

# Decoded: Inside Morgan Stanley's Trade-Miscoding Misadventure

Six industry bars and a couple dozen other sanctions later, Finra may be nearing the end of a two-year run of disciplinary actions against former Morgan Stanley advisors accused of improperly coding trades in shared accounts. FA-IQ reconstructs what went wrong and how the wirehouse and regulators responded.

By **Glenn Koch** | February 1, 2024

It started with a retired advisor complaining he was being deprived of revenue from clients he handed off to a colleague at **Morgan Stanley** before riding off into the sunset. Two years, a programwide sweep, at least 42 discharges, six industry bars and a couple dozen sanctions later, with the affected retirees presumably made whole, industry lawyers sift through the rubble for lessons and warnings to heed.

Since December 2021, the **Financial Industry Regulatory Authority** has barred or otherwise sanctioned 30 former Morgan Stanley advisors over miscoding allegations, according to an FA IQ tally of announced disciplinary actions.

During a good chunk of that time, observers could almost set their calendars by the disciplinary announcements: At least one surfaced in 17 of the 20 months between December 2021 and July 2023. Four more such actions have been announced since late November.

But a review of Form U5 filings suggests that the industry's self-regulator may be running out of miscoding advisors to punish. Since October 2017, Morgan Stanley has discharged or otherwise parted ways with at least 42 advisors accused of miscoding trades, according to a data set of more than 101,000 Form U5 filings collected by FA IQ last year via requests from state securities regulators.

The aforementioned 30 advisors plus an earlier two have already been sanctioned by Finra, either for alleged miscoding of trades or for declining to cooperate with its investigation of the allegations. That leaves 10 advisors who, for now at least, have not been disciplined by Finra. At least five seem unlikely to be punished by Finra, either because they've already been sanctioned by a state regulator or because their alleged miscoding involved negligible trades or insignificant revenue, according to a source familiar with the matter.

## Forensic Findings

The matter began when a retired Morgan Stanley advisor complained about not receiving revenue from accounts shared via the Former Advisor Program, through which retiring brokers pass on their client book to other Morgan Stanley advisors, according to attorney **Brian Neville**, who represented at least two of the advisors discharged amid allegations of miscoded trades.

Morgan Stanley “saw that that retired advisor’s allegations were true and from that they decided to do a wholesale review of all the FAP participants, and that’s where we got all these folks having been let go,” Neville, of New York based **Lax & Neville**, told FA IQ.

The number of advisors accused of miscoding was a fraction of one percent of Morgan Stanley’s advisor ranks, but it was enough to force the wirehouse’s hand, according to an attorney who represented one of the advisors and asked not to be identified. And though Finra may have considered an advisor’s intent or the extent of wrongdoing in issuing punishment, the attorney said that Morgan Stanley discharged all the advisors who acknowledged having changed trade codes, regardless of the reason.

“We expect Advisors who enter into partnership agreements to abide by those agreements, and we are committed to ensuring that retiring Advisors receive what they are entitled to,” a Morgan Stanley spokesperson told FA IQ via email.

The discharges were issued slowly at first, totaling six between 2017 and 2019, according to FA IQ’s Form U5 data. Most landed in a nine-month stretch between November 2020 and August 2021, when 29 advisors were discharged. Two other accused advisors voluntarily resigned or were “permitted to resign” during that period, the filings show. Finra, which had sanctioned two of the advisors for trade coding at that point, took note of the Form U5 disclosures and began its disciplinary run four months later.

Six advisors who didn’t cooperate with Finra’s investigation of the matter were barred. The cooperators all paid fines of either \$2,500 or \$5,000 and received suspensions of 10 days to six months.

Finra’s published disciplinary rulings do not explain the rationale for the severity of the sanctions, but the fines and suspensions seemed largely in step with the alleged number of miscoded trades. The advisors who were fined \$5,000 averaged 474.3 miscoded trades with a high of 1,286 and those who were fined \$2,500 averaged 178.8 miscoded trades. (The 32 advisors sanctioned to date were alleged to have miscoded a total of 9,081 trades, receiving fines totaling \$102,500, or about \$11.29 a trade, according to the disciplinary filings.)

Similarly, the advisors who received six-month suspensions averaged 695.6 miscoded trades; those who received three month suspensions averaged 470.5 miscoded trades; and those who received suspensions ranging from 10 days to one month averaged 200.9 miscoded trades.

### Excuses, Excuses

Nearly all the Finra consent filings reflect the advisor’s explanation for changing trade codes. Three advisors convinced Finra that the retired advisor had agreed to change the codes, and though Neville said that the FAP agreement required any modification of the agreement to be submitted to the firm in writing, Finra was kindest to these three, who were the only ones to receive 10 day suspensions.

And one of the two 15 day suspensions was issued to an advisor who claimed that he had been instructed by a supervisor to change the codes.

As for the others’ excuses, none seemed more of a factor than the number of trades involved, as there were multiple instances of advisors who presented the same excuse being punished with greatly differing severity but roughly in line with the number of trades.

The most common excuses were that the advisor mistakenly believed that new assets in the shared accounts were not subject to the FAP, that the advisor didn't realize that a particular account was included in the FAP, or that the advisor incorrectly believed that permission to change the code had been granted.

"A lot of this is not willful intent to defraud," said New York-based attorney **Bill Singer**, whose specialties include financial services regulatory matters. "It's just a very significant misunderstanding of whether inherited businesses continue to be inherited despite the fact that the account holder may no longer be actively making the decisions," Singer, who did not represent any of the advisors involved, told FA-IQ.

Neville said that some coding issues stemmed from transactions involving insurance, annuities and other products that required certain licensing the retired advisor did not possess, and he added that some advisors claimed to have been instructed to use their individual representative code when opening new accounts for a child or trust related to a client in a shared account.

Meanwhile, all but seven of the 42 discharged advisors — including three of the six advisors who were ultimately barred — later registered at another firm. None of the advisors moved to another wirehouse.

### Aftermath

A small number of disciplinary actions may still be in the works at Finra, but Morgan Stanley, for its part, has modified its trading system to prevent brokers from changing trade codes in shared accounts. Nearly two years have passed since Morgan Stanley last discharged an advisor for miscoding trades, according to Form U5.

Neville said he believes that miscoding of trades is not endemic to Morgan Stanley and that the lack of Finra sanctions against other firms' advisors in recent years suggests that those firms are handling such infractions in a less punitive manner — such as by issuing a letter of education — that does not appear on Finra's radar.

"I wouldn't be surprised if there's still some new activity that we'll see, but I think ... we're very close to the end of this as a story," Neville said.

### Data Dive

The Form U5 data cited in this article, covering the period from 2017 through mid to late 2023, was gathered by FA IQ last year via requests made to state securities regulators. Twenty six of the 50 states provided information, totaling 101,084 unique records. Included among the respondents were industry hubs such as New York, Florida, Texas, Illinois, Connecticut and New Jersey. Much of the information from states that did not cooperate was nevertheless gleaned because the broker had also registered in a state that did cooperate.