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JANUARY 11-15, 2021

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INDUSTRY LEADERS LOOK FOR ANSWERS TO WHAT 2021 MAY HOLD IN STORE

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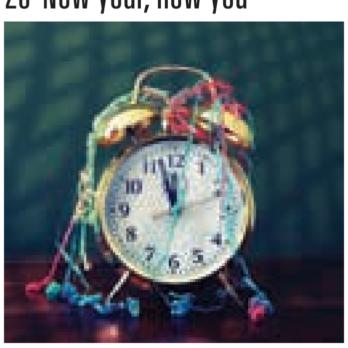
INSIDE

JANUARY 11-15, 2021

Regulators are taking a closer look at how Robinhood attracts novice investors to its platform.



Kristine McManus offers advisers new and different ways to measure their success in 2021.

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Advisers remain confident after riots rock U.S. Capitol

BY BRUCE KELLY AND STAFF

KEY POINTS

- A wide range of industry leaders were dismayed by the riot in the U.S. Capitol.
- They called attention to the resilience of the country and the economy.

THE BROAD FINANCIAL advice community, from planners to investment analysts to bank CEOs, expressed grave apprehension over the riot last Wednesday afternoon at the U.S. Capitol building that resulted in four deaths, one by gunshot, and an hours-long disruption of lawmakers' procedural vote to declare Joseph R. Biden the next president of the United States.

Concern, of course, is perhaps the least to be expected, but what stood out in comments last Wednesday evening and Thursday from the financial advice world was the calm and confidence expressed on the broad market, the economy and the country.

Financial advisers are, at heart, an optimistic group of people and believe in the future, and they were clearly distraught about the mob storming the U.S. Capitol building, which has not been breached since 1814, according to news reports.

"Yesterday's events were shocking and deeply saddening, and I join all those who pray that yesterday will prove to be the worst of this era," said Ric Edelman, founder of Edelman Financial Engines. "There is no evidence, however, that this abhorrent behavior by a select few will have any lasting impact on our nation's security and democracy."

"Nor will it interfere in efforts to eradicate COVID-19 and restore the American economy to its full potential," Edelman added. "On that basis we see no reason to make recommendations for chang-ing any financial planning or investment management strategies."

Another financial adviser said that he would reassure clients that Wednesday's Capitol riot showed that the rule of law held up. For instance, the Electoral College vote count was confirmed, and it's still against the law to break into a building. It's that same rule of law that ensures the integrity of the financial markets.

"The rule of law prevailed yesterday," said Brian O'Neill, founder of Winged Wealth Management and Financial Planning. "Rule of law under-

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LPL fined $6.5M by Finra over lax supervision

BY BRUCE KELLY

THE FINANCIAL Industry Regulatory Authority Inc. closed out 2020 by hitting LPL Financial, the largest independent broker-dealer in the industry, with a $6.5 million fine on Dec. 31 for shortcomings in a variety of supervisory issues, ranging from record keeping to fingerprinting of non-registered employees and supervision of advisers' consolidated reports.

One former LPL broker exploited the weak supervision of consolidated reports, essentially documents that summarize customers' assets, to send reports containing fictitious assets to several LPL customers as part of a $1 million Ponzi scheme, according to Finra.

$70M
FINES AND RESTITUTION PAID BY LPL IN 2014 AND 2015

The broker, identified only as JTB in the settlement, was eventually arrested and pled guilty to securities fraud, according to Finra. The broker ran the fraudulent scheme while he was registered with other firms and not just LPL, Finra noted, and LPL has paid restitution to clients harmed in the matter.

LPL has a history of compliance problems and coming under scrutiny from regulators like Finra and states. In 2014 and 2015 alone, the firm

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Merger mania hits RIAs as $160B in assets changes hands in 2021

BY BRUCE KELLY

AFTER ENDING 2021 at a fevered pitch, registered investment adviser dealmaking started 2021 with a bang and boom last week, with eight significant deals announced and a total of $159.6 billion in assets under management changing hands.

Among the buyers and sellers were some of the most significant names in the burgeoning RIA industry.

Chicago-based aggregator Hightower kicked off the action last Monday morning announcing its largest acquisition ever, the purchase of Bel Air Investment Advisors, an $8 billion wealth management firm based in Los Angeles. Also last week, Mercer Global Advisors scooped up two RIAs in Atlanta with a total of $1.6 billion in assets.

But the largest transaction was announced last Tuesday, when Aquiline Capital Partners said it had purchased a majority stake in Sageview Advisory Group, which has $119 billion in assets under advicement, representing the latest major investment by a private equity firm in a large retirement adviser firm.

That deal was completed before the end of the year, signaling that buyers and sellers wanted to complete transactions before the switch to a Democratic administration and a potential tax hike.

"There were definitely a number of sellers who were motivated to get deals done before the end of 2020, with the potential for the Biden administration to increase capital gains taxes and reduce net proceeds retained by sellers. Dec. 31 was something of a finish line for deals that were in progress for the better part of last year," said Mark Bruno, managing director at Echelon Partners. "It's important to note that deals don't come together in a matter of weeks or months, so the change in administration was an accelerator, but obviously not the lone motivator."

MOTIVATED SELLERS AND BUYERS

Motivation has apparently been abundant among RIA buyers and sellers. Late last Monday, Boston Private Financial Holdings said it was being acquired by SVB Financial Group, creating a $17.7 billion wealth management enterprise.

Last Wednesday, Truist Financial Corp. said it sold its $10 billion 401(k) unit, with OneDigital buying the investment advisory relationships and Empower Retirement and Ascensus taking on portions of the firm's record-keeping business.

Also on Wednesday, storied East Coast wealth management firm Rockefeller Capital Management said it was expanding its Midwest footprint with the acquisition of Whitnell & Co., a $1.4 billion multifamily office based in Chicago.

Finally, last Thursday, Captrust Financial Advisors said it was adding Phoenix-based MRA Associates, a 59-person firm with $3.3 billion under management.

The flurry of RIA dealmaking activity last week was no surprise, Bruno said.

"Given that most deals take nine to 12 months to execute, if not longer, from beginning to end, we expected to see 2020 end with a larger-than-normal amount of activity," he said.

Bruno pointed to Echelon's research showing that there were 69 transactions in the final quarter of 2020, a new record for a single quarter and a 25% increase over the previous quarter.

"For context, the second half of 2020 was by far the most active period of M&A on record for the wealth management industry," he added.

bkelly@investmentnews.com

Are advisers investing their clients in Bitcoin as cryptocurrencies soar to new highs?

BY NICOLE CASPERSON

THE POPULARITY OF cryptocurrencies is gaining steam, with large industry players ramping up offerings tailored to institutional investors, and the growing investor demand is expected to soon spill over to financial advisers.

Bitcoin jumped 50% in December alone, then repeatedly hit new records over the course of last week, approaching $42,000 on Friday morning, according to Bloomberg.

There has been increased institutional adoption of digital assets, with 36% of institutions surveyed invested in the asset class and more than six in 10 investors agreeing that digital assets have a place in portfolios, Fidelity research shows.

In that light, Fidelity Digital Assets announced a new offering that enables advisers on Fidelity's institutional-grade digital assets custody platform to pledge bitcoin as collateral for cash loans. While Fidelity's offerings cater to institutional investors, the expectation is more advisers will become interested, said Christine Sandler, head of sales and marketing at Fidelity Digital Assets.

The Fidelity unit, which launched in 2018, currently has 100 firm clients,

including registered investment advisers, family offices, hedge funds and banks, Sandler said. The custodian is also working to eliminate some of the inherent frictions for advisers looking to hold Bitcoin in a portfolio, she said.

The investor interest in digital assets is not just institutional, as Blockchange is also looking to bring cryptocurrencies down to RIAs by rolling out its digital asset management platform designed for advisers in July.

The cloud-based investing platform gives advisers discretionary investment management over digital assets, including Bitcoin, Ethereum, Bitcoin Cash and Litecoin, among others, purchased through a qualified custodian and exchange.

Even with the interest from institutional investors, advisers remain skeptical of Bitcoin and other digital assets for individual investors, arguing cryptocurrencies' short historical record is too murky to trust in clients' portfolios.

"I caution my clients against speculating in digital currencies," said Matt Morris, an adviser with Sanderling Finance. "A broker may argue its suitability for a particular client, but I don't think financial advisers operating under a fiduciary standard have any grounds to recommend it."

The problem with digital assets is that the risks and rewards aren't quantifiable, he said. There are other alternatives that have a more robust history and are subject to additional regulation to promote investor safety. The products also perform based on quantifiable data, like earnings, dividend payout and book value, Morris said.

Lack of guidance on custody is likely slowing adoption as lawmakers urge the SEC to clarify how brokers can hold digital securities.

Still, cryptocurrency advocates point out that the digital currency is a noncorrelated asset class that can serve as a safe store of value when markets

CONTINUED ON PAGE 22

2 more states adopt the NAIC's annuity rule

BY MARK SCHOEFF JR.

THE NEW YEAR IS beginning with momentum for a state-level regulation designed to strengthen consumer protections surrounding annuity sales.

In the final week of 2020, Arkansas and Michigan became the most recent states to adopt the rule, which is based on a model measure approved last February by the National Association of Insurance Commissioners. Other states that have approved the rule are Iowa, Arizona and Rhode Island.

The rule amends the NAIC annuity suitability rule to clarify that annuity recommendations by insurance agents and carriers must be in the best interests of consumers and that salespeople cannot put their financial interests ahead of those of the consumer. The model rule requires that salespeople act with "reasonable diligence, care and skill."

The model rule is similar to the Securities and Exchange Commission's new investment advice standard for brokers — Regulation Best Interest — that went into force on June 30. SEC rule does not cover transactions involving insurance products.

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Robinhood opens the regulatory revolving door

Robinhood Financial has determined that it takes a regulator to deal with the regulators.

The online trading platform's popularity has skyrocketed over the last several months, as people use its app and website to buy and sell investments — often for the first time.

But its fast growth also has generated increased regulatory scrutiny.

In December, Robinhood agreed to pay $65 million to settle Securities and Exchange Commission charges that it did not execute trades at the best prices for its customers because of agreements to send its order flows to certain firms.

KEY POINTS

- Robinhood hired a former regulator as its chief legal officer as it faces scrutiny.
- But questions can arise when ex-regulators join private firms.

