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## Key Take-Aways from SEC Roundtable on Regulation Best Interest and Form CRS

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The Securities and Exchange Commission ("SEC") staff hosted a roundtable with the Financial Industry Regulatory Authority ("FINRA") on October 26, 2020, to discuss their observations on the implementation of, and compliance with, Form CRS and Regulation Best Interest (BI). While the roundtable discussion touched on a variety of points, the summary below highlights some of the recurring themes and key commentary. Unless otherwise noted, what follows is attributable to Staff at the SEC and/or FINRA.

### **Form CRS**

- *Conflicts of Interest.* Generally, firms provided adequate conflicts disclosure; however:
  - disclosure relative to compensation conflicts continues to fall short; and
  - extraneous descriptions of how conflicts are addressed and mitigated are impermissible because, in the Staff's opinion, these descriptions have the effect of reducing the value of disclosure by downplaying the conflict(s).
- *Website Disclosure.* Staff noted that trying to locate a link to a firm's Form CRS on the firm's website is too often reminiscent of playing a game of "Where is Waldo?".
  - Firms should not use small fonts, hyperlinks away from the homepage, or other approaches that reduce the prominence of Form CRS; and
  - Form CRS should be easily identifiable by name and prominently available on the homepage of a firm's website (i.e., Form CRS should not be hidden within a list of other documents).
- *Disciplinary History.* The biggest single issue Staff has noticed in early implementation relates to the disciplinary section of the Form. Specifically, the Staff observed:
  - Firms answering "no" when they should have answered "yes", or providing a longer response rather than affirmatively answering "yes", which contravenes the form's instructions; and
  - Responses lacking required information, such as heading/conversation starters or providing extraneous narrative explanations. [1]
- *Plain English.* Some firms are using vague and generic boilerplate information which goes against the requirements of Form CRS.
- *Layered Disclosure.* Generally, firms appropriately leveraged cross references to more detailed information; however, some did not include these references or merely referenced that other documents

existed. Firms should make it as easy as possible for investors to find additional information.

### **Regulation BI**

- *Written policies and procedures.* Firms have generally made good faith efforts to implement written policies and procedures. A few recurring issues identified in early implementation efforts include, without limitation:
  - Policies that simply restate the standards and do not provide registered representatives ("RR") with specific, practical instructions for how to comply.
    - For example, a firm might have a policy that says that RRs should consider costs when making recommendations to clients, but the policy doesn't detail or specify what costs to take into consideration. Accordingly, firms should ensure that their policies and procedures are designed to allow RRs to identify how to comply, and not just that they need to comply. [2]
  - Policies where it appears to the Staff that nothing more was done than a global "find-and-replace" to change "*suitability*" to "*best interest*". (More on this below.)
- *Training.* There had been a wide variety of approaches to training prior to the changes in workplace norms driven by the pandemic. Ultimately, most firms have switched to online training.
  - Staff noted some positive steps firms have taken to ensure that training is effective include:
    - post-training tests (requiring test takers to repeat training if a test is failed); and
    - assessing fines for failing to timely complete training (with completion measured by passing the applicable test).
  - Similar to Staff's comments on policies and procedures, the biggest weakness identified in the "Training" category was a focus on what the requirements are, instead of a focus on how to comply with the requirements.
- *Care Obligation.*
  - The Adopting Release for Regulation BI encouraged firms to build on their current suitability-analysis processes and procedures. Staff expressed concern that this guidance was misunderstood, as it appears that many firms have failed to distinguish between "suitability" and "best interest". For example, Staff observed firms focusing solely on risk standards of the two terms, but not providing guidance on how to apply cost considerations and selection among available alternatives.
  - Staff observed that some firms are relying on RR's executing a certification form affirming that a recommendation complies with Regulation BI. Staff noted that, while this may be an element of a reasonably designed supervisory system for complying with Regulation BI, certifications alone are likely insufficient.
- *Conflicts.* Staff indicated that some firms continue to be opaque or vague about their compensation arrangements. In this regard, Staff noted that firms should regularly consult the FAQs (linked below), as Staff regularly updates them with additional guidance regarding Staff's expectations for implementation, particularly with regard to steps necessary to fully identify, mitigate, eliminate and/or disclose conflicts.

- *Disclosure Obligation.*
  - Staff reminded firms that highly legalistic or technical language in disclosures violates the *plain English* requirement; and
  - Staff noted that firms should reference the FAQs (linked below) for the most current guidance on disclosure obligations and, in particular, the use of electronic delivery for disclosures.

**Useful Links:**

1. Chairman Clayton's remarks are available [here](#).
2. Archived webcast is available [here](#).
3. Regulation Best Interest FAQs are available [here](#). Version 4; Last updated: August 4, 2020.
4. Form CRS FAQs are available [here](#). Version 6; Last updated: October 8, 2020.

If you have any questions about the requirements of, and/or how to comply with, Regulation Best Interest or Form CRS, or if you are preparing for or responding to an examination by OCIE or FINRA, please feel free to contact us.

By the ***Investment Manager and Broker-Dealer Team*** at ***Kilpatrick Townsend & Stockton***

**Footnotes**

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[1] Form CRS FAQs make clear that firms are not permitted to add descriptive or qualitative language, or to otherwise attempt to explain the disciplinary history in the Form CRS. Firms must affirmatively respond to this Item 4 of Form CRS with a “yes” or “no” and include a link to investor.gov/CRS. However, in response to the required conversation starter “As a financial professional, do you have any disciplinary history? For what type of conduct?”, a firm may provide additional detail to the prospective client.

[2] In an analogous context, the Commission recently disciplined an advisory firm (with a million dollar fine) for having policies that restrict trading on MNPI but leaving it to each associated persons’ own judgement and personal knowledge to identify whether particularly information met the definition of MNPI.