



# Harbor Implementation “3” of Regulation Best Interest

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June 11, 2020

# Topics We Will Cover

1. Form CRS & Disclosure Delivery

2. Stepping Up to Duty of Care

3. Account Selection Assessment

4. Investment Recommendations

5. Servicing

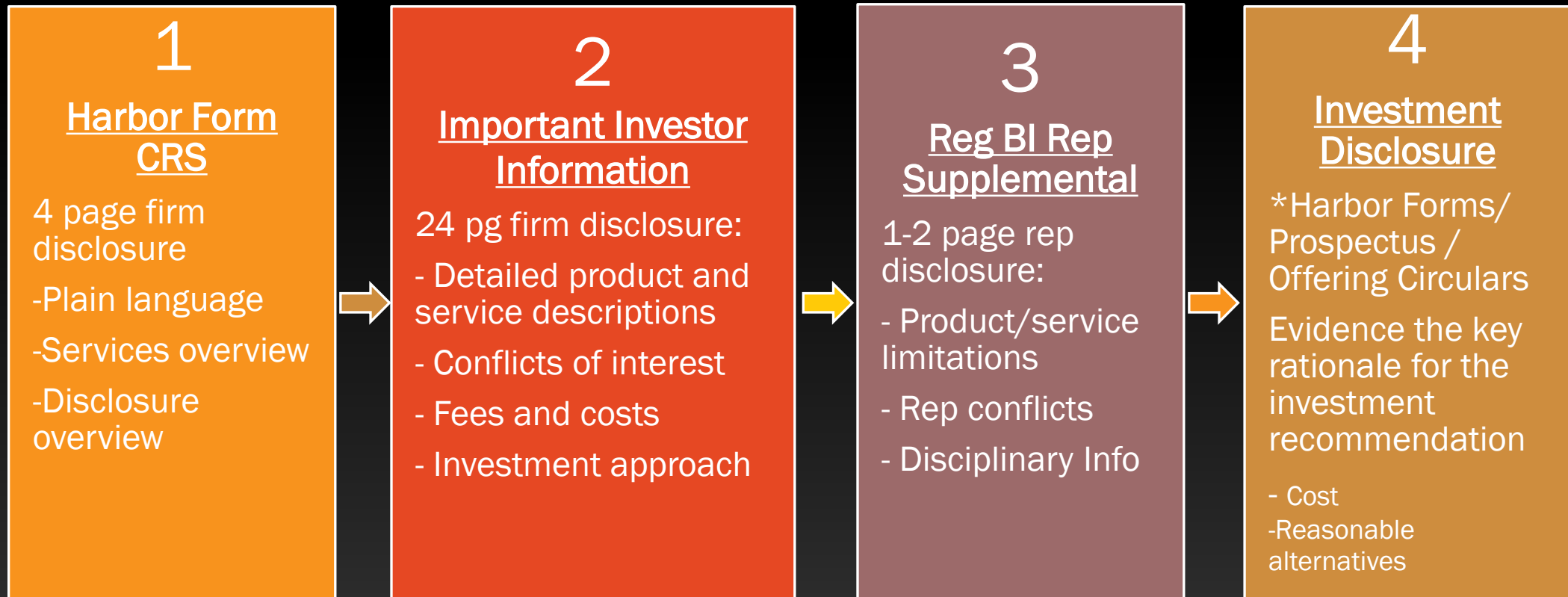
6. Q&A (Email [tbeaman@harborfs.com](mailto:tbeaman@harborfs.com))

# 1. Form CRS and Supplement Disclosures

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# Reg BI Layered Disclosures



\* Harbor Complex Product/Platform Forms: e.g. HF188 Annuity, HF166 Mutual Fund, HF126 529 Accounts, HF188 Rollover, HF162 Alternative Investment, HF172 Inverse, HF186 Structured

# Your Disclosure Delivery Obligations- Adviser or Registered Rep

	Form CRS (Form ADV Part 3)	Important Client Information	Rep Specific: Oral, ADV2B, Supplement	Product/ Platform Disclosure
<b><i>Prospective Clients</i></b>				
1. Before or at the time a recommendation is made (prior to new account opening or new direct investment; e.g. mutual fund, 529, annuity), or investment strategy (e.g. day trading, bond ladder)	X	X	<b>Disclose capacity, limitations, conflicts, disciplinary actions, etc</b>	e.g. ADVs, Harbor Product Forms*, Prospectus, Offering Circular
<b><i>Existing Clients</i></b>				
2. Before or at the time a recommendation is made (prior to opening a new account, or new direct investment)	X	X	See above	See above
3. Before or at the time a recommendation is made to convert a client account platform (e.g. commission-based to fee-based, fee-based to commission based, direct to commission-based, fee based platform change)	X	X	See above	See above
4. Before or at time a recommendation is made to add Margin or Option account	X	X	As needed	Options disclosure
5. Before or at time a trade recommendation is made for an existing account			As needed	As needed

