

BDWEEK

Regulatory and Compliance News for Broker-Dealers

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Home

Search Articles

Topical Index

Print Issues

Print Current Issue

PDF Issues/Archives

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Discussion Forum

Conferences

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Special supervision is a big risk, compliance pros caution

Tell supervisors who want to put a problematic rep on special, heightened supervision, that doing so means the supervisor is vouching for that person, and if problems with that rep erupt, the supervisor could lose his or her license, compliance pros suggested at a recent conference.

"They're vouching for this person, saying, 'I believe in him or her. I will go to bat' [for that person], and that is a huge responsibility," said Andrea Golls, director of field and sales compliance with Thrivent Financial for Lutherans, speaking at the recent NRS Spring Compliance conference. Golls said when she tells supervisors at her firm the risk they take when putting someone on special supervision as opposed to terminating the rep, the supervisors typically decide to fire the person.

Golls said she personally doesn't support giving reps the special supervision option. Similar reluctance was voiced by the other speaker, John McGovern, senior vice president and chief compliance officer of IFMG Securities, Inc., a Sun Life Company, and a former examiner in NASD's New York District office.

McGovern said the only times he has allowed someone to stay on under heightened supervision are when: a) McGovern has just joined the firm, done his own quality assurance regimen, and discovered people who shouldn't have been hired in the first place; and b) when the firm applies some type of new surveillance system and discovers problems that were previously unknown.

"I have become so paranoid that in those few cases, I will take those items, I will make a matrix, I will assign it to a surveillance analyst," McGovern said. He then puts the item on his calendar to ensure the surveillance analyst stays on top of the case, he said.

Despite their own hesitancy to give reps this break, Golls said the decision should be a "gut" check for those who want to consider that option. If your gut tells you the rep merely made some errors in judgment, maybe had received insufficient training, and if you think your firm can put a program in place to correct the behavior, perhaps you can justify your decision to regulators, Golls continued.

"For me, in all my years dealing with regulators and dealing with these types of issues, I think the biggest part of the battle is really believing what you're doing," Golls said.

Stick to the plan

If your firm puts a rep on special supervision, it's essential that the tasks detailed in the plan get accomplished, and on schedule, both said.

"Unless this person is so egregious that they should have been terminated without cause, they [regulator] will quickly accept your reason for putting them on special supervision, but then they'll look at your plan of special supervision to see if it's substantive enough, and if it is and it says you're going to do 20 things, they will test to

10.1

see if those 20 things are done," McGovern said.

If you were supposed to conduct a certain number of meetings, for instance, regulators will look for proof that all those meetings were held.

"If they were supposed to take three more continuing education modules in the first three months after signing this letter, did they? And God forbid that they took the three, in four months Then you've violated your plan of special supervision. So that's where they're really stress-testing it to make sure you have complied," McGovern said.

One session attendee said his firm had placed three individuals on increased supervision NASD's suggestion two years ago, and that at the end of last year, SEC examiners came and drilled down into the records to determine whether the plan was being followed. The SEC left and FINRA came in and drilled down some more on same individuals. The only way the firm could save itself was to terminate the people because the firm was at risk, that attendee said.

McGovern also mentioned the need to keep an eye on data related to reps who need closer-than-normal supervision, but who don't need special supervision yet. Cross tabulate data to identify those reps by business and by activity. That way, you can tell, for instance, those reps who do a high amount of variable annuities business and who also have higher-than-usual 1035 exchanges, who may frequently be the last to undergo annual compliance training, and who have had other issues that indicate they need to be watched, McGovern said.

How long on special supervision?

Golis said those on special supervision plans should stay on those plans at least a year. Some organizations allow six months, but Golis insisted that's not long enough.

"In my mind, that's worthless. You don't have nearly enough time to demonstrate whether someone has changed their behavior," Golis said. At the end of a year, the person's supervisors need to sit down and look at progress that has been made during the course of the year, Golis said.

Categories | [Supervision](#) | [Financial Industry Regulatory Authority \(FINRA\)](#)

[\[print article\]](#)

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Northwestern Mutual

720 East Wisconsin Avenue
Milwaukee, WI 53202

SUPERVISORY MEMO

REPRESENTATIVE'S NAME

R. Brian Fechtel

AGENT NUMBER

57178

(Check one):

☒ Registered with NMIS

☐ "Associated person" of NMIS

☐ No relationship with NMIS

(Check all that apply):

☐ Non-Variable Insurance Products – Life, DI, LTC, Fixed Annuity

☐ Variable Product – VLA, VA

☐ Mutual Funds

☐ Securities – Stocks, Bonds

☐ Advisory Product

☒ Not Product Specific

1. Summary of concerns noted: (Check one)

☐ Type 1

(Copy to Managing Partner)

☒ Type 2

(Signed by Managing Partner and
copy to Home Office)

☐ Type 3

(Signed by Managing Partner, notify Home Office
and copy to Home Office)

Representative included private, confidential identifying client information in correspondence beyond what was necessary for the business need.

