

STATE OF ALASKA  
DEPARTMENT OF COMMUNITY AND ECONOMIC DEVELOPMENT  
DIVISION OF BANKING, SECURITIES, AND CORPORATIONS  
P.O. BOX 110807  
JUNEAU, ALASKA 99811-0807

In the Matter of )  
J. P. Morgan Securities Inc., ) Alaska Order 04-03 S  
Respondent. )  
270 Park Avenue )  
New York, NY 10017 )  
CONSENT ORDER

WHEREAS, J. P. Morgan Securities Inc. ("JPMSI") is a broker-dealer registered in the State of Alaska; and

WHEREAS, coordinated investigations into J. P. Morgan Securities Inc.'s activities in connection with certain of its equity research practices during the period of approximately July 1999 through June 2001 have been conducted by a multi-state task force and a joint task force of the U.S. Securities and Exchange Commission, the New York Stock Exchange ("NYSE"), and the NASD, Inc. ("NASD") (collectively, the "regulators"); and

WHEREAS, J. P. Morgan Securities Inc. has cooperated with regulators conducting the investigations by responding to inquiries, providing documentary evidence and other materials, and providing regulators with access to facts relating to the investigations; and

WHEREAS, J. P. Morgan Securities Inc. has advised regulators of its agreement to resolve the investigations relating to its research practices; and

WHEREAS, J. P. Morgan Securities Inc. agrees to implement certain changes with respect to its research practices, and to make certain payments; and

WHEREAS, J. P. Morgan Securities Inc. elects to permanently waive any right to a hearing and appeal under the Alaska Securities Act (the "Act") with respect to this Administrative Consent Order (the "Order");

NOW, THEREFORE, the Alaska division of banking, securities, and corporations (the "Division"), as administrator of the Act, hereby enters this Order:

**FINDINGS OF FACT**

**A. Background**

1. This action concerns the period of July 1, 1999 to June 30, 2001 (the "relevant period"). During that time, several JPMSI predecessor entities engaged in both research and investment banking ("IB") activities.

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- 1     1.    Research analysts were responsible for providing analyses of the financial outlook  
2       of particular companies in the context of the business sectors in which those  
3       companies operated and the securities market as a whole.
- 4     2.    Research analysts evaluated companies by, among other things, examining  
5       financial and other information contained in public filings; questioning company  
6       management; investigating customer and supplier relationships; evaluating  
7       companies' business plans and the products or services offered; building financial  
8       models; and analyzing competitive trends.
- 9     3.    After synthesizing and analyzing this information, research analysts drafted  
10       research reports and more abbreviated "notes" that typically contained a  
11       recommendation, a price target, and a summary and analysis of the factors upon  
12       which the analyst relied in issuing the price target and recommendation.
- 13    4.    The Firm published research on publicly traded companies, and this research was  
14       distributed to the Firm's institutional and private equity customers. Published  
15       research was made available through mailing lists, the Firm's website, and  
16       subscription services provided by First Call. In addition, the research was made  
17       available to some retail customers of another broker dealer and offered via  
18       websites offering brokerage and investment services.
- 19    5.    In addition to performing these research functions, certain research analysts  
20       participated in IB activities.
- 21    6.    These IB activities included identifying and/or vetting companies as prospects for  
22       IB services, participating in pitches of IB services to companies, participating in  
23       "roadshows" associated with underwriting transactions, and speaking to investors  
24       to generate interest in underwriting transactions.<sup>1</sup>
- 25    7.    These IB activities also included participating in commitment committee and due  
      diligence activities in connection with underwriting transactions and assisting the  
      IB Department in providing merger and acquisition ("M&A") and other advisory  
      services to companies.<sup>2</sup>
8.    The Firm encouraged all research analysts to support its businesses, including the  
      Firm's IB business, and in some cases, research analysts were expected to  
      participate in the foregoing IB activities. The level of analyst participation in these  
      IB activities was sometimes significant.
9.    For example, in an e-mail dated May 23, 2000, and sent by a research analyst to  
      the Head of Research at RESPONDENT JPMSI, the analyst requested approval  
      to hire another junior analyst. The analyst stated: **"I'd like to get yet another**

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<sup>1</sup> A "roadshow" is a series of presentations made to potential investors in conjunction with the marketing of an upcoming underwriting.

<sup>2</sup> The "commitment committee" was responsible for, among other things, evaluating and then either approving or rejecting the Firm's participation in initial public offerings ("IPOs") and other IB transactions.

