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Regulation Best Interest: Is the SEC Finally Choosing Main Street Over Wall Street?

Ana Marcos
University of Miami School of Law

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Ana Marcos[1]

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[1] Ana Marcos is a Second-Year law student at the University of Miami School of Law. Prior to Law School, Ms. Ana Marcos attended and graduated from the University of Notre Dame, earning a Bachelor of Science in Business Administration–Finance. Ms. Marcos would like to thank Professor Verges for her time and commitment in assiting her with this paper.

I. INTRODUCTION

Broker-dealers and investment advisers, two types of financial service providers, play an important role in helping retail investors organize their finances, accumulate wealth, and manage their savings. In particular, investors rely on broker-dealers and investment advisers for investment advice and expect that the advice given is in the investor's best interest. The regulatory regime that governs the provision of investment advice to retail investors is crucial in assuring that legal obligations of investment advisers and broker-dealers match the expectation and needs of investors. Though broker-dealers and investment advisers are regulated extensively, the two financial professionals actually operate under different rules since they are subject to different standards under federal law when providing investment advice about securities and investment strategies.[2]

Hence, the regulatory schemes for investment advisers and broker-dealers are designed to protect investors through different approaches. In the United States, investment advisers must adhere to the Investment Advisers Act of 1940, which calls on advisers to perform fiduciary duties in regards to their clients' accounts.[3] While broker-dealers, are governed for the most part by the Securities Exchange Act of 1933, Securities Exchange Act of 1934, specific Exchange Act rules and Self-Regulatory Organization ("SRO") rules.[4] The rules based on the Exchange Act principles are constructed on principles of fairness and transparency.[5]

Yet, retail investors generally are not aware of the regulatory differences between broker-dealer and investment advisers or their legal implications. Many investors are confused by the different standards of care that apply to broker-dealers and investment advisers.[6] Hence, the confusion has been a source of great concern for both regulators and Congress.[7] It has caused concern particularly because many financial services firms today allow their employees to be "dually registered," further blurring the line between broker-dealer and investment adviser responsibilities.[8]

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2 *See* STAFF OF THE U.S. SECURITIES AND EXCHANGE COMMISSION, STUDY ON INVESTMENT ADVISERS AND BROKER-DEALERS AS REQUIRED BY SECTION 913 OF THE DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT i (Jan. 2011) , www.sec.gov/news/studies/2011/913studyfinal.pdf [hereinafter 913 STUDY] (discussing the different regulatory regimes of broker-dealers and investment advisers).

3 *Id.* at iii.

4 *Id.*

5 *Id.*

6 *Id*. at i.

7 *Id.*

8 913 STUDY, *supra* note 2, at 12.

Consequently, on June 5, 2019, the Securities and Exchange Commission ("SEC") officially adopted a new rule 15*l*-1 under the Exchange Act, known as "Regulation Best Interest."[9] Regulation Best Interest established a new standard of conduct for broker-dealers meant to strengthen investor protection by: (1) reinforcing the obligations that apply to broker dealers when making an investment recommendation to retail customers; and (2) reducing the possible harm to retail investors from potential conflicts of interest.[10] Through its new rule, the SEC sought to (i) educate retail customers about the services offered by broker-dealers and investment advisers to enable them to make informed decision; (ii) provide transparency with respect to the standards of conduct applicable to broker-dealers and investment advisers; and (iii) help fill the gap that currently exists in the level of protection provided to each regime.[11]

This Article provides an overview of the rules and regulations governing the standard of conduct of broker-dealers and investment advisers and the impact Regulation Best Interest will have on the investment recommendations made to retail customers. Part I will introduce the regulatory differences between broker-dealers and investment advisers. Part II will look at the creation of the two regulatory frameworks governing broker-dealers and investment advisers and discuss the impact they have in today's financial services industry. Part III will introduce Regulation Best Interest and explain the different components to the rule. Finally, Part IV will look at what Regulation Best Interest attempts to achieve, the notable gaps in the regulation, and propose reasonable improvements to Regulation Best Interest.

II. PRIOR LAW AND PERSPECTIVE

A. The Creation of the Regulatory Frameworks Governing Broker-Dealers and Investment Advisors

The legal framework for determining the regulatory authority that governs broker- dealers and investment advisers begins with the development of the Federal Securities Regulation and creation of the SEC.[12] Following the stock market crash of October 1929, public

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9 17 C.F.R. § 240.15*l*-1 (2019).

10 Adopting Release 34-86031 (June 5, 2019) 4-5, www.sec.gov/rules/final/2019/34-86031.pdf [hereinafter Reg BI Release] (discussing the release of regulation best interest).

11 David W. Soden & Cody J. Vitello, *The New Standards for Investor Protection: An Analysis of Regulation Best Interest, Form CRS and Two Interpretations of the US Investment Advisers Act*, IX 250 THE NATIONAL LAW REVIEW, Sept. 19 2019.

12 *See generally* Richard J. Kubiak, *Comment: Off-Regulation: Examining the SEC's and the DOL's Dissonant Regulation of Broker-Dealers*, 68 Emory L.J. 369, 376 (2018).

confidence in the markets plummeted and there was a general consensus that for the economy to recover, the public's faith in the capital markets needed to be restored.[13] As a result, Congress enacted the Securities Act of 1933 ("Securities Act") and the Securities Exchange Act of 1934 ("Exchange Act").[14] The Securities Act together with the Exchange Act, which created the SEC, were designed to restore investor confidence in the capital markets by providing investors with more reliable information and clear rules of honest dealing.[15]

The Securities Act had two basic objectives: (1) require that investors receive financial and other significant information concerning securities being offered for public sale; and (2) prohibit deceit, misrepresentations, and other fraud in the sale of securities.[16] Further, a year later, the Exchange Act empowered the SEC with broad authority over all aspects of the securities industry.[17] It included the power to register, regulate, and oversee brokerage firms, clearing agencies, stock exchanges, and SROs such as the Financial Regulatory Authority ("FINRA").[18] The Act also provided the SEC with disciplinary powers over regulated entities and their associates persons.[19] Yet, these two Acts left out a group of professionals known as "Investment Advisers."

Investment Advisers provide a wide range of investment advisory services to clients. From individuals and families looking to plan for retirement or grow their capital, clients seek the services of investment advisers to help them evaluate their investment needs and provide ongoing financial planning advice for a fixed fee.[20] Investment Advisers are governed by the Investment Advisers Act of 1940 ("Advisers Act").[21] Its general objective "was to protect the public and investors against malpractices by persons paid for advising others about securities."[22] Investment Adviser employees under the Advisers Act are regulated as

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13 SEC, *What We Do*, https://www.sec.gov/Article/whatwedo.html#org (last visited Nov. 3, 2019).

