

# **A Matter of Interpretation: Exploring the SEC's New Rules for Investment Advisors**

**By Fred Reish of Faegre Drinker Biddle & Reath**

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# A milestone for RIAs

The history of debate around standards of care owed to investors by financial service providers is long and continuing. TD Ameritrade was not around to have weighed in on the Investment Advisers Act of 1940, nor the 1963 Supreme Court case *SEC v. Capital Gains Research Bureau, Inc.* that first articulated a fiduciary standard for RIAs.

But following the SEC's initial proposal of its "Merrill Lynch Rule," allowing brokers to charge fees without registering under the '40 Act, our predecessor TD Waterhouse in 2004 and 2005 submitted two formal comment letters to the SEC opposing this rule.

The SEC passed the rule over our objections, and was promptly sued by the Financial Planning Association (FPA). We submitted a friend-of-the-court brief supporting the FPA, and in 2007 the court overturned the rule. RIAs ever since have expressed their great appreciation for our support, and our advocacy mission was born.

A decade later, TD Ameritrade Institutional keeps a close eye on the ever-evolving policy and legislative landscape, so you can focus on running your business. We alert clients to new developments through a variety of channels, as well as do our best to simplify and inform advisors about important changes. We listen to your feedback and we reach out to policymakers in Washington to help ensure that your voice is heard.

The SEC's June 2019 release of its final "Regulation Best Interest" is a milestone for advisors and brokers. In keeping with our commitment to keep advisors informed, we commissioned securities and ERISA attorney Fred Reish of Faegre Drinker Biddle & Reath to produce this brief analysis of the new rules that apply directly to RIAs and how the new rules may affect their firms.

We hope you find it insightful and valuable. At 17 pages, it's certainly more manageable than the 1,363 pages handed down by the SEC!

Visit the newly redesigned TD Ameritrade Institutional [website](#) for my blog featuring regulatory updates. You also can follow me on [Twitter](#). And stay in touch: keep letting us know how you feel about policy issues impacting your business and your clients. We're here for you.

Sincerely,



**Skip Schweiss**

MD, Advisor Advocacy

# Introduction

On June 5, 2019, the SEC issued its Interpretation Regarding Standard of Conduct for Investment Advisers (RIA Interpretation) and Form CRS Relationship Summary; Amendments to Form ADV (Form CRS Rule). The RIA Interpretation was effective on July 12, 2019; in other words, the services of investment advisors are already governed by its provisions. The Form CRS Rule requires compliance beginning on June 30, 2020.

This paper discusses the new rules and the specific steps that investment advisors should be taking. However, the scope of the paper is limited to fee-only advisors. If an investment advisor is also a registered representative of a broker-dealer, there are additional requirements under the SEC's RIA Interpretation, the Form CRS Rule, and Regulation Best Interest. Before getting into the details of the guidance, an overview of the rules will help.

## RIA Interpretation

The SEC says that the RIA Interpretation's purpose is:

to address in one release and reaffirm—and in some cases clarify—certain aspects of the fiduciary duty that an investment adviser owes to its clients under section 206 of the Advisers Act.

While that sounds like the RIA Interpretation is just an explanation of existing rules, there is more to it than that. Investment advisors may find that some of their practices are not in compliance with the SEC's interpretation of the rules.

**The RIA Interpretation applies to both state- and SEC-registered investment advisors.**

### SEC resources



See page 19 for a full list of websites that can give a deeper dive into and help you further navigate:

- › Interpretation of an RIA's standard of care
- › More detailed explanation of the new Form CRS

## Form CRS Rule

The Form CRS Rule is a new requirement, but compliance is not required until June 30, 2020. While this new disclosure document is becoming popularly known as Form CRS, it is also called Form ADV Part 3, which may help investment advisors understand its purpose, delivery, and filing.

In the instructions for investment advisors' Form ADV, the SEC explains the new ADV Part 3 as follows:

Part 3 requires advisers to create a relationship summary (Form CRS) containing information for retail investors. The requirements in Part 3 apply to all investment advisers registered or applying for registration with the SEC, but do not apply to exempt reporting advisers. Every adviser that has retail investors to whom it must deliver a relationship summary must include in the application for registration a relationship summary prepared in accordance with the requirements of Part 3 of Form ADV.