1           **junior....**The deals are really dragging me down, and I'm not spending nearly  
2           enough time with buy-side clients. Even though the market is crap, we continue to  
3           process deals in hopes of market recovery....I am trying to remove myself from the  
4           day-to-day production of research. I actually like doing it, but it's not what you pay  
5           me for." (Emphasis in the original.)

- 6
- 7           10. IB business was an important source of revenue for the Firm. In 2000, the  
8           combined operating revenues for JPM and Chase totaled \$32.793 billion, and the  
9           combined revenues for the Equity Capital Markets ("ECM") and the M&A  
10           Departments at JPM and Chase totaled \$1.687 billion.

11

12           **D. Participation in Investment Banking Activities Was a Factor in Evaluating and**  
13           **Compensating Research Analysts**

- 14
- 15           1. The compensation system at the Firm provided an incentive for research analysts  
16           to participate in IB activities and to assist in generating IB business for the Firm.
- 17           2. The performance of research analysts was evaluated by the Head of Research  
18           through an annual review process and, where not set by contract in advance, the  
19           research analyst's bonus was determined through this process.
- 20           3. The Head of Research evaluated the research analysts' job performance through  
21           responses to self-evaluation forms; surveys of the sales force; input from the IB,  
22           Sales, and Trading departments; consideration of market factors and rankings by  
23           investor publications; and, in some cases, written "team reviews" submitted by  
24           individual investment bankers.
- 25           4. The self-evaluation forms contained questions on areas constituting the major  
              allocations of research analysts' time, including questions relating to participation  
              in IB activities.
5. In response to questions relating to participation in IB activities, research analysts  
              reported one or more of the following: their IB activities, accomplishments, and  
              goals; their participation in lead- and co-managed underwritings; and the fees  
              associated with IB transactions on which the analyst worked.
6. For example, the "Investment Banking Activities" section of a 1999 self-evaluation  
              form queried: "In what way have you assisted in discovering or executing banking  
              transactions (i.e., due diligence sessions, pitches)? Be specific." In response, a  
              research analyst stated: "Helped put together and develop pitch books for KV  
              Pharma and King Pharmaceuticals;" "Helping to come up with creative ideas and  
              contributing to brainstorming sessions with bankers – ad hoc and in biweekly  
              Monday meetings;" "Have a good handle on which companies will need financing  
              in the near future and stepping up research efforts to ensure a place for H&Q on  
              the cover;" and "Increasing responsibility in the office allows [another research  
              analyst] to travel and be more active in pitching and winning deals with new  
              companies."

- 1 7. In another example, a research analyst stated the following in response to IB  
2 questions contained in his year 2000 self-evaluation form: "Completed 21  
3 investment banking deals, including 11 lead-managed deals....Biotechnology new  
4 issues have generated \$70 million in primary fees in fiscal year 2000 YTD. In  
5 2000 we were ranked #1 in healthcare common equity offerings by U.S. Issuers,  
6 raising \$3.9 billion and capturing 21.9% market share." In addition, the analyst  
7 listed all deals on which he worked that were "Lead Managed," "Co-managed,"  
8 "Pitched," and "Pending."
- 9 8. The self-evaluation forms conveyed to research analysts some of the criteria used  
10 to evaluate their performance. As reflected in the IB questions contained in the  
11 forms, contribution to the Firm's IB business was an important part of the analyst's  
12 job.
- 13 9. In some circumstances, research analysts requested that individual investment  
14 bankers complete a written "team review" of the analyst, which was then submitted  
15 to the Head of Research. In these reviews, the investment banker described his  
16 or her contact with the analyst and the analyst's participation in IB activities,  
17 including pitch and underwriting activities.
- 18 10. For example, in a 1999 review of a research analyst by an investment banker, the  
19 banker stated the following: "I have worked extensively with [this research analyst]  
20 over the past year. I probably speak to her everyday [sic] on topics ranging from  
21 executing live transactions, evaluating potential business opportunities, drafting  
22 'pitch' presentations, coordinating scheduling and marketing efforts across IB, and  
23 strategizing about the Internet practice....I consider [her] to be a partner in our  
24 building of the firm's Internet franchise and, as a result, probably work more  
25 closely with her than anyone in IB."
11. Research analysts sometimes provided reviews of investment bankers in  
conjunction with the banker's performance review. In these reviews, analysts  
described their contact with the banker and referenced participation in specific IB  
activities.
12. For example, in an e-mail dated Dec. 14, 2000, a research analyst provided a  
review of an investment banker. The analyst stated: "I've probably had more  
opportunity to work with [this investment banker] and observe him in action than  
anybody else in the bank....[The banker and I] have been in sync about where the  
quality banking prospects are so that I don't have to fend off garbage banking  
deals.... • **Built semiconductor banking practice from nothing:**....[The banker  
and I] have built a profitable semiconductor banking practice, starting from literally  
zero four years ago....In 1999, we posted a couple of successes....With a touch  
more luck, we could have doubled the revenue potential this year....We are still  
banking the semiconductor sector pretty much the way we did three years ago,  
which means going after a dozen or so key prospects (split evenly between  
existing public companies and quality IPO candidates) and then doing everything  
else opportunistically rather than strategically....The message here is that we have  
not developed the semiconductor banking machine that our strongest dozen

1 competitors have, and that makes it hard to gain market share." (Emphasis in the  
2 original.)

