

**Staff Bulletin¹: Standards of Conduct for Broker-Dealers and
Investment Advisers
Care Obligations**

Background: The following is a staff bulletin styled as questions and answers reiterating the standards of conduct for broker-dealers and investment advisers in addressing their care obligations when they are providing investment advice and recommendations to retail investors.² Accordingly, this bulletin is focused primarily on the Care Obligation of Regulation Best Interest (“Reg BI”) for broker-dealers and the duty of care enforced under the Investment Advisers Act of 1940 (the “IA fiduciary standard”) for investment advisers (together, “care obligations”).

Both Reg BI for broker-dealers and the IA fiduciary standard for investment advisers are drawn from key fiduciary principles that include an obligation to act in the retail investor’s best interest and not to place their own interests ahead of the investor’s interest.³ Complying with their care obligations is an important aspect of how firms and financial professionals form a reasonable belief that their investment advice and recommendations are in the retail investor’s best interest.⁴ Although the specific application of Reg BI and the IA fiduciary standard may differ in some

¹ This staff bulletin and other staff documents (including those cited herein) represent the views of the staff of the Securities and Exchange Commission (“Commission”) and are not a rule, regulation, or statement of the Commission. The Commission has neither approved nor disapproved the content of these documents and, like all staff statements, they have no legal force or effect, do not alter or amend applicable law, and create no new or additional obligations for any person.

² For purposes of this staff bulletin, we use the term “retail investor” to mean any person who qualifies as a “retail customer” as defined in Exchange Act rule 15l-1(b)(1), or a natural person client of an investment adviser.

³ This staff bulletin is expressly limited in scope to the duties owed by a broker-dealer or investment adviser, including their financial professionals, when providing recommendations or investment advice to retail investors. We do not address, for example, other care obligations of investment advisers, such as the duty to seek best execution of a client’s transactions where the adviser has the responsibility to select broker-dealers to execute client trades, the duty to provide advice and monitoring over the course of the client relationship, or an adviser’s care obligations when providing impersonal advice. [Commission Interpretation Regarding Standard of Conduct for Investment Advisers](#), Investment Advisers Act Release No. 5248, 84 FR 33669, 33669 n.7, 33672 (June 5, 2019) (“Fiduciary Interpretation”). Although an investment adviser’s fiduciary duty applies to all advisory clients (whether retail investors or otherwise) and applies to the entire advisory relationship, the adviser’s duties when providing advice to retail investors is the focus of this bulletin. Reg BI’s obligation to act in the best interest of the retail customer, however, applies only when making a recommendation of a security or investment strategy involving securities (including account recommendations) to a retail customer for personal, family, or household use. Exchange Act rule 15l-1; [Regulation Best Interest: The Broker-Dealer Standard of Conduct](#), Exchange Act Release No. 86031, 84 FR 33318, 33320-21 (June 5, 2019) (“Reg BI Adopting Release”). Although this obligation is comprised of four component obligations—Care, Disclosure, Conflict of Interest, and Compliance—except where expressly noted, this bulletin is focused on the Care Obligation only.

⁴ An investment adviser’s fiduciary duty under the Investment Advisers Act of 1940 (“Advisers Act”) comprises a duty of care and a duty of loyalty, and the adviser’s obligation to act in the best interest of its client is an overarching principle that encompasses both duties. Fiduciary Interpretation, *supra* note 3, at 33671. Reg BI’s obligation to act in the retail customer’s best interest is satisfied only by complying with each of the rule’s four component obligations: Disclosure, Care, Conflict of Interest, and Compliance. Exchange Act rule 15l-1; Reg BI Adopting Release, *supra* note 3, at 33320-21.

respects and be triggered at different times, in the staff’s view, they generally yield substantially similar results in terms of the ultimate responsibilities owed to retail investors.

In the context of providing investment advice and recommendations to retail investors, the care obligations generally include three overarching and intersecting components. As discussed in more detail in the following questions and answers, these components are:

- Understanding the potential risks, rewards, and costs associated with a product, investment strategy, account type, or series of transactions (the “investment or investment strategy”);⁵
- Having a reasonable understanding of the specific retail investor’s investment profile, which generally includes the retail investor’s financial situation (including current income) and needs; investments; assets and debts; marital status; tax status; age; investment time horizon; liquidity needs; risk tolerance; investment experience; investment objectives and financial goals; and any other information the retail investor may disclose in connection with the recommendation or advice;⁶ and
- Based on the understanding of the first two elements, as well as, in the staff’s view, a consideration of reasonably available alternatives,⁷ having a reasonable basis to conclude that the recommendation or advice provided is in the retail investor’s best interest.⁸

⁵ Reg BI’s Care Obligation requires broker-dealers and their financial professionals to have a reasonable basis to believe that a recommendation of a securities transaction or investment strategy involving securities (including account recommendations) could be in the best interest of at least some retail investors. Exchange Act rule 15l-1(a)(2)(ii)(A). An investment adviser’s duty of care requires conducting a reasonable investigation into the investment sufficient not to base the advice on materially inaccurate or incomplete information. Fiduciary Interpretation, *supra* note 3, at 33672, 33674.

⁶ Exchange Act rule 15l-1(a)(2)(ii)(B)-(C); Reg BI Adopting Release, *supra* note 3, at 33379, 33492; Fiduciary Interpretation, *supra* note 3, at 33673; *see also* Staff Bulletin: Standards of Conduct for Broker-Dealers and Investment Advisers Account Recommendations for Retail Investors, available at <https://www.sec.gov/tm/iabd-staff-bulletin> (“Staff Bulletin on Account Recommendations”) (listing examples of investor characteristics to consider to have a reasonable basis to believe the account recommendation is in the retail investor’s best interest).

⁷ *See* Reg BI Adopting Release, *supra* note 3, at 33381 (stating that considering reasonably available alternatives is an “inherent aspect of making a ‘best interest’ recommendation, and is a key enhancement over [then-] existing broker-dealer suitability obligations,” explaining “this concept has been applied in the context of guidance regarding suitability and heightened supervision of complex products”); *see also* *O.N. Investment Management Company*, Investment Advisers Act Release No. 5944 (Jan. 11, 2022) (investment adviser violated its duty of care obligations when it “failed to consider alternative, lower-fee . . . money market funds” that were readily available to the adviser when it purchased other money market funds for its clients that generally resulted in revenue sharing being paid to the adviser or its affiliate), available at <https://www.sec.gov/litigation/admin/2022/ia-5944.pdf> (settled action); *Rothschild Investment Corp.*, Investment Advisers Act Release No. 5860 (Sept. 13, 2021) (adviser violated its duty of care obligations when it recommended money market funds that resulted in revenue sharing but “failed to consider alternative funds with similar strategies” that were available to the adviser and which had lower costs and higher yields), available at <https://www.sec.gov/litigation/admin/2021/34-92951.pdf> (settled action); *Cowen Prime Advisors, LLC*, Investment Advisers Act Release No. 5874 (Sept. 27, 2021) (same), available at <https://www.sec.gov/litigation/admin/2021/ia-5874.pdf> (settled action).

⁸ Exchange Act rule 15l-1(a)(2)(ii)(B)-(C). Under Reg BI, the Care Obligation also applies to a series of

Whether a recommendation or advice satisfies the care obligations is an objective evaluation, turning on the facts and circumstances of the particular recommendation or advice and the investment profile of the particular retail investor at the time the recommendation is made or when the advice is provided.⁹ When adopting and implementing reasonably designed policies and procedures regarding their care obligations, broker-dealers and investment advisers should tailor those policies and procedures, taking into consideration their particular business models and relationships with retail investors.¹⁰

This staff bulletin is designed to assist firms and their financial professionals with meeting their care obligations such that they comply with their obligations to provide advice and

recommended transactions. Exchange Act rule 15l-1(a)(2)(ii)(C) (requiring broker-dealers and their financial professionals to have “a 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 and is in the retail customer’s best interest when taken together in light of the retail customer’s investment profile and does not place the financial or other interest of the broker, dealer, or such natural person making the series of recommendations ahead of the interest of the retail customer.”); *see also* Reg BI Adopting Release, *supra* note 3, at 33384. An investment adviser’s duty to provide advice that is in the best interest of the client includes the duty to provide advice that is suitable for the client. Fiduciary Interpretation, *supra* note 3, at 33672. Additionally, “an investment adviser must have a reasonable belief that the advice it provides is in the best interest of the client based on the client’s objectives.” *Id.* at 33673.

⁹ Reg BI requires broker-dealers and their financial professionals to act in the best interest of retail investors *at the time* the recommendation is made. *See* Exchange Act rule 15l-1(a)(1) (emphasis added). *See also* Reg BI Adopting Release, *supra* note 3, at 33326 (noting that determining whether a broker-dealer’s recommendation satisfies the Care Obligation will be an objective evaluation turning on the facts and circumstances of the particular recommendation and the particular retail customer); Fiduciary Interpretation, *supra* note 3, at 33672-33673 (stating that in order to provide investment advice that is in the best interest of the client, an investment adviser must have a reasonable understanding of the client’s objectives based on the specific facts and circumstances). The duty of care for investment advisers includes, among other things, the duty to provide advice and monitoring over the course of the relationship. *Id.* at 33672.