In a separate action, Massachusetts Secretary of the Commonwealth William Galvin charged Robinhood with violating the state's new fiduciary rule by the way it targets users, entices them to trade and fails to maintain the platform's infrastructure.

Earlier this year, members of Congress pressed Robinhood to increase investor protections on its platform in the wake of the suicide of one of its users.

The person leading Robinhood's response to the regulators and lawmakers is former SEC Commissioner Daniel Gallagher Jr., who became the firm's chief legal officer in June.

D.C.INSIDER
MARK SCHOEFF JR.

Previously a Robinhood board member, Gallagher moved to a daily role to help build its legal, compliance and government relations operations.

"We've made so many meaningful improvements at Robinhood just in 2020 to the control environment," Gallagher said. "We're in a really good place right now."

Robinhood founders Vladimir Tenev and Baiju Bhatt seem to have brought the same intensity to shoring up the firm's compliance function that they did to developing its technology.

"They had this vision for best-in-class legal and compliance and thought I was the one who could help them do it," Gallagher said.

But his work at the SEC — as a commissioner from 2011 to 2015 and as a staffer and co-director of the Division of Trading and Markets from 2008 to 2010 — means that Gallagher's move to the private sector has taken him through the revolving door.

Whenever that door swings back and forth with people going from government agencies to financial firms and vice versa it increases the possibility of regulatory capture.

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More money, more problems: Planning for lottery winners

BY EMILE HALLEZ

A FEW VERY lucky lottery players could find themselves with newfound fortunes this week, with Powerball and Mega Millions jackpots each at more than $400 million.

And a few financial advisers might also find themselves with valuable new clients.

Regardless of whether there is a single winner in each lottery or if the jackpots are split among multiple people, the prizes are large — as are the risks of not having a solid financial plan.

Some big lottery winners reportedly end up going bankrupt, and there are many instances of other misfortunes that have followed such windfalls.

A GOOD PLAN

Four years ago, financial adviser Diane Pearson got a call from a prospect who did not want to disclose any information over the phone. At the following in-person meeting, the woman and her husband told Pearson that she won a $1.2 million lump sum in a Pennsylvania state lottery. Pearson, the new client said, was the third person to find out.

"They had not told anyone — no one in their family. This was really well thought out," said Pearson, whose firm is Pearson Financial Planning. "That's exactly what I would do — sit down with an adviser and put a game plan together." That plan included an updated estate plan and ensuring they had proper insurance coverage.

At the time, the couple had a combined income of about $80,000 — she as a drugstore co-manager and he as a grocery store co-manager, Pearson said.

"This was changing their lives forever, and they kind of knew that," she said. "They wanted to be prepared and make the right decisions up front, instead of blowing it."

That couple, now in their mid-50s, has upgraded houses and paid off a child's student loans. The woman quit her job, and the man will be able to retire a little early, at 62, Pearson said.

Adviser John Bovard, who recently founded Incline Wealth Advisors, compares lottery winners to professional athletes — people experiencing sudden wealth that, if it's not carefully planned for, can vanish

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Bob Doll's 2021 predictions

Nuveen's chief equity strategist offers a divided outlook for the global economy and markets this year.

1. U.S. real GDP will grow at its fastest pace in 20 years.
2. Inflation will approach 2% as the 10-year U.S. Treasury yield reaches 1.5%.
3. The U.S. dollar will sink to a five-year low.
4. Stocks will reach a new high for the 12th consecutive year but will fail to keep pace with strong earnings growth.
5. Stocks will outperform cash, but cash will outperform Treasury bonds for the first time since 2013.
6. Value, small-cap and non-U.S. stocks (especially those of emerging markets) will outperform growth, large-cap and U.S. stocks.
7. The health care and financial sectors will outperform energy and utilities.
8. U.S. federal debt will rise to more than 100% of GDP on its way to an all-time high.
9. The U.S.-China cold war will continue, but the argument becomes quieter and more multilateral.
10. Despite polarization, President Joe Biden, Senate Majority Leader Mitch McConnell and moderate forces will achieve some compromise legislation.

Editor's Note: The final prediction was made before the Jan. 5 Georgia runoff election

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Merck	MRK	4.85%
Pfizer	PFE	4.79%
Abbott Labs	ABT	4.55%
Abbvie	ABBV	4.43%
Thermo Fisher Scientific	TMO	4.32%
Medtronic	MDT	3.69%
Danaher	DHR	3.29%
Bristol Myers Squibb	BMY	3.28%

*Components and weightings as of 12/31/20. Please see website for daily updates. Holdings subject to change.

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STATE STREET GLOBAL ADVISORS

Opinion

EDITOR'S NOTE

Sometimes hope is hard

On Monday morning, I started thinking about the first note of the year, and I landed on the idea of hope.

Every year the turning of the calendar creates hope, but after the mess that was 2020, the Pennsylvania sky did seem a shade bluer and the promise of better days for the country and the pandemic put a skip in my step.

GEORGE B. MORIARTY

Then Wednesday happened.

Throughout the afternoon that sense of hope was dimmed. Galling acts of dishonor stained our Capitol, and an arcane, yet beautiful, act of government work was interrupted. I saw my four children, all of whom became fully engaged in their community and country over the past two years, gathered around a TV asking unanswerable questions.

But as I write this on Thursday morning, hope prevails again. In politics, the wee hours of this morning saw the election confirmed and peace restored to Washington, D.C.

And as regards the pandemic, we have seen vaccinations begin and updates on new trials and vaccines continue to emerge. There are weeks and months before any level of all clear, but there is a crack in the clouds.

So I'm choosing to focus on the blue sky again, and look forward to a summer spent at baseball games, with family, and hosting friends in person. It's not often hope is the harder course, but right now it is, and I'm relishing the climb.

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Investing depends upon a stable government

What do people look for in a financial adviser? The answer to that question has never been more important than it is at this moment in U.S. history.

In plain terms, a financial adviser is someone who looks at current events and trends through the filter of what's happened in the past to make an informed and reasonable guess as to what that will mean for their client and his or her assets in the future, and to guide them to protect those assets and make them grow.

So by its nature, being a financial adviser means being part analyst looking to the past and part soothsayer looking to the future. The mission of *InvestmentNews* is to help advisers serve their clients by offering news, analysis and context of industry events to help them fulfill that role.

A NO-BRAINER

When the editorial board met last week to choose a topic for this week's column, it seemed a no-brainer. Write a few words about the promise of the new year, tout the many predictions and resolutions by industry leaders that the *InvestmentNews* staff had worked diligently to compile in the past several weeks, offer words of encouragement and strength for 2021 and be grateful that 2020 was finally over. Happy New Year.

That was on Jan. 5.

The next day, everything we thought as a nation about the stability of our republic was thrown into question in just a few short hours. That is no exaggeration. Speculation and fears about what could happen next were on everyone's mind as images of a mob ransacking the Capitol building and disrupting the peaceable working of our government flashed on screens across the country.

PEOPLE LOOK TO ADVISERS TO HELP THEM MAKE SENSE OF THE FUTURE.

The *InvestmentNews* team responded quickly, contacting advisers and thought leaders to get their impressions about what was happening in Washington, D.C., as it was unfolding. Appearing under the byline of Bruce Kelly, the lead writer, the article, "'Rule of law prevailed': Advisers confident after riots at US Capitol," is in fact an effort of the full team that we are all very proud of.

GRAVITY OF THE MOMENT

While many of the comments reflected the gravity of the moment, the most prescient sentiment was expressed by Brian O'Neill, founder of Winged Wealth Management and Financial Planning: "The rule of law prevailed." More importantly, he went on to say that the rule of law "underpins how and why we can invest."

Thus, it would be impossible for financial advisers, wealth managers, institutional and retail investors, and retirement savers to plan for and prosper in the future without a stable government and sober, level-headed stewardship of the economy, and to shun those who place short-term gains and their political capital ahead of what's good for the country and the continued economic prowess of these United States.

So to answer the question posed at the beginning of this column, people look to advisers to help them make sense of the future and to mitigate the uncertainty that goes hand in hand with investing for that future — which is as impossible to predict as whatever was in the minds of those who stormed the Capitol.

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Social Security may not be a Ponzi scheme, but it sure acts like one

Dear Editors,

Ponzi schemes are a form of investment fraud made popular by Charles Ponzi in the 1920s. They work by promising high returns with low risk in order to lure investors. Once enough people invest, the schemer pays back the promised investment with new income from other investors drawn into the scam. While Social Security is not a Ponzi scheme by the pure definition since it is not an investment, there are many aspects of this benefit that are Ponzi-like.

Ponzi schemes ultimately collapse by not bringing in enough money from new investors to pay those pulling their money out. The advantage the government has with Social Security is that every working citizen is forced to contribute, whether they want to or not. And the contributor is not allowed to access their funds until age 67 or later if they want the maximum benefit. It is presented to workers as a benefit they contribute to out of every paycheck for their entire life and then in retirement get a monthly payout. It seems akin to a 401k plan or pension plan to most Americans.

The dirty secret is that there is no "lockbox" or account with your money in it. In this way, Social Security does act like a Ponzi scheme, as it is funded through current workers' contributions.

According to the 2020 CBO, the Social Security Trust Fund will run short of money in 2031. Over the years, similar dire warnings have been met with changes to the promised benefit. In 1993 changes were made so that up to 85% of Social Security benefits would be taxed at the federal ordinary income tax rate. This begins for single filers and couples filing jointly with more than $34,000 and $44,000, respectively, and has not been adjusted for inflation in 25 years! Even if you have income less than that, you are taxed on up to 50% of your benefits. Another recent change to the rules was to increase the full benefit age to age 67 from 65.

Sadly, this never had to be the case. If your contributions had been put in a personal account for you, in U.S. Treasuries, not only would you have substantially more money when it came time to withdraw, but it would truly be your own account that you could leave to named beneficiaries.

As it stands now, the Social Security system is also one of the largest discriminatory programs in history. Life expectancy for African Americans is five years less than white Americans, seven years less than Hispanic Americans, and 11 years less than Asian Americans. Black Americans who pass away earlier lose their benefits instead of being able to pass along the "unused" funds to their children.

The only real way to keep Ponzi schemes solvent is to get more investors. In the case of Social Security, more workers are needed for the forced Social Security tax. However, the average family is having fewer children today. Unfortunately, the best solution of setting up guaranteed U.S. Treasury private accounts that workers' Social Security goes into won't work because those funds are needed to pay out current recipients.