3 13. Based upon comments in the self-evaluations completed by research analysts and  
4 the reviews completed by both analysts and investment bankers, the two groups  
5 worked closely on IB transactions and shared a common goal of building the  
6 Firm's IB business.

7 14. The Head of Research reviewed the self-evaluations and team reviews and  
8 provided a verbal and/or written evaluation of the research analyst. The written  
9 evaluations provided feedback on the analyst's performance during the year and in  
10 certain cases highlighted the analyst's participation in IB activities, including the  
11 revenues generated by IB transactions on which the analyst worked.

12 15. For example, the Head of Research at RESPONDENT JPMSI stated the following  
13 in the first paragraph of his year 2000 evaluation of a research analyst: "By every  
14 measure, [the research analyst] had an outstanding year in 2000. Most  
15 importantly, [he] led the charge in establishing J.P. Morgan as the #1 biotech shop  
16 with a resounding 21.9% share of the underwriting wallet in his sector. [He]  
17 supported 21 transactions this year, 11 of which were as the lead underwriter.  
18 The revenue attributable to these transactions is over \$70 mm." Later in the  
19 evaluation, the Head of Research stated that the analyst's contribution to the  
20 Firm's "corporate underwriting business" was "enormous."

21 16. Comments by the Head of Research conveyed to research analysts the  
22 performance areas that were important to research management and the Firm.  
23 Based upon these comments, certain analysts were encouraged to participate in  
24 IB activities, increase IB revenues, and enhance the reputation of the Firm's IB  
25 franchise.

17. Research analyst bonuses were determined by the Head of Research in his  
discretion after considering several factors that contributed to the analyst's market  
value.

18. The research analyst's contribution to and impact on the Firm's IB business, and  
the fees generated by IB transactions on which the analyst worked, were some of  
the factors used to determine the analyst's bonus. If the analyst did not disclose in  
the self- evaluation form the fees generated by the IB transactions on which he or  
she worked, the Head of Research requested this information from the ECM  
Department at the Firm.

#### **E. Investment Banking Interests Influenced the Firm's Decision to Initiate and Maintain Research Coverage**

1. In general, the Firm determined whether to initiate and maintain research  
coverage based upon institutional investors' interest in the company and/or based  
upon IB considerations, such as attracting companies to generate IB business or  
maintaining a positive relationship with existing IB clients.

- 1 2. Regarding companies for which the Firm lead- or co-managed an underwriting  
2 transaction, research coverage was typically initiated and maintained for a period  
of time beyond the transaction.
- 3 3. The Head of Research was responsible for approval of the determination to issue,  
4 maintain, and drop research coverage. The Head of Research solicited input from  
5 other departments, including the IB Department, to determine the coverage  
preferences of those departments. IB considerations sometimes played a role in  
the decision to initiate and maintain research coverage.
- 6 4. For example, after the merger of JPM and Chase, the Director of U.S. Equity  
7 Research at RESPONDENT JPMSI sent an e-mail entitled: "U.S. Equity  
8 Research Organizational Announcement." Attached was an internal memorandum  
9 "outlining Investment Banking Coordination Responsibilities," which stated: "One  
of the important duties of the Director of Research is to work closely with  
Investment Banking to ensure that research resources are appropriately aligned  
with identified investment banking opportunities."
- 10 5. In addition, the Head of Research requested that research analysts obtain from  
11 investment bankers lists of companies that the bankers wanted under coverage.
- 12 6. For example, an e-mail dated November 4, 1999, from the Head of Research to all  
13 equity research analysts, stated: "[T]alk to your counterparts in IB and prepare a  
list of the companies that they would like you to cover....Please be sure to have a  
conversation with the appropriate bankers before you submit your list."
- 14 7. Some research analysts and investment bankers actively coordinated the initiation  
15 and maintenance of research coverage based upon, among other things, IB  
16 considerations. This coordination consisted of meetings and communications by  
telephone and e-mail.
- 17 8. For example, a research analyst sent an e-mail, dated March 9, 2001, to the  
18 Director of U.S. Equity Research at RESPONDENT JPMSI which stated:  
19 "[Another research analyst] and I have prioritized the coverage area in  
20 coordination with banking, and we are moving to a more **targeted** (no pun  
21 intended) investor marketing plan which leverages our combined coverage....We  
22 are clearly focused on building both the brokerage and banking businesses....We  
23 are actively discussing trimming a couple of the less relevant of these companies  
24 and replacing them with larger market capitalization firms which we can bank....In  
25 total, I would look to us to initiate on **two** non-deal related stocks this year, keeping  
the total names under coverage around the current level. In addition to two non-  
deal initiations, we have mapped out the year and have planned original theme  
pieces and other value-added activities for investors including non-deal related  
road shows....**Banking:** We already did KPMG, for which I believe we were paid  
**\$12.5M**. And we have been mandated as a senior co-manager on Accenture,  
another large transaction. Beyond these, a likely opportunity later in the year is  
**Technology Partners International**, an outsourcing consultant. We are well  
positioned to lead this company's IPO....[An investment banker] leads the  
coordinated banking effort covering the sector, and we are working closely with

