

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. 2015044226501**

TO: Department of Market Regulation
Financial Industry Regulatory Authority (“FINRA”)

RE: Morgan Stanley & Co. LLC, Respondent
Broker-Dealer
CRD No. 8209

Pursuant to FINRA Rule 9216 of FINRA’s Code of Procedure, Morgan Stanley & Co. LLC (the “firm” or “Morgan Stanley”) submits this Letter of Acceptance, Waiver and Consent (“AWC”) for the purpose of proposing a settlement of the alleged rule violations described below. This AWC is submitted on the condition that, if accepted, FINRA will not bring any future actions against the firm alleging violations based on the same factual findings described herein.

I.

ACCEPTANCE AND CONSENT

- A. The firm hereby accepts and consents, without admitting or denying the findings, and solely for the purposes of this proceeding and any other proceeding brought by or on behalf of FINRA, or to which FINRA is a party, prior to a hearing and without an adjudication of any issue of law or fact, to the entry of the following findings by FINRA:

BACKGROUND

Morgan Stanley became a FINRA member on June 5, 1970. Morgan Stanley is headquartered in New York, New York. The firm has 38 branch offices and approximately 4,008 registered individuals.

RELEVANT DISCIPLINARY HISTORY

On December 16, 2015, FINRA accepted an AWC in which the firm was censured and fined \$15,000 for violations of FINRA Rule 7450 on August 18 and 19, 2014.

OVERVIEW

Between January 2011 and July 2019, the firm erroneously submitted approximately 380 million reports to the Order Audit Trail System (“OATS”) that it was not required to report and submitted more than 400 million reports to OATS with inaccurate data in

violation of FINRA Rules 7450 and 2010.¹ Furthermore, the firm failed to establish a supervisory system, including written supervisory procedures, reasonably designed to achieve compliance with its OATS reporting obligations in violation of FINRA Rules 3110 and 2010 and NASD Rule 3010.

FACTS AND VIOLATIVE CONDUCT

FINRA Rule 7450

FINRA Rule 7450 requires firms to transmit to OATS reports “containing each applicable item of order information identified in Rule 7440(b), (c), and (d) whenever an order is originated, received, transmitted to another department within the member or to another member, modified, canceled, or executed.” Rule 7440 requires firms’ OATS reports to reflect, among other things, the origin of the order, the date and time of order receipt and whether the order originated with a reporting member.

FINRA established OATS as an integrated audit trail of order, quote, and trade information for all NMS stocks and OTC equity securities. FINRA uses this audit trail system to recreate events in the life cycle of orders and more completely monitor the trading practices of member firms. The firm impeded these objectives by (1) submitting OATS reports with inaccurate time stamps, which impact FINRA’s ability to create accurate order life cycles; (2) reporting inaccurate Special Handling Codes, which result in either false or missed alerts; and (3) reporting non-material order modifications to OATS, which creates the risk of false alerts in FINRA’s surveillance.

The Firm’s Violations of FINRA Rule 7450

Improper Submission of Cancel/Replace (“CR”) Reports

The firm’s OATS reporting violations resulted from unrelated instances of faulty programming logic that occurred on different desks and systems over several years. Starting in January 2011, the firm’s Convertible Bond, Program and Swap Trading Desks implemented programming logic that caused its system to incorrectly report a CR Report to OATS any time a non-material change was made to a customer order (a CR Report is only required for material changes to the terms of an order, i.e., price or quantity). This faulty logic impacted 7,459,169 reportable order events (“ROEs”) on these three desks between January 2011 and September 2016. The firm began implementing a series of fixes to its OATS reporting logic in August 2016 and fully remediated its over-reporting issue in November 2017.

Beginning on February 1, 2015, the firm’s Alternative Trading System (“ATS”) also over-reported CR Reports. Internal updates to an algorithm that routed orders to the firm’s ATS resulted in CR Reports being unnecessarily reported to OATS. This erroneous programming resulted in the firm reporting 384,830,864 CR Reports to OATS that it was not required to report between February 1, 2015 and May 11, 2016.

