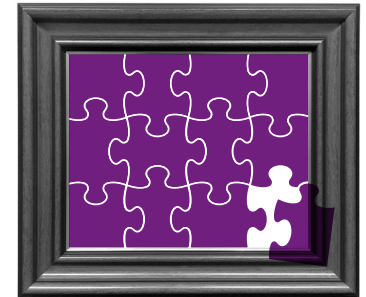


Getting the full picture

The emerging best interest and fiduciary duty patchwork

August 14, 2019



Putting the pieces together

As anticipated, this year has seen a number of fiduciary and best interest investment advice regulations at both the federal and state levels. Firms subject to these regulations will face challenges in dealing with rules that will impose a host of new obligations, and that may overlap and conflict with one another. This chart is intended to help firms take stock of the evolving framework and aid firms in putting the pieces together.

	SEC- and State-Registered Investment Advisers	SEC-Registered Broker-Dealers [Under Proposed SEC Regulation Best Interest]	Proposed Nevada Securities Regulation and Financial Planning Statute	Proposed Massachusetts Securities Regulation	Proposed New Jersey Securities Regulation	ERISA Fiduciaries Subject to DOL Rules	Producers and Insurers Subject to New York Regulation 187
Duty Owed	Advisers are fiduciaries; they owe a duty of care and a duty of loyalty, and they must act in the best interest of clients.	Broker-dealers must act in the best interest of their retail customers at the time recommendations are made, and their interests must not be placed ahead of the customers' interests.	Broker-dealers and investment advisers in Nevada owe a fiduciary duty to clients.	Broker-dealers and advisers owe a fiduciary duty to customers, which requires broker-dealers, agents, advisers and investment adviser representatives to satisfy both the duty of care and duty of loyalty.	Broker-dealers and investment advisers owe a fiduciary duty to customers, which requires broker-dealers, agents, investment advisers and investment adviser representatives to satisfy both the duty of care and duty of loyalty.	ERISA fiduciary is subject to duties of loyalty, prudence and diversification; also prohibitions on transactions with "parties in interest" (which includes a broker-dealer), on acting with a self-interest or conflicted interest, and on receiving payments from third parties.	When making recommendations, a producer (or insurer where no producer is involved) must act in the best interest of the consumer, and only the interests of the consumer shall be considered in making recommendations.
Source of Duty	Common law and Section 206 (the anti-fraud provisions) of the Advisers Act. For state-registered advisers, common law and state securities laws and rules.	SEC Proposed Rule Regulation Best Interest.	Explicit provisions in the statute and proposed regulation.	Massachusetts' securities regulations prohibit broker-dealers and advisers from engaging in dishonest or unethical practices. Massachusetts' Securities Law provides the secretary with authority to impose an administrative fine or censure or deny, suspend or revoke any registration or take any other appropriate action in the public interest when a broker-dealer or adviser engages in dishonest or unethical practices.	Failure to act in accordance with a fiduciary duty would constitute a dishonest or unethical business practice under New Jersey's Securities Law.	Explicit statutory provisions in ERISA.	Explicit provisions in NY Regulation 187.

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Trigger	Establishing an advisory-client relationship.	Making recommendations of any securities transaction or investment strategy to a retail customer.	<p>Providing investment advice to a client, managing assets, performing discretionary trading, using certain titles or terms, or otherwise establishing a fiduciary relationship with clients.</p> <p>The fiduciary duty owed by an investment adviser and a representative of an investment adviser is triggered by the establishment of an advisory-client relationship and includes the time period for which the adviser or representative engages in certain activities set forth in the Regulation.</p> <p>The fiduciary duty owed by an investment adviser or broker-dealer and a representative of an investment adviser/broker-dealer is triggered by providing advice and other enumerated instances.</p>	<p>When providing investment advice or recommending to a customer an investment strategy, the opening of any type of account, the transferring of assets to any type of account, or the purchase, sale, or exchange of any security.</p> <p>When making ongoing recommendations or providing investment advice, in any capacity, to a customer or client, or receiving ongoing compensation in connection with the recommendation or advice.</p> <p>When making a recommendation or providing investment advice and (i) acting with discretionary authority over a customer's or client's account or (ii) a contractual fiduciary duty.</p> <p>When making a standalone recommendation, a broker-dealer's or adviser's fiduciary duty extends through the execution of the recommendation.</p>	<p>When providing investment advice or recommending to a customer an investment strategy, the opening of any type of account, the transfer of assets to any type of account, or the purchase, sale, or exchange of any security.</p> <p>The regulation also provides that it is a dishonest or unethical practice if an adviser or a broker-dealer or its agent who has discretionary authority over a customer's account or a contractual fiduciary duty or who is acting as an adviser, fails to act in accordance with a fiduciary duty to a customer when providing investment advice.</p>	Providing investment advice for a fee to an ERISA plan or participants, or exercising discretion in the investment of ERISA plan assets, within the meaning of ERISA.	Making recommendations to consumers for a sales transaction or an in-force transaction with respect to policies delivered or issued for delivery in the State of New York.

