

HARBOR FINANCIAL SERVICES, LLC

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SEC Regulation BI and **SEC Fiduciary** **Guidance**

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SEC Reg BI

<https://www.sec.gov/rules/final/2019/34-86031.pdf>

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Conformed to Federal Register version

SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 240

Release No. 34-86031; File No. S7-07-18

RIN 3235-AM35

Regulation Best Interest: The Broker-Dealer Standard of Conduct

AGENCY: Securities and Exchange Commission.

ACTION: Final rule.

SUMMARY: The Securities and Exchange Commission (the “Commission”) is adopting a new rule under the Securities Exchange Act of 1934 (“Exchange Act”), establishing a standard of conduct for broker-dealers and natural persons who are associated persons of a broker-dealer (unless otherwise indicated, together referred to as “broker-dealer”) when they make a recommendation to a retail customer of any securities transaction or investment strategy

SEC Reg BI

- Upgrades BD duty from arms-length, suitability standard to quasi-fiduciary “best interest standard
- Reg BI applies only to retail customers
- Implementation deadline June 30, 2020
- Composed of 4 obligations

SEC Reg BI- 4 Obligations- BD

1. Obligation to act in clients' best interest at:
 - Time of recommendation of account opening or changes (platform selection, rollovers)
 - Time of strategy recommendations (asset allocation, hold recommendations)
 - Time of investment transaction

2. Disclosure Obligation (Prior to or at time of recommendation)
 - Acting as BD
 - **Material fees and costs that apply to transaction, holdings and account**
 - Type and scope of services provided
 - Conflicts of interest

SEC Reg BI- 4 Obligations- BD

3. Care Obligation (Exercise reasonable diligence, care and skill)

- Must evidence review of alternative recommendations
- Rollovers review similar to DOL
- Documenting written and oral disclosures

4. Conflict of Interest Obligation (Identify, disclose, eliminate)

- Limitations (i.e. representative only trades in ETFs, but firm offers a full suite of products, requires rep to disclose to customers)
- Rule instructs firms to develop a penalty system for any rep that does not adequately manage or disclose their conflicts of interest.
- Eliminate sales contests, sales quotas, and non-cash compensation based on sales of specific securities

SEC Reg BI- Implementation

- **Develop new or changes to policies, procedures and controls**
 - Account Type recommendations/ Retirement plan rollovers
 - Client onboarding process
 - Analyze products/services, fees and costs
 - Marketing material
 - Best interest vs suitability

SEC Reg BI- Implementation

- **Technology and record keeping**
 - Account monitoring
 - Disclosure delivery
 - All information collected and provided to retail customer pursuant to Reg BI
- **Identify and mitigate conflicts of interest**
- **Training**

SEC Reg BI- Investment Advisers

- Provide Advice in the best interest of the client
- Duty of loyalty
- Best Execution for client transactions
- Disclosure of conflicts of interest

SEC Reg BI- Will Not

- Extend beyond a particular recommendation or require BD to continuously monitor
- Require BD to refuse to accept a customer's order that is contrary to the broker's recommendation
- Apply to self-directed or unsolicited transactions by a retail customer, whether or not the customer receives separate recommendations from broker

SEC Reg BI- Form CRS

1. Mandatory Form CRS Delivery
 - Before or at time firm enters into client agreement
 - Opens a new account for existing client
 - Recommends a rollover
 - Recommends or provides a new advisory service
2. Mandatory “prominent” post Form CRS on Firm’s website
3. Communicate any changes to Form CRS to existing clients within 60 days
4. Deliver Form CRS to existing clients within 30 days

Delivery mechanism?

SEC Reg BI- Investor.gov

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The screenshot shows the Investor.gov website. At the top left is the U.S. Securities and Exchange Commission logo. The main header features the "Investor.gov" logo in red and black, with "U.S. SECURITIES AND EXCHANGE COMMISSION" below it. To the right of the logo are links for "About Us", "Contact Us", "Follow Us", and "Información En Español", along with a search bar containing the text "Search Investor.gov".