The new Form CRS must be filed with the SEC, but is only required to be delivered to “retail investors.” A retail investor is defined as ***a natural person, or the legal representative of such natural person, who seeks to receive or receives services primarily for personal, family or household purposes.***

The SEC describes the purpose of the new two-page form as follows:

We are adopting a new set of disclosure requirements designed to reduce retail investor confusion in the marketplace for brokerage and investment advisory services and to assist retail investors with the process of deciding whether to engage, or to continue to engage, a particular firm or financial professional and whether to establish, or to continue to maintain, an investment advisory or brokerage relationship. Firms will deliver to retail investors a customer or client relationship summary (“relationship summary” or “Form CRS”) that provides succinct information about the relationships and services the firm offers to retail investors, fees and costs that retail investors will pay, specified conflicts of interest and standards of conduct, and disciplinary history, among other things.

In other words, the purpose is to help investors determine whether to use an investment advisor or a broker-dealer and, if the decision is to use an investment advisor, to allow investors to choose among advisors based, at least in part, on the information disclosed in the form.

**The Form CRS Rule applies only to SEC-registered investment advisors.**

# What should you do now?

The RIA Interpretation applies to you now. The first step is to familiarize yourself with the SEC's interpretation of your duties. This paper is a good starting point for that. But the guidance is detailed and complex, so you need to go beyond the limits of this paper and work with your consultant or lawyer to fully appreciate what the SEC expects under the new guidance.

For example, one area in which investment advisors may be falling short is in the disclosures of conflicts of interest. That comes up in two ways.

## 1. Are all conflicts being disclosed?

The SEC views a recommendation to a participant to roll money out of a retirement plan and into an IRA with the advisor as a conflict of interest that must be disclosed. Another example is a recommendation to a client to transfer money to the advisor (which, if the recommendation is accepted, will result in compensation for the advisor).

## 2. The quality of the disclosure

The SEC's position is that an advisor cannot state that conflicts "may" exist if they currently do exist for at least some clients. Instead, if the advisor engages in practices that result in conflicts, they must be disclosed as currently existing. That could, for example, include revenue-sharing payments from custodians.

While the Form CRS is not required to be delivered to retail investors until June 30, 2020, advisors should familiarize themselves with the required disclosures and begin work on developing the form. Some investment advisor associations have prepared sample CRS Forms that offer a good starting point. However, those sample documents will need to be modified to reflect the advisor's practice.

### Federal Register Rules & Regulations references

- › SEC Interpretation Regarding Standard of Conduct for Investment Advisers [govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12208.pdf](https://www.govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12208.pdf)
- › Form CRS Relationship Summary; Amendments to Form ADV [govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12376.pdf](https://www.govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12376.pdf)

See more on page 19.

# Discussion of the RIA Interpretation

The SEC describes the fiduciary duty for both SEC- and state-registered investment advisors as including a **Duty of Care** and a **Duty of Loyalty**. Those two duties, when combined, are referred to as the duty to provide advice that is in the best interest of the client.

The SEC also reinforced that these duties must be independently and separately satisfied, stating that “disclosure under the Duty of Loyalty does not mean that the Duty of Care has been fulfilled” and that “disclosure and consent do not themselves satisfy the adviser’s duty to act in the client’s best interest.” As an example, the proper disclosure of a conflict arising from payments by custodians would satisfy the Duty of Loyalty, but if it results in higher costs for the client, it can run up against the Duty of Care if lower-cost share classes of the same mutual funds were available for selection.

Before looking more closely at the two duties, it is important to understand the SEC’s views on the scope of those duties, that is, when do they apply and to what extent. The SEC has an expansive view:

An adviser’s fiduciary duty is imposed under the Advisers Act in recognition of the nature of the relationship between an adviser and its client—a relationship of trust and confidence. The adviser’s fiduciary duty is principles-based and applies to the entire relationship between the adviser and its client. The fiduciary duty follows the contours of the relationship between the adviser and its client, and the adviser and its client may shape that relationship by agreement, provided that there is full and fair disclosure and informed consent.

In other words, the fiduciary duty covers all advice given to all clients of an investment advisor, but is limited by the scope of the relationship. The fiduciary duty cannot be waived, but the scope of the relationship can be limited and the advisor will not be a fiduciary for areas that the advisor has not accepted responsibility for. For example, an advisor can provide a financial plan for a client for a one-time fee, and agree that the advisor will not have a duty to monitor the financial plan.

