

Changes expected as Finra weighs controversial broker-comp rule

Wirehouses largely back recruiting incentive regulation but IBDs oppose it

By **Mark Schoeff Jr.**

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1 comment



Finra could soon act on a rule that would force brokers to reveal recruiting incentives to their clients, but the controversial regulation may undergo some changes on its way to final approval.

The **Financial Industry Regulatory Authority** Inc. has put the topic on the agenda for its Sept. 19 meeting, after bumping it off the schedule for its July meeting.

Under its original proposal in January, Finra would require brokers to disclose enhanced recruitment compensation — including signing bonuses, upfront or back-end bonuses, loans, accelerated payouts and transition assistance, among other arrangements — to any client they solicited for one year following their transfer to a new firm. The rule would not apply to incentives totaling less than \$50,000.

“My own guess is, it’s not going to go,” said Peter Chepucavage, general counsel at Plexus Consulting Group LLC. “The board is either going to table it or modify it.”

Whatever the Finra board decides Thursday will not be the last word. It may issue a revised proposal and ask for comments from its members or it could send the rule to the **Securities and Exchange Commission**, which would conduct its own comment period and possibly make its own changes.

Finra chief executive Rick Ketchum said the rule is designed to make potential conflicts of interest transparent to consumers.

“We believe investors should be informed of conflicts involving recruitment packages when they make the important decision to move an account, especially when the decision to move means having to sell off proprietary products and taking a possible tax hit,” Mr. Ketchum said in a speech this year. “When a broker moves to a new firm and calls a customer and says, ‘You should move your account

with me because it will be good for you,' the customer needs to know all of the broker's motivations for moving.”

The proposal generated 65 comments letters. Generally, large wirehouses came out in favor, while independent broker-dealers opposed it. [mssb.htm](http://topics.investmentnews.com/companies-and-associations/morgan-stanley-smith-barney-mssb.htm) title="http://topics.investmentnews.com/companies-and-associations/morgan-stanley-smith-barney-mssb.htm">Morgan Stanley Smith Barney LLC, for instance, argued that the rule would help protect clients. Cetera Financial Group said it would be too complex, difficult to implement and would violate brokers' privacy.

The **Financial Services Institute Inc.**, which represents independent broker-dealers and financial advisers, said it supports illuminating conflicts of interest, but asserted that the rule is flawed because it's too broad in one instance by including transition assistance and too narrow in another because it leaves out retention bonuses.

David Bellaire, the FSI's executive vice president and general counsel, anticipates that Finra will make changes.

“I would suspect we'll see that retention bonuses will be included in the rule and also that we will see Finra take a more principles-based approach,” Mr. Bellaire said. “It could put the burden on firms to identify recruiting practices that create conflicts of interest, and then give guidance on how to disclose them to investors.”

One broker recruiter wants the rule to die but concedes that that is probably wishful thinking.

“I believe Finra is hellbent to get this passed, and a case can be made that the wirehouses are behind it,” said Ron Edde, president and chief executive of Millennium Career Advisors. “They know it will suppress adviser movement. They'd like nothing more than to eliminate these bonuses. This is not popular among advisers in the field force.”

Another critic said that Finra's original rule would fail to achieve its objective of shining a light on potential compensation conflicts because it doesn't look at all of them.

“The way this has been drafted is silly,” said Brian Hamburger, president and chief executive of MarketCounsel LLC, a business and regulatory compliance consulting firm. “To only disclose the amount in recruiting deals takes off the hook those firms that are paying obscene amounts in retention deals. To only disclose this narrow subset of compensation practices is completely misleading.”

The premise of the rule is wrong, according to Mr. Edde.

“I have yet to see — nor has anyone else — a single shred of evidence where a client has been materially harmed by an adviser receiving a transition bonus for changing firms,” he said. “The public doesn't have a need to know everything.”

A better approach would be a more generic one, Mr. Chepucavage said. He would favor a simple disclosure by the adviser's new firm saying he or she may have received a significant bonus for making a job change. After receiving the notice, a potential client could delve further into the situation.

"It only applies to customers who are interested," Mr. Chepucavage said. "If they're happy with this rep, they're going to go with him. If they're not happy, they're going to stay at the old firm."



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