¹⁰ Reg BI’s Compliance Obligation requires broker-dealers to establish, maintain and enforce written policies and procedures reasonably designed to achieve compliance with Reg BI. *See* Exchange Act rule 15l-1(a)(iv); *also* Reg BI Adopting Release, *supra* note 3, at 33386 (stating “broker-dealers should have flexibility to tailor their policies and procedures to their particular business model, focusing on specific areas of their business that pose the greatest risk of noncompliance and greatest risk of potential harm to retail customers as opposed to a detailed review of each recommendation.”). A broker-dealer must have policies and procedures reasonably designed to comply with Reg BI and when adopting those policies and procedures should consider the nature of that firm’s operations and how to design such policies and procedures to prevent violations from occurring, detect violations that have occurred, and to correct promptly any violations that have occurred. *See* Exchange Act rule 15l-1(a)(iv); *see also* Reg BI Adopting Release, *supra* note 3, at 33397 (stating “[a] firm’s compliance policies and procedures should be reasonably designed to address and be proportionate to the scope, size, and risks associated with the operations of the firm and the types of business in which the firm engages.”). Rule 206(4)-7 under the Advisers Act requires investment advisers to adopt and implement written policies and procedures reasonably designed to prevent violations of the Advisers Act, which include preventing breaches of the fiduciary standard in violation of Section 206 of the Advisers Act. “Each adviser should adopt policies and procedures that take into consideration the nature of that firm’s operations” and “should first identify conflicts and other compliance factors creating risk exposure for the firm and its clients in light of the firm’s particular operations, and then design policies and procedures that address those risks.” Compliance Programs of Investment Companies and Investment Advisers, Investment Advisers Act Release No. 2204 (Dec. 17, 2003), 68 FR 74714, 74716 (Dec. 24, 2003) (footnotes omitted), *available at* <https://www.govinfo.gov/content/pkg/FR-2003-12-24/pdf/03-31544.pdf>.

recommendations in the best interest of retail investors. The bulletin should be read in conjunction with, among other sources, Reg BI and the specific Commission releases discussing Reg BI and the IA fiduciary standard.¹¹ In addition, the staff has made available other resources, including a variety of staff FAQs addressing compliance with Form CRS, Reg BI and the IA fiduciary standard, risk alerts, and other statements highlighting relevant compliance practices and staff observations.¹²

Understanding the Investment or Investment Strategy

1. Do I need to understand the investment or investment strategy I am advising on or recommending?

Yes. Under the care obligations, investment advisers, broker-dealers, and their financial professionals need to understand the investments and investment strategies on which they provide advice and recommendations before advising on or recommending them to retail investors.¹³ This includes developing a sufficient understanding of the potential risks, rewards, and costs of the investment or investment strategy to have a reasonable basis to believe that the recommendation or advice could be in a retail investor's best interest.¹⁴ Without this understanding, firms and their financial professionals cannot have a reasonable basis to believe that their recommendation or advice aligns with a retail investor's investment profile in a way

¹¹ See Reg BI Adopting Release, *supra* note 3; Fiduciary Interpretation, *supra* note 3.

¹² See SEC Spotlight, Regulation Best Interest, Form CRS and Related Interpretations, available at <https://www.sec.gov/regulation-best-interest>. The staff of the Divisions of Trading and Markets and Investment Management have previously published staff bulletins that discuss examples of practices that can assist firms in meeting their obligations relating to account type recommendations and conflicts of interest. See Staff Bulletin on Account Recommendations, *supra* note 6; Staff Bulletin: Standards of Conduct for Broker-Dealers and Investment Advisers Conflicts of Interest, available at <https://www.sec.gov/tm/iabd-staff-bulletin-conflicts-interest>.

¹³ See Reg BI Adopting Release, *supra* note 3, at 33376; Fiduciary Interpretation, *supra* note 3, at 33674.

¹⁴ See Exchange Act rule 15l-1(a)(2)(ii)(A); Reg BI Adopting Release, *supra* note 3, at 33376-77; Fiduciary Interpretation, *supra* note 3, at 33674 (“A reasonable belief that investment advice is in the best interest of a client also requires that an adviser conduct a reasonable investigation into the investment sufficient not to base its advice on materially inaccurate or incomplete information. . . . 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 Commission has brought enforcement actions when investment adviser representatives lacked a reasonable understanding of an investment’s risks and key attributes. See, e.g., *Frontier Wealth Management, LLC and Shawn Sokolosky*, Investment Advisers Act Release No. 5847 (September 3, 2021) (settled action) (Sokolosky made unsuitable recommendations to clients in part because he “did not adequately understand the Feeder Fund’s trading strategy, underlying investments, and risks.”); cf. *UBS Financial Services, Inc.*, Investment Advisers Act Release No. 6060 (June 29, 2022) (settled action) (UBS violated § 206(2) where its advisory representatives lacked “a reasonable belief that the advice they provided . . . was in the best interest of their clients” because the representatives did not sufficiently “understand the significant downside risk” of the complex options strategy they recommended).

that satisfies their obligations to make a recommendation or provide advice that is in the specific investor's best interest.¹⁵

2. What factors should firms and financial professionals consider to develop such an understanding of an investment or investment strategy?

As part of their care obligations, broker-dealers, investment advisers, and their financial professionals must develop an understanding of the investment or investment strategy to form a reasonable basis for making recommendations or providing advice to retail investors. What is reasonable depends on the facts and circumstances, and the specific terms and features that a firm or financial professional would need to understand about the investment or investment strategy under consideration will necessarily vary.¹⁶

The following is a non-exhaustive list that the staff believes are some of the important factors that may be relevant to consider as part of evaluating the potential risks, rewards, and costs of an investment or investment strategy:

- the objectives of the investment or investment strategy (such as whether it is designed to provide income, principal protection, growth, or exposure to a specific market sector, or is designed to be held for a long or short term);
- the initial and ongoing costs of the investment or investment strategy (such as direct and indirect costs, as well as potential costs, such as redemption fees);
- the investment or investment strategy's key characteristics and risks (such as liquidity or volatility), or other features that may impact the investment (e.g., margin call terms or early repayment of debt underlying a securitized product);

¹⁵ It will be generally necessary for an adviser to a retail investor to update the investor's investment profile in order to maintain a reasonable understanding of the investor's objectives and adjust the advice to reflect any changed circumstances; such updating would not be needed with one-time investment advice. Fiduciary Interpretation, *supra* note 3 at 33673 and n.37. In addition, an adviser may provide comprehensive, discretionary advice in an ongoing relationship with a retail investor that includes obligations such as monitoring and periodic adjustments of the client's portfolio. *Id.* at 33671-33672. While broker-dealers generally are not required to monitor accounts, where a broker-dealer agrees to provide the retail customer with specified account monitoring services, such an agreement will result in buy, sell or hold recommendations subject to Reg BI, even when the recommendation to hold is implicit at the time the agreed-upon monitoring occurs. *See* Reg BI Adopting Release, *supra* note 3, at 33325, 33340-41.

¹⁶ *See* Reg BI Adopting Release, *supra* note 3, at 33376. Broker-dealers also have a duty to investigate the truth of their representations pursuant to the general antifraud provisions of the federal securities laws. *See, e.g., Hanly v. SEC*, 415 F.2d 589, 596 (2d Cir.1969) ("A broker . . . has a duty to investigate the truth of the representations he makes to clients, because, by virtue of his title, clients are entitled to presume that the representations made were the result of reasonable investigation."). Fiduciary Interpretation, *supra* note 3, at 33674 (footnotes omitted) ("A reasonable belief that investment advice is in the best interest of a client also requires that an adviser conduct a reasonable investigation into the investment sufficient not to base its advice on materially inaccurate or incomplete information. We have taken enforcement action where an investment adviser did not independently or reasonably investigate securities before recommending them to clients.").

- the investment or investment strategy’s likely performance in a variety of market and economic conditions;
- the expected returns, expected payout rates, and potential losses of the investment or investment strategy;
- any special or unusual features of the investment or investment strategy (such as tax advantages or guaranteed payments); and
- the role of the investment or investment strategy within the context of the retail investor’s actual or anticipated investment portfolio.¹⁷

Where there is an ongoing monitoring obligation, the reasonable investigation will require continued analysis after purchase of the investment and over the course of the relationship.¹⁸

3. Are costs always a relevant factor to consider when recommending or providing advice on investments or investment strategies?

