TIAA Broker-Dealer Settles SEC Allegations for $96 Million

By Wagner Law Group *Thu, Jul 22, 2021*

TIAA-CREF Individual and Institutional Services, LLC, a subsidiary of Teachers Insurance and Annuity Association of America is alleged to have failed to adequately disclose conflicts of interest and to have misled customers.

In what the Wagner Law Group believes may be the first of many prosecutions to come, the Securities and Exchange Commission has fined a TIAA-CREF broker-dealer $96 million in a settlement over its rollover practices. This action also resolved a parallel action by the Office of the New York Attorney General.

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Dually registered as a broker dealer and an investment adviser, TIAA Sub was charged with incenting or pressuring its advisors to recommend that participants in retirement plans record-kept by the parent company roll assets out of those employer-sponsored plans into TIAA Sub’s more expensive managed account program. Those incentives and pressures included paying more variable compensation than what was paid for alternative programs and punishments for failure to meet sales targets.

Pressure to sell the managed account program

Seeing the leakage from assets it held as plan participants retired, TIAA Sub created a new division to offer managed accounts. Rather than move assets to other providers, retiring participants could move their account to the managed program. They were encouraged to bring in new assets also. Fees ranged from 0.40% to 1.15% of assets per year (in addition to fund costs), compared to no additional fees for accounts held in the employer-sponsored plans. Advisors were trained to recognize the “pain points” for those clients and to convince them that the managed option was the right solution for them.

Advisors were paid significantly more for putting clients in managed accounts versus other products and an additional bonus could be earned. During regular meetings with advisors, supervisors praised those who gained rollovers into the managed accounts and placed advisors who failed to meet sales goals on performance improvement plans.

Misleading Statements, Failed Disclosures and Deficient Policies and Procedures

TIAA Sub's practices, not surprisingly, led to a flood of new managed accounts. The SEC found that the advisors made misleading statements when they told clients they provide "objective" and "disinterested" advice that was in the clients' "best interest" and that they acted as "fiduciaries." It also found that the conflicts of interest were not adequately disclosed in the firm's Form ADV Part brochure when it stated that the incentive compensation was proportionate to the effort required to recommend a product "designed to meet more complex needs" like a managed account.

Finally, the SEC found that TIAA Sub's own policies and procedures were not properly implemented. The firm did have written manuals that incorporated components of FINRA Regulatory Notice 13-45, which requires broker dealers to present clients with four options for rollovers: (i) leaving the client's assets in the employer-sponsored plan; (ii) rolling over the assets into a self-directed individual retirement account ("IRA") or managed IRA such as a managed account; (iii) rolling over the assets to a new employer's plan; and (iv) cashing out the account value/taking a lump sum distribution. It also required advisors to discuss other factors, including fees and expenses relating to the rollover options.

These policies were not enforced, however, when supervisors directed advisors not to follow them and some training materials encouraged advisors to avoid discussing fees and expenses with clients. Rollover recommendations regularly lacked any documentation confirming that fees and expenses about the managed program were discussed with a client or how they compared to expenses inside the employer-sponsored plans.

Observations

1. We believe that this action by the SEC is meant to be fair warning and that other advisors can expect the SEC to bring charges for their rollover practices.

2. Variable compensation is problematic. Industry practitioners have known this for some time but it is clear that paying different compensation for different advisory products brings conflicts of interest and so does paying more to roll assets outside of an employer-sponsored plan. Advisors will always be incentivized to sell what pays them more. The DOL now offers its new prohibited transaction exemption, PTE 2020-02, as guidance for how to adequately deal with compensation differentials. It remains to be seen, however, how the SEC will respond with attempts to mitigate these inherent conflicts.

3. Compliance manuals are not merely window dressing. It is critical that advisors

maintain appropriate policies and procedures, monitor that the procedures are being followed, and keep adequate records of their findings. Firms must scour all their writings, including training manuals, firm meeting scripts and client communications, to ensure that they are consistent with their formal policies and procedures.

We encourage advisory firms to hire competent counsel and consultants to draft adequate policies and procedures, including forms that detail comparative costs and expenses.

4. Fiduciary advisors will be able to continue to rely on the DOL's nonenforcement policy in FAB 2018-02. That release stated that the DOL will not pursue prohibited transaction claims against investment advice fiduciaries who work diligently and in good faith to comply with "Impartial Conduct Standards" for transactions that would have been exempted in the now invalidated 2016 exemptions. Similar to the SEC's findings in this action, the DOL requires compliance with three components – a best interest standard, a reasonable compensation standard, and a bar on misleading statements to plan investors about investment transactions. We understand that the IRS will follow a similar non-enforcement policy.

None of this prevents actions by private parties, actions by federal regulators who believe there has not been a good faith effort to comply, DOL action taken as soon as the nonenforcement period expires, or further state enforcement action. We encourage all firms to prepare diligently by implementing appropriate policies and procedures and to train, train, train.