers, and dual registrants to assist and enhance preparedness for the June 30, 2020, implementation date for Regulation Best Interest (Reg. BI) and Form Client Relationship Summary (Form CRS). Lowenstein generated Reg. BI and Form CRS resources are available [here](#).*

#### I. Introduction

On April 2, 2020, Jay Clayton, Chairman of the U.S. Securities and Exchange Commission (SEC), announced that the implementation date for both Reg. BI and Form CRS remains on schedule for June 30, 2020. The Chairman highlighted that the SEC's initial compliance review would be focused on "good-faith" efforts. The Chairman also recognized the general strain on resources and disruption caused by the ongoing response to COVID-19, stating that a firm unable to comply—or experiencing difficulty complying—with the requirements should

"engage" with the SEC for relief.

The SEC and the Financial Industry Regulatory Authority (FINRA) also recently published guidance to assist and inform firms in their preparedness for the June 30, 2020, implementation date. The SEC published two Risk Alerts, one summarizing the areas of focus for a Reg. BI examination and another summarizing the areas of focus for a Form CRS examination. FINRA also published common practices it observed from broker-dealers during preparedness reviews it conducted regarding Reg. BI and Form CRS.

#### II. SEC Reg. BI Risk Alert

The *Reg. BI Risk Alert* reiterates that firms should make good faith efforts to have policies and procedures reasonably designed to achieve compliance with Reg. BI and have made reasonable progress toward implementing those policies and procedures. The *Reg. BI Risk Alert* highlights document requests for each of Reg. BI's enumerated obligations.

A sample list of information that the SEC staff may request while conducting a Reg. BI exam is available [here](#).

## 1. Disclosure Obligation

The Disclosure Obligation requires broker-dealers to disclose all material facts relating to the scope of their customer relationship as well as the conflicts of interest associated with a recommendation. For broker-dealers to comply, disclosure should include the capacity in which the broker-dealer is operating; material fees and costs that apply to the retail customer's transactions, holdings, and accounts; and any material limitations in offerings or services.

To assess compliance with this obligation during exams, SEC staff may request and review the content of the disclosures, and other firm records provided below, in order to ascertain whether the disclosures provide the required information to retail customers:

- Fee schedules and disclosures related to fees charged both directly and indirectly
- Compensation methods for associated persons, including sources and types of compensation, and disclosure-related conflicts of interest associated with recommendations
- Disclosure related to account monitoring or material limitations on products and services offered
- Lists of proprietary products offered by the broker-dealer

## 2. Care Obligation

The Care Obligation requires broker-dealers to exercise reasonable diligence, care, and skill when making a recommendation that is in the best interest of a retail customer, taking into account their investment profile and the attendant risks, rewards, and costs.

To assess compliance during exams, SEC staff may request and review:

- Information collected to create an investment profile, such as new account forms, correspondence, and agreements between the customer and the broker-dealer
- The process for having a reasonable basis for believing a recommendation is in the best interest of the customer, such as the factors used and the means to avoid placing

a broker-dealer's financial or other interests ahead of the customer's interest

- The process for how a broker-dealer makes recommendations for significant investment decisions, such as rollovers and account types, as well as recommendations for risky or complex products, and the basis for why it is reasonable and in their customers' best interest

## 3. Conflict of Interest Obligation

The Conflict of Interest Obligation requires broker-dealers to establish, maintain, and enforce written policies and procedures to reasonably address conflicts of interest associated with recommendations to retail customers.

To assess compliance during exams, SEC staff may request and review a broker-dealer's policies and procedures to determine:

- Whether and how policies and procedures address conflicts related to incentives and material limitations on products and services provided
- Whether broker-dealers have eliminated sales contests, sales quotas, bonuses, and noncash compensation based on the sale of specific securities or specific types of securities within a limited period of time
- Whether a broker-dealer adequately documented and established a structure to identify, mitigate, eliminate, and disclose conflicts of interest, as necessary

## 4. Compliance Obligation

The Compliance Obligation requires broker-dealers to establish, maintain, and enforce written policies and procedures reasonably designed to achieve compliance with Reg. BI as a whole.

To assess compliance during exams, SEC staff may request and review a broker-dealer's policies and procedures and evaluate any controls, remediation of noncompliance, training, and periodic review and testing included therein.

## III. SEC Form CRS Risk Alert

The *Form CRS Risk Alert* stated that examinations for compliance with the Form CRS will focus on four areas: Delivery and Filing,

Content, Formatting, and Updates.

## 1. Delivery and Filing

All firms subject to Form CRS<sup>1</sup> must file their Form CRS with the SEC through either Web CRD or IARD, or both, and must post their Form CRS on their public website by June 30, 2020.<sup>2</sup> Following a firm's filing Form CRS, it must deliver its Form CRS to all existing customers within 30 calendar days. During this time, and thereafter, a firm must deliver its Form CRS at the time—or before—it opens an account or provides a recommendation to both existing and new customers, and must post the Form CRS to its public website. During exams, SEC staff will review the firm's delivery and filing policies and procedures, and confirm filing and delivery dates by reviewing records tracking and ensuring compliance.