Yes. While costs should not be the only consideration, and a firm or financial professional cannot satisfy its obligations simply by recommending the lowest cost option, the firm and financial professional must always consider cost as a factor when providing a recommendation or advice to a retail investor.¹⁹ In the staff’s view, the firm and financial professional should consider the total potential costs when evaluating whether the recommendation or advice is in a retail investor’s best interest, including direct and indirect costs that could be borne by the retail investor.²⁰ For example, when determining whether an investment or investment strategy is in

¹⁷ See generally Reg BI Adopting Release, *supra* note 3, at 33376; Fiduciary Interpretation, *supra* note 3, at 33674; Staff Bulletin on Account Recommendations, *supra* note 6 (discussing examples of factors to consider when making account recommendations).

¹⁸ See Fiduciary Interpretation, *supra* note 3, at 33672; Reg BI Adopting Release, *supra* note 3, at 33325, 33340-41.

¹⁹ See Exchange Act rule 15l-1(a)(2)(ii) (requiring consideration of cost under Reg BI’s Care Obligation); see also Fiduciary Interpretation, *supra* note 3, at 33674 (cost would generally be one of many important factors to consider when determining if a security or investment strategy is in the client’s best interest). See also Staff Bulletin on Account Recommendations, *supra* note 6 (stating “you must always consider cost as a factor when making an account recommendation.”). The Commission has brought enforcement actions against investment advisers for recommending higher-cost products, which generally paid revenue sharing to the adviser or the adviser’s affiliate to clients when similar, lower-cost products were available. See In the Matter of Centaurus Financial, Inc., Investment Advisers Act Release No. 5744 (June 2, 2021), available at <https://www.sec.gov/litigation/admin/2021/34-92095.pdf> (settled action); In the Matter of Cowen Prime Advisors, LLC, Investment Advisers Act Release No. 5874 (Sept. 27, 2021), available at <https://www.sec.gov/litigation/admin/2021/ia-5874.pdf> (settled action); In the Matter of O.N. Investment Management Company, Investment Advisers Act Release No. 5944 (Jan. 11, 2022), available at <https://www.sec.gov/litigation/admin/2022/ia-5944.pdf> (settled action); In the Matter of Rothschild Investment Corp., Investment Advisers Act Release No. 5860 (Sept. 13, 2021), available at <https://www.sec.gov/litigation/admin/2021/34-92951.pdf> (settled action).

²⁰ See Exchange Act rule 15l-1(a)(2)(ii) and Fiduciary Interpretation, *supra* note 3, at 33674. See also Staff Bulletin on Account Recommendations, *supra* note 6 (stating the staff believes firms and financial professionals “should consider the total potential costs when evaluating whether an account is in a retail investor’s best interest, including indirect costs that could be borne by the retail investor.”).

the investor's best interest, in the staff's view, the firm and financial professional should consider, where relevant, the following non-exhaustive list of potential costs: commissions, markups or markdowns, and other transaction costs; sales loads or charges; advisory or management fees; other fees or expenses that may affect a retail investor's return (such as Rule 12b-1 fees, other administrative and service fees, revenue sharing, and transfer agent fees); the trading and other costs associated with an investment strategy (such as the need to continually buy and sell options or futures contracts or pay margin interest, daily rebalance fees, and any structural features of the investment that could magnify investor losses); the costs of exiting an investment or investment strategy (such as deferred sales charges or liquidation costs); any relevant tax considerations; and the likely impacts of those costs over the retail investor's expected time horizon.²¹ In other words, an analysis of costs, in the staff's view, should include costs beyond the explicit costs disclosed on a trade confirmation or account statement.

4. My firm has reviewed and compiled an approved list of investments for our retail investors. Can I rely solely on the firm's review to satisfy my own obligation to understand the investment or investment strategy I am recommending or on which I am providing advice?

No. Although firms have duties under their care obligations, including a general responsibility to understand the investments or investment strategies that they are recommending or on which they provide advice, financial professionals also have this responsibility.²² In the staff's view, firms should generally help ensure those financial professionals have sufficient information and training to understand the investments and investment strategies they recommend or advise on;²³

²¹ See Staff Bulletin on Account Recommendations, *supra* note 6 (providing examples of costs to consider when making account recommendations). An adviser would not satisfy its fiduciary duty to provide advice that is in the client's best interest by simply advising its client to invest in the lowest cost (to the client) or least remunerative (to the investment adviser) investment product or strategy without any further analysis of other factors in the context of the portfolio that the adviser manages for the client and the client's objective. See Fiduciary Interpretation, *supra* note 3 at 33674. Similarly, a broker-dealer would not satisfy the Care Obligation by simply recommending the least expensive or least remunerative security without any further analysis of the investment or investment strategy and the retail investor's investment profile. Reg BI Adopting Release, *supra* note 3, at 33380-81. In Reg BI the Commission emphasized the requirement to consider costs in light of other factors and the retail customer's investment profile while noting cost should never be the only consideration. See Reg BI Adopting Release, *supra* note 3, at 33326; Exchange Act rule 15l-1(a)(2)(ii).

²² Exchange Act rule 15l-1(a)(2)(ii)(A) (imposing this obligation on broker-dealers and their financial professionals). The Commission has brought enforcement actions when investment adviser representatives lacked a reasonable understanding of an investment's risks and key attributes. See, e.g., *Frontier Wealth Management, LLC and Shawn Sokolosky*, Investment Advisers Act Release No. 5847 (September 3, 2021) (settled action) (Sokolosky made unsuitable recommendations to clients in part because he "did not adequately understand the Feeder Fund's trading strategy, underlying investments, and risks."); cf. *UBS Financial Services, Inc.*, Investment Advisers Act Release No. 6060 (June 29, 2022) (settled action) (UBS violated § 206(2) where its advisory representatives lacked "a reasonable belief that the advice they provided . . . was in the best interest of their clients" because the representatives did not sufficiently "understand the significant downside risk" of the complex options strategy they recommended).

²³ Exchange Act rule 15l-1(a)(2)(iv); Reg BI Adopting Release, *supra* note 3, at 33398 (explaining that a reasonably designed compliance program generally would include, among other things, training); Fiduciary Interpretation,

however, financial professionals cannot satisfy their own care obligations by solely relying on the efforts of others at their firm. Rather, financial professionals remain responsible for personally understanding an investment or investment strategy before they recommend or provide advice with regard to that investment or investment strategy.

Understanding the Retail Investor’s Investment Profile

5. What is an “investment profile?” How does the investment profile help me satisfy my care obligation?

The term “investment profile” refers to information that the firm or financial professional generally should make reasonable efforts to ascertain about the retail investor. Obtaining and then evaluating information about the retail investor’s investment profile is a critical step to satisfying your care obligation.²⁴ In order to have a reasonable basis to believe a particular investment or investment strategy is in the best interest of a particular retail investor, you must obtain and evaluate enough information about the retail investor to have a reasonable basis to believe that the recommendation or advice is in the retail investor’s best interest. The reasonableness of efforts to collect information needed about a retail investor’s financial situation, investment objectives, and other information and characteristics of that retail investor to meet this requirement depends on the specific facts and circumstances of the particular situation, including considering the nature and characteristics of the investment or investment strategy at issue.²⁵ You must also have a reasonable basis to believe that your recommendation

supra note 3, at 33674 (noting that investment advisers are required to conduct a reasonable investigation into the investment sufficient not to base its advice on materially inaccurate or incomplete information).

²⁴ Importantly, once you have obtained and evaluated sufficient information about the retail investor’s investment profile, in the staff’s view, only then is it possible for you to assess whether the particular recommendation or advice is in the retail investor’s best interest. Reg BI Adopting Release, *supra* note 3, at 33379 (“[b]roker-dealers must obtain and analyze enough customer information to have a reasonable basis to believe that the recommendation is in the best interest of the particular retail customer.”). This includes using the investment profile, among other factors discussed below, in determining the scope of available alternatives. *See* Reg BI Adopting Release, *supra* note 3, at 33381 (explaining “[w]hat will be a reasonable determination of the scope of alternatives considered will depend on the facts and circumstances, at the time of the recommendation, including both the nature of the retail customer and the retail customer’s investment profile”). For investment advisers, “[t]he duty to provide advice that is in the best interest of the client based on a reasonable understanding of the client’s objectives is a critical component of the duty of care.” Fiduciary Interpretation, *supra* note 3, at 33673. An investment adviser generally should make a reasonable inquiry into a client’s investment profile in developing a reasonable understanding of the client’s objectives.

²⁵ Reg BI Adopting Release, *supra* note 3, at 33379; Fiduciary Interpretation, *supra* note 3, at 33673-33674 (stating that in addition to the investment profile, whether advice is in a client’s best interest must be evaluated in the context of the client’s portfolio, and that an adviser generally should apply heightened scrutiny to various high risk or complex investments or investment strategies (derivatives, penny stocks or other thinly traded securities, inverse or leveraged exchange-traded products) and investment strategies (hedging, purchasing on margin, short-term trading)).

or advice is not based on materially inaccurate, incomplete, or outdated information about the retail investor.