In emphasizing that the fiduciary duty cannot be waived, the SEC stated:

A contract provision purporting to waive the adviser’s federal fiduciary duty generally, such as (i) a statement that the adviser will not act as a fiduciary, (ii) a blanket waiver of all conflicts of interest, or (iii) a waiver of any specific obligation under the Advisers Act, would be inconsistent with the Advisers Act, regardless of the sophistication of the client.

As a result, investment advisors should review their agreements to see if they contain provisions that attempt to limit their fiduciary duties.

## SEC interpretation of the two duties

### Duty of Care

“[R]equires an investment adviser to provide investment advice in the best interest of its client, based on the client’s objectives.”

### Duty of Loyalty

“An investment adviser must eliminate or make full and fair disclosure of all conflicts of interest which might incline an investment adviser—consciously or unconsciously—to render advice which is not disinterested such that a client can provide informed consent to the conflict.”

## Duty of Care

The Duty of Care includes, among other things:

- 1 The duty to provide advice that is in the best interest of the client**
- 2 The duty to seek best execution of a client's transactions where the advisor has the responsibility to select broker-dealers to execute client trades**
- 3 The duty to provide advice and monitoring over the course of the relationship**

### 1A: Duty to provide advice that is in the best interest of the client

The starting point for satisfying the duty to provide advice that is in the best interest of a client is to make a reasonable inquiry into the client's objectives. That process will vary depending on a number of factors, such as the nature of the client, the scope of the relationship, and the nature and complexity of the anticipated investment advice. The SEC provides specific guidance about the process for developing advice for "retail clients." In that case, an advisor must, at a minimum, make a reasonable inquiry into the client's financial situation, level of financial sophistication, investment experience, and financial goals. The SEC refers to that information as a retail client's "investment profile." (A retail client is a natural person, or the legal representative of such natural person, who seeks to receive or receives services primarily for personal, family, or household purposes.)

Within those categories of information, the detail and weight will vary depending on the scope and nature of the engagement. For example, the information needed for financial planning will be different from the information needed to recommend a rollover from a workplace retirement plan.

### 1B: Reasonable belief that advice is in the best interest of the client

After evaluating the relevant information (including the client investment profile for retail investors), and considering the alternatives available to the client, an advisor should develop a reasonable belief that the advice is in the best interest of the client. The considerations for that belief will vary depending on a number of factors, such as the client's risk tolerance, financial sophistication, and objectives. The SEC lists several items to consider:

The cost (including fees and compensation) associated with investment advice would generally be one of many important factors—such as an investment product's or strategy's investment objectives, characteristics (including any special or unusual features), liquidity, risks and potential benefits, volatility, likely performance in a variety of market and economic conditions, time horizon, and cost of exit—to consider when determining whether a security or investment strategy involving a security or securities is in the best interest of the client.

The SEC's highlight of "costs" is intentional. The objective is to elevate the significance of costs in the analysis. However, the SEC is clear that the recommendation of more expensive investments or strategies can satisfy the Duty of Care, where the investment advisor takes costs into account and determines that other factors justify the additional expense. The moral of the story is that costs should be part of the analysis of every investment recommendation, but they are not the only factor to be considered.

In explaining that higher costs can be justified, the SEC said:

For example, it might be consistent with an adviser's fiduciary duty to advise a client with a high risk tolerance and significant investment experience to invest in a private equity fund with relatively higher fees and significantly less liquidity as compared with a fund that invests in publicly-traded companies if the private equity fund was in the client's best interest because it provided exposure to an asset class that was appropriate in the context of the client's overall portfolio.

But, of course, there is more to fiduciary advice than considering costs. The RIA Interpretation also includes several examples of the type of analysis that should be used in providing best interest advice. Here are two:

For example, when an adviser is advising a retail client with a conservative investment objective, investing in certain derivatives may be in the client's best interest when they are used to hedge interest rate risk or other risks in the client's portfolio, whereas investing in certain directionally speculative derivatives on their own may not.

For that same client, investing in a particular security on margin may not be in the client's best interest, even if investing in that same security without the use of margin may be in the client's best interest.

### **There are two takeaways for advisors from these examples.**

- The advice to retail clients will be more closely scrutinized than in the past, particularly on issues such as cost and risk. The SEC chairman has made clear that he intends to focus on "Main Street Investors."
- A careful process, taking into account costs, risks, client investor profile, and other relevant factors, is critical. While the rules do not require written documentation of that process, it would be good risk management to have documentation, particularly where the rationale for the advice would not be obvious to an objective third party.