While Social Security technically isn't a Ponzi scheme, it operates very much like one. The original promises to workers have long since been broken and the benefits will continue to be watered down with each passing decade to keep it solvent.

Sincerely,
Eric J. Reinhold
Vice President/Financial Advisor
Ameriprise Financial Services

The evolution of nontraded REITs can't be overlooked any longer

Dear Editors,

The assertion in Bruce Kelly's Dec. 10, 2020, "On Advice" column that nontraded real estate investment trusts lack transparency is an outdated and inaccurate view of a product class that's transformed itself over the last decade.

The nontraded REITs industry has evolved since the global financial crisis, and there have been tremendous advancements as new institutional players and legacy firms have brought new products and strategies to the market for the retail customer and sophisticated investor alike that directly address the issues Kelly points to in his column.

As a long-time advocate for investor choice and market access, the Institute for Portfolio Alternatives has been a champion for investors who want and need access to investment strategies that are less correlated to equity markets. That is why we worked closely with Finra and other regulatory bodies to develop guidelines that provide more efficient share price values to investors and greater liquidity. These guidelines have been adopted across the industry.

As Kelly pointed out, the industry has its past blemishes, and like many other financial products, it struggled in the aftermath of the 2008 financial crisis. However, over the last decade, the industry has changed meaningfully. Today, the instances that Kelly chooses to call out are the exception, not the rule.

On the back of the Finra 15-02 guidelines, as well as ongoing product evolution, the new generation of nontraded REITs has been tested and proven itself throughout the 2020 global pandemic and performed as expected throughout this year's unprecedented volatility.

Despite the financial challenges brought on by the pandemic this year, new data from Robert A. Stanger & Co. underscores that nontraded REITs have been a resilient product built for diversified, long-term returns.

According to Stanger, the average annualized yields on nontraded REITs remain in line with or above 5%, demonstrating how nontraded REITs have continued to deliver long-term gains for investors seeking a stable income. Investors are taking notice too as the funds raised $1.37 billion in Q3 alone.

NONTRADED REITS HAVE BEEN A RESILIENT PRODUCT BUILT FOR DIVERSIFIED, LONG-TERM RETURNS.

It's important to reiterate that volatility in any asset class can be expected and is not unique, even in times of high growth and prosperity. It's also important to remember that volatility in markets throughout most of 2020 isn't the result of weak underlying market fundamentals or fundamental flaws with the investment, and instead the product of an unpredictable virus sweeping the globe.

I personally believe that our industry was on a stronger-than-ever footing as we entered 2020, and that those fundamentals will drive our industry forward as we look to a recovery.

Sincerely,
Anthony J. Chereso
President and CEO
Institute for Portfolio Alternatives

MARKET WATCHERS SEARCH FOR SILVER LININGS IN 2021

WILL MORE STIMULUS, CURBING COVID AND RELEASING PENT-UP DEMAND FUEL A SECOND-HALF SURGE?

BY JEFF BENJAMIN

The understandable desire to put 2020 behind us unfortunately offers a less-defined transition into the new year when it comes to the economy and financial markets.

While analysts and market watchers across the spectrum see glimmers of hope and express general optimism regarding the year ahead, much of the good stuff isn't expected to kick in until some time in the second quarter or later.

"The first half of the year could be ugly, with more stress on small businesses, consumer defaults and COVID is not behind us yet," said Gary Zimmerman, chief executive of MaxMyInterest.

"As we get into the second half and people start to come out of their cocoons, and as the vaccine becomes more widely distributed, we'll start to see the results of pent-up demand," he said.

It is never fair to peg broad market and economic outlooks to anything as specific as a new calendar year, but the transition to 2021 offers proximity to several significant factors likely to impact the way money is earned, invested and spent.

Along those lines, the most common references among financial advisers and market prognosticators when considering the next several months include the new presidential administration, the efficacy and adoption of COVID-19 vaccines, and the shifting of power in Washington to an increasingly progressive Democratic party.

First things first: With the Georgia runoff election last week confirming that Democrats will control both Houses of Congress in addition to the White House for at least the next two years, all eyes are now on the lookout for higher taxes and increased regulations across financial services.

But despite President-elect Joe Biden's campaign rhetoric regarding higher taxes, there is a general sense and hope that he can maintain a moderate stance.

"There are still some more centric Democrats and Republicans, so that thin majority line one way or the other probably won't lead to any dramatic policy changes," said Charlie Ripley, senior investment strategist for Allianz Investment Management.

Jim McDonald, chief investment strategist at Northern Trust, said the financial markets wrapped up 2020 expecting a divided government, in which Republicans retained control of the Senate.

"With the Democrats winning both Georgia Senate seats, it means they will be able to pass tax legislation and spending through the reconciliation process, but they won't be able to pass anything else," he said. "They also may be constrained in the level of tax and spending increases achievable, as the majority will be razor-thin and Democratic senators and representatives from Republican states or districts will be averse to major tax hikes or spending programs."

Paul Schatz, president of Heritage Capital, said the market was so convinced that the Republicans would retain control of the Senate that a win by the Democrats could be a "catalyst" for market disruption during the first quarter.

"You're going to have a strong headwind in 2021 and 2022, assuming that corporate taxes go up, individual taxes on high earners go up, and capital gains taxes go up," he said. "The tailwind to counter that will be another massive stimulus program early in 2021, but that's a one-shot deal."

Schatz expects the stimulus spending to "juice the economy" in the second half of the year. "But don't forget that the stock market is already trading as if it is the second half of the year," he noted.

Noah Hamman, CEO of AdvisorShares, said complete Democratic control in Washington should trigger "adjusted investor expectations over the next two to four years."

"Higher taxes will have a negative impact, but the devil is in the details," he said. "If it's just a blind repeal of the Trump tax cuts, that will be bad. Hopefully, we can find a balance, but that's a lot to count on from politicians who don't always keep their promises."

Eric Beiley, executive managing director at Steward Partners Global Advisory, also believes the win by the Democrats in Georgia will disrupt the markets, agreeing with other analysts that the markets were fully anticipating the Republicans would maintain Senate control.

"The markets could step back, anticipating more substantial changes to the tax code," he said.

Regarding the initial stock market rally last week when it became clear that the Democrats would win the Senate, Beiley gave a nod toward the power of market momentum.

"It clearly shows the current strength of investor sentiment in the stock market," he said. "The strong market conditions that ended 2020 appear to continue in 2021 despite the political environment and the potential for higher tax rates."

The election in Georgia was such an issue for the fi-

CONTINUED ON PAGE 10

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nancial markets because of the outcome of the November presidential election that put Biden in the White House, along with his many promises to raise taxes and support government spending.

"Biden has signaled they would like to eliminate the Trump tax cuts," said Ed Cofrancesco, chief executive of International Assets Advisory.

But in addition to Democrats' holding the smallest House majority in history, Cofrancesco believes the more moderate Democrats will be able to keep the extreme left in check.

"By putting Janet Yellen in charge of the Treasury, I think they're signaling they are not supporting an ultra-left socialist agenda," he added.

Steve Skancke, chief economic adviser at Keel Point, also believes the slim margins in Congress will prevent Biden from accomplishing many of his more radical tax proposals that would rattle financial markets.

"Picking up both Georgia Senate seats gives the Democrats the advantage in managing the agenda of the Senate, confirming executive and judicial appointees and enacting moderate, consensus legislation" he said. "But in terms of passing anything that's going to be radically different, there are enough moderate Democrats to make that unlikely.

"There will be a perception that things will change but the probability of big increases in corporate taxes, which are high on Biden's agenda, are very unlikely as the economy is still in rebound mode. Additional fiscal stimulus and a bigger infrastructure spending package financed with more borrowing will be the biggest differences," Skancke said.

THE PANDEMIC FACTOR

Then there's COVID-19 and the optimistic but sluggish rollout of the vaccines that began in late December.

"When it comes to investing, we normally talk about risk on and risk off, but now we're talking about COVID on and COVID off," said Sébastien Page, head of global multi-asset strategies at T. Rowe Price.

"The vaccine news is a significant positive surprise," he added, before referencing the way the financial markets have seemingly become disconnected from the realities of a global pandemic.

"Even with unemployment still more than double what it was before the pandemic, stocks are closer to fair priced than most people think," Page said.

The point is that even with all the negative impacts of pandemic-induced lockdowns and business shutdowns, the relative strength of the equity markets is simply the result of money finding the rivers being carved by government stimulus efforts, including the Federal Reserve's monetary policies.

"The market is a cash-flow discounting machine, and during COVID rates went down by 100 basis points; that alone could justify a higher [price-to-earnings] ratio," Page said. "If you think stocks are expensive, have you looked at bonds recently?"

POST-COVID REBOUND

Virtually across the board, prognosticators are betting on pent-up demand to drive the economy and the markets as soon as everyone gets the all-clear to get back to business and life in a newly vaccinated post-COVID world. But that could still be months away.

"We think GDP will rebound in the second half up to close to 4%, and inflation will move back toward the Fed's target range," said Ripley of Allianz.

He doesn't see the Fed raising rates until at least 2023 and expects the 10-year Treasury yield to be around 1.25% at the end of 2021.

Ripley anticipates an "above-average return" for the S&P 500, adding that "close to 10% is not out of the cards."

"A lot of this is hinged on the effectiveness around the vaccine," he said. "There's room for the markets to continue to rise from here. It's a rebound in earnings that have been depressed from the COVID environment."

Another factor supporting the pent-up demand theory is the bulked-up savings that were a byproduct of reduced spending in 2020.

While a lot of people lost their jobs as a result of the pandemic, those who were able to keep working realized a boost in real disposable income, according to Saumen Chattopadhyay, chief investment officer at Carson Group.

"We are sitting on pretty strong economic conditions because people didn't shop or travel, so they saved money," he said. "Pent-up demand is pretty strong, and you can see that in the housing market, where young buyers are the largest cohort."

According to Chattopadhyay's analysis, among working Americans, disposable income per capita is up nearly 6% from a year ago.

"The last time we saw it that high was 1984," he said. "We probably have a pretty strong year ahead of us. I would not be surprised if the S&P finished over 4,500," which is a gain of more than 20% from the end of 2020.

