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Failure to Disclose — Enforcement Cases Analysis

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Although certain types of conflicts of interest are defined as prohibited activities, some conflicts of interest are a normal part of operating as a broker/dealer. For example, most registered representatives receive commissions on the purchase or sale of securities they recommend. This can pose a conflict of interest, because the representative directly benefits from the trade. However, as long as this compensation is disclosed, the registered representative is complying with regulatory rules regarding the disclosure of conflicts of interest.

FINRA disciplinary cases are filled with instances of member firms and registered representatives who have been fined and/or suspended for not making a required disclosure to a client, regulator, or the representative's firm. 22% of FINRA enforcement cases between June 2009 and May 2010 included some form of undisclosed conflict of interest.¹ Here is a detailed account of the number of disciplinary cases that involved a failure to disclose.

¹ The true statistics for this analysis may have small variances attributed to the fact that some cases have multiple types of failures to disclose. Approximately five cases had two types, and one case had three types.



Cases in which material information was not properly disclosed by firms or representatives to clients:

Failed to Disclose...	# of Cases
<i>Material Information to clients</i>	
Average Price Execution	10
Buy/sell indicators	1
Commissions mark ups/downs	7
Compensation type	1
Correct information on confirmations	2
Delivery of prospectus	1
Directed trade arrangements	1
Discretionary activities	2
Extended offering period/reconfirmation to subscribers	1
Financial Interest	8
Inconsistencies in offering memorandums	1
Principal capacity/market maker capacity	17
Product fees and/or features	3
Relationship with issuer	4
Risks of products being recommended	5
Routing venues/profit sharing arrangements	1
Routing venues/trade execution	1
Soft dollar arrangements	1
Time order received/executed	2
Unspecified	10
Valuation methods	3



Cases in which material information was not properly disclosed by a representative to the rep's firm:

Failed to Disclose...	# of Cases
<i>Material Information to Firm</i>	
Borrowing from clients	6
Client identity	1
Discretionary activities	1
Finder fee arrangements with nonregistered persons	2
Gifts	1
Outside business	11
Personal brokerage accounts	13
Private securities transactions	4
Replacement transactions	1
Selling away	2
U-4 information	66
Unspecified	4

Cases in which material information was not properly disclosed by firms to regulators:

Failed to Disclose...	# of Cases
<i>Material Information to Regulators</i>	
U-5 information (complaints)	2
Unspecified	1
Use of nonregistered cold callers	1

Cases in which material information was not properly disclosed by representatives or firms in communications to the public:

Failed to Disclose...	# of Cases
<i>Material Information in Communications</i>	
Basis for performance figures	1
Limits or restrictions on benefits	2
Member's name	1
Name of wholesale entity	1
Research reports/ firm ratings distribution	1
Research reports/material information (unspecified)	1
Research reports/securities holdings	1
SIPC disclosures	1
Sound basis for recommendation	1
Unspecified	1



So what can we learn from this analysis? One notable conclusion is the number of failure to disclose U-4 information (66 cases) outnumbered the second highest failure to disclose, principal capacity disclosure (17 cases), by almost 400%. This statistic raises many questions, such as:

- Is the failure to disclose U4 information deliberate?
- Do representatives who fail to disclose U4 information feel they will be able to get away with it?
- If more representatives knew these statistics, would they be less likely to withhold U4 information?

What conclusions would you draw from this exercise?

Click the link at the bottom of this page and let us know. All responses remain anonymous, and a summary is sent to all who participate.****

Was this excerpt everything that you thought it would be? Are there conflict of interest issues that FIRE could report on or investigate for you? FIRE would love to hear any and all feedback regarding this excerpt. Click [here](#) to let us know your thoughts.

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