SEC Regulation Best Interest: Enhancing Investor Protections

ISSUE: Standard of Care for Securities Licensed Professionals

BACKGROUND: The Securities and Exchange Commission (SEC) has finalized a regulation to address possible retail investor confusion about the relationships that they have with investment professionals. The goal of the regulation is to strengthen the standard of conduct owed to customers, reduce marketplace confusion and provide additional transparency through simple, plain English disclosures.

The regulation imposes a duty on broker-dealers and their registered representatives to act in the best interest of the client when making a recommendation, without putting other interests ahead of the customer.

Reg BI aligns the broker-dealer’s standard of conduct with retail customers’ reasonable expectations by requiring broker-dealers, among other things, to: (1) act in the best interest of the retail customer at the time the recommendation is made, without placing the financial or other interest of the broker-dealer ahead of the interests of the retail customer; and (2) address conflicts of interest by establishing, maintaining, and enforcing policies and procedures reasonably designed to identify and fully and fairly disclose material facts about conflicts of interest, and in instances where we have determined that disclosure is insufficient to reasonably address the conflict, to mitigate or, in certain instances, eliminate the conflict.

Professionals would be required to disclose key facts about the relationship, including material conflicts of interest; to exercise reasonable diligence, care, skill and prudence; to have a reasonable basis to believe that the recommendation(s) are in the customer’s best interest. Additionally, the proposed regulation requires that broker dealers establish, maintain and enforce policies and procedures reasonably designed to identify and then disclose and mitigate, or eliminate material conflicts of interest, especially any arising from financial incentives to the broker-dealer.

There are titling restrictions in the final rule to allow “advice” and “adviser/advisor” to be used by Broker-Dealers (BDs)/Registered Representatives (RRs) as descriptive terms in marketing communications and in dual licensed firm names, even if the RR is not licensed as an Investment Advisor Representative (IAR). Although the final package does not retain a separate “titling restriction” rule, the functional restriction on use of “adviser/advisor” in Registered Representatives’ names and titles remains in place as a component of Regulation BI’s disclosure obligation. Please make sure you understand the complexity of this provision (and all others) by seeking guidance from your BDs.

NAIFA supports a workable best interest standard that does not inadvertently and unnecessarily reduce access to individualized professional assistance, or that imposes a one-size-fits-all compensation structure that would leave many Main Street families without choices in how to affordably work with a broker-dealer.

NEXT STEP: The SEC is expected to provide ongoing guidance and assistance in the implementation of this regulation, but as stated earlier and cannot be overstated, it is imperative that you know, understand and abide by whatever are the requirements of your Broker Dealer.

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