As part of establishing a reasonable understanding of the retail investor's investment profile, the staff believes that you generally should seek to obtain and consider, without limitation: the investor's financial situation (including current income) and needs; investments; assets and debts; marital status; tax status; age; investment time horizon; liquidity needs; risk tolerance; investment experience; investment objective and financial goals; and any other information the retail investor may disclose to you in connection with the recommendation or advice.²⁶ This list of factors is non-exhaustive and you can, and in some cases may need to, consider additional or different factors as appropriate under the specific facts and circumstances of the retail investor or the recommendation or advice.²⁷ For example, when making account recommendations, the staff believes that you should consider, without limitation, the retail investor's: anticipated investment strategy (e.g., buy and hold versus more frequent trading); level of financial sophistication; preference for making their own investment decisions or relying on advice from a financial professional; and need or desire for account monitoring or ongoing account management.²⁸

²⁶ See Exchange Act rule 15l-1(b)(2) (defining "retail customer investment profile" for purposes of Reg BI); Reg BI Adopting Release, *supra* note 3, at 33492; Fiduciary Interpretation, *supra* note 3, at 33673 (listing types of information—generally similar to those appearing in Reg BI's definition of retail customer investment profile—that advisers would generally need to know to provide a comprehensive financial plan to a client). See also Staff Bulletin on Account Recommendations, *supra* note 6 (providing examples of investor characteristics to be considered to have a reasonable basis to believe an account recommendation is in the retail investor's best interest).

²⁷ Reg BI Adopting Release, *supra* note 3, at 33379 (declining to include additional factors in the definition of "retail customer investment profile," noting that the list of factors in the definition is non-exhaustive and broker-dealers can consider additional factors as appropriate under the unique facts and circumstances of each recommendation, such as based on the unique nature of its particular securities products, investment strategies, and retail customers); Fiduciary Interpretation, *supra* note 3, at 33673-33674 (identifying additional considerations regarding investment characteristics (such as liquidity and leverage) and investment strategies (such as hedging or purchasing on margin) that may be appropriate for clients with investment profiles that include a high risk tolerance and significant investment experience). The significance of specific types of retail investor information generally will depend on the facts and circumstances of the particular case, including the nature and characteristics of the investment or investment strategy at issue. Reg BI Adopting Release, *supra* note 3, at 33379. For investment advisers, the amount and type of information obtained for an investment profile is viewed in the context of the agreed-upon scope of the relationship and, accordingly, may involve consideration of a subset of the relevant factors depending on the services to be provided and the duration of the relationship. Fiduciary Interpretation, *supra* note 3 at 33673 ("How an adviser develops a reasonable understanding [of a client's investment objectives] will vary based on the specific facts and circumstances, including the nature of the client, the scope of the adviser-client relationship, and the nature and complexity of the anticipated investment advice. In order to develop a reasonable understanding of a retail client's objectives, an adviser should, at a minimum, make a reasonable inquiry into . . . the retail client's 'investment profile.' . . . Whether the advice is in a client's best interest must be evaluated in the context of the portfolio that the adviser manages for the clients and the client's objectives.").

²⁸ For more information on account recommendations, see Staff Bulletin on Account Recommendations, *supra* note 6 (stating that "[t]he staff also believes that you should consider, without limitation, the retail investor's: anticipated investment strategy (e.g., buy and hold versus more frequent trading); level of financial sophistication; preference

6. Is gathering information for the retail investor’s investment profile a once-and-done exercise?

No. Broker-dealers and investment advisers must have sufficient information to make a recommendation or provide advice in the retail investor’s best interest. What constitutes sufficient information may change based on the investments or investment strategy being recommended or advised, or where the firm is aware or has reason to be aware that information in the investment profile has changed (e.g., birth of a child, marriage/divorce, retirement) or contains information that is inconsistent (e.g., a profile that contains multiple investment objectives that appear inconsistent with each other).²⁹

In addition, broker-dealers and investment advisers may need to update the investor’s investment profile to comply with their respective obligations. Broker-dealers generally should make a reasonable effort to ascertain information regarding an existing retail investor’s investment profile prior to the making of a recommendation on an “as needed” basis—that is, where a broker-dealer knows or has reason to believe that the customer’s investment profile has changed,³⁰ and must periodically attempt to update customer account information consistent with existing Exchange Act books and records requirements.³¹ Similarly, investment advisers must generally update the client’s investment profile in order to maintain an understanding of the client’s objectives and adjust the advice to reflect any changed circumstances.³²

Ultimately, investment advisers and broker-dealers must have sufficient information when a recommendation or advice is given to assess whether a particular recommendation or advice is in the best interest of the retail investor.³³

for making their own investment decisions or relying on advice from a financial professional; and the need or desire for account monitoring or ongoing account management.”).

²⁹ Reg BI Adopting Release, *supra* note 3, at 33379; Fiduciary Interpretation, *supra* note 3, at 33673.

³⁰ Reg BI Adopting Release, *supra* note 3, at 33379.

³¹ See Exchange Act rule 17a-3(a)(17); Reg BI Adopting Release, *supra* note 3, at 33398.

³² Fiduciary Interpretation, *supra* note 3, at 33673. The frequency with which such updates should occur will turn on the facts and circumstances, including whether the adviser is aware of events that have occurred that could render inaccurate or incomplete the investment profile on which the adviser currently bases its advice. *Id.* For instance, in the case of a financial plan where the investment adviser also provides advice on an ongoing basis, a change in the relevant tax law or knowledge that the client has retired or experienced a change in marital status could trigger an obligation to make a new inquiry.

³³ Reg BI Adopting Release, *supra* note 3, at 33379 (stating “[b]roker-dealers must obtain and analyze enough customer information to have a reasonable basis to believe that the recommendation is in the best interest of the particular retail customer.”). Staff Bulletin on Account Recommendations, *supra* note 6 (stating “[y]ou . . . must obtain and evaluate enough information about the retail investor to have a reasonable basis to believe the account recommendation is in the best interest of that retail investor and that your recommendation is not based on materially inaccurate or incomplete information.”). See also *supra* note 8.

7. What do I do if investor information is unavailable?

Where investor information is unavailable despite your reasonable diligence to obtain it, you should carefully consider whether you have a sufficient understanding of the retail investor to evaluate if any recommendation or advice you are considering providing is in that retail investor's best interest.³⁴ The staff believes you will not be able to have a reasonable belief that a recommendation or advice is in a retail investor's best interest without sufficient information about the retail investor, and therefore should generally decline to provide such recommendations or advice until you obtain the necessary investor information.³⁵ If you determine not to obtain or evaluate information that would normally be contained in an investment profile, the staff believes you should consider documenting the basis for your belief that such information is not relevant in light of the facts and circumstances of the particular recommendation or advice.³⁶

8. As discussed above, tax status is part of the retail investor's investment profile. What does it mean to consider the investor's tax status when providing recommendations or advice?

There are many investments and investment strategies where a primary feature may be a tax advantage for the investor (e.g., 529 plans, tax loss harvesting, opportunity zone funds, donor-advised funds, direct and custom indexing, variable annuities, government securities, 401(k) accounts, and IRAs). Where a retail investor or a financial professional identifies a goal with tax implications (e.g., including, but not limited to, saving for retirement or a child's education) or seeks to obtain a particular tax advantage (e.g., tax loss harvesting or limiting capital gains) as an investment objective, the staff believes that a firm and its financial professionals should consider

³⁴ Fiduciary Interpretation, *supra* note 3, at 33673 (“[I]t will generally be necessary for an adviser to a retail client to update the client’s investment profile in order to maintain a reasonable understanding of the client’s objectives and adjust the advice to reflect any changed circumstances.”) and n.37 (“We believe that any obligation to update a client’s investment profile, like the nature and extent of the reasonable inquiry into a retail client’s objectives, turns on what is reasonable under the circumstances.”); Reg BI Adopting Release, *supra* note 3, at 33379 (stating “where retail customer information is unavailable despite a broker-dealer’s reasonable diligence, the broker-dealer should carefully consider whether it has a sufficient understanding of the retail customer to properly evaluate whether the recommendation is in the best interest of that retail customer.”); Staff Bulletin on Account Recommendations, *supra* note 6 (explaining that if information is unavailable “the staff believes you should carefully consider whether you have a sufficient understanding of the investor to evaluate if any account recommendation is in that investor’s best interest.”).

³⁵ Reg BI Adopting Release, *supra* note 3, at 33379; Staff Bulletin on Account Recommendations, *supra* note 6.

³⁶ See Reg BI Adopting Release, *supra* note 3, at 33379 (stating that “consistent with existing obligations, where a broker-dealer determines not to obtain or analyze one or more of the factors specifically identified in the definition of ‘Retail Customer Investment Profile,’ the broker-dealer should document its determination that the factor(s) are not relevant components of a retail customer’s investment profile in light of the facts and circumstances of the particular recommendation.” (citing FINRA Rule 2111.04)); Staff Bulletin on Account Recommendations, *supra* note 6.

whether the tax-advantaged option covered by their recommendation or advice is in the best interest of the retail investor based on the retail investor's investment profile.

