Agenda

CEFLI Compliance & Ethics Committee Meeting
Wednesday, April 15, 2020
2 PM EDT/1 PM CDT/12 Noon MDT/11 AM PDT
Dial In: (800) 239-9838
Passcode: 5690858

I. Welcome and Introduction. **Donald J. Walters**

A. Antitrust Statement.

II. Approval of Minutes – March 18, 2020 Meeting. **The Committee**

III. Issues for Review. **The Committee**

A. Coronavirus (COVID 19).

CEFLI has convened a Networking Forum to explore compliance issues associated with COVID-19. Meetings of this initial, pilot Networking Forum take place every other Thursday at 3 PM EDT. The next meeting of the CEFLI COVID-19 Networking Forum is scheduled to take place on Thursday, April 23 at 3 PM EDT. Please contact Nancy Perez (NancyPerez@cefli.org) to let us know if you or your colleagues may be interested in participating in the COVID-19 Networking Forum.

Companies are working diligently to follow the array of different announcements and bulletins that been issued by various states in their efforts to provide relief for consumers in light of the COVID-19 pandemic.

Life insurers have demonstrated strong community leadership by making contributions to various national and local relief efforts attempting to assist their communities in meeting the economic challenges arising out of the COVID-19 pandemic.

Over the next several months, we will continue to include an agenda item for our Compliance & Ethic Committee meeting so individuals may have an appropriate Forum in which to present timely and relevant compliance challenges that may be of interest to the Committee.

The Committee will be asked to discuss current compliance challenges associated with issues arising out of the COVID-19 pandemic.

B. Collection of Applicant Information - COVID-19.

A key question arising out of the onset of the COVID-19 pandemic is the collection of accurate information from applicants for life insurance policies. Specifically, life insurance companies maintain an interest in the accuracy of information concerning potential insureds as part of their underwriting practices.

With this in mind, a question has been presented to the Committee concerning whether any companies have elected to file amendments to their application forms to include specific health questions concerning whether an applicant for life insurance may have tested positive for COVID-19 or has incurred COVID-19 symptoms.

In addition, there is interest in determining whether companies may be instructing their agents to ask preliminary questions concerning whether an applicant for life insurance may have tested positive for COVID-19 or has incurred COVID-19 symptoms.

The Committee will be asked to discuss whether their company may have filed amendments to their current applications or may be instructing their agents ask preliminary questions concerning whether an applicant for life insurance may have tested positive for COVID-19 or has incurred COVID-19 symptoms.

C. Fraud in Accelerated Underwriting.

Many life insurers now offer consumers an opportunity to be considered for Accelerated Underwriting as part of a way to expedite the life insurance policy application process.

Accelerated Underwriting practices may require an insured to submit basic personal information which is then supplemented by the life insurance company through a variety of different investigative methods utilizing external sources (e.g., public records, social media, etc.) as a means to forgo providing medical samples (e.g., blood, urine, etc.) as part of the underwriting process.

In light of the growth of these activities throughout the life insurance industry, a question has been presented to the Committee to discuss possible fraudulent activities that may be associated with the pursuit of Accelerated Underwriting opportunities at life insurance companies.

The Committee will be asked to discuss the extent to which their companies may have encountered fraudulent activities, if any, associated with Accelerated Underwriting practices.

D. Interest on Death Claims.

The Committee has been asked to revisit an issue that we have explored over the past several months related to the calculation of interest on the payment of death claims. (See, Section III, D of the March 18 Committee meeting minutes.)

As we explored during our previous discussions, practices vary among insurers with respect to the method used to calculate interest on death claims. Through our discussions we have determined that certain states have specific guidelines with respect to how interest should be calculated with respect to the payment of death claims and practices may vary by state. We also have noted that the calculation of interest on death claims has become the subject of market conduct examinations in selected states.

One company has indicated that their practice with respect to the calculation of interest on death claims is to examine the requirements of the state of the insured's residence, the state of the beneficiary's residence and the state in which the policy was issued and then pay the highest amount of interest based upon these calculations.

The question presented is whether other companies follow a similar practice.

The Committee will be asked to discuss their practices with respect to the calculation of interest on the payment of death claims.

E. Providing Notice - Not Required to Take a Required Minimum Distribution (RMD).

Congress recently enacted the Setting Every Community Up for Retirement Enhancement Act of 2019 (the "SECURE Act") which included changes to current laws pertaining to certain retirement accounts (e.g., 401(k), 403(b), 457 and IRA accounts and the rules requiring these retirement account owners to take a Required Minimum Distribution (RMD) from their retirement accounts.

The SECURE Act made significant changes to RMD rules. If a retirement account owner reached age 70 ½ in 2019, the account owner would be subject to the prior RMD rules and will be required to take a RMD by April 1, 2020. However, the SECURE Act provides that if a retirement account owner will reach age 70 ½ in 2020 or later, the retirement account owner will not be required to take a RMD until April 1 of the year in which they reach age 72.

Now, with passage of the Coronavirus Aid, Relief and Economic Security Act (the "CARES Act"), RMDs are suspended for calendar year 2020 for all qualified retirement plans and IRAs.

Therefore, a question has been presented to the Committee concerning whether life insurance companies plan to issue a notice to retirement account owners that, due to the changes in RMD requirements under the CARES Act, they are not be required to take a RMD from their retirement accounts.

The Committee will be asked to discuss their company's practices with respect to whether they plan to issue a notice to retirement account owners that they are not be required to take a RMD in 2020.

IV. Reporting Items. CEFLI Staff.

A. SEC Won't Extend Compliance Date for Regulation Best Interest and Form CRS Summary.

SEC Chairman Jay Clayton has indicated that the SEC will not extend the June 30, 2020 compliance date for Regulation Best Interest and the Form CRS Summary.

Chairman Clayton's announcement was premised upon the fact that firms have made "considerable progress" with respect to their efforts to comply with the requirements of Regulation Best Interest and the Form CRS Summary.

B. SEC and FINRA Announce That Initial Regulation Best Interest and Form CRS Examinations Will Be Focused on "Good Faith" Efforts To Comply.

Both the SEC and FINRA have announced that the initial round of examinations to determine compliance with the requirements of Regulation Best Interest and the Form CRS Summary will be focused on determining whether a firm has made "good faith" efforts to comply with these requirements.

The SEC has issued to Risk Alerts outlining their plans with respect to examination expectations for Regulation Best Interest and the Form CRS Summary. (See, copy of the Risk Alerts attached.)

Shortly after issuance of the SEC's Risk Alerts, FINRA issued a statement to confirm that their examination practices will take the same approach as set forth within the SEC's Risk Alerts. (See, copy of FINRA's statement attached.)

C. FINRA Issues Report on Firms' Best Practices for Compliance with Regulation Best Interest and Form CRS.

FINRA recently issued a report on firms' best practices for compliance with Regulation Best Interest.

In late 2019, FINRA reviewed several small, medium and large size firms to determine their degree of preparedness with respect to Regulation Best Interest and Form CRS.

(See, copy of FINRA report attached.)

These best practices were designed to assist firms in continuing their work to prepare for the June 30, 2020 compliance date.

Areas identified in the report included:

- Governance and Implementation Management;
- Training;
- Written Supervisory Procedures and Supervisory Systems
- Conflicts of Interest;
- Compensation;
- Surveillance;
- Disclosure;
- Use of the Terms “Adviser” or Advisor;”
- Sales Contests; and
- Form CRS.

D. Securities Regulators Will Monitor COVID-19-Related Fraud.

Representatives from the SEC, FINRA and the North American State Securities Regulators recently reported that they are monitoring for a wide spectrum of possible fraud in light of the COVID-19 crisis.

Specifically, they reminded firms to be aware of possible risks associated with provisions of the CARES Act which allows workers to withdraw up to $100,000 from their retirement accounts without a penalty.

E. New York and New Jersey Issue Emergency Regulation/Executive Order Requiring Life insurers to Extend Grace Periods for Payment of Premiums up to 90 days.

1. New York.

The New York Department of Financial Services issued an emergency regulation requiring insurers to extend grace period for the payment of premiums on life insurance and annuity contracts up to 90 days.

Among its other provisions, the emergency regulation will also require life insurers to:

- Waive late payment fees otherwise due, and not report late payments to credit rating agencies, during the 90 day period;

- Allow premiums due but not paid during the 90 day period to be paid over the course of the following year in 12 equal monthly installments; and

- Extend by 90 days the period to exercise policyholder and contract holder rights and benefits under life insurance and annuity contracts.

