

UNSCRUPULOUS FEES

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A popular method for unscrupulous brokers and advisors to generate revenue to make those quotas and to keep their sales managers happy is churning. Churning is when in a broker excessively trades an account to generate commissions. Currently fraud charges are being brought against firms that are levying excessive fees in wrap accounts. This past December the former state attorney for New York sued UBS Paine Webber for overcharging customers where investors pay a percentage of their assets each year for a flat annual fee. The reality is that in certain circumstances certain individuals are better off paying commissions.

The Wall Street Journal reported that UBS is denying the charges. Other financial firms to be accused of the same shenanigans include Morgan Stanley, A.G. Edwards, and Raymond James. They have all paid fines for this despite neither admitting nor denying guilt. Currently the Securities and Exchange Commission is probing Merrill Lynch for the same misconduct. What the firms are doing is moving the wrong investors to fee-based accounts.

For example: Client A has a handful of securities worth approximately \$750,000. Client A's securities are not to be sold and are used to provide income. No hedging strategies are used in the account. Client A SHOULD NOT be paying 3% a year in a wrap account, yet according to the New York state attorneys office there are thousands of clients in this predicament who paid millions of dollars in unnecessary fees and commissions and his suit is limited to just UBS. One 91-year old woman cited in the suit paid \$35,000 for four trades over two years. The NASD warned all its member firms in 2003 that they must ensure that only appropriate clients would be placed into fee-based accounts.

In an article in Investment News, the Spectrum Group conducted a study finding that nearly half of affluent investors who owned mutual fund wrap products and managed accounts did not have any idea regarding the amount of fees they were paying. The report entitled, "Perception and Understanding of Fee's," found that 46% of affluent investors with \$500,000 or more in investible assets were unaware of how much they paid in fees for mutual fund wrap accounts. In another finding, 42% of affluent managed-account owners did not know what percentage of assets they paid in fees for their managed accounts. However, when asked if they had a good understanding of fees in general, nearly three-quarters responded they did.

To avoid this situation you need to ask certain questions. We are always railing against conflicts of interest, so make sure you ask how your broker or advisor is paid, always ask if he or she receives extra compensation for selling certain financial products or services over others. Make sure you always ask if the fee structure proposed by your broker or advisor is the most economical arrangement for you and why. Have your broker or advisor put it in writing citing all the services that our included.