

## Potential Advisor Rules Changes in 2021 - Transcript

**Tom Mullooly:** ... So you asked how this might impact our clients. I think it's important that clients understand that the world that we operate in is changing. I also think it's important to realize, or to make listeners realize, right now there are a lot of rules and there's a lot of things that are prohibited. And so we can't say things that we want to say. The flip side to that is when you see firms and other people in our industry saying things that they shouldn't be saying, it should be a bright red flag for people to run.

**Casey Mullooly:** Yeah. We're operating within a framework that kind of, we're kind of like threading the needle, saying things, but using language that isn't very specific. So when advertisements seem really good, I think people should want to know more and question that and go to their own advisors, or when they're looking to start with another advisor, use those advertisements and kind of try and pick them apart, be like, "Hey, well you said this. What does that mean? How exactly do you go about doing that?"

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**Tom Mullooly:** Welcome back to the podcast. This is episode number 337. If you listen to the podcast often enough, you'll hear at the very beginning that Tom Mullooly is an investment advisor. And our disclaimer that's being mentioned at the beginning of that podcast that is read by Casey Mullooly, who is joining me today for a very special end of the year 2020 podcast. Casey, welcome to the podcast.

**Casey Mullooly:** It's good to be here. Compliance Casey reading those disclosures. That's how I'm known here in the office.

**Tom Mullooly:** But you're known for a lot more, but it's also episode 337, which was your batting average.

**Casey Mullooly:** It's higher than that, come on.

**Tom Mullooly:** The reason why I asked Casey to come in here today, we're recording this on December 22nd, right at the end of the year, 2020, quite a year. Casey alerted me to some news that came out just today, hot off the presses from our friends at the Securities and Exchange Commission.

**Casey Mullooly:** Yeah. So we're looking at a press release from the SEC about how they plan to adopt a modernized marketing rule for investment advisors. So this is going to have big implications on our firm and all of the other investment advisory firms out there. Pretty big change, it looks like it's coming down the pipeline. It's not a rule just yet, but it's a proposed rule,

which means in the next 60 days, they will either vote to pass it or not. Yes, some big change is coming our way.

**Tom Mullooly:** So the process, the way it normally unfolds is they'll issue this proposed act, or this comes with a press release like this along with some facts. And then as Casey mentioned, they'll open it for public question and answer period. And so there'll be 60 days where people who are impacted by this can pose questions or comments. After the 60 days, then the SEC will actually close the comments and questions and then they'll vote on this. So I would imagine that this is going to be voted on sometime before the end of the first quarter. And then they'll have some kind of like an icebreaker period of time where they'll say, "Okay, this'll be effective June 1st or something like that." And then they also mentioned in this press release that there'll be like an 18-month window of time where people can get up to speed because they did change some other things, bookkeeping issues as well.

So this kind of leads to a greater discussion. One of the things that they talk about are payments to solicitors. We don't pay a solicitor, but a lot of people in our industry do. Let's talk about that, because I don't think a lot of people that are investors or clients, I don't even think they're aware of what this practice is.

**Casey Mullooly:** Right. So, pretty much when you pay solicitors, what that means is you're paying someone else, usually some sort of third party to either get on their platform and help attract new clients that way. So you're not really dealing with the investment advisory firm themselves, you're dealing with someone who's paid to act on their behalf-

**Tom Mullooly:** Right.

**Casey Mullooly:** ... which can kind of be misleading for the everyday investor out there.

**Tom Mullooly:** It could also be as simple as paying someone to cold call for you.

**Casey Mullooly:** Yeah.

**Tom Mullooly:** Or have people come to your chicken dinner seminar, which I haven't had too many of them this year with the pandemic, but to get people-

**Casey Mullooly:** Zoom chicken dinner.

**Tom Mullooly:** ... to come to a Zoom chicken dinner seminar, come to some kind of meeting online or in person, or just make appointment centers.

**Casey Mullooly:** Yeah.

**Tom Mullooly:** And these people get paid and they get paid really well.

**Casey Mullooly:** Yeah. But you got to think about how they get paid. So maybe they get paid on like every new lead that they generate or every new client that they get in. They get a cut of that.

So the incentive behind that is fit every person that you're calling into the model that the firm is using. So it might not always be in the client's best interest, but they don't really know that.