And the duty to provide advice that is in the best interest of a client is not limited to investments. The SEC explains:

An adviser's fiduciary duty applies to all investment advice the investment adviser provides to clients, including advice about investment strategy, engaging a sub-adviser, and account type. Advice about account type includes advice about whether to open or invest through a certain type of account (e.g., a commission-based brokerage account or a fee-based advisory account) ... **In providing advice about account type, an adviser should consider all types of accounts offered by the adviser and acknowledge to a client when the account types the adviser offers are not in the client's best interest.**

While a requirement to recommend the appropriate account type may have been implicit under the fiduciary standard for investment advisors, the SEC has now made it explicit. It is a part of the Duty of Care. As a result, an advisor must recommend (and monitor) the account type that is in the best interest of the client. Depending on the range of services offered by an advisor, those account types could include, among other things, managed discretionary accounts, advised nondiscretionary accounts, third-party asset managers, point-in-time advice, and subscription advice. The factors to be considered include those discussed elsewhere in this article; as might be expected, though, the primary focus is on the investment profiles of retail investors.

The SEC's discussion of account types also points out that a rollover recommendation is advice to a retail client about account types.

Advice about account type includes ... advice about whether to roll over assets from one account (e.g., a retirement account) into a new or existing account that the adviser or an affiliate of the adviser manages.

As a result, a recommendation to a participant to take a distribution and roll it over into an IRA is subject to the investment advisor's fiduciary standard, including the Duty of Care and the Duty of Loyalty, and must be in the best interest of the participant. Unfortunately, the SEC did not provide guidance about the factors to be considered in the best interest analysis. However, in Regulation Best Interest for broker-dealers, the SEC gave specific directions to broker-dealers to consider, among other things, the investments, costs, and services in the retirement plan and how the participant's account is invested. It is hard to imagine that the broker-dealer best interest standard would be more demanding than the investment advisor best interest standard.

## 2: Duty to seek best execution

An investment advisor's Duty of Care includes a duty to seek best execution of a client's transactions where the advisor has the responsibility to select broker-dealers to execute client trades (typically in the case of discretionary accounts).

The SEC explains that compliance with that duty requires the following:

An adviser fulfills this duty by seeking to obtain the execution of securities transactions on behalf of a client with the goal of maximizing value for the client under the particular circumstances occurring at the time of the transaction. Maximizing value encompasses more than just minimizing cost. When seeking best execution, an adviser should consider "the full range and quality of a broker's services in placing brokerage including, among other things, the value of research provided as well as execution capability, commission rate, financial responsibility, and responsiveness" to the adviser.

An advisor must also periodically evaluate the execution it is receiving for its clients.

## 3: Duty to provide advice and monitoring over the course of the relationship

An investment advisor's Duty of Care also encompasses the duty to provide advice and monitoring at a frequency that is in the best interest of the client, taking into account the scope of the agreed relationship.

The SEC explains:

For example, when the adviser has an ongoing relationship with a client and is compensated with a periodic asset-based fee, the adviser's duty to provide advice and monitoring will be relatively extensive as is consistent with the nature of the relationship.

Conversely, absent an express agreement regarding the adviser's monitoring obligation, when the adviser and the client have a relationship of limited duration, such as for the provision of a one-time financial plan for a one-time fee, the adviser is unlikely to have a duty to monitor.

However, an advisor and client may agree to the frequency of the advisor's monitoring (for example, agreement to monitor quarterly or monthly and as appropriate in between based on market events), provided that there is full and fair disclosure and informed consent. The SEC noted:

We consider the frequency of monitoring, as well as any other material facts relating to the agreed frequency, such as whether there will also be interim monitoring when there are market events relevant to the client's portfolio, to be a material fact relating to the advisory relationship about which an adviser must make full and fair disclosure and obtain informed consent as required by its fiduciary duty.

## Duty of Loyalty

The Duty of Loyalty requires that an advisor not subordinate its clients' interests to its own. In other words, an investment advisor must not place its own interest ahead of its clients' interests. To meet its Duty of Loyalty, an advisor must make full and fair disclosure to its clients of all material facts relating to the advisory relationship.

In addition, an advisor must eliminate or at least expose, through full and fair disclosure, all conflicts of interest "which might incline an investment adviser—consciously or unconsciously—to render advice which was not disinterested."

