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HEADLINE: Digging Up Dirt. And Deciphering It. Recent disclosure rules make it important for investors to understand whether an adviser has a questionable record-or is getting a bum rap

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BODY:

Regulators have made it easier for investors to dig into financial advisers' backgrounds. But all that new information has left some investors wondering: What should they do with it?

While choosing a financial pro with a squeaky clean public record is obviously the safest option for investors, the odds of finding at least some flaws in an adviser's past have risen. Not only are old blemishes resurfacing on some advisers' records as a result of new, expanded disclosure rules, but periods of market volatility like the one that began in late 2008 typically result in more customer complaints as investors seek to assign blame for their losses.

The challenge for investors, securities lawyers say, is sorting out truly egregious behavior from a bum rap. To do that, investors need to do more than just read broker disclosure reports-they also must learn to decipher them.

"They might not know what's really bad, so this gives them an opportunity to have the discussion with an adviser," says Luigi Spadafora, a lawyer for Winget, Spadafora & Schwartzberg LLP in New York.

Making It Public

The Financial Industry Regulatory Authority, Wall Street's self-policing organization, has been broadening the scope of information about securities-industry professionals available to investors through its free BrokerCheck service at www.finra.org/brokercheck .

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BrokerCheck now discloses certain customer complaints and legal actions involving brokers as far back as 1999. A broker previously had to rack up three or more such complaints before they appeared on BrokerCheck. Some information, such as criminal convictions and certain penalties, are now permanently available. Some details about brokers who are no longer registered but who may be working as another type of financial adviser, such as a financial planner, are now available for 10 years, instead of two.

Registered investment advisers, who are regulated by the Securities and Exchange Commission or states, also must publicly disclose information such as certain lawsuits, investment-related misdemeanor convictions and regulatory problems. Those details are available through the SEC's Investment Adviser Public Disclosure database at www.adviserinfo.sec.gov. That system was recently expanded to retain information about advisory firms and representatives who de-registered over the past 10 years. A new rule also requires most investment advisers this year to give clients a brochure that describes their businesses, fees, and disciplinary history, among other things.

A recent SEC staff study suggested one way to improve the sites would be to include more definitions of commonly used terms. While the sites already have glossaries, investors may need more help understanding some of the lingo, the study says. For example, saying an adviser was terminated for "violating firm policies and procedures" may leave an investor wondering what that means. The study suggests getting input from investors about which terms confuse them.

Many advisers with tarnished public records may not be incompetent or dishonest, says Richard Roth, a lawyer with The Roth Law Firm in New York. "People are complained about and pursued in arbitration at the drop of a hat," he says.

Investors should first read an adviser's employment history and note how many problems occurred during those years, says Mr. Roth. "If a broker is in business for 10 years and has 10 problems, that's a bad thing. But 10 in 30 years isn't," he says.

Brokers and securities firms must often defend against securities arbitration claims filed by investors who lost money. Cases that are pending or resolved appear on an adviser's BrokerCheck report.

But that doesn't necessarily mean there's a problem with the broker or firm, says Raymond Moss, a securities lawyer for Sims Moss Kline & Davis LLP in Atlanta. Settling cases is often a business decision, says Mr. Moss. "Unfortunately, the cost of arbitration is very expensive," he says.

Customer losses are more common when markets are volatile, so investor arbitration claims typically rise when markets fall. "It doesn't always mean that a broker or firm violated the rules," says Mr. Moss.

Investors should carefully read disclosures about arbitrations and other legal actions. Disclosures typically include some general details about the allegations. Complaints of unauthorized trading or selling securities that aren't suitable for an investor are among the most serious. Investors should ask advisers to explain the circumstances, say lawyers.

Cases involving brokers and brokerage firms that don't settle are typically decided by a panel of three arbitrators. Investors should be wary if they read a broker was found "jointly and severally liable," says Laurence Landsman, a securities lawyer for Block & Landsman in Chicago. It means the broker and firm are equally responsible for the losses. "It's something that could be of significance," he says.

Some advisers have run-ins with regulators, such as Finra and the SEC, but may return to work after paying a fine and enduring a temporary suspension. Many regulatory offenses aren't as egregious as stealing, but may reflect on an adviser's character, say lawyers. An adviser, for example, recently agreed to a \$5,000 fine and one-year suspension by Finra for allegedly giving other advisers answers to a test required for a continuing-education requirement.

A long-term suspension or lifetime bar may apply for more serious offenses, such as forging customers' signatures

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or felony convictions. Those advisers may no longer work for brokerages, but may still represent themselves as other types of financial professionals. The permanent disclosure of regulatory offenses through BrokerCheck can help investors avoid this crowd.

Other regulatory offenses are more technical, such as record-keeping lapses, and not directly related to investing, says Mr. Moss. Settling these cases with regulators is common, he says. That doesn't necessarily mean guilt or innocence, but a need to move on, he says.

Employment Problems

An adviser with a history of job-hopping could spell trouble, says Mr. Roth, the New York-based lawyer. "If you stay in the same place, the employer probably likes you," he says.

Finra's BrokerCheck reports may signal when a broker has left under a cloud. The word "termination" often means there's more digging to do, says Marc Dobin, a securities lawyer in Jupiter, Fla. "It doesn't necessarily mean the broker did something so terribly wrong," he says. Investors need to read the explanation included by the employer, he says. A termination for "insubordination," for example, could mean the adviser and supervisor didn't get along.

The phrase "violation of firm policies and procedures" suggests a range of potential conduct, so investors need to read the explanation and ask the adviser for more details.

Brokers who are "permitted to resign" can be a risky bet, say lawyers. The designation usually comes about after firms give the adviser a choice between resigning or being fired.

Advisers who "voluntarily resign" also may have a hidden story to tell, such as an internal investigation that isn't yet resolved, says Mr. Dobin. That information may not appear on BrokerCheck, but could show up in other types of disclosures available through state regulators, he says.

Finra is instructing brokerages-and in some cases requiring them-to be specific about certain disclosures. Many firms have long feared defamation lawsuits by brokers for including unflattering details. But they're starting to realize the advantages of specifics, says Mr. Dobin. "I think the firms are coming around," he says.

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