

**UNITED STATES OF AMERICA  
BEFORE THE  
SECURITIES AND EXCHANGE COMMISSION**

**Securities Exchange Act of 1934  
Release No. 56634 / October 10, 2007**

**Administrative Proceeding  
File No. 3-12864**

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<b>In the Matter Of</b>	:	<b>ORDER INSTITUTING ADMINISTRATIVE</b>
	:	<b>AND CEASE-AND-DESIST PROCEEDINGS,</b>
<b>MORGAN STANLEY &amp; CO.</b>	:	<b>MAKING FINDINGS, AND IMPOSING</b>
<b>INCORPORATED,</b>	:	<b>REMEDIAL SANCTIONS AND A CEASE-</b>
	:	<b>AND-DESIST ORDER PURSUANT TO</b>
	:	<b>SECTIONS 15(b), 15B(c) AND 21C OF THE</b>
<b>Respondent.</b>	:	<b>SECURITIES EXCHANGE ACT OF 1934</b>
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**I.**

The Securities and Exchange Commission (“Commission”) deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Sections 15(b), 15B(c) and 21C of the Securities Exchange Act of 1934 (“Exchange Act”) against Morgan Stanley & Co. Incorporated (“MS&Co”), on behalf of itself and as successor to Morgan Stanley DW Inc. (“MSDW” or “Respondent”).

**II.**

In anticipation of the institution of these proceedings, the Respondent has submitted an Offer of Settlement (“Offer”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over it and over the subject matter of these proceedings, which are admitted, the Respondent consents to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order Pursuant to Sections 15(b), 15B(c) and 21C of the Securities Exchange Act of 1934 (“Order”), as set forth below.

### III.

On the basis of this Order and the Respondent's Offer, the Commission finds that:

#### A. Summary

These proceedings arise out of MSDW's failure over a five year period to provide to its customers accurate and complete written trade confirmations for certain fixed income securities. Starting as early as May 2000, two former MSDW registered representatives complained to management about missing or incorrect information on MSDW trade confirmations relating to yield, call data, and other bond features. For several years, however, MSDW failed to fix the problems identified by the registered representatives even after it established a Task Force in late 2003 to address numerous other fixed income trade confirmation problems known to management. In December 2004, the Commission's staff became aware of the longstanding noncompliance of MSDW's fixed income securities trade confirmations. After the staff contacted MSDW regarding these longstanding regulatory deficiencies, MSDW commenced an internal investigation into its trade confirmation practices, during the course of which it uncovered several additional regulatory problems relating to its trade confirmations. In 2005, MS&Co voluntarily disclosed certain fixed income trade confirmation violations it had discovered during a separate review into its own trade confirmation practices. As a result of the staff's inquiries, MSDW and MS&Co firmly committed the resources to correct their trade confirmation problems.

#### B. Respondent

1. Morgan Stanley & Co. Incorporated is a Delaware corporation with its principal place of business in New York, New York. MS&Co is a registered broker-dealer with the Commission pursuant to Section 15(b) of the Exchange Act, a member of the Financial Industry Regulatory Authority ("FINRA") (formerly known as the National Association of Securities Dealers ("NASD")), the New York Stock Exchange ("NYSE"), and the Municipal Securities Rulemaking Board ("MSRB"). MS&Co is a wholly owned subsidiary of Morgan Stanley, a Delaware corporation whose common stock trades on the New York Stock Exchange. MS&Co provides comprehensive brokerage, investment and financial services nationwide.

2. Morgan Stanley DW Inc., during the relevant time period of 2000 to 2006, was a Delaware corporation with its principal place of business in New York, New York and then Purchase, New York. Also during the relevant time period, MSDW was a registered broker-dealer with the Commission pursuant to Section 15(b) of the Exchange Act, and a member of the NASD, the NYSE, and the MSRB. MSDW was a wholly owned subsidiary of Morgan Stanley until April 1, 2007, when MSDW merged into MS&Co to form a single broker-dealer. Before the merger, MSDW provided comprehensive brokerage, investment and financial services nationwide.

### C. Facts

3. As early as May 2000, customers of two MSDW financial advisors began to complain that their written confirmations of certain fixed income securities transactions contained inaccurate information. After orally providing their clients with the correct information, the financial advisors, along with their branch manager, reported the customers' complaints to MSDW headquarters. The inaccuracies identified by the customers primarily related to (1) missing, exaggerated, understated or multiple yield information, (2) erroneous or missing call and ratings data, and (3) erroneous instrument descriptions on both corporate and municipal bonds. The financial advisors were repeatedly told by managers in MSDW's retail fixed income department that MSDW was working on the problems. However, the problems persisted for many months, and MSDW continued to issue trade confirmations with the identified deficiencies.