- 2. Description of corrective actions taken:** Include documentation of contact with the home office. (**Important:** Notify the Market Conduct division **immediately** if disciplinary action involving special supervision, suspension, termination, withholding of commissions or imposition of fines greater than the recommended range is being considered.)
Matter to be addressed in person by RVP in face to face meeting with FR at Network Office. Written instructional letter will be given to FR at face to face meeting. FR is on a special supervision plan and this policy violation will also be addressed with the FR in conjunction with that plan.

3. Follow-up plans (Complete if applicable):

4. Follow-up results (Complete if applicable):

5. Signatures (Required if Type 2 or 3)

MANAGING PARTNER

DATE (MM/DD/YYYY)

MANAGING DIRECTOR (If Applicable)

DATE (MM/DD/YYYY)

6. Required reporting to the Market Conduct division of the Compliance/Best Practices department:

- Send the Supervisory Memo and related documentation for Type 2 and Type 3 concerns to the Market Conduct division (Room E4L, Phone 1-866-571-7222, #5, FAX 414-665-3547). (For Type 2 concerns, send **after** corrective actions have been taken.)
- Notify the Market Conduct division **immediately** by phone, FAX or e-mail if a disciplinary action listed in #2 above is being considered **or** if a Type 3 concern has been discovered.

Home Office Use Only

Reviewed by: _____ Date: _____ (MM/DD/YYYY) Acknowledged by: _____ Date: _____ (MM/DD/YYYY)



Northwestern Mutual

June 10, 2008

Hand-Delivered

Mr. R. Brian Fechtel
Northwestern Mutual Life
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Poughkeepsie, NY 12601-3123

Mark S. Bishop, CPA
Regional Vice President
Agency Department

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Milwaukee, WI 53202-4797
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414 625 4723 fax
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RE: Field Information Manual ("FIM") 4.2.16.9.1 Communication about Personal Customer Information Limited to Business Needs Only

Dear Brian:

In your correspondence of May 21, 2008, addressed to Edward J. Zore, President & CEO, and the Trustees of Northwestern Mutual, you disclosed personal customer information that was not required or necessary to the content of the letter.

The Company policy on this matter is as follows:

FIM 4.2.16.9.1 Communication About Personal Customer Information Limited to Business Needs Only

When requesting, using or disclosing Personal Customer Information, Financial Representatives and their staff must not request, access, use or disclose more information than they need to accomplish the business purpose. In addition, care must be taken to protect the privacy of the customer. Discretion and good judgment should be used when Personal Customer Information is communicated through any vehicle, including LINKgrams, telephone, voice mail, facsimile, or e-mail. Any electronic message you send out could be read by many people - including competitors, regulators or news reporters.

Casual or non-business communication about Personal Customer Information is not permitted. Personal Customer Information should not be shared with other Northwestern Mutual employees, contract employees, or field personnel unless they need the information to do their jobs. Personal Customer Information should never be shared casually during or after work. Third parties should not be permitted access to, or be provided with, Personal Customer Information unless there is a legitimate business purpose and the access or disclosure is legally permitted and in accordance with Company policy.

Brian, as you know, you are under a Special Supervision Plan. Your violation of this policy is of serious concern to me as I continue to supervise you. I trust you understand the seriousness of this matter and will take immediate steps to comply with this policy.

Any future violation of this or any other policy may result in further disciplinary action, including termination of your registration with Northwestern Mutual Investment Services, LLC, and termination of your agent's contract.

Please contact me with any questions on this matter.

Sincerely,

A handwritten signature in cursive script that reads "Mark S. Bishop". The signature is written in dark ink and is positioned above the printed name.

Mark S. Bishop

Notes on Northwestern's "The Right Way to Write" webcast program that I watched more than 2 times (often stopping the play to back-up and listen to sections again) on June 17, 2008. I took handwritten notes as I watched. Below I transcribe my notes and make additional comments. Quotes are accurate, I'm not guaranteeing 100% word for word, but just about that level of accuracy. My comments are in [].

