

## *Advisory News Brief*

The shenanigans of several Wall Street firms have recently been receiving a fair amount of press. While the current transgressions are indeed noteworthy, questionable corporate practices in the financial industry are anything but new. During the past twenty years, investors have been burned by periodic misdeeds that have ranged from self-dealing to outright fraud and deception.

Roof Advisory Group has often cautioned investors to cast a jaundiced eye toward Wall Street's games and claims; particularly when purporting to represent your best interests. The latest revelations make it clear that a prudent approach for an investor to take when reviewing brokerage firm recommendations might be continually repeating that sage Latin phrase "*caveat emptor*", i.e. 'let the buyer beware'.

On April 28<sup>th</sup>, the egregious conflict of interest that has long existed between the research and investment banking areas of major brokerage firms was exposed for all to see. Ten of the largest securities companies in the country agreed to collectively pay \$1.4 billion to settle extensive charges of flagrant investor abuse. (see 4/29/03 Wall Street Journal article). Some of the charges included distributing fraudulent investor research, paying other firms to 'guarantee' favorable research of an investment banking client, and "spinning" initial public offerings (IPOs) by providing pre-issue shares to corporate executives from whom the brokerage firms wanted investment banking business. This latter practice was described by regulators as "virtual commercial bribery".

Will the culture that spawned such investor-unfriendly practices be dramatically and sincerely changed by this financial slap on the wrist? It is doubtful.

To wit, the Wall Street Journal reported that on the day after the settlement was finalized Morgan Stanley's Chairman Philip Purcell appeared to discount any concerns retail investors should have about his firm's alleged practices. This response was immediately met with a strongly worded rebuke from Securities and Exchange Commission Chairman William Donaldson. Mr. Donaldson noted that Mr. Purcell's "reported comments evidence a troubling lack of contrition" and "reflect a disturbing and misguided perspective" on his firm's alleged misconduct. Mr. Purcell apologized, agreeing not to deny the SEC allegations.

Soon after on May 12<sup>th</sup>, it was reported that a Bear Stearns research analyst, (in fact, a senior managing director), had recently appeared in a road show promotion touting an impending IPO. This is a practice the brokerage firms agreed to eliminate as part of their April 28<sup>th</sup> settlement with the SEC. Bear Stearns apologized, swearing it would never happen again.

Now the SEC has launched a fact finding probe to determine if brokerage firms have conflicts of interest in the way they are compensated when selling mutual funds to investors. The Wall Street Journal reported on May 22<sup>nd</sup> that the probe will examine "whether brokerage firms have pushed mutual-fund products on customers because of compensation they receive, rather than based on customer needs". It also reported that the SEC wants to determine "whether brokers receive undisclosed compensation for selling certain mutual funds". Stay tuned for the results but don't expect good news for brokerage firm clients.

*(over)*

Conversely, Roof Advisory Group clientele don't worry about conflicts of interest. We have always been an independent *fee-only* investment advisory, management, and financial planning services firm. Our full compensation is completely disclosed and comes directly from the services, not products, we provide. The firm does not receive commissions, trailers, or referral fees for any work we do. This approach assures clients of our objectivity and that their best interests *are* top priority.

Also included for your review is a recent PA Business article by Roof Advisory Group's Stephen Franklin that reinforces the value and necessity of proper financial planning.

As a client, we again thank you for your valued business. Remind those who are not, "*Caveat emptor, caveat emptor, caveat emptor...*"

**E. Jeffrey Roof**