**Tom Mullooly:** Right. So they are pegs round and square. Some of them are round and they're going to fit.

**Casey Mullooly:** And they're jamming up in there-

**Tom Mullooly:** Others are square.

**Casey Mullooly:** ... because they are paid to do that.

**Tom Mullooly:** Yeah, they're not going to fit. That's why on our website, we talk about coming in for a fit meeting. That's part of our process. We can't really have people come in the office right now, but we can have people meet over the phone or on a Zoom meeting. And we talk about, "Let's find out if we're a fit for each other." We don't use a solicitor. And so when people find us on the web or find us through a referral, we encourage them to schedule a meeting with us, which they can do right through the website. And then it's a 15, 20, 30-minute chat just to hear their questions and concerns and ask us all the questions they can think of to find out if we're a good fit. It's a practice that I wish other firms were doing. I'm surprised more of them don't, but it's easier to just write a check to somebody like a solicitor-

**Casey Mullooly:** Yeah.

**Tom Mullooly:** ... and have them go ahead and do this.

**Casey Mullooly:** This new update to the rule sounds like it's actually going to make it easier for those firms hiring the solicitors to do their job and bring in more clients. Am I reading that right?

**Tom Mullooly:** Yeah. So what I imagine now is when you type in financial advisor near me, financial planner near me into Google, what you're going to see are going to be things like what you would find when you go to type in insurance. You're going to find select quote. You're going to find all these things where they're basically just lead producers and it's going to be like, "Call us, we will fit you with the right guy or girl." And those people will get paid a lot of money to place potential clients with these firms, will cost a lot of money to do it. But I think we're going to see that part of the industry is probably going to rip a lot higher.

**Casey Mullooly:** That sounds like whoever has the biggest advertising budget is going to be coming out on top. Something to keep an eye on.

**Tom Mullooly:** Right. So think about who does a lot of advertising right now? The big firms do a ton of advertising, but when I say a big firm, I think of the big brokerage firms like Merrill Lynch and Morgan Stanley and places like that, but Fidelity and Vanguard do even more advertising.

**Casey Mullooly:** Yeah. You think about, especially with all these big firms buying RIA branches and stocking up these billion-dollar RIA firms into these JPMorgan, Morgan Stanley, all of these big firms are just kind of... Even Charles Schwab is kind of making a play into the RIA space.

**Tom Mullooly:** Right.

**Casey Mullooly:** So, yeah, it'll be really interesting to watch and see how that plays out.

**Tom Mullooly:** Makes me scratch my head and wonder what is Fisher Investments going to do. They spend a lot of money as a pure RIA, registered investment advisory firm on not only television ads, but print ads, mail campaigns, they even do banner ads. They do click through ads on search engines. They're everywhere.

**Casey Mullooly:** Yeah.

**Tom Mullooly:** And they get clients everywhere.

**Casey Mullooly:** Yeah. We're going to have to get creative.

**Tom Mullooly:** Yeah. They talk about this marketing rule. And I just want to spend some time talking about marketing and advertising the way our industry is set today and then talk about what they're proposing to change.

**Casey Mullooly:** Sure.

**Tom Mullooly:** So right now, we can basically say nothing in our ads. Come talk with us.

**Casey Mullooly:** Yeah.

**Tom Mullooly:** That's about the long and short of it.

**Casey Mullooly:** Yeah. We're even limited on some of the language that we can use if it's over promissory or not. We have to be really careful when we're wording even the phrases on our website and especially if we're using print or any other type of ads, even words like confident, certain, we really have to thread the needle there in terms of what we say. We can't talk about any specific investments, any sort of performance or anything like that, really. We just kind of have to say what we do in the most basic language possible.

**Tom Mullooly:** And it's not just us. This is every-

**Casey Mullooly:** Right. Yeah. Everyone's playing by the same rules.

**Tom Mullooly:** ... every firm that's out there. So when you do find a firm that is not complying with the rules, that's a red flag.

**Casey Mullooly:** Hopefully the SEC would find that first.

**Tom Mullooly:** Yeah. They're kind of spread pretty thin.

**Casey Mullooly:** Yeah.

**Tom Mullooly:** But, yeah, even phrases, we were cautioned. I'll use that phrase. We were cautioned that getting investors on track or staying on track or reaching your retirement goals, these are promissory words and phrases that we really should not be using in our marketing, marketing covering letters, ads that we run. And we run ads, website, which is considered an advertisement in the eyes of the regulators.

**Casey Mullooly:** Yeah. It's tough. Yeah, this is currently what's going on. So this is kind of the framework that we're operating under now.

**Tom Mullooly:** This is why you see a lot of websites and a lot of ads for people in our industry with pictures of sailboats.