ECONOMIC DRIVERS TO WATCH

In terms of economic drivers, Chattopadhyay anticipates "almost immediate" passage of new $1,400 stimulus checks, expanded unemployment benefits, and more money for state and local governments.

"There is likely to be a continuous series of fiscal cliffs over the next two years, including debt ceiling increases that will be required in the summer," he said.

Chattopadhyay said the medium-term impact of Democratic control will likely include an increased focus on climate policy, health care policy, immigration and anti-trust enforcement focused on technology firms.

"At the same time, due to a narrow Senate majority, there will be a very low probability of tax increases," he added.

Eddy Augsten, managing director at Concurrent Advisors, cites the vaccine, an accommodative Federal Reserve, and a polarized government as reasons to be bullish in the year ahead.

"Expect life to accelerate in 2021," he said. "The pandemic has created an excellent stock-picking environment and I expect active will outperform passive."

Like most market watchers right now, Augsten points to the fixed-income market as an understated driver of stock market performance.

"Real rates are still highly negative and that has historically been good for equities," he said.

Cofrancesco of International Assets Advisory is singing the same tune about skimpy bond yields giving investors no choice but to load up on stocks.

"Fixed income has to be in very short-term investments right now because there is no yield," he said, adding that investors and advisers should be prepared for the next logical step on the economic road map: inflation.

"By 2022 we're going to see inflation from all this, and we don't know how the industry will deal with it, because most people in this industry have never seen inflation," Cofrancesco said.

Schatz of Heritage Capital is also already looking past what appears to be a rosy 2021 to the threat of inflation further down the road.

"The inflation genie is out of the bottle," he said. "We do need a little inflation, but the 2020s are going to be about old-fashioned food inflation that all the real people will feel. If wages don't go up and you've got food inflation, that's less money to go elsewhere, but that's a mid-2020s story."

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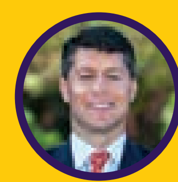
Charlie Ripley, senior investment strategist, Allianz Investment Management
"S&P target for above average, close to 10% not out of the cards."



Paul Schatz, president, Heritage Capital
"S&P will peak at over 8% but finish the year up 4.5%."

Ed Cofrancesco, chief executive, International Assets Advisory
"S&P will finish the year up 17%."

Eric Beiley, executive managing director, Steward Partners Global Advisory
"I see it being a more modest year for equities. I don't see these strong levels continuing. The market will finish up somewhere in the single digits, which wouldn't be a bad thing."

Steve Skancke, chief economic adviser, Keel Point
"S&P up 10% to 15% first half. For all of 2021 there are two scenarios. If it all works and the assessment is positive, 20% for the year; if it's not working, then 8% to 10%."

Saumen Chattopadhyay, chief investment officer, Carson Group
"Would not be surprised if S&P finished 2021 over 4,500, which is a 22% gain."

Advisers predict only partial return to normal in 2021

MOST ARE STILL BRACING FOR LIMITS ON BUSINESS ACTIVITY AND VOLATILITY IN MARKETS

After a year of ups and downs, most advisers are anticipating more of the same in 2021.

Overall, a majority of financial advisers look forward to improvements in the economy and equity markets over the next 12 months, according to an InvestmentNews Research survey of more than 300 advisers fielded in the final weeks of 2020.

NUMBERSGAME
DEVIN MCGINLEY

Advisers have been largely optimistic about stock indexes since markets began their initial rebound from the COVID-19 shock, but the gap between their expectations for equities and the overall economy has narrowed. Seventy-two percent expected growth in the S&P 500 and 68% anticipated overall economic improvement, compared with 60% and 44%, respectively, in a July survey.

Yet adviser optimism, which was underpinned by the nearly universal expectation of a successful vaccine rollout by year-end, had its limits. Most anticipated that restrictions on business activity would last through the entirety of the next year.

Only 44% of advisers thought the economy would be fully reopened in the next 12 months, and only 28% expected a full resumption of in-person work or business travel.

And although the market outlook for a year from now was overwhelmingly positive, even that came with a caveat. Most advisers expected some choppiness along the way, with 58% saying a market correction was likely to occur.

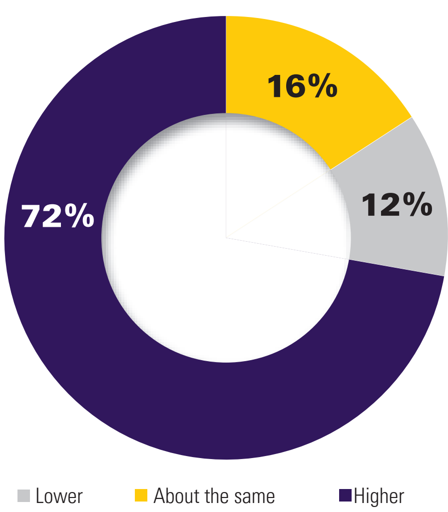
With volatility expected to persist, survey respondents continued to be on the lookout for alpha, with 25% expecting to increase their use of individual stock picks and 24% saying they would increase usage of actively managed ETFs. International equity was the asset class poised to gain the most over the next year, with 42% of advisers planning to increase their exposure, according to the survey.

Still, the overall buoyancy of the industry stands out against the expectation that many of the headwinds from 2020 will persist through 2021.

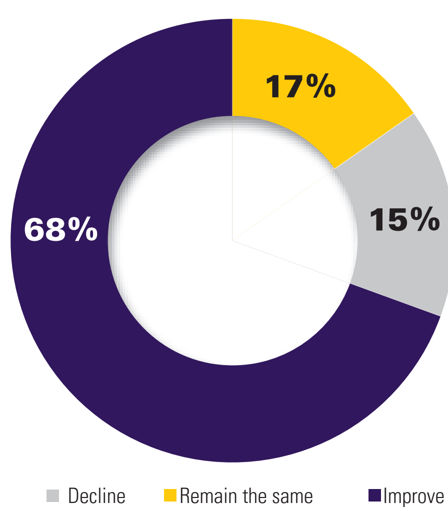
But advisers have one more reason to be optimistic about the next year: At least they've faced those headwinds before.

For more information on IN's research offerings, contact INResearch@investmentnews.com.

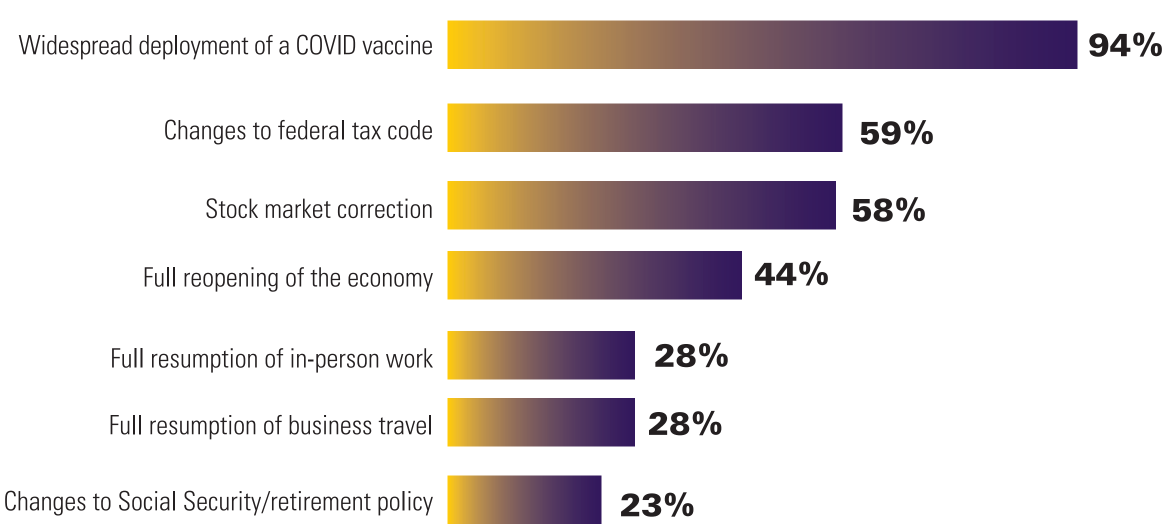
WHERE DO YOU EXPECT THE S&P 500 TO BE IN 12 MONTHS?

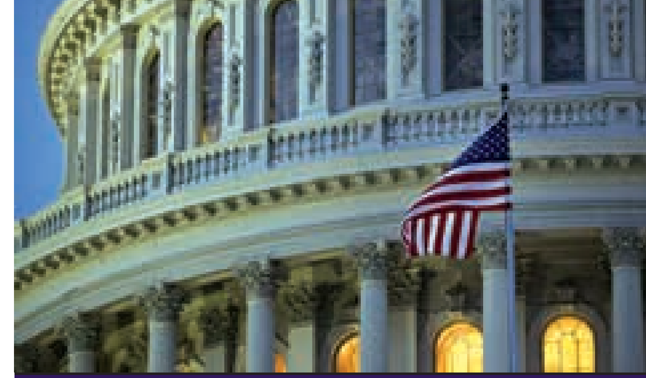


HOW DO YOU EXPECT U.S. ECONOMIC PERFORMANCE TO CHANGE OVER THE NEXT 12 MONTHS?



WHICH OF THE FOLLOWING DO YOU BELIEVE ARE LIKELY TO OCCUR OVER THE NEXT 12 MONTHS?





Razor-thin majority in Senate endangers Biden's agenda

Democrats claimed both Senate seats in the Georgia runoff elections and have captured the slightest possible Senate majority, but it will still be tough for President-elect Joe Biden to get his agenda through the chamber.

The Rev. Raphael Warnock, a Democratic candidate, defeated Republican Sen. Kelly Loeffler for one of the Georgia Senate seats. Democrat Jon Ossoff won the other race, beating Republican Sen. David Perdue.

The twin wins give Democrats operational control of the Senate, which is split 50-50 between Democrats and Republicans. Democrats claim the majority because of the tie-breaking vote of Vice President-elect Kamala Harris.

The gossamer-thin Democratic majority hardly allows the party free rein to advance legislation. All Democrats will have to stand together — including those on the left, such as Sen. Elizabeth Warren, D-Mass., and moderates, such as Sens. Joe Manchin, D-W.Va., and Jon Tester, D-Mont.

"They're going to have to carefully thread the needle in terms of what they want to accomplish," said Jason Rosenstock, a partner at Thorn Run Partners, a government relations consultancy.