2. New Jersey.

In New Jersey, Governor Phil Murphy issued an Executive Order that mandates a minimum 90-day grace period for premium payments for life insurance and annuity products.

The Executive Order also includes the following requirements:

- Insurance companies will be required to notify policyholders of this emergency grace period and to waive certain late fees, interest, or other charges associated with delays in premium payments as directed by the Commissioner of Banking and Insurance. Insurers will also be required to provide each policyholder with an easily readable written description of the terms of the extended grace period. The extended grace periods will not apply to employer-funded health plans, which under federal law, are regulated exclusively by the federal government.

- Insurance companies will be required to pay any claim incurred during the emergency grace period that would be covered under the policy. The Order further prohibits insurance companies from seeking recoupment of any claims paid during the emergency grace period based on non-payment of premiums.

- To ensure that policyholders are not required to make a lump sum payment on unpaid premiums at the end of the grace period, any unpaid premium will be amortized over the remainder of the policy term or a period of up to 12 months, as appropriate and as directed by the Commissioner of Banking and Insurance.

V. CEFLI Activities.

A. CEFLI Webinar - Regulation Best Interest - Wednesday, April 22 - 1 PM EDT/12 Noon CDT.

CEFLI will be conducting the next installment in its Educational Webinar Series to explore the compliance requirements of the SEC's Regulation Best Interest.

CEFLI is pleased to have James Lundy, Partner with CEFLI Affiliate Member law firm Faegre Drinker, serve as our faculty member for this session. James served previously on the staff of the SEC and will share his insights concerning key compliance challenges posed by firms attempting to comply with the requirements of Regulation Best Interest.

Registration for the webinar is currently available on the CEFLI website. We hope you will be able to join us!

B. CEFLI Virtual Summit Meeting - Exploring the Recent Revisions to the NAIC Suitability in Annuity Transactions Model Regulation.

Later this month, CEFLI will be launching its Virtual Summit Meeting to explore the recent revisions to the NAIC Suitability in Annuity Transactions Model Regulation. CEFLI's Virtual Summit Meeting was developed to provide the same content and information that was planned to be offered during CEFLI's in-person Educational Summit Meeting scheduled to take place in Des Moines, Iowa on April 8.

The Virtual Summit Meeting will include five different segments to provide insights offered by company representatives, regulators and industry experts regarding the key compliance provisions of the new version of the NAIC Suitability in Annuity Transactions Model Regulation.

Key topics will include:

- An Overview of the ***Emerging and Dynamic Sales Standards*** that led to the revisions to the NAIC Suitability in Annuity Transactions Model Regulation;
- A review of the ***Disclosures*** required by the Model Regulation;
- Insurer ***Training*** requirements posed by the Model Regulation;
- Insurer ***New Business Processes*** in light of the Model Regulation; and
- ***Oversight and Supervision*** practices required by the Model Regulation.

The Virtual Summit Meeting will be available "on demand" on CEFLI's website (www.CEFLI.org).

More information concerning the availability of CEFLI's Virtual Summit Meeting will be announced within the coming weeks.

C. CEFLI COVID-19 Networking Forum – Thursday, April 23 and Thursday, May 7 – 3 PM EDT/2 PM CDT/1 PM MDT/12 Noon PDT.

The next meetings of CEFLI's new Networking Forum to explore COVID-19 operational issues will take place on Thursday, April 23 and Thursday, May 7 at 3 PM EDT/2 PM CDT/1 PM MDT/12 Noon PDT. Please contact Nancy Perez (NancyPerez@cefli.org) if you or your colleagues would like to be added to the new COVID-19 Networking Forum.

VI. Next Meeting.

The next meeting of the Committee is scheduled to take place:

Wednesday, May 13, 2020 - 2 PM EDT/1 PM CDT/12 Noon MDT/11 AM PDT

Please mark your calendar and plan to join us!

The remaining Committee meeting dates for 2020 will be as follows:

Wednesday, June 17, 2020 - 2 PM EDT/1 PM CDT/12 Noon MDT/11 AM PDT
Wednesday, July 22, 2020 - 2 PM EDT/1 PM CDT/12 Noon MDT/11 AM PDT
Wednesday, August 19, 2020 - 2 PM EDT/1 PM CDT/12 Noon MDT/11 AM PDT
Wednesday, September 16, 2020 - 2 PM EDT/1 PM CDT/12 Noon MDT/11 AM PDT
Wednesday, October 14, 2020 - 2 PM EDT/1 PM CDT/12 Noon MDT/11 AM PDT
Wednesday, November 12, 2020 - 2 PM EST/1 PM CST/12 Noon MST/11 AM PST
Wednesday, December 16, 2020 - 2 PM EST/1 PM CST/12 Noon MST/11 AM PST

VII. Other Business.

The Committee will be asked to identify and discuss any other business to be brought before the Committee.

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Minutes
Meeting of the
CEFLI Compliance & Ethics Committee
March 18, 2020

A meeting of the CEFLI Compliance & Ethics Committee (the "Committee") was held via conference call on Wednesday, March 18 at 2 PM EDT/1 PM CDT/12 Noon MDT/11 AM PDT.

The following CEFLI member company representatives participated in the meeting:

Ro Adebiyi, Thrivent Financial
Derek Albanese, UNUM Life
Marcie Allen, Texas Life
Renee Ambrosy, CNO Financial
Jenna Austin, Guggenheim Life
Brendan Bakala, Catholic Order of Foresters
Lauren Barbaruolo, Oxford Life Insurance
Chad Batterson, Athene
Ann Binzer, Cincinnati Life
Kate Blalock, Western & Southern
Amy Brech, Western & Southern
Bryan Brewster, Wilson Re
Emmanuelle Brooks, Pacific Life
Jason Broussard, American National
Donna Brown, Lombard International
Amy Burggraff, Securian Financial Group
Nancy Campbell, Symetra
Courtney Colby, Thrivent
Steve Corbly, Cincinnati Life
Jacquie Crader, CUNA Mutual
Becky Criswell, Americo
Nicholas Criscitelli, VOYA Financial
John Cunningham, Fidelity Investments Life
Shirley Dayton, Pacific Guardian Life
Dustin Degroote, Homesteaders Life
Tony Dowling, Jackson National Life
Jill Fiddler, Assurity Life
Kris Fischer, Thrivent
Patrick Garcy, Sagicor
Geoff Gentilucci, Legal & General America

Paula Gentry, Cincinnati Life
Jennifer Gibb, Pacific Life
Jim Golembiewski, Sagicor Life
Meagan Gonzales, Oxford Life
Shirley Grossman, Lincoln Heritage
Dennis Herchel, SBLI MA
Lisa Holland, State Farm
Michelle Holmes, VOYA Financial
Nathan Huss, Sammons
Margaret Immerfall, CUNA Mutual
Jeremy Intihar, Brighthouse Financial
Eileen Jarres, Pacific Life
De Keimach, Delaware Life
Kristen Kirkwood, Western & Southern
Carly Kleiman, Western & Southern
Jenna Klinck, Allianz
Jennifer Knabe, Ohio National
Samantha Knackmuhs, State Farm
Megan Knapp, American Enterprise Group
Hannah Krone, Western & Southern
Michele Kryger, AIG Life
Marla Lacey, Homesteaders Life
Dan Leblanc, SBLI MA
Laurie Lewis, Amica Life
Andy Mayorga, USAA Life
Wanda McNeece, Lincoln Heritage
Ryan Meehan, RiverSource
Morgan Milner, Modern Woodmen
Matt Missik, Pacific Life
Cynthia Mueller, Thrivent
Christopher Nguyen, Pacific Guardian Life
Jim Odland, Thrivent
John Pankratz, Voya Financial
Monique Pascual, Pacific Guardian
Liza Perry, USAA Life
Megan Phillips, Principal Life
Sandy Ray, Symetra
John Ricci, Amica Life
Michael Roberson, Pacific Guardian Life
Michelle Ross, Lombard International
Heather Russo, Illinois Mutual
John Sharp, Assurity Life
Devin Smith, Securian Financial
Craig Stille, Country Financial

Elena Sullivan, USAA Life
Molly Swami, Western & Southern Financial
Nancy Sweet, CNO Financial
Stephanie Teater, Western & Southern Financial
Bill Turner, American Fidelity
Chris Vellante, Delaware Life
Norm Von Seggern, AAA Life
Rochelle Walk, Wilton Re
Patrick Wallen, VOYA Financial
Larry Welch, Citizens Inc
Stacey White, American National
Emily Wilburn, Illinois Mutual
Karen Yeo, Primerica Life

Donald J. Walters, President & CEO, and Carla Strauch, Vice President-Compliance & Ethics, and Mallory Bennett, Director of Member Relations, Communications and Meetings also attended the meeting.

