



# Duty of Care When Providing Investment Advice

## Important Disclosures

*Please carefully review the following disclosures and limitations of this course.*

- ❑ Although the sponsor of this course, RIA Compliance Consultants, Inc. (“Sponsor”), is an affiliate of a law firm and Sponsor may have an individual on its staff that is also licensed as an attorney providing legal services in a completely separate capacity, Sponsor is **not** a law firm and does **not** provide legal services or legal advice. A consulting relationship with Sponsor does not provide the same protections as an attorney-client relationship.
- ❑ This course is offered for educational purposes only and should not be considered an engagement with Instructor or Sponsor. This presentation should not be considered a comprehensive review or analysis of the topics discussed today. These educational materials are not a substitute for consulting with an attorney or compliance consultant in a one-on-one context whereby all the facts of your situation can be considered in their entirety.



***Key Point:** Taking this educational course does not create an attorney-client relationship or a compliance consulting relationship between you and your Instructor or the program Sponsor. If you have questions about your particular circumstances, we encourage you to discuss them with your compliance professional and/or your attorney.*

## Please Read Our Fine Print

- ❑ Instructor and Sponsor make all reasonable efforts to ensure the educational material is current and accurate at the time of presentation. Instructor and Sponsor are not be under an obligation to advise you of any regulatory developments or subsequent changes to educational material presented in this IAR CE course.
- ❑ Information provided during this course is provided "as is" without warranty of any kind, either express or implied, including, without limitation, warranties and merchantability, fitness for a particular purpose, or non-infringement. Instructor and Sponsor assume no liability or responsibility for any errors or omissions in the content of the presentation.
- ❑ There is no guarantee or promise that concepts, opinions and/or recommendations discussed will be favorably received by any particular court, arbitration panel or securities regulator or result in a certain outcome.



**Key Point:** *Laws and regulations change over time, and it is impossible to predict how a court, arbitration panel, or securities regulator will act in the future. After taking this course, you should be alert for future regulatory developments.*

## Keep in Mind...

- ❑ Communication with Instructor is not protected from discovery by third-parties during litigation or regulatory proceedings. Please keep questions during this course in a hypothetical form.
- ❑ Reviewing the slides and/or attending this course does not create a consulting engagement with RIA Compliance Consultants, Inc. A consulting relationship can be established only after the following two events have been completed: (1) our thorough review with you of all the relevant facts pertaining to a potential engagement; and (2) the execution of a written engagement and fee agreement and our advance receipt of any retainer required under such an agreement. The slides and/or course should not be regarded as a complete analysis of the subjects discussed. The information on these slides and in the course should not be relied upon as a substitute for one-on-one compliance advice. Often times, a party needs professional advice that applies to his or her specific situation. Your investment adviser firm should retain a compliance professional and/or attorney to provide you with specific guidance regarding your firm's situation.



*Key Point: Do not disclose confidential or proprietary information during this course. If you have questions about your particular circumstances, we encourage you to discuss them with your compliance professional and/or your attorney.*

Live Course  
Has Not Yet  
Been  
Approved  
by NASAA

RCC Has Submitted This  
Live Presentation to  
NASAA for Approval as an  
IAR CE Course

If Approved, RCC Will  
Contact Attendees About  
Next Steps for Obtaining  
IAR CE Credit

# NASAA Disclosure

**NASAA does not endorse any particular provider of investment adviser representative continuing education courses. The content of this course and any views expressed are our own and do not necessarily reflect the views of NASAA or any of its member jurisdictions.**



# Live Course Requirements

- ▶ **Login for Virtual Attendees** - You must be logged in during the live presentation under your email address.
- ▶ **View Entire Live Presentation** – You are required to watch the entire live presentation the course. If you do not watch the entire live presentation, you will have to watch the recorded version in its entirety.
- ▶ **Attendance Codes** - As you watch the live presentation, you will receive two attendance codes, each containing three alphanumeric characters. Save these codes. You will need to enter the full six-character attendance code prior to accessing the final quiz.
- ▶ **Login** – You will need to login into <https://www.CE4Advisers.com> and select this course.
- ▶ **IAR Acknowledgement** – Sign the IAR CE Acknowledgement & Attestation.
- ▶ **Final Quiz** - You must complete each lesson and receive a score of **70%** on the final quiz to receive IAR CE credit (assuming the course has been approved by NASAA).

