

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER, AND CONSENT
NO. 2020067484501**

TO: Department of Enforcement
Financial Industry Regulatory Authority (FINRA)

RE: Morgan Stanley & Co. LLC (Respondent)
Member Firm
CRD No. 8209

Pursuant to FINRA Rule 9216, Respondent Morgan Stanley & Co. LLC 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 Respondent alleging violations based on the same factual findings described in this AWC.

I.

ACCEPTANCE AND CONSENT

- A. Respondent accepts and consents to the following findings by FINRA without admitting or denying them:

BACKGROUND

Morgan Stanley has been a FINRA member since 1970. The firm's principal place of business is New York, New York, and it has offices throughout the country. The firm has more than 4,000 registered personnel, and it provides a full range of financial services to its retail and institutional clients, including publishing research reports.

On August 9, 2010, pursuant to AWC No. 2008013782301, FINRA found that, among other things, the firm published equity research reports that contained inaccurate conflict-of-interest-related disclosures, failed to include required price charts and disclosures regarding the firm's price targets in certain equity research reports, and engaged in related supervisory failures, in violation of NASD Rules 2711 and 2110. The firm consented to a censure, a \$800,000 fine, and undertakings.¹

OVERVIEW

Between August 30, 2019, and February 28, 2020, Morgan Stanley published approximately 11,000 equity research reports that included price charts with inaccurate historical stock ratings. As a result, the firm violated FINRA Rules 2241(c)(3) and 2010.

¹ For more information about the firm, including prior regulatory events, visit BrokerCheck® at www.finra.org/brokercheck.

These errors resulted, in part, from the firm's failure to establish and maintain a supervisory system, including written supervisory procedures (WSPs), reasonably designed to achieve compliance with FINRA Rule 2241(c)(3). As a result, the firm violated FINRA Rules 3110(a) and (b)(1) and 2010.

In addition, between April 7 and May 17, 2021, the firm failed to accurately disclose required beneficial ownership information in 1,616 equity research reports. As a result, the firm violated FINRA Rules 2241(c)(4)(F) and 2010.

FACTS AND VIOLATIVE CONDUCT

This matter originated from a Rule 4530 disclosure by the firm.

1. Morgan Stanley Published Research Reports That Included Inaccurate Historical Stock Ratings.

FINRA Rule 2241(c) sets forth content and disclosure requirements for equity research reports distributed by member firms, including the requirement to disclose, under certain circumstances, historical ratings and a price chart of a subject company's security. When a research report includes a rating or price target for a subject company's security, and the member firm has assigned a rating or price target to the security for at least one year, FINRA Rule 2241(c)(3) requires the research report to include a price chart. Such price chart must include the security's daily closing prices, as well as any ratings or price targets assigned by the member firm (and the dates on which the member firm assigned or changed such ratings or price targets), for the past three years or for the period that the member firm had assigned any ratings or price targets, whichever is shorter.

A violation of FINRA Rule 2241 is also a violation of FINRA Rule 2010, which requires member firms to observe high standards of commercial honor and just and equitable principles of trade in the conduct of their business.

At all relevant times, the firm used a software program to generate price charts that appeared in its research disclosures. The firm revised the software on or around August 30, 2019, to address new European Union regulatory requirements that required the disclosure of five years of information for a recommended security under certain circumstances. The revised software contained a typographical error that caused the price charts in certain research reports to display stock ratings from five years prior to the report, but labeled those ratings, inaccurately, as being from three years prior to the report. For example, if a stock was rated "overweight" five years before a research report's publication date and "equal-weight" three years before the publication date, the software error caused the price chart to incorrectly disclose that the stock was rated "overweight" three years before the publication date, instead of "equal-weight." The software error impacted only the presentation of historical ratings within the price charts.

A firm supervisory analyst identified an inaccurate historical stock rating in a price chart of a research report in January 2020 and escalated the issue. While the firm worked to

resolve the issue, it continued to publish research reports containing inaccurate historical stock ratings until it resolved the issue on February 29, 2020.

As a result of the price-chart software error, between August 30, 2019, and February 28, 2020, the firm published approximately 11,000 research reports that included price charts with inaccurate historical stock ratings. Therefore, the firm violated FINRA Rules 2241(c)(3) and 2010.

2. Morgan Stanley Failed to Establish and Maintain a Supervisory System, Including WSPs, Reasonably Designed to Achieve Compliance with Disclosure Requirements for Historical Stock Ratings.

FINRA Rule 3110(a) requires a member firm 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.

FINRA Rule 3110(b)(1) requires a member firm to establish, maintain, and enforce written procedures to supervise the types of business in which it engages and the activities of its associated persons that are reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable FINRA rules.

A violation of FINRA Rule 3110 is also a violation of FINRA Rule 2010.

As described above, between August 30, 2019, and February 28, 2020, the firm published approximately 11,000 research reports that included price charts with inaccurate historical stock ratings. Although the ratings inaccuracies arose from an error in the price-chart software, they ultimately resulted in inaccurate disclosures in published research reports because the firm had no policy or procedure to enable it to reasonably determine that the historical stock ratings in its research reports, required by FINRA Rule 2241(c)(3), were accurate. Accordingly, the firm failed to establish and maintain a supervisory system, including WSPs, reasonably designed to achieve compliance with the disclosure requirements of FINRA Rule 2241(c)(3). Therefore, the firm violated FINRA Rules 3110(a) and (b)(1) and 2010.