I. Welcome and Introduction.

The meeting began with a recitation of CEFLI's anti-trust statement.

II. Approval of Minutes – February 12, 2020.

On motion, duly made and seconded and unanimously carried, the Committee: RESOLVED, that, the Minutes of the February 12, 2020 meeting are hereby approved.

III. Issues for Review.

A. Coronavirus (COVID-19).

As the world addresses issues that have arisen as a result of the onset of the Coronavirus (COVID-19) pandemic (i.e. "social distancing", negative economic impacts, etc.), the life insurance industry is not immune from these developments. Committee members were asked to share their perspectives regarding how the Coronavirus has impacted their company's policies and procedures and steps their companies may be taking over the months ahead to protect the health and safety of their employees, distributors and other stakeholders. The Committee discussed the following:

- *Has your company instructed employees to work from home?*

  Committee members on the call noted that most, or nearly all, staff are

working from home. In some cases, on-site staffing is restricted to critical functions that cannot be carried out from a remote location. Committee members commented on the fact that productivity has been good and that, in some cases, productivity has increased. One Committee member noted the implementation of an on-site vs. work-from-home rotation strategy for its executives. Several Committee members commented on enhanced facilities cleaning protocols that had been put in place.

- *Has your company instituted a travel ban (domestically and/or internationally) for all **non-essential travel** or for any conferences or industry gatherings? If so, for how long?*

  Committee members shared insight regarding company travel restrictions which varied from allowing travel only for executives and sales staff to a complete ban on any nonessential travel. Many Committee members commented on prohibitions related to conference travel, indicating such prohibitions were for an indefinite period of time or for specific period, such as the end of April.

  One Committee member noted their company's request to employees to also limit personal travel during this time. Several Committee members referenced new mandatory self-quarantine guidelines for staff who may have traveled internationally or to a domestic hot zone.

- *Has your company begun to implement business continuity plans (BCP) in light of the onset of the Coronavirus?*

  Committee members noted that aspects of their companies' business continuity plans had been implemented or that they were currently evaluating potential implementation of elements of their respective plans.

  Committee members also shared insight regarding new requirements in several states related to timely notification to regulators of business continuity plan implementation and/or impacts to company operations. Such states included the state of Florida (OIR-20-03M), the state of West Virginia (Bulletin No. 20-04), the state of New York (Circular Letter No. 5, dated March 10, 2020), the state of Maine (Bulletin 442) and the state of Minnesota (Bulletin 2020-1, directed toward Property & Casualty insurers.

  Some states require specific, timely action on the part of insurers, including a response to the regulator by a specified date.

  It was reported that the state of New Mexico had issued a Bulletin to carriers selling limited benefit plans (i.e. LTC, hospital indemnity, etc.),

mandating that carriers issue notices to policyholders by March 27th regarding the limited nature of their coverage and requiring insurers provide a certificate of compliance to the state.

One Committee member noted the American Property Casualty Insurance Association (APCIA) offers a summary of state-by-state information that may be a resource for some.

- *Has your company begun to implement restrictive expense control strategies in light of a 0% interest rate environment?*

  One Committee member noted the likelihood of delays with future product launches.

- *Will your company's underwriting requirements change to mandate testing for Coronavirus?*

  One Committee member shared that no changes had been made, further indicating that may need to be addressed in the future.

B. Requests for Extensions of Time for Premium Payments (Grace Periods) - Emergencies/Natural Disasters.

During periods of national emergencies or natural disasters, life insurance companies will often post notices to their websites to advise policyholders to contact the company to discuss whether extensions of time for premium payments (i.e., grace periods) may be granted due to the extraordinary nature of these events. The Committee was asked to discuss whether companies may be planning to implement broader strategies with respect to providing extensions of time for premium payments.

During the discussion, Committee members noted limited regulatory activity in this area, thus far. Only the state of Maine was referenced as having some form of action to date. Several carriers indicated a plan to work with impacted insureds on a case-by-case basis and indicated a willingness to consider premium payment extensions, upon request, based on the consumer's circumstances.

C. Maryland Market Conduct Action – Vaping/E Cigarettes

The Maryland Insurance Administration recently submitted a market conduct action request to several insurers. The request posed a series of questions to determine company underwriting practices with respect to a prospective insured's use of Vaping or E Cigarettes.

The Committee was asked to discuss whether their companies have received a similar letter from the Maryland Insurance Administration.

Several Committee members noted their receipt of the Maryland market conduct questionnaire.

D. Calculation of Interest on Delayed Claim Payments.

Life insurance laws and regulations in several states allow insurers to retain the proceeds of a life insurance policy, under certain conditions, following the death of an insured. The same laws and regulations often outline the conditions under which life insurance companies are required to calculate interest on delayed claim payments. A key question pertains to whether life insurance companies must compute simple interest or compound interest on delayed claim payments.

While it had been generally understood that compound interest may represent a standard practice throughout the industry, a member company encountered market conduct examinations from two different jurisdictions (Washington and Vermont) indicating interest on delayed claim payments should be computed using simple interest (rather than compound interest).

The Committee was asked to discuss their company's practices with respect to the method used to compute interest (i.e., compound interest or simple interest) on delayed claim payments.

One Committee member noted that its processes related to who to pay, when to pay, and the amount of interest to be paid are clear. The Committee member went on to indicate that there is a lot of ambiguity regarding whether to apply simple or compound interest. In such cases, the Committee member noted their practice of paying compound interest.

IV. Reporting Items. CEFLI Staff.

A. Massachusetts Fiduciary Rule.

The Massachusetts Securities Division has adopted regulations which will apply a fiduciary standard of conduct to broker-dealers and agents when dealing with their customers. The regulation will become effective upon its publication in the Massachusetts Register. The Securities Division has indicated that the Final Regulations will be enforced effective September 1, 2020.

B. NAIC Executive/Plenary Committees Approved Revisions to the NAIC Suitability in Annuity Transactions Model Regulation.

On Thursday, February 13, the NAIC's Executive/Plenary Committees approved recent revisions to the NAIC Suitability in Annuity Transactions Model Regulation.

CEFLI has been monitoring the activities of the NAIC's Annuity Suitability (A) Working Group and the NAIC's Life Insurance and Annuities (A) Committee to follow these important developments.

The revised Model Regulation conforms with many of the requirements of the SEC's Regulation Best Interest.

C. Iowa Insurance Division Proposes its version of the revised NAIC Suitability in Annuity Transactions Model Regulation.

The Iowa Insurance Division has been one of the first states to propose its version of the revisions to the NAIC Suitability in Annuity Transactions Model Regulation. If approved, Iowa's proposed rule will be effective January 1, 2021.

The Iowa rule proposal also outlines Best Interest Obligations in the Brokerage Business for broker-dealers and investment advisory firms.

D. FINRA Submits Proposed Rule to Amend FINRA Rule 2111 (Suitability) and Non-Cash Compensation Rules.

FINRA has issued proposed rules to amend FINRA Rule 2111 (Suitability) to state that it will not apply to recommendations subject to the SEC's Regulation Best Interest. The Proposed Rule amendments would conform FINRA's rules governing non-cash compensation to Regulation Best Interest's limitations on sales contests, sales quotas, bonuses and non-cash compensation.

The Proposed Rule amendments must be approved by the SEC. If they are approved, they will become effective on June 30, 2020 – – the effective date of the SEC's Regulation Best Interest.

E. SEC Issues Final Rule on Summary Prospectus for Variable Annuities.

The SEC has issued its long-awaited final rule on a Summary Prospectus for variable annuity products. A link to the 713 page final rule can be found through the following URL: https://www.sec.gov/rules/final/2020/33-10765.pdf

The Summary Prospectus rule will allow investors to receive a more concise version of the prospectus accompanying variable annuity products similar to the

more concise prospectus provided in conjunction with mutual fund products.