# Content Questions & Technical Help

If you have questions about the content of this course or need technical help, please contact us via the email address below:

[ContEd@ria-compliance-consultants.com](mailto:ContEd@ria-compliance-consultants.com)



# Your Instructor



Bryan Hill, President  
RIA Compliance Consultants, Inc.

Bryan has over 28 years of experience working with investment advisers, broker-dealers and investors as a compliance consultant, attorney and executive.

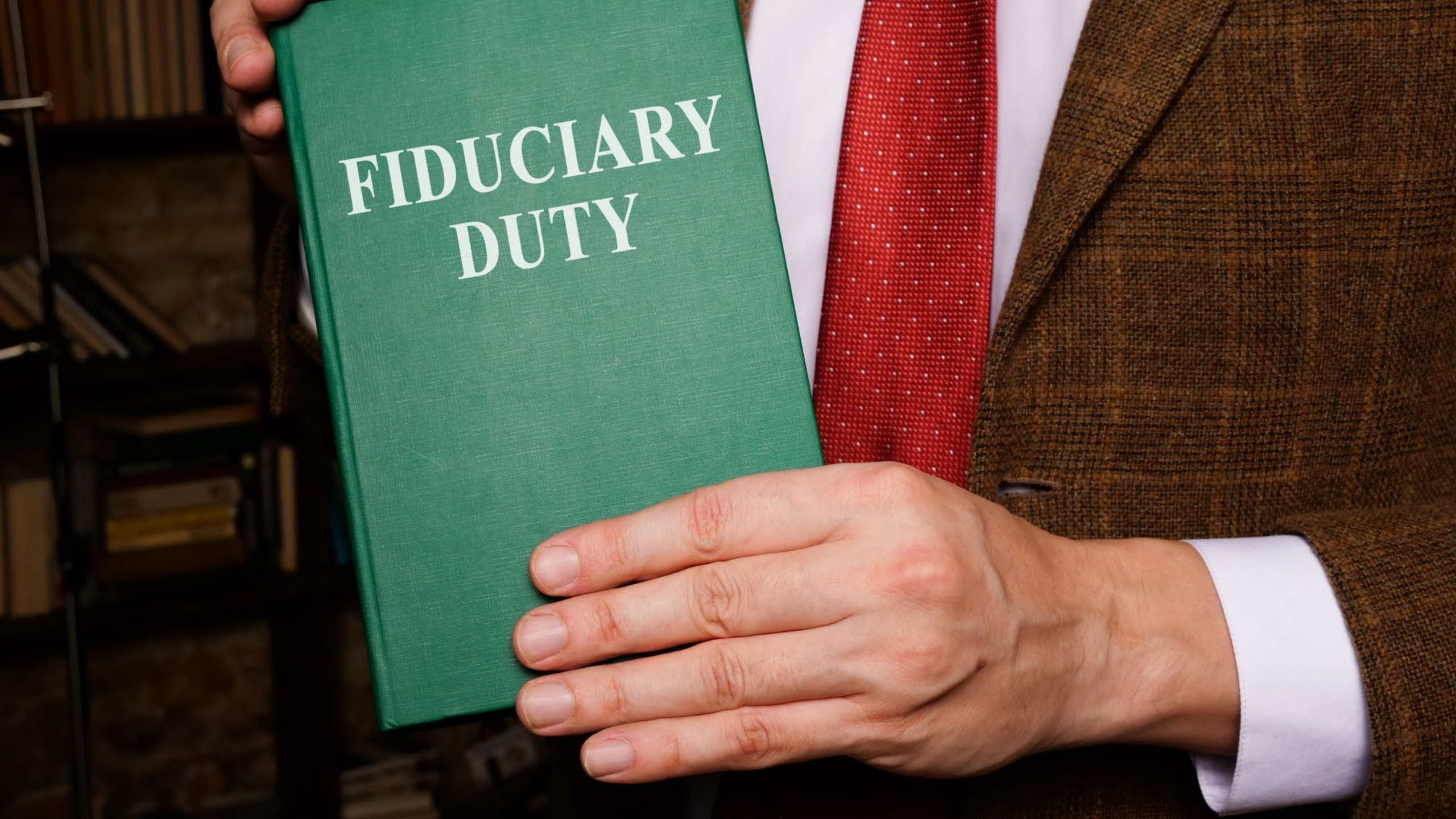
[bhill@ria-compliance-consultants.com](mailto:bhill@ria-compliance-consultants.com)

