

Alert

SEC Proposes Investment Adviser Standards of Conduct and Enhanced Regulation

April 19, 2018

On April 18, 2018, the SEC proposed a set of rules and interpretations addressing the standards of care applicable to investment advisers and broker-dealers.¹ Two of the proposals apply only to retail investors: “Regulation Best Interest” — which would impose a standard of care on broker-dealers — and proposed Form CRS — which would require SEC-registered investment advisers (“RIAs”) and broker-dealers to provide a “relationship summary” to retail clients.

The third proposal, however, applies to investment advisers more broadly and also includes a request for comment on enhancing investment adviser regulation. The “Proposed Commission Interpretation Regarding Standard of Conduct for Investment Advisers; Request for Comment on Enhancing Investment Adviser Regulation” includes four separate sections:

1. A proposed interpretation of an investment adviser’s fiduciary duties under federal law;
2. A request for comment on federal licensing and continuing education requirements for personnel of RIAs;
3. A request for comment on the provision of account statements to RIA clients; and
4. A request for comment on financial responsibility requirements.

The broadest aspect of this proposal is the proposed interpretation of an adviser’s fiduciary duty, which is focused on fiduciary duty as a general concept and is not limited to the duties owed to a single category of clients (e.g., retail clients). The SEC proposal identifies and explores several subsidiary duties that are subsumed within an overall fiduciary duty:

- The duty of care, which includes:
 - A duty to provide advice that is in the client’s best interest;
 - A duty to seek best execution; and
 - A duty to act and to provide advice and monitoring over the course of the relationship.
- The duty of loyalty.

While the proposed fiduciary duty interpretation reiterates general standards well-established in prior precedent, it also includes a discussion of conflicts of interest that reflects more recent SEC staff perspectives. For example, the proposed interpretation indicates that “an adviser disclosing that it ‘may’ have a conflict is not adequate disclosure when the conflict actually exists.”

¹ SEC proposal available [here](#) and SEC press release available [here](#).

In its request for comment with respect to federal licensing and continuing education, the SEC focuses on “investment adviser representatives” — typically, a supervised person of an RIA who has more than five clients who are natural persons but not qualified clients and more than 10 percent of whose clients are natural persons but not qualified clients. However, while it is focused on investment adviser representatives, the request for comments also asks whether other advisory personnel should be included in any federal licensing and continuing education requirements, including all supervised persons or any individuals for whom an adviser must deliver a Form ADV Part 2B brochure supplement. This additional element of the SEC proposal, on its face, is not limited to advisers with retail clients.

The request for comment on the provision of account statements is more narrowly focused on retail clients, but it also more generally asks about the costs and benefits of requiring the provision of account statements specifying dollar amounts of fees and expenses.

Finally, the request for comments as to financial responsibility asks whether RIAs should be subject to net capital rules or other financial responsibility requirements, such as a fidelity bond, to ensure they can meet their financial obligations. The request also asks whether registered investment advisers should “be required to obtain annual audits of their own financials and to provide such information on Form ADV.”

Comments on the proposals will be due within 90 days of publication in the Federal Register, and we look forward to discussing these issues with our clients as we prepare comments for submission.

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If you have any questions concerning this *Alert*, please contact your attorney at Schulte Roth & Zabel or one of the authors.

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