An investor's or account's tax status may also be an important consideration when selecting or providing advice on a particular investment or investment strategy relative to other options – such as whether a fixed income investment pays taxable, tax-free, or deferred interest, whether an out of state 529 plan is in the best interest of a customer who lives in a state that offers tax benefits for investing in the home state's plan, or whether a buy-and-hold or more frequent trading strategy is best for a particular account. Still, the staff believes the existence of a tax advantage alone would not provide a reasonable belief that a recommendation or particular advice would be in the retail investor's best interest.³⁷

Ultimately, the staff believes a factor such as tax advantage should be considered in light of the other features of the investment or investment strategies (including, but not limited to, limitations on withdrawal), reasonably available alternatives, and the retail investor's entire investment profile, including the retail investor's investment time horizon. If a retail investor already has one or more tax advantaged investments, the staff believes that factor generally should be considered when recommending or providing advice regarding another tax advantaged investment.³⁸

Considering Reasonably Available Alternatives

In the Reg BI Adopting Release, the Commission made clear that a broker-dealer generally should consider reasonably available alternatives as part of determining whether it has a reasonable basis to believe that a recommendation is in the best interest of its retail customer.³⁹ In order to fulfill what the Commission viewed as an inherent aspect of making a “best interest” recommendation, and consistent with a broker-dealer's related Compliance Obligation, the Commission stated that “a broker-dealer should have a reasonable process for establishing and understanding” the scope of reasonably available alternatives to be considered in order to fulfill the Care Obligation.⁴⁰ Similarly, the Commission stated in the Fiduciary Interpretation that advisers have a duty to act in the best interest of the client that cannot be satisfied through

³⁷ See Fiduciary Interpretation, *supra* note 3, at 33673 (noting tax status as one of a range of personal and financial types of information included in a client's investment profile); Reg BI Adopting Release, *supra* note 3, at 33379.

³⁸ Under Reg BI, a retail investor's investment profile is defined to include tax status. See Exchange Act rule 15l-1(b)(2). Thus, the Care Obligation requires a broker-dealer to have a reasonable basis to believe that an IRA or IRA rollover is in the best interest of the retail customer at the time of the recommendation, taking into consideration the retail investor's investment profile and other relevant factors, as well as the potential risks, rewards, and costs of the IRA or IRA rollover compared to the investor's existing 401(k) account or other circumstances. See Reg BI Adopting Release, *supra* note 3, at 33383. For investment advisers, whether the advice is in a client's best interest must be evaluated in the context of the portfolio that the adviser manages for the client and the client's objectives. Fiduciary Interpretation, *supra* note 3, at 33673.

³⁹ See Reg BI Adopting Release, *supra* note 3, at 33381.

⁴⁰ *Id.*

disclosure alone,⁴¹ and the Commission has brought enforcement actions against investment advisers for failing to consider certain available alternatives when selecting or recommending investments for their clients.⁴² Accordingly, while what advisers should consider depends on the facts and circumstances, the staff believes that the Commission’s statements about broker-dealers with respect to consideration of reasonably available alternatives likewise may provide a useful framework for investment advisers to consider in satisfying their care obligations when providing investment advice.

9. Should I consider reasonably available alternatives when recommending or providing advice about investments or investment strategies to retail investors?

Yes. It would be difficult for firms and their financial professionals to form a reasonable basis to believe a recommendation or advice is in the retail investor’s best interest without considering alternatives that are reasonably available to achieve the investor’s investment objectives.⁴³ Accordingly, the staff believes this is a key component of satisfying the care obligations of broker-dealers and investment advisers.⁴⁴

Moreover, in the view of the staff, consideration of reasonably available alternatives should begin early in the process of formulating a recommendation or providing advice rather than as a retroactive exercise undertaken after the firm or financial professional has already decided what to recommend or what advice to provide. The staff further believes that such consideration

⁴¹ See Fiduciary Interpretation, *supra* note 3, at 33676, n.58 (“We believe that while full and fair disclosure of all material facts relating to the advisory relationship or of conflicts of interest and a client’s informed consent prevent the presence of those material facts or conflicts themselves from violating the adviser’s fiduciary duty, such disclosure and consent do not themselves satisfy the adviser’s duty to act in the client’s best interest.”).

⁴² See, e.g., *O.N. Investment Management Company*, Investment Advisers Act Release No. 5944 (Jan. 11, 2022) (adviser violated its duty of care obligations when it “failed to consider alternative, lower-fee . . . money market funds” that were readily available to the adviser when it purchased other money market funds for its clients that generally resulted in revenue sharing being paid to the adviser or its affiliate), *available at* <https://www.sec.gov/litigation/admin/2022/ia-5944.pdf> (settled action); *Rothschild Investment Corp.*, Investment Advisers Act Release No. 5860 (Sept. 13, 2021) (adviser violated its duty of care obligations when it recommended money market funds that resulted in revenue sharing but “failed to consider alternative funds with similar strategies” that were available to the adviser and which had lower costs and higher yields), *available at* <https://www.sec.gov/litigation/admin/2021/34-92951.pdf> (settled action); *Cowen Prime Advisors, LLC*, Investment Advisers Act Release No. 5874 (Sept. 27, 2021) (same), *available at* <https://www.sec.gov/litigation/admin/2021/ia-5874.pdf> (settled action).

⁴³ For broker-dealers, the Commission views such a consideration as an inherent aspect of making a “best interest” recommendation. See Reg BI Adopting Release, *supra* note 3, at 33381. As noted, the Commission has brought enforcement actions in certain circumstances when an investment adviser failed to consider available alternatives. See *supra* note 39.

⁴⁴ See *id.*

should involve comparing reasonably available alternatives in light of a particular retail investor's investment profile.⁴⁵

For example, when a firm or financial professional is evaluating a mutual fund to recommend to a retail investor or to include in the investor's investment portfolio, the staff likely would not view a firm as having sufficiently considered reasonably available alternatives if it merely considers different share classes of one fund. Rather, in the staff's view, the evaluation should, for example, begin with consideration of other investments and investment types that are reasonably available to investors through the firm and could be used to achieve the investor's investment objectives. The firm or financial professional, in the view of staff, should conduct a comparative assessment of these alternatives in order to identify the investments or investment strategies that they reasonably believe are in the retail investor's best interest.⁴⁶

Ultimately, the staff believes what will be a reasonable consideration of available alternatives by firms or financial professionals will depend on the facts and circumstances. In the staff's view, firms should have and implement a reasonable process for establishing and understanding the scope of such reasonably available alternatives that should be considered as part of satisfying their care obligations.⁴⁷ When providing ongoing advice or services (e.g., ongoing monitoring), this may include both evaluation of alternatives prior to investment and consideration of alternative investments throughout the investment period.⁴⁸

10. How should firms approach developing a process to identify the scope of reasonably available alternatives that financial professionals should evaluate?

The staff believes that firms should have a reasonable process for identifying the scope of reasonably available alternatives that their financial professionals should consider.⁴⁹ Although

⁴⁵ See *id.*

⁴⁶ See *id.*

⁴⁷ See Reg BI Adopting Release, *supra* note 3, at 33381. See also In the Matter of Educators Financial Services, Inc., Investment Advisers Act Release No. 5836 (Aug. 27, 2021), available at <https://www.sec.gov/litigation/admin/2021/ia-5836.pdf> (settled action) (finding, among other things, that an investment adviser failed to adopt and implement written compliance policies and procedures reasonably designed to prevent violations of the Advisers Act when it breached its duty of care by failing to "consistently evaluate whether there were available lower-cost share classes" for certain clients); *cf. also* Advisers Act rule 206(4)-7.

⁴⁸ See *supra* note 14.

⁴⁹ See Reg BI Adopting Release, *supra* note 3, at 33381 (noting that, under Reg BI's Compliance Obligation, a broker-dealer should have a reasonable process for establishing and understanding the scope of "reasonably available alternatives" that would be considered by particular associated persons or groups of associated persons (e.g., groups that specialize in particular product lines) in fulfilling the reasonable diligence, care, and skill requirements under the Care Obligation). See also generally Advisers Act rule 206(4)-7 (requiring investment advisers registered or required to be registered under the Advisers Act to adopt and implement written compliance policies and procedures reasonably designed to prevent violations of the Advisers Act, which include preventing breaches of the IA fiduciary standard in violation of section 206 of the Advisers Act). Similarly, Reg BI's

the specific steps may vary, as a general matter the staff believes the process of developing a recommendation or advice should begin by considering a broader array of investments or investment strategies that are generally consistent with the retail investor's investment profile, and then narrowing to a smaller universe of potential investments or investment strategies as the analysis is more focused on meeting the best interest of a particular retail investor.

For example, in the staff's view, this analysis should first begin with firms identifying the investments or investment strategies that generally can be made available to their retail investors by a firm's financial professionals. The scope of such alternatives may depend on a variety of factors, including the nature of the firm's business and its customer or client base and the scope of its relationship with such customers or clients. In the staff's view, the scope of such alternatives should be narrowed further in light of the particular retail investor's investment profile. For example, in the staff's view, if the retail investor has a high need for liquidity, the financial professional should consider excluding investments with longer time horizons and limited or no secondary market.