877-345-4034 x 101

# Course Overview

- ▶ **Fiduciary Duty Components**
- ▶ **Duty of Care**
  - **What Is Duty of Care**
  - **Acting with Care When Providing Investment Advice**
    - *Understanding Investments & Clients*
    - *Risks vs. Benefits*
    - *Available Alternatives*
  - **Best Execution**
  - **Ongoing Advice & Monitoring**
- ▶ **Questions**

**FIDUCIARY  
DUTY**



# Fiduciary Duty - Background

Investment Advisers Act of 1940 Effectively  
Creates a Federal Fiduciary Duty



However Not Specifically Defined by Statute or  
Rule



Fully Articulated by U.S. Supreme Court Case  
in SEC v. Capital Gains Research Bureau, Inc.

# Components of Fiduciary Duty Under IAA '40

Duty of Care

Duty of Loyalty

# Regulatory Resources

*Commission Interpretation Regarding Standard of Conduct for Investment Advisers (Effective 7/12/2019) @ <https://www.sec.gov/files/rules/interp/2019/ia-5248.pdf>*

*Staff Bulletin: Standards of Conduct for Broker-Dealers and Investment Advisers Account Recommendations for Retail Investors (3/30/2022) @ <https://www.sec.gov/tm/iabd-staff-bulletin>*

*Staff Bulletin: Standards of Conduct for Broker-Dealers and Investment Advisers Conflicts of Interest (8/3/2022) @ [https://www.sec.gov/tm/iabd-staff-bulletin-conflicts-interest#\\_ftn1](https://www.sec.gov/tm/iabd-staff-bulletin-conflicts-interest#_ftn1)*

*SEC Staff Bulletin: Standards of Conduct for Broker-Dealers and Investment Advisers Care Obligations (4/20/2023) @ [https://www.sec.gov/tm/standards-conduct-broker-dealers-and-investment-advisers#\\_ftn1](https://www.sec.gov/tm/standards-conduct-broker-dealers-and-investment-advisers#_ftn1)*

# Limited Focus

This Course Doesn't Cover the Duty of Loyalty  
Component of Fiduciary Duty Such as  
Identifying, Disclosing and Mitigating/Eliminating  
Conflicts of Interest

# What Is Duty of Care?

Duty to Provide  
Advice that Is in **Best  
Interest of Client**

Duty to Seek Best  
Execution of a  
Client's Transactions  
When the  
Investment Adviser

Duty to Provide  
Advice & Monitor  
Over Course of  
Relationship





Satisfying Duty of  
Care When Providing  
Investment Advice &  
Recommendations

# Understanding the Investment & Strategy

Investment Adviser Required to  
Make Independent & Reasonable  
Investigation of Security Before  
Recommending



