

The Second Circuit Hears the Reg BI Challenge Oral Argument

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A three-judge panel of the Second Circuit entertained arguments on June 2, 2020, in a lawsuit seeking to vacate and set aside the Securities and Exchange Commission's (SEC's) Regulation Best Interest (Reg BI). By way of background and in brief summary, Reg BI requires that broker-dealers make recommendations that are in the "best interest" of the retail customer, disclose conflicts of interest, and specify the services customers are receiving and the associated costs. As previously covered [in this blog](#), the plaintiffs initially challenged Reg BI in September 2019. Despite this pending legal challenge and brokerage firms' strained resources due to the pandemic and quarantining, SEC Chairman Jay Clayton said on April 2, 2020, in a public statement that the June 30, 2020, compliance deadline for Reg BI would remain.

At the oral argument, counsel for a group of investment advisers argued that Reg BI does not meet the expectations of the Dodd-Frank Act. They argued that Congress required the SEC to "harmonize" the investment adviser and broker-dealer regulatory regimes. Further, they argued that Congress intended for the SEC to extend the fiduciary duty imposed on investment advisers to broker-dealers, but the SEC failed to do so. Eight states represented by the New York attorney general's office at the argument joined in by advocating the view that Reg BI was contrary to law and exceeded the SEC's authority.

In their briefs, the plaintiffs had argued that in not rising to a fiduciary duty standard, Reg BI resulted in a regulatory regime similar to FINRA's suitability rule, and this offers less, not greater, retail investor protection. Along those lines, two of the judges on the Second Circuit panel noted at the argument that Congress had given the SEC discretion on whether to take any action at all. Thus, the SEC could have left the FINRA suitability standard in place. Among the arguments in response, the SEC argued that if Reg BI were vacated, the regulatory regime for broker-dealers reverts to the suitability standard, which would result in less investor protection.

With Reg BI's effective date less than 30 days away, we will monitor the Second Circuit closely for a ruling on this challenge to the regulation. As previously described in this blog, the SEC's Office of

Compliance Inspections and Examinations issued [a risk alert on April 7, 2020](#), providing guidance regarding its expectations for how it will examine for Reg BI compliance after June 30, 2020.

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