Once reasonably available alternatives have been identified that are consistent with the retail investor's investment profile, the staff believes firms should have a reasonable process, tailored to their particular business model and investment offerings, for evaluating those alternatives.⁵⁰ In the view of the staff, this process should include guidance (e.g., policies and procedures, employee training) for the firm's financial professionals that defines the scope of alternatives that should be considered and the factors that should be weighed (e.g., costs, potential benefits and risks as well as compatibility with the retail investor's investment profile) in evaluating the available alternatives.

Ultimately, the scope of alternatives considered should be sufficient to enable the firm and its financial professionals to have a reasonable basis to believe that their recommendation or advice is in the retail investor's best interest. Accordingly, in the view of the staff, firms should consider providing guidance on the types of investments and investment strategies financial professionals should consider when recommending investments or investment strategies to achieve particular investment objectives (e.g., long-term growth, short-term savings, income, preservation of capital, tax advantages, or exposure to a particular market segment). Such guidance could include specific factors to consider in determining which options are in the best interest of a particular retail investor in light of their investment profile.

Compliance Obligation requires broker-dealers to establish, maintain, and enforce written policies and procedures reasonably designed to achieve compliance with Reg BI.

⁵⁰ See *id.*

11. My firm operates with an open architecture framework.⁵¹ Do I have to evaluate every alternative available through my firm?

The staff recognizes that certain firms may have business models sufficiently broad in scope that it may be difficult for financial professionals to be familiar with every investment available to investors.⁵² In such cases, a financial professional does not have to evaluate every possible alternative available through the firm.⁵³ On the other hand, the staff believes that financial professionals would still need to evaluate a range of potential alternatives sufficient to have a reasonable basis to believe a recommendation or advice is in the best interest of the retail investor. As discussed above, in the staff's view, the scope of alternative investments and investment strategies that might be considered will depend on the facts and circumstances, including but not limited to the nature of the firm's business, the retail investor's investment profile, the scope of its relationships with its customers and clients, and the reasonable availability of alternative investments or investment strategies.⁵⁴

12. My firm has a limited menu of investments. Do I have to consider all of them when evaluating reasonably available alternatives?

It depends. In the staff's view, a financial professional associated with a firm that has only a limited menu of investments generally should be familiar with each of those investments that are available to investors. That said, certain investments on that limited menu that can be made available to retail investors in general may be inconsistent with an individual retail investor's investment profile, such that the investments are not reasonable alternatives for that particular retail investor.⁵⁵ At the same time, a firm and its financial professionals cannot rely on a limited menu to justify recommending an investment or providing advice that does not satisfy the obligation to act in a retail investor's best interest. The staff believes investment advisers who are engaged in providing ongoing investment advice, in particular, should periodically consider whether the investment options they make available to their clients are sufficient to meet their

⁵¹ The Commission used the term "open architecture" in the Reg BI adopting release "to mean a firm's product menu that includes both third-party and proprietary products, or [where] a firm offers a large range of products to their retail customers that are not limited, for example, to a small list of approved managers or funds (i.e., a product menu that is not limited to proprietary products or otherwise constrained to certain retail customers or registered representatives)." Reg BI Adopting Release, *supra* note 3, at 33372 n.554.

⁵² See Reg BI Adopting Release, *supra* note 3, at 33381.

⁵³ See *id.* ("a broker-dealer does not have to conduct an evaluation of every possible alternative, either offered outside of the firm (such as where the firm offers only proprietary or other limited range of products) or available on the firm's platform").

⁵⁴ Under Reg BI, the Commission stated, "[w]hat will be a reasonable determination of the scope of alternatives considered will depend on the facts and circumstances, at the time of the recommendation, including both the nature of the retail customer and the retail customer's investment profile, and the particular associated persons or groups of associated persons that are providing the recommendations." See Reg BI Adopting Release, *supra* note 3, at 33382.

⁵⁵ *Id.*

clients' best interest, and whether other investment options that may better serve their clients' interests may be available.⁵⁶

As noted earlier, the staff believes that firms, including those with a limited investment menu, should have a reasonable process, tailored to their particular business model and investments, for considering reasonably available alternatives.

13. Can I satisfy my care obligations by simply recommending or providing advice on the “most appropriate” available option from among my firm’s limited menu of investments?

No. When considering a limited menu of reasonably available alternatives, there may be one “most appropriate” possible alternative among the limited options available, yet that alternative may still not be in the best interest of the particular retail investor in light of their investment profile. Accordingly, one possible outcome of such a process is that the firm or financial professional may conclude that no investment or investment strategy they offer is in the retail investor’s best interest. If that occurs, the firm and financial professional would not satisfy their care obligations if they recommended or advised any of those investments or investment strategies to the retail investor.⁵⁷

14. Does every investment or investment strategy have a reasonably available alternative?

The staff recognizes that product innovation, particularly in the realm of complex products, has resulted in the development of products with highly particular features that make them unique. However, the staff believes that products that are not identical may still be comparable to each other for purposes of identifying them as reasonably available alternatives based on the retail investor’s investment profile, among other factors.

For example, if a retail investor’s investment objectives include exposure to a particular market sector, the staff believes the firm should consider a range of products that offer such exposure and are consistent with the investor’s investment profile. In this scenario, the staff believes that the firm should begin with a comparison of the types of products that would achieve exposure to the market sector in a manner consistent with the entirety of the retail investor’s investment

⁵⁶ While Reg BI does not require an evaluation of alternatives offered outside the firm, when a broker-dealer materially limits its product offerings to certain proprietary or other limited menus of products, it must still comply with the Care Obligation—even if it has disclosed and taken steps to prevent the limitation from placing the interests of the broker-dealer ahead of the retail customer, as required by Reg BI’s Disclosure and Conflict of Interest Obligation—and thus could not use its limited menu to justify recommending a product that does not satisfy the obligation to act in a retail customer’s best interest. *See* Reg BI Adopting Release, *supra* note 3, at 33326; *see also* Fiduciary Interpretation *supra* note 3, at 33676 (“a dual registrant acting in its advisory capacity should disclose any circumstances under which its advice will be limited to a menu of certain products offered through its affiliated broker-dealer or affiliated investment adviser.”).

⁵⁷ *See* Reg BI Adopting Release, *supra* note 3, at 33326.

profile, including investment objectives, rather than simply selecting a product that offers exposure to that sector and then looking for other products with similar features to consider as alternatives. In the staff's view, the unique features and benefits of alternatives considered do not need to be an exact match so long as the risks, rewards and costs associated with the alternatives are consistent with the retail investor's investment profile.

15. In the staff's view, do I need to consider the risks, rewards, and costs associated with the reasonably available alternatives I have identified?

Yes. You must consider the potential risks, rewards, and costs when recommending or providing advice on investments and investment strategies in order to have a reasonable basis to believe that a recommendation or advice is in a retail investor's best interest.⁵⁸ Accordingly, in the view of the staff, you generally would need to understand the potential risks, rewards, and costs associated with reasonably available alternatives as part of having a reasonable basis to believe that a recommendation or advice is in the best interest of the retail investor. For example, when recommending an investment with a higher cost or higher risk as compared to reasonably available alternatives, the staff believes you should consider whether any reasonably available alternative to the investment is less costly or has lower risk that is consistent with the investor's investment profile. Similarly, when recommending an investment based on a particular special feature or reward (such as tax advantage), the staff believes you should consider whether any reasonably available alternatives offer similar special features or rewards, in addition to considering the broader range of risks, rewards, and costs of such alternatives, in light of the retail investor's investment profile.

