

FINRA Requests Comment on a Proposed Rule to Require Disclosure of Conflicts of Interest Relating to Recruitment Compensation Practices

There are many issues relating to this proposed rule. First is that although it seems on the surface to be protecting investors, it does little to achieve that. There are usually one of three reasons that an investor uses a particular broker: 1) they are a friend or relative, 2) they were referred to this broker by a friend or relative, or 3) the investor called the company and the company assigned a broker. Very few, if any, investors get the name of a broker from the yellow pages. Bottom line is that if a broker is doing well for his clients, they will follow him or her wherever they go.

In either of the first two instances, the fact that the broker is getting a bonus for moving his/her accounts is of little or no concern to the investor. In the third, the investor will probably not switch and ask for a new broker (unless the assigned broker has done a terrific job for the investor and then they will move with him or her anyway).

This rule seems meant only for the large firms that can afford to pay those outsized bonuses. Small firms cannot compete with the cash outlay of those large firms. Small firms would more than likely offer larger payout percentages to a broker because of the lack of cash. That would be just as much reason to let the client know about it, but the rule doesn't address it.

These large payouts are usually based on the trailing 12 months of commissions that were earned by the broker. Therefore, if some illegal commission inflating were going on, it had already occurred in the previous 12 months. If that is the case, then the previous firm should have been monitoring for churning or other illegal activity that would boost the commissions. So there are already rules and prohibitions that would cover these activities. Again, this rule does not address that.

Is it possible that the broker is moving because the new firm has a better trading department? Or better working conditions? Or a better computer system? Is better organized? Is a step up for their career? Or a hundred other reasons that would actually go along with the bonus? This rule doesn't address any of those reasons.

Is there no conflict of interest if a broker got a very large bonus and is staying at the same firm? Isn't it possible that the commissions earned by that broker were based on the same sort of illegal activities? This rule doesn't address that contingency either.

This rule seems to go along with a spate of new rules (some mandated by Dodd-Frank) that purport to protect investors but really don't. They just look good for public relations purposes. They go after the low hanging fruit, the worker bees of the industry – the brokers.

We don't ask our doctors why they switched hospital affiliations or how much they made last year. If we have a good lawyer, we don't ask them how much of a bonus they got to switch firms. These types of rules make it seem like all brokers are crooks.

It would seem to be more important to name names at the large firms when there is an enforcement action. The large firms seem to get away with just naming the firm when the small firms have everyone named – the CEO, CFO, CCO, COO and anyone else they can find. All firms, by FINRA rules, must list the supervisors in their WSP's. FINRA needs only to look at the WSP's and name some names. That would stop a lot of the illegal activities at these firms. When supervisors see that names are named, they have something to lose, it takes those fines out of the "cost of doing business" category and makes it personal. Those illegal activities effect a lot more investors than a bonus paid to some broker.

In sum, let's see some rules that actually mean something instead of rules that attract PR but have no substance. This rule has as little substance and investor protection as the new expanded broker check rules – low hanging fruit again.

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