F. FINRA Regulatory Notice 20-08 - Pandemic-Related Business Continuity Planning, Guidance and Regulatory Relief.

FINRA has issued guidance reminding firms to revisit their business continuity planning in light of the Coronavirus (COVID-19) pandemic.

FINRA is also providing regulatory relief to those firms that may not be able to meet regulatory filing deadlines due to the pandemic.

G. NAIC Coronavirus Resource Center.

The NAIC has established a robust website with links to additional information concerning the Coronavirus.

The website can be found through the following link:

https://content.naic.org/naic_coronavirus_info.htm

V. CEFLI Activities.

A. CEFLI Educational Summit Meeting - April 8 - Des Moines, Iowa – CANCELLED

CEFLI recently announced the cancellation of its Educational Summit Meeting scheduled to take place on April 8 in Des Moines, Iowa due to the concerns related to the Coronavirus (COVID-19). The Educational Summit Meeting was designed to review the key compliance requirements of the recent revisions to the NAIC Suitability in Annuity Transactions Model Regulation.

CEFLI is exploring the possibility of conducting these sessions “virtually” via a series of webinars in the coming weeks.

B. CEFLI Compliance Fundamentals Training Conference - May 6-8 - Nashville, Tennessee - POSTPONED.

CEFLI recently announced the postponement of its Compliance Fundamentals Training Conference scheduled to take place on May 6-8 in Nashville, Tennessee due to concerns related to the Coronavirus (COVID-19).

CEFLI is exploring possible dates for rescheduling the Compliance Fundamentals Training Conference later in the year.

C. CEFLI Webinar - Fraud Detection and Prevention - Wednesday, March 25 - 1 PM EDT/12 PM CDT/11 AM MDT/10 AM PDT.

CEFLI will be conducting the next session in its Educational Webinar Series to examine Fraud Detection and Prevention practices on Wednesday, March 25 at 1 PM EDT/12 PM CDT/11 AM MDT/10 AM PDT.

We hope you will be able to join us!

VI. Next Meeting.

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VII. Other Business.

There being no additional business the meeting was adjourned.

RISK ALERT
OFFICE OF COMPLIANCE INSPECTIONS AND EXAMINATIONS

April 7, 2020

Examinations that Focus on Compliance with Regulation Best Interest

In this Alert: *Examinations related to Regulation Best Interest.*

Key Takeaways: *After the compliance date, OCIE staff intends to engage in examinations to assess broker-dealers' implementation and operational effectiveness of Regulation Best Interest.*

I. Introduction

The Office of Compliance Inspections and Examinations ("OCIE")[1] is issuing this Risk Alert to provide broker-dealers with information about the scope and content of initial examinations after the compliance date for Regulation Best Interest.[2] Regulation Best Interest establishes a new standard of conduct under the Exchange Act for broker-dealers and associated persons of a broker-dealer (collectively "broker-dealers" or "firms").[3] When making a recommendation of any securities transaction or investment strategy involving securities (including account recommendations) to a retail customer,[4] a broker-dealer must act in the best interest of the retail customer at the time the recommendation is made, without placing its own financial or other interest ahead of the retail customer's interest.[5] This general obligation is satisfied only if a broker-dealer complies with four component obligations: a Disclosure Obligation, a Care Obligation, a Conflict of Interest Obligation, and a Compliance Obligation.[6]

After the compliance date, OCIE will begin examinations to assess implementation of Regulation Best Interest. These initial examinations, which will likely occur during the first year after the compliance date, are designed primarily to evaluate whether firms have established policies and procedures reasonably designed to achieve compliance with Regulation Best Interest. OCIE will also evaluate whether firms have made reasonable progress in implementing those policies and procedures as necessary or appropriate, including making such modifications

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1 This Risk Alert represents the views of the staff of OCIE. It is not a rule, regulation, or statement of the U.S. Securities and Exchange Commission ("Commission"). The Commission has neither approved nor disapproved its content. This Risk Alert, like all staff guidance, has no legal force or effect: it does not alter or amend applicable law, and it creates no new or additional obligations for any person.

2 On June 5, 2019, the Commission adopted Rule 15*l*-1 ("Regulation Best Interest") under the Securities Exchange Act of 1934 ("Exchange Act"), which has a compliance date of June 30, 2020. Exchange Act Release No. 86031 (June 5, 2019) ("Regulation Best Interest Adopting Release"). Additional information on Regulation Best Interest, including frequently asked questions, is available at: https://www.sec.gov/regulation-best-interest.

3 Regulation Best Interest Adopting Release at 19.

4 A "retail customer" is "a natural person, or the legal representative of such natural person, who: (A) receives a recommendation of any securities transaction or investment strategy involving securities from a broker, dealer, or a natural person who is an associated person of a broker or dealer; and (B) uses the recommendation primarily for personal, family, or household purposes." Exchange Act Rule 15*l*-1(b)(1).

5 Exchange Act Rule 15*l*-1(a)(1).

6 Exchange Act Rule 15*l*-1(a)(2).

as may be necessary or appropriate, in light of information gained from the implementation process and other facts and circumstances.

OCIE stands ready to work with firms and our colleagues in the Division of Trading and Markets on issues that may arise in the course of examinations and understands that the coronavirus disease 2019 (COVID-19) has created challenges for firms.[7]

This Risk Alert is not intended to be an explanation of the requirements of Regulation Best Interest. Firms are encouraged to familiarize themselves with the specific requirements of Regulation Best Interest by reviewing the Regulation Best Interest Adopting Release and the Small Entity Compliance Guide.[8] Questions regarding Regulation Best Interest may be directed to: IABDQuestions@sec.gov.

II. Examinations for Compliance with Regulation Best Interest

Initial examinations will focus on assessing whether firms have made a good faith effort to implement policies and procedures reasonably designed to comply with Regulation Best Interest, including the operational effectiveness of broker-dealers' policies and procedures. Examples of areas the staff may focus on are discussed below.

- **Disclosure Obligation**. The Disclosure Obligation requires a broker-dealer, prior to or at the time of the recommendation, to provide a retail customer, in writing, full and fair disclosure of:
    - all material facts relating to the scope and terms of the relationship with the retail customer; and
    - all material facts relating to conflicts of interest that are associated with the recommendation.[9]

  Specific Disclosures. Staff may assess how the firm has met the Disclosure Obligation's requirement to disclose material facts relating to the scope and terms of the relationship, including: (i) the capacity in which the recommendation is being made, (ii) material fees and costs that apply to the retail customer's transactions, holdings, and accounts, and (iii)

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[7] While the Commission and staff across Commission divisions and offices continue to monitor the effects of COVID-19 on market participants, including broker-dealers, the Commission has not extended the compliance date for Regulation Best Interest. OCIE staff remains fully operational nationwide and continues to execute its investor protection mission. *See* OCIE Statement on Operations and Exams (Mar. 23, 2020), *available at:* https://www.sec.gov/ocie/announcement/ocie-statement-operations-health-safety-investor-protection-and-continued.

[8] The Regulation Best Interest Adopting Release is available at: https://www.sec.gov/rules/final/2019/34-86031.pdf; the Small Entity Compliance Guide is available at: https://www.sec.gov/info/smallbus/secg/regulation-best-interest.

[9] Exchange Act Rule 15*l*-1(a)(2)(i) ("The broker, dealer, or natural person who is an associated person of a broker or dealer, prior to or at the time of the recommendation, provides the retail customer, in writing, full and fair disclosure of: (A) All material facts relating to the scope and terms of the relationship with the retail customer, including: (1) That the broker, dealer, or such natural person is acting as a broker, dealer, or an associated person of a broker or dealer with respect to the recommendation; (2) The material fees and costs that apply to the retail customer's transactions, holdings, and accounts; and (3) The type and scope of services provided to the retail customer, including any material limitations on the securities or investment strategies involving securities that may be recommended to the retail customer; and (B) All material facts relating to conflicts of interest that are associated with the recommendation.").

material limitations on the securities or investment strategies involving securities that may be recommended to the retail customer.

