

NEW YORK STOCK EXCHANGE, INC.

EXCHANGE HEARING PANEL DECISION 04-134
SPEAR, LEEDS & KELLOGG SPECIALISTS LLC
MEMBER ORGANIZATION

August 11, 2004

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Violated Exchange Rule 342 in that the Firm: (a) failed to have adequate systems and procedures in place reasonably designed to ensure compliance with the Exchange's Allocation Policy and Procedures; and (b) failed to have reasonable procedures in place relating to allocation applications and letters signed and submitted to the Exchange; Violated the Exchange's Allocation Policy and Procedures by having prohibited contact with a proposed listing company; Engaged in acts detrimental to the interests or welfare of the Exchange in that the Firm violated the Exchange's Allocation Policy and Procedures by failing to disclose contacts with a listing company; Violated Exchange Rule 476(a)(4) in that the Firm submitted an allocation application letter, which contained a misstatement – Consent to censure and \$50,000 fine.

Appearances:

For the Division of Enforcement
Margaret M. Tolan, Esq.

For the Respondent
Ida Wurczinger Draim, Esq.
Christina Schulz, Esq.

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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 Spear, Leeds and Kellogg Specialists LLC (the "Firm"), a member organization. Without admitting or denying guilt the Firm consented to a finding by the Hearing Panel that it:

- I. Violated Exchange Rule 342 in that the Firm:
 - A. Failed to have adequate systems and procedures in place reasonably designed to ensure compliance with the Exchange's Allocation Policy and Procedures; and
 - B. Failed to have reasonable procedures in place relating to allocation applications and letters signed and submitted to the Exchange.
- II. Violated the Exchange's Allocation Policy and Procedures by having contact with a proposed listing company during the restricted period.
- III. Engaged in acts detrimental to the interests or welfare of the Exchange in that the Firm violated the Exchange's Allocation Policy and Procedures by failing to disclose to the Exchange one or more contacts with a listing company.

- IV. Violated Exchange Rule 476(a)(4) in that the Firm submitted to the Exchange an allocation application letter, which contained a misstatement.

For the sole purpose of settling this disciplinary proceeding, and without admitting or denying any of the facts or matters referred to in the Stipulation of Facts and Consent to Penalty, the Firm stipulates to the entry of findings, the substance of which follows:

Background and Jurisdiction

1. The Firm is a broker-dealer registered with the Securities and Exchange Commission, pursuant to Section 15(b) of the Securities Exchange Act of 1934 (the "Exchange Act"), since December 1996. In addition, the Firm is an Exchange member organization. On October 31, 2000, the Firm's parent company, Spear, Leeds & Kellogg, L.P., was acquired by The Goldman Sachs Group, Inc., the securities of which are registered with the Commission pursuant to Section 12(b) of the Exchange Act, and the Firm became an indirect subsidiary of The Goldman Sachs Group, Inc.
2. Howard Eisen ("Eisen") (See Exchange Hearing Panel Decision 04-125), was a Managing Director in the Firm's Corporate Relations Department from February 1997 through August 2002.
3. The Exchange's Division of Market Surveillance commenced an investigation to determine if the Firm and/or any of its employees violated the Exchange's Allocation Policy and Procedures and Exchange Rules by impermissibly contacting XYZ ("XYZ") after the "green sheet" and accompanying XYZ letter was issued by the Exchange soliciting allocation applications from specialist units (hereinafter "the restricted period") and by failing to disclose certain communications with XYZ.
4. By letter dated September 23, 2003, Enforcement notified the Firm that a formal investigation had been commenced based on a matter referred by the Division of Market Surveillance

Violation of Allocation Policy

5. In direct contravention of the Exchange's Allocation Policy and Procedures and Exchange Rules, while acting as the Firm's representative, Eisen contacted a company which was about to list its shares on the Exchange, during the restricted period. Also in contravention of the Allocation Policy, Eisen caused the Firm to fail to disclose certain contacts that Eisen and his subordinates at the Firm had with the company in the six months prior to the time allocation applications were solicited and to make a misstatement in its allocation application letter submitted to the Exchange.
6. In or about April 2002, XYZ was in the process of listing its shares of stock on the Exchange. At or about this time, XYZ exercised its option to make its final selection of a specialist unit from a group selected by the Exchange Allocation Committee.
7. On April 11, 2002, the Exchange issued a written notice ("green sheet") to all specialist units soliciting applications for the allocation of XYZ. XYZ attached a

letter to the notice stating certain specialist firm characteristics that XYZ preferred. XYZ's letter also indicated that it preferred a specialist firm that did not act as a specialist for one of its competitors.

