COMMISSION NEWS

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COMMISSION APPROVES FINAL ANALYST CONFLICT SETTLEMENT AGREEMENT

Citigroup to pay Arizona $2.37 million

PHOENIX – Yesterday, the Arizona Corporation Commission unanimously approved a settlement with Citigroup Global Markets, Inc., formerly known as Salomon Smith Barney, Inc. A total of $2.37 million in penalties will be deposited in the Arizona General Fund as a result of the Commission's order.

Unlike the previous settlements in which legal representatives appeared by telephone only, Citigroup was represented by Sallie Krawcheck, Chairperson and CEO of the firm's newly reorganized research, analysis and securities sales subsidiary, Smith Barney. Additionally, local attorneys from the law firm of Osborn Maledon and in-house legal counsel for Smith Barney attended the Commission's open meeting.

An additional $197,660 from the Citigroup settlement is earmarked for investor education in Arizona. This amount will be placed in an Investor Education Fund to be administered by a nonprofit organization. The funds will be used to develop and promote programs aimed at equipping people with knowledge and skills to make informed investment decisions.

The Commission's decision wraps up investigations by state and federal regulators into the stock-research abuses and IPO distribution practices of ten Wall Street brokerage firms. Similar to the Credit Suisse First Boston case approved last month, the Citigroup case involves violations of the antifraud provisions of Arizona's Securities Act. Citigroup consented to the settlement terms without admitting or denying allegations contained in the order.

One of the focal points of the investigation involved the conduct of Jack Grubman, a prominent analyst with

Salomon Smith Barney. He was considered by many to be the nation's top telecommunications analyst whose recommendations were watched by small, large and institutional investors alike.

According to the multi-state investigation into conflicts of interest, Grubman's compensation "exceeded $67.5 million, including his multi-million dollar severance package" for the period beginning in 1999 and ending in August 2002 when he left Salomon. Among other things, Grubman and other Salomon Smith Barney analysts were found to have:

- Engaged in "IPO spinning," a practice where executives at current or potential investment banking clients received shares in hot new public stock offerings;
- Maintained inaccurate books and records in connection with IPO spinning and the IPO distribution process;
- Presented information purported to be independent, objective and unbiased when in fact, analysts were encouraged to support the investment banking business through their inflated ratings;
- Published fraudulent research reports which did not reflect the analyst's privately held opinion.

Most troubling to the Commissioners were the allegations that Salomon Smith Barney published fraudulent research reports, including a report on two telecommunications companies that were never profitable, and in reality, were racking up huge debts.

"Saying you're neutral or ambivalent about a stock is one thing. But sugar-coating a loser is another thing entirely," said Commissioner Bill Mundell. "This is tantamount to giving failing students a C grade instead of a D or F. It does not signal genuine concern about the future of a company. Investors were misled and that is unacceptable."

Similar to the other settlements, Citigroup agreed to implement significant reforms to its stock research practices. In part, these changes include:

- Disclosing on research reports any investment banking compensation the firm received or expects to receive from the companies covered,
- Separating compensation for research analysts from the firm's investment banking business,
- Prohibiting investment bankers from influencing analysts' compensation,

- Establishing a Research Recommendations Committee to ensure the veracity of stock research recommendations,
- Prohibiting all employees from promising or implying that a recommendation would be made in exchange for the firm being awarded an investment banking transaction, and
- Designating a compliance monitor who will ensure compliance with the agreement and be available to research analysts who feel undue influence or pressure from any source.

"When I came to Smith Barney 15 months ago, my mandate – along with broad authority – came from the CEO and board of directors at Citigroup," Krawcheck told the Commissioners. "That mandate was to develop and deliver the highest quality research – research that is truly independent from investment banking for the benefit of Smith Barney clients."

"To carry out that mandate for the past 15 months, I've overseen an extensive reorganization of the business. We made Smith Barney, which consists of the private client or retail brokerage business and global research, one of Citigroup's four major businesses," Krawcheck testified. "That business unit – Smith Barney, my business unit – is completely separate from the corporate and investment bank and all other Citigroup business units – and its clients consist solely of investors. Thus, our analysts have a very clear mandate in who their clients are and how to service them."

Krawcheck also testified that Smith Barney has established a dedicated compliance team. A new compensation structure is in place to reward analysts based on the quality of their analysis and the success of their stock picks.

Commission Chairman Marc Spitzer cited testimony from the case involving Jack Grubman that he said "does not suggest contrition…does not suggest an admission of wrongdoing." Spitzer asked Krawcheck if senior management at Citigroup is sincere in its efforts to reform its practices.

"To me the actions of this company going forward not only mean that they 'get it' but that we as an organization have put in place the procedures and the processes, and really the culture, that this type of thing cannot happen again," Krawcheck stated. "We cannot have senior management talking to analysts about their research recommendations or attempting to influence them. The culture is in place. The processes are in place. The rules are in place. The training is in place."

Commissioner Bill Mundell asked "Since this settlement was entered into have you or anybody affiliated with

Citigroup made any public statements downplaying the significance of the actions contained in the settlement?"

"Absolutely not," Krawcheck replied.

Commissioner Jeff Hatch-Miller drew an analogy of the relationship between consumers and the Wall Street community to the relationship between two married people. "All of a sudden you find out that one of the partners wasn't being fully truthful or was engaging in some activities you didn't expect. And you might be able to keep the marriage going, but that doesn't mean you keep the trust. How do you restore that trust?"

"This isn't about splitting legal hairs or 'we did this but we didn't do this.' It is about doing the right thing for our clients," Krawcheck said.

"Sadly, a period of time needs to pass where Wall Street needs to get itself out of the newspapers, make sure it's operating as it should and win back the public," she explained. "And that's going to take some time. In the meantime it is absolutely imperative for all of us on Wall Street, not just Citigroup, to make sure that we are doing what's right for our clients. It's not just a nice thing to do. It is, frankly, a very good business thing to do."

Commissioner Mike Gleason characterized the settlement agreement as a mandate to "go forth and sin no more."

"In the long term, this only works if you have adequate and just regulation," Gleason suggested, "because people change within companies. Isn't that correct?"

"We believe we have a great deal of regulation at both the federal and at the state level," Krawcheck offered. "And what we have here with the global settlement is additional regulation which does, we believe, a very good job of shoring that up. Within Smith Barney we have procedures that are adequate, with belts and suspenders, to allow us to go forth and not sin."

Commissioner Kristin Mayes said she appreciated the fact that Citigroup believed the matter was serious enough to send Smith Barney's CEO and senior representatives of its legal team.

"Something had to change," Commissioner Mayes said after the meeting. "Smith Barney has some 11,600 registered securities salespersons within U.S. Of those, approximately 6,000 hold Arizona registrations and 192 are physically located in Arizona. Those numbers represent people who are influencing the investment choices of everyday citizens. These are regular people who lost small fortunes on the stock market, partly based on misinformation, inappropriate recommendations and fraudulent stock ratings. We and the other state regulators will be watching to be certain that the reforms Ms. Krawcheck talked about are carried through."

To read about Commission actions against other Wall Street brokerage firms or to learn about enforcement actions by the Commission, view the news releases section of the website at: http://www.ccsd.cc.state.az.us/news_releases/index.asp. Investors can find a variety of helpful brochures and tips on wise investing at: http://www.ccsd.cc.state.az.us/investor_education/index.asp. To call the Commission's Securities Division, dial 602-542-4242 or toll free, 1-877-811-3878.

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