Document Requests. To assess compliance with this obligation, staff may review the content of the disclosures, and other firm records, to determine if the disclosures provide the required information to retail customers. Staff may also review the timing of the disclosures. Staff may review documents such as:

- Schedules of fees and charges assessed against retail customers and disclosures regarding such fees and charges, including disclosures regarding the fees and costs related to services and investments that retail customers will pay or incur directly and indirectly (*e.g.,* custodian fees, account maintenance fees, fees related to mutual funds and variable annuities, and other transactional fees and product-level fees);
- The broker-dealer's compensation methods for registered personnel, including (i) compensation associated with recommendations to retail customers, (ii) sources and types of compensation (*e.g.,* direct payments by an investor, payments by a product sponsor), and (iii) related conflicts of interest (*e.g.,* conflicts associated with recommending proprietary products or with receiving payments for inclusion on a product menu);
- Disclosures related to monitoring of retail customers' accounts;
- Disclosures on material limitations on accounts or services recommended to retail customers; and
- Lists of proprietary products sold to retail customers.

- **Care Obligation**. The Care Obligation requires a broker-dealer to exercise reasonable diligence, care, and skill when making a recommendation to a retail customer. The broker-dealer must understand potential risks, rewards, and costs associated with the recommendation. The broker-dealer must then consider these factors in light of the retail customer's investment profile and make a recommendation that is in the retail customer's best interest.[10]

  Document Requests. To assess compliance with this obligation, staff may review:

  - Information collected from retail customers to develop their investment profiles (including any new account forms, correspondence, and any agreements the customer has with the broker-dealer).
  - The broker-dealer's process for having a reasonable basis to believe that the recommendations are in the best interest of the retail customer (which may

[10] Exchange Act Rule 15*l*-1(a)(2)(ii) ("The broker, dealer, or natural person who is an associated person of a broker or dealer, in making the recommendation, exercises reasonable diligence, care, and skill to: (A) Understand the potential risks, rewards, and costs associated with the recommendation, and have a reasonable basis to believe that the recommendation could be in the best interest of at least some retail customers; (B) Have a reasonable basis to believe that the recommendation is in the best interest of a particular retail customer based on that retail customer's investment profile and the potential risks, rewards, and costs associated with the recommendation and does not place the financial or other interest of the broker, dealer, or such natural person ahead of the interest of the retail customer; and (C) 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.").

include, *e.g.,* any process for establishing, understanding, and implementing the scope of reasonably available alternatives when making a recommendation).

- The factors the broker-dealer considers to assess the potential risks, rewards, and costs of the recommendations in light of the retail customer's investment profile.
- The broker-dealer's process for having a reasonable basis to believe that it does not place the financial or other interest of the broker-dealer ahead of the interest of the retail customer.

- How the broker-dealer makes recommendations related to significant investment decisions, such as rollovers and account recommendations, and how the broker-dealer has a reasonable basis to believe that such investment strategies are in a retail customer's best interest.
- How the broker-dealer makes recommendations related to more complex, risky or expensive products and how the broker-dealer has a reasonable basis to believe that such investments are in a retail customer's best interest.

- **Conflict of Interest Obligation**. The Conflict of Interest Obligation requires a broker-dealer to establish, maintain, and enforce written policies and procedures reasonably designed to address conflicts of interest associated with its recommendations to retail customers.[11]

  Document Requests. To assess compliance with this obligation, staff may review the broker-dealer's policies and procedures to assess:

  - Whether and how the policies and procedures address the following, as required by Regulation Best Interest:
    - conflicts that create an incentive for an associated person to place its interest or the interest of a broker-dealer ahead of the interest of the retail customer;
    - conflicts associated with material limitations (*e.g.,* a limited product menu, offering only proprietary products, or products with third-party arrangements) on the securities or investment strategies involving securities that may be recommended to a retail customer; and
    - the elimination of the following conflicts: sales contests, sales quotas, bonuses, and non-cash compensation based on the sale of specific securities or specific types of securities within a limited period of time.

[11] Exchange Act Rule 15*l*-1(a)(2)(iii) ("The broker or dealer establishes, maintains, and enforces written policies and procedures reasonably designed to: (A) Identify and at a minimum disclose, in accordance with paragraph (a)(2)(i) of this section, or eliminate, all conflicts of interest associated with such recommendations; (B) Identify and mitigate any conflicts of interest associated with such recommendations that create an incentive for a natural person who is an associated person of a broker or dealer to place the interest of the broker, dealer, or such natural person ahead of the interest of the retail customer; (C)(1) Identify and disclose any material limitations placed on the securities or investment strategies involving securities that may be recommended to a retail customer and any conflicts of interest associated with such limitations, in accordance with subparagraph (a)(2)(i), and (2) Prevent such limitations and associated conflicts of interest from causing the broker, dealer, or a natural person who is an associated person of the broker or dealer to make recommendations that place the interest of the broker, dealer, or such natural person ahead of the interest of the retail customer; and (D) Identify and eliminate any sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sales of specific securities or specific types of securities within a limited period of time.").

- How the policies and procedures establish a structure for identifying the conflicts that the broker-dealer or its associated person may face. Staff may request documentation identifying all conflicts associated with the broker-dealer's recommendations.
- How the policies and procedures establish a structure to identify and assess conflicts in the broker-dealer's business as it evolves. Staff may request to see all policies and procedures in place during the scope period of the examination.
- How the policies and procedures provide for disclosure of conflicts and what conflicts are disclosed.
- How the policies and procedures provide for mitigation or elimination of conflicts and what conflicts are mitigated or eliminated.[12]

- **Compliance Obligation.** The Compliance Obligation requires a broker-dealer to establish, maintain, and enforce written policies and procedures reasonably designed to achieve compliance with Regulation Best Interest as a whole.[13]

  Document Requests. To assess compliance with this obligation, staff may review the broker-dealer's policies and procedures and evaluate any controls, remediation of noncompliance, training, and periodic review and testing included as part of those policies and procedures.

While these are the primary focus areas for the initial Regulation Best Interest examinations, staff may select additional areas for review based on risks identified during the course of the examinations. As part of OCIE's efforts to promote compliance, OCIE is including, as an Appendix to this Risk Alert, a sample request for information and documents to be reviewed during these examinations.

III. Conclusion

In sharing the focus for these initial examinations, OCIE encourages firms to assess their implementation plans for Regulation Best Interest. Not every document listed in this Risk Alert will be applicable to every firm, and OCIE will conduct examinations based on the profile of each broker-dealer. OCIE is providing transparency into its plans regarding Regulation Best Interest examinations to empower broker-dealers to assess their level of preparedness as the compliance date nears.

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[12] Under Regulation Best Interest, a broker-dealer must establish, maintain, and enforce written policies and procedures reasonably designed to mitigate or eliminate certain conflicts of interest. Conflicts related to incentives to associated persons must be identified and mitigated. Exchange Act Rule 15*l*-1(a)(2)(iii)(B). Conflicts related to any sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sales of specific securities or specific types of securities within a limited period of time must be identified and eliminated. Exchange Act Rule 15*l*-1(a)(2)(iii)(D).

[13] Exchange Act Rule 15*l*-1(a)(2)(iv) ("In addition to the policies and procedures required by paragraph (a)(2)(iii) of this section, the broker or dealer establishes, maintains, and enforces written policies and procedures reasonably designed to achieve compliance with Regulation Best Interest.").

This Risk Alert is intended to highlight for firms risks and issues that OCIE staff has identified. In addition, this Risk Alert describes risks that firms may consider to (i) assess their supervisory, compliance, and/or other risk management systems related to these risks, and (ii) make any changes, as may be appropriate, to address or strengthen such systems. Other risks besides those described in this Risk Alert may be appropriate to consider, and some issues discussed in this Risk Alert may not be relevant to a particular firm's business. The adequacy of supervisory, compliance and other risk management systems can be determined only with reference to the profile of each specific firm and other facts and circumstances.

APPENDIX

This document provides a sample list of information that the U.S. Securities and Exchange Commission's Office of Compliance Inspections and Examinations ("OCIE") may request when conducting examinations of broker-dealers regarding Regulation Best Interest. OCIE has published this document as a resource for broker-dealers. This document should not be considered all-inclusive of the information that OCIE may request or the validation and testing OCIE may perform of firm policies and procedures. Accordingly, OCIE will alter its requests for information as it considers the specific circumstances presented by each firm's business model. OCIE understands that not every document listed below will be applicable to every firm.

The following document requests apply to a broker-dealer's ("Registrant's") business units that may open accounts for and/or make recommendations to natural persons or their legal, non-professional representatives, including high net worth individuals, primarily for personal, family, or household purposes ("retail customers"). For purposes of this request, "Relationship Summary" refers to the document completed pursuant to Form CRS. In addition, broker-dealers should be aware that the "Scope Period" will differ for each examination and may include a time period prior to the compliance date.