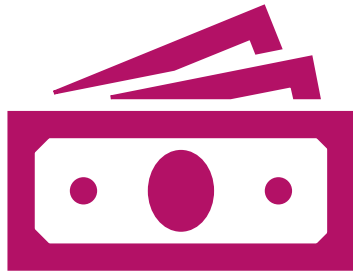
## Reasonable Investigation:

- Initial & Ongoing Costs
- Investment Strategy & Objectives
- Characteristics (including any special or unusual features such as tax advantages, guaranteed payments, margin call terms or early repayment of debt underlying a securitized product)
- Liquidity
- Risks and Potential Benefits
- Volatility
- Likely Performance in a Variety of Market and Economic Conditions
- Expected Returns, Expected Payout Rates & Potential Losses
- For Retail Investors, Role of Investment or Strategy within Actual or Anticipated Portfolio
- Time Horizons
- Costs of Exit

Reasonable  
Investigation

Where Providing  
Ongoing Advice &  
Monitoring, Required to  
Continue Analysis of  
Such Items Over Course  
of Relationship

# Must an Investment Adviser Recommend Lowest Cost Investment



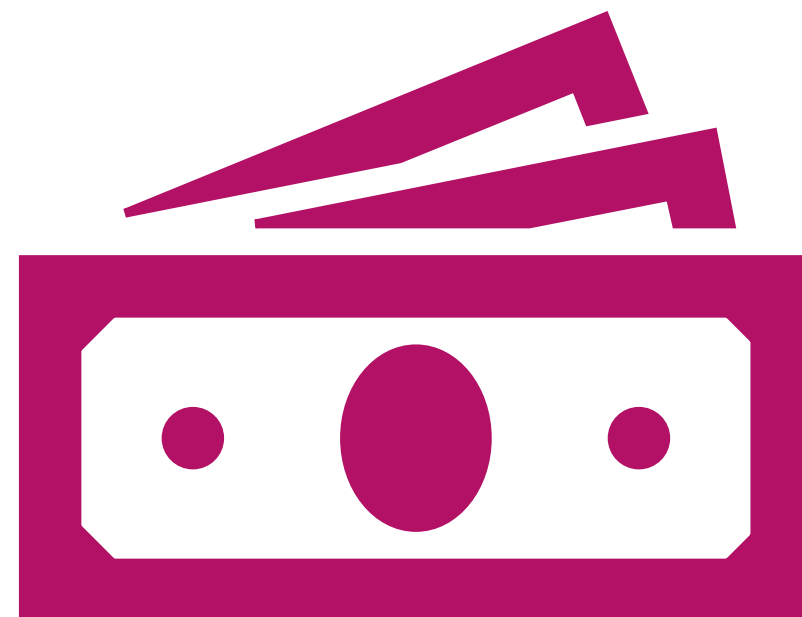
Best Interest Isn't Simply Advising Client to Invest in Lowest Cost Investment Without Any Further Analysis or Other Factors



"...[M]ust always consider cost as a factor when providing a recommendation or advice to a client."

## Should Consider Total Potential Costs Including Direct and Indirect Costs to Client

- ❑ Commissions, markups/markdowns and transaction costs
- ❑ Sales loads or charges
- ❑ Advisory or management fees
- ❑ Fees or expenses that may affect a client's return (e.g., Rule 12b-1 fees, administrative fees, revenue sharing and transfer agent fees)
- ❑ Trading and other costs associated with an investment strategy (e.g., options or futures contracts, margin interest, daily rebalance fees)
- ❑ Costs of exiting an investment or investment strategy (such as deferred sales charges or liquidation costs)
- ❑ Any relevant tax considerations
- ❑ Likely impacts of costs over client's expected time horizon



Can  
Investment  
Adviser  
Recommend  
Higher Cost  
Investment or  
Strategy?

