DO INVESTORS KNOW WHAT THE PROTOCOL MEANS?

Tom Sedoric and Casey Snyder

October 2018

While we live in most uncertain times, one would like to be assured that "financial advisors" would act as fiduciaries for their clients - placing client needs before their own as well as their firm's needs.

Sadly, for too many investors, that has been and is now a costly assumption to make.

Transparency is the fundamental basis of trust. Transparency has become a pleasant "buzz word" used in our profession but it is more bandied about than practiced consistently.

Let's consider what has happened to the Protocol for Broker Recruiting established in 2004. The "Protocol" between major financial institutions and many smaller independent firms was instituted to facilitate the transfer of talent between firms. By 2017, more than 1,700 signatories (firms) had joined the Protocol. While there has been some transparent reporting in various trade publications in 2018 after the firms Morgan Stanley and UBS announced they were abandoning the Protocol, the public is largely unaware and uneducated of the implications of that decision. Both firms, in their polite way, have actually locked their advisors and their clients in place.

Stripped down to its basic elements, the Protocol was designed to smooth a financial advisor's transition from one firm to another amid a fierce competition for talent. The Protocol set standards as to how much client information an advisor can take with them when they transition to another firm, with the idea that specific guidelines would pave the way for less litigation and client disruption. Ideally, the protocol would balance the interests of firms, advisers, and, in our view most importantly, the investors who have trusted their hard-earned money to their advisors and the firms they represent.

The original draft of the Protocol also required the disclosure of the amount of up-front money or signing bonus an advisor would receive for changing firms. Sadly, that additional transparency provision never became finalized in the Protocol, the lack thereof increased the opacity of what an advisor receives when leaving one firm to join another.

While an imperfect system, the goal was to provide some stability in a market where successful advisors could listen to the needs of their clients and align themselves with the appropriate firm. A secondary benefit to the Protocol was reducing litigation costs between some of the largest investment firms. But, as illustrated in the latest lawsuit filed by Morgan Stanley against six departing Illinois advisors, that dam is beginning to burst.

We strongly agree with Phil Shaffer, the founder and chief executive of Halite Partners, who told the New York Times that "firms leaving the broker Protocol is very, very bad for clients. As ones who have tried to build our careers on a 'client first' mentality we believe this needs to be shouted from the mountaintops."

There are many balancing acts in our complex industry. We believe these big questions need to be clearly answered: Who actually owns the relationship with the advisor? Is it the client or the firm? Are advisors working in the best interests of their clients or do they focus on what's best for the firms that employ them? Are clients fully briefed on all of the financial incentives of their advisors?

Investors should ask why there has been no regulatory requirement for firms to be transparent, communicate and fully disclose to clients when a firm has left the Protocol resulting in a fundamental change in the relationship between clients and their advisor.

Earlier this year, our team changed affiliation from a major bank to a smaller dually registered investment firm. Our partnership with Raymond James Financial Services, Inc. through Steward Partners is no accident. Earlier this year at a conference in Florida, Tash Elwyn (President and CEO of Raymond James Associates) advocated for a Protocol 2.0 with even standards to meet the need of clients. "It's time to set aside lip service," Elwyn said. "If our profession truly cares about the well-being of our clients to the extent the profession professes, then we need to swing the pendulum in the other direction."

Through our dedication to continue to educate investors, we strive to insure our clients have no doubt who we represent and we are determined to help swing that pendulum in the right direction.

Does anything you've read trigger a question? Send us an email.

If you wish to share this with someone else please click here.

THE SEDORIC GROUP

of Steward Partners