Republicans will be able to stop many bills with a filibuster, which requires 60 votes for passage and is likely to remain a parliamentary tool in the new Congress.

Democrats could turn to what is known as reconciliation to pass by a simple majority a bill focusing on tax and budget policy. They could use the process to advance tax increases on personal and capital gains rates for the wealthy.

It's almost a certainty that Republicans will stand united against tax increases. That will put the burden completely on Democrats, who hold the House by just a handful of seats in addition to their narrow Senate majority.

"Getting 50 votes is not a foregone conclusion," said Brian Gardner, chief Washington policy strategist at Stifel Financial and author of an analysis of the impact of the Georgia elections. "You can't lose anybody. A tax hike is going to be done on a party-line vote. Democrats are going to have to do it on their own."

So reconciliation as a path toward tax increases remains in doubt even as Democrats are about to claim control of the Senate.

"How they view a reconciliation package will depend on what's in it," Rosenstock said. "It's too early to know what they will include."

Biden, who spent decades in the Senate before being elected vice president in 2008, is confident of his ability to strike deals with Republicans.

"But I'm also just as determined today as I was yesterday to try to work with people in both parties — at the federal, state, and local levels — to get big things done for our nation," he said in a statement last Wednesday about the Georgia Senate results.

That approach is the only one that will work, Gardner said.

"Because of the narrow majorities, any legislation is going to have to be bipartisan to pass," he said.

— Mark Schoeff Jr.

80% PORTION OF WORK RETIREMENT PLANS THAT OFFER TARGET-DATE FUNDS, UP FROM 68.6% IN 2018

SOURCE: PSCA'S 63RD ANNUAL SURVEY

Strategies for Social Security lump-sum payouts

MARY BETH FRANKLIN

ONRETIREMENT

Based on recent email questions from *InvestmentNews* readers, I detect increased interest in lump-sum payouts of Social Security benefits, perhaps reflecting economic uncertainties caused by the COVID-19 pandemic.

It's important to note that lump-sum payouts of retroactive benefits are available only under certain circumstances. Even then, inconsistent guidelines from the Social Security Administration seem to have inhibited or delayed some requests.

One adviser wrote saying he had suggested to a soon-to-be-retired couple, where both spouses are 63, that they apply for six months of retroactive Social Security benefits. He was surprised when the Social Security Administration informed the clients that retroactive benefits are not available before full retirement age.

The adviser asked me if that is correct. Yes, it is.

FULL RETIREMENT AGE OR OLDER

Individuals who are full retirement age or older when they file for Social Security have the right to request a lump-sum payment of up to six months of retroactive benefits, beginning no sooner than their full retirement age. Because a portion of their past benefits are paid out in a lump sum, their future monthly benefits will be slightly smaller.

If you postpone claiming Social Security beyond your full retirement age, your benefit increases by 0.66% per month — for a total of 8% per year in delayed retirement credits — up until age 70. However, you cannot receive a lump-sum payout and delayed retirement credits for the same period.

For example, if your full retirement age is 66 and you wait until 67 to claim benefits, you can request a lump-sum payout of six months of retroactive benefits. But if you applied at 66 and 3 months, you could only receive three months of benefits in a lump sum as retroactive benefits cannot be paid before full retirement age.

Last year, I reported about some legitimate requests for lump-sum payouts that initially were denied by the Social Security Administration. At the time, I asked SSA if there had been a policy change or temporary administrative holds on requests for lump-sum retroactive benefits.

"We temporarily adjusted our procedures to hold the release of retroactive payments to applicants who many need additional time to provide any necessary evidence due to unexpected circumstances from the COVID-19 pandemic," public affairs specialist Nicole Tiggemann replied by email in May. Clear as mud!

Last month, I received an email from an *InvestmentNews* reader who shed some light on the murky lump-sum request procedure.

Warren Strauss, a financial adviser in Sarasota, Florida, said one of his clients had requested a lump-sum payout, but nothing happened for more than three months.

"I had gotten all kinds of unimaginable explanations for the delay for my client, until I spoke with a supervisor who admitted that she was not trained in this special request," Strauss wrote in an email. The supervisor investigated and learned that a "wet signature" — a handwritten signature — is required for such requests.

"My client submitted the request in writing via fax," he said. "The six months in back benefits funds arrived in client's checking account within a few days after submitting the request in writing via fax."

LIKE INDIANA JONES

I complimented Mr. Strauss, telling him he was like Indiana Jones unearthing a secret treasure! But a wet signature may not always do the trick, said Matthew Allen, CEO of Social Security Advisors, a consulting service that helps advisers and consumers optimize their claiming strategies and file for benefits.

"Social Security has issued guidance that suggests claims representatives request additional identification and increase their level of scrutiny for lump sum payouts during COVID," he said. "However, the execution of this has been anything but consistent."

Allen said he has heard Social Security representatives suggest various protocols, from requiring wet signatures and faxing IDs to making an appointment and coming into an office, though offices have been closed to the public since mid-March due to COVID.

"When we run into this for clients, we escalate the matter beyond the local office to the regional commissioner's office, citing the rules and regulations that require SSA to pay these funds," he said. "We have had success with every case we've had to deal with like this."

I asked the Social Security Administration for an update on how it's handling requests for lump-sum payments of retroactive benefits.

"Agency employees continue to work remotely to provide the vital services the public relies on through online services and phone services," Ms. Tiggemann said via email last week. "However, we have provided guidance to our field offices to schedule in-office dire need appointments to obtain required evidence where applicable."

Bottom line for advisers: If your clients are eligible for a lump-sum payout, be persistent, and get help if you need it.

(Questions about new Social Security rules? Find the answers in my ebook at InvestmentNews.com/MBFebook.)

Mary Beth Franklin, a certified financial planner, is a contributing editor for InvestmentNews.
mbfranklin@investmentnews.com

KEY POINTS

- Lump-sum payouts of benefits are limited to those who've reached full retirement age.
- But some clients may have difficulty getting such payouts.

INmail

BY MARY BETH FRANKLIN

Earnings after age 66 may increase Social Security benefits

Tom: I am 71 and started receiving my Social Security benefits last year. My self-employment earnings for the current and past several years should replace some earlier earning years in the calculation that determines my Social Security benefits. How and when will I see an adjustment in my benefits?

MBF: The Social Security Administration reviews your earnings record each year you continue to work, regardless of your age or whether you're currently receiving Social Security benefits.

Social Security benefits are typically calculated using your highest 35 years of indexed earnings. If your latest year of earnings turns out to be one of your highest years, SSA will automatically recalculate your benefits and pay any increase that is due. Benefits are paid in December of the following year. For example, in December 2020, you should get an increase for your 2019 earnings if those earnings raised your benefit. The increase would be retroactive to January 2020.

To compute a worker's retirement benefit, SSA first adjusts his or her earnings to reflect the changes in general wage levels that occurred during the worker's years of employment to ensure that future benefits reflect the general rise in the standard of living that occurred during the worker's career.

An insured worker becomes eligible for retirement benefits at age 62. If 2021 were the year of eligibility, SSA would divide the national average wage index for 2019 by the national average wage index for each year prior to 2019 in which the worker had earnings and multiply each ratio by the worker's earnings. This would give the indexed earnings for each year prior to 2019. SSA would use the face value of earnings in 2019 and afterwards to compute the worker's primary insurance amount, or PIA.

Benefits claimed before full retirement age are reduced below the PIA. Benefits claimed after full retirement age grow by 8% per year above the PIA up to age 70. To see how your benefits are calculated based on your age of eligibility, see the SSA's indexing calculator (https://www.ssa.gov/oact/cola/awifactors.html). For more information on how benefits are determined, see https://www.ssa.gov/pubs/EN-05-10070.pdf.

69 RECORD NUMBER OF MERGERS AND ACQUISITIONS OF REGISTERED INVESTMENT ADVISORY FIRMS IN THE FOURTH QUARTER OF 2020.

SOURCE: ECHELON PARTNERS

Breakaway brokers tell tales of risk … and reward

BY JEFF BENJAMIN

THE COVID-19 PANDEMIC slowed but did not completely halt the pace of breakaway brokers heading toward the independent advisory channels.

But for those advisers that pulled up stakes and made the move in 2020, an already challenging undertaking proved to be an even steeper climb, but every bit worth the effort.

"I wish I had done it sooner," said George Nottingham, who left Wells Fargo in May to join Steward Partners, where he is now a managing director and wealth manager.

Nottingham, who had switched firms twice before in his career, describes this as his "third and final move."

After spending 18 months researching his options and preparing to move his five-person team outside of the brokerage industry, Nottingham said he decided on Steward Partners in January.

But even six months in, Nottingham said the transition remains a work in progress as he has so far brought on $180 million in client assets of the $200 million his team was managing at Wells Fargo.

"I'm still actively pursuing about 10 or 12 clients," he said. "Some relationships you think are tight as a tick, and you find out they're not, and other relationships you don't think are so tight and find out they are."

At some point in the due diligence process, Tommy Leeman, a Wells Fargo colleague, but not part of Nottingham's team, joined the track to transition his business to Steward Partners.

"We just had our six-month anniversary here and there is nothing we would have done differently, except that I would have done it sooner," said Leeman, who has so far brought over $55 million of the $60 million in client assets he was managing at Wells Fargo.

"I am very happy with what I call the invited-guest list that came over," he said. "There are probably seven clients that have not transitioned over, and I thought they would, but they also have not told me to leave them alone."

CHECK THE TIMELINE

Jeffrey Gonyo, divisional president and founding partner at Steward Partners, said a typical breakaway transition from commitment to actual departure requires a timeline of six to eight weeks.

But in the age of COVID-19, "we are probably looking at a 12-to-18-week process," he said.

According to Echelon Partners, 387 brokers left brokerage firms for the independent advisory space during the first nine months of 2020.

That compares to 424 during the same period in 2019.

Despite a pandemic-related slowdown, Echelon is projecting a strong final quarter and a full-year tally of 516 breakaways, which will rank 2020 behind the last two years but well ahead of the 2017 total of 423.

A QUESTION OF CLIENTS

As any breakaway broker can attest, the months leading up to the decision to leave and where to go only kick-start more months of scrambling to recruit suddenly former clients to join you as a registered investment adviser.