Below the header is a dark blue navigation bar with four white text links: "Introduction to Investing", "Research Before You Invest", "Protect Your Investments", and "Additional Resources".

The main content area features a large image of a man and a woman looking at a laptop. Overlaid on the image is the text "Check Out Your INVESTMENT PROFESSIONAL" in white. Below this is a search bar with a dropdown menu set to "Individual" and the placeholder text "Name or CRD#". Underneath the search bar is the text: "It's a great first step toward protecting your money. Learn about an investment professional's background, registration status, and more."

Below the main content area is a grid of red navigation buttons with white text: "ABOUT INVESTMENT PROFESSIONALS", "INVESTMENT PRODUCTS", "UNDERSTANDING FEES", "INVEST FOR YOUR GOALS", "FINANCIAL TOOLS AND CALCULATORS", and "ICOS AND OTHER DIGITAL ASSETS".

At the bottom are three promotional boxes: "FEATURED INFORMATION" with a white star icon and the text "Chairman's Videos: Choosing and Working with a Financial Professional"; "INVESTOR ALERTS AND BULLETINS" with a white pushpin icon and the text "Investor Bulletin: Seven Ways to Use"; and "GET HELP" with a white folder icon and the text "Submit Questions and Complaints" and "Ask a question or report a problem concerning your investments, your".

SEC Reg BI- Investor Form CRS Resources

<https://www.investor.gov/CRS>

[Know the Difference](#)

SEC “Protect Your Investments”

- Research Your Investment
- Search the Database
- Research Your Investment Professional
- Monitor Your Accounts
- Know the Fees You’re Paying
- Beware of Investment Scams

RESEARCH YOUR INVESTMENT

Do your “due diligence” by researching before you invest. Companies, bond issuers, mutual funds, and ETFs must regularly provide information to the public. Carefully review these disclosures, which are available for free on [EDGAR](#) and can help you decide if an investment is right for you.

- ▶ [Researching Investments](#)
- ▶ [Five Questions to Ask Before You Invest](#)
- ▶ [10 Ways to Use Investor.gov](#)
- ▶ [Investment Products](#)
- ▶ [Using EDGAR - Researching Public Companies](#)

MONITOR YOUR ACCOUNTS

Monitor your investment accounts for any suspicious activity. You should confirm that you authorized all of the transactions that appear in your account statements and trade confirmations. Also, look out for any changes to your account information that you do not recognize (e.g., a change to your address, phone number, e-mail address).

SEARCH THE DATABASE

[Search the Database](#) - It’s a great first step toward protecting your money. Learn about an investment professional’s background, registration status, and more.

KNOW THE FEES YOU’RE PAYING

As with anything you buy, there are fees and costs that come with investments. These fees may seem small, but over time they can have a major impact on your investment portfolio.

- ▶ [Updated Investor Bulletin: How Fees and Expenses Affect Your Investment Portfolio](#)
- ▶ [Understanding Fees](#)
- ▶ [Investor Bulletin: Mutual Fund Fees and Expenses](#)
- ▶ [Investor Bulletin: Brokers’ Miscellaneous Fees](#)
- ▶ [FINRA’s Fund Analyzer](#) 

RESEARCH YOUR INVESTMENT PROFESSIONAL

Never invest your money with someone who is not licensed and registered. If you choose to work with an investment professional, start by learning about the investment professional’s background, registration status, and any disciplinary history.

- ▶ [Search the Database](#) to check out an investment professional
- ▶ [Investor Bulletin: Top Tips for Selecting a Financial Professional](#)

BEWARE OF INVESTMENT SCAMS

Learn the red flags of investment scams. A few minutes of your time may save you from handing over your money to fraudsters.