14 *Id.*

15 *Id.* (explaining that the Securities Act focused on companies publicly offering securities for investment dollars (primary market), while the Exchange Act focused on the people who sell and trade securities such as broker-dealers and exchanges (secondary market)).

16 *Id.*

17 *Id.*

18 *Id.*

19 SEC, *supra* note 13.

20 913 STUDY, *supra* note 2, at 6-7.

21 *Id.* (explaining that the Advisers Act resulted from a congressionally mandated study conducted by the Commission of investment companies, investment counsel, and investment advisory services).

22 *Id.* (citing S. Rep No. 1760, 86th Cong., 2d Sess. 1 (1960)).

"investment adviser representatives," and subject to state statutes and provisions under the Act. [23]

Under the Advisers Act, a person falls within the meaning of an "investment adviser" if that person: (1) provides advice, or issues reports or analyses, regarding securities; (2) is in the business of providing such services; and (3) provides such services for compensation.[24] An important thing to note is that the Advisers Act excludes from its definition of investment adviser any broker dealer: (i) whose investment advisory service is "solely incidental"[25] to the conduct of its business as a broker or dealer; and (ii) who receives no "special compensation" for its advisory services.[26] Thus, a registered representative of a broker-dealer is entitled to rely on the broker-dealer exclusion of the Advisers Act if he or she is providing advisory services to customers within the scope of his or her employment as a broker-dealer.[27]

Though the fiduciary duty to which advisers are subject to is not defined in the Advisers Act, in *SEC v. Capital Gains Research Bureau, Inc.*, the Supreme Court construed the Advisers Act Section 206(1) and (2) as establishing a federal fiduciary standard governing the conduct of investment advisers.[28] As such, under the Advisers Act, a fiduciary standard applies to the investment adviser's relationship with its clients.[29] The fiduciary standard requires that the investment adviser must satisfy "an affirmative duty of outmost good faith, and full and fair disclosure of all material fact," as well as an obligation to use reasonable care to avoid misleading clients.[30] The duties of loyalty and care which require an adviser to serve the best interest of its clients are fundamental to the fiduciary standard.

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23 *Id.* at 14.

24 *Id.* at 15.

25 *Id.* at 15-16 (noting that "solely incidental" elements amounts to recognition that broker-dealers give a certain amount of advice to their customers in the course of their regular business and it would be inappropriate to bring them within the scope of the Advisers Act).

26 913 STUDY, *supra* note 2, at 15-16 (noting that "special compensation" amounts to clear recognition that a broker or dealer is specially compensated for rendering advice should be considered an investment adviser and not excluded for the purview of the Advisers Act).

27 *Id.* at 16.

28 *See* SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180,194 (1963) (noting that the Act's legislative history leaves no doubt that Congress intended to impose enforceable fiduciary obligations).

29 913 STUDY, *supra* note 2, at 22.

30 *See SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. at 193.

Under the duty of care, investment advisers are required to provide investment advice that is congruent with the client's objectives.[31] As explained in more detail below, the duty of care is composed of various sub-duties. First, an investment adviser has a duty to provide advice that is in the best interest of the client.[32] This means that an investment adviser must have both a "reasonable understanding of the client's objectives" and "a reasonable belief that the advice it provides is in the best interest of the client," based on his or her objectives.[33] To have a reasonable understanding of the client's objectives, "at minimum an adviser must inquire about a client's financial situation, level of investment sophistication, investment experience and financial goals."[34] Second, under the duty of care, an investment adviser has a duty to seek best execution of a client's securities transactions, when it is responsible for selecting executing broker-dealers.[35] Lastly, an investment adviser has a duty to provide advice and frequently monitor a client's account over the course of the agreed upon relationship.[36]

Likewise, the duty of loyalty requires that an investment adviser not put his own interest ahead of its client's interests.[37] To meet its duty of loyalty, an investment adviser is required to make full and fair disclosure to its clients of all material facts relevant to the adviser-client relationship, including the capacity in which the firm is acting with respect to the advice provided, particularly when the firm is dually registered.[38] An adviser must also make full and fair disclosure of any conflict of interest and obtain the client's informed consent.[39] For disclosure to be "full and fair," an adviser is required to present the client with specific facts so that the client is able to understand the material facts and any potential conflict of interest to make an informed decision as to whether or not to provide consent.[40] Whether the disclosure is considered full and fair will depend upon various things such as the nature of the client, the scope of the services provided, and the material facts or conflicts.[41]

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31 *See* Adopting Release IA-5248 (July 12, 2019) 8, https://www.sec.gov/rules/interp/2019/ia-5248.pdf [hereinafter *Fiduciary Interpretation*] (discussing the Commission's interpretation regarding the standard of conduct for Investment Adviser's after Regulation Best Interest.)

32 *Id.* at 12.

33 *Id.* at 13, 15.

34 *Id.*

35 *Id.* at 19.

36 *Id.* at 20.

37 *Fiduciary Interpretation*, *supra* note 31 at 21.

38 *Id.* at 22.

39 *Id.* at 23.

40 *Id.* at 24.

41 *Id.* at 25.

Though most broker-dealers are not considered investment advisers under the Advisers Act, they are subject to additional regulatory oversight apart from the SEC. In 1938, the Maloney Act amended the Exchange Act and authorized the SEC to "register self-regulated voluntary national associations of broker-dealers that would operate under SEC oversight."[42] Consequently, FINRA was created to protect investors and strengthen market integrity through the regulation of its registered members.[43] FINRA's registered members include "every firm and broker that sells securities to the public in the United States."[44] Thus, by law, every firm and broker is required to register with FINRA.[45]

FINRA established standards of conduct that broker-dealer members must adhere to when operating on behalf of clients.[46] Under FINRA's Rule 2111, a broker-dealer could only recommend a transaction or investment strategy if "it had reasonable basis to believe that a recommendation or investment strategy involving a security was suitable for the customer."[47] This means that a broker-dealer is required to choose from a selection of suitable investment based on client's risk tolerance, age, and investment objectives. [48] Yet, under this rule, unlike an investment adviser, a broker-dealer is not required to act in the best interest of its retail customer.[49]

B. Overview of the Current Regulatory Landscape

Today, many financial services firms offer both investment advisory and broker-dealer services, allowing their employees to be dually registered as investment adviser and broker-dealer representatives.[50] The dual registration model allows advisers to be affiliated with a broker dealer for commission-based securities while separately meeting the standards of

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42 Nat'l Ass'n of Sec. Dealers, Inc., (1997), https://www.finra.org/sites/default/files/Corporate/p009762. pdf (last visited Nov. 3, 2019).