"The most difficult part is putting clients through it," Nottingham said. "The average client has six accounts and you've got to redocument all those accounts. It was 60 days of 12- to 14-hour days without a day off, and it was probably 90 days before you felt like you were almost there. And there was absolutely no time for new client prospecting."

Leaving a firm like Wells Fargo, which is part of the broker protocol agreement, Nottingham and Leeman were able to take with them basic lists of clients' names, addresses and phone numbers.

But those breakaways leaving firms that have exited protocol have an additional challenge that often entails relying on a good memory.

"We couldn't even take phone numbers, so we basically sat in a room and brainstormed client names after we left," said Emily Bowersock Hill, who was part of a six-person team that left Morgan Stanley to join Sanctuary Wealth and establish Bowersock Capital Partners.

"We decided to leave a long time before we left; I had known for a long time this is something we would need to do," she said.

Part of Hill's due diligence process was "calling teams we'd read about that had already done this. We started watching to see where people were going and researched those options."

Gonyo said the biggest difference between leaving a protocol and a non-protocol firm is where the bulk of the work occurs.

"With a protocol firm, there's definitely more work that happens on the front end," he said, citing the packages that are prepared in advance for each client, which can't be shipped until the day the broker leaves the firm.

But at least they are starting with a basic list that includes some client details.

"THE MOST DIFFICULT PART IS PUTTING CLIENTS THROUGH IT."

GEORGE NOTTINGHAM, STEWART PARTNERS

"When it's a non-protocol firm, there's a lot more work on the back end," Gonyo said.

If there is an upside to the logistical scramble of suddenly leaving a firm and then trying to compete against that firm to capture as many of your clients as possible, it is the ability to "break up" with some clients.

"We did not invite all of our clients to come with us, because one of our goals was to reduce our total number of clients," said Hill. "We reduced our clients pretty substantially. We want to spend our time working with clients we're excited about. We are not interested in running a volume business."

While Hill did not invite all her former clients to join her new independent advisory firm, she has surpassed her initial goal by growing to more than $450 million since leaving Morgan Stanley.

"Our initial goal was hoping to hit $350 million, in our wildest imagination," she said.

BIGGER ISN'T BETTER

While smaller clients are sometimes the first to be cut in breakaway transitions, Nottingham and Leeman said some clients with large portfolios can also be more work than they're worth.

"We didn't invite some small accounts because they didn't fit in with what we're doing going forward," Nottingham said. "But we also had a couple of larger relationships that didn't want to listen to me."

Leeman said some of his larger accounts "were very needy, and they were not going to be a good fit for me."

Nottingham and Leeman both said they had clients track them down and ask why they didn't get invited to be clients at the new firm.

Jason Juhl, who left US Bank Corp. in September to join the Carson Group as a wealth adviser, said trimming his client base was a significant factor in the decision to go independent.

"I went from 800 clients and an average net worth of $250,000 to 220 clients and an average net worth of $1.5 million," he said. "I was working 12 to 15 hours a day, and I have a 19–month-old child and pregnant wife. You can't be of great service to 800 people. It's a disservice to them and disservice to me."

Even though Juhl describes himself as a "glass is half full kind of guy," he said he has had to adjust his expectations for how long it takes to bring clients from his former firm on board.

"I had to change my attitude a bit, because I was thinking I'd get 100% of my assets in a couple of weeks, but people move at different paces and we're in the middle of a pandemic," he said. "I've been here 90 days and we're at about 90% assets."

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SEC's stepped-up oversight of risky products to continue

BY MARK SCHOEFF JR.

OVER THE LAST several weeks, the Securities and Exchange Commission has stepped up its oversight of risky, complex financial products, a trend that experts say likely will continue and intensify in a new presidential administration.

On Nov. 13, the SEC announced a $3 million settlement with three investment advisory firms and two dually registered firms for unsuitable sales of exchange-traded products linked to market volatility.

A few days later, the Office of Compliance Inspections and Examinations warned firms to shore up their policies and procedures for selling complex financial products and ensure that their advisers understand how they work and whether they're a good idea for clients.

This sequence of events followed SEC approval of a derivatives rule that removed a sales practice provision that would have required due diligence by brokers and advisers selling leveraged and inverse exchange-traded funds. Instead, SEC officials sought public comment on the need for additional protections related to customer purchases of complex products through self-directed accounts.

The SEC's concerns about complex products won't wane in the Biden administration.

KEY POINTS

- Agency says advisers, brokers must apply 'heightened scrutiny' to sales of risky ETPs.
- SEC's concerns won't wane in the Biden administration.

"Expect the focus on complex ETPs to survive the transition to new leadership at the SEC — these products, and other products with similar features, will continue to be in the cross hairs, along with the firms that sell them," said Kurt Wolfe, a securities compliance attorney at Troutman Pepper.

"What the SEC sees is a bunch of registered reps and investment advisers who may not understand the products selling them to clients who don't understand the products and for whom they may be unsuitable," Wolfe added.

In fact, the SEC may become more intense about complex products next year.

"I believe we'll see, especially with the administration change, an increased focus on complex financial instruments that are offered to retail investors," said Valerie Dahiya, a partner at Perkins Coie. "You'll see more enforcement actions related to sales practice obligations."

CAUTION ADVISED

The enforcement action was initiated before Regulation Best Interest, the new broker advice standard, was implemented in June. In its follow-up statement, OCIE used Reg BI and fiduciary duty, which governs investment advisers, to make its point that advisers need to be cautious with investments that are volatile and opaque.

"Under these standards, a financial professional recommending a complex or risky product should apply heightened scrutiny to understand the terms, features and risks of the product and whether such product fits within the client or customer's risk tolerance and specific trading objective, and whether it would require daily monitoring by the investor or the financial professional," OCIE said.

The Financial Industry Regulatory Authority Inc., the broker-dealer regulator, also has been sending warnings. It released a regulatory notice in May warning brokerages to tighten up their policies and procedures for selling exchange-traded products linked to oil.

"Anything that happens after June 30, the SEC and Finra have a more blunt instrument to go after B-Ds who fail to make adequate disclosures and put the best interests of their clients first," Dahiya said in reference to Reg BI.

Most advisers who recommend complex products probably understand them, but that doesn't mean they can translate them to clients, said Matt Bacon, an adviser at Carmichael Hill & Associates. Even if they can, that doesn't mean the client will retain the knowledge.

"If you ask them in a month how [complex products] work, my guess is they would struggle to explain it," Bacon said.

Traditional ETFs are linked to indexes such as the S&P 500 and rise or fall as the index does. But when they move in an opposite direction and use debt to amplify those swings or when they are linked to market volatility, the dangers for investors increase exponentially.

A CLEAR MESSAGE

The message the SEC is sending is "there's not just elevated reward with these products, there's elevated risk," said Todd Rosenbluth, director of mutual funds and ETF research at CFRA. "The fund that is at the top of the ladder could become the fund at the bottom of the ladder very quickly and vice versa."

Those swings can decimate portfolios, especially if a client buys and holds a complex financial product that is meant to be traded on a daily basis.

"I consider them financial weapons of mass destruction," said Jim Stewart, owner of Carmichael Hill & Associates.

Complex financial products likely will continue to proliferate as investors chase higher returns, and regulators won't ban them outright. But caution will be the watchword for using them.

Financial professionals must "do a significant amount of assessment and due diligence before offering products and determining whether the products are suitable or appropriate for any retail investors," Dahiya said.

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Commissioner Elad Roisman named acting chairman of SEC

INVESTMENTNEWS

ELAD L. ROISMAN has been appointed acting chairman of the Securities and Exchange Commission by President Donald Trump. He fills the vacancy created by the departure of Jay Clayton on Dec. 23.

President-elect Joe Biden will nominate a permanent successor to Clayton.

Roisman, a Republican, has served as a commissioner since September 2018. Earlier, he served as chief counsel on the U.S. Senate Committee on Banking, Housing, and Urban Affairs, and as a counsel to SEC Commissioner Dan Gallagher.

In the private sector, he was an attorney at NYSE Euronext and an associate at the law firm of Milbank, Tweed Hadley & McCloy.

In a joint statement, Commissioners Heather M. Peirce, Allison Herren Lee and Caroline A. Crenshaw said: "We heartily congratulate Commissioner Roisman on his designation as Acting Chairman of the Securities and Exchange Commission and look forward to continuing our work together to further the agency's vital mission."

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$1T TOTAL VALUE OF CRYPTOCURRENCIES AFTER FIVEFOLD MARKET CLIMB IN 2020.
SOURCE: COINGECKO

Robinhood under pressure for adding 'gamification' to investing

BY NICOLE CASPERSON

ROBINHOOD IS under fire for its use of gamification strategies to attract young investors. A complaint filed by the Massachusetts Securities Division last month alleges the fintech manipulated its customers, many of whom are novice investors, into excessive trades.

The regulators defined gamification as the application of typical elements of game playing to other activities, typically as a marketing technique to boost engagement with a product or service.

Gamification strategies in the Robinhood app — like sending daily push notifications or displaying confetti raining down after each trade — are used to "lure customers" into consistent participation and long-term engagement with the trading platform, which in turn generates more revenue for the app, according to the complaint.

KEY POINTS

- The free trading app has been applauded for democratizing the market.
- But critics and regulators are starting to take a closer look.

A customer who hasn't yet traded in an account, for example, could receive a push notification from Robinhood with the message: "Top Movers: Choosing stocks is hard. [flexing bicep emoji] Get started by checking which stock prices are changing the most," according to regulators. After clicking the notification, the customer is redirected to a "Top Movers" list that documents prices of popular stocks, the complaint said.

Yet gamification is a tried-and-true practice and Robinhood is far from the only company using similar tactics. Popular apps, like the fitness app Peloton, use gamification to capture their users' attention and influence their behavior to keep them engaging with their products. Fintechs like Betterment, Wealthfront, Acorns and Stash use push-button notifications and similar techniques.

The problem is Robinhood's strategies encourage frequent trading, regulators say, which can lead to significant losses for investors. They also differ from those used by other digital apps that encourage seemingly beneficial habits like fitness, saving or financial planning, said Sophie Schmitt, senior analyst with the Aite Group.

"[Online banking apps] encourage healthy financial habits," Schmitt said. "Online trading has the potential to set back young investors from achieving financial goals. And that likelihood expands if the app encourages frequent engagement, which can lead to quick decisions driven by emotions."