4. By August 2003, MSDW was aware of numerous fixed income securities trade confirmation deficiencies, including the issues raised by the financial advisors. As a result, MSDW established a task force comprised of trading, operations, information technology and compliance personnel (the "Task Force") to specifically address these trade confirmation issues. Although the Task Force resolved some of these issues, many problems were not resolved due to insufficient accountability of the relevant MSDW personnel, a general lack of managerial oversight of the Task Force, and a failure to allocate sufficient resources. For example, the Task Force noted on November 12, 2003, that one issue "[n]eed[ed] to be prioritized" but five months later, on April 21, 2004, it stated that there was "[n]o timetable for when the project might be started." By August 2004, the Task Force had resolved only 20 of the 43 regulatory and non-regulatory trade confirmation issues it had identified. Nevertheless, MSDW continued to knowingly issue noncompliant trade confirmations.

5. In December 2004, the Commission staff became aware of the longstanding regulatory deficiencies with MSDW's fixed income trade confirmations. When contacted by the staff, MSDW commenced a comprehensive investigation into its trade confirmation practices and, during the course of its internal review, MSDW uncovered additional regulatory violations relating to its trade confirmations for fixed income securities. MSDW committed substantial resources to correct the fixed income trade confirmation problems. It also reorganized its reporting structure, hired new management, implemented a new process to identify, mitigate and remediate any future confirmation issues, and increased the legal, technical and financial support for its confirmation process.

6. At various times during the relevant period, MSDW's trade confirmations for certain fixed income securities were noncompliant in the following respects, among others:

- Certain trade confirmations failed to disclose MSDW's role as agent and the commissions charged on the agency trade;
- Certain trade confirmations failed to disclose the put details (put date; price; yield-to-put) of corporate and municipal bonds with put features;

- Certain trade confirmations provided inaccurate or outdated call or put dates for municipal bonds with rolling call or put features;
- All sell-side trade confirmations of corporate, agency and treasury bonds failed to disclose the yield;
- Certain trade confirmations failed to disclose the yield information involving purchases of corporate zero coupon bonds as well as asset-backed and mortgage-backed debt securities; and
- Certain trade confirmations provided inaccurate yield calculations for stepped bonds and premium call municipal bonds with declining premiums.

7. In 2005, MS&Co voluntarily disclosed to the Commission’s staff that, due to operations system errors, it too had provided its customers with corporate and municipal bond trade confirmations containing noncompliant information. Among other violations, MS&Co had calculated the wrong yield in both corporate and municipal bonds with call or put features, provided an inaccurate description of bonds with negative yields as having positive yields, failed to disclose all put features for municipal bonds, and erroneously disclosed that MS&Co had executed certain trades in a “principal” capacity when in fact it had executed those transactions as an “agent”.

#### **D. Violations**

8. As a result of the conduct described above, MSDW and MS&Co willfully violated Rule 10b-10 under the Exchange Act which requires broker-dealers, when effecting securities transactions for customers, to accurately disclose certain terms of the transaction in a written confirmation to the customer.<sup>1</sup> See 17 C.F.R. § 240.10b-10(a). Rule 10b-10 mandates that the confirmation disclose whether the broker-dealer is acting as an agent or as principal and, if as an agent, the amount of any remuneration it received. Id. For trades involving debt securities, broker-dealers must disclose, among other things, either the yield to maturity or the yield at which the transaction was effected (depending on whether the transaction was effected exclusively on the basis of a dollar price or on the basis of yield). Id. at § 240.10b-10(a)(5) and (6).