As with any recommendation or advice, if you ultimately choose to recommend or provide advice about an investment that has a higher risk or cost than reasonably available alternatives, or that offers a special feature or reward that reasonably available alternatives do not, you must

⁵⁸ Under Reg BI, broker-dealers must understand the potential risks, rewards, and costs associated with a recommendation. See Exchange Act rule 15l-1(a)(2)(ii)(A). See also Fiduciary Interpretation, *supra* note 3, at 33674 (“[t]he 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.”) [emphasis added]. Further, as noted, the Commission has brought enforcement actions against investment advisers for breaching their duty of care when they failed to consider alternative funds. See, e.g., *O.N. Investment Management Company*, Investment Advisers Act Release No. 5944 (Jan. 11, 2022) (adviser violated its duty of care obligations when it “failed to consider alternative, lower-fee . . . money market funds” that were readily available to the adviser when it purchased higher-cost funds for its clients that paid revenue sharing to the adviser or an affiliate) (settled action); *Rothschild Investment Corp.*, Investment Advisers Act Release No. 5860 (Sept. 13, 2021) (adviser violated its duty of care obligations when it recommended higher-cost money market funds that paid revenue sharing to the adviser or an affiliate but “failed to consider alternative funds with similar strategies” that were available to the adviser and which had lower costs and higher yields.) (settled action); *Cowen Prime Advisors, LLC*, Investment Advisers Act Release No. 5874 (Sept. 27, 2021) (same) (settled action).

have a reasonable belief that the recommendation or advice is nonetheless in the retail investor's best interest, in light of the particular investor's investment profile.⁵⁹

16. Should firms document the evaluation of reasonably available alternatives?

Although there is no requirement of such documentation, in the staff's view, it may be difficult for a firm to demonstrate compliance with its obligations to retail investors, or periodically assess the adequacy and effectiveness of its written policies and procedures, without documenting the basis for certain recommendations.⁶⁰ This could include documentation of the consideration of reasonably available alternatives.⁶¹ The staff believes documentation demonstrating that the financial professional considered reasonably available alternatives can be particularly important where a recommendation may seem inconsistent with a retail investor's investment objectives on its face and/or poses conflicts of interest for the firm or the financial professional.⁶²

⁵⁹ Reg BI allows a broker-dealer to recommend products that entail higher costs or risks for the retail customer, or that result in greater compensation to the broker-dealer, or that are more expensive, than other products, provided that the broker-dealer complies with the rule's specific component obligations, including the requirement to make these recommendations exercising reasonable diligence, care, and skill to have a reasonable basis to believe that the recommendation is in the retail customer's best interest and does not place the broker-dealer's interest ahead of the retail customer's interest. *See* Reg BI Adopting Release, *supra* note 3, at 33334. *See also* Fiduciary Interpretation, *supra* note 3, at 33674 (“[T]he adviser could recommend a higher-cost investment or strategy if the adviser reasonably concludes that there are other factors about the investment or strategy that outweigh cost and make the investment or strategy in the best interest of the client, in light of that client's objectives.”).

⁶⁰ In adopting Reg BI, the Commission determined not to require broker-dealers to document the basis for any recommendations, but encouraged them to take a risk-based approach when deciding whether to document certain recommendations. For example, it stated that broker-dealers may wish to document an evaluation of a recommendation and the basis for the particular recommendation in certain contexts, such as the recommendation of a complex product, or where a recommendation may seem inconsistent with a retail customer's investment objectives on its face. *See* Reg BI Adopting Release, *supra* note 3, at 33360. While the Commission has not addressed documentation of reasonably available alternatives for investment advisers, the staff notes that investment advisers registered or required to be registered are required to maintain certain records related to the adviser's recommendations and investment advice. *See* Advisers Act rule 204-2(a)(7) (requiring that investment advisers registered or required to be registered make and keep written communications received or sent by advisers relating to, among other matters, “[a]ny recommendation made or proposed to be made and any advice given or proposed to be given”). *See* Staff Bulletin on Account Recommendations, *supra* note 6 (providing staff views on documentation of the basis of account recommendations).

⁶¹ *See id.*

⁶² *See* Reg BI Adopting Release, *supra* note 3, at 33378 (stating that broker-dealers may wish to document an evaluation of a recommendation and the basis for the particular recommendation in certain contexts, such as the recommendation of a complex product, or where a recommendation may seem inconsistent with a retail customer's investment objectives on its face).

Special Considerations: Complex or Risky Products

17. Can it be consistent with a financial professional’s care obligations to recommend, or provide advice about, a complex or risky product?

Yes. Neither Reg BI nor the IA fiduciary standard prohibits recommendations of, or advice about, complex or risky products to retail investors where the financial professional has established a reasonable basis to believe the complex or risky product is in the best interest of the retail investor in light of the retail investor’s particular investment profile, including their financial situation and objectives. These products may not be in the best interest of a client absent an identified, short-term, customer-specific trading objective.⁶³ In the view of the staff, firms and financial professionals should consider whether less complex, less risky or lower cost alternatives can achieve the same objectives for their retail customers as part of their overall reasonable basis analysis. Moreover, firms and their financial professionals generally should apply “heightened scrutiny” to whether a risky or complex product is in the retail investor’s best interest.⁶⁴

18. What does it mean to apply heightened scrutiny in the context of recommending, or providing advice about, a complex or risky product?

Certain products are more complex or have additional risk features, which may make it more difficult for firms and their financial professionals to develop an understanding of the terms, features, and risks of those products in order to have a reasonable basis to believe that the products are in the best interest of retail investors.⁶⁵ Examples of products where heightened scrutiny may be necessary include, but are not limited to, inverse or leveraged exchange-traded products, investments traded on margin, derivatives, crypto asset securities, penny stocks, private placements, asset-backed securities, volatility-linked exchange-traded products, and reverse-convertible notes.⁶⁶

⁶³ See generally Reg BI Adopting Release, *supra* note 3, at 33376 (discussing recommendations of high-risk products and stating “these products may not be in the best interest of a retail customer absent an identified, short-term, customer-specific trading objective.”); Fiduciary Interpretation, *supra* note 3, at 33673-33674 (noting that high-risk products, for example inverse or leveraged exchange-traded products that are designed primarily as short-term trading tools for sophisticated investors, “may not be in the best interest of a retail client absent an identified, short-term, client-specific trading objective . . .”).

⁶⁴ See Reg BI Adopting Release, *supra* note 3, at 33376 (“[W]hen a broker-dealer recommends a potentially high risk product to a retail customer—such as penny stocks or other thinly-traded securities—the broker-dealer should generally apply heightened scrutiny to whether such investments are in a retail customer’s best interest.”); Fiduciary Interpretation, *supra* note 3, at 33673 (“[W]hen an adviser is assessing whether high risk products—such as penny stocks or other thinly-traded securities—are in a retail client’s best interest, the adviser should generally apply heightened scrutiny to whether such investments fall within the retail client’s risk tolerance and objectives.”).

⁶⁵ See Reg BI Adopting Release, *supra* note 3, at 33376; Fiduciary Interpretation, *supra* note 3, at 33673-33674.

⁶⁶ See, e.g., Reg BI Adopting Release, *supra* note 3, at 33376; Fiduciary Interpretation, *supra* note 3, at 33673-33674. The Commission has also noted the need to develop a specific understanding of the features of variable annuities. See also Reg BI Adopting Release, *supra* note 3, at 33376-33377 (noting that, consistent with existing

In addition to developing an understanding of the product, firms and their financial professionals should obtain information about the retail investor that supports a conclusion that a complex or risky product is in that retail investor's best interest. Depending on the product in question, such information might include, for example, whether the retail investor has an identified, investor-specific trading objective that is consistent with the product's description in its prospectus or offering documents, and/or has the ability to withstand heightened risk of financial loss.⁶⁷ However, the fact that an investor has such an objective or ability does not automatically mean that the product is in the retail investor's best interest. Firms and their financial professionals must still have a reasonable basis to believe that, based on the overall relevant facts and circumstances, the investment is in a retail investor's best interest. As with recommendations of, or advice about, other investments and investment strategies, firms and their financial professionals should also evaluate reasonably available alternatives as described throughout this bulletin.

19. What procedures should a firm consider implementing to address complex or risky product recommendations or advice?

A firm's written policies and procedures should be tailored to the firm's business.⁶⁸ Extending that point, the staff believes that firms that recommend, or provide advice about, complex or risky products to retail investors should strongly consider establishing procedures specifically designed to address recommendations of, or advice about, complex or risky products. For example, the staff believes firms should consider developing procedures outlining the due diligence process for complex or risky financial products, to help ensure that these products are assessed by qualified and experienced firm personnel. Firms should also consider establishing procedures requiring appropriate training and supervision to help ensure financial professionals understand the features, risks, and costs of a complex financial product.⁶⁹ Additionally, firms

FINRA rules, among other regulatory obligations, that "recommendations of these products would require careful attention and a specific understanding of certain factors, such as whether the product provides tax-deferred growth, or a death or living benefit, before a broker-dealer could establish an understanding of the product, and apply that understanding to a retail customer's investment profile in making a recommendation").

⁶⁷ See *supra* note 64.

⁶⁸ See Reg BI Adopting Release, *supra* note 3, at n. 810 (discussing the Compliance Obligation's affirmative obligation to establish, maintain, and enforce written policies and procedures reasonably designed to achieve compliance with Regulation Best Interest and how it is similar to the obligation for investment advisers); see also Compliance Programs of Investment Companies and Investment Advisers, IA Release No. 2204 (Dec. 17, 2003) ("IA Release 2204") at 74728; Questions Advisers Should Ask While Establishing or Reviewing Their Compliance Programs (May 2006), available at https://www.sec.gov/info/cco/adviser_compliance_questions.htm. The staff notes that some firms have implemented policies that limit the type of retail investor to whom certain high-risk or complex products can be recommended.

