



# **RIA's Are Increasingly Reaping the Benefits of the Protocol for Broker Recruiting**

Insights

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The Protocol for Broker Recruiting, which was implemented six years ago by three of the largest wire houses, is being embraced by RIA's and small and medium sized broker-dealers – a result that was unintended and unimagined at the time. In 2004, Merrill Lynch, Citigroup and UBS Financial Services formed the Protocol for Broker Recruiting (the "Protocol"). The Protocol is an agreement among a group of securities industry competitors to refrain from enforcing non-competes against brokers who move between signatory firms. Although the Protocol states that it was implemented to further clients' interests in following their broker from firm to firm, it is clear that the initial signatories were at least equally motivated to protect against potential claims by aggressive regulators who were concerned about the movement of private customer information among firms. Although other broker-dealers could, and were invited to join the Protocol, no one really expected that they would. Yet, six years after its inception, membership in the Protocol includes almost 550 firms, including the majority of the largest wire houses. Most surprising though is the trend of smaller broker-dealers joining the Protocol to obtain the secondary benefit that the Protocol provides - protection and predictability when hiring financial advisors.

## **What is the Protocol for Broker Recruiting?**

The Protocol is an agreement that essentially eliminates costly litigation by and between its participants. If a financial advisor leaves a member firm to join another member firm and follows the provisions set forth in the Protocol, there should not be any litigation against the broker or hiring firm. The provisions of the Protocol establish a procedure for transitioning between firms that, when followed, saves the recruit and his new firm from legal fees, an injunction, a possible damages award, and the uncertainty inherent in litigation.

The Protocol requires specific procedures for resigning and, most importantly, limits the customer information that can be taken by the departing financial advisor. Under the Protocol, prior to resigning, the financial advisor should prepare two lists: the first containing his or her customers' names, addresses, telephone numbers, email addresses and account types; the second containing all the information in the first, plus client account numbers.

The financial advisor must resign in writing to someone in management. When the financial advisor resigns, the advisor should provide the customer list containing the account numbers to someone in

management with their resignation letter. Again, the list provided to management should include account numbers even though the list being taken does not. The financial advisor can then take the other list to their new firm and use it to solicit customers to transfer their accounts. The Protocol provides that only the financial advisor is permitted to use the list taken from the old firm.

## **Benefits**

If a firm participates in the Protocol and counsels its recruits (who must also be coming from a Protocol firm) to follow these procedures, neither the firm nor its recruit will have to contend with any lawsuits or liability for claims such as breach of a non-solicitation agreement or misappropriation of trade secrets. In addition to eliminating litigation, there will not be any injunction prohibiting the recruit from contacting his or her clients, nor will any damages be assessed for clients who transfer. Membership in the Protocol saves the expense of litigation, eliminates the uncertainty of whether the recruit will be subject to an injunction and allows the recruit to unabashedly solicit their customers to transfer their accounts.

## **Potential Pitfalls**

The Protocol does not protect recruits and their new firms from all potential litigation, particularly when departing employees make common mistakes. Areas that still provide fertile ground for litigation include: pre-resignation solicitation, claims for amounts due under promissory notes, claims for training costs, violations of the Protocol, and raiding claims arising from group hires. Hiring firms should be clear that the recruit is not to solicit customers before he resigns and should only take the customer list to the new firm after he resigns.

Partnerships are another area of potential pitfalls. In many cases, the recruit will be part of a team or partnership at the old firm. If the entire team is not moving to the new firm, this can raise potential disputes and individual members must pay attention to the Protocol's rules for partnerships.

Recruits must also be counseled to leave behind all but the permitted information. This means that recruits with ACT databases or contact management programs must carefully plan their conduct with appropriate advice from counsel.

## **Escape Hatches**

The Protocol does not require perfection, but rather "good faith" compliance. Signatories to the Protocol agree to adhere to it in "good faith". In practice, firms have taken this language to mean that litigation should only ensue if the Protocol was flagrantly ignored. Further, in those cases, firms routinely work behind the scenes to reach an agreement as to a suitable "punishment" for those breaches and rarely resort to litigation. Moreover, when they do resort to litigation, they generally seek only to force compliance with the Protocol.

The final escape hatch provided by the Protocol is that firms can withdraw at any time. The Protocol merely requires that the firm “endeavor” to provide ten days prior notice.

A copy of the Protocol for Broker Recruiting is available in pdf format at the bottom of this post. While the trend of RIA’s and small and medium sized broker-dealers taking advantage of the Protocol may not have been expected, it has become the norm and is likely to continue as long as the benefits of being able to hire with minimal risk outweigh the downside when firms lose advisors. Firms seeking to participate should seek counsel familiar with the process to ensure compliance and maximize the avoidance of risk and litigation. Please feel free to comment on this post in the comment section below.

[Protocol For Broker Recruiting.PDF \(87.99 kb\)](#)

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