

INSTANT MESSAGING: THE 'PERFECT STORM' FOR REGULATORY NON-COMPLIANCE

ABSTRACT

While many companies are well underway in seeking to comply with industry regulations pertaining to managing instant messages as records, underlying market conditions and usage patterns are creating the perfect storm — a storm that threatens to undermine record keeping practices within the Securities and Investments industry. More than one-quarter of Securities and Investments firms either lack a stated policy with regard to instant messaging or have failed to adequately communicate that policy to their employees. Most companies that have a policy permit the use of instant messaging, but nearly one-third forbid instant messages. Although firms are motivated by concerns for network security and an inability to manage and control instant messaging, in fact usage appears to occur in spite of management efforts and, in one-third of companies, without formal product evaluation.

Most importantly, however, is the underlying behavior of employees. The majority of respondents already view instant messaging as an essential business tool — suggesting they will use it when and if they need to — and the majority believe that it is already widely used by all departments within an organization for both business and social communications. This groundswell support for instant messaging at the bottom represents a movement much like e-mail, in which instant messaging is a strategic enterprise application supporting all operations of the organization. Added to this perfect storm is the final tsunami — wireless instant messaging, already moving into mainstream. Fully, half of Securities and Investments firms do not have a policy in place.

This White Paper evaluates further instant messaging trends within the Securities and Investments industry, summarizes where these organizations may be at risk for regulatory violations of record-keeping practices, and makes recommendations for keeping pace with the changing dynamics of electronic messaging.

Introduction

A U.K. research study published in July 2003 suggested that UK-based investment banks could be putting themselves at risk by allowing workers to use unregulated Instant Messaging networks to exchange business and financial information usage.¹ In the study, approximately half of the UK investment community admitted that instant messaging use was widespread within their organizations and that important transactions were being made via free instant messaging networks including AOL, MSN and Yahoo! Given that the regulatory environment is currently more stringent in the U.S. than in the U.K., Iron Mountain was interested in understanding whether U.S. Securities and Investment firms, as well as others in the financial services industry, were equally at risk as those companies in the U.K.

Further indicators were available that the Securities and Investments industry could be at substantial risk due to a lack of adequate record-keeping practices from instant messaging. In a survey of executives at a Securities Industry News Web seminar, vendor Akonix Systems found that 61% reported their organizations did not have an instant messaging archive system in place and 39% did not have a stated policy with respect to usage of instant messaging. Earlier this year, a study conducted by AIIM International and Kahn Consulting² found that 46% of organizations (of all types, not limited to financial services) use instant messaging for business, but that less than half of those companies using it have a formal policy for managing instant messaging. Gartner Group has forecast that 70% of all enterprises will use instant messaging in 2003 and that by 2005 it will represent 50% of all business-to-client communications. With this groundswell occurring, Securities and Investments firms can no longer ignore the challenges and risks it represents to their organizations.

Financial institutions in the U.S. are required by both the Securities and Exchange Commission (SEC) and the National Association of Securities Dealers (NASD) to monitor all electronic messages, including instant messages, and to conduct periodic audits to ensure compliance. Under SEC regulations, broker-dealers must retain originals of all communications received and copies of all communications sent. More specific rules apply to instant messaging: the New York Stock Exchange has explicitly included instant messages in a requirement to retain all messages related to a company's business, and NASD has indicated that instant messaging must comply with their guidelines for record retention.

For these reasons, Iron Mountain undertook a survey targeted at key individuals within the financial services industry, in various occupations related to instant messaging policy development ranging from IT, legal and compliance staff, and those departments that would actually have a need to use it. More than 2,000 e-mail invitations were sent to highly targeted individuals within the financial services industry and, in addition, an invitation to participate was posted to the Records Management Listserv and ARMA International's financial services industry member forum. Respondents could also learn about the survey and opt to take it through informational articles in BD Week and Iron Mountain's Compass Point publications. A total of 212 individuals completed the survey and 68 (or 32%) of these were within the Securities and Investments industry, the primary focus of both our White Paper and of the U.K. study.

Do Companies Have an Instant Messaging Policy?

The lack of a policy regarding how instant messages are used within an organization represents a potential threat to non-compliance with regulations. Instant messages are usually viewed as sales literature or correspondence under Securities and Exchange Commission (SEC) rules governing communications with the public. For the Securities and Investments sector in particular, these rules dictate that companies must maintain compliance systems in order to supervise the use of instant messaging technologies and make the usage of instant messaging

¹ Vanson Bourne Research and FaceTime Communications, 2003.

² "Managing Email in the New Business Reality," AIIM International and Kahn Consulting, Inc., 2003.

consistent with that of e-mail policies. Within the financial services industry, the Securities and Investments sector is the most likely to have a policy in place regarding instant messaging -- nearly three-quarters (73.5%) of the respondents report that their company has such a policy (Table 1). Thus, the Securities and Investments sector appears well aware of SEC requirements, although more than one-quarter of respondent companies remain at risk for SEC violations, since lack of a stipulated policy most likely indicates inadequate monitoring and compliance with regulations.

Table 1. Does your organization have a policy regarding instant messaging?