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Coverage	Investment advisers subject to the Advisers Act or corresponding state laws, as well as supervised persons of such investment advisers.	Broker-dealers, as well as any persons associated with the broker-dealer (i.e., registered representatives and principals), when making recommendations of a securities transaction or investment strategy to retail customers.	Any person who acts as a "financial planner" in Nevada, including broker-dealers, sales representatives, investment advisers, and representatives of investment advisers.	It applies to all SEC-registered broker-dealers who are also registered in Massachusetts. The proposed regulation contains its own definition of "adviser," which is defined as "any person, including persons registered or excluded from registration under the [Massachusetts Securities Act], who receives any consideration from another person primarily for advising the other person as to the value of securities or their purchase or sale, whether through analyses or reports or otherwise." There is a rebuttable presumption under the proposed regulation that an "adviser" includes investment advisers and investment adviser representatives, as well as other persons who charge fees based on assets under management or portfolio performance for rendering investment advice. The statutory definition of "investment adviser" also includes financial planners.	It applies to all SEC-registered broker-dealers who are also registered in New Jersey. It applies to state-registered advisers, but not SEC-registered advisers.	"Fiduciaries" who provide investment advice for a fee or have discretion in the investment of plan assets, within the meaning of ERISA. Discretionary advice is and has always been fiduciary activity.	Insurance producers (and insurers where no producer is involved) recommending sales transactions or in-force transactions involving life insurance or annuities to consumers.

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Modifying Scope of Duty via Client Consent	An adviser's responsibilities and the scope and nature of services provided can be altered with client consent but the fiduciary duty cannot be waived or changed by clients.	Unable to modify scope of best interest duty via client consent.	Not expressly addressed in Regulation.	Unable to modify scope of fiduciary duty via client consent.	Not expressly addressed in Regulation.	May specify by agreement the type and scope of services to be provided (e.g., manage the fixed income sleeve of a defined benefit plan, or advise as to the investment options for a defined contribution plan), but may not modify the statutory fiduciary duty.	Unable to modify scope of best interest duty via client consent.
Ongoing Duty to Monitor	Generally yes, unless altered with client consent.	No ongoing duty to monitor investment performance. Duty extends only to the specific recommended securities transaction or investment strategy.	Ongoing monitoring obligation only relieved if firm qualifies for the "Episodic Fiduciary Duty Exemption." Dual registrants prohibited from relying on this exemption.	For a broker-dealer, agent, or adviser, the fiduciary obligation extends through the execution of the recommendation. If a broker-dealer, adviser, or agent (i) makes ongoing recommendations; (ii) provides investment advice in any capacity to a customer or client; or (iii) receives ongoing compensation in connection with the recommendation or advice, the fiduciary duty will be ongoing.	For broker-dealers, the fiduciary obligation extends through the execution of the recommendation. If a broker-dealer also provides investment advice in any capacity, has discretionary authority over a customer's account, or a contractual fiduciary duty, the fiduciary duty will be applicable to the entire customer relationship, regardless of the customer account type.	Primarily a matter for agreement with the investor, although DOL has suggested a duty to monitor may be inherent in recommending more complex investments.	No ongoing duty to monitor the policy to which recommendations are provided. Duty extends only to the specific recommendation.