9. As a result of the conduct described above, MSDW and MS&Co willfully violated Section 15B(c)(1) of the Exchange Act and MSRB Rule G-15. Section 15B(c)(1) makes it unlawful to use the mails or other means or instrumentalities of interstate commerce to effect transactions in or induce the purchase or sale of any municipal security in contravention of the MSRB rules. See 15 U.S.C. § 78o-4(c)(1) (2006). MSRB Rule G-15, in particular, requires,

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<sup>1</sup> Rule 10b-10 works to protect investors and combat broker-dealer fraud by ensuring full and fair disclosure to investors of the substance of the transactions effected by their broker. See In re: Hattier, Sanford & Reynoir, Exchange Act Release No. 34-39543, 66 SEC Docket 624, 1998 WL 7454, at \*4 n.16 (Jan. 13, 1998).

among other things, that a broker-dealer provide its customer with a written confirmation disclosing whether it acted as “principal” or as an “agent” when effecting the transaction in municipal securities. MSRB, Rule G-15(a)(i)(A)(1)(d) (2003). MSRB Rule G-15 also requires that a broker-dealer disclose on the written trade confirmation the yield information and dollar price of the municipal bond.<sup>2</sup> MSRB, Rule G-15(a)(i)(A)(5). For transactions effected on the yield-to-call date or yield-to-put date, the trade confirmation must indicate if that yield is to a call date or to a put date, “along with the date and dollar price of the call or put.” Id.

**E. Respondent’s Remedial Efforts**

10. In determining to accept the Offer, the Commission considered the remedial acts promptly taken by MSDW and MS&Co when contacted by the Commission’s staff and the subsequent cooperation the firms afforded.

**F. Undertakings**

MS&Co has undertaken to do the following actions.

11. The Respondent shall retain, within thirty (30) days of the issuance of the Order, at Respondent’s expense, a qualified independent consultant (the “Consultant”), not unacceptable to the Commission staff, to (1) verify that the deficiencies in the Respondent’s policies, practices and procedures relating to fixed income securities trade confirmations, which were identified during the course of the Respondent’s internal investigation or review (as described in Section III, paragraphs 5, 6 and 7 above), have been eliminated and that these policies, practices and procedures are now sufficient to provide for ongoing compliance with Exchange Act Rule 10b-10 and MSRB Rule G-15; and (2) prepare a Report confirming compliance and, with respect to any policies, practices or procedures not in compliance with Exchange Act Rule 10b-10 or MSRB Rule G-15, making recommendations for how the Respondent should modify or supplement its policies, practices and procedures to remedy the deficiencies identified by the Consultant in the Report. The Respondent shall provide a copy of the engagement letter detailing the Consultant’s responsibilities to Fredric D. Firestone, Associate Director, Division of Enforcement, Securities and Exchange Commission, 100 F Street, N.E., Washington, DC, 20549-7561.

12. The Respondent shall cooperate fully with the Consultant, including providing the Consultant with access to its files, books, records, and personnel as reasonably requested for the above-mentioned review, and obtaining the cooperation of its employees or other persons under its control.

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<sup>2</sup> The MSRB has stated that, “[t]he yield disclosure on confirmations of purchases from customers is intended to provide customers with a means of assessing the merits of alternative investment strategies (such as different possible reinvestment transactions) and the merits of the particular transaction being confirmed.” MSRB, G-15 Interpretive Notice Concerning Yield Disclosure Requirements for Purchases from Customers (Sept. 1, 1981).

13. The Respondent shall require the Consultant to report to the Commission staff on his/her activities as the staff shall request.

14. The Respondent shall permit the Consultant to engage such assistance, clerical, legal or expert, as necessary and at reasonable cost, to carry out his/her activities, and the cost, if any, of such assistance shall be borne exclusively by the Respondent.

15. The Respondent shall require the Consultant to complete his/her review of the Respondent's policies, practices, and procedures relating to Exchange Act Rule 10b-10 and MSRB Rule G-15, and prepare, within one hundred and eighty (180) days of the issuance of the Order, unless otherwise extended by the staff for good cause, the written Report referenced above in paragraph 11. The Consultant shall provide the Report simultaneously to both the Commission staff (at the address set forth above) and the Respondent. The Respondent shall afford the Consultant the option to seek an extension of time, for good cause shown, to submit the Report by making a written request to the staff at the address set forth above, a copy of which the Consultant shall provide to the Respondent.