- ▶ [What You Can Do to Avoid Investment Fraud](#)
- ▶ [Types of Fraud](#)

FIDUCIARY RULE CHANGES....in motion

- **CFP Board-** Code of Standards 10/1/19
 - New Code of Standards imposes a fiduciary duty on CFPs who provide financial advice in commission-based accounts (inconsistent with Reg BI).
 - Act as a fiduciary
 - Provide various client disclosures
 - New Code of Ethics and Standards of Conduct delayed to June 30, 2020
 - Board does not have regulatory authority but reviewing how to “enforce”
- **DOL** scheduled to propose new fiduciary rule in December (revival of a rule) for advice on retirement accounts (in conjunction with Reg BI)
- **FINRA** will enforce Reg BI. Anticipate FINRA will review Suitability Rule 2111 and Standards of Commercial Honor Rule 2010

FIDUCIARY RULE CHANGES....in motion

- **SEC Regulation BI has multiple spinoffs.** Criticism Reg BI doesn't set higher fiduciary bar for broker conduct
 - **House bill (HR3351)** passed to cut funding for SEC's Reg BI. Unlikely to move thru Senate
 - **States Securities Laws.** To date, only Nevada and Connecticut have formally adopted such laws; Massachusetts and New Jersey, currently pending. Unsure they will survive *court challenges*.
 - **State Insurance Laws.**
 - NY187- Suitability and Best Interest effective with annuities August 1, 2019, life insurance on March 1, 2020
 - NAIC model rule proposal scheduled in October. Best-interest standard expected: care, disclosure, conflict of interest and documentation

State Fiduciary Regulations

- Adopted Regulations:
- **Connecticut**-Required conflict disclosure in connection with administration of government plans (*effective January 1, 2019*)
- **Nevada**-Fiduciary duty law for BDs and IAs effective July 1, 2017 (proposed regulations to be adopted in order to implement is awaiting final rule).
- **New York**-Suitability and best interest standards for sellers of annuities (*effective August 1, 2019*) and life insurance (*effective February 1, 2020*)

- Pending Regulations:
- **Massachusetts**-Fiduciary standard on BDs and IAs. Request for comment issued on June 14, 2019; comment period ended July 26, 2019. (Raymond James submitted a comment letter.)
 - Previously proposed regulations would require fee disclosures for *state-registered* RIAs.
- **New Jersey**-Comment period for fiduciary rule closed on July 18, 2019. (Raymond James submitted a comment letter.)
- **Nevada**--Regulations to implement fiduciary duty law *pending* (comment period ended March 2019)

FIDUCIARY RULE (2) SEC Interpretations

- Standard of Conduct for IAs
- Solely Incidental Prong for BD Exclusion

FIDUCIARY RULE SEC Interpretation – Standard of Conduct for IAs

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<https://www.sec.gov/rules/interp/2019/ia-5248.pdf>

Issued June 5, 2019

Effective July 12, 2019

Conformed to Federal Register version

SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 276

[Release No. IA-5248; File No. S7-07-18]

RIN: 3235-AM36

Commission Interpretation Regarding Standard of Conduct for Investment Advisers

AGENCY: Securities and Exchange Commission.

ACTION: Interpretation.

SUMMARY: The Securities and Exchange Commission (the “SEC” or the “Commission”) is publishing an interpretation of the standard of conduct for investment advisers under the Investment Advisers Act of 1940 (the “Advisers Act” or the “Act”).

DATES: Effective July 12, 2019.

FOR FURTHER INFORMATION CONTACT: Olawalé Oriola, Senior Counsel;

Matthew Cook, Senior Counsel; or Jennifer Songer, Branch Chief, at (202) 551-6787 or

Larules@sec.gov, Investment Adviser Regulation Office, Division of Investment Management,

FIDUCIARY RULE SEC Interpretation

IA Standards of Conduct Expectations:

Deficiency 1- Failure to adopt, implement, or document periodic review of client accounts

- Interpretation requires **more than annual review** of portfolio from advisers who agree to provide continuous discretionary advice and charge an ongoing fee
- SEC expects ongoing account monitoring and rebalancing, with documentation to prove it.