43 Press Release, FINRA, NASD and NYSE Member Regulation Combine to Form the Financial Industry Regulatory Authority - FINRA (July 30, 2007), https://www.finra.org/media-center/news-releases/2007/nasd-and-nyse-member-regulation-combine-form-financial-industry (last visited Feburary 24, 2021).

44 Member Regulation, FINRA, http://www.finra.org/industry/member-regulation (last visited Nov. 3, 2019).

45 *Id.*

46 Rules and Guidance, FINRA,https://www.finra.org/industry/rules-and-guidance (last visited Nov. 3, 2019).

47 See FINRA Manual, Contents: Rule 2111, FINRA (May 1, 2014), https://www.finra.org/rules-guidance/rulebooks/finra-rules/2111 (last visited Nov. 3, 2019) [hereinafter FINRA Manual].

48 *Id.*

49 *Id.*

50 913 STUDY, *supra* note 2, at 12.

a fee-based investment adviser.[51] Dual registration also allows firms to provide a variety of services to customers that would not be available if those entities were solely registered as investment advisers or broker-dealers.[52] Consequently, retail investors may have a number of different accounts at a financial services firm that are subject to investment adviser or broker-dealer regulations.[53] Though having multiple accounts may bring certain benefits to investors such as taking advantage of the different forms of compensation paid to brokers-dealers and investment advisers, they also present conflicts and confusion regarding the different responsibilities dual registrants have towards retail investors.[54]

When acting as dual registrants, investment advisers and broker-dealers must adhere to different standards of conduct based on the role they have chosen to take when interacting with their investor clients.[55] As previously mentioned, these standards of conduct are imposed by federal securities laws, and in the case of broker-dealers, by self-regulatory organizations, such as FINRA.[56] Therefore, when a dually registered financial services employee is acting as an "investment adviser," meaning he or she is in the business of providing investment advice for compensation, the Investment Advisers Act controls.[57]

On the other hand, when a dual registrant acts solely as a broker-dealer when interacting with investor clients, the Advisers Act does not apply[58] since it excludes from the investment adviser definition any broker-dealer who provides "solely incidental advice" to clients.[59] Thus, the disparity that exists between the two regulatory frameworks is a source of great concern for Congress regarding (1) the potential harm to retail customer resulting from broker-dealer recommendations where conflicts of interests exist, and (2) the insufficiency of broker-dealer regulatory requirements to address these conflicts.[60] In other words, Congress is concerned that existing requirements do not require a broker-dealer's recommendation to be in the best interest of the retail customer.

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51 Sarah O' Brien, Booming: The new dually registered advisor model, CNBC (Mar. 16, 2015), https://www.cnbc.com/2015/03/16/booming-the-new-dually-registered-advisor-model.html.

52 913 STUDY, *supra* note 2, at 12.

53 *Id.*

54 *Id.*

55 *Id.*

56 *Id.*

57 *Id.*

58 *See* FINRA Rules, https://www.finra.org/rules-guidance/rulebooks/finra-rules (last visited Nov. 4, 2019).

59 Opinion of the General Counsel Relating to Section 202(a)(11)(C) of the Investment Advisers Act of 1940, Investment Advisers Act Release No. 2 (Oct. 28, 1940).

60 913 STUDY, *supra* note 2, at 9.

III. MAIN REGULATION AT HAND

A. The Emergence of Regulation Best Interest

On January 2011, the SEC conducted a study on investment advisers and broker-dealers as required by Section 913 of the Dodd Frank Wall Street Reform and Consumer Protection Act ("Dodd Frank Act").[61] Section 913 requires that the SEC conduct a wide-ranging study regarding gaps or deficiencies in the regulation of broker-dealers and investment advisers.[62] Since these firms often perform similar functions but are regulated differently, Congress set forth key items the SEC must consider in its study including "any other consideration the SEC deems appropriate."[63] In doing so, Congress gave the SEC new rulemaking authority.[64] Yet, the SEC's new authority, fell short of empowering it to fully address the study's potential findings since the provision intended to address the gaps in the regulation had a gap of its own-a gap between the issues the study found and the tools the SEC had been provided to solve them.[65]

In light of the inconsistencies between the study's scope and the SEC's new rulemaking authority, the Department of Labor ("DOL") attempted to expand the fiduciary rule for investment advisers under the Employee Retirement Income Security Act of 1974 ("ERISA").[66] Yet, the DOL's efforts to create a Fiduciary Rule came to a halt when the Fifth Circuit Court concluded that the DOL had overreached its mission.[67] In response to the political pressures prompted by the Court's split 2-1 decision, the SEC stepped up and proposed a new rule 15*l*-1 under the Exchange Act on April 18, 2018.[68] This new rule, known as "Regulation Best Interest"

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61 See generally *id.*

62 Dodd Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. § 913. 124 Stat. 1376, 1824 (2010) (mandating study and rulemaking regarding obligations of brokers, dealers, and investment advisers).

63 *Id.* at § 913(b)-(b)(1).

64 *Id.* at § 913(c) (explaining that the SEC could commence a rulemaking, as necessary or appropriate in the public interest and for the protection of retail customers to address the legal or regulatory standards of care for broker-dealers, investment advisers, and their associated persons).

65 *Id.* (noting that in giving the SEC new rulemaking authority, Congress recognized the need of additional legislation to reform the regulations of broker dealers and investment advisers).

66 *Id.* (explaining that the DOL's Fiduciary Rule, also known as the "Conflict of Interest" rule, stated that advisers must give conflict free advice on retirement accounts, putting their client's needs ahead of their own potential compensation).

67 Alessandra Malito, The fiduciary rule is officially dead. What its fate means to you, MARKETWATCH (June 25, 2018), https://www.marketwatch.com/story/is-the-fiduciary-rule-dead-or-alive-what-its-fate-means-to-you-2018-03-16.

68 Reg BI Release, *supra* note 10, at 9.

sought to materialize the broad rule-making authority given to the SEC by the Dodd Frank Act.