In the RIA Interpretation, the SEC says that the disclosure must be sufficiently specific to enable a client to:

- 1. Understand the conflict of interest**
- 2. Make an informed decision about whether to provide consent, implied or explicit**

The SEC's emphasis on the information needed for a client to be "informed" is illustrated by its discussion of the use of the word "may":

Disclosure that an adviser "may" have a particular conflict, without more information is not adequate when the conflict actually exists. For example, we would consider the use of "may" inappropriate when the conflict exists with respect to some (but not all) types or classes of clients, advice, or transactions without additional disclosure specifying the types or classes of clients, advice, or transactions with respect to which the conflict exists.

On the other hand, the word "may" could be appropriately used to disclose to a client a potential conflict that does not currently exist but might reasonably present itself in the future.

This guidance is consistent with the SEC's Share Class Selection Disclosure Initiative (SCSDI) and its follow-up enforcement actions. Where a conflict exists for at least some clients, the disclosure cannot say that it "may" exist. And, in the SCSDI, the SEC took the position that the disclosures needed to explain the source and nature of the payments, as well as the advisor's ability to have recommended less expensive share classes of the same funds.

It appears that the SEC has higher expectations about disclosures than many advisors expect. The higher expectations relate to conflicts that must be disclosed and to the affirmative and detailed nature of the disclosures. For example, the SEC position is that a recommendation of a rollover from a retirement plan to an IRA with an advisor is a material conflict of interest, as is a recommendation to a client to transfer additional assets to the advisor. Both of those should be disclosed in a compliant manner. And, in order to obtain an implicit "informed" consent from the client, advisors should consider explaining the nature of the conflict.

Even where disclosures are properly made, there are cases where consent may not be implied. The SEC explains: "We believe, however, that it would not be consistent with an adviser's fiduciary duty to infer or accept client consent where the adviser was aware, or **reasonably should have been aware**, that the client did not understand the nature and import of the conflict."

In effect, this creates an "individualized" analysis where an advisor has reason to believe that a client did not understand the disclosures. In that case, the client's consent cannot be implied. Without consent, an advisor cannot proceed with a transaction that involves a conflict. The advisor will need to either avoid the conflict or obtain consent, after explaining the conflict in a manner that can be understood. But, where a client has diminished capacity to understand financial transactions and associated conflicts, that may not be possible. In that case, the advisor can proceed only if the conflict is eliminated.

The unanswered question is, how much information does a client need to have to provide an informed consent? Unfortunately, the SEC has not clearly answered that question. As a result, advisors should consider taking a conservative approach to disclosing conflicts by, for example, providing more details about any payments received and by explaining, where appropriate, any alternatives to the conflicted advice.

# Discussion of Form CRS/ADV Part 3

Beginning June 30, 2020, investment advisors must deliver a two-page Form CRS relationship summary to existing retail investors and to new retail customers. The Form CRS must be filed with the SEC as Form ADV, Part 3 (and subsequently updated as required).

This part of the paper discusses those requirements and offers insights about some of the requirements. The regulation for the Form CRS Rule is 178 pages of fine print in the Federal Register and it has specific and detailed requirements for the form. Unfortunately, those rules are so voluminous that they cannot be fully explained in this paper; however, this paper does provide a general understanding of what needs to be done.

A CRS relationship summary must disclose specific information about the firm in the following categories. It starts with an **introduction**, followed by **relationships and services**, and then a discussion of **fees, costs, conflicts, and standard of conduct**. The summary then concludes with **disciplinary history** and **additional information**.

We will now explore the requirements and offer some insights.

## Instructions for SEC forms

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**Form ADV:**  
[sec.gov/rules/  
final/2019/34-86032-  
appendix-a.pdf](https://sec.gov/rules/final/2019/34-86032-appendix-a.pdf)

**Form CRS:**  
[sec.gov/rules/  
final/2019/34-86032-  
appendix-b.pdf](https://sec.gov/rules/final/2019/34-86032-appendix-b.pdf)

For more helpful resources, turn to page 19.

## 1. Filing, delivery, and updating

The requirements for drafting, updating, filing, and delivery of the Form CRS are specified in the SEC's regulatory guidance. They are detailed and specific and summarized in the bullet points that follow.

