



March 5, 2013

Via Electronic Filing

Ms. Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

Dear Ms. Asquith,

The University of Miami School of Law Investor Rights Clinic (“the IRC”) greatly appreciates the opportunity to comment on the proposed rule to require disclosure of conflicts of interest relating to recruitment compensation practices. The IRC submits this letter in regard to the proposed rule in Regulatory Notice 13-02 (“the Proposed Rule”) of the Financial Industry Regulatory Authority (“FINRA”) that would require specific disclosure by the recruiting member firms of the financial incentives a representative receives as part of his or her relationship with the new firm. The recruiting member firm would be required to provide the disclosure before a former retail customer of the representative makes a final determination to transfer an account to the new firm.

The IRC is a clinical program in which students provide representation to individuals of modest means who have suffered investment losses as a result of broker misconduct but, due to the size of their claim, cannot find legal representation. Under faculty supervision, law students provide legal assistance and advice to investors who may have claims involving misrepresentation, unsuitability, unauthorized trading, excessive trading, and failure to supervise, among other claims. For more information, please see <http://investorrights.law.miami.edu>.

Many member firms offer significant financial incentives to recruit registered representatives to join their firms, yet these compensation arrangements are not disclosed to customers when they consider transferring their accounts to a representative’s new firm. Requiring the broker to disclose their recruitment compensation package to clients will allow for clients to be fully informed of the financial incentives for the broker’s change of employers. Many brokers may represent the switch as being in the clients’ best interest, resulting from the new firm’s better capabilities or superior products, when in reality the lucrative financial package offered to the broker triggered the switch. Full disclosure of recruitment compensation makes the client fully aware of the broker’s potential conflict of issue at play. Disclosure of recruitment compensation may prompt savvy investors to review their last year of statements for potential misconduct aimed at increasing a broker’s production. Other investors may not be aware that most brokers’ compensation packages are based on that broker’s trailing twelve months of production

and that a broker's production is based on fees and commissions earned from client assets.

The IRC supports the aims of transparency and disclosure of the Proposed Rule, but would suggest certain modifications. First, notwithstanding the Proposed Rule's overall positive goal of investor protection, disclosure of recruitment compensation may have some unintended or negative results on uninformed investors because many customers considering the switch to follow their broker may have no idea how the industry works and may not be equipped with the proper information to fully understand their brokers' financial incentives for leaving his or her current firm. For example, disclosure of a broker's financial incentives may encourage current clients to follow brokers that receive significant recruitment compensation. Clients may conclude that if their broker is coveted by other financial institutions that are willing to pay the broker substantial recruitment compensation, they should continue using the broker's services. However, the fact that a broker has generated large amounts of revenues does not necessarily equate to that broker providing the best service to his or her clients.

To more fully achieve the purpose of the Proposed Rule, and to provide context to investors in interpreting the disclosed compensation, the IRC respectfully suggests that investors may benefit from educational material created by FINRA summarizing standard compensation practices in the retail securities industry. This educational material might address how brokers are typically compensated, including fee structures, commissions, and bonuses. This material could also provide some general explanation of the lateral movement of brokers from one firm to the next and briefly explain how firms generally calculate recruitment compensation to entice brokers to switch firms. Member firms should be required to distribute this educational material, or a link to it, either before or in conjunction with the compensation disclosure.

Second, the Proposed Rule restricts the disclosure requirement to brokers that change firms and does not extend to brokers who receive equally substantial retention compensation from their current firms. This practice raises many the same conflict of interest concerns as brokers leaving for new firms, yet these customers would not receive disclosure under the Proposed Rule. FINRA might consider enlarging the scope of the Proposed Rule to encompass retention packages offered to brokers by their current firms.

Third, the Proposed Rule leaves a gap when it comes to the protection of new clients. New clients to a broker who recently changed firms after being paid a bonus are equally vulnerable to potential sales practice violations committed by brokers seeking to hit lofty production goals, but these investors would not be made aware of the potential conflict of interest under the Proposed Rule. FINRA may wish to consider extending the scope of the Proposed Rule to new clients of a broker who recently changed firms and to limit the length of time that a broker would be required to disclose compensation information.

Fourth, the IRC submits that both individual investors and institutional investors should be given the same disclosure when considering whether to transfer their accounts

to a broker's new firm. Due to the level of assets held in institutional accounts, they are especially susceptible to misconduct aimed at increasing a broker's production. A small percentage increase in fees in an institutional account may contribute significantly to a broker's revenues. Brokers servicing institutional accounts may act upon incentives to churn these accounts to increase profits, thus leading to a greater recruitment packages.

Fifth, the Proposed Rule limits the required disclosure to compensation packages greater than \$50,000.00. Firms will be quick to adapt and restructure deals to evade the disclosure requirement, which would frustrate the purpose of the Proposed Rule. If firms structure future deals to avoid the disclosure requirement, FINRA may need to consider how much additional disclosure is necessary to protect customers and serve the purpose of the Proposed Rule.

Sixth, a broker's compensation information is not otherwise publicly available, and the Proposed Rule contains no provision protecting the confidentiality of this information. Many brokers and firms may take the position that this rule places brokers in an unfairly exposed position, and that brokers may decide to leave the retail space for positions in related areas of the securities industry, such as investment banking or institutional wealth management. This potential consequence would not benefit retail investors. Thus, the IRC supports the insertion of a customer confidentiality provision into the disclosure required by the Proposed Rule, with an exception to permit customers to share the information with an attorney, a financial professional, or an accountant for the purpose of consultation. Absent a confidentiality provision, broker-dealers may also complain that the Proposed Rule forces disclosure of confidential trade practices.

Seventh, the IRC submits that the disclosure process should be conducted in writing. Limiting the rule to written disclosure may prevent unnecessary disputes as to whether the proper disclosure was made and conflicting testimony in litigation.

The IRC is committed to investor education and protection and supports the Proposed Rule change and modifications stated herein. Disclosure by recruiting member firms of the financial incentives a representative receives as part of his or her relationship with the new firm places additional information relevant to investment decisions in the hands of the client. The Proposed Rule would lead to greater transparency into the industry and increased customer awareness of potential conflicts of interest relating to recruitment compensation. Thank you for the opportunity to comment on this proposal.

Respectfully submitted,



Practitioner-in-Residence, Investor Rights Clinic

James Schlosser
Legal Intern, Investor Rights Clinic