Presenter Sandy Botcher

Home Office has 70 lawyers, 7 work full time defending the company against lawsuits.

Litigation is a fact of life – spans all areas of our business.

Litigation isn't just about the truth. We spin things - She actually says, "We spin the story that we want to sell to the jury. Litigators are story-tellers. We want to spin stories that are helpful to the company." [This is just the first of many things that I found so shocking about her presentation b/c where I come from spin has a pretty negative connotation – and those trying to persuade others do not typically refer to their own actions as spin, do they?]

Anything on which you store information can be available – napkins, etc. etc. etc. Where you put it doesn't matter.

Mentions notes on the back of an agent satisfaction survey and says, "we really rather they not see this agent satisfaction survey" Survey stated " person needs more help and person doesn't like their job." "They will know more about this individual than we want our adversary to know."

She then poses the question, "When should you communicate by writing." And her answer is "only when it is essential to do so." "Only write when necessary to create an essential record of what has occurred." [Again, I found/find her advice to be arising from such a defensive posture. Only communicate in writing when it is essential.]

She stated 4 "Dos" of writing:

- 1) Only state facts
- 2) Draw conclusions from the facts
- 3) Write clearly and simply - BIGGER or more is not better, in other words don't expound
- 4) Choose your word carefully and with regard to such a) no swearing, b) do not write when in a hurry or you are angry, c) don't use sarcasm and d) don't interject your judgments – I'm pretty sure she says, "I don't need your judgments."

She also states that 1) looks do matter – sloppiness is bad, and no writing in margins

She says, "calling someone just plain nuts" shouldn't be in a business letter."

She talked about being careful not to write something like, "They totaled ignored my request." " Do it right this time." She asked, "what is the business need for such an express?" [in my opinion, there can be a real business need for such statements. Admittedly, such statements can make it difficult for the company to defend some action or inaction, but concerns about defending the company should not be the supreme concern in communications. For example, if some department had messed up something time and time and time again, firm language catch someone's eye and lead to a problem being fixed. I'm not endorsing tactless writing, but again I believe that 'defending the company' is not the first concern of internal business writing.

Sandy commented though that such comments above are "not what we want to paint to a jury." [Isn't the best way to solve a company's litigation problems, is by solving the problems? And not being so worried about what gets painted to a jury. Shouldn't a company endeavor to eliminate it litigation problems by eliminating the problems, rather than by

eliminating the evidence the litigators find problematic? The former solves a problem, the latter just endeavors to avoid responsibility for the problem.]

She continued to 1) date all notes

2) note all participants in meeting

3) be careful about judgments and editorial remarks,

4) attribute comments written down – who said what

5) don't characterize/interpret what happened – just note the facts

6) scribble notes today

She gave examples of what not to write down 1) Don't write "Tired receiving phone calls from Tom"

Don't write "There something about her that is very suspicious." [Again, what about if there is something about her that is suspicious?]

Don't write, "FR has lied to me on other claims. I don't trust him." Sandy says such written statements have "no business purpose." I recall that she said, "You see why I would prefer that this note had not been made." [It baffles me that she or anyone could say that such statements do not have a business purpose. They have a clear purpose – perhaps the FR or this situation should have been investigated. They just don't have Sandy's purpose in mind]

Label a Draft a Draft - but be aware that labeling can be irrelevant.

If you are dealing with an attorney only by labeling something privileged and confidential do you preserve its confidentiality.

Emails are the hottest topic - avoid inadvertently replying to all when you only want to reply to 1

What you say can and will be used against you.

Avoid wrong email address

Avoid mixing personal w/ business in the same email.

When to Discard - When NOT to discard – if threat of litigation – must save all

The Right Way to Write is really about using Common Sense.

I really found this course) shocking in its defensive posture – can't help but think things must be very bad on the litigation front to have produced such a video, and 2) shocking in its underlying assumption that "litigation concerns" must be the paramount consideration when considering writing anything, 3) shocking in some of the really horrible examples that seemed like they must have been just slightly modified from situations that the home office litigators have had to deal with – but again if these are some of the types of problems that they are having, then they have got bigger problems than just simply what is being written – they have got the problem of what is being written about b/c they really picked some examples that just made me cringe and 4) shockingly obvious – and consequently insulting that Mark Bishop had asked me to watch it because a) I know how to write and b) if you were upset about all the misrepresentations I cited in my letter, isn't it a little perverse to think that making me watch such a video that tries to safeguard the company from litigation is going to have an impact upon me when I have just written that I think the Board of Trustees should all try to buy more E&O coverage.