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Receipt of Compensation From Product Issuers and Other Third Parties	Permissible to receive compensation from third parties, if client consent is obtained and conflicts are mitigated. However, compensation cannot be paid for distribution or offering activity conducted on behalf of issuers without being registered as a broker-dealer and without such activity being subject to requirements applicable to broker-dealers.	Permissible, if broker-dealer establishes procedures to identify, disclose, and mitigate (or eliminate) material conflicts of interest arising from financial incentives, which includes receipt of compensation from product issuers and other third parties.	Transaction-based compensation is permissible so long as it is in the client's best interest to be charged on a transaction basis as opposed to some other basis, and the commission is reasonable. Nevada law does require a financial planner to disclose to clients any commission or third-party compensation. Compensation cannot be received for distribution or offering activity conducted on behalf of issuers without being registered as a broker-dealer with Nevada and without such activity being subject to requirements applicable to broker-dealers.	There is a presumption of a breach of the duty of loyalty for offering or receiving, direct or indirect compensation to or from a broker-dealer, agent, or adviser, for recommending an investment strategy, the opening of a specific type of account, the transferring of assets to a specific type of account, or the purchase, sale or exchange of any security that is not "the best of the reasonably available options." It is not a breach of fiduciary duty when a broker-dealer or agent receives transaction-based remuneration, provided that: (i) the remuneration is reasonable; (ii) the remuneration represents the "best of the reasonably available remuneration options;" and (iii) the duty of care is satisfied.	There is a presumption of a breach of the duty of loyalty for offering, receiving, direct or indirect compensation to or from the broker-dealer, agent, or adviser, for recommending the opening of a specific type of account, the transfer of assets to a specific type of account, or the purchase, sale, or exchange of a specific security that is not "the best of the reasonably available options." It is not a breach of fiduciary duty when the broker-dealer or agent receives a transaction-based fee, provided that: (i) the fee is reasonable; (ii) the fee is the best of the reasonably available fee options, and (iii) the duty of care is satisfied.	If a fiduciary, prohibited absent an applicable statutory or DOL-prohibited transaction exemption, which tend to be product-specific. Also, crediting the value of the third-party compensation back to the plan, including through fee offsets or additional services, avoids the prohibited conflict.	Insurance producers may be compensated if the amount of the compensation or the receipt of the incentive does not influence the recommendation. Moreover, insurers may maintain within and across product lines variations in compensation or other incentives that comply with New York insurance laws and regulations provided that the insurer's compensation and incentive practices, when taken as a whole, are designed to avoid recommendations by producers that are not in the best interest of consumers.

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Conflict Management	An adviser is required to disclose and mitigate conflicts.	Broker-dealer must establish procedures to identify, disclose, and mitigate (or eliminate) material conflicts of interest arising from financial incentives associated with the recommended securities transaction or investment strategy. Material conflicts of interest not arising from financial incentives need to be identified and disclosed and/or eliminated.	Regulation specifically requires that in order to satisfy fiduciary duty, potential conflicts need to be disclosed.	<p>Duty of Care: When making a recommendation or providing investment advice, a broker-dealer, agent, or adviser must use the care, skill, prudence, and diligence that a prudent person acting in a like capacity and familiar with such matters would use taking into consideration all of the facts and circumstances.</p> <p>For the duty of care to be satisfied, a broker-dealer, agent, or adviser must make reasonable inquiry, including: risks, costs, and conflicts of interest related to the recommendation or investment advice, the customer's investment objectives, financial situation, and needs, and any other relevant information.</p> <p>Duty of Loyalty: When making a recommendation or providing investment advice, a broker-dealer, agent, or adviser must avoid conflicts of interest and make recommendations and provide investment advice without regard to the financial or any other interest of the broker-dealer, agent, adviser, any affiliated or related entity or any other third-party.</p>	<p>Duty of Care: When making a recommendation or providing investment advice, a broker-dealer or investment adviser must use the care, skill, prudence and diligence that a prudent person acting in a like capacity and familiar with such matters would use taking into consideration all of the facts and circumstances.</p> <p>For the duty of care to be satisfied, broker-dealers and agents must make a reasonable inquiry, including risks, costs and conflicts of interest related to any recommendation or investment advice, and the customer's investment objectives, financial situation, and needs, and any other relevant information.</p> <p>Duty of Loyalty: For a broker-dealer or investment adviser, recommendations or advice must be made without regard to the financial or any other interest of the broker-dealer, agent, adviser, any affiliated or related entity and its officers, directors, agents, employees, or any other third-party.</p>	Prohibited conflicts are allowable only to the extent permitted under an applicable statutory or DOL-prohibited transaction exemption, which regularly include conflict mitigation conditions.	No express requirement imposed under the Regulation to manage compensation-related conflicts. However, insurers are required to establish, maintain, and audit a system of supervision that is reasonably designed to achieve the insurer's and producers' compliance with the best interest standard. Moreover, producer compensation arrangements and product offering limitations are subject to specific disclosure requirements.