A. General Information. To the extent applicable, provide the following information as of the date of this request and identify any changes made over the Scope Period (*e.g.,* under item 1, any account types introduced; and under item 6, any products that have been removed from the list).

1. Description of available brokerage account types that a retail customer may establish, including any limitations on the types of retail customers that may establish such account types (*e.g.,* high net worth only or based on minimum account values), the basic features of such account types, and any services or products (including account monitoring) associated with such account types.

2. Description of any non-brokerage accounts, including advisory accounts, that a prospective customer who is a retail customer may establish through an associated person of the Registrant, even if the account will be held outside of the Registrant.

3. Copy of any schedule of fees and charges that may be assessed for retail customers.

4. Copy of any grid or schedule given to registered personnel that sets forth a compensation method, which may be limited to registered personnel who provide services or recommendations to retail customers.

5. If not covered by the prior item, description of the compensation method used for registered personnel that may be paid by any third party. Include any additional compensation that may be paid for certain types of products or accounts, or based on certain earning levels.

6. A list of any proprietary products sold to retail customers.

7. A list of any third parties or affiliates with which the Registrant has arrangements for sale of their products to retail customers.

8. If the Registrant subjects any products or account types to a focused review to determine consistency with Regulation Best Interest or to consider potential modifications or limitations for consistency with Regulation Best Interest, a list of those products or account types.

9. If not covered by the items above, a list of any other products offered by the Registrant for sale to retail customers.

10. Copies of marketing materials given to retail customers, including any that use the term "adviser" or "advisor."

11. Documentation that identifies and analyzes all conflicts of interest associated with recommendations to retail customers.

B. Copies of all written policies, procedures, memoranda, or other materials (including changes made over the Scope Period) on which the Registrant relies for compliance with respect to Regulation Best Interest, which may include, for example, documents that:

1. Include the process, as applicable, to (a) identify and disclose; (b) identify and mitigate; and (c) identify and eliminate any conflicts of interest related to recommendations to retail customers.

2. Include the process to create, update, file, and deliver the Relationship Summary and other disclosures to be made to retail customers under Regulation Best Interest.

3. Include the process to make and document oral disclosures.

4. Include the process to obtain and update customer investment profiles.

5. Include the process to understand the risks, rewards, and costs associated with products offered to retail customers.

6. Include the process for identifying implicit hold recommendations.

7. Include the process for how the Registrant determines that it has a reasonable basis to believe that a recommendation is in the best interest of the retail customer.

8. Provide to registered personnel of the Registrant any considerations and limitations on making recommendations to retail customers (including when recommendations must be documented) and the disclosures that must be made to retail customers.

9. Provide any supervisory or compliance reviews or authorizations prior to recommending any account or product, including any rollovers from other accounts.

10. Include the process to monitor or surveil trading or account establishment for compliance with Regulation Best Interest.

C. Copy of the Relationship Summary provided to retail customers and all other documents provided to retail customers for the purpose of meeting the Disclosure Obligation under

Regulation Best Interest. If different documents are used for different types of retail customers (*e.g.,* based on business segment or account type), identify which documents would be given to each type of retail customer.

D. Copies of any training materials used to train employees on Regulation Best Interest.

E. Copies of any surveillance and monitoring reports designed to identify recommendations inconsistent with Regulation Best Interest, which may include any analysis of account type recommendations, rollovers, high account turnover, complex products, and high risk products.

F. For the Scope Period, provide:

1. A list of all new accounts established on behalf of individual customers (including new accounts established for existing customers), which may include some or all of the following: account identifying information; the date the account was opened; the date the Relationship Summary was delivered; the date any other documents were delivered for purposes of Regulation Best Interest and the type of document delivered; the type of account established; whether the account type was recommended; the registered person assigned to the account; and whether the assets in the account were transferred from another account at the Registrant or from a retirement account outside of the Registrant, and, if so, the type of account from which the assets were transferred.

2. A blotter containing all trading conducted on behalf of individual customers, which may include some or all of the following: the trade date; whether the trade was a purchase or sale; the security name; the CUSIP; the share quantity; the share price; account identifying information; the account type; whether the trade was solicited or unsolicited; and the name and CRD number of the registered person assigned to the account.

3. A list of retail customers for which a customer investment profile was created or updated, which may include some or all of the following: the date the information was received, account identifying information, and the types of accounts held at Registrant.

RISK ALERT
OFFICE OF COMPLIANCE INSPECTIONS AND EXAMINATIONS

April 7, 2020

Examinations that Focus on Compliance with Form CRS

I. Introduction

In this Alert: *Examinations related to Form CRS.*

The Office of Compliance Inspections and Examinations ("OCIE")[1] is issuing this Risk Alert to provide SEC-registered broker-dealers and investment advisers ("firms") with information about the scope and content of initial examinations after the compliance date for Form CRS.[2] Form CRS and its related rules ("Form CRS") require firms to deliver to retail investors[3] a brief customer or client relationship summary ("relationship summary") that provides information about the firm.[4] Firms must also file their initial relationship summaries (and any amendments) with the Commission, using the Central Registration Depository ("Web CRD") or Investment Adviser Registration Depository ("IARD"), as applicable, and post the current relationship summary on the firm's public website, if the firm has one. After the compliance date, OCIE will begin examinations to assess compliance with Form CRS. Initial examinations will focus on assessing whether firms have made a good faith effort to implement Form CRS.

OCIE stands ready to work with firms and our colleagues in the Divisions of Trading and Markets and Investment Management on issues that may arise in the course of examinations and understands that the coronavirus disease 2019 (COVID-19) has created challenges for firms.[5]

This Risk Alert is not intended to be an explanation of the requirements of Form CRS. Firms are encouraged to familiarize themselves with the specific requirements of Form CRS by reviewing

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1 This Risk Alert represents the views of the staff of OCIE. It is not a rule, regulation, or statement of the Securities and Exchange Commission ("Commission"). The Commission has neither approved nor disapproved its content. This Risk Alert, like all staff guidance, has no legal force or effect: it does not alter or amend applicable law, and it creates no new or additional obligations for any person.

2 On June 5, 2019, the Commission adopted Form CRS under both the Securities Exchange Act of 1934 ("Exchange Act") and the Investment Advisers Act of 1940 ("Advisers Act"), both of which have a compliance date of June 30, 2020. *See* Exchange Act Release No. 86032 (June 5, 2019) ("Form CRS Adopting Release"). Additional information on Form CRS, including frequently asked questions, is available at: https://www.sec.gov/regulation-best-interest.

3 A "retail investor" is defined as "a natural person, or the legal representative of such natural person, who seeks to receive or receives services primarily for personal, family or household purposes." Exchange Act Rule 17a-14(e)(2); Advisers Act Rule 204-5(d)(2).

4 *See* Exchange Act Rule 17a-14; Advisers Act Rule 204-5.

5 While the Commission and staff across Commission divisions and offices continue to monitor the effects of COVID-19 on market participants, including investment advisers and broker-dealers, the Commission has not extended the compliance date for Form CRS. OCIE staff remains fully operational nationwide and continues to execute its investor protection mission. *See* OCIE Statement on Operations and Exams (Mar. 23, 2020), *available at:* https://www.sec.gov/ocie/announcement/ocie-statement-operations-health-safety-investor-protection-and-continued.

the Form CRS Adopting Release and the Small Entity Compliance Guide.[6] Questions regarding Form CRS may be directed to: IABDQuestions@sec.gov.

II. Examinations for Compliance with Form CRS

Initial examinations of firms with retail investors conducted after June 30, 2020 may include an assessment relating to Form CRS. Examples of the areas the staff may focus on during examinations are discussed below.

