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C O U N S E L O R S A T L A W

How to Manage the SEC's New Recordkeeping Rules

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Overview of the Rule Changes

- Three Types of Rule Amendments
 - Sales Practices
 - Local Office
 - Federalize SRO Rules
- Three Main Areas of Change
 - Customer Account Information - Suitability
 - Records re: Associated Persons
 - Records to be kept at Local Offices
- Changes went effective May 2, 2003

Account Record for Account Owners

- Customer's Name
- Tax Id Number
- Address
- Telephone Number
- Date of Birth
- Association with Broker-Dealer
- Employment Info
- Annual Income
- Net Worth (excluding value of primary residence)
- Investment Objectives for Account
- Joint Accounts
 - Personal information for each customer
 - Joint financial information

Delivery of Account Records

- Effective May 2, 2003 Customer Information must be confirmed within 30 days of:
 - Opening of a New Account
 - Changes of Account Investment Objectives
 - Change of Name or Address
- For Accounts already open on May 1, 2003, must send account record to customer by May 1, 2006

Prominent Statements

- “The customer or owner should mark any corrections and return the account record or alternate document to the broker-dealer.”
- “The customer or owner should notify the broker-dealer of any future changes to information contained in the account record.”

Account Record Delivery

- Broker-Dealer is required to make a good faith effort to obtain the required information
- Keep record that attempt was made
- If any material information is missing, the Broker-Dealer has the burden of explaining why information is unavailable

Exemptions from Account Record Requirement

- Broker-dealers are not required to create an account record for an account if the firm is not required (under federal or SRO rules) to make a suitability determination
- Broker-dealers are not required to create account records except where the account owner is a natural person
 - Required
 - 401(k)s & IRAs
 - UTMAs, UGMAs
 - Not required
 - Corporations
 - Partnerships
 - Most Trusts

Associated Person Records

- **Must keep**
 - Current listing of all associated persons
 - Current listing of every office where each associated person regularly conducts business
 - Listing of all internal identification numbers
 - CRD number for each associated person
 - Record of all compensation - Cash & non-cash
 - All agreements between associated persons and firm, including oral agreements
 - If compensation is not calculated on a per trade basis, records describing method of compensation

Customer Complaints

- Record as to each associated person received by broker-dealer including complainant's name, address, account number, and date received.
 - Must record any other Associated Person named in complaint, a description of complaint and its disposition
- Simply keep a copy of the original complaint by Associated Person
- Record that each customer provided with address and telephone number to which complaints should be sent

Brokerage Order and Transaction Tickets

- Identify associated person responsible for the account
- Identify person accepting order
- Identify person entering order
- Whether or not discretionary
- Time order accepted
- If entered by customer electronically, a notation to that effect and, if feasible, time of execution or cancellation
- “Time of receipt”

Miscellaneous Amendments

- Communications with the Public
 - Make a record that firm is complying with existing applicable requirements
 - Retain all written communications including Written Sales Scripts
- Firm Organizational Documents
- Special Reports (e.g. Regulatory Inquiries)
- Compliance Manuals

Miscellaneous Amendments

- Record listing principals responsible for establishing compliance procedures
 - “Principal” defined as any individual registered with an SRO as a principal or branch manager, or any other person delegated supervisory responsibility for the firm or its associated persons
- Designate Individual to explain records & their content
 - By Name or Title

Definition of Office

- “Office” -- Any location where an associated person regularly conducts business, including home offices
 - Residences used as office -- Broker-dealer not required to produce records at residence if
 - Only family members conduct business from that location
 - Office not held out to public
 - No funds or securities handled
 - Records held at another location within same state

Definition of Office

- Multiple Locations -- (e.g., bank “circuit riders”)
 - Okay to treat all locations as single office
 - Must select one location as “the office”
 - No requirement to notify securities regulators which location selected

Records Kept At Each Office

- Rule 17a-3(f) requires firms to make and keep current, as to each office, the following books and records
 - Blotters (a)(1)
 - Brokerage orders (a)(6)
 - Principal Transactions (a)(7)
 - Associated persons (a)(12)
 - Account record (a)(17)

Records Kept At Each Office

- Customer complaints by representative (a)(18)
- Associated person compensation records (a)(19)
- Advertisements and sales literature compliance records (a)(20)
- Identity of record explainer (a)(21)
- Principals responsible for establishing policies and procedures (a)(22)
- If a broker-dealer does not maintain records at an office, but chooses to produce records on request, it must produce the records “promptly”

Electronic Recordkeeping

- Records must be preserved in a non-rewriteable, non-erasable format
- Brokers may use systems that prevent rewriting or erasing only for designated period, but permit rewriting or erasing after that period
- Brokers may not use systems that merely note changes
- If records are required to be kept for periods longer than SEC rules require, brokers must ensure records are not deleted even after SEC required period has ended
- System must include auditing features providing accountability regarding the inputting of records