16. The Respondent shall adopt and implement all recommendations set forth in the Report within one hundred and twenty (120) days of the Respondent's receipt of the Report; provided, however, that as to any recommendation that the Respondent considers to be, in whole or in part, unduly burdensome or impractical, the Respondent may submit in writing to the Consultant and the staff (at the address set forth above), within sixty (60) days of receiving the Report, an alternative policy, practice, or procedure designed to achieve the same objective or purpose. The Respondent and the Consultant shall then attempt in good faith to reach an agreement relating to each recommendation that the Respondent considers to be unduly burdensome or impractical and the Consultant shall reasonably evaluate any alternative policy, practice, or procedure proposed by the Respondent. Such discussion and evaluation by the Respondent and the Consultant shall conclude within ninety (90) days after the Respondent's receipt of the Report, whether or not the Respondent and the Consultant have reached an agreement. Within fourteen (14) days after the conclusion of the discussion and evaluation by the Respondent and the Consultant, the Respondent shall require that the Consultant inform the Respondent and the staff (at the address set forth above) of his/her final determination concerning any recommendation that the Respondent considers to be unduly burdensome or impractical. The Respondent shall abide by the determinations of the Consultant and, within sixty (60) days after final agreement between the Respondent and the Consultant or final determination by the Consultant, whichever occurs first, the Respondent shall adopt and implement all of the recommendations that the Consultant deems appropriate.

17. The Respondent shall certify in writing to the Consultant and the staff (at the address set forth above) within fourteen (14) days of the Respondent's adoption of all of the recommendations that the Consultant deems appropriate, that the Respondent has adopted and implemented all of the Consultant's recommendations and that the Respondent has established policies, practices, and procedures pursuant to Exchange Act Rule 10b-10 and MSRB Rule G-15 that are consistent with the Order.

18. The Respondent may apply to the Commission's staff for an extension of the deadlines described above before their expiration, and upon a showing of good cause by the Respondent, the Commission's staff may, in its sole discretion, grant such extensions for whatever time period it deems appropriate.

19. The Respondent shall (i) not terminate the Consultant without prior written approval of the Commission's staff, (ii) compensate the Consultant and persons engaged to assist the Consultant for services rendered pursuant to the Order at their reasonable and customary rates; and (iii) not be in and shall not have an attorney-client relationship with the Consultant and shall not seek to invoke the attorney-client or any other doctrine or privilege to prevent the Consultant from transmitting any information, reports, or documents to the Commission or its staff.

20. The Respondent shall require the Consultant to enter into an agreement that provides that, for the period of engagement and for a period of two years from completion of the engagement, the Consultant shall not enter into any employment, consultant, attorney-client, auditing or other professional relationship with the Respondent or any of their present or former affiliates, directors, officers, employees, or agents acting in their capacity as such. The agreement will also provide that the Consultant will require that any firm with which he/she is affiliated or of which he/she is a member, and any person engaged to assist the Consultant in the performance of his/her duties under the Order shall not, without the prior written consent of the Commission's staff, enter into any employment, consultant, attorney-client, auditing or other professional relationship with the Respondent, or any of its present or former affiliates, directors, officers, employees, or agents acting in its capacity as such, for the period of the engagement and for a period of two years after the engagement.

21. The Respondent shall certify in writing to the staff (at the address set forth above), in the second year following the issuance of the Order, that the Respondent has established and continues to maintain policies, practices, and procedures pursuant to Exchange Act Rule 10b-10 and MSRB Rule G-15 that are consistent with the Order.

#### **IV.**

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in the Respondent's Offer.

Accordingly, pursuant to Sections 15(b), 15B(c) and 21C of the Exchange Act, it is hereby ORDERED that:

A. MS&Co shall be, and hereby is, censured;

B. MS&Co shall cease and desist from committing or causing any violations and any future violations of Rule 10b-10 under the Exchange Act, or Section 15B(c) of the Exchange Act, including failing, at or before the completion of a transaction in municipal securities with or

for the account of a customer, to give or send to the customer a written confirmation that complies with certain requirements under MSRB Rule G-15;

C. Within ten days of the issuance of this Order, MS&Co shall pay a civil money penalty in the aggregate amount of \$7,500,000 to the United States Treasury. Such payment shall be: (1) made by United States postal money order, certified check, bank cashier's check or bank money order; (2) made payable to the Securities and Exchange Commission; (3) hand-delivered or mailed to the Office of Financial Management, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Stop 0-3, Alexandria, VA 22312; and (4) submitted under cover letter that identifies Morgan Stanley & Co. Incorporated as the Respondent in these proceedings, and the file number of these proceedings, a copy of which cover letter and money order or check shall be sent to Fredric D. Firestone, Associate Director, Division of Enforcement, Securities and Exchange Commission, 100 F Street, N.E., Washington, DC 20549-7561; and

D. MS&Co shall comply with the undertakings enumerated in Section III, paragraphs 11 through 21 above.

By the Commission.

Nancy M. Morris  
Secretary