3. Morgan Stanley Failed to Accurately Disclose Required Beneficial Ownership Information in Research Reports.

FINRA Rule 2241(c)(4)(F) requires a member firm to “disclose in any research report at the time of publication or distribution of the report ... if the member or its affiliates beneficially own 1% or more of any class of common equity securities of the subject company[.]”

As stated above, a violation of FINRA Rule 2241 is also a violation of FINRA Rule 2010.

At all relevant times, the firm populated the beneficial ownership disclosures in its research reports using data uploaded to the firm's system through a beneficial ownership data feed. The firm updated the beneficial ownership feed each month with data from the prior month.

On March 1, 2021, the firm completed its acquisition of an investment management company. The investment management company's securities holdings increased the firm's overall holdings of many equity securities and thus changed the beneficial ownership disclosures the firm was required to include in its research reports.

On April 7, 2021, the firm updated its beneficial ownership feed to include the investment management company's securities holdings for the first time (with data from the prior month, March 2021). However, the firm's system rejected the updated feed as potentially erroneous, which resulted in the investment management company's holdings being excluded from the feed used to report the firm's beneficial ownership on research reports. Although the firm's system was designed to notify firm personnel when it rejected a data feed, the system failed to send such notification in this instance due to a software error. Therefore, beginning on April 7, 2021, the firm's system used data that excluded the investment management company's holdings to generate beneficial ownership disclosures for research reports, rather than the updated feed that included such holdings.

The firm identified the issue in May 2021, during its monthly surveillance review of research disclosures, and resolved the issue shortly thereafter.

As a result, between April 7 and May 17, 2021, the firm failed to accurately disclose beneficial ownership information required under FINRA Rule 2241 in 1,616 research reports. Affected reports failed to disclose that the firm or its affiliates held a beneficial ownership stake of 1% or more (thereby underreporting the firm's holdings) or erroneously disclosed a beneficial ownership stake of 1% or more where none existed (thereby overreporting the firm's holdings).

By failing to accurately disclose the beneficial ownership information described above, the firm violated FINRA Rules 2241(c)(4)(F) and 2010.

CREDIT FOR EXTRAORDINARY COOPERATION

In resolving this matter, FINRA has recognized Morgan Stanley's extraordinary cooperation. The firm retained outside counsel to investigate, and correct, the historical stock ratings and beneficial ownership disclosure issues before the issues were detected by any regulator, and the firm self-reported both issues to FINRA. After discovering the issues, the firm promptly took steps to correct them and voluntarily enhanced its supervisory systems and procedures regarding disclosure reviews and disclosure-related software updates. In addition, the firm provided substantial assistance to FINRA in its investigation, including by identifying the causes, scope, and impact of the disclosure errors and omissions, proactively explaining the findings to FINRA staff in multiple

meetings, and providing detailed factual summaries prior to receiving Rule 8210 requests.

B. Respondent also consents to the imposition of the following sanctions:

- a censure and
- a \$325,000 fine.

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

Respondent specifically and voluntarily waives any right to claim an inability to pay, now or at any time after the execution of this AWC, the monetary sanction imposed in this matter.

The sanctions imposed in this AWC shall be effective on a date set by FINRA.

II.

WAIVER OF PROCEDURAL RIGHTS

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

- A. To have a complaint issued specifying the allegations against it;
- 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, Respondent 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 its acceptance or rejection.

Respondent 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.

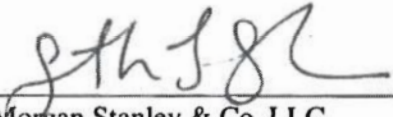
OTHER MATTERS

Respondent 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 Respondent; and
- C. If accepted:
 - 1. this AWC will become part of Respondent's permanent disciplinary record and may be considered in any future action brought by FINRA or any other regulator against Respondent;
 - 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 its subject matter in accordance with FINRA Rule 8313; and
 - 4. Respondent 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. Respondent 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 Respondent's right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party. Nothing in this provision affects Respondent's testimonial obligations in any litigation or other legal proceedings.
- D. Respondent may attach a corrective action statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. Respondent 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.

The undersigned, on behalf of Respondent, certifies that a person duly authorized to act on Respondent's 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 Respondent 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 in this AWC and the prospect of avoiding the issuance of a complaint, has been made to induce Respondent to submit this AWC.

7/18/2022
Date


Morgan Stanley & Co. LLC
Respondent

Print Name: Samantha L. Schreiber

Title: Executive Director, Co-Head US Litigation

Reviewed by:

Nader Salehi /w/o
Nader H. Salehi
Counsel for Respondent
Kirkland & Ellis LLP
1301 Pennsylvania Avenue, N.W.
Washington, D.C. 20004

Accepted by FINRA:

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

8/3/2022
Date


Adam N. Stern
Counsel
FINRA
Department of Enforcement
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Rockville, MD 20850