- **Delivery and Filing.** Staff may (1) review whether the firm has filed its relationship summary, including any amendments, with the Commission and whether the relationship summary is posted on the firm's public website, if any; (2) evaluate the process for delivering the relationship summary to existing and new retail investors;[7] and (3) review policies and procedures to assess whether they address the required relationship summary delivery processes and dates. In particular, the staff may review records of the dates[8] that each relationship summary was provided to retail investors to validate whether the firm has complied with the following delivery obligations:
    - *Existing Retail Investors*. The initial delivery of the relationship summary to existing retail investors by July 30, 2020,[9] and before or at the time of:
        - The opening of a new account that is different from the retail investor's existing account;
        - A recommendation of a rollover of assets from a retirement account into a new or existing account or investment; or
        - A recommendation of a new brokerage or investment advisory service or investment that does not necessarily involve the opening of a new account and would not be held in an existing account (*e.g.*, a first time purchase of a direct-sold mutual fund through a "check and application" process).
    - *New Retail Investors*. The delivery of the relationship summary to new retail investors before or at the earliest of:
        - Entering into an investment advisory contract with the retail investor;
        - A recommendation to a retail investor of an account type, a securities transaction, or an investment strategy involving securities;
        - Placing an order for the retail investor; or
        - The opening of a brokerage account for the retail investor.
- **Content.** Staff may review a firm's relationship summary to assess whether it (1) includes all required information; and (2) contains true and accurate information and does

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6 The Form CRS Adopting Release is available at: https://www.sec.gov/rules/final/2019/34-86032.pdf; the Small Entity Compliance Guide is available at: https://www.sec.gov/info/smallbus/secg/form-crs-relationship-summary.

7 *See* General Instruction 10 to Form CRS.

8 *See* Exchange Act Rule 17a-3(a)(24); Advisers Act Rule 204-2(a)(14)(i).

9 Broker-dealers and investment advisers are required to deliver the relationship summary to existing customers and clients within 30 days after the date the firm must file the relationship summary with the Commission. Thirty days after the June 30, 2020 compliance date is July 30, 2020. *See* General Instruction 7.C.iv. to Form CRS.

not omit any material facts necessary in order to make the required disclosures, in light of the circumstances under which they were made, not misleading.[10] For example, the staff may review relationship summaries for information about:

- How the firm describes the relationships and services it offers to retail investors, including statements regarding account monitoring and investment authority.
- How the firm describes its fees and costs, including disclosures about the principal fees and costs that retail investors will incur, other fees and costs related to services and investments that retail investors will pay directly or indirectly, and examples of the categories of the most common fees and costs applicable to the firm's retail investors (*e.g.,* custodian fees, account maintenance fees, fees related to mutual funds and variable annuities, and other transactional fees and product-level fees).
  - Staff may review fee schedules, advisory agreements, and brokerage agreements and compare the fees listed in those documents against the fees listed in the relationship summary.
- How the firm describes the manner in which its financial professionals are compensated, including cash and non-cash compensation, and the conflicts of interest those payments create.
- How the firm describes its conflicts of interest, including incentives related to proprietary products, third-party payments, revenue sharing, and principal trading.
- Whether the firm accurately discloses if the firm or its financial professionals have legal or disciplinary history.[11]

- **Formatting.** Staff may review a firm's relationship summary to assess whether it is formatted in accordance with the instructions (*e.g.,* it includes particular wording where required, it uses text features where required, and it is written in plain English).[12]
- **Updates.** Staff may review a firm's policies and procedures for updating the relationship summary to: (1) assess how and whether a firm updates and files its relationship summary within 30 days after any information becomes materially inaccurate; (2) assess how and whether a firm communicates these changes to retail investors within 60 days after the updates are required to be made; and (3) assess the firm's process for highlighting to retail investors the most recent changes and including an exhibit highlighting or summarizing material changes with any filed updates.[13]
- **Recordkeeping.** Staff may review the firm's records related to delivery of the relationship summary, and the policies and procedures regarding record-making and recordkeeping, to assess how the firm complies with applicable delivery and recordkeeping obligations.

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[10] *See* General Instruction 2.B. to Form CRS.

[11] *See* Form CRS Items 2–4.

[12] *See* General Instructions 1-4 to Form CRS.

[13] *See* General Instruction 8 to Form CRS.

III. Conclusion

In sharing the focus for these initial examinations, OCIE encourages firms to assess their implementation plans for Form CRS. OCIE is providing transparency into its plans regarding Form CRS examinations to empower firms to assess their level of preparedness as the compliance date nears.

This Risk Alert is intended to highlight for firms risks and issues that OCIE staff has identified. In addition, this Risk Alert describes risks that firms may consider to (i) assess their supervisory, compliance, and/or other risk management systems related to these risks, and (ii) make any changes, as may be appropriate, to address or strengthen such systems. Other risks besides those described in this Risk Alert may be appropriate to consider, and some issues discussed in this Risk Alert may not be relevant to a particular firm's business. The adequacy of supervisory, compliance and other risk management systems can be determined only with reference to the profile of each specific firm and other facts and circumstances.

FINRA

News Release

April 08, 2020

Michelle Ong, (202) 728-8464

FINRA Statement on SEC's OCIE Risk Alerts for Reg BI and Form CRS

On April 7, 2020, the SEC's Office of Compliance Inspections and Examinations (OCIE) released Risk Alerts for Reg BI and Form CRS. These Risk Alerts set forth OCIE's expectations for firms' compliance with Reg BI and Form CRS and provide broker-dealers with information about the scope and content of OCIE's initial examinations following the compliance date of June 30, 2020. FINRA will take the same approach as set forth in the SEC Risk Alerts when FINRA examines broker-dealers and their associated persons for compliance with Reg BI and Form CRS. This initial approach will focus primarily on assessing whether firms have made a good faith effort to establish and implement policies and procedures reasonably designed to comply with Reg BI and Form CRS. However, as always, FINRA will take action in the event FINRA observes indications of customer harm or conduct that would have violated current standards (*e.g.*, suitability).

We also emphasize that we stand ready to work with firms and the SEC on issues that may arise in the course of examinations for compliance with Reg BI and Form CRS and understand that the coronavirus disease (COVID-19) has created challenges for firms. As with the SEC, we appreciate that implementation will be an iterative process, and our focus will be on firms continuing good faith and reasonable efforts, including taking into account firm-specific effects from disruptions caused by COVID-19.

FINRA Highlights Firm Practices from Regulation Best Interest Preparedness Reviews

On June 5, 2019, the U.S. Securities and Exchange Commission ("SEC") adopted Regulation Best Interest (Reg BI) under the Securities Exchange Act of 1934 ("Exchange Act").[1] Reg BI establishes a "best interest" standard of conduct for broker-dealers and associated persons when they make a recommendation to a retail customer of any securities transaction or investment strategy involving securities, including recommendations of types of accounts. The SEC also adopted new rules and forms to require broker-dealers and investment advisers to provide a brief relationship summary, Form CRS, to retail investors.[2] The compliance date for Reg BI and Form CRS is June 30, 2020.

Starting in late 2019, FINRA reviewed a set of small, mid-size and large firms to assess their preparedness for Reg BI and Form CRS. These assessments were not undertaken with the purpose of making findings of anticipated violations of Reg BI or Form CRS, but rather as a helpful dialogue with firms about their ongoing efforts and potential challenges. This report presents practices FINRA observed during those reviews and through ongoing conversations with firms about their preparedness initiatives. This report discusses information we obtained during our reviews (late 2019 to early 2020) and, as implementation is ongoing, firms likely have made further progress in preparing for Reg BI and Form CRS that may not be reflected by the particular elements described herein.

Additional Resources

Firms may find additional information regarding their obligations by referring to:

- SEC's Regulation Best Interest, Form CRS and Related Interpretations resources page;
- SEC's Frequently Asked Questions on Regulation Best Interest;
- SEC's Frequently Asked Questions on Form CRS;
- FINRA's Reg BI Topic Page; and
- FINRA's Reg BI and Form CRS Checklist.

Firm Practices Observed in Reg BI Preparedness Reviews

FINRA is sharing the following common practices we observed while conducting Reg BI preparedness reviews and other ongoing conversations with firms. We hope this helps firms assess their Reg BI initiatives and continue their work preparing for the compliance date.

1. Governance and Implementation Management – Firms developed governance structures to lead and manage Reg BI and Form CRS compliance requirements, including:

- **Project Teams and Working Groups** – Firms established project teams, workstreams or working groups either as part of a steering committee or as separate bodies reporting to the leadership team, including those that were:
  - Composed of multi-member steering committees representing multiple functions (at larger firms) or one or two designated staff (at smaller firms);
  - Structured around the four component obligations of Reg BI (*i.e.,* disclosure, care, conflict of interest and compliance) and Form CRS; and
  - Included representatives from multiple areas of a firm (*e.g.,* business units, compliance, legal and communications) (at larger firms).

