

Heed the New Guidance on Form CRS

Requesting brevity, the SEC explains how firms must answer questions in its Joint Statement.

On Oct. 8, the SEC released a Joint Statement Regarding New FAQs for Form CRS, which focused on the disciplinary history section of the Client Relationship Summary (Form CRS), which became effective earlier this year. I sat down with my colleague, Ryan Walter, to discuss the Joint Statement.

Ryan advised that the firms that need to pay special attention to the new guidance are those which have tried to provide extraneous or explanatory details of their own or their representatives' disciplinary history.

Under the Instructions for Form CRS, a firm must include the heading: "Do you or your financial professionals have legal or disciplinary history?" and answer "yes" or "no," depending upon whether the firm or any of its financial professionals has a triggering event. The Joint Statement made clear that "firms may not add descriptive or other qualitative or quantitative language."

On the same day as the Joint Statement was issued, the SEC amended its Frequently Asked Questions on Form CRS by adding four new questions and answers.

The first two FAQs made clear that: 1) firms may not omit the disciplinary history section, even if they and their representatives have no disciplinary information to report; and 2) the specific language of the disciplinary history section heading ("Do you or your financial professionals have legal or disciplinary history?") may not be altered.

The remaining two FAQs concern the requirement regarding the above heading pertaining to a firm or representative's disciplinary history, and to provide



a corresponding "yes" or "no" response. A number of firms were frustrated by this "yes" or "no" limitation, because it provides no real insight as to the details surrounding the underlying event. This called into question whether the answer is of any real value for a retail investor, and tends to disadvantage a larger firm.

For example, a firm employing 50 representatives, with no firm-level disciplinary history, could still be required to answer "yes" if a written client complaint was made against a single representative — regardless of the merits or ultimate outcome of the complaint. This is because client complaints alleging certain misdeeds are reportable on the Form U4 at Item 14.I.3, based on the terms of the complaint itself, with no consideration for the complaint's validity.

For firms that have tried to combat this limitation by providing explanatory details regarding their disciplinary history in the Form CRS, it may be time to re-think this approach. The FAQ states clearly this is not permissible:

In the staff's view, it *would not be appropriate* to add descriptive or other qualitative or quantitative language. Adding such language might

... obfuscate or otherwise minimize the disciplinary history. Accordingly, based on your facts, in the staff's view, it *would not be appropriate* to respond, for example, "No for our firm. Yes for only one of our 50 financial professionals."

Instead, the most leeway granted to firms is to draw a distinction between disciplinary disclosures concerning the firm and those concerning its representatives:

The staff would not object if a relationship summary includes a separate "yes" or "no" response for the firm (including relevant affiliates) and the firm's financial professionals. Accordingly ... the staff would not object if the firm included the following concise response "No for our firm. Yes for our financial professionals." or "Firm — no." "Financial professionals — yes."

Similarly, in circumstances where the firm (or relevant affiliates) has disciplinary history but none of the financial professionals does, the staff would not object if a relationship summary includes the following concise response: "Yes for our firm. No for our financial professionals." or "Firm — yes." "Financial professionals — no."

As if to leave no room for doubt, the staff concluded the new FAQs with the following (in pertinent part):

Q: If we answer "Yes" in Item 4, may we include additional information in our relationship summary to explain the disciplinary history?

A: No.

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