1 [him] and the other coverage bankers to bank existing companies and to identify  
2 quality early stage firms." (Emphasis in the original.)

3 9. In another example, an investment banker sent an e-mail, dated May 17, 2001, to  
4 a group of biotechnology analysts and bankers to arrange a meeting to discuss  
5 "coverage strategy." The e-mail stated: "On the heels of [a research analyst and  
6 a banker] leaving, we probably need to discuss coverage strategy. Also would be  
7 a good time to talk about where we might shake loose some business...M&A  
8 ideas to pitch, IPOs coming in next wave etc."

9 10. In another example, a research analyst sent an e-mail, dated March 1, 2001, to  
10 biotechnology analysts and the Head of U.S. Equity Research that contained the  
11 following subject line: "bankers wish list for biotech research." The e-mail stated:  
12 Attached is the culmination of the survey of bankers – as a reminder, I asked them  
13 for 3 groups of names....1. Companies we 'owe' research to since they paid us in  
14 2000 and are not covered by research today. Most of these are from analysts who  
15 have left (on the H&Q side) and we haven't even had research take a formal look  
16 at some of these, which is obviously the first step for deciding on what to do. 2.  
17 Public companies where bankers have a good relationship and think we can get  
18 banking business if research is on board. The goal here is to have research  
19 evaluate the story as soon as possible, so we can either go full bore on getting the  
20 business, or re-assign bankers elsewhere if research is negative. 3. Private  
21 companies that are focus names—we'll commit to have research spend time with  
22 these companies as much as possible before the IPO to put us in the best position  
23 possible to win the books. Also, research is going to add their own names if some  
24 of their favorites were not mentioned by any of the bankers."

25 11. The following e-mails reflect the IB influences in the initiation and maintenance of  
research coverage as perceived by an individual research analyst.

12. In an e-mail dated November 2, 2000, a research analyst provided a team review  
of an investment banker that stated the following: "I have worked with [the banker]  
on the International Rectifier (IRF) account since around mid-1998...and he  
lobbied me very actively to pick up coverage so that JPM could go after the  
banking business, especially equities but also potentially debt, M&A, etc. My  
attitude initially was that IRF is a low-grade semiconductor company that would be  
hard to sell to buy-side clients, but [he] kept pushing the banking  
potential....Finally, I picked up coverage in December 1998.... Then, IRF threw  
sand in our eyes by giving the lead to Morgan Stanley....We picked up coverage  
when they needed us most at the bottom of the semiconductor cycle and  
supported the stock enormously. When the plum banking assignment came up  
that would pay us back for our support, IRF handed the deal to MS, which had  
zero history with the company."

13. In an e-mail dated August 8, 2000, the same research analyst stated: "Given how  
thoroughly we just got screwed on IRF, [the Head of Research of RESPONDENT  
JPMSI] is not interested in hearing stories about how if we initiate coverage, then  
we will be considered for banking business. He wants to hear that the banking  
business is locked up. We've been screwed too many times...[O]ur not covering

1 IFX [Infineon Technologies] is a direct result of being offered money-losing table  
2 scraps in the IPO....I guess I'm still in the same old place. Initiating coverage of  
3 IFX some time in the next six months is no problem, especially as [a research  
4 analyst] is going to have to cover it eventually anyway. It doesn't make sense to  
5 have a European semiconductor analyst that does not cover Infineon." (Emphasis  
6 in the original.)

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8 14. In addition, consideration of "investment banking sensitivities" was included in a  
9 discussion of the Firm's "Long Term Buy" ("LTB") research rating.

