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Protocol for Broker Recruiting Cannot Strip Non-Signatories of Rights

FINRA Arbitration Panel Finds Morgan Stanley Smith Barney's Repeated Attempts to Impose Protocol on Non-Signatory to be an Unfair and Deceptive Business Practice

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A recent decision issued by a FINRA Arbitration Panel in Massachusetts firmly rejected the argument that the terms of the Protocol for Broker Recruiting should be imposed on a non-signatory as purported industry standard. The Protocol for Broker Recruiting (the "Protocol") was created in 2004 by a few major brokerage firms to permit departing representatives to take certain limited client information with them to a new firm and solicit those customers without the fear of being sued by their former employer. Representatives of firms that have signed the Protocol can take client names, addresses, phone numbers, email addresses and account title information with them when they change firms and use it to solicit those clients, provided they leave a copy of this information (along with applicable account numbers) for their manager upon resignation. The full text of the Protocol is available by clicking here.

In the recent case before FINRA, the Panel made the following findings of fact, *See Fidelity Brokerage Services LLC v. Brian Wilder & Morgan Stanley Smith Barney, LLC,* FINRA Arbitration Number 11-03937, available by clicking here (Sept. 14, 2012): The representative at issue was a former employee of Fidelity Brokerage Services LLC ("Fidelity") named Brian Wilder. *Wilder* at 1-2. Wilder signed an Employee Agreement with Fidelity containing confidentiality and non-solicitation clauses. *Id.* at 2, 9. Morgan Stanley Smith Barney ("MSSB") provided Wilder with a copy of and required him to sign MSSB's Financial Advisor Account Transition Policy, which specifically instructed representatives to take client information such as that permitted by the Protocol from their former employer – regardless of whether or not the former employer was a signatory to the Protocol. *Id.* at 14-15. Two weeks before resigning from Fidelity, Wilder met with an attorney paid by MSSB to develop a "non-protocol" strategy for his transition from Fidelity to MSSB. *Id.* at 8. After meeting with the attorney, Wilder prepared a list of customer information from Fidelity's confidential database as he had been instructed to do by MSSB. *Id.* at 15. Upon his resignation, Wilder was reminded by the Fidelity branch office manager of his obligation to return all customer information and to abide by his non-solicitation agreement. *Id.* at 14. Instead of returning the information he had taken or leaving a copy as required by the Protocol, the panel concluded Wilder "lied to his Fidelity branch manager about having the list and proceeded to use the list aggressively to solicit Fidelity's customers." *Id.* at 8, 13. Notably, the Panel found that this same sequence of events had occurred with regard to five other representatives hired away from Fidelity by MSSB in the past 18 months, thereby concluding that this was MSSB's intentional practice and not a one-off occurrence or mistake. *Id.* at 13-16.

In response to Fidelity's claims for misappropriation of trade secrets, breach of contract, intentional interference with contract, and unfair and deceptive practices, MSSB argued that Wilder was permitted to take customer information from Fidelity under the Protocol—even though Fidelity was not a signatory—because the Protocol had so many signatories it had become the industry standard. *Id.* at 10-11. The Panel firmly rejected this argument. *Id.* at

10-12 ("Based on rudimentary principals of contract law, it is axiomatic that Fidelity, as a non-signatory, cannot be bound by or have the terms of the Protocol imposed upon it by a signatory firm").

The Panel also rejected MSSB's argument that the existence of the Protocol somehow nullified the trade secret status of customer lists at non-Protocol firms, concluding that "[p]roclaiming that the Protocol is the purported industry standard" does not make it so. *Id.* at 11-13 ("When a Fidelity broker leaves to work for a Protocol firm, Fidelity's proprietary customer information does not thereby lose its confidential status, become vitiated and converted into a Protocol-compliant list, which the ex-Fidelity broker can then use to freely solicit Fidelity customers."); *see also id.* at 12-13 (noting that, if signatory firms were permitted to impose the terms of the Protocol on non-signatories, "it would, in one fell swoop, render null and void all existing non-solicitation and confidentiality provisions contained in every non-Protocol firm's employment agreement with its brokers").

The Panel found it instructive that MSSB invoked certain aspects of the Protocol "when it suited [its] purposes" but failed to comply with other mandatory provisions of the Protocol such as leaving a copy of the client list with the representative's former employer. *Id.* at 12-13. For example, MSSB argued vehemently that it "did not treat Wilder as a Protocol hire," but also "implored the Panel" to find that its conduct was not wrongful because the Protocol was industry standard. *Id.* at 12-13, 16 (describing the "incongruity" of MSSB's positions as "mystifying," "perplexing," and "disingenuous").

By its express terms, the Protocol applies only to firms that have signed a joinder agreement. *See* Protocol at 3 (providing that the Protocol is "of no … force or effect with respect to" non-signatories). Despite this clear language, firms and individual representatives throughout the country often attempt to avoid liability for taking client information from non-signatory firms by arguing that the terms of the Protocol should be applied to the non-signatory. Every court to consider this argument has rejected it. *See, e.g., Ayco Co., L.P. v. Feldman,* No. 10-1213, 2010 WL 4286154, *11 (N.D.N.Y. Oct. 22, 2010) (finding that "Defendant's reliance upon the Protocol for Broker Recruiting … as a guaranteeing [sic] his right to retain [client] information is misplaced" because his former firm was not a party to the Protocol and, therefore, "is not bound by the terms of that document"); *Bank of America, N.A. v. Immel*, No. 10-2483, 2010 WL 2380877, *2 (N.D. Cal. June 11, 2010) (rejecting argument that the Protocol applied to the trade secret client information of non-signatories); *Genworth Fin. Wealth Mgmt., Inc. v. McMullan*, 721 F. Supp. 2d 122, 125, 127 (D. Conn. 2010) (defendants "lacked a reasonable basis to conclude that their actions were authorized under the Protocol" where former firm was not a signatory and repeatedly stressed the "proprietary nature of client information"); *J.J.B. Hilliard, W.L. Lyons, Inc. v. Clark*, No. 07-811, 2007 WL 2589956, *6 (W.D. Mich. Aug. 31, 2007) (rejecting argument that Protocol was the industry standard, such that its terms might be forced upon non-signatories, because the "clear and unambiguous terms of the Protocol" provide that "it is not intended to bind those firms who opt not to sign it").

The recent decision in *Wilder* not only joins but adds to this line of authority by holding that Protocol firms who instruct, permit or encourage recruits to take customer information from non-Protocol firms are engaging in a willful and knowingly unfair and deceptive practice, which may expose them to punitive damages as well as attorneys' fees. *See Wilder* at 8-17 (awarding approximately $82,000 in compensatory damages, $82,000 in punitive damages and $500,000 in attorneys' fees and costs). Protocol firms would thus be well-warned to respect the confidentiality of customer information and the contractual relationships of non-signatory firms when bringing a new representative from a non-signatory firm on board.

For more information on the matters discussed in this *Locke Lord QuickStudy*, please contact one of the authors:

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