⁶⁹ The Commission has brought enforcement actions against registered investment advisers for compliance rule violations relating to the failure to provide adequate training and guidance to financial professionals who recommended complex financial products. See, e.g., *In the Matter of Wells Fargo Clearing Services, LLC, and Wells Fargo Advisors Financial Network, LLC*, Exchange Act Release No. 88295 (Feb. 27, 2020) (settled action) (dual registrant recommended that many retail investment advisory clients and brokerage customers buy and hold single

should consider establishing procedures for evaluating reasonably available alternatives to complex or risky products they recommend or provide advice about.⁷⁰ As stated above, when recommending, or providing advice about, complex or risky products, the staff believes firms should consider whether lower risk or less complex options can achieve the same investment objectives. In the staff's view, firms that make recommendations of, or provide advice about, complex or risky products to retail investors should also consider documenting the process and reasoning behind the particular recommendation or advice, including consideration of less complex alternatives, and how it fits within the retail investor's broader goals or strategy.⁷¹ Finally, for circumstances where the firm or financial professional has an obligation to monitor investor accounts, the staff believes that the firm should consider establishing procedures for ongoing evaluation of the complex or risky products held by retail investors to ensure that they continue to be in the investor's best interest.⁷²

Special Considerations: Recommendations and Advice by Dual Registrants

20. I am a dually licensed financial professional working at a dually registered firm, and some of our retail investors have both brokerage and advisory accounts with us.

a. How do I know which standard applies when providing advice and recommendations to such investors?

Whether Reg BI or the IA fiduciary standard applies to a particular recommendation made or advice provided by a dually registered firm and/or financial professional depends on a facts and circumstances analysis, with no one factor being determinative.⁷³ The Commission considers,

inverse exchange-traded funds without having adequate compliance policies and procedures and without providing financial advisors proper training and supervision of single-inverse exchange-traded funds), *available at* <https://www.sec.gov/litigation/admin/2020/34-88295.pdf>; *In the Matter of Summit Financial Group, Inc.*, Advisers Act Release No. 5626 (Nov. 13, 2020) (settled action) (investment adviser failed to adopt and implement policies and procedures reasonably designed to prevent unsuitable investments in volatility-linked exchange traded products), *available at* <https://www.sec.gov/litigation/admin/2020/ia-5626.pdf>.

⁷⁰ See Reg BI Adopting Release, *supra* note 3, at 33321; Fiduciary Interpretation, *supra* note 3, at 33673-33674.

⁷¹ See Reg BI Adopting Release, *supra* note 3, at 33360 (encouraging broker-dealers to record the basis for their recommendations, especially more risky products, as a potential way a broker-dealer could demonstrate compliance with the Care Obligation); see also IA Release No. 2204 at 74716 (“ . . . an adviser’s policies and procedures, at a minimum, should address . . . consistency of portfolios with clients’ investment objectives . . .”).

⁷² Cf. *Morgan Stanley Smith Barney, LLC*, Investment Advisers Act Rel. No. 4649 (Feb. 14, 2017) (settled action) (finding that Morgan Stanley violated the Advisers Act’s compliance rule in part by failing to implement its policies and procedures requiring its investment advisory representatives to monitor client positions in single-inverse exchange traded products), *available at* <https://www.sec.gov/litigation/admin/2017/ia-4649.pdf>; see also Fiduciary Interpretation, *supra* note 3, at 33675, n.52 and accompanying text (generally discussing policies and procedures with respect to monitoring).

⁷³ See Reg BI Adopting Release, *supra* note 3, at 33379; see generally Fiduciary Interpretation, *supra* note 3, at 33674. See also Staff Bulletin on Account Recommendations, *supra* note 6 (discussing dually licensed financial professionals’ obligations when recommending accounts to prospective retail investor).

among other factors, the type of account, how the account is described, the type of compensation, and the extent to which the dually registered firm and financial professional made clear to the customer or client the capacity in which they were acting.⁷⁴ In this vein, the disclosure obligations of both Reg BI and the IA fiduciary standard require a firm or financial professional to disclose to the retail investor the capacity in which the firm or financial professional is acting (e.g., broker-dealer or investment adviser).⁷⁵ The staff cautions that the disclosure of capacity may not be determinative if the facts and circumstances suggest the financial professional was acting in a different capacity from the one disclosed.⁷⁶

Ultimately, as stated above, although the specific application of Reg BI and the IA fiduciary standard may differ in some respects and be triggered at different times, in the staff's view they generally yield substantially similar results in terms of the ultimate responsibilities owed to retail investors. Regardless of the firm's or financial professional's capacity, you should obtain and evaluate enough information about the retail investor and the investment or investment strategy being recommended to have a reasonable basis to believe a recommendation or advice is in the best interest of that retail investor and that your recommendation is not based on materially inaccurate or incomplete information.⁷⁷

b. Do I need to consider whether a brokerage or advisory account is more appropriate for an investment or investment strategy when providing recommendation or advice to a retail investor of a dually licensed financial professional?

Yes. Dually registered firms and dually licensed financial professionals have an obligation to reasonably believe the recommendation or advice they provide regarding account type is in the

⁷⁴ See Reg BI Adopting Release, *supra* note 3, at 33346; Fiduciary Interpretation, *supra* note 3, at 33674, n.44 (regarding account type recommendations) and at 33675-33676 (regarding the capacity in which the financial professional is acting).

⁷⁵ See Reg BI Adopting Release, *supra* note 3, at 33321; Fiduciary Interpretation, *supra* note 3, at 33675-33676.

⁷⁶ Separately, if a financial professional is only registered as an associated person of a broker-dealer (regardless of whether the financial professional works for a dually registered firm or a broker-dealer affiliated with an investment adviser), the financial professional would need to take into consideration only the brokerage accounts available at the broker-dealer. See Reg BI Adopting Release, *supra* note 3, at 33340; see also Frequently Asked Questions on Regulation Best Interest (discussing whether an associated person of a broker-dealer that is a dual registrant needs to consider both brokerage and advisory accounts when making an account recommendation), available at <https://www.sec.gov/tm/faq-regulation-best-interest#recommendation>. Conversely, a financial professional who is only a supervised person of an investment adviser (regardless of whether that advisory firm is a dual registrant or affiliated with a broker-dealer) may only recommend an advisory account the adviser offers when the account is in the client's best interest. See Fiduciary Interpretation, *supra* note 3, at 33674, n.44. Finally, a broker-dealer and its financial professionals cannot rely on a limited menu of investment options to justify recommending an investment or providing advice that does not satisfy the obligation to act in a retail investor's best interest. See Reg BI Adopting Release, *supra* note 3, at 33326.

⁷⁷ See also Staff Bulletin on Account Recommendations, *supra* note 6.

retail investor's best interest.⁷⁸ Moreover, where a retail investor holds both brokerage and advisory accounts, the staff believes a dually registered firm or dually licensed financial professional should consider whether a recommendation of an investment or investment strategy is better suited for the investor's brokerage account or advisory account.⁷⁹ In the staff's view, this process should include consideration of the difference in reasonably expected total costs depending on whether the investment or investment strategy is held in the retail investor's brokerage or advisory account, including but not limited to any account level costs, such as commissions, advisory fees on assets under management, or, as relevant, tax consequences, over the expected life of the investment. For example, a retail investor whose objective is to buy and hold a long-term investment may be better off paying a one-time commission to a broker-dealer for the purchase of that investment rather than paying an ongoing advisory fee merely to hold the same investment. However, it may be more cost effective or otherwise appropriate for that same investor to hold investments in an advisory account because the overall costs to the retail investor are lower or because the retail investor (or the type of investment) will require regular, ongoing advice with respect to those investments or investment strategies.

⁷⁸ See Reg BI Adopting Release, *supra* note 3, at 33340 (discussing a dually licensed broker-dealer's obligation to have a reasonable basis to believe that a recommended account is in the best interest of a retail investor); Fiduciary Interpretation, *supra* note 3, at 33674, n.44 (" . . . in providing advice to a client or customer about account type, a financial professional who is dually licensed (*i.e.*, an associated person of a broker-dealer and a supervised person of an investment adviser (regardless of whether the professional works for a dual registrant, affiliated firms, or unaffiliated firms)) should consider all types of accounts offered (*i.e.*, both brokerage accounts and advisory accounts) when determining whether the advice is in the client's best interest."); see also Staff Bulletin on Account Recommendations, *supra* note 6 (discussing the obligation of dually licensed firms and financial professionals to consider both advisory and brokerage accounts when recommending an account type).

⁷⁹ See Reg BI Adopting Release, *supra* note 3, at 33383 ("Where the financial professional making the recommendation is dually registered (*i.e.*, an associated person of a broker-dealer and a supervised person of an investment adviser (regardless of whether the professional works for a dual-registrant, affiliated firms, or unaffiliated firms)) the financial professional would need to make [an account type] evaluation taking into consideration the spectrum of accounts offered by the financial professional (*i.e.*, both brokerage and advisory taking into account any eligibility requirements such as account minimums), and not just brokerage accounts."); Fiduciary Interpretation, *supra* note 3, at 33674 ("An adviser's fiduciary duty applies to all investment advice the investment adviser provides to clients, including advice about . . . 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). . . .").