Moreover, Robinhood's tactics could be seen as addictive and manipulative, said Daniel Simon, CEO of Vested.

"Hacking human psychology to improve how we interface with products and services can be used for good and ill," Simon said. "With any good user experience, companies can improve their products, making them simpler and easier to use, but can also manipulate their customers."

OPENING UP MARKETS

To be fair, Robinhood has been applauded for democratizing the market for young investors through the use of a free mobile experience that has driven a new millennial client base to investing for the first time, said Robert Norris, managing principal at Capco.

However, research has shown that millennials could suffer from massive overconfidence in investing, Norris said. In fact, a TIAA study found 62% of millennials assess their own financial knowledge as high or very high; however, only 19% of these respondents could answer three financial literacy questions correctly.

While investing is not a game, the use of confetti or flashing lights to drive user engagement isn't necessarily alarming, said Will Trout, director of wealth management at Javelin Strategy & Research.

"Where I see a problem is knowingly leading people who can't swim out to the deep water, and then absolving oneself of responsibility," Trout said. "More safeguards need to be in place to prevent inexperienced investors from harm. Firms need to take on this burden before the regulator does it for them."

FUELING FINTECH REGULATION

Robinhood's gamification strategy could be seen as aggressive in the sense that it takes advantage of the fact that, especially for the younger investor, there is a need for immediate gratification, said Kim Muhota, consulting firm SSA & Co.'s head of financial services for North America.

"Getting young adults to start to engage with the stock market is not a bad thing on the whole — it increases the addressable market for the industry in general," Muhota said. "But doing so without training wheels for the more sophisticated, high-risk instruments could be dangerous for the consumer, as well as Robinhood itself, which could face regulatory adverse actions, or litigation."

Some analysts see Robinhood's major growth trajectory — racking up 13 million users and boasting an $11.2 billion valuation — as the fuel that is causing regulators, including the SEC and Finra, to keep a close eye on the company, Simon said.

"Robinhood is getting the heat because they're the best at what they do," he said. "They captured the attention of a generation and are the poster child for simple, mobile-based and addictive investing."

Robinhood has done what no other wealthtech app could do — executed at scale and curated a massive market impact that has been hugely successful by capturing a client base any incumbent financial services company would be envious of, Norris said.

"[Robinhood] is perceived as leading the Next Gen of financial services," Norris said. "Usually the big fish in the pond gets the first attention."

Fintechs are generally known to be a few years ahead of new regulations, and regulators are just now trying to keep up with Robinhood as its scale erupts, Muhota said.

"The regulatory framework may just be catching up to where Robinhood is potentially shaping the industry" he said. "And that's not necessarily a bad thing."

PROCEED WITH CAUTION

Moving forward, it may be a good time for Robinhood to step back and think about whether the gamification tactics to acquire customers is a good long-term strategy or a temporary way to expand market share, Muhota said.

"This is the heart of the matter," he said. "In order for them to truly scale and build a business that lasts, they have to get in front of this and take the perspective of protecting the consumer, and not just maximizing new accounts opened and trades per account."

More broadly, Robinhood's case could also mark a threshold moment for the fintech industry when regulators make a concerted effort to pay closer attention to various players, Muhota said.

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38% PORTION OF FAMILY OFFICES THAT SAY THEY PLAN TO BOOST THEIR ALLOCATION TO HEDGE FUNDS

SOURCE: BLACKROCK GLOBAL FAMILY OFFICE SURVEY

Strategic delegating is key to success

As you map out your business strategy for the coming year, make a resolution that you're only going to do the things you really enjoy doing and are very good at, and that are absolutely essential to the success of your firm, and that you'll delegate all the rest.

GUESTBLOG
SCOTT HANSON

Why delegate? When it comes to running a business, there's nothing worse than workaholic leaders ineffectually banging their head against the wall and gumming up the works because they won't delegate.

When I coach or mentor advisers, strategic delegating is a key lesson, and one that frankly, I myself took much too long to figure out.

As counterintuitive as it may seem, if you spend 2021 primarily doing things that are a combination of what you most enjoy, what you are really good at and what moves your company's needle, and let go of everything else, you'll finish the year ahead of where you ended 2020.

But is it really that easy?

Here's what you should do. Make a comprehensive list on the left side of a page of all your activities. List everything from meeting with clients to managing portfolios, trading, research, marketing, paying the bills, negotiating leases, dealing with vendors, hiring — everything.

Make three categories across the top of the page: Passion, Skill Set and High Value. Then give yourself a score on each activity in each of the three categories from 1 to 5, with 5 being the highest.

PASSION RATING

Try not to overlap. For the passion rating, forget about how important the function may be to your practice and focus on how much you like doing it. For example, you may really like talking with vendors and wholesalers (4), but you may hate trading (1).

KEY POINTS

- Focus on the things you love and do best.
- Give yourself scores on activities to see which to hand off.

On skill set, be honest. Let's say you love managing portfolios, yet you've underperformed the benchmarks. If that's the case, give yourself a low number.

High value measures the impact the activity has on the bottom line.

Once you've rated everything, any activity where the total of the three columns adds up to less than, say, 9, should, if possible, be delegated or outsourced.

If you redirect the energy you've been spending away from all the things that don't move the needle or bring you happiness, my experience has been that both the activities you are good at, and those you don't like or are not so good at, will get more attention, and your business will have a better year because of it.

Scott Hanson is co-founder of Allworth Financial, formerly Hanson McClain Advisors, a fee-based RIA with $8 billion in AUM.

Wishing you a successful new year

Happy 2021! Like most of you, I am thrilled to welcome the new year. There's something about the promise of new beginnings that resonates deeply. It's the chance to start off fresh and clean, and think about what we want to change and achieve in the year to come.

Usually, the top resolutions have to do with money (e.g., save more for retirement, pay off debt or find a new job). Between wild market fluctuations, furloughs and job losses, there was a lot of financial uncertainty in 2020 that may cause many people to seek professional advice.

But what does success mean for advisers? As you think about the year ahead, consider what will make it a great one for you. Given all that's happened the past 12 months, many advisers are taking a long look at their practices — and their lives —

GUESTBLOG
KRISTINE MCMANUS

and coming up with different metrics for success in 2021.

TIME

In 2020, many advisers worked remotely, some for the first time in their careers. Although there are downsides, many suddenly found they had more time in their day. Zoom calls brought efficiencies compared to meeting clients in person, commute time was nil, and advisers embraced the opportunity to rethink their workday. No one misses hours spent commuting in traffic, and it seems likely a hybrid model of in-person and remote work will be the preferred practice moving forward.

FLEXIBILITY

One key victory has been the increased flexibility. Some advisers have taken the good advice they give to clients (e.g., live a full life and don't wait until you retire to do the things you want to do) to heart and are taking advantage of the ability to work remotely. One is planning a 60-day trip with his wife through Michigan to Wyoming, Montana and Colorado. They'd planned to take trips in their Airstream when the adviser retired, but because he was working remotely and client meetings were all via Zoom, they realized they could make their dream a reality now. The adviser plans to blog about their travels so his clients can keep tabs on them. Many of the firm's clients are excited about his journey and are talking about which of their dreams they could start to execute on, too. How's that for sending a message?

INDEPENDENCE

More advisers are reaching out to discuss their options for breaking away and creating their own independent firm. They've simply had enough of the constraints placed on them by their current firms, such as account minimums, investment choices or the inability to leverage social media. As one adviser told me, "I should be able to run my practice the way I want to do it, thinking only of my clients, without all these other constraints." Some advisers have wanted to change their affiliation for years; the events of the past year helped many decide they can no longer wait to make a change for the better.

FAMILY

One silver lining for many advisers has been the chance to spend more quality time with their families. Families sat down to meals, played board games and watched movies together. One adviser confided that he used to work crazy hours and had a long commute, which meant he came home long after his children went to sleep. Since the pandemic began, he has realized just how much he's missed by not putting his kids to bed, and he has resolved to be home by bedtime.

COMMUNITY

It's a curious thing: Financial advisers are in the business of managing money, yet no one I've spoken to has specified increased production as a measure of their success. Many have told me they make more money than they thought possible. But money is not their motivator; instead, their focus is on giving back and helping less fortunate members of their community. Not surprisingly, these advisers are feeling a renewed sense of purpose and meaning in their work.

Do any of these goals resonate for you? Although no one wants to repeat the past year, the positives it generated are ours to keep. Whatever your vision for success, here's hoping 2021 brings you closer to attaining it!

Kristine McManus is vice president and chief business development officer at Commonwealth Financial Network.

RIOT REACTION

CONTINUED FROM PAGE 2

pins how and why we can invest."

Ryan Greiser, founder of Opulus, a registered investment advisory firm, said he had talked with millennial clients who thought Wednesday was "a dark day for our country." But they remain optimistic about investing.

"Here's where our conversations have landed, they still believe that America is better than this," Greiser wrote in an email. "They believe that American ingenuity and leadership will see us through, hopefully, sooner than later. The clients we talk to still value America's core beliefs. As we continue to align those values with our clients' investments, we can connect the two to a brighter future."

Meanwhile, advisers and analysts also cautioned investors and clients not to confuse ugly, divisive political action like riots with what's happening in the broad stock market, which has been on a record run since March and the advent of COVID-19.

"The market will do whatever it needs to do to prove the largest number of people wrong at any given moment," said Ron Carson, founder and CEO of Carson Group. "Always has, always will. Market highs despite COVID-19 is a great example."

DIVISIVENESS 'LAID BARE'

"The biggest risk is trying to outguess it," Carson said. "So while the chaos at the Capitol in Washington, D.C. yesterday has had everyone on the edge of their seats as a deep divisiveness was laid bare for the world to see, the market seems to be sitting back and viewing the world through rose-colored glasses."

"Investors would be wise to untether themselves from politics when it comes to their investment strategy," he added.

"The markets have been separated from Washington since President Obama, through Donald Trump and likely through a Biden administration,'" Gary Schwartz, founder of Madison Planning Group in West Harrison, N.Y., wrote in an email. "America has gone through far worse and always come out the better for it."

"History has traditionally rewarded those who have maintained their faith in the American economy, the best the world has ever seen," he added.

"THE RULE OF LAW PREVAILED ... [IT] UNDERPINS HOW AND WHY WE CAN INVEST."

