

NEW YORK STOCK EXCHANGE, INC.

**EXCHANGE HEARING PANEL DECISION 02-223**

November 15, 2002

DEUTSCHE BANK SECURITIES, INC.  
MEMBER ORGANIZATION

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Violated Rule 440 and SEA Section 17(a) and SEC Reg. 17a-4 by failing to preserve for a period of three years and/or preserve in an accessible place for two years, electronic communications relating to the business of the firm and violated Exchange Rule 342 by failing to reasonably supervise and control the activities of its employees to assure compliance with Exchange Rules and federal securities laws relating to retention of electronic communications – Consent to censure, \$1,650,000 fine (reduced by amounts paid pursuant to agreements to pay a civil penalty of \$550,000 to the U.S. Treasury and a fine of \$550,000 to the NASD) and an undertaking.

**EXCHANGE HEARING PANEL DECISION 02-224**

GOLDMAN, SACHS & CO.  
MEMBER ORGANIZATION

\* \* \*

Violated Rule 440 and SEA Section 17(a) and SEC Reg. 17a-4 by failing to preserve for a period of three years and/or preserve in an accessible place for two years, electronic communications relating to the business of the firm and violated Exchange Rule 342 by failing to reasonably supervise and control the activities of its employees to assure compliance with Exchange Rules and federal securities laws relating to retention of electronic communications – Consent to censure, \$1,650,000 fine (reduced by amounts paid pursuant to agreements to pay a civil penalty of \$550,000 to the U.S. Treasury and a fine of \$550,000 to the NASD) and an undertaking.

**EXCHANGE HEARING PANEL DECISION 02-225**

MORGAN STANLEY & CO. INCORPORATED  
MEMBER ORGANIZATION

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Violated Rule 440 and SEA Section 17(a) and SEC Reg. 17a-4 by failing to preserve for a period of three years and/or preserve in an accessible place for two years, electronic communications relating to the business of the firm and violated Exchange Rule 342 by failing to reasonably supervise and control the activities of its employees to assure compliance with Exchange Rules and federal securities laws relating to retention of electronic communications – Consent to censure, \$1,650,000 fine (reduced by amounts paid pursuant to agreements to pay a civil penalty of \$550,000 to the U.S. Treasury and a fine of \$550,000 to the NASD) and an undertaking.

**EXCHANGE HEARING PANEL DECISION 02-226**

SALOMON SMITH BARNEY INC.

MEMBER ORGANIZATION

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**Violated Rule 440 and SEA Section 17(a) and SEC Reg. 17a-4 by failing to preserve for a period of three years and/or preserve in an accessible place for two years, electronic communications relating to the business of the firm and violated Exchange Rule 342 by failing to reasonably supervise and control the activities of its employees to assure compliance with Exchange Rules and federal securities laws relating to retention of electronic communications – Consent to censure, \$1,650,000 fine (reduced by amounts paid pursuant to agreements to pay a civil penalty of \$550,000 to the U.S. Treasury and a fine of \$550,000 to the NASD) and an undertaking.**

**EXCHANGE HEARING PANEL DECISION 02-227**

U.S. BANCORP PIPER JAFFRAY INC.

MEMBER ORGANIZATION

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**Violated Rule 440 and SEA Section 17(a) and SEC Reg. 17a-4 by failing to preserve for a period of three years and/or preserve in an accessible place for two years, electronic communications relating to the business of the firm and violated Exchange Rule 342 by failing to reasonably supervise and control the activities of its employees to assure compliance with Exchange Rules and federal securities laws relating to retention of electronic communications – Consent to censure, \$1,650,000 fine (reduced by amounts paid pursuant to agreements to pay a civil penalty of \$550,000 to the U.S. Treasury and a fine of \$550,000 to the NASD) and an undertaking.**

**Appearances:**

For the Division of Enforcement

David P. Doherty, Esq.

Robert A. Marchman, Esq.

Linda S. Riefberg, Esq.

James E. Shipley, Jr., Esq.

For the Respondents

Carmen J. Lawrence, Esq.

(For Deutsche Bank Securities, Inc.)

Gandolfo V. DiBlasi, Esq.

(For Goldman, Sachs &amp; Co.)

Steven G. Bradbury, Esq.

(For Morgan Stanley &amp; Co. Incorporated)

Fraser L. Hunter, Jr., Esq.

(For Salomon Smith Barney Inc.)

