

Montana regulators target LPL REIT sales

Management at brokerage caught unaware by ongoing probe

By **Bruce Kelly**

Mar 24, 2013



LPL Financial LLC is being further dogged by state regulators investigating the sale of non-traded real estate investment trusts and faces a new complaint from the Montana Auditor's Department focusing on REIT sales to unsophisticated investors, according to a published report.

A story in last Friday's New York Times reported that Montana, which brought a case last year against LPL for failing to supervise a broker, is preparing a new case involving multiple brokers. The story also called into question the sophistication of LPL's broader compliance efforts.

Lucas Hamilton, a spokesman for the Auditor's Department, confirmed the state's concern about LPL brokers. "We do have more complaints" about LPL advisers than others, he said. He declined to comment on any investigation into the firm.

LPL's faulty compliance on REIT sales was first brought to light in December. That's when the Massachusetts Securities Division filed a complaint against the firm, alleging it failed to supervise registered representatives who sold nontraded REITs in violation of both state limitations and the company's rules.

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In February, the country's largest independent broker-dealer, with more than 13,000 contractor representatives and advisers, was ordered by Massachusetts to pay up to \$2 million in restitution to clients and a fine of \$500,000. Ameriprise Financial Inc. and LPL Financial are the two largest sellers of nontraded REITs, accounting for about 20% of the annual \$10 billion in sales of such investments.

A problem for LPL is that sales of alternative investments represent a growing stream of revenue. Commission revenue for alternative investments jumped 25% to \$143 million last year, from \$114 million in 2011.

As demand increases, regulators are watching how financial advisers sell the products more closely than ever. LPL was caught flat-footed by the comments of the Montana regulators in the Times article.

“We are not aware of any pending regulatory filings from the state of Montana and, in fact, were very surprised to read the comments from the Montana securities staff,” company spokeswoman Betsy Weinberger said.

“LPL Financial views compliance as a mission-critical function. Our long-term track record demonstrates the emphasis we place on regulatory compliance and our history of maintaining the highest standards of protection for the investors our advisers serve,” Ms. Weinberger said.

“We plan to increase our compliance staff by 10% in this year alone,” she said. In a letter to advisers last Friday, LPL's national sales manager, Derek Bruton, took issue with the Times article.

“We were disappointed with the disproportionate focus in the article on certain past compliance matters in Montana, as well as the one-year view of disciplinary actions taken against LPL Financial advisers,” he wrote. “That specific information falls far short of conveying a fair or accurate picture of the positive long-term track record of LPL Financial, including the firm's record in recent years, which, when compared against other major broker-dealers, ranks very strong.”

CHANGES TO OVERSIGHT

As a consequence of Massachusetts' investigation into its sale of nontraded REITs, LPL already has made some changes to the oversight of its alternative products, including nontraded REITs.

“In July of 2012, LPL changed its policies and procedures, creating a separate complex-products team to review all alternative investments,” according to the Massachusetts lawsuit.

In a move that shows how wary the firm has become of complex products, LPL this year also put restrictions on its advisers' sales of leveraged, inverse and monthly- reset mutual funds.

LPL's recent rash of compliance problems stem from inadequate oversight of its far-flung group of reps and advisers, according to the Times story.

State regulators, who operate as local cops on the beat, have long faulted the independent-broker-dealer industry for a shortcoming in overseeing its reps.



Bruce Kelly - Bruce Kelly covers the securities industry, with a focus on independent broker-dealers; please contact him if you have news, information or industry scuttlebutt to discuss.