# What is a Recommendation

## Factors considered in determining whether a recommendation has taken place:

- The communication “reasonably could be viewed as a ‘*call to action*”
- Account recommendations *include recommendations of account types, as well as recommendations to roll over or transfer assets* from one type of account to another.
- An investment strategy recommendation includes a *recommendation to use a bond ladder, day trading, margin strategy, irrespective of whether the recommendation mentions particular securities*
- The *more tailored the communication* to a specific customer or a targeted group of customers about a security(ies), *the greater likelihood that it will be viewed as a recommendation.*

# Required Timing

A recommendation is defined as a “**call to action**” or information that would influence a prospect to do which of the following actions?  
(Select all that apply)

When engaging with a prospect, the delivery of Form CRS and the Important Investor Information **disclosures are required before or at the time of a recommendation.**




- a) Open an account
- b) Engage in a securities transaction\*
- c) Consider a suggested investment strategy

\* For “direct business”, the earliest call to action would be a securities transaction recommendation.

# Best Time

Note: If you recommend several different accounts at the same time for a single prospect, one initial Form CRS delivery is required.

When engaging a prospect about becoming a client, when would be **the best time to deliver** Form CRS and Important Investor Information?

- a) When you are first introduced to a prospect (no recommendation has been made).
-  b) When you and a prospect mutually agree to begin a financial business relationship (no recommendation has been made).
- c) During the onboarding process (recommendation has been made).



## 2. Stepping Up to Duty of Care

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- Reg BI provides a new (“fiduciary-like) standard of conduct for BDs
- Secondary intent was to preserve the broker-dealer model.

New distinction between BD and Advisory: Point-in-time duty of care for a commission, vs ongoing duty of care for a fee.

# What is “Best Interest” and when does it apply under Reg BI?

A recommendation is in the “best interest” when the recommending party acts in the best interest of the retail customer **at the time the recommendation is made**, without placing the financial or other interest of the firm or associated person making the recommendation ahead of the interest of the retail customer.

# Commission-Based vs Fee-Based Account Recommendation

Regardless of how you conduct business, you must act in your client's best interest

Commission-Based Brokerage Account		Fee-Based Advisory Account		
Execution Only	Non-Discretionary Custom Portfolio	Non-Discretionary	Discretionary	Outsourced Model Management
Best Interest Standard		Fiduciary Standard		
<ul style="list-style-type: none"> <li>Must act in client's best interest at the time of any investment recommendation</li> </ul>		<ul style="list-style-type: none"> <li>Must act in client's best interest</li> <li>Must deliver agreed-upon services regardless of trading activity</li> </ul>		
<ul style="list-style-type: none"> <li>Recommendation process must address compensation conflict at transaction level</li> </ul>		<ul style="list-style-type: none"> <li>Level fee structure eliminates compensation conflict at transaction level.</li> </ul>		
<ul style="list-style-type: none"> <li><b>Periodic or ongoing/continuous monitoring not permitted by Firm</b></li> <li><b>Hold recommendations not permitted by Firm</b></li> </ul>		<ul style="list-style-type: none"> <li>Ongoing duty to monitor and ensure advice continues to be in client's best interest for duration and scope of agreement.</li> </ul>		

Consider these tradeoffs when evaluating the types of services you provide to clients and what they can expect.

# Why does account monitoring matter?

The SEC's "Solely Incidental" interpretation deemed ongoing/continuous monitoring as an advisory function subject to the Advisor's Act.

Under Reg BI, a broker-dealer might permit representative's to **periodically monitor** a customer's account (i.e. quarterly).

1. When a Firm permits a representative to periodically monitor, then he must, of course, actually monitor. If the representative offers quarterly reviews, and the representative does not communicate with the customer on that basis, it is deemed to be a **recommendation to hold** (even though it is implicit) and will then be deemed as **continuous monitoring**. (But, if the broker-dealer does not agree to monitor, silence will not be considered to be a recommendation to hold.)
2. When a Firm limits a representative to voluntarily reviews of a customer's account on an unscheduled basis, the voluntary review is not considered to be "account monitoring", nor does it create an implied agreement to monitor.