10 15. An e-mail dated December 29, 2000, which was sent to all Chase H&Q research  
11 analysts, including the Head of Research at Chase H&Q, described the stock  
12 rating system to be used after the merger of JPM and Chase.

13 16. The e-mail's subject line stated: "Public dissemination of coverage and Re-Rating  
14 your stocks—IMPORTANT\*\*\*\*." The e-mail stated: **The guidelines for  
15 determining the rating are below.... Long-Term Buy: 0-10% outperformance  
16 of the relevant benchmark target within a twelve to eighteen month time  
17 frame. Shorter-term catalysts to explain the 'longer-term' nature of the  
18 recommendation, or in certain circumstances investment banking  
19 sensitivities, are appropriate for this designation.** (Emphasis in the original.)

#### 20 **F. The Firm Provided Certain Companies With an Informal "Warranty" of Research 21 Coverage in Conjunction With Investment Banking Transactions**

22 1. The Firm typically initiated research coverage on companies that engaged the  
23 Firm in an IB transaction.

24 2. H&Q and Chase H&Q had an informal policy of providing certain companies with a  
25 "warranty" of research coverage in conjunction with IB transactions.

1 3. For example, in an e-mail dated November 22, 2000, and sent by the Head of  
2 eBusiness at Chase H&Q to the Head of Research at Chase H&Q and others, the  
3 Head of eBusiness stated the following: "I think that it is important to guaranty [sic]  
4 some level of consistent coverage for our fee paying IB clients. In terms of a  
5 'warranty period,' I think that a period of 18 months would be a fair and appropriate  
6 coverage period, as well as a reasonable timeframe for a company to show  
7 progress and perhaps 'earn' an extension of coverage. During this transition  
8 period...we could offer more of a general, maintenance-only, 'no name' research  
9 coverage...[that] could be done by a 'team' of junior associates from both the IB  
10 and research side of the house as part of the 'pod' approach to a sector. This  
11 coverage would allow the pod to continue to maintain a relationship with the  
12 company, generating additional income from the account."

13 4. The Firm verbally promoted this warranty research coverage in conjunction with  
14 pitches of IB business to companies, and research coverage would be maintained  
15 on certain companies subject to the warranty.

- 1 5. For example, in an e-mail dated October 20, 1999, an investment banker sent an  
2 e-mail to senior executives at H&Q that contained the following subject line:  
3 "Follow Up on a Pitch Please." The e-mail stated: [Head of IB:] Please call...[the]  
4 Chairman of CCC Info. Services....Script: You know that [a team of investment  
5 bankers] presented to the board yesterday and that we are very excited about the  
6 prospect of serving as agent for a private round with financial and strategic parties  
7 and as lead manager on their IPO in early 00....Our pitch is...4. Best aftermarket  
8 'warranty.'"
6. Also, in an e-mail dated December 19, 2000, from an investment banker to a  
member of the board of directors of Epicor Software Corporation ("Epicor"), the  
banker stated: "Just a heads up that the extended warranty provided for Epicor is  
running out." In an e-mail dated December 22, 2000, the board member replied:  
"not a surprise. thanks for sticking to the deal."

### 9 **G. The Firm's Pitch Materials Contained Discussions of Research Coverage**

- 10 1. During the relevant period, companies considered research coverage to be an  
important factor in selecting a firm for an underwriting transaction.
- 11 2. In certain pitch materials, the Research Department, and research analysts in  
12 particular, were described to implicitly suggest that the Firm would provide  
13 favorable research coverage after the IB transaction.<sup>3</sup> The research analyst's  
14 reputation and industry ranking, statistics regarding the percentage of lead- and  
15 co-managed IPOs currently under coverage, and the Firm's "aftermarket support"  
16 were promoted in pitch materials. In addition, the Firm utilized "case studies" of  
companies under coverage that included charts comparing the dates of positive  
published research to the company's stock price. The case studies showed the  
stock price increases following the analyst's positive recommendation and/or  
placement on the analyst's or the Firm's "Focus Lists."
- 17 3. For example, in an e-mail dated February 23, 2000, an investment banker  
18 forwarded pitch materials to an employee of Participate.com to persuade the  
19 company to employ the Firm as an underwriter for an upcoming IPO and private  
20 offering. The pitch materials identified the research analyst who would cover the  
company after the IB transaction. In pages captioned "[Research analyst's name]:  
Authoritative Voice in the Marketplace," "case studies" were presented on the  
analyst's past coverage of two companies: Wireless Facilities and AppNet.
- 21 4. The case studies contained charts that showed the stock price increases following  
22 placement of the stocks on the analyst's and Firm's focus lists. The "Wireless  
23 Facilities Case Study" stated the following: "Chase H&Q adds WFI to Focus List:  
24 WFI gains 11.7% (1/27/00)." The "AppNet Case Study" stated the following:  
"Chase H&Q adds AppNet to Focus List: AppNet gains 7.5% (8/2/99)...While on  
[the research analyst's] Focus List, AppNet appreciates 309% (8/2/99-10/26/99)."