**Casey Mullooly:** It's hard to stand out. It's hard to be unique because we're all... We're very different specific firms are very different in their actual processes. We all do things differently, but we all kind of say that we do the same things and have to use sort of the same language because of these rules that are in place that are limiting us to not really be able to explain what we do in specific ways. We're not able to say that we help people. I'm not going to say what we're not allowed to say, but yeah, it's tough. It sounds like some changes that are on the way, which are going to open the door for investment advisory firms like ours to kind of not necessarily take the reins off completely, but to be a little bit more open in the way we say things.

**Tom Mullooly:** A little more transparent.

**Casey Mullooly:** Hopefully.

**Tom Mullooly:** Less opaque.

**Casey Mullooly:** Yeah.

**Tom Mullooly:** Yeah.

**Casey Mullooly:** Although this kind of does this adoption of... It's a proposed rule. So nothing's final yet. This could all be washing two months, but it's interesting to see... We had the whole fiduciary rule. What was that, 2018? So a couple of years ago now, and now with the form CRS that came out this year. Form CRS is the customer relationship summary.

**Tom Mullooly:** Right.

**Casey Mullooly:** Client relationship summary. So that was a new form that all investment advisory firms and all-

**Tom Mullooly:** All the firms.

**Casey Mullooly:** ... All financial firms had to adopt this new form, which is basically another disclosure form where we make it very easy for our clients and prospective clients to see where our conflicts of interests are.

**Tom Mullooly:** It's very similar in my opinion, to form ADV, which we're required to give to all of our clients.

**Casey Mullooly:** Right. It's more of a condensed version of that. And I do think that it's easier to identify the important factors for the everyday investor. The form ADV, 30, 35 pages.

**Tom Mullooly:** It's a lot to go through.

**Casey Mullooly:** Form CRS has to be two pages, has to be similar formatting for all of these firms. But it's interesting to see because it looks like in some ways it's getting harder for us, meaning we're required to disclose more and we have to be more transparent. And then this new rule kind of walks that back a little bit and kind of loosens it up a little.

**Tom Mullooly:** Now, I thought, and I think you were just as surprised as I was. So I'll share with you some of the numbers that Casey and I learned about over the summer with form CRS, this was a new required form that all advisory firms had to...

**Casey Mullooly:** Had to send to their clients in 2020.

**Tom Mullooly:** Yeah. And we did, had to make it available and send to our clients. We found that 40%, 40% of advisors didn't even do it. And another large percentage left it blank or incomplete.

**Casey Mullooly:** Interesting.

**Tom Mullooly:** I don't know what the adoption rate is going to be on this new advertising rule, this new marketing rule. But I fully suspect that one of the things that they talk about are testimonials.

**Casey Mullooly:** Right. That's the big change.

**Tom Mullooly:** That is huge. Right now, you can't have testimonials or endorsements. Not an endorsement by a celebrity or a testimonial from a client, current client, past client, doesn't make a difference. You can't use testimonials in our business in 2020, and it's been this way for my entire career.

**Casey Mullooly:** Which dates back to...

**Tom Mullooly:** 1983. So it's important to underscore that if you're looking at someone's website or marketing material, which is a website it's considered marketing material in our business, and you see testimonials, even testimonials where they just have someone's initials. That's prohibited.

**Casey Mullooly:** Yeah.

**Tom Mullooly:** In fact, you can't even use testimonials where they say, "I like working with this firm because they call me back."

**Casey Mullooly:** Yeah.

**Tom Mullooly:** Or, "They answer their phones on the first ring." Or, "They do things promptly." You can't even say things like that. And so there's that implied promise to deliver in those testimonials, you can't use them, but it appears that that might be changing with this new rule.

**Casey Mullooly:** Yeah. It appears that that's just going to be completely flipped. The new proposed rule will allow the use of testimonials and endorsements, which include traditional referral and solicitation activity, subject to certain conditions. So pretty much the new rule is saying that you're going to be allowed to use these testimonials and endorsements, but you're going to have to disclose where they're coming from in some regard.

**Tom Mullooly:** They can make that print pretty small.

**Casey Mullooly:** Yeah. It's so weird because reading it is... These press releases, especially from the SEC, the government, they're pretty tedious and boring to read through, but that's huge.

**Tom Mullooly:** It's a huge change.

**Casey Mullooly:** Allowing testimonials and endorsements, that completely changes the advertising game for the entire financial landscape.

