



May 1, 2007 12:00 PM

PLEASING ALL MASTERS

QUESTION:

I always live by the rule of “The Client Comes First.” But, sometimes I feel that my bosses are pushing in the opposite direction. What do I do when I feel a product or solution that is not proprietary is a better fit for my client, but my bosses are pushing me to sell our company products for the benefit of the company? I've always been a team player. But, being a team player often appears to clash with my motto of putting the client first.

ANSWER:

The question you raise and concerns you have are both legitimate and all too common in the securities industry. It's the classic push-and-pull of an industry that relies heavily on the advice of an individual who is earning a commission. Being a “team player” and “putting the client first” aren't incompatible, however.

Let's assume that you have a self-employed client in need of advice for his pension account. He speaks to you about his risk tolerance, his time horizon for investing and his prior experience in the market. After a thorough discussion, during which you've obtained all the relevant information, you research suitable investment recommendations. If there's no product, proprietary or otherwise, that addresses the specific needs of your client then your concern is a moot point. The conflict also doesn't exist if your firm does not have a proprietary product that suits your client's needs, but a suitable investment is available from an outside source.

The problem arises when you've got to choose between proprietary and non-proprietary investment products that both appear to fit your client's needs. How do you choose? NYSE Rule 405, known as the “Know Your Customer” rule, states: “Every member organization is required ... to use due diligence to learn the essential facts relative to every customer, every order, every cash or margin account ...” Additionally, the rule goes on to state that every member organization is required to “supervise diligently all accounts handled by registered representatives of the organization.”

Nowhere does the rule specifically prohibit the recommending of proprietary investments over non-proprietary products. Rather, Rule 405 specifies that a registered person is required to obtain all of the essential information available about a client prior to making a determination about the suitability of an investment recommendation. Moreover, part two of the rule places a heavy burden on the firm to oversee the activity of a registered person — you — to ensure compliance with the basic tenets of the rule. So, not only are you charged with knowing and understanding the needs of your client, your firm has an equal or greater burden to “diligently” supervise the accounts you serve to ensure compliance as well.

The fact that you may want to recommend a proprietary product does not automatically make it suspect and, thus, unworthy of recommending. If that were the explicit interpretation of the rule, then you, as the investment advisor, might be severely limited in the recommendations you could offer to a client. Your firm may have a product that is just the right fit, making it unwise for you to rule out suggesting it to your client.

If you find yourself in the quandary of what to recommend when there are both proprietary and non-proprietary products available:

- Make a careful and reasoned analysis of the choices.
- If, after this analysis is conducted, you believe that your client would be best served by the non firm-sponsored investment vehicle, you have an obligation to offer that investment to the client.

- Should your decision to offer a non company product be questioned by your supervisors, you might want to provide them with the analysis that you conducted on the firm's versus outside offerings.
- Highlight for them the basis for your recommendations.
- Underscore your desire to do the right thing — both as a team player who follows the rules, thus protecting the firm, and as an investment advisor who makes sound and suitable investment recommendations for his clients.

Jeffrey S. Feinberg, Esq.
Bernstein Nackman & Feinberg,
New York City, 212-709-8229.
jfeinberg@jsf-law.net