Regulation Best Interest proposed enhancements to the broker-dealer standard of conduct when making recommendations to retail customers.[69] Specifically, the regulation established an express best interest obligation that would require all broker-dealers and associated persons, to act in the best interest of the retail customer, at the time of recommending a security transaction or investment strategy.[70] Under this new regulation, a broker-dealer could not place its financial interest ahead of the interest of its customers.[71] This new standard of conduct established by Regulation Best Interest emerges from key fiduciary principles, including those that apply to investment advisers, yet does not impose a formal fiduciary standard for broker-dealers.[72] Rather, it requires that whether a retail investor chooses a broker-dealer or an investment adviser (or both), the investor will be entitled to receive an investment recommendation that is in his or her best interest based on his or her financial needs and investment objectives.[73]

In response to its proposed release, the SEC received over 6,000 comment letters from individual investors, financial services firms, state securities regulators, among others.[74] Despite various concerns and proposed recommendations to the rule, on June 5, 2019, the SEC voted 3-1 to approve a package of rules and regulations that would enhance the quality and transparency of investors' relationships with broker-dealers and investment advisers.[75] The rule became effective on September 10, 2019, and requires compliance by June 30, 2020.[76]

B. A Broker-Dealer's Obligations under Regulation Best Interest

Regulation Best Interest is composed of two parts: (1) an overall provision setting forth that a broker-dealer must act in the retail customer's best interest and cannot place its own interest ahead of the retail customers (hereinafter, "General Obligation"); and (2) a second provision requiring compliance with specific sub-component obligations in order to satisfy the

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69 *Id.*
70 *Id.*
71 *Id.*
72 Reg BI Release, *supra* note 10, at 68.
73 *Id.*
74 *See* Staff of the Securities and Exchange Commission, Regulation Best Interest, Release No. 34-83062 1 (April 18, 2018), https://www.sec.gov/rules/final/2019/34-86031.pdf (last visited Nov. 6, 2019) [hereinafter Proposel Rule].
75 Soden & Vitello, *supra* note 11.
76 Reg BI Interest, *supra* note 10, at 2.

General Obligation standard.[77] The General Obligation is satisfied only if the broker-dealer complies with four specific sub-component obligations, which include: the (i) Disclosure Obligation, (ii) Care Obligation, (iii) Conflict of Interest Obligation, and (iv) Compliance Obligation.[78] Thus, a violation of any of the four sub-component obligations will lead to a violation of the General Obligation.[79] It is important to note that intent is not required to establish a violation of the General Obligation.[80]

First, the Disclosure Obligation requires that a broker dealer "prior to or at the time of [a] recommendation, reasonably disclose to the retail customer, in writing, the material facts relating to the scope and terms of the relationship with the retail customer and all material conflicts of interest associated with the recommendation."[81] Pursuant to this obligation, the Reg BI Release noted that material facts include: (1) whether the broker-dealer was acting in a broker, dealer, or associated person capacity with respect to the recommendation; (2) fees and costs that apply to the retail customer's transactions, holdings, and accounts and how those fees are deducted (e.g., on a per transaction basis or quarterly); (3) type and scope of services,[82] and (4) conflicts of interest the customer should know about.[83] Though the form and manner of disclosure is flexible under Regulation Best Interest, broker-dealers and investment advisers are also required to deliver to retail investors the Relationship Summary.[84] The Relationship Summary is considered the initial layer of disclosure, with the Disclosure Obligation reflecting more specific and additional detailed

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77 *Id.* at 13 (discussing the enhancements to standard of conduct that applies when broker-dealers make recommendations to retail customers, specifically the proposal of Regulation Best Interest).

78 *Id.* at 15 (explaining that although Regulation Best Interest identifies specified obligations with which a broker-dealer must comply in order to meet its General Obligation, compliance with each of the component obligation of Regulation Best Interest will be principles-based. In other words, whether a broker-dealer has acted in a retail customer's best interest will turn on an objective assessment of the fact and circumstances at the time the recommendation is made).

79 *See* i*d.*

80 *Id.*

81 *Id.* at 130.

82 *See id.* at 14 (noting that type and scope of services includes the following examples of facts that are deemed to be material and require disclosure: (1) whether a broker-dealer had material limitations on the securities; (2) whether a broker-dealer provides account monitoring and if so, its frequency; (3) whether a broker-dealer has any new account balance requirements; (4) the "general basis or strategy" for a recommendation; (5) the "general risks associated with a particular recommendation).

83 *Id.*

84 *See id.* at 134 (explaining that the Relationship Summary provides information about the relationship and services offered as well as fees and costs that the retail investor will pay).

layers of disclosure.[85] Accordingly, the Disclosure Obligation encourages investors to ask questions and request additional sources of information when needed.[86]

Second, the Care Obligation requires that a broker-dealer, when making a recommendation of any security transaction or investment strategy involving securities to a retail customer, exercise "reasonable diligence, care, and skill" in meeting the three components that make up the Care Obligation.[87] These three components are the following: (1) a Reasonable- Basis Component, which requires a broker-dealer to understand the potential risks, rewards, and costs associated with a recommendation and have "reasonable basis" to believe that the recommendation could be in the best interest of at least some retail customers; (2) a Customer-Specific Component, which requires that a broker-dealer must have reasonable basis to believe the recommendation is in the best interest of a "particular" retail customer based on the retail customer's investment profile; and (3) a Quantitative-Care Component, which requires that a broker-dealer must have reasonable basis to believe that a series of recommended transactions, even if in the retail customer's best interest, when viewed in isolation, is not excessive.[88] The Care Obligation is considered the heart of Regulation Best Interest and was intended to incorporate and enhance existing suitability requirements applicable to broker-dealers under the federal securities laws.[89]

Third, the Conflict of Interest Obligation requires a broker-dealer to establish, maintain, and enforce written policies and procedures that are reasonably designed to identify and address the effect of the broker-dealer's conflict of interest on a recommendation.[90] At a minimum, a broker-dealer is required to (1) disclose or eliminate, all conflict of interests associated with a recommendation and (2) identify the material facts associated with that conflict in order to establish specific requirements with respect to the policies and procedures for the mitigation and elimination of certain conflicts.[91] These policies and procedures are designed to address potential conflicts of interest and broker-dealers must disclose the material limitations of the menu of securities when the conflict stems from such limitation so that the conflict is either mitigated or

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85 *Id.*

86 *Id.*

87 *Id.* at 245.

88 *See id.* at 245.

89 *See id.*

90 Soden & Vitello, *supra* note 11 (explaining that this obligation achieves greater consistency with the treatment of conflicts under the Advisers Act since it requires that a broker-dealer expose all conflicts of interest through full and fair disclosure).

