

Regulation Best Interest and Form CRS: Examinations and Enforcement Heat Up

September 16, 2021

Not long after the SEC adopted Regulation Best Interest (Reg BI) and the related Form CRS Relationship Summary in June 2019, the SEC Office of Compliance Inspections and Examinations (now the Division of Examinations) issued two risk alerts outlining its examination focus on compliance with Reg BI and Form CRS. The Division of Examinations staff updated its Reg BI examination guidance in December 2020 for examinations beginning in January 2021.

For its part, FINRA reviewed several broker-dealers in late 2019 and 2020 to assess preparedness for Reg BI and Form CRS. FINRA published the results of its assessment on its website and also prepared a Reg BI and Form CRS firm checklist and other compliance guidance.

As usual, broker-dealers' sales of variable insurance products have been one area of regulators' concern.

Reg BI

When making a recommendation, a broker-dealer and its associated persons are required to act in a retail customer's best interest and cannot place its own interests ahead of the customer's interests.

The SEC conducted initial examinations of broker-dealers in 2020 to assess processes relied on to comply with Reg BI. The SEC has expanded the scope of its examinations in 2021 to assess the implementation of broker-dealers' policies and procedures designed to address the four components of Reg BI: disclosure, care, conflict of interest, and compliance. The 2021 exams also have focused on the need for broker-dealers to consider alternatives to any product they are recommending, including cost considerations. Issues arising when making recommendations to new customers, recommending complex products, and assessing conflicts of interest also have taken center court.

Form CRS

Broker-dealers and registered investment advisers are required to deliver to retail customers a relationship summary that provides information about the firm. Firms also must file Form CRS and post it on their public website.

In announcing its 2021 examination priorities, the SEC Division of Examinations noted that even though “over 13,000” Form CRS filings were made, it sent notices to “hundreds” of firms that had not timely filed Form CRS.

For those firms that received multiple late filing warnings, the SEC took swift enforcement action. In late July, the SEC announced 27 settled enforcement actions involving late Form CRS filings by 21 investment advisers and six broker-dealers. The SEC orders alleged willful violations, with civil money penalties ranging from \$10,000 to \$97,523. The orders imposed the largest penalties on those investment advisers with the greatest amount of regulatory assets under management. The firms did not admit or deny the findings.

What’s Next?

As of the publication of this article, no reported Reg BI enforcement actions appear on the SEC or FINRA websites. But just as SEC warnings of late Form CRS filings led to enforcement actions, SEC and/or FINRA enforcement actions will likely follow from the current Reg BI and Form CRS focused examinations.

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