- The Form CRS for investment advisors is filed as Form ADV, Part 3 electronically with the Investment Adviser Registration Depository (IARD). It may be filed beginning May 1, 2020, and must be filed no later than June 30, 2020.
- The Form CRS must be delivered to each "retail investor," that is, a "natural person, or the legal representative of such natural person, who seeks to receive or receives services primarily for personal, family or household purposes." The delivery must be made to existing clients by June 30, 2020, and, for new clients after that, before or at the time of entering into an investment advisory contract.
- After the initial delivery, a copy of the most recent CRS must also be delivered to an existing client who is a retail investor before or at the time that:
  - A new account is opened that is different from the retail investor's existing account;
  - A recommendation is made to roll over assets from a retirement account into a new or existing account or investment; or
  - A recommendation is made of a new investment advisory service or investment that does not necessarily involve the opening of a new account and would not be held in an existing account (for example, mutual funds or insurance products held away).
- The Form CRS must be updated and filed within 30 days of whenever any information in the CRS becomes "materially inaccurate." Changes in the updated CRS must be communicated to the retail investors within 60 days after the updates are required to be made and without change. The changes must be highlighted.

## 2. The Form CRS coverage

- The Form CRS may not exceed two pages in paper format. If delivered electronically, it may not exceed the equivalent of the paper limit. The current version of the Form CRS must be posted prominently on the firm's public website in a location and format that is easily accessible to retail investors.
- The CRS (and any updates) may be delivered electronically, consistent with SEC guidance regarding electronic delivery.
- If the CRS is delivered electronically, it must be presented prominently in the electronic medium.
- If the CRS is delivered in paper as a part of a package, it must be first among the documents in the package.

## 3. Drafting the Form CRS

- The CRS must include the specified disclosures and conversation starters. It may not include anything other than disclosures required or permitted in the instructions.
- A Form CRS must be written in plain English, considering retail investors' level of financial experience. **It should be concise and direct.**

### DOS

- Short sentences and paragraphs
- Definite, concrete, everyday words
- Active voice



### DON'TS

- Legal jargon
- Multiple negatives



- The CRS must be written as if speaking to the retail investor, using "you," "us," "our firm," etc.
- In a CRS posted on a firm's website or otherwise provided electronically, firms must provide a means of facilitating access to any referenced information that is also posted online, for example, links to fee schedules, conflicts disclosures, and other regulatory disclosures.

## 4. Maintenance of records

Investment advisors are required to:

- Make and preserve a record of the dates that each relationship summary was given to any client or prospective client who subsequently becomes a client.
- Retain copies of each relationship summary and each amendment or revision thereto.
- Maintain and preserve these records in an easily accessible place for a period of not less than five years from the end of the fiscal year during which the last entry was made on such record, or for the first two years in an appropriate office of the investment advisor.

As this discussion suggests, the rules covering the drafting, filing, delivery, and updating of the Form CRS are detailed and demanding. However, once investment advisors have prepared their initial Form CRS and delivered it to their retail clients, the requirement will seem less daunting, partially because of the similarities to the Form ADV and advisor familiarity with the delivery, filing, and updating of the Form ADV.

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### Conversation starters

**The following questions must be highlighted for the retail investor to ask the financial professional:**

Given my financial situation, should I choose an investment advisory service? Why or why not?

How will you choose investments to recommend to me?

What is your relevant experience, including your licenses, education, and other qualifications  
What do these qualifications mean?

Help me understand how these fees and costs might affect any investments. If I give you \$10,000 to invest, how much will go to fees and costs, and how much will be invested for me?

How might your conflicts of interest affect me, and how will you address them?

As a financial professional, do you have any disciplinary history? For what type of conduct?

Who is my primary contact person? Is he or she a representative of an investment advisor or a broker-dealer? Who can I talk to if I have concerns about how this person is treating me?

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# What's next?

Steps to consider to ensure compliance with the SEC's RIA Interpretation now and to begin to prepare for the Form CRS Rule.

## STEP 1

**The most significant, and demanding, interpretations deal with the disclosure of conflicts.** Advisors should review every recommendation that could increase their fees from clients or third parties. Those recommendations should be evaluated to determine if they have associated conflicts. If so, the RIA's disclosure documents (for example, Form ADV) should be amended to add those conflicts as disclosures.

## STEP 2

**The RIA Interpretation also requires enhanced disclosure of conflicts.** Advisors should review their conflict disclosures to determine if they are detailed and specific enough to enable clients to provide informed consent to those conflicts. In particular, advisors should review their Forms ADV to see if the disclosures say that conflicts "may" exist (or use similar words or phrases). If so, advisors should determine if those disclosures would be problematic under the SEC's interpretation. Finally, advisors should consider whether to disclose that there may be alternatives that do not cause conflicts or that cost less for the client (for example, share classes at custodians that do not pay revenue-sharing).