- Yes, If Investment Adviser Reasonably Concludes that Other Factors Outweigh Cost & Making Such Investment or Strategy in Client's Best Interest in Light of Client's Objectives


# Example of High-Cost Investment Which May Be Consistent with Fiduciary Duty

It might be consistent with an investment adviser's fiduciary duty to advise a client with a high-risk tolerance and significant investment experience to invest in a private equity fund with relatively higher fees and significantly less liquidity as compared with a fund that invests in publicly-traded companies if the private equity fund was in the client's best interest because it provided exposure to an asset class that was appropriate in the context of the client's overall portfolio



# Can IAR Rely Upon Firm's Review of Investment or Strategy

No – An IAR Can't  
Satisfy Obligation by  
Solely Relying Upon  
Others at Firm



An IAR Is Responsible  
for Personally  
Understanding an  
Investment or  
Strategy Before  
Providing Advice or  
Recommending

# Client's Profile Should Include

Financial situation (including current income) and needs

Investments, assets and debts

Marital status

Tax status

Age

Investment time horizon

Liquidity needs

Risk tolerance

Investment experience

Investment objective and financial goals

Other information client may disclose related to the recommendation or advice

# Understanding Client for Comprehensive Financial Plan

*An investment adviser undertaking a comprehensive financial plan for a retail client would generally need to obtain range of personal and financial information about the client such as current income, investments, assets and debts, marital status, tax status, insurance policies and financial goals*

# Update Client's Investment Profile

Must Have a Reasonable Basis Believing Recommendation or Advice Is Not Based on Materially Inaccurate, Incomplete, or Outdated About the Client



Investment Adviser Needs to Update Retail Client's Investment Profile to Reflect Any Change Circumstances

- Frequency Depends Upon Facts and Circumstances

## What Does It Mean to Consider Client's Tax Status When Providing Advice or Recommendations?

- a. When Client Identifies a Goal with Tax Implications (e.g., saving for retirement or a child's education) or Seeks to Obtain a Tax Advantage (e.g., tax loss harvesting or limiting capital gains) as an Investment Objective, IAR Should Consider Whether Tax-Advantaged Option Is in Client's Best Interest
- b. Client's Tax Status Is an Important Consideration When Providing Advice Relative to Other Options
  - i. whether a fixed income investment pays taxable, tax-free, or deferred interest
  - ii. whether an out of state 529 plan is in the best interest of a customer who lives in a state that offers tax benefits for investing in the home state's plan
  - iii. whether a buy-and-hold or more frequent trading strategy is best for a particular account
- c. If Client Already Has 1 or More Tax Advantaged Investments, That Factor Generally Should Be Considered When Providing Advice or Recommendation About Another Tax-Advantaged Investment

# Examples of Required Risk-Benefit Analysis

For A Client With A Conservative Objective, Investing In Certain Derivatives May Be In Client's Best Interest When They Are Used To Hedge Interest Rate Risks In Client's Portfolio Whereas Investing In Directionally Speculative Derivatives On Their Own May Not

For A Client With A Conservative Objective, Investing In A Particular Security On Margin May Not Be In The Client's Best Interest, Even If Investing In That Same Security Without The Use Of Margin May Be In The Client's Best Interest

For Sophisticated Client Such As A Fund That Has The Appropriate Risk Tolerance, It May Be In The Client's Best Interest To Invest In Such Derivatives Or Securities On Margin

For High-Risk Investment (e.g., Penny Stocks, Thinly Traded Securities) – Investment Adviser Should Apply Heightened Scrutiny To Whether Such High-Risk Investment Fall within Client's Risk Tolerance & Objective

For A Complex Product (e.g., Inverse or Leveraged ETFs) Designed Primarily For Short-Term Trading For A Sophisticated Investor May Not Be in Best Interest of a Retail Client Absent an Identified, Short-Term, Client-Specific Trading Objective

# Reasonably Available Alternatives

Must consider alternatives that are reasonably available to achieve the client's objectives

Consideration should begin early in the process of formulating a recommendation

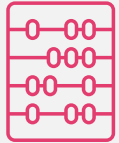
# Process for Identifying Reasonably Available Alternatives

Should have a reasonable process for identifying the scope of reasonably available alternatives

Analysis should begin with identifying investments consistent with client's profile, then narrowing to a smaller universe of potential investments

This includes guidance for IARs defining the scope of alternatives and the factors to be weighed in evaluating them





Reasonably available alternatives include those investments or investment strategies that could reasonably be offered by the firm and are consistent with the client's investment profile



Consideration should include the nature of the firm's business, customer base, relationship with customers, and the particular client's investment profile.

