

THE REVIEW OF
**SECURITIES & COMMODITIES
REGULATION**

AN ANALYSIS OF CURRENT LAWS AND REGULATIONS
AFFECTING THE SECURITIES AND FUTURES INDUSTRIES

Vol. 52 No. 13 July 17, 2019

DIGITAL ADVICE PLATFORMS: COMPLIANCE AND LEGAL CHALLENGES

The SEC and FINRA have issued regulatory guidance for registered robo-advisers. The authors discuss this guidance with regard to various compliance issues, including disclosures for the business model, the scope of advisory services, and conflicts of interest. They also discuss the presentation of disclosures, suitability requirements, and compliance programs. They preface their discussion by noting the challenges of complying with Rule 3a-4 under the Investment Company Act, and close with several recent SEC enforcement actions against robo-advisers.

By Stephen P. Wink, Naim Culhaci and Deric Behar *

Robo-advisers, or digital advice platforms, have rapidly become a standard part of financial services offerings. Virtually every incumbent retail brokerage firm either has established or is planning to establish a digital advice platform, joining the pure FinTech players who pioneered this market. This turn toward robo-advisers is being driven by the potential for cost efficiencies, as well as the desire to connect with younger investors, who often prefer an online interface.

Over the past few years, regulators, lawyers, and compliance professionals have grappled with how to apply established regulatory concepts to the robo-advisory context, in which human involvement can be minimal to nonexistent. In this paper, we provide an overview of the digital marketplace for securities brokerages, discuss the SEC's and FINRA's guidance

for robo-advisers, and conclude with a review of recent regulatory enforcement actions in this area.

The digital marketplace for securities brokerages consists of roughly three models: (i) self-directed brokerages, where clients exercise full direct investment discretion over their online brokerage accounts; (ii) the pure robo-adviser model with little or no human interaction available, where discretionary asset management services are offered to clients through online algorithmic-based programs (investment decisions are digitally made for an investor based on various financial models and assumptions); and (iii) the hybrid robo-adviser model, typically characterized by a digital robo-adviser that also provides for periodic or optional meetings with a financial advisor. The hybrid model provides for semi-dedicated human relationships to exist in support of the digital advice.

*STEPHEN P. WINK is a partner at Latham & Watkins LLP. NAIM CULHACI is an associate and DERIC BEHAR is a knowledge management lawyer at the same firm. Their e-mail addresses are Stephen.wink@lw.com, Naim.Culhaci@lw.com, and Deric.Behar@lw.com. This article is of necessity summary in nature and should not be relied on as legal advice. The information contained in this article regarding specific legal or regulatory matters has been obtained from publicly available sources, and is current as of May 14, 2019.

INSIDE THIS ISSUE

- **SEC BREAKTHROUGH BRINGS DÉJÀ VU: LORENZO COURT RECLAIMS EXPANSIVE SCOPE OF FEDERAL SECURITIES LAWS, Page 157**