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Required Disclosure	Required by fiduciary duty and also specific requirement in Form ADV.	At the time the recommendations are made, the broker-dealer must reasonably disclose to the retail customer, in writing, the material facts relating to the scope of the brokerage relationship, including all material conflicts of interest that are associated with securities recommendations. Form CRS also would impose additional disclosure requirements for broker-dealers at the outset of the customer relationship.	Among other things, Regulation calls for specific disclosure regarding, as applicable, the sale of proprietary products or that the advice was based on a limited pool of products. Broad ranging requirement to disclose all information related to conflicts.	None.	None.	Disclosure does not alone cure a prohibited ERISA conflict. Prohibited conflicts are allowable only to the extent permitted under an applicable statutory or DOL-prohibited transaction exemption, which often require disclosures.	The best interest standard requires, among other things, that there be a reasonable basis to believe that the consumer has been reasonably informed of certain features of the policy and potential consequences of the transaction, both favorable and unfavorable.
Provides for Client Consent to Proceed With Activity That Constitutes a Conflict	Client consent is needed to proceed with activity that constitutes a conflict. Such consent may often be satisfied by full and fair disclosure.	Client consent not needed to proceed with activity that constitutes a conflict, although certain financial conflicts will need to be mitigated (or eliminated) regardless of client consent.	Not specifically addressed in Regulation.	No. There is no presumption that disclosing a conflict of interest alone will satisfy the duty of loyalty.	No. There is no presumption that disclosing a conflict of interest in and of itself will satisfy the duty of loyalty.	Client consent, even after disclosure, does not alone cure a prohibited ERISA conflict. Prohibited conflicts are allowable only to the extent permitted under an applicable statutory or DOL-prohibited transaction exemption, which often require consent from an independent fiduciary or plan participant.	Client consent not needed to proceed with activity that constitutes a conflict.
Private Remedy	Only limited private rights of action under federal law (to recover investment advisory fees). Clients may have other private rights of action under state common law.	SEC indicates that no private right of action or right of rescission created by Regulation Best Interest.	Broker-dealers and sales representatives have the burden of proving in arbitration, or civil or administrative actions, that an exemption to the fiduciary duty exists; financial planner statute expressly provides for private right of action.	Explicit statutory authority provides private right of action for offering or selling a security by means of any untrue statement of a material fact or any omission to state a material fact necessary.	Explicit statutory authority provides private right of action for engaging in dishonest or unethical practices.	Private right of action under ERISA.	No private right of action created by NY Regulation 187.

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Enforceability	Legally enforceable against adviser and supervised persons of advisers by SEC.	Legally enforceable standard against broker-dealer and/or registered persons of the broker-dealer by SEC.	Legally enforceable standard against broker-dealers, sales representatives, investment advisers, and representatives of investment advisers by the Administrator of the Nevada Securities Division.	Legally enforceable in private actions and by administrative action of state securities regulators.	Legally enforceable in private actions and by administrative action of state securities regulators.	Legally enforceable in private actions or by DOL.	Legally enforceable against insurance producers and insurance companies by the New York superintendent of insurance.

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For more commentary regarding the emerging landscape related to the standards of conduct for investment professionals, visit Eversheds Sutherland's www.secfiduciaryrule.com. If you have any questions about this Legal Alert, please feel free to contact any of the attorneys listed below or the Eversheds Sutherland attorney with whom you regularly work.

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