FINRA Plan on Outside Business Activities to Spark 'Much Debate'

Janet Levaux | March 08, 2018

FINRA office in New York. (Photo: Ron Pechtimaldjian)

The Financial Industry Regulatory Authority is likely to get pushback from large independent broker-dealers regarding the proposed rule floated Wednesday to free broker-dealers of liability over investment advisors' outside business activities.

While "cheers" will be heard from investment advisors "who have had to pay their broker-dealers a percentage of their advisory fees for required supervision," said Cipperman Compliance Services, "the larger independent broker-dealers will lobby heavily against this proposal as it cuts off a lucrative revenue source."

However, the plan "would help smaller regional firms that want to recruit reps but don't have the currently -required supervisory resources," Cipperman opined. "We expect much debate."

Indeed, Jon Henschen of BD recruiting firm Henschen & Associates told ThinkAdvisor in a previous interview that the plan is a "good-news, bad-news story."

The proposed rule on outside business activities seeks to streamline BDs' obligations by "generally excluding from FINRA's rule on a registered person's personal investments and work performed on behalf of a firm's affiliate," and eliminate supervisory obligations for non-broker-dealer outside activities, including investment advisory activities at an unaffiliated third-party advisor, Henschen explained.

The good part is that broker-dealers "will no longer have to track and most importantly have liability for RIA business," Henschen said.

The bad news: "The motive for taking a percentage payout on the RIA's advisory business will go away, leaving them only a profit center from commissions and trail business if the advisory assets are held away" at firms like TD Ameritrade and Schwab.

In announcing the proposed rule in Regulatory Notice 18-08, FINRA states that it's proposing a "single streamlined rule" to address the outside business activities of registered persons.

Under the proposal, third-party investment advisors would need to receive informed consent for their activities, but the BD would not have supervisory obligations.

The BD could impose certain requirements based on a required risk assessment of conflicts of interest and customer confusion. The proposal also limits BD obligations to supervise non-investment related activities.