# Account Monitoring

Periodic BD account monitoring agreements not permitted

**Voluntary account reviews**, not “regularly” scheduled or implied to be periodic monitoring replace **commitments** to periodic **account review** meetings.

# Account Monitoring

## HF173 Hold Recommendation (BD)- Form retired

Hold recommendations require ongoing/continuous monitoring to identify signal for a future buy/sell recommendation.

The image shows a Harbor Financial HF173 Hold Recommendation form. The form is tilted and has a large red 'X' drawn over the registration information. The form includes the following fields and text:

- HARBOR FINANCIAL** logo
- Address: 11 N. Water Street, Ste 21290, Mobile, AL 36602, (251) 650-0840, Fax (251) 281-2007
- Form # HF173
- Account #
- Branch #
- FA #
- Registered Representative
- Date
- Time
- Meeting Format:  Phone Conversation  In-Person Meeting
- Client(s) present
- Account/Policy number
- Account/Policy held at:  Raymond James Financial  Other/Direct

# 3. Account Selection Assessment

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# What is your Process for Account Selection?

- SEC defined key considerations
- SEC defined disclosures
- SEC defined clients

How do you stay on track?

*Note: Recommending the same account platform for all clients, when others are available, will likely result in heightened review of the account selection process under Duty of Care.*

# HF011 Update -Account Assessment Key Considerations

## New Account Recommendation – Care & Disclosure Checklist

- **Stay on track**
  - Client attributes & best interest considerations
  - Disclosures
  - Fee-based and Commission-based specific considerations

HF011  
revised  
6/30/20



**HARBOR FINANCIAL** 11 N. Water Street Ste 21290 Mobile, AL 36602 (251) 650-0840 Fax (251) 261-2007

HF011-COB Form # Account # Branch # FA #

**Enhanced Due Diligence**  
**For use with accounts opened in COB ONLY**

**Purpose & Scope:** The purpose of this form is to collect client KYC data and attributes not currently captured in Client Onboarding (COB).

**Client Name:** \_\_\_\_\_

**Liquidity Needs**  
The ability to quickly and easily convert to cash all or a portion of the investments in this account without experiencing significant loss in value from, for example, the lack of ready market or incurring costs or penalties is (check one):

Significant (Primary need is liquidity)       Moderate (May need quick access to cash)       None (Other sources of cash)

Yes No Will the account be funded by a liquidation of a mutual fund held less than 3 years or an annuity prior to surrender? (If yes, additional compliance documents may be required.)

**Documentary Evidence**

ID Type	ID Number	Issue Date	Expiration Date	State	Country
_____	_____	_____	_____	_____	_____

**Account Assessment**

I acknowledge this account recommendation is an institutional (non-retail) brokerage account and I am properly licensed in the client's resident state.

I acknowledge this account recommendation is an advisory account or retail brokerage account. Recommendations about account types, must be in the client's best interest when fulfilling the SEC Advisers Act and Reg BI obligations. You should consider and assess all account types that you may offer provided by the firm, recommend only those account types that are in the client's best interest, and acknowledge to the client when certain account types are not in the best interest (check all that apply):

Tool: New Account Selection Assessment

# Account Assessment Checklist- HF011 Update

## Account Assessment

- I acknowledge this account recommendation is an institutional (non-retail) brokerage account and I am properly licensed in the client's resident state.
  
- I acknowledge this account recommendation is an advisory account or retail brokerage account.  
*Recommendations about account types, must be in the client's best interest when fulfilling the SEC Advisers Act and Reg BI obligations. You should consider and assess all account types that you may offer provided by the firm, recommend only those account types that are in the client's best interest, and acknowledge to the client when certain account types are not in the best interest (check all that apply):*
  
- After discussing with my client and addressing any questions regarding the differences between fee-based and commission-based relationships, it was determined the account type recommended was in the client's best interest based on a review of the relevant features, services, and costs, as well as the following client attributes:
  - a. Investment objectives
  - b. Financial situation
  - c. Level of financial sophistication
  - d. Investment experience
  - e. Financial goals
  - f. Preferences and expectations
  
- Prior to an account recommendation to a Retail Investor\*, all Form CRS and supplemental disclosure documents were delivered at the appropriate time.
  