¹ A violation of FINRA Rule 7450 also constitutes a violation of FINRA Rule 2010.

In December 2016 and July 2017, the firm implemented logic specific to two new systems that caused the firm to over-report CR Reports between December 2016 and April 2019. This issue caused the firm to report 32,371 CR Reports that it should not have reported. The firm resolved this issue in July 2019.

At times between January 2011 and July 2019, the above-described violations represented as much as 9.4 percent of all CR Reports that the firm transmitted to OATS.

Orders with an Inaccurate Order Received Time

The February 2015 programming change to the firm's ATS also resulted in order events being reported to OATS out of sequence. In accordance with the requirements of FINRA Regulatory Notice 14-07 (February 14, 2014), the firm started reporting its ATS order flow under a unique MPID. The OATS reporting logic used to submit this order flow inadvertently generated incorrect timestamps for order modifications (CR Reports), which in turn caused the subsequent Route ("RT") reports to be incorrectly reported with the order identifier of the original order instead of the new order identifier generated by the CR Report. In total, the firm submitted 424,412,081 CR reports to OATS with an incorrect order receipt time. These reports represented 10.36 percent of the total number of CR Reports submitted by the firm between February 2015 and February 2016. The firm resolved this issue on February 22, 2016.

Incorrect Special Handling Codes

Starting in October 2011, the implementation of faulty programming logic caused the Program Trading desk to report the Seller Option ("SLR") Special Handling Code instead of the Next Day ("ND") or Same Day ("SD") Special Handling Codes. This erroneous logic impacted 1,572 New Order ("NW") Reports. Also, starting in April 2016, the firm implemented erroneous logic that resulted in the failure of its Program Trading and Cash Trading desks to submit the Counter Party Restriction ("CPR") Special Handling Code on 7,420 NW Reports. The firm corrected the logic in July 2019.

The conduct described in the paragraphs above constituted separate and distinct violations of FINRA Rules 7450 and 2010.

FINRA Rules 3110 and NASD Rule 3010¹

FINRA Rule 3110(a) requires firms to establish and maintain a system to supervise the activities of each associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable FINRA Rules. Additionally, FINRA Rule 3110(b) requires firms to establish, maintain, and enforce written procedures to supervise the types of business in which they engage and the activities of their associated persons that are reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable FINRA rules.

¹ FINRA Rule 3110 superseded NASD Rule 3010 on December 1, 2014.

The Firm's Violations of FINRA Rule 3110 and NASD Rule 3010

The firm's written supervisory procedures ("WSPs") required firm personnel to review FINRA's OATS website for unmatched executions and routes, late submissions, rejected ROEs, inter-firm mismatches and FORE status on a daily basis. The firm's WSPs also stated that the firm was to hold monthly compliance meetings to review all data in FINRA monthly report cards. The firm's supervisory system, including its written supervisory procedures did not, however, include a review for reporting violations that could only be identified from a comparison to its books and records.¹ For example, the firm's supervisory reviews would not have identified instances where the firm either over or under-reported data to OATS or reported incorrect timestamps or Special Handling Codes to OATS. The conduct described in this paragraph constitutes violations of FINRA Rule 3110 (for conduct on or after December 1, 2014) and FINRA Rule 2010 and NASD Rule 3010 (for conduct prior to December 1, 2014).

B. The firm also consents to the imposition of the following sanctions:

1. A censure;
2. A fine of \$300,000 (consisting of a \$200,000 fine for the OATS violations and a \$100,000 fine for the supervision violation); and
3. An undertaking to revise the firm's WSPs with respect to the areas described above. Within 30 business days of this AWC becoming final, a principal of the Respondent shall submit to the COMPLIANCE ASSISTANT, DEPARTMENT OF ENFORCEMENT, 15200 OMEGA DRIVE, SUITE 300, ROCKVILLE, MD 20850, a signed, dated letter, or an e-mail from a work-related account of the registered principal to MarketRegulationComp@finra.org, providing the following information: (1) a reference to this matter; (2) a representation that the firm has revised its WSPs to address the deficiencies described in this AWC; and (3) the date the revised procedures were implemented.