BRIAN O'NEILL, WINGED WEALTH MANAGEMENT

"By any account what happened yesterday at the Capitol was disgusting and sad," said Manish Khatta, president and chief investment officer at Potomac Fund Management. "However, let's not confuse noise with substance. When it comes to the markets, geopolitical events have little correlation with the performance of the stock market."

"The markets were supposed to crash after Trump took office, the China trade war, Iran tensions, contested elections, etc. I could go on and on," Khatta said. "It's all noise. Follow the price because price is all that matters. Price is pure. There is truth in price."

— Liz Skinner, Mark Schoeff Jr., Emile Hallez, Jeff Benjamin and Sean Allocca contributed to this report.

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LPL FINE

CONTINUED FROM PAGE 2

paid $70 million in fines and restitution to customers, a staggering sum for a retail-focused broker-dealer.

In recent years, LPL has not faced as many severe penalties, although in 2018 Finra fined the firm $2.75 million for failing to list dozens of customer complaints against its brokers and for not filing hundreds of suspicious activity reports in its anti-money laundering program.

SIX-YEAR SPAN

LPL's settlement with Finra covers the period from January 2014 to September 2019. During that time, LPL failed to fingerprint more than 7,000 non-registered associated persons and failed to screen these individuals for disqualification based on criminal convictions, according to Finra, allowing one employee who should not have been hired to work at the firm.

LPL also failed to retain electronic records in the required format, according to Finra, affecting at least 87 million records and leading to the permanent deletion of over 1.5 million customer communications maintained by a third-party data vendor.

INSUFFICIENT REPORTING

The firm also fell short in supervision of consolidated reports generated by outside vendors that its advisers used, according to Finra. The vendors did not send the reports to LPL and the firm did not review them.

LPL accepted the settlement without admitting or denying Finra's findings.

"We take our compliance obligations seriously, and have been proactive in identifying, reporting and remediating these issues," LPL spokesperson Jeff Mochal wrote in an email. "We've made significant investments to strengthen our capabilities related to this important work."

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BITCOIN

CONTINUED FROM PAGE 3

get choppy.

But that argument wasn't holding water earlier this year when global markets continued to slide in response to plummeting oil prices and growing panic about the economic fallout from the coronavirus. While the S&P 500 and Dow industrials experienced some of their steepest drops in history, Bitcoin performed even worse.

That type of volatility has stopped Michael Caligiuri, founder and CEO of Caligiuri Financial, from recommending cryptocurrencies to his clients, for now.

"Advisers need to be extremely clear about the risks of cryptocurrencies with clients as there could be a relatively high chance that they could lose everything," he said. "I believe Bitcoin is more of a short-term fad than a long-term sustainable asset class."

NOT WORTH THE EFFORT

For some advisers, the legwork to incorporate digital assets isn't worth the return on investment. For example, trading cryptocurrencies requires multiple account openings, which is tedious, according to Thomas Hlohinec, founder and CEO of Rise Financial Partners. "For a small percentage of a client's portfolio, it isn't always worth it," he said.

Matt Bacon, an adviser with Carmichael Hill, agrees that crypto assets are too volatile and speculative right now to be of much use to advisers. Long term there could be a place for it, but it's going to take time for it to truly solidify its status as a unique asset class, according to Bacon.

"It could act as a hedge and store of value in a way that's similar to gold, but it's not there yet," he said. "We don't recommend crypto assets to clients but do purchase them upon request."

Yet there are advisers who believe that digital assets are here to stay and that like any disruptive technology, it takes time for new innovations to take hold, said Lexington, Kentucky-based adviser James Vermillion.

"We don't see Bitcoin as a fad or trend, in fact, we see an acceleration of its adoption as both a financial instrument for transactions and an investment asset class for both institutional and retail investors," he said.

More education for advisers on how digital assets could benefit a client's portfolio could also lead to more adoption among RIAs, said Mike Casey, president and founder of American Executive Advisors.

"Cryptocurrencies should be considered for every investor's portfolio," Casey said. "Advisers who take the time to learn and understand the implications of blockchain technology and digital assets will be well positioned to advise their clients."

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ANNUITY RULE

CONTINUED FROM PAGE 3

Michigan Gov. Gretchen Whitmer signed an annuity best interest law on Dec. 29, while the Arkansas Department of Insurance approved a rule on the same day.

The state-level annuity rule aligns with Reg BI and is "creating a strong state and federal network that protects consumers," said Michelle Carroll Foster, regional vice president for state relations at the American Council of Life Insurers. "The [annuity] model rule is protecting more and more consumers across the country with a best interest standard of conduct."

The NAIC model rule must be adopted legislatively or through the regulatory process by each state. COVID-19 hit just as the state-by-state effort was being launched. That slowed down the process, but it picked back up later in the year.

"We are very pleased with the momentum coming out of 2020," said Liz Pujolas, director of state affairs at the Insured Retirement Institute. "Not only did industry have to pivot and work in a remote environment, so did legislators and regulators. This has been tremendous. I anticipate an active first quarter."

Variable annuities are often cited by investor advocates to illustrate the harmful results of financial advisers' conflicts of interest.

The products provide something most investors want — a guaranteed income stream during retirement — but also can be complex and carry high fees that can enrich the insurance agents and brokers recommending them.

The Center for Economic Justice and the Consumer Federation of America said the NAIC model rule is insufficient for curbing conflicts of interest related to annuity sales.

'FULL OF LOOPHOLES'

The annuity sales rule "does not impose a true best interest standard," Birny Birnbaum, executive director of the Center for Economic Justice, and Barbara Roper, director of investor protection at the Consumer Federation of America, wrote in a December 2019 letter to the insurance commissioners. "It is simply a restatement of the obligation to make suitable recommendations. Calling it a best interest standard is misleading. Moreover, the standard is vague and full of loopholes. The current draft remains considerably weaker than even the vague and ineffective SEC rule."

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LUCKY LOTTO

CONTINUED FROM PAGE 4

quickly. Bovard has an NFL client who is currently in his third contract.

OUT OF THE WOODWORK

A common scenario for the newly wealthy is that old acquaintances or extended family members come knocking, advisers said. Financial professionals can serve as intermediaries who help protect accounts from being drained by an abundance of well-intentioned lending and gift-giving.

Bovard, for example, said clients should have a form they give to anyone asking for money, which the adviser can review.

"That can oftentimes be used as a good deterrent for the majority of people asking for money," he said.

REMAINING ANONYMOUS

"If you live in one of the handful of states that allow lottery winners to remain anonymous, do so," financial planner Danielle Harrison wrote in an email. "And for those who don't, put the ticket in a safe place and make sure you have your team assembled before notifying anyone of your fortune."

Brent Bell, owner of Bell Financial Planning, recommends putting a winning ticket in a safe place, even before signing it.

In some states, "hiring an estate attorney to set up a trust and allowing your trustee to sign the ticket allows for you to potentially set up a barrier between you and anyone else that may want your money," Bell wrote in an email. "If your state doesn't allow for this type of anonymity, then I would recommend signing the ticket right away, locking up the ticket again and then deciding on whether to hire someone to address the media for you."

ASSEMBLING A TEAM

Lottery winners need a good estate planning lawyer, an accountant and a fee-only fiduciary adviser, said Harrison, whose firm is Harrison Financial Planning.

"And finally, who I would deem the most important person on the entire team — a therapist well versed in helping clients understand their relationship with money," she wrote.

More money can indeed cause more problems, including feelings of guilt, anxiety, isolation and strains on relationships, she said.

BIG BUMP IN BUSINESS

Firms that take on such clients can see their assets under management more than double in an instant. In 2013, for example, Jacksonville, Florida-based Madden Advisory Services was hired by Gloria Mackenzie, then 84, who received a lump-sum payment of $371 million from Powerball, or $270 million after taxes. At the time, the four-person firm managed about $203 million. The bump in assets would allow the firm to expand in order to help the client, the firm indicated.

Having a big new client can also help a firm hire up and boost its breadth of in-house expertise, Bell said.

"Having a client of this magnitude would also mean that my firm could provide more pro bono financial planning for families and spend more time to educate children and young adults to be more financially successful," he wrote.

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ROBINHOOD

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"There are a lot of questions raised by the revolving door on the intentions of all the parties," said Scott Amey, general counsel at the Project on Government Oversight. "People with friends in high places are often treated differently than those who are not in the same situation. That can be beneficial for Robinhood but can come at a price to the public, especially when there are serious allegations against a company."

Gallagher counters that it's good for financial firms to employ former SEC officials because they bring the agency's investor-protection ethos with them.

"We're cognizant of everything the SEC expects and we're steeped in the ways of the securities laws," Gallagher said. "We're an ambassador for that view, which should be elevating everybody's game. That's a pretty powerful thing to bring into the private markets."

SETTING GOOD EXAMPLES

In 2014, LPL Financial hired former Vermont securities director John Cronin to help it better supervise its far-flung adviser network. Cronin transitioned to government relations and is now "one part of a concerted effort to create, build and enhance relations with our state regulators," he wrote in an email.

I saw him do that firsthand during a North American Securities Administrators Association annual conference in Providence a couple years ago. Once a NASAA leader, the affable Cronin was active on the sidelines of the meeting chatting up his former colleagues.

His other role is internal consulting. "The goal of these efforts is to allow [LPL] access to a state regulator's perspective as they examine issues and respond," Cronin wrote.

Steven J. Thomas brought the insight of a former South Dakota chief compliance examiner to his role as chief operations and compliance officer at SGL Financial.

"When you teach other examiners, you know what they're going to be looking for when they come in and examine a firm," Thomas said. He said firm leaders listened to him when he urged them not to let advisers sell shares in Woodbridge Group, a luxury real estate developer that committed fraud and went bankrupt.

He established when he was hired that compliance would be respected.

"It's my way or the highway, or I'm not taking the job," Thomas said.

When erstwhile regulators join a firm, they can attract others from similar positions. Gallagher has hired a number of former high-ranking SEC and Capitol Hill staffers.

The Robinhood government relations team is trying to change how Washington views the firm. Their message is that Robinhood is beefing up compliance but also is attracting new investors to the capital markets.

"Most of it is telling what Robinhood is and how we got started and demystifying and correcting a lot of narratives that have been persisting," Gallagher said.

The revolving door is more likely to lead to regulatory capture when it swings as an industry official or lawyer takes a break from a Wall Street career to run the SEC. Perhaps that will be the subject of a future column.

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