- Prior to an account recommendation, I confirmed I am properly licensed in the client's resident state.

# Account Assessment Checklist con't- HF011 Update

The recommended account type included the following additional disclosures and/or considerations listed (select all that apply):

<u>Fee-Based</u>	<u>Commission-Based</u>
<p><input type="checkbox"/> All relevant disclosure brochures (e.g., ADV2A, ADV 2B, RJA ADV2A or Wrap Brochure, and a third party manager ADV if appropriate) related to the investment account type selection were delivered to the client at the appropriate time.</p> <p><input type="checkbox"/> Prior to recommending the specific fee-based relationship in the client's best interest, the features, services, and cost associated with managed and client-directed advisory accounts were considered.</p> <p><input type="checkbox"/> In addition to the required ongoing monitoring, the client is interested in receiving at least one of the following services below:</p> <ul style="list-style-type: none"><li>•Advice &amp; guidance on asset allocation</li><li>•Advise &amp; guidance on investment vehicle</li><li>•Financial planning</li><li>•Education planning</li><li>•Estate planning</li><li>•Retirement education</li><li>•Advice &amp; guidance on investment managers</li></ul>	<p><input type="checkbox"/> All relevant investment account type disclosure documents (e.g. Client Agreement, my personal supplemental disclosure) were delivered to the client at the appropriate time.</p> <p><input type="checkbox"/> If an investment product has also been recommended that has a disclosure brochure (prospectus, offering circular, etc.), the document was delivered to the client at the appropriate time.</p>

# 4. Investment Recommendations

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# What is “reasonable basis”

“Reasonable basis” in the Care Obligation is assessed only at the time of the recommendation and will vary depending on the complexity of and risks associated with the recommended security or investment strategy.

Despite the unique nature of every recommendation, the SEC advises brokers to consider important factors, such as:

1. The security or investment strategy’s characteristics, investment objectives, likely performance in a variety of economic and market conditions, liquidity, and volatility
2. Expected return
3. Any financial incentives related to the recommendation

Note: FINRA’s Suitability Rule still applies.

# Product Catalog Overview

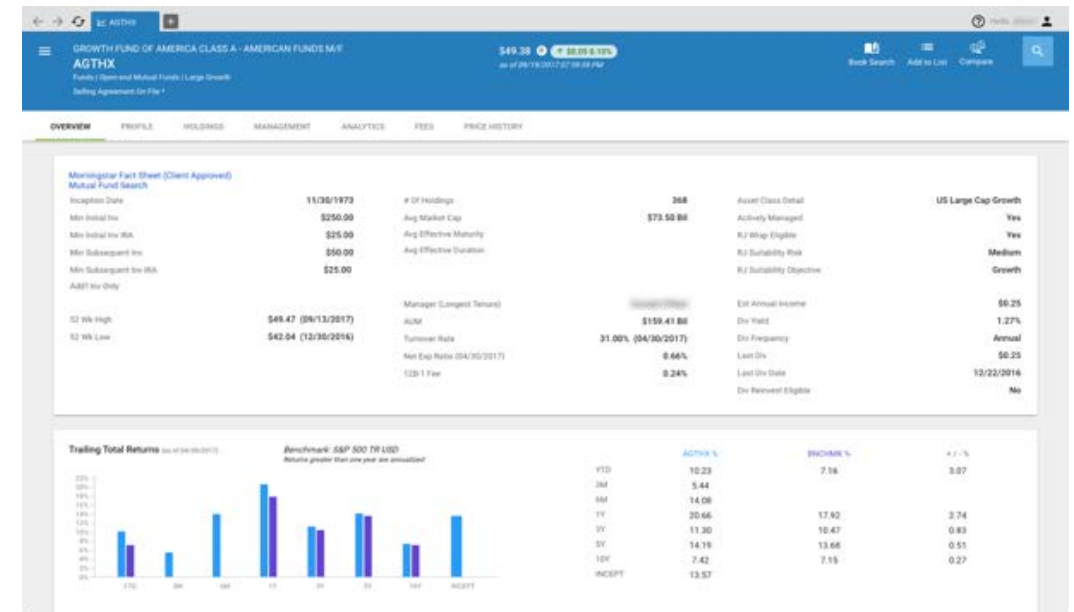
A product research tool to search, screen, compare, and create product lists

Product Screener- refine your search with attributes such as sector, rating or annual dividend.