FIDUCIARY RULE SEC Interpretation

IA Standards of Conduct Expectations:

Deficiency 2- Failure to adopt, implement, or document a policy for the selection of account types

- Firms that are dually registered will need to consider whether a brokerage or an advisory account is most appropriate
- Interpretation indicates advisers recommending rollovers of 401(k) plans will need to document the reasons why the rollover is in the client's best interest. Remember DOL rule.

FIDUCIARY RULE SEC Interpretation

IA Standards of Conduct Expectations:

Deficiency 3- Failure to conduct due diligence on investments

- Commission cites the Larry Grossman case as a reminder of consequences of failing to investigate securities before recommending to client (disgorgement and an industry bar)
- Fiduciary duty not satisfied by simply advising client to invest in “lowest cost” investment product without further analysis

FIDUCIARY RULE SEC Interpretation

IA Standards of Conduct Expectations:

Deficiency 4- Failure to provide full and fair disclosure of conflicts of interest

- SEC views *all conflicts as material*
- Interpretation requires disclosure to be clear and detailed enough for the client to make an informed decision

Deficiency 5- Failure to seek best execution

- Share class

FIDUCIARY RULE SEC Interpretation

IA Standards of Conduct Expectations:

Deficiency 6- Failure to establish that the Adviser has a reasonable understanding of the client's objectives

- Interpretation recommends at a minimum inquire into client's financial situation, level of financial sophistication, investment experience, and financial goals.

FIDUCIARY RULE SEC Interpretation- IA Standards of Conduct

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	Account Type Choice	Retirement AC Rollovers	Account Monitoring
What are the impacts?	Documentation of basis for recommendation is key	Similar to DOL	Must provide advice and monitoring
What can I do now?	If you aren't documenting already, you should begin now	Review educational resources to ensure clients understand options	Apply a prudent process
What are resources?	Advisor Mobile and CRM are two tools to leverage	Transfer Rollover Due Diligence HF189	Goal Planning & Monitoring, Account Review HF169

FIDUCIARY RULE SEC Interpretation- IA ELEVATE

Standards of Conduct Client Objectives

HFS Form

IPQ HFS Client- Score client objective
and risk tolerance

RISK TOLERANCE QUESTIONNAIRE

Client Document

FIDUCIARY RULE SEC Interpretation- Solely Incidental Prong of the B/D Exclusion

<https://www.sec.gov/rules/interp/2019/ia-5249.pdf>

Conformed to Federal Register version

Issued June 5, 2019
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SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 276

[Release No. IA-5249]

**Commission Interpretation Regarding the Solely Incidental Prong of the Broker-Dealer
Exclusion from the Definition of Investment Adviser**

AGENCY: Securities and Exchange Commission.

ACTION: Interpretation.

SUMMARY: The Securities and Exchange Commission (the “SEC” or the “Commission”) is

SEC Interpretation BD Solely Incidental Advice

BD not subject to the Act if:

- **Solely incidental Advice**
 - **Level of investment discretion (unlimited discretion is NOT solely incidental)**
 - Discretion limited to time, scope MAY be deemed solely incidental
 - **Account monitoring frequency**
 - Continuous, previously agreed-upon account monitoring would NOT be considered solely incidental
 - Periodic account monitoring or voluntary monitoring would likely be considered solely incidental
- **Only commissions and not asset-based fees are received**

FIDUCIARY RULE SEC Interpretation- Solely Incidental Prong of the B/D Exclusion

Harbor Policy Update

HFS Supervisory Procedures
Section 7.3 Fiduciary Duty

“Registered Representatives are forbidden to provide continuous account monitoring for brokerage accounts. Any monitoring of brokerage accounts is solely incidental (voluntary or may be agreed upon on a periodic basis, i.e. quarterly, as it would occur at specific time frames and not be considered continuous”