**Tom Mullooly:** I don't know how many listeners have seen our commercial that runs on the local cable channels. But we've been running them, we've been running the same two ads now for about four years. I think if people see them a lot, they're probably getting tired of them.

**Casey Mullooly:** Yeah.

**Tom Mullooly:** But maybe we should change them once this rule, if it becomes effective and have a couple of clients on there talking about what their experience has been like. It'll definitely be different.

**Casey Mullooly:** Yeah. I think that that's certainly helpful for people. We've seen the explosion of Yelp and other online review services in the last couple of years. And I'm just thinking about like, when I go on somewhere, I definitely look up not necessarily the Yelp review, but I'm thinking of like Amazon, the reviews left on an Amazon product are testimonials or endorsements. They're really helpful when I'm trying to decide what new shoes to get. Or those

are probably the main things that I pay attention to when I'm looking to buy a new service or a product I'm thinking about also, just local like plumbers or electricians or contractors. If they have any sort of web presence at all, that has to be one of the main drivers of their business.

On that hand, I think it could be really helpful for the new investor or prospective client to see what other people's experiences have been like. I agree that it could be a slippery slope in terms of what happens for one client isn't necessarily going to happen for the other client. Like that definitely has to be kept in mind, but it could be good, I think for people trying to decide which advisor to use.

**Tom Mullooly:** Now, there is one thing that I've learned in the last 12 months, and this comes from our friends at Twenty Over Ten, including Samantha Russell. She pointed out quite correctly that Google reviews are fine. I am not asking clients to go on Google and leave a review. We don't ask people to leave reviews. But one of the reasons why a Google review is acceptable is because the review has to be posted by someone who's got a verified account, a Gmail account or something like that.

**Casey Mullooly:** Right.

**Tom Mullooly:** They have an identification and it cannot be altered. And it can't be removed by us by the business owner if they find it to be inflammatory, incorrect or whatever, even if someone were to leave a review that's less than stellar, what Twenty Over Ten has recommended is don't respond. We don't encourage people to go out and do it, but if you're so inclined, if you logged into Google and you want to leave a review, we're not going to stop you. I really do believe that marketing it's important now, it's only going to get more important as we see a lot of firms change their marketing approach with this upcoming rule change.

**Casey Mullooly:** Yeah. It could be good. It could be bad depending on the review. It kind of just opens the door for the people to have more say, I guess. They can kind of leave whatever comment they want and we, as the business owners and all of the other advisory firms aren't going to be able to necessarily do anything about it. And I think that's a positive for the person looking for an investment advisor because they get... If we could go in there and delete the negative comments or the negative reviews, then obviously firms would go in and curate that and want to appear in the best light possible.

**Tom Mullooly:** Sure.

**Casey Mullooly:** So since we're not able to do that, I think that's good for the people out there because they get the complete picture.

**Tom Mullooly:** Yeah. So one other area that they are now going to lighten up on the reins a bit is with citing performance numbers. That's not really an issue for us. We don't cite performance numbers because everybody's got their own individual mix of investments.

**Casey Mullooly:** Right. Yeah. I think that's more for funds.

**Tom Mullooly:** For the fund firms.

**Casey Mullooly:** Right.

**Tom Mullooly:** So, it wouldn't be a total surprise to see some of the big mutual fund firms, like a Fidelity or Vanguard, and some of the others to really start to pound the table on some of the numbers that they've been posting over the last few years.

**Casey Mullooly:** Yeah. It'll definitely be interesting to see how that plays out. Before we turned the mics on, you were saying, "Oh, well, it'll be interesting to see how one firm comes out and says, 'Well, we did 20.1%.' And someone else comes out and says, 'We did 20.2%.'" It's like, "All right, well, who really cares?"

**Tom Mullooly:** Right.

**Casey Mullooly:** That's not really our ballpark, so to speak. We're kind of helping choose which funds to use. And while performance does... Past performance like that does come into our decision, we do factor it in, it's definitely not the only factor that we consider.

**Tom Mullooly:** Let's talk for a minute about some of the in-house work that we have to do when it comes to books and records.

**Casey Mullooly:** Sure.

**Tom Mullooly:** So with advertising and Casey ultimately will become the chief compliance officer for the firm. And so this is where Casey's nose is just about every day of the week, books and records.

