



SEC Regulation Best Interest: Examination preparedness for 2021

Division of Examinations staff intends to expand the scope of Regulation Best Interest examinations in 2021 and place additional focus on whether broker-dealers have written policies and procedures and systems in place.

After Regulation Best Interest's (Reg BI) June 30, 2020 compliance date, the Division of Examinations (Division) launched an initial examination initiative to assess the Reg BI implementation efforts of broker-dealers.^{1,2} Having completed this initial examination initiative, the Division has now moved into a new phase of examinations (starting in January 2021), inclusive of transaction-level testing and focused on whether broker-dealers have implemented written policies and procedures for Reg BI compliance, including systems and processes that go beyond the suitability standard and meet the higher standard of Reg BI.³

[Reg BI](#) requires broker-dealers and their financial professionals to act in the best interest of retail customers when recommending securities transactions or investment strategies involving securities.⁴ Reg BI covers recommendations regarding not only securities but also account types, rollovers, exchanges, and holds. The [regulation](#) requires broker-dealers and their financial professionals to not place their own financial or other interests ahead of the interests of the retail customer.⁵ This general obligation can be satisfied only if the broker-dealer also complies with four component obligations, namely the Disclosure, Care, Conflict of Interest, and Compliance Obligations. In addition to Reg BI, the SEC also adopted new disclosure requirements under the [Form CRS Relationship Summary](#) directing registered investment advisers and broker-dealers to provide a written relationship summary to each retail investor.⁶

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On December 21, 2020, the Division released a public statement highlighting upcoming Reg BI examinations and topics for which the Division Staff plans to conduct transaction-level testing in its examinations.⁷ Components of Reg BI that are areas of regulatory focus include:

Reg BI Obligation	Areas of Regulatory Focus	Deloitte's Point of View
Care	<ul style="list-style-type: none"> • Evaluation of how firms have considered costs in making recommendations, which may include: • What information is available to firm personnel to identify relevant costs; • How any such information has been used; and, • Any documentation of the consideration of costs. 	<p>Firms should be able to evidence how costs have been considered in the recommendation process and illustrate how this cost consideration is documented. This may involve demonstrating how the firm has enhanced financial advisor and supervisory tools and processes to enable consideration of cost in the recommendation process.</p>
Care	<ul style="list-style-type: none"> • Evaluation of the processes firm personnel have used to make recommendations to new customers(e.g., rollovers, account type recommendations), which may include: • What information was gathered from new customers • What disclosures were made at the time of recommendation; • How alternatives were considered; and, • What documentation was retained. 	<p>Firms should expect to demonstrate the processes and systems that they use for compliance with the Care Obligation when making recommendations to new customers. This may include what information was gathered from customers and the analysis of the customer's investment profile; what disclosures were made (and how); and how reasonably available alternatives (RAA) were considered. Firms should also be reviewing their recordkeeping related to Reg BI to evaluate if they are keeping all required documentation under the Regulation.</p>
Care	<p>Evaluation of the processes firm personnel have used to recommend complex products, including what information was available and used to consider RAA.</p>	<p>Firms should expect to show why complex products were appropriate, as well as how the rationale for the recommendation is evidenced (potentially including documentation of the rationale). Firm should also expect to show how RAAs were considered. Firms should also be reviewing their processes and training regarding complex product recommendations.</p>
Conflict of interest	<p>Evaluation of the processes that firms have used to identify and address conflicts related to recommendations.</p>	<p>Firms should expect to demonstrate to the Division how they identify and address conflicts (related to recommendations) and how their process has evolved for Reg BI compliance. This would generally include demonstrating the effectiveness of conflict policies and procedures, a conflicts register and regular reviews of compensation programs.</p>
Compliance	<p>Continued evaluation of firm policies and procedures, including evaluating specific firm processes for compliance with the Regulation, and alterations to firm product offerings, including the removal of higher cost products when lower cost products are available.</p>	<p>Firms should expect to show the Division how their product due diligence policies and procedures have evolved since the Reg BI compliance date. Firms should also expect to be able to explain the compliance rationale for changes they may have made to their product offerings.</p>

In addition to the examination topics listed above, the Division encouraged firms to continue evaluating their processes and “consider whether initial programs adopted are reasonably designed, in practice, to achieve compliance with Reg BI.”

As firms prepare for the Division's examination initiative covering Reg BI, we would encourage them to plan ahead and proactively consider the Division's focus areas.

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Endnotes

1. Securities and Exchange Commission (SEC), "[Regulation Best Interest: The Broker-Dealer Standard of Conduct](#)," accessed January 22, 2021.
2. SEC, "[Examinations that Focus on Compliance with Regulation Best Interest](#)," accessed January 22, 2021.
3. SEC, "[Statement on Recent and Upcoming Regulation Best Interest Examinations from the SEC Division of Examinations](#)," accessed January 22, 2021.
4. Deloitte, "[New Rule Recasts Broker-Dealer Retail Sales Practices](#)," accessed January 22, 2021.
5. Deloitte, "[Investment Firms Can Leverage Regulatory Relief Now](#)," accessed January 22, 2021.
6. SEC, "[Form CRS Relationship Summary: Amendments to Form ADV](#)," accessed January 22, 2021.
7. SEC, "[Statement on Recent and Upcoming Regulation Best Interest Examinations from the SEC Division of Examinations](#)," accessed January 22, 2021.



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