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Breaking Bad Broker-Dealer Behaviors

Some IBDs are targeting advisors set to depart by playing hardball; here's a look at five specific tactics these firms are using.

When I formed our recruiting firm in 2001, we recruited advisors not only to independent broker-dealers but also to regional broker-dealers and wirehouse firms.

After six months, we made a conscientious decision to narrow our focus to recruiting to just IBDs.

We enjoyed conversing with staff with independent broker-dealers and their advisors, who tended to be more entrepreneurial and displayed a substantially lower "ego factor."

Working with IBDs was far less corporate—meaning more streamlined and less bureaucratic. In other words, working with them was a delight.

Having worked as a broker in the '90s at both Prudential Securities and Merrill Lynch, I found it to be a breath of fresh air to witness the cooperative environment between IBDs and their affiliated advisors, even when the advisors moved from one broker dealer to another.

The independent broker dealer had the task of supervision, processing business and perhaps supplying some services to help the advisor to operate more efficiently or grow their client base.

It was understood that the advisor's clients were indeed their own; they had control of their client relationships because of the trust and relationship they'd established with their clients over the years, not because of a broker dealer's branding.

If an advisor was dissatisfied or felt their BD was no longer a fit, they were free to move to a new firm unhindered.

To this day, our litmus test for deciding if a broker-dealer is truly independent is if its affiliated advisors are able to leave unfettered.

That independent spirit has been waning and is being substituted by a more captive, wirehouse approach, as IBDs have started to work around the system to hinder advisors from leaving their firm or to punish them on the way out.

To a large degree, IBDs don't employ these behaviors all the time. Instead, they seem to do so on a targeted basis in order to point out situations contrary to such criticism.

Recently we've seen IBDs targeting advisors leaving to join specific broker-dealers that appear to be especially successful at recruiting advisors from their firms in particular. These IBDs react by playing hardball in return and tend to employ these tactics:

1. They refuse to transfer Albridge data.

If you want to give advisor heart palpitations, not transferring their Albridge client data is one way to do so. When the broker-dealer can't be convinced to do the right thing and transfer this data to the new firm, the advisor oftentimes will need to lawyer up and fight back to get the data transferred.

This is one of the most spiteful actions for a broker-dealer to take, and it flies in the face of independence.

2. They don't pay residual fees, trails and commissions.

From the day an advisor gives notice of departure to their indie broker-dealer, the IBD they're leaving is required to continue to pay the advisor's residual fees, trailing fees and commissions for a period of 30-90 days.

The broker-dealer contract will specify the time, which 90% of the time is for 30 days.

In cases where an advisor owes the broker-dealer money, such as that tied to a forgivable note or to open litigation, it's understandable for the BD not to pay out residual income.

Otherwise not paying the advisor for the money earned during the contractual period is another way the BD can impose punitive action when an advisor leaves.

3. They break up departing groups of producing advisors.

We've witnessed large groups change BDs and lose up to half their advisors, who choose to stay behind.

It's one thing when an advisor doesn't want the inconvenience of moving BDs, but another when the original broker-dealer intervenes and offers carrots to team members to get them to stay.

Broker-dealers may go to war with a particular producer group (recently motivated to leave by the broker-dealer they're joining), and the gloves come off as the BD poised to lose advisors offer the following to get some in the group to stay:

- An enhanced payout, or even 100% payout for up to three years;
- Lowering their rep-directed advisory administrative fee percentage;
- Waiving broker-dealer expenses for 1–2 years; Albridge fee waivers;
- Rebate of Envestnet costs;
- Retention notes that are unusually high (20–25% of trailing012 gross dealer concession)

Office of Supervisory Jurisdiction groups and Super OSJ groups may have rep counts that can go into the hundreds; some also include a lead OSJ and several OSJs within a group.

Still, regardless of their size, they should be able to move freely to a new firm with all the advisors in their group.

If one of their advisors chooses to stay, that's (of course) their choice. But it isn't ethical for a broker-dealer to intervene at the time of exit and apply divisive tactics.

4. They assign clients to another advisor.

Although a less common occurrence in the IBD channel, this wirehouse tactic is employed by a few independent broker dealers that claim to be independent.

We've also had some advisors tell us that their prior firms made up false narratives about them and shared such stories with their clients in order to make clients feel insecure about moving away from the existing BDs and going to their advisor's new firms.

One broker-dealer firm has regional managers compensated with a year-end bonus tied to the amount of assets in their territory. Thus, it's from the regional manager that the orders to keep assets at the firm at any cost seem to trickle down.

5. They delay the release of a license to the new firm.

The old firm is required to release the advisor's license to the new firm within 30 days.

With the tactic of waiting the full 30 days before releasing the license, the BD's motive is to decrease the advisor's retention in the hope of increasing the number of orphan accounts that will then be swept into the prior BD's house accounts.

This is a petty vengeful tactic to employ, but it happens more frequently than you may think.

The Consequences of Bad Behavior

Broker-dealers that decide to cross over into these non-independent broker-dealer tactics risk poisoning their recruiting waters.

Not only do third-party recruiters like me zero in on such behavior, but wholesalers and advisors talk about this heavy-handed spiteful behavior, too.

Over time, an IBD's reputation in the recruiting world can be irreversibly damaged, no matter how much they offer in upfront dollars.

A good reputation is a broker dealer's most valuable possession, and the thinking that they can indulge in these tactics without impunity seems delusional.

When firms get into a pattern of ethical compromise, like the character Walter White in the series Breaking Bad, their moral compass becomes broken.

As they drift into rationalization, their reputation and recruiting ability can be irreversibly damaged as word hits the street about their non-independent behavior.

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