**Casey Mullooly:** I swear, I'm good at parties. It's boring, but it's got to get done.

**Tom Mullooly:** Someone has to do it. But when it comes to things like books and records, not only do we need to keep records of our personal securities transactions-

**Casey Mullooly:** Yep.

**Tom Mullooly:** ... but we also need to keep track of every place where we have an advertisement.

**Casey Mullooly:** That's right.

**Tom Mullooly:** What about when we send out a letter when we do direct mail and we do-

**Casey Mullooly:** Yeah.

**Tom Mullooly:** ... Where do we advertise?

**Casey Mullooly:** Direct mail, the local newspaper, on TV, some local church bulletins or website like we said, all of our social media accounts. So that's Facebook, Twitter-

**Tom Mullooly:** And we have multiple accounts on Twitter-

**Casey Mullooly:** ... LinkedIn-

**Tom Mullooly:** ... LinkedIn.

**Casey Mullooly:** ... our website.

**Tom Mullooly:** Every piece of that needs to be archived.

**Casey Mullooly:** Yeah.

**Tom Mullooly:** Which is a huge, huge job. Every tweet that we put out is archived. Every page on our website, archived. We've got over 1,800 posts on our website. Every ad in the local newspaper, every catalog of how many times our TV commercials run, all of that needs to be archived, catalog.

**Casey Mullooly:** So what's the change that they're proposing with this new rule? We're not sure about that, but just the advertising in general for a firm like ours, we have to be very careful with what we say and where we say it, because we're operating under these rules from the Investment Advisers Act, who knows if they're going to do more updates to this. The Investment Advisers Act was put in place in 1940. They're updating these, but like you said before, you got started in your career in the eighties and you haven't really seen updates since then to this act. Think about all the changes that happened since then.

**Tom Mullooly:** Oh, my goodness.

**Casey Mullooly:** Social media wasn't a thing.

**Tom Mullooly:** Wasn't even in existence. I remember I wanted to send out [crosstalk 00:24:36].

**Casey Mullooly:** Was the internet even around?

**Tom Mullooly:** No, I wanted to send a letter to some prospective clients that I had. This is 1986, maybe 1987, talking about this government bond fund that we had. And branch manager called me up on the internal line, "Tom Mullooly, come upstairs to my office." I'm like, "Oh, great. I'm in trouble." He's like, "You want to send this letter out?" And I was like, "Yeah, I've got like, 15 or 20 people that I want to send it to." He goes, "You know, you have to send this with a prospectus." And I was like, "Aah." He goes, "That was on the Series 7 exam."

**Casey Mullooly:** Yeah, I know. I know.

**Tom Mullooly:** I know. I know. So I said, "Well, I guess I'm not sending it." And he said, "That's right."

**Casey Mullooly:** Yeah.

**Tom Mullooly:** So, we're just not doing that. But yeah, if you want to buy a mutual fund, you could send out a letter. No problem. You couldn't cite returns.

**Casey Mullooly:** Yeah.

**Tom Mullooly:** You couldn't promise what the returns are going to be. And it had to come with a prospectus.

**Casey Mullooly:** Mm-hmm (affirmative).

**Tom Mullooly:** Same thing with IPOs. 20 years ago, when I was a broker, people were asking me all the time, "Hey, can you get me information on this company that's going to go public?" I'd be like, "Okay, I'll try and get the prospectus." But sometimes the deals would come so fast that we would get the prospectus like a month later. And it would be the red herring. It wouldn't even have all the details in it. A lot of confusions.

**Casey Mullooly:** So the rule was written when everything was by mail.

**Tom Mullooly:** Oh, yeah.

**Casey Mullooly:** And phone?

**Tom Mullooly:** Yeah.

**Casey Mullooly:** But now the world has changed completely. So on that note, I'm glad to see that they're updating it and loosening up the framework a little bit, it seems, but yeah, the world has completely changed in the last 40 years. So it'll be interesting to see what we're allowed to do, the ins and outs. I'm sure, we'll get more information if the rule is passed, maybe we'll get another FAQ series like they did with the fiduciary rule back in 2018, never came to light. It was going to completely change the game. And it sounds like this might do the same.

**Tom Mullooly:** Right. So, stay tuned. A lot more coming. This is literally hot off presses. We got this about an hour ago.

**Casey Mullooly:** Yeah, about 1:30.

**Tom Mullooly:** And so, we're recording this because we want to be a little bit ahead of the curve and we wanted to share this, but we also wanted to use this opportunity to help shed a little light on our industry. And what's permitted, what's not permitted. And hopefully the things we've covered in this podcast help to do that. Casey, thank you, that's going to wrap up episode 337. Will catch up with you on the next podcast.