91 *Id.*

eliminated.[92] In doing so, the Conflict of Interest Obligation is intended to reduce the information asymmetry that exists between a retail customer and broker dealer with respect to the broker dealer's conflict of interests that may have an effect on the recommendation provided to the retail customer.[93] Thus, by having a process in place to identify and address conflict of interests at the time of recommendation, retail customers can make a better assessment of the efficiency of the recommendation they receive.[94]

Fourth, the Compliance Obligation requires in addition to the policies and procedures required by the Conflict of Interest Obligation, that broker-dealers establish, maintain, and enforce policies and procedures "reasonably designed" to achieve compliance with Regulation Best Interest.[95] The Compliance Obligation "creates an affirmative obligation under the Exchange Act" to comply with Regulation Best Interest as a whole by not only addressing conflicts of interests but also complying with the Disclosure and Care Obligations.[96] In addition, the Compliance Obligation requires that a firm's policies and procedures be "reasonably designed" to address the "scope, size, and risks associated with the operations of the firm and the types of businesses in which the firm engages."[97] Though the SEC does not mandate specific requirements to the Compliance Obligation, a reasonably designed compliance program generally would include: "(1) remediation of non-compliance; (2) controls; (3) compliance training; and (4) periodic review and testing."[98]

Additionally, in addition to its General Obligation and sub-component obligations, Regulation Best Interest requires adoption of "record-making and record keeping requirements."[99] The requirements include a record of all information collected from and provided to the retail customer when recommending a security or investment strategy and retention of all records and account information for at least six years.[100] Examples of record keeping requirements under the rule include having a "retail customer investment profile[s]," and all written disclosures provided to

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92 *Id.*

93 Reg BI Release, *supra* note 10, at 568.

94 *Id.* at 574.

95 *Id.* at 358.

96 *Id.*

97 *Id.* at 360.

98 *Id.*

99 Reg BI Release, *supra* note 10, at 361 (specifying minimum requirements with respect to the records that broker-dealers must make, and how these records must be kept).

100 *Id.* at 369 (noting that the six-year minimum requirement is six years after the earlier of the date the account was closed or the date on which the information was replaced or outdated).

customers.[101] A broker-dealer does not need to maintain record on a "recommendation-by-recommendation basis," but it should be able to explain in general terms the process by which the firm determines what recommendations are in its customers' best interest and similarly how that process would be applied to a particular recommendation.[102]

Finally, Regulation Best Interest has also incorporated Form CRS as part of its requirements.[103] Form CRS is a new question and answer, open-ended disclosure document that helps address investor confusion about the nature of their relationship with investment professionals.[104] Form CRS is intended to provide retail investors with simple, easy to understand information about: (1) the types of services offered; (2) applicable fees the retail customer may pay; (3) the legal standard of conduct applicable to the broker-dealer; (4) financial professional compensation; and (5) any reportable disciplinary history the firm has.[105] Form CRS must be written in layman's terms and must not be longer than 2 pages. Further, Regulation Best Interest requires that broker-dealers complete Form CRS and file it electronically by June 30, 2020.[106]

C. What Regulation Best Interest Attempts to Achieve

Prior to June 5, 2019, when that SEC voted to adopt Regulation Best Interest, broker-dealers were subject to a suitability standard under FINRA Rule 2111.[107] The suitability standard required that "broker-dealers [and their] associated persons have reasonable basis to believe that a recommended transaction or investment strategy involving a security or securities [was] suitable for the customer, based on information obtained through reasonable [due] diligence . . . to ascertain the customer's investment profile."[108] In its decision to implement Regulation Best Interest, the SEC sought to enhance the quality and transparency of investors relationship with broker-dealers and investment advisers by

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101 *See* Soden and Vitello, *supra* note 11.

102 Reg BI Release, *supra* note 10, at 204-05.

103 *See* Adopting Release 34-86032 (June 5, 2019) 1, https:// www.sec.gov/rules/final/2019/34-86032.pdf [hereinafter Form CRS Release] (discussing Form CRS Relationship Summary and Amendments to Form ADV).

104 *Id.* at 5.

105 *Id.* at 1.

106 *Id.* at 28.

107 *See generally* Reg BI Release, *supra* note 10.; *see also* The SEC Approves Regulation Best Interest: The Broker-Dealer Standard of Conduct, KING & SPALDING (June 27, 2019), https://www.kslaw.com/news-and-insights/the-sec-approves-regulation-best-interest-the-broker-dealer-standard-of-conduct (explaining how the SEC approved Regulation Best Interest by a 3-1 vote, with Commissioner Robert Jackson dissenting).

108 FINRA Rule 2111 (Suitability) FAQ, available at https://www.finra.org/rules-guidance/key-topics/suitability/faq (last visited Feb. 24, 2021).

aligning the broker-dealer standard of conduct with a retail customer's reasonable expectations.[109]

Under Regulation Best Interest, broker-dealers and their associated persons are required to act in the best interest of the retail customer at the time an investment recommendation is made.[110] Broker-dealers are also required to address conflicts of interest by establishing procedures that are reasonably designed to identify and fairly disclose material facts about potential conflicts of interest, and in certain cases are prompted to mitigate or eliminate the conflict.[111] As a result, Regulation Best Interest is expected to enhance the efficiency of the recommendations broker-dealers make to retail customers since retail customers will be able to better analyze the recommendations received and make informed decisions.[112]

Yet, it is important to note that Regulation Best Interest specifically stated that it would not apply to investment advice provided to a retail customer by a dual-registrant when acting in the capacity of an investment adviser, even if the retail investor has a brokerage relationship with the dual-registrant.[113] Moreover, the regulation noted that a "facts and circumstances" test would be used to determine the capacity in which a dual-registrant makes a recommendation.[114] Specific factors would include: (1) the type of account; (2) how the account is described; (3) the type of compensation; and (4) the extent to which the dual-registrant made clear to the customer the capacity in which it was acting.[115] Thus, the regulation's limitation in its need to "assess the facts and circumstances" of an investment adviser's recommendation prior to determining whether the regulation's obligations apply leaves a significant gap in the standard of conduct of Broker-Dealers and Investment Advisers.

IV. ANALYSIS

A. The Notable Gaps Left by Regulation Best Interest

Though an investment adviser's fiduciary duty under the Advisers Act and a broker-dealer's duties under Regulation Best Interest sound very

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109 Reg BI Release, *supra* note 10 at 373.

110 *Id.*

111 *Id.* at 374.

112 *Id.* (noting that "[w]hile a suitable recommendation must take into account the elements of a retail customer's investment profile that make securities transactions or an investment strategy efficient for that particular retail customer, this requirement for suitability may not always lead to an efficient result for the retail customer").