	Accounting	Banking	Insurance	Securities and Investments	Total
Yes	4 66.7%	8 40.0%	2 18.2%	50 73.5%	64 61.9%
No	2 33.3%	11 55.0%	7 63.6%	14 20.6%	34 32.4%
Don't know	0 0.0%	1 5.0%	2 18.2%	4 5.9%	7 6.7%
	6 100.0%	20 100.0%	11 100.0%	68 100.0%	105 100.0%*

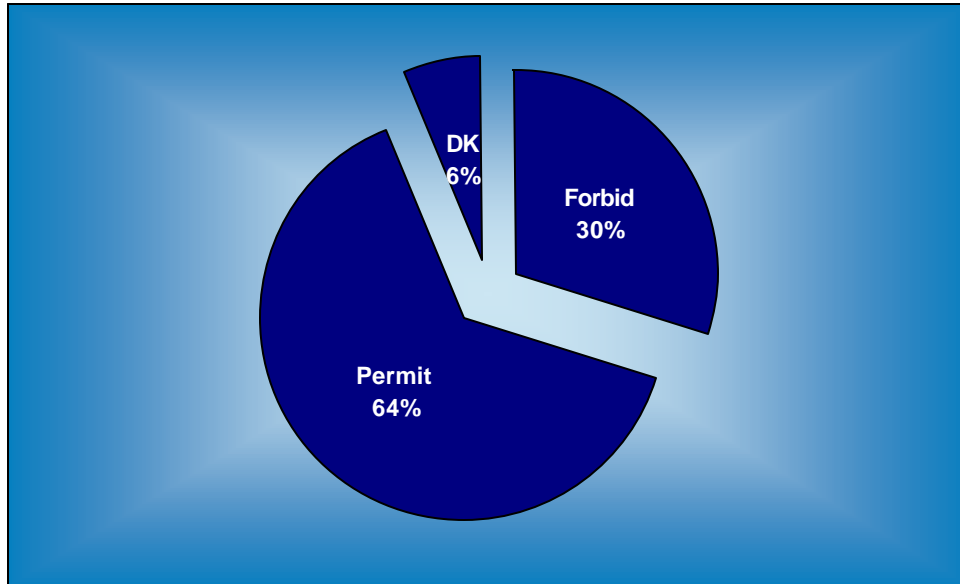
*Due to rounding, percentages may not total to 100%.

Focusing specifically upon the Securities and Investments industry, 48% of respondent organizations expressly permit the use of instant messaging for business communications and other transactions. When taking into account policies that permit the use of instant messaging but only under specific circumstances, fully 64% of respondents from companies that have a policy in place *permit* the use of instant messaging (Figure 1).

It may be noted that nearly 20% of those respondents reported something “other” than expressly forbidding or permitting the use of instant messaging, and in these instances what they reported is often a more specific policy. For instance:

- Policies may allow a *single* instant messaging solution that is available to users requiring instant messaging.
- Some policies permit use of instant messaging for certain groups of employees and only for business transactions (instant messages are allowed only by special permission for a particular business need).
- Communications are permitted but they are not used for evidencing transactions.
- Use of in-house instant messaging is permitted (not through a firewall) or the organization actively forbids external instant messaging but permits its use internally.
- In some instances, instant messaging is allowed only if the message is encrypted.
- Some organizations permit instant messaging use only with compliance approval.

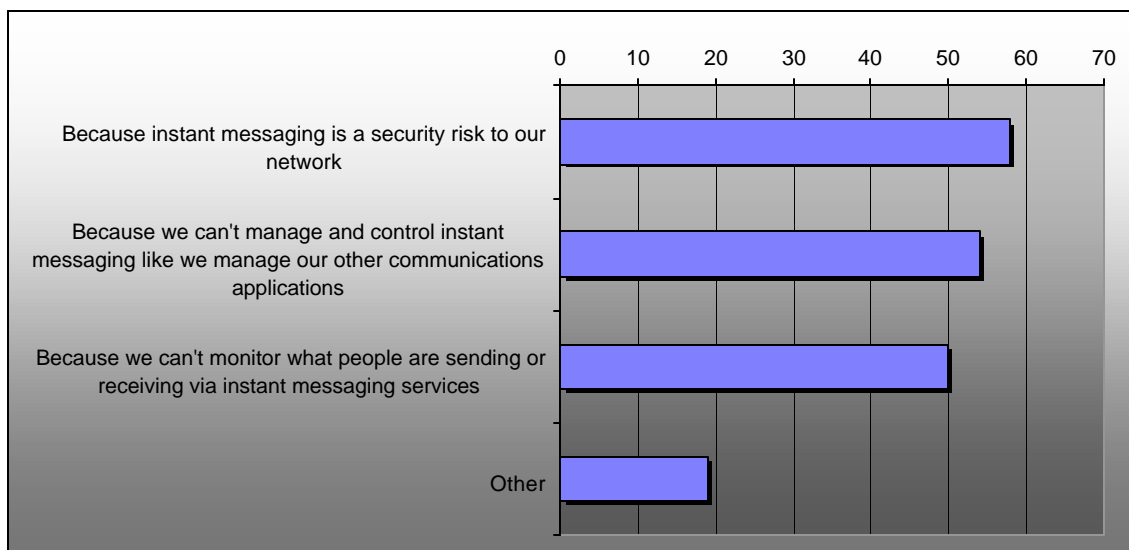
Figure 1. Which of the following best describes your policy?