

Morgan Stanley's Insider-Trading Program: 'Sort of Scary'

By Andrew Singer

In November, Morgan Stanley, the Wall Street investment firm, conducted a live, hour-long webcast on a serious compliance risk for investment firms: insider trading.

"Barred from the Business: Insights on Insider Trading" was the brainchild of Morgan Stanley CEO John J. Mack, who co-hosted the event with Chief Legal Officer Gary Lynch, a top SEC enforcement official in the 1980s.

Broadcast to Morgan Stanley employees after trading hours on November 19th, the program offered more than the usual bells and whistles. It began with news montages of insider trading cases over the years, including those involving Morgan Stanley. It moved to taped interviews with two convicted (insider-trading) felons, and then it presented four insider trading 'scenarios' with professional actors. During the scenario segment, the in-house audience was outfitted with electronic touch pads which they pressed when they believed that a fictional character 'crossed the line' into illegality.

CEO Mack was keenly aware of several well-publicized cases of insider trading—technically speaking, misuses of *material non-public information* (MNPI)—at financial services firms recently, including at Morgan Stanley, explained Jacqueline LiCalzi, Managing Director, Morgan Stanley, Legal and Compliance (New York), in a recent interview.

According to a memorandum the CEO sent to employees in advance of the program, Mack said, "This behavior is contrary to everything we stand for, which is why I asked our Legal and Compliance Department to put together a program that helps everyone at Morgan Stanley understand the proper handling of MNPI and the consequences of misuse."

Driving the message

The two seven-minute taped interviews with convicted felons arguably had the biggest impact on the audience, according to LiCalzi. They "drove the whole message about consequences." (This "scared straight" type of approach was reportedly favored by CEO Mack.)

One interviewee was the former CEO of a boutique investment bank who spent time in prison as a result of leaking inside information about impending bank mergers to his girlfriend.

The other was with a former securities trader who spent 10 months in prison after purchasing securities based on tips received from a former Morgan Stanley employee.

"People don't think they'll get into these situations," comments LiCalzi. They think that they are too smart. "But here was a smart, successful guy [the investment banker] who ended up in the wrong place." He eventually found his picture and story on the cover of a major New York City newspaper.

Former SEC enforcement chief Lynch told the audience in so many words that 'Things have changed—but not that much. There are still people doing bad things.'

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The convicted felons were paid a nominal fee to appear, she says, adding that it takes some work to edit an hour interview down to seven minutes.

The core idea is that “You may think that it can’t happen to you,” that you won’t get into a situation where you’ll divulge material, non-public information, she says. “But it can happen, even inadvertently.”

The program begins with CEO Mack, who after some opening remarks introduced Gary Lynch, former chief of the Enforcement Division of the Securities & Exchange Commission, who in the 1980s brought cases, and obtained settlements, against Dennis Levine, Ivan Boesky and Michael Milken, among others. Lynch told the Morgan Stanley audience in so many words that “Things have changed—but not that much. There are still people doing bad things.”

With regard to insider trading, Lynch told the audience: Don’t even think about getting away with it. They will find you.

The taped interviews with the two convicted felons were followed by the case studies in which professional actors presented four scenarios. Each covered a situation that could arise in one of the firm’s four major business lines. A retail brokerage employee might inadvertently tip off people regarding MNPI, including friends, family members and colleagues.

Audience members were asked to vote on ethical aspects of the case studies using electronic touch pads when they thought an employee in a scenario had crossed the line with regard to the misuse of material, non-public information. The discussion was led by Steve Priest of the Ethical Leadership Group.

Mandatory viewing for new hires

Attendance at the live webcast was voluntary. Why not mandatory? When it comes to insider trading, the firm already does a lot of mandatory training, LiCalzi told us. They didn’t want to chase people down to watch the program which had the endorsement and push of senior management which in itself would spark some interest, it

An interview with a former investment banker who spent time in prison as a result of leaking inside information to his girlfriend was a highlight of the program.

was thought.

The webcast was filmed and later edited. A recut version—with the “ahs,” and “ohs” eliminated, and subtitles added for places like China and Japan—was distributed in early 2008 to employees in Europe and Asia. LiCalzi estimates that at least half of Morgan Stanley’s 40,000 employees have viewed the program—perhaps as many as 32,000.

When the filmed version is presented overseas, attendance is often mandatory. Typically the program is introduced by the business-line head e.g., the head of retail brokerage introduces it to retail brokers, and so on. The filmed version is now mandatory viewing for new Morgan Stanley hires.

There have been changes at the firm in recent years. New people have come on board, and many are unfamiliar with the corporate ‘culture,’ notes LiCalzi, another reason they put some effort into this project.

Employees learn from this, among other things, “Don’t cross into a gray area,” says LiCalzi. If there are any questions about right and proper conduct, “Raise your hand” and ask questions.

Asked about the overall response to the program, LiCalzi answered, “People were impressed with it,” adding that the interviews with the two convicted felons were seen “as very impactful” in the audience’s mind. The overall viewers’ verdict: “It was interesting and engaging—but also sort of scary.” □

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