

Excerpts from:

Take on the Street

What Wall Street and Corporate America Don't Want You to Know

What You Can Do to Fight Back

By Arthur Levitt

Former Chairman of the Securities and Exchange Commission

Concerning the brokerage industry:

“Brokers may seem like clever financial experts, but they are first and foremost salespeople.”

“Warren Buffett, the chairman and CEO of Berkshire Hathaway Inc. and one of the smartest investors I’ve ever met, knows all about broker conflicts. He likes to point out that any broker who recommended buying and holding Berkshire Hathaway stock from 1965 to now would have made his clients fabulously wealthy. But any broker who did so would have starved to death. While working for his father’s brokerage firm in Omaha, Buffett says he learned that “the broker is not your friend. He’s more like a doctor who charges patients on how often they change medicines. And he gets paid far more for the stuff the house is promoting than the stuff that will make you better.” I couldn’t agree more. In sixteen years as a Wall Street broker, I felt the pressures; I saw the abuses.”

“Sadly, the brokerage industry still has numerous flaws. That’s not to say that all brokers are commission hungry wolves on the prowl for naïve investors. Some are; others are just inept. Most are honest professionals. They are good people stuck in a bad system, whose problems remain fourfold. First, some brokers are not trained well enough for the enormous tasks they are expected to carry out. Second, the system in which brokers operate is still geared toward volume selling, not giving objective advice. Third, to increase sales, firms use contests to get brokers to sell things that investors may not need. Most brokers rarely, if ever, disclose to their clients how they are paid or how their bonuses are structured, even though such disclosures would go a long way to resolving the conflict-of-interest problem. Fourth, branch office managers and other supervisors, who are paid commissions just like their brokers, have an incentive to push everyone to sell more and to turn a blind eye to questionable practices.”

“Brokerage firms never seem to run out of novel ways to use commissions to motivate their brokers—and take more money out of your pocket.”

“... the temptation to sell anything to anyone, no matter how inappropriate, is overwhelming.”

“... the broker is likely to push unwanted or unneeded products, especially those paying higher commissions.”

“If you have more than \$50,000 to invest, you should fire your broker and find an investment advisor. Brokerage firms would like you to think that they perform the same functions as investment advisors. But they’re not the same as independent investment advisors. Brokers do not have a fiduciary duty—a legal obligation—to put your interests above his or the firm’s. An investment advisor’s fiduciary duty is on a higher plane, like that of a lawyer, a trustee, or the executor of an estate.”