Product Compare- view performance and analytics side by side

Product Lists- Create custom product lists to manage your investment lineups

Integration- Integrated with AMS products, RJ research, ratings



# Product Vetting Process

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## Define Your Process and Develop a Checklist- Example

### Mutual Fund Selections

1. Determine asset allocation strategy for client's objective and risk profile.
2. Filter for upper quartile funds
3. Review fund management team
4. Review fund expenses- consider breakpoint opportunities
5. Review analyst and Morning Star ratings
6. Document and save review

# Product Vetting Process

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## Define Your Process and Develop a Checklist- Example

### Annuity Selections

1. Review asset strategy for client's objective and risk profile.
2. Review policy terms and benefits
3. Review insurance company ratings
4. Review policy expenses
5. Follow Firm's due diligence/ client disclosure process
6. Document and save review

# Product Vetting Process

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## Define Your Process and Develop a Checklist- Example

### Equity Selections

1. Exchange listed- suitability process
2. Low priced- follow Firm's due diligence review process

# 5. Servicing

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# Understand your servicing requirements based on relationship

## Brokerage

- No account monitoring
- Voluntary reviews best practice, but do not represent ongoing monitoring

## Advisory

- Ongoing account monitoring required
- Must be documented at least annually

# Case Study 1

A retail brokerage client comes to you and asks your opinion of high tech stocks. You tell them that although you think many are currently overpriced, you still believe that the long-term prospects for high tech is excellent.

Would this conversation be covered under Reg BI?

Yes

No

You have not made a recommendation, but simply provided general information about the market for high tech stocks.



# Case Study 2

A prospective brokerage client comes to your office looking for an aggressive investment that could maximize her returns. A colleague had mentioned to you that he had found a new fund that invests in private equity deals, and that in addition to providing for high returns, the trail commission looked favorable.

Although you have not reviewed the prospectus, you deliver a compliance approved product disclosure and recommend to the client. The client agrees to open a new account and invest \$20,000.



Would this transaction be a violation under Reg BI?

Yes

No

Although you provided the product disclosure, you have violated the Care Obligation. There is no mention that you made any effort to determine if the investment was in fact in the customer's best interest. There is no effort to understand the potential risks, and costs associated with the recommendation and therefore there is no reasonable basis to make the recommendation.

# Case Study 3

Tom, a dually registered representative, is beginning a relationship with a new, affluent client. The client qualifies as an accredited investor and is only seeking advice on an occasional transaction.



Tom believes he should still deliver Form CRS at or prior to signing an agreement with his client. Is he correct?

Yes

No

A retail customer is an individual, or their legal representative who receives a recommendation of any securities transaction or investment strategy involving a security and uses the recommendation primarily for personal, family, or household purposes. Net worth does not impact the definition of a retail client.

# Biggest Challenges for Some Producers

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- A. Changing documentation from notepads and moving into electronic format
- B. Creating repeatable processes
- C. Assuming this does not apply to your business model
- D. Not embracing new technology
- E. Resisting change and/or reacting out of fear of the unknown
- F. Post Reg BI, documentation is mandatory- must prove there was a thought process how you got from point A to point B.

# What should I be doing now?

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<b>Follow</b>	For recommendations with a Harbor specific review/disclosure form, follow form instructions to document your recommendation. Anticipate form revisions. Anticipate account/product policy updates. <b>Adjustments to processes, particularly around Duty of Care obligations will occur well beyond June 30<sup>th</sup>.</b>
Train and Use	For recommendations without a Harbor Form, start using RJ CRM to contemporaneously document your considerations and verbal disclosures to clients. RJ CRM will be mandatory as of 6/30/20. Start CRM Training now. Anticipate including costs and alternatives as standard considerations.
<b>Continue</b>	Continue to work with clients to update investment profiles (missing or outdated information). Anticipate NIGOs (not-in-good-order) rejections of new business with missing data.
<b>Develop</b>	Develop a repeatable business process that establishes consistency in your practice and demonstrates actions you take in clients' best interest on a regular basis. <b>Define your process checklist for investment selections.</b>
<b>Practice</b>	Role play /practice your introduction of disclosures and Conversation Starter questions. Exercise key consideration in your recommendation process. <b>Practice documenting contemporaneous notes in RJ CRM.</b>

# How can I access Harbor Reg BI information?



- Harborfs1.com  
New – Reg BI tab
- Attend Meetings  
and read notices
- Ask Compliance

# Q&A

Email your questions to [tbeaman@harborfs.com](mailto:tbeaman@harborfs.com)