25 <sup>3</sup> "Pitch materials" are the written materials provided to the management of an issuer in conjunction with the Firm's pitch or presentation of its strengths and capabilities in conducting an upcoming IPO or other IB transaction.

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5. Also presented were excerpts of positive commentary by the research analyst that accompanied the Buy ratings and/or placement on the focus lists.

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#### **H. Research Analysts Were Visible on Stocks to Generate Investment Banking Business**

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1. Research analysts were encouraged to increase their visibility, or level of communication, on certain stocks to generate IB business.
  2. Lists of stocks were distributed to various departments at the Firm, including the Research Department.
  3. The "ECM [Equity Capital Markets] target list" contained stocks of companies from which the Firm was seeking IB business during the next eighteen (18) months.
  4. The "trading focus list" contained stocks of companies from which the Firm was seeking IB or underwriting business during the next three months.
  5. The Research Department and other departments were at times encouraged to increase the trading volume of the stocks on the lists for IB purposes.
  6. The following e-mail, dated May 11, 2001, and sent from an investment banker to individuals on the "IB Ebusiness" distribution list, explains the rationale for the two lists: "The criteria for being on the [ECM target] list is...potential equity business over the next 18 months where we would like to target the resources of the firm to win the books....Our objective is to make sure we are being as proactive as possible from an equity perspective, and focusing the equity resources of the firm on these targets to help you win the books for these transactions....The criteria for being placed on the trading focus list is an investment banking event with [sic] the NEXT THREE MONTHS....This investment banking list could be an m&a event or an equity event....In cases where the investment banking event will occur far in advance, our first approach is to work with the traders, analysts and sales traders to increase our trading activity naturally, before we start spending the firm's capital." (Emphasis in the original.)
  7. Trading rank was important to a company's choice of a firm for IB transactions, and the Firm's trading rank was often promoted in pitch materials provided to potential IB clients.
  8. For example, pitch materials provided in conjunction with the AppNet IPO contained a section entitled, "Commitment to Corporate Clients Delivers Institutional Credibility and Trading Strength." There, H&Q's Autex trading rank is identified as "#1," "#2," "#3," and "#4" in the stocks of specific companies that engaged H&Q for an IPO.
  9. Certain research analysts were encouraged to increase their visibility, or level of communication, on stocks contained in the lists.

- 1 10. For example, in an e-mail dated September 27, 2000, from an investment banker,  
2 to a research analyst and others, the banker forwarded September's focus list and  
3 stated: "The list is okay but we are falling way short on a few names. Vicinity we  
4 are not AT [sic] the goal, we are below the goal for the past two months. This is a  
5 problem. On Intertrust and Mypoints, we are not even close to our targets. Less  
6 critical, but we need to do a better job. Concord EFS paid us \$5 MM last year and  
7 we are the #18 trader of that stock. Also disappointing...[Y]ou [research analyst]  
8 need to get more visible on these names with the salespeople so that trading  
9 doesn't have that excuse to hide behind."

#### 6 I. Payments for Research

- 7 1. During the relevant period, H&Q and Chase H&Q made seven payments totaling  
8 \$1,312,500 for research issued in conjunction with five underwriting transactions in  
9 which the Firm was a lead- or co-manager.
- 10 2. H&Q and Chase H&Q made these payments for research without disclosing or  
11 ensuring their disclosure in offering documents or elsewhere.