## 2. Content

The Form CRS must fully and fairly describe a firm's operations. During exams, SEC staff will review the Form CRS to ensure that all required information is provided and that it is true and accurate, and no material fact is omitted. SEC staff will particularly review descriptions of account monitoring, compensation structure, and conflicts of interest related to proprietary or third-party products. Further, disclosures related to fees (including fee schedules listed in the brokerage agreements and Form CRS) and legal or disciplinary history will also be looked at carefully.

## 3. Formatting

Form CRS must be written in plain English and adhere to prescribed formatting instructions. During exams, SEC staff will review Form CRS to confirm that the prescribed wording, text features, and layout are followed.

## 4. Updates

Form CRS must remain accurate, and should be updated, if necessary, in a timely manner. During exams, SEC staff will confirm and review policies and procedures relating to updating, highlighting, or summarizing material changes, and distributing amended versions of Form CRS. Materially inaccurate information must be

updated and filed within 30 days and distributed to retail customers within 60 days of the update.

## IV. FINRA Broker-Dealer Practices and Preparedness Review

FINRA conducted a survey of member broker-dealers, starting in late 2019, to assess both their preparedness and approach for complying with Reg. BI and Form CRS.

FINRA highlighted that broker-dealers often created cross-operational working groups, prepared timelines to meet the implementation date, and started delivering training or were in the process of developing such training to educate their associated persons. Broker-dealers also updated their Written Supervisory Procedures (WSPs) to meet the new requirements of Reg. BI and Form CRS. To do this, broker-dealers leveraged earlier updates of WSPs to meet the previously enacted Department of Labor Fiduciary Rule, and conducted gap analyses to determine where new WSPs would be necessary. Broker-dealers also sought the assistance of outside counsel for drafting or revising existing WSPs and sought to implement technology to assist in operational supervision.

Broker-dealers created logs of existing conflicts and potential conflicts of interest as well as committees to review, assess, and address these compliance issues with Reg. BI and Form CRS. Broker-dealers also reviewed and altered compensation structures and disclosures provided to address conflicts of interest, such as capping or eliminating certain sales contests or creating schedules of all fees associated with certain transactions. In addition, broker-dealers updated existing surveillance or created new surveillance tools to review for excessive trading or unusual commissions and address conflicts of interest requirements, and reviewed and updated existing or created new account documentation and customer disclosure forms. Contexts in which the term "adviser" is used were reviewed or altered to comply with the Reg. BI restriction of the term for a firm solely registered as a broker-dealer.

Broker-dealers also took steps to draft Form CRS to include the required information while conforming to the required length. Additionally,

<sup>1</sup> Applicable firms include all broker-dealers and investment advisers that have retail customers.

<sup>2</sup> As of April 6, 2020, firms are able to voluntarily file their Form CRS. See the Form CRS FAQs by visiting <https://www.sec.gov/investment/form-crs-faq>.

broker-dealers reviewed and developed procedures for timely delivery of Form CRS, working closely with vendors and clearing agents.

## V. Conclusion

For additional information regarding Reg. BI and Form CRS, you can reference the following resources.

- [FINRA Reg. BI Website](#)
- [FINRA Broker-dealer Practices and Preparedness Review](#)
- [SEC Reg. BI and Form CRS Statement](#)
- [SEC Reg. BI: A Small Entity Compliance Guide](#)
- [SEC Reg. BI: FAQs](#)
- [SEC Reg. BI: Risk Alert](#)
- [SEC Form CRS: A Small Entity Compliance Guide](#)
- [SEC Form CRS: Instructions](#)
- [SEC Form CRS: FAQs](#)
- [SEC Form CRS: Risk Alert](#)

Please contact one of the listed authors of this Client Alert or your regular Lowenstein Sandler contact if you have any questions with respect to Reg. BI and Form CRS or would like assistance preparing for the implementation date, including reviewing and updating your compliance policies and procedures, training, and/or disclosures as well as drafting a Form CRS.

## Contacts

Please contact the listed attorneys for further information on the matters discussed herein.

### **ETHAN L. SILVER**

Partner

**T: 212.419.5862**

[esilver@lowenstein.com](mailto:esilver@lowenstein.com)

### **LAUREN A. SCHWARTZ**

Associate

**T: 646.414.6933**

[lschwartz@lowenstein.com](mailto:lschwartz@lowenstein.com)

### **ALEXANDER D. ZOZOS**

Associate

**T: 646.414.6868**

[azozos@lowenstein.com](mailto:azozos@lowenstein.com)

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NEW YORK

PALO ALTO

NEW JERSEY

UTAH

WASHINGTON, D.C.

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