113 Form CRS Release, *supra* note 103, at 67-69.

114 *Id.* at 71.

115 *See generally id.* at 67-78.

similar, gaps still exist between the two standards. According to the SEC's interpretation, a broker-dealer's standard of conduct obligations under Regulation Best Interest are "more prescriptive" than an Investment Adviser's "fiduciary duty obligations," which are principles-based.[116] Regulation Best Interest requires that a broker-dealer act in the best interest of its retail customers and "not place [its] own interests ahead" when making securities recommendations to its retail customers.[117] However, the general obligation of putting its retail customers' best interest first, can only be achieved by satisfying Regulation Best Interest's four prescriptive obligations: the "Disclosure Obligation," the "Care Obligation" the "Conflict of Interest Obligation," and the "Compliance Obligation."[118] On the other hand, the Investment Adviser Act is based on two principles: the "Duty of Care," and "Duty of Loyalty," which encompass the "overarching principle," that of acting in "the best interest" of a client.[119] Though similar, these two obligations can be interpreted quite differently, particularly because Regulation Best Interest does not include an explicit duty of loyalty.[120] Thus, the lines are blurred as to when a broker-dealer must make full and fair disclosures and provide account monitoring to a retail customer's account under Regulation Best Interest.

1. A Broker-Dealers' Duties Limited to Certain Forms of Investment Discretion

First, unlike the Advisers Act, Regulation Best Interest limits broker-dealers' duties to certain forms of investment discretion. For example, though the SEC believes that when a broker-dealer has discretion over a customer's account, the relationship has similar characteristics to that of an investment adviser under the Advisers Act, the SEC has taken the position that temporary discretionary authority can be considered "solely incidental" to the broker-dealer's business.[121] If a broker-dealer's advice is considered solely incidental, then it excluded from the definition of an

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116 Anna Young Black, Richard T. Choi, Ann Began Furman, Thomas C. Lauerman & Chip Lunde, *Unpacking the SEC's Regulation Best Interest Package*, THE NATIONAL REVIEW (2019), https://www.natlawreview.com/article/unpacking-sec-s-regulation-best-interest-package (last visit Dec. 27, 2019).

117 *Id.*

118 *Id.*

119 Fiduciary Interpretation, *supra* note 31, at 8.

120 Black et al., *supra* note 116 (noting that a duty of loyalty requires that an investment adviser provide frequent advice and monitoring that is consistent with the adviser-client relationship).

121 *See* Soden & Vitello, *supra* note 11.

"investment adviser" and does not require that a broker-dealer owe a fiduciary duty to its retail customer. [122]

Though the SEC will consider the totality of the circumstances to determine whether an advice was solely incidental, it has provided certain examples of temporary or limited investment discretion.[123] The SEC also requires that a broker-dealer not receive special compensation for such services. [124] Examples of temporary or limited investment advice include: (1) discretion as to the price or time at which to execute an order, (2) discretion, on an infrequent basis, to purchase or sell a security when a customer is unavailable, (3) discretion to purchase or sell securities to satisfy margin requirements, (4) discretion to purchase or sell a security limited by specific parameters established by the customer, among other things, (5) discretion as to cash management, and (6) discretion to purchase a bond with a specified credit rating and maturity date .[125] Consequently, if these situations apply, a broker-dealer will not owe a fiduciary duty to its retail customer. Hence, under Regulation Best Interest, instances likes the ones mentioned above limit a broker-dealer's legal obligations towards its retail customers.

2. No Duty to Provide Ongoing Advice and Monitoring

Second, under Regulation Best Interest, a broker-dealer's obligations do not extend beyond a particular recommendation since a broker-dealer's relationship with a retail customer is considered "mainly transactional" and "episodic."[126] Hence, Regulation Best Interest does not require a continuous duty to monitor a customer's account or impose a duty on self-directed or unsolicited orders.[127] This gap is particularly important because the duty to monitor a customer's account is an obligation of a fiduciary. Unlike, broker-dealers, investment advisers under the Advisers Act have a duty to provide advice and monitoring that is relatively extensive and consistent with the nature of the relationship. In doing so, investment

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122 *Id.*

123 Adopting Release IA-5249 (June 5, 2019) 17, https://www.sec.gov/rules/interp/2019/ ia-5249.pdf [hereinafter, Solely Incidental Interpretation Release].

124 *Id.* at 2.

125 *Id.* at 17.

126 *See* Reg BI Release, *supra* note 10, at 60.

127 Fiduciary Interpretation, *supra* note 31, at 10 (explaining that "the specific obligations that flow from the adviser's fiduciary duty depend upon what functions the adviser, as agent, has agreed to assume for the client, its principal. For example the obligation of an adviser providing comprehensive, discretionary advice in an ongoing relationship with a retail client . . . [is] different from the obligations of an adviser [providing advice] to a registered investment company or private fund where the contract defines the scope of the relationship").

advisers are required to review the performance of the account, make appropriate changes to the portfolio, and evaluate whether a program type continues to be in the best interest of the client.[128] Though a broker-dealer can agree to provide continuous monitoring of a customer's account, every review of the account without a recommendation to sell is considered an "implicit hold" recommendation.[129]

3. The Continued Existence of Broker-Dealer Compensation Model

Third, the sustained existence of a transaction-based (e.g., commission) compensation structure for broker-dealers under Regulation Best Interest, provides a continued incentive to a broker-dealer to seek its own compensation or other financial interest at the expense of the customer to whom it is making investment recommendations.[130] Though the Conflict of Interest Obligation requires that a broker give "conflict free" advice, the SEC does not require a broker-dealer to recommend the "single best" or "least costly" of all possible alternatives that might exist since more than one alternative might be in the "best interest" of the retail customer.[131] Further, under Regulation Best Interest, the SEC does not require an associated person of a broker-dealer to be "familiar with every product on a broker-dealer's platform."[132]

4. A Retail Customer's Lack of Investment Knowledge

Fourth, it is important to note that while Regulation Best Interest seeks to enhance the efficiency of the recommendations broker-dealers make to retail customers, many retail customers may not always have the investment knowledge or time to identify efficient strategies on their own.[133] In addition, investors may have limited access to information that would allow them to properly evaluate investment choices.[134] This is due to the fact that the efficiency of an investment recommendation depends on various factors, such as : (1) the menu of investment products and strategies that a broker-dealer and its associated persons consider when making an investment recommendation, (2) the return and costs of the recommended securities and strategies, (3) the associated person's