#### 11 J. The Firm Failed to Adequately Supervise Its Research and Investment Banking 12 Departments

- 13 1. While the role of research analysts was to produce objective research, the Firm  
14 also encouraged them to participate in IB activities.
- 15 2. In addition, the Research and IB Departments had a formal connection within the  
16 Firm's organizational structure. From February to December 2000 at  
17 RESPONDENT JPMSI, the Head of Research had a dual reporting line to both the  
18 Head of Equities and the Head of Investment Banking.
- 19 3. Also, in 2000 at Chase H&Q, research analysts were organized and placed into  
20 "Analyst Sub-pods" for purposes of managing and monitoring their IB activities.  
21 Research analysts reported to "Sub-pod Managers," who were investment bankers  
22 and were responsible for the day-to-day coordination of the research analysts' IB  
23 activities.
- 24 4. The Analyst Sub-pod system for Chase H&Q "Internet Research and Banking" is  
25 explained in a May 2000 Chase H&Q interoffice memorandum which contained a  
"coordination chart." In the chart, the Analyst Sub-pods had a direct reporting line  
to the Sub-pod Managers. The memorandum stated the following: "The 'Analyst  
Sub-pod' is the organizational engine for all that we do." Sub-pod Managers, who  
were investment bankers, were responsible for the "pipeline management  
and...the day-to-day coordination of the particular analyst as it relates to  
investment banking activity....The Sub-pod Manager is not responsible for  
executing all of that particular analyst's transactions, but is responsible for  
ensuring that appropriate resources are allocated. As such, the Sub-pod Manager  
should expect to spend a majority of his time banking the Sub-pod Analyst with the  
balance of his time spent banking other analysts as the demands of the business  
require it." (Emphasis in the original.)

1 5. The Analyst Sub-pod system was created to provide "enhanced coordination  
2 between Banking and Research."

3 6. As a result of the foregoing, research analysts were subject to IB influences and  
4 conflicts of interest between supporting the Firm's IB business and publishing  
5 objective research. The Firm had knowledge of these IB influences and conflicts  
6 of interest yet failed to manage them adequately to protect the objectivity of  
7 published research.

8 7. The Firm failed to establish and maintain adequate policies, systems, and  
9 procedures reasonably designed to ensure the objectivity of its published  
10 research. Although the Firm had some policies governing research analysts'  
11 activities during the relevant period, these policies were inadequate and did not  
12 address the IB influences and conflicts of interest that existed.

### 13 CONCLUSIONS OF LAW

14 1. The Division has jurisdiction over this matter pursuant to The Alaska Securities Act.

15 2. The Division finds that Respondent JPMSI failed to establish and enforce written  
16 supervisory procedures reasonably designed to ensure that analysts were not unduly  
17 influenced by investment banking concerns in violation of AS 45.55.060(a)(7) and (b)(1).

18 3. The Division finds that Respondent JPMSI engaged in acts and practices that  
19 created or maintained inappropriate influence by the IB Department over research analysts,  
20 therefore imposing conflicts of interest on its research analysts, and failing to manage these  
21 conflicts in an adequate or appropriate manner, constituted violations of AS 45.55.060(a)(7)  
22 and (b)(1).

23 4. The Division finds that Respondent JPMSI made payments for research to other  
24 broker-dealers not involved in an underwriting transaction when the Firm knew that these  
25 payments were made, at least in part, for research coverage, and by failing to disclose or  
cause to be disclosed in offering documents or elsewhere the fact of such payments  
constituted a violation of AS 45.55.060(a)(7) and (b)(1).

5. The Division finds the following relief appropriate and in the public interest.

### ORDER

On the basis of the Findings of Fact, Conclusions of Law, and JPMSI's consent to the  
entry of this Order, for the sole purpose of settling this matter, prior to a hearing and without  
admitting the Findings of Facts or Conclusions of Law

IT IS HEREBY ORDERED:

1. This Order concludes the investigation by the Division and any other action that the  
Division could commence under applicable Alaska law on behalf of Alaska as it relates to J.  
P. Morgan Securities Inc., relating to certain **research** practices at J. P. Morgan Securities  
Inc.

1  
2 2. J. P. Morgan Securities Inc. will CEASE AND DESIST from violating AS  
3 45.55.060(a)(7) and (b)(1) in connection with research practices referenced in this Order  
4 and will comply with AS 45.55.060(a)(7) and (b)(1) in connection with research practices  
5 referenced in this Order and will comply with the undertakings of Addendum A,  
6 incorporated herein by reference.

7  
8 3. IT IS FURTHER ORDERED, ADJUDGED AND DECREED that:

9  
10 As a result of the Findings of Fact and Conclusions of Law contained in this Order, J.  
11 P. Morgan Securities Inc shall pay a total amount of \$80,000,000.00. This total amount  
12 shall be paid as specified in the SEC Final Judgment as follows:

13  
14 \$25,000,000 to the states (50 states, plus the District of Columbia and Puerto Rico).  
15 Upon execution of this Order, J. P. Morgan Securities Inc. shall pay the sum of  
16 \$250,000.00 of this amount to the State of Alaska as a civil monetary penalty pursuant to  
17 the agreement of the parties, to be deposited in the Alaska general fund. The total amount  
18 to be paid by JPMSI to state securities regulators pursuant to the state settlement offer may  
19 be reduced due to the decision of any state securities regulator not to accept the state  
20 settlement offer. In the event another state securities regulator determines not to accept  
21 JPMSI's state settlement offer, the total amount of the Alaska payment shall not be  
22 affected, and shall remain at \$250,000.00;

23  
24 \$25,000,000 as disgorgement of commissions, fees and other monies as specified in  
25 the SEC Final Judgment;

\$25,000,000, to be used for the procurement of independent research, as described  
in the SEC Final Judgment;

\$5,000,000, to be used for investor education, as described in Addendum A,  
incorporated by reference herein.