The firm agrees to pay the monetary sanction upon notice that this AWC has been accepted and that such payment is due and payable. It has submitted an Election of Payment form showing the method by which it proposes to pay the fine imposed.

The firm specifically and voluntarily waives any right to claim that it is unable to pay, now or at any time hereafter, the monetary sanction imposed in this matter.

The sanctions imposed herein shall be effective on a date set by FINRA staff.

¹ See FINRA Notice to Members 98-96 requiring member firms' written supervisory procedures to describe the following: (1) a specific identification of the individual(s) responsible for supervisory review; (2) the supervisory steps and reviews to be taken by the appropriate supervisor; (3) the frequency of such reviews; and (4) how such reviews will be documented.

II.

WAIVER OF PROCEDURAL RIGHTS

The firm specifically and voluntarily waives the following rights granted under FINRA's Code of Procedure:

- A. To have a Complaint issued specifying the allegations against the firm;
- B. To be notified of the Complaint and have the opportunity to answer the allegations in writing;
- C. To defend against the allegations in a disciplinary hearing before a hearing panel, to have a written record of the hearing made and to have a written decision issued; and
- D. To appeal any such decision to the National Adjudicatory Council ("NAC") and then to the U.S. Securities and Exchange Commission and a U.S. Court of Appeals.

Further, the firm specifically and voluntarily waives any right to claim bias or prejudgment of the Chief Legal Officer, the NAC, or any member of the NAC, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including acceptance or rejection of this AWC.

The firm further specifically and voluntarily waives any right to claim that a person violated the ex parte prohibitions of FINRA Rule 9143 or the separation of functions prohibitions of FINRA Rule 9144, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including its acceptance or rejection.

III.

OTHER MATTERS

The firm understands that:

- A. Submission of this AWC is voluntary and will not resolve this matter unless and until it has been reviewed and accepted by the NAC, a Review Subcommittee of the NAC, or the Office of Disciplinary Affairs ("ODA"), pursuant to FINRA Rule 9216;
- B. If this AWC is not accepted, its submission will not be used as evidence to prove any of the allegations against the firm; and
- C. If accepted:
 - 1. this AWC will become part of the firm's permanent disciplinary record and may

be considered in any future actions brought by FINRA or any other regulator against the firm;

2. this AWC will be made available through FINRA's public disclosure program in accordance with FINRA Rule 8313;
 3. FINRA may make a public announcement concerning this agreement and the subject matter thereof in accordance with FINRA Rule 8313; and
 4. The firm may not take any action or make or permit to be made any public statement, including in regulatory filings or otherwise, denying, directly or indirectly, any finding in this AWC or create the impression that the AWC is without factual basis. The firm may not take any position in any proceeding brought by or on behalf of FINRA, or to which FINRA is a party, that is inconsistent with any part of this AWC. Nothing in this provision affects the firm's: (i) testimonial obligations; or (ii) right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party.
- D. The firm may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. The firm understands that it may not deny the charges or make any statement that is inconsistent with the AWC in this Statement. This Statement does not constitute factual or legal findings by FINRA, nor does it reflect the views of FINRA or its staff.

The undersigned, on behalf of the Firm, certifies that a person duly authorized to act on its behalf has read and understands all of the provisions of this AWC and has been given a full opportunity to ask questions about it; that it has agreed to the AWC's provisions voluntarily; and that no offer, threat, inducement, or promise of any kind, other than the terms set forth herein and the prospect of avoiding the issuance of a Complaint, has been made to induce the firm to submit it.

April 15, 2020

Date

Respondent

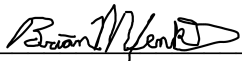
Morgan Stanley & Co. LLC

By:  _____

Name: Michelle Stratton

Title: Managing Director

Reviewed by:

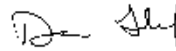


Counsel for Respondent

Accepted by FINRA:

April 17, 2020
Date

Signed on behalf of the
Director of ODA, by delegated authority



Dean A. Floyd
Senior Counsel
Department of Enforcement