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128 *See* Barbara Black, *Brokers and Advisers – What's in a Name?*, 11 FORDHAM J. CORP. & FIN. L. 31, 38 (2005).
129 Reg BI Release, *supra* note 10, at 13.
130 *See id.* at 6-7.
131 Black et al., *supra* note 116.
132 *Id.*
133 Reg BI Release, *supra* note 10, at 378.
134 *Id.*

knowledge of those securities and strategies, (4) the retail customer's objectives and risk tolerance, and (5) the retail customer's financial constraints.[135] Thus, it is probable that Regulation Best Interest's efforts to provide more information to investors and raise the standard of conduct for broker-dealers, may fall short since retail customers will likely still follow a broker-dealer's advice without making an informed decision.[136]

B. Investor and State Response to Regulation Best Interest

Regulation Best Interest is expected to have important implications on broker-dealer and investment adviser 's recommendations to retail customers. Yet, its impact on consumer protection remains uncertain because the Regulation Best Interest "retains a muddled standard that exposes millions of Americans to the costs of conflicted advice."[137] As Commissioner Jackson, the sole dissenter to the rule explained, "[Regulation Best Interest] fails to require that investor interest come first, instead the adopted rule 'remains far too ambiguous about a question on which there should be no confusion.'"[138] As Jackson claimed, "The rule relies on a weak mix of measures that are unlikely to make a difference in improving the quality of advice investors receive from their brokers."[139]

Since the SEC's decision to adopt Regulation Best Interest, investor confusion and criticism has heightened. Seven states and the District of Columbia have sued the SEC and agency Chairman Jay Clayton to overturn Regulation Best Interest.[140] Attorney Generals for the states of New York, California, Connecticut, Delaware, Maine, New Mexico, and Oregon have filed lawsuits in the U.S. District Court for the Southern District of New York seeking to vacate Regulation Best Interest.[141] In the Complaint, states allege that the SEC exceeded its statutory authority in

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135 *Id.* at 380-381.

136 *See id.* at 378.

137 The Investment Management Practice, *SEC Adopts Rules & Interpretative Guidance Designed to Enhance and Clarify the Obligation of Financial Professionals*, PAUL HASTINGS., https://www.paulhastings.com/publications-items/details/?id=5ddb3c6d-2334-6428-811c-ff00004cbded.

138 *Id.*

139 Robert J. Jackson, Jr., *Statement on Final Rules Governing Investment Advice*, SEC.GOV (June 5, 2019), https://www.sec.gov/news/public-statement/statement-jackson-060519-iabd.

140 Greg Iacurci, *SEC Sued by Seven States to Kill Reg BI Investment-Advice Rule*, INVESTMENT NEWS (Sep. 10, 2019), https://www.investmentnews.com/article/20190910/FREE/190919999/sec-sued-by-seven-states-to-kill-reg-bi-investment-advice-rule.

141 *Id.* ("Massachusetts, New Jersey and Nevada have proposed rules to require a fiduciary standard of care for broker-dealers.").

violation of the Administrative Procedure Act.[142] The Administrative Procedure Act governs the process by which federal agencies such as the SEC, develop and issue regulations.[143] More specifically, plaintiffs allege that the SEC failed to implement a uniform standard of conduct.[144] In doing so, the SEC increased the risk of harm to retail investors because they cannot always differentiate the proper standard of conduct that applies when they get an investment recommendation from a broker-dealer vs. a registered investment adviser.[145]

Furthermore, a few weeks after Regulation Best Interest was adopted, the U.S House of Representative passed legislation prohibiting the SEC from implementing and enforcing Regulation Best Interest when a broker-dealer is making an investment recommendation to a retail customer.[146] In addition, various state legislatures and state securities regulators have taken steps to adopt a uniform fiduciary standard for broker-dealers and investment advisers at the local level.[147] So far, states like Massachusetts, Nevada, New Jersey, and New York have all taken steps to require greater levels of disclosure or have sought to impose a uniform fiduciary standard on all investment professionals.[148]

Yet, one important issue left unaddressed by the SEC is whether state fiduciary rules would preempt the federally promulgated Regulation Best Interest.[149] In its passing of Regulation Best Interest, the SEC did not take a position regarding preemption and chose to defer that issue to the judicial branch.[150] The SEC stated that "The preemptive effect of Regulation Best

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142 *Id.*

143 *See* Promoting the Rule of Law Through Transparency and Fairness in Civil Administrative Enforcement and Adjudication, 84 Fed. Reg. 55239 (Oct. 19, 2019) (explaining that the APA includes requirements for publishing notices of proposed and final rulemakings in the Federal Register and provides opportunities for the public to comment on notices of proposed rulemaking).

144 Iacuri, *supra* note 140.

145 *Id.* (explaining that investor confusion is caused by the fact that the rule makes it easier for brokers to market themselves as "trusted advisers" while still being able to give conflicted advice).

146 Mirella DeRose et al., *Regulation Best Interest: Updates and Developments*, JD SUPRA (Nov. 1, 2019), https://www.jdsupra.com/legalnews/regulation-best-interest-updates-and-97361/ (explaining that the legislation passed is a funding bill for various federal agencies, including the SEC. The bill includes an amendment that would prohibit regulators from moving forward with the controversial Regulation Best Interest.).

147 *Id.*

148 *Id.* (clarifying that the fiduciary standards these states seek to impose include requiring annual table of fees and services to advisory clients in order to increase transparency for retail investors and imposing duties of care and loyalty to broker-dealers).

149 *See id.*

150 Daniel Nathan, Daniel Streim, Nicholas Peterson & Trace Schmeltz, *The SEC's Regulation Best Interest: How to Prepare for the New Standard of Conduct*, A.B.A. (June 19, 2019),

Interest on any state law governing the relationship between regulated entities and their customers will be determined in future judicial proceedings based on the specific language of that state law."[151] Thus, much remains unknown as to how Regulation Best Interest will be implemented and enforced by states and self-regulatory organizations like FINRA.

C. Thinking Ahead: Reasonable Solutions to Regulation Best Interest

While the fate of Regulation Best Interest is unclear, the potential June 2020 compliance deadline is quickly approaching, and investor confusion persists as to the different standards of care between broker- dealers and investment advisers. Though the SEC's new rule attempts to enhance the broker-dealer standard of conduct by aligning a broker-dealer's duties with that of a retail customer's reasonable expectations, the rule clearly lacks enforcement and teeth to hold broker-dealers to a best interest standard. Particularly because the rule fails to expand on consumer protections and add clarity to the broker vs. advisor roles.