17  
18 J. P. Morgan Securities Inc. agrees that it shall not seek or accept, directly or  
19 indirectly, reimbursement or indemnification, including, but not limited to payment made  
20 pursuant to any insurance policy, with regard to all penalty amounts that J. P. Morgan  
21 Securities Inc. shall pay pursuant to this Order or Section II of the SEC Final Judgment,  
22 regardless of whether such penalty amounts or any part thereof are added to the  
23 Distribution Fund Account referred to in the SEC Final Judgment or otherwise used for the  
24 benefit of investors. J. P. Morgan Securities Inc. further agrees that it shall not claim,  
25 assert, or apply for a tax deduction or tax credit with regard to any state, federal or local tax  
for any penalty amounts that J. P. Morgan Securities Inc. shall pay pursuant to this Order or  
Section II of the SEC Final Judgment, regardless of whether such penalty amounts or any  
part thereof are added to the Distribution Fund Account referred to in the SEC Final  
Judgment or otherwise used for the benefit of investors. J. P. Morgan Securities Inc.  
understands and acknowledges that these provisions are not intended to imply that Alaska  
would agree that any other amounts J. P. Morgan Securities Inc. shall pay pursuant to the  
SEC Final Judgment may be reimbursed or indemnified (whether pursuant to an insurance  
policy or otherwise) under applicable law or may be the basis for any tax deduction or tax  
credit with regard to any state, federal or local tax.

1  
2 4. J. P. Morgan Securities Inc. shall comply with the undertakings of Addendum A,  
incorporated herein by reference.

3 5. If payment is not made by J. P. Morgan Securities Inc. or if J. P. Morgan Securities  
4 Inc. defaults in any of its obligations set forth in this Order, the Division may vacate this  
5 Order, at its sole discretion, upon 10 days written notice to J. P. Morgan Securities Inc. and  
without opportunity for administrative hearing.

6 6. This Order is not intended by the administrator to subject any Covered Person to  
7 any disqualifications under the laws of any state, the District of Columbia or Puerto Rico  
8 (collectively, "State"), including, without limitation, any disqualifications from relying upon  
9 the State registration exemptions or State safe harbor provisions. "Covered Person"  
means J. P. Morgan Securities Inc., or any of its officers, directors, affiliates, current or  
former employees, or other persons that would otherwise be disqualified as a result of the  
Orders (as defined below).

10 7. The SEC Final Judgment, the NYSE Stipulation and Consent, the NASD Letter of  
11 Acceptance, Waiver and Consent, this Order and the order of any other State in related  
12 proceedings against J. P. Morgan Securities Inc. (collectively, the "Orders") shall not  
13 disqualify any Covered Person from any business that they otherwise are qualified,  
licensed or permitted to perform under applicable law of Alaska and any disqualifications  
from relying upon this state's registration exemptions or safe harbor provisions that arise  
from the Orders are hereby waived.

14 8. For any person or entity not a party to this Order, this Order does not limit or create  
15 any private rights or remedies against J. P. Morgan Securities Inc. including, without  
16 limitation, the use of any e-mails or other documents of J. P. Morgan Securities Inc. or of  
others regarding research practices, or limit or create liability of J. P. Morgan Securities Inc.  
or limit or create defenses of J. P. Morgan Securities Inc. to any claims.

17 9. Nothing herein shall preclude Alaska, its departments, agencies, boards, commissions,  
18 authorities, political subdivisions and corporations, other than the division of banking,  
19 securities, and corporations and only to the extent set forth in paragraph 1 above (collectively,  
20 "State Entities") and the officers, agents or employees of State Entities from asserting any  
claims, causes of action, or applications for compensatory, nominal and/or punitive damages,  
or administrative, civil, criminal, or injunctive relief, against J. P. Morgan Securities Inc. in  
connection with certain research practices at J. P. Morgan Securities Inc.

21 BY ORDER OF THE ADMINISTRATOR OF SECURITIES

22 Dated this 11 day of September, 2003.

23  
24  
25 /s/ Mark R. Davis  
Mark R. Davis  
Administrator of Securities