## STEP 3

**The RIA Interpretation expresses the view that disclosure of conflicts of interest can satisfy the Duty of Loyalty, but do not, in and of themselves, satisfy the Duty of Care.** Advisors should review their conflicts of interest to determine if they present issues under the Duty of Care. For example, if an investment or service makes payments to an advisor, is that based on higher costs to the client? If so, can those higher costs be justified under the Duty of Care?

## STEP 4

**With regard to the Form CRS, advisors should familiarize themselves with the requirements for the form.** While June 2020 is months away, advisors need to prepare, file and deliver the form by that time. In addition to preparing the form, advisors may need to establish policies and procedures, and training, to support the delivery and updating of the form.

## STEP 5

**Advisor should review the "Conversation starters" above and prepare answers to those questions.** In addition, for firms that have a number of advisors, the answers should be standardized and their delivery should be supervised.

# Conclusion

The SEC's RIA Interpretation will, as a practical matter, impose demanding standards on advisors, particularly with regard to the **Duty of Loyalty** and conflicts of interest. The SEC has also enhanced the **Duty of Care**, with a focus on costs and risks for retail investors.

However, for fee-only advisors the burden may not be significant. They will likely need to augment their conflicts disclosures, for example, to include rollover recommendations and advice to clients about transferring money to the advisor, but that is a manageable task. For advisors who receive third-party compensation (such as payments from custodians), the job is bigger. Those advisors will need to disclose the conflicts and explain whether lower-cost investments for the client could have been recommended.

The Form CRS will initially require some attention and cost, but over time, it should not be unduly burdensome for fee-only investment advisors.

# Additional resources

Visit these official U.S. government websites for more information about Regulation Best Interest and Form CRS.

## Federal Register

**SEC Interpretation Regarding Standard of Conduct for Investment Advisers**

[govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12208.pdf](https://www.govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12208.pdf)

**Form CRS Relationship Summary; Amendments to Form ADV**

[govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12376.pdf](https://www.govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12376.pdf)

**Regulation Best Interest: The Broker-Dealer Standard of Conduct**

[govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12164.pdf](https://www.govinfo.gov/content/pkg/FR-2019-07-12/pdf/2019-12164.pdf)

## SEC

**Small Entity Compliance Guide to the Form CRS Relationship Summary; Amendments to Form ADV**

[sec.gov/info/smallbus/secg/form-crs-relationship-summary](https://sec.gov/info/smallbus/secg/form-crs-relationship-summary)

**Small Entity Compliance Guide for Regulation Best Interest**

[sec.gov/info/smallbus/secg/regulation-best-interest](https://sec.gov/info/smallbus/secg/regulation-best-interest)

**Instructions for Form ADV**

[sec.gov/rules/final/2019/34-86032-appendix-a.pdf](https://sec.gov/rules/final/2019/34-86032-appendix-a.pdf)

**Instructions for Form CRS**

[sec.gov/rules/final/2019/34-86032-appendix-b.pdf](https://sec.gov/rules/final/2019/34-86032-appendix-b.pdf)

## FINRA

**Regulation Best Interest and Form CRS Checklist**

[finra.org/sites/default/files/2019-10/reg-bi-checklist.pdf](https://finra.org/sites/default/files/2019-10/reg-bi-checklist.pdf)

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#### About the author

Fred Reish of Faegre Drinker Biddle & Reath represents clients in fiduciary issues, prohibited transactions, tax-qualification, and Department of Labor, Securities and Exchange Commission, and FINRA examinations of retirement plans and IRA issues.

Fred works with both private and public sector entities and their plans and fiduciaries and represents plans, employers, and fiduciaries before federal agencies such as the DOL and IRS. He consults with banks, trust companies, insurance companies, and mutual fund management companies on 401(k) recordkeeping services, investment products, and issues related to plan investments and retirement income. He also represents broker-dealers and Registered Investment Advisors on issues related to fiduciary status and compliance, prohibited transactions, and internal procedures.

His experience also includes advising insurance companies and investment managers on the development of products and services that are consistent with ERISA's fiduciary standards and prohibited transaction restrictions, including retirement income investments and guarantees.

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