- **Timelines** – Firms developed timelines and project plans for making the necessary updates, including:
  - Staggering deliverables by prioritizing either updates with longer implementation periods (such as changes that require technology or delivery methodology changes) or clear rule obligations and easier "quick win" items;
  - Developing reverse timelines by setting deadlines for major goals and working backwards to set intermediate goals;
  - Creating multistage review processes for all projects with an initial senior-level review of Reg BI impacts, development of detailed impact assessments and action plans, and executive review and sign-off on plans and execution near June 30;
  - Designating one or more individuals to update and review the various project teams' calendars and hold periodic (*e.g.,* weekly or monthly) meetings to keep the teams working towards and meeting target dates;
  - Running pilots to confirm that updates were working and can be rolled out by the compliance deadline; and
  - Developing contingency plans for the possibility that technology updates would not be ready by the compliance date.

- **Training** – Firms either started delivering training to staff and supervisors or were in the process of developing such training by, for example:

- Identifying vendors to provide training;
- Planning to train staff prior to the compliance date or later in the implementation process after completing all necessary policy, process and technology changes;
- Using a cross-functional approach to developing training plans, such as collaboration between training and corporate communications departments to determine relevant topics for overall firm communication and training plans; and
- Providing, or planning to provide, training through multiple channels, including newsletters or notices, "lunch and learn" events, dedicated in-person or on-line training, seminars or sessions at firm events (such as sales summits), as well as at regularly scheduled (*e.g.,* monthly) meetings between compliance and business units.

2. Written Supervisory Procedures (WSPs) and Supervisory Systems – Firms were developing written policies and procedures and implementing technological tools to meet their obligations under Reg BI and Form CRS, including:

- **Inventory of Changes** – Firms identified gaps for which new or amended policies and procedures or supervisory systems need to be developed, including:
  - Conducting the inventory by, for example, using "traceability" exercises to review their obligations under Reg BI and then trace those back to existing compliance policies to evaluate what, if any, changes needed to be made or whether new procedures must be created; and
  - Categorizing all required changes into tiers, where changes in earlier tiers would be completed prior to the completion of the following tiers.

- **WSPs** – Firms were planning to or had already made changes to their policies and procedures, but there was significant variation in the scope of these changes and firms' approaches to them, including:
  - Developing substantially new policies and procedures (or planning to do so);
  - Implementing modifications to existing policies and procedures (including but not limited to addressing 401(k) plan rollovers; documenting the risk, rewards and costs of recommendations of account types; and categorizing clients and products to determine if products are in clients' best interest); and
  - Relying primarily on either internal resources or outside consultants or counsel to revise existing or develop new policies and procedures.

Firms that had updated their policies and procedures, including to implement the now-vacated Department of Labor ("DOL") Fiduciary Rule, generally believed they could utilize this work and make limited modifications, particularly for obligations relating to:

    - Providing clear criteria to determine whether a particular recommendation is in a customer's best interest; and
    - Updating policies covering recommendations of account types when made in a broker-dealer capacity.

- **Technology Tools** – Even prior to completing their work on policies and procedures, firms initiated efforts to identify and develop supervisory system modifications, including:
    - Starting discussions with clearing firms and vendors about their systems' capabilities;
    - Leveraging existing technology tools to monitor compliance with Reg BI obligations by, for example, using existing trade monitoring systems to generate exception reports for excessive trading or unusual commissions or to block transactions; and
    - Rolling out systems, tools and reporting on a pilot basis prior to June 30 to confirm they are functioning correctly.

3. Conflicts of Interest – Firms were addressing conflicts of interest requirements by, for example:

- **Conflict Inventory** – Firms created inventories or logs of conflicts (some of which may have been previously developed), implemented automated tools to track, report and document existing conflicts and initiated reviews of controls to mitigate or eliminate those conflicts.

- **Conflicts Committees** – Firms relied on existing or created new Conflicts Committees that, for example:
    - Were composed of various functions, such as legal, risk, compliance, finance and business unit representatives, to identify existing or potentially new conflicts of interest, for example, if a firm introduced a new product, service or account;
    - Worked with other firm committees or sub-committees, subject matter experts and relevant Reg BI workstream(s) to address all new conflicts and changes to existing conflicts; and
    - Reviewed presentations by business lines about new products or services and related conflicts.

- **Limitations on Products** – Firms addressed conflicts of interest related to products, including:
    - Creating automatic point-of-sale alerts or "product menus" to organize products by risk;
    - Narrowing the selection of products available to registered representatives;
    - Placing additional restrictions on less experienced registered representatives; and
    - Prohibiting sales of specified products to all firm customers.

- **Compensation** – Firms planned to or had already started to address product sales that could result in the payment of

differential compensation. For instance, sales of proprietary products or products within a particular product category (*e.g.,* mutual funds or variable annuities) may offer higher compensation rates than other products. Firms addressed these conflicts, including:

- Adding compensation caps;
- Leveling the compensation across comparable products within a category;
- Making changes to compensation for certain product lines; and
- Addressing concerns about compensation directly with the product manufacturer or issuer.

Firms that had already changed their compensation practices in preparation for the DOL Fiduciary Rule generally believed they could leverage those changes, including:

- Leveling compensation across products (by, for example, creating a new product compensation model based on neutral factors, such as complexity, cost and time involved in selling each product); and
- Moving from trailing one-month to trailing twelve-month compensation grids.

- **Surveillance** – Firms updated existing account surveillance or created new surveillance tools to, for example:
  - Review for excessive trading or unusual commissions; and
  - Address conflicts of interest requirements, including compensation and other forms of recognition.

- **Disclosure** – Firms had either reviewed and updated existing, or created new, account documentation and customer disclosure forms by, for example:
  - Working with their internal technology departments, as well as outside vendors, to confirm revised and new disclosures would be available to customers;
  - Creating new schedules of commissions and fees for presentation to prospective customers;
  - Developing new processes and, as appropriate, implementing technology solutions to deliver required disclosures at the earliest triggering event, which could be when there is a "call to action" versus at account opening for prospective customers; and
  - Preparing summary fact sheets and templates for each product that educate registered representatives on the relevant conflicts of interest standards and other Reg BI implications for each product.

- **Use of the Terms "Adviser" or "Advisor"** – Firms implemented restrictions relating to the use of the terms "adviser" or "advisor," depending on the registration status of the firm or its associated persons by, for example:

    - Reviewing all of their marketing content to evaluate the use of "advisor" and "adviser;" and
    - Developing branch inspection programs and surveillance tools to review email, social media and other sources to confirm that registered representatives who are not investment advisory representatives obtained the relevant state licenses or used new titles.

- **Sales Contests** – Prior to the adoption of Reg BI or in preparation for the compliance date, firms had prohibited sales contests, sales quotas, bonuses and non-cash compensation practices based on the sales of specific securities or specific types of securities within a limited time period.

4. Form CRS – Firms had started developing their Form CRS and developing related delivery timelines by, for example:

- **Drafting** – Firms prepared and revised drafts of Form CRS, focusing on conforming to the size limitations and making the form simple to understand for customers. Some firms intended to seek feedback on such drafts from industry forums and conferences.

- **Timely Delivery** – Firms developed procedures and timelines to provide Form CRS to retail investors within required timeframes, including:
    - Working with internal technology departments, vendors, clearing firms and consultants;
    - Addressing concerns about providing Form CRS to prospective customers by considering the use of their web portals in the situations where disclosures would need to be provided, but the meeting place is not conducive to traditional delivery methods;
    - Evaluating customer needs, preferences and limitations when determining hard copy or electronic delivery methods; and
    - Developing processes to capture, supervise and audit the delivery of Form CRS (some larger firms created integrated approaches into their customer relationship management (CRM) systems that reflect the date Form CRS was delivered or a copy of the email sent to the retail investor).

FINRA shares this report to provide firms with information on how some firms are preparing for Reg BI and Form CRS. However, this does not imply that FINRA requires firms to implement any of the practices described above, nor that implementing any of the practices would constitute compliance with Reg BI and Form CRS. FINRA will continue to provide resources to firms to assist them with their efforts to meet the new compliance obligations.

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1 *See* Securities Exchange Act Release No. 86031 (June 5, 2019), 84 FR 33318 (July 12, 2019); *see also* U.S. Securities and Exchange Commission, SEC Adopts Rules and Interpretations to Enhance Protections and Preserve Choice for Retail Investors in Their Relationships With Financial Professionals (June 5, 2019) (providing overview of Reg BI and list of relevant SEC resources).

2 *See* Securities Exchange Act Release No. 86032 (June 5, 2019), 84 FR 33492 (July 12, 2019).