Yet, in the midst of the grey areas left by the Regulation Best Interest, firms should work diligently together to achieve a successful compliance framework.[152] By developing policies and procedures that provide a higher standard of care to their investors, firms can not only educate their investors on the differences between broker-dealers and investment advisers responsibilities but can also come one step closer towards satisfying a regulator's compliance expectations.[153] In doing so, firms are

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https://www.americanbar.org/groups/litigation/committees/securities/practice/2019/how-to-prepare-for-new-standard-of-conduct-regulation-best-interest/ (advising that states that have extended fiduciary obligations to broker-dealers should observe the higher state standard until the judiciary branch determines whether Regulation Best Interest displaces those state laws).

151 Reg BI Release, *supra* note 10, at 515 n. 1163 (explaining that there are unknown factors which keep the SEC from deciding whether Regulation Best Interest should preempt state law such as: (1) the final language in any proposed state legislation; (2) whether the language would constitute the type of law, rule, or regulation that is expressly preempted by the securities law; and (3) whether, if there was any preemption, that preclusion of state law would have any positive or negative effects on investors when compared with the effects of Regulation Best Interest).

152 Ghillaine Reid and Kurt Wolfe, *Firms Should Stay Course Amid New Broker Standard Suits*, LAW360 (Sep. 25, 2019, 3:12 PM), https://advance.lexis.com/api/permalink/92c04248-9a52-4171-8fa7-2ef327a3bf63/?context=1000516 (advising that for firms who compliance efforts are underway should stay in the course of compliance regardless of the current lawsuits seeking to set the regulation aside).

153 *Id.* (explaining that while the SEC and states have not agreed to a uniform fiduciary standard, by designing and implementing policies and procedures that comply with the

likely to conform their conduct as closely as possible to the Regulation Best Interest standard.[154]

Moreover, while the SEC refused to provide further guidance as to what constitutes "best interest," a more robust financial outreach campaign initiated by FINRA might be a viable solution towards addressing the gaps left by Regulation Best Interest.[155] For instance, the campaign could provide more details as to when a broker-dealer's advice is considered "solely incidental" to its business. Though in such circumstances the SEC mentioned it would apply a totality of the circumstances test, having a more comprehensive explanation as to what the limits are, can help investors decipher when a fiduciary duty is owed to them. The campaign can also help educate investors as to when and under what circumstances a broker-dealer is required to monitor an account. Doing so would help close the gap that currently exists in retail investors' expectations and what a dual registrant must do when providing investment advice.

Further, while the SEC has failed to clarify whether state fiduciary rules would preempt the federally promulgated Regulation Best Interest, a workable solution might be for states to follow state promulgated fiduciary standards since they impose a higher ethical duty for broker-dealers when compared to Regulation Best Interest.[156] If states with fiduciary rules follow them, they will certainly meet the four obligation under Regulation Best Interest which include: (i) Disclosure Obligation, (ii) Care Obligation, (iii) Conflict of Interest Obligation, and (iv) Compliance Obligation. Consequently, it is unlikely that broker-dealers in such states will encounter a problem for choosing to put their state fiduciary rules first. Likewise, another feasible solution might be for more states to enforce a state fiduciary rule. Doing so would help narrow the gap that exists in retail customers' knowledge as to the roles of broker-dealers and investment advisers. Many states such as Massachusetts, Nevada, New Jersey, and New York have already done so at a local level and are one step closer towards achieving a uniform fiduciary standard.[157]

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most restrictive regulatory requirements, firms can establish a single internal standard that applies to all securities transactions where the broker-dealer or investment adviser recommends securities or investment strategies to retail investors).

154 *Id.*

155 Daniel Nathan, Daniel Streim, Nicholas Peterson & Trace Schmeltz, *supra* note 150 (clarifying that in its adoption of Regulation Best Interest, the SEC largely left the term "best interest undefined since it solely explained the four obligations under the rule).

156 *See* Ross Jordan, *Thinking Before Rulemaking: Why The SEC Should Think Twice Before Imposing a Uniform Fiduciary Standard on Broker-Dealers and Investment Advisers*, 50 U. LOUISVILLE L. REV. 491, 505 (2012).

157 DeRose et al., supra *note* 146.

V. CONCLUSION

The problem of conflicting standards for broker-dealers and investment advisers has troubled the financial services industry for way too long. For years, main street investors have been left unprotected and confused about the different legal obligations and standard of conduct broker-dealers and investment advisers carry when making investment recommendations. As financial services firms turned to a dually registration model, investor confusion widened. Dual registration allowed firms to offer both advisory and broker-dealer services to investors while their employees adhered to different standards of conduct based on the services provided. Accordingly, the dually registered model further blurred the lines that existed between investment advisers and broker-dealer responsibilities.

In its decision to pass Regulation Best Interest, the SEC sought to finally put investors first. The Commission adopted a package of rules and interpretations that would enhance the quality and transparency of retail investors' relationship with broker-dealers and investment advisers. The regulation brought legal requirements and mandated disclosures for broker-dealers and investment advisers in line with reasonable investor expectations. By enhancing the current suitability standard under FINRA Rule 2111, the SEC hoped to improve the efficiency of the recommendations broker-dealers made to retail customers. Yet, the SEC's initiative to choose Main Street over Wall Street fell short.

Though Regulation Best Interest requires that a broker-dealer must act in the retail customer's best interest and cannot place its interest ahead of its customers, its impact on investor protection remains uncertain. While broker-dealers have until June 30, 2020, to comply, the adopted rule remains far too ambiguous and has increased investor confusion. In its adoption of Regulation Best Interest did not explain how a broker-dealer must go about complying with the rule. The rule also did not address whether Regulation Best Interest would preempt state fiduciary rules. Since many states have already extended fiduciary obligations to broker-dealers, whether Regulation Best Interest will displace those state laws is likely to be determined through litigation.

Consequently, since Regulation Best Interest's compliance deadline is quickly approaching, possible feasible solutions include: (i) firms working together to achieve a compliance framework by developing policies and procedures that achieve a higher standard of care for broker-dealer; (ii) FINRA providing further guidance to firms and investors as to what constitutes "best interest" and "solely incidental advice" by providing example scenarios and details on the rule's limitations; (iii) states choosing to follow their state fiduciary rules despite the Regulation Best Interest;

and (iv) promoting other states to implement local/ state fiduciary rules. Thus, by implementing the mentioned solutions, states, firm, and regulators could once and for all help narrow the gap that currently exists between broker-dealer responsibilities and retail customers' reasonable expectations.