What  
Constitutes  
A  
Reasonably  
Available  
Alternative

# Single Best Alternative

No requirement to recommend the single "best" alternative

Multiple alternatives may be in the best interest of client

# Documentation of Consideration of Reasonably Available Alternatives



- While no specific requirement to document consideration, firms may choose to do so as part of their compliance policies
- Documentation may include the process for identifying and evaluating alternatives, and the basis for determining that a recommendation is in the best interest of client

# Proprietary Products

- Firms offering only proprietary products or a limited range of offerings must still consider reasonably available alternatives within that scope
- Firms must have policies and procedures to ensure that the limitations do not result in recommendations that place the firm's interests ahead of the client's interest.

# Complex Products




Firms recommending complex products must have a deeper understanding of the products and consider reasonably available alternatives



Policies and procedures must be in place to ensure that recommendations are in the best interest of the client, considering the complexity of the products

# Rollovers from Retirement Plans to IRAs

Must consider reasonably available alternatives when recommending rollovers from retirement plans to IRAs



Consideration should include the investment options, fees, expenses, services and penalties associated with both the existing plan and IRA

# Duty to Seek Best Execution

Where Investment Adviser Has Responsibility to Select B-D to Execute Client Trades

Adviser Must Seek to Obtain Best Execution of Transactions for Each of Its Clients Such That Client's Total Cost or Proceeds in Each Transaction Are the Most Favorable – Goal Is to Maximize Value

Maximizing Value Means More Than Minimizing Cost

When Seeking Best Execution, Investment Adviser Should Consider

Value of Research Provided

Execution Capability

Commission Rate

Financial Responsibility

Responsiveness to Adviser

Investment Adviser Should Periodically and Systematically Evaluate Execution for Clients

# Duty to Provide Advice & Monitor During Course of Relationship

Includes Duty to Provide Advice & Monitoring at Frequency that Is In Client's Best Interest of Client Taking Into Consideration Scope of the Client Agreement

Example – When Investment Adviser Has Ongoing Relationship with Client and Is Compensated with Periodic Asset-Based Fee, Investment Adviser Has Duty to Provide Advice and Monitoring As Is Consistent with Nature of Relationship.

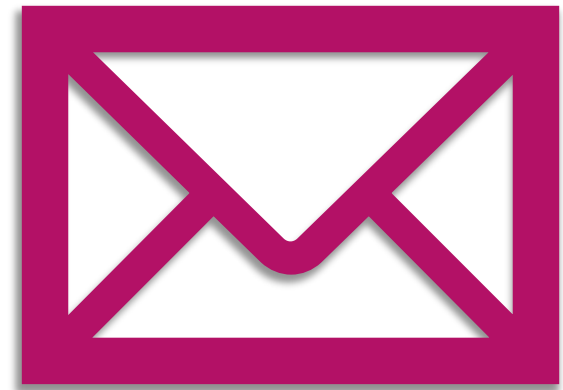
Example – When Investment Adviser Does Not Have an Agreement with Client Regarding Monitoring and the Relationship Is of Limited Duration (e.g., one-time financial plan for a one-time fee), Adviser Is Unlikely to Have Duty to Monitor



# Questions

Please submit any question online or email with any questions about the content of this course.

[ContEd@ria-compliance-consultants.com](mailto:ContEd@ria-compliance-consultants.com)



Thank You