Dean M. Jeske, Esq.

(For U.S. Bancorp Piper Jaffray Inc.)

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An Exchange Hearing Panel met to consider a Stipulation of Facts and Consent to Penalty entered into between the Exchange's Division of Enforcement and Deutsche Bank Securities, Inc., Goldman, Sachs & Co., Morgan Stanley & Co. Incorporated, Salomon Smith Barney Inc. and U.S. Bancorp Piper Jaffray Inc. (the "Firms"). Without admitting or denying guilt, the Firms consent to a finding by the Hearing Panel that the Firms:

- I. Violated Exchange Rule 440 and Section 17(a) of the Securities and Exchange Act of 1934 and SEC Regulation 17a-4 by failing to preserve for a period of three years, and/or preserve in an accessible place for two years, electronic communications relating to the business of the firm.
- II. Violated Exchange Rule 342 in that it failed to reasonably supervise and control the activities of its employees, including a separate system of follow-up and review to assure compliance with Exchange Rules and federal securities laws relating to retention of electronic communications.

For the sole purpose of settling this disciplinary proceeding, without admitting or denying the findings herein, the Division of Enforcement and the Firms stipulate to the following:

#### **Background and Jurisdiction**

1. Deutsche Bank Securities, Inc. ("Deutsche Bank") is a Delaware corporation with its principal place of business in New York, New York. Deutsche Bank is registered with the Securities and Exchange Commission ("Commission") and is a member organization of the Exchange and NASD. Deutsche Bank engages in a nationwide securities business.
2. Goldman, Sachs & Co. ("Goldman Sachs") is a New York limited partnership with its principal place of business in New York, New York. Goldman Sachs is registered with the Commission and is a member organization of the Exchange and NASD. Goldman Sachs engages in a nationwide securities business.
3. Morgan Stanley & Co. Incorporated, ("Morgan Stanley") is a Delaware corporation with its principal place of business in New York, New York. Morgan Stanley is registered with the Commission and is a member organization of the Exchange and NASD. Morgan Stanley engages in a nationwide securities business.
4. Salomon Smith Barney Inc. ("Salomon Smith Barney") is a New York corporation with its principal place of business in New York, New York. Salomon Smith Barney is registered with the Commission and is a member organization of the Exchange and NASD. Salomon Smith Barney engages in a nationwide securities business.
5. U.S. Bancorp Piper Jaffray Inc. ("Piper Jaffray") is a Delaware corporation with its principal place of business in Minneapolis, Minnesota. Piper Jaffray is registered with the Commission and is a member organization of the Exchange and NASD. Piper Jaffray engages in a nationwide securities business.

### **Overview**

6. This action concerns the Respondents' violations of the record-keeping requirements of Section 17(a) of the Exchange Act and Rule 17a-4 thereunder and Exchange Rule 440 during the period of 1999 through at least 2001 (the "relevant period"). During all or part of the relevant period, each Respondent failed to preserve for three years, and/or to preserve in an accessible place for two years electronic mail communications (including interoffice memoranda and communications) received and sent by its agents and employees that related to its business as a member of an exchange or broker or dealer. Each Respondent lacked adequate systems or procedures for the preservation of electronic mail communications.

### **Non-Compliance with Books and Records Requirements**

7. The employees of each Respondent used electronic mail communications in part to conduct the Respondent's business as a broker, dealer and member of an exchange.
8. Respondents failed to preserve copies of electronic mail communications for three years, and/or maintain electronic mail communications for the first two years in an accessible place. Respondents did not have adequate systems or procedures in place during all or part of the relevant period to retain and/or make accessible electronic mail communications. Each Respondent's failure to preserve electronic mail communications and/or to maintain them in an accessible place was discovered during investigations being conducted jointly and separately by the Commission, the New York Stock Exchange, and NASD. The deficiencies in Respondents' systems and procedures for the preservation of electronic mail communications preexisted these investigations.
9. Some Respondents backed up electronic mail communications on tape or other media that Respondents represent was part of a process designed as a disaster recovery or business continuity measure, or for another business purpose. While some Respondents relied on these back-ups to preserve electronic mail communications during the relevant period, Respondents had inadequate systems or procedures to ensure the retention of such back-ups for three years and/or to maintain such data in a readily accessible manner for two years. These Respondents discarded, or recycled and overwrote their back-up tapes and other media, often a year or less after back-up occurred. In those instances in which Respondents did retain electronic mail communications, those electronic mail communications were often stored in an unorganized fashion on back-up tapes, other media, or on the hard drives of computers used by individual employees of Respondents. Before the filing of these proceedings, one or more Respondents took steps to develop new database systems for the retention of electronic mail communications.
10. While some Respondents relied on employees to preserve copies of their electronic mail communications on the hard drives of their individual personal computers or elsewhere, and many e-mails were preserved, there were inadequate systems or procedures to ensure that employees did so for the requisite record-keeping period. In some instances, hard drives of computers were erased when individuals left the employment of the Respondent.

**Section 17(a)(1) of the Exchange Act and Applicable Exchange Rules**

11. Section 17(a)(1) of the Exchange Act provides that each member of a national securities exchange, broker, or dealer “shall make and keep for prescribed periods such records, furnish copies thereof, and make and disseminate such reports as the Commission, by rule, prescribes as necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this title.”
12. The Commission has emphasized the importance of the records required by the rules as “the basic source documents” of a broker dealer. *Statement Regarding the Maintenance of Current Books and Records by Brokers and Dealers, 4 SEC Docket 195 (April 6, 1974)*. The record keeping rules are a “keystone of the surveillance of brokers and dealers by [Commission] staff and by the securities industry’s self-regulatory bodies.” *Edward J. Mawod & Co., 46 S.E.C. 865, 873 n. 39 (1977)*(citation omitted), *aff’d sub. nom. Mawod & Co. v. SEC, 591 F.2d 588 (10<sup>th</sup> Cir. 1979)*.
13. Pursuant to its authority under Section 17(a)(1) of the Exchange Act, the Commission promulgated Rule 17a-4. Rule 17a-4(b)(4) in turn requires each Respondent to “preserve for a period of not less than three years, the first two years in an accessible place. . .[o]riginals of all communications received and copies of all sent by such member, broker or dealer (including inter-office memoranda and communications) relating to his business as such.” Rule 17a-4 is not by its terms limited to physical documents. The Commission has stated that internal electronic communications fall within the purview of Rule 17a-4 and that, for the purposes of Rule 17a-4, “the content of the electronic communication is determinative” as to whether that communication is required to be retained and accessible. *Reporting Requirements for Brokers or Dealers under the Securities Exchange Act of 1934, Rel. No. 34-38245 (Feb. 5, 1997)*.
14. Exchange Rule 440 requires that: “every member organization shall make and preserve books and records as the Exchange may prescribe and as prescribed by Rule 17a-3. The record keeping format, medium and retention period shall comply with Rule 17a-4 under the Securities Exchange Act of 1934.”
15. Exchange Rule 342 requires that member firm organizations provide for appropriate supervisory control over every business activity and compliance with securities laws and regulations, including a separate system of follow-up and review to assure the proper exercise of authority and responsibility.
16. Based on the foregoing, each Respondent violated Section 17(a) of the Exchange Act and Rule 17a-4 thereunder, and Exchange Rules 440 and 342 by failing to preserve electronic mail communications for three years and/or by failing to preserve electronic mail communications for the first two years in an accessible place.

**DECISION**

The Hearing Panel, in accepting the Stipulation of Facts and Consent to Penalty, found the Firms guilty as set forth by unanimous vote.

**PENALTY**

In view of the above findings, the Hearing Panel, by unanimous vote, imposed the penalty consented to by the Firms of a censure and a fine in the amount of \$1,650,000, for total fines of \$8,250,000 from all Respondents. The amount to be paid to the NYSE by each Respondent shall be reduced by amounts paid by each Respondent pursuant to agreements to pay a civil monetary penalty of \$550,000 to the U.S. Treasury and a fine of \$550,000 to NASD in related proceedings. In addition to the monetary fine, Respondents shall complete an appropriate undertaking to review its procedures regarding the preservation of electronic mail communications for compliance with the federal securities laws and regulations, and the rules of the Exchange and NASD. Within 90 days of the execution of the Stipulation and Consent each Respondent undertakes and agrees to inform the Exchange in writing that it has completed its review and that it has systems and procedures in place reasonably designed to ensure compliance with those laws and rules concerning the preservation of electronic mail communications. The Division of Enforcement shall have the discretion, upon a showing of good cause, to extend the deadline for compliance with the undertaking set forth in this paragraph.

For the Hearing Panel

Edward W. Morris, Jr.  
Chief Hearing Officer