8. The Firm is a specialist for one of XYZ's competitors.
9. The Exchange's Allocation Policy ¹states, in relevant part:

Specialist units or any individual acting on their behalf may not have any contact with a listing company from the earlier of the time that written notice is given that the listing company filed its listing application with the Exchange; or the time that the allocation applications are solicited with reference to that company.

Specialist units must describe in their applications to be allocated the stock of a listing company any contacts they, or any individual acting on their behalf, have had with any employee of that company, or any individual acting on behalf of that company with regard to its prospective listing on the Exchange, within six months prior to the earlier of the date that written notice is given that the listing company filed its listing application with the Exchange or the date that allocation applications are solicited with respect to that company.

10. On the afternoon of April 11, 2002, Eisen contacted XYZ after XYZ's notice had already been disseminated and before the Firm had submitted its allocation application for XYZ. In this conversation, Eisen raised the issue of XYZ's preferences and explained to XYZ why there was no conflict if a specialist firm represented XYZ and one of its competitors. As a result of this conversation, XYZ inquired of the Exchange about the possibility of changing XYZ's letter regarding XYZ's preferences.
11. Eisen failed to note his conversation with XYZ in the Firm's ACT database, the database where the Firm records substantive contacts with listing companies and contacts that were likely to affect the listing company's view of the Firm and the Exchange.
12. Although the ACT database was the central repository for contacts with customers, employees of the Firm exercised discretion regarding whether an interaction with a listing company or prospect was substantive and hence had to be entered into the ACT database.
13. There were no Firm written procedures to inform the Firm employees about the requirements and restrictions of the Allocation Policy.
14. On the evening of April 11, 2002, Eisen instructed an employee to prepare a draft of the Firm's allocation application for XYZ including who the proposed individual specialist would be. The employee, in preparing the application letter, reviewed the Firm's ACT database in order to report prior contacts with the company for inclusion

¹ Subsequently codified as Rule 103(b).

in the application letter. The employee completed a draft of the letter on April 11 and submitted it, along with a one page standard application form, to a member of the Firm's management team for final review.

15. As a result of Eisen's failure to disclose his contacts with XYZ, the Firm failed to disclose in its application the following contacts with XYZ, which were required to be disclosed:
 - a. e-mail to XYZ from Eisen dated March 16, 2002, attaching various documents relevant to NYSE listing process;
 - b. e-mail to XYZ from Eisen dated March 16, 2002 with additional recap of marketing meeting;
 - c. e-mail to XYZ from the Firm dated March 20, 2002, following up on Eisen's previous correspondence and referencing an attachment XYZ might find useful as it progressed through the listing and allocation process.
16. On the afternoon of April 12, 2002, a Managing Director of the Firm, contacted the director of the Exchange Committee Support area, to inform her that the Firm was in the process of submitting its application to trade XYZ a few hours past the deadline.
17. The application and letter were submitted to the Exchange on April 12, 2002 and affirmatively stated "all contact has ceased due to the release of the green sheet on April 11, 2002." The application letter failed to disclose Eisen's post-green sheet call to XYZ.
18. In contravention of the Allocation Policy, Eisen and the Firm failed to disclose in the Firm's application all of the contacts that Eisen and his subordinates at the Firm had with XYZ in the six months prior to the time allocation applications were solicited.
19. The Firm application and letter were submitted to the Exchange with the signature of the Firm's Chief Executive Officer despite the fact that he did not review or sign the XYZ application or letter and he had not delegated the authority to sign his name.
20. At that time, the Firm lacked adequate procedures for the review and signature of the final application and letter.
21. Ultimately, the Firm was not selected as XYZ's specialist.

DECISION

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

PENALTY

In view of the above findings, the Hearing Panel, by unanimous vote, imposed the penalty consented to by the Firm of a censure and a fine in the amount of \$50,000.

For the Hearing Panel

Vincent F. Murphy
Hearing Officer