Botched Back-Office Integration Cost Morgan Stanley Clients $16M

By Bradley Saacks, *Ignites*, January 17, 2017 [subscription required]

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Botched integration of back-office systems following the 2009 merger of **Morgan Stanley** and **Smith Barney** has ended up costing the parent companies $14 million in regulatory fines.

The SEC Friday announced a settlement with Morgan Stanley involving claims that the broker-dealer overcharged clients in its TRAK mutual fund wrap program and other fee-based accounts by more than $16 million over the course of several years.

The wirehouse agreed to pay a $13 million fine to federal authorities, and repaid its clients, with interest. In addition, Morgan Stanley agreed to several systems changes to prevent similar errors in the future. Morgan Stanley neither denied nor admitted the charges.

The order followed one day after the New York attorney general's office announced it had reached a settlement with **Citigroup Global Markets** with respect to TRAK mutual fund wrap accounts it administered. The state regulator found that Citi, which previously owned Smith Barney, overcharged nearly 50,000 clients more than $22.5 million in fees. The Citigroup subsidiary agreed to reimburse clients, with interest. Citi also agreed to a $1 million fine to New York State.

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The overcharging by broker-dealers is a systemic problem, says Niels Holch, founding partner at Holch & Erikson in Washington, D.C.

While his focus is more on broker-dealers' violating breakpoint agreements listed in fund prospectuses, Holch likens such failures to making adjustments to systems involving fee-based accounts. “It's not in the economic interests of brokers to charge their customers the least amount,” he notes.

According to internal data compiled by his firm, Holch determined that distributors have paid more than $330 million in Finra fines and restitutions since 2004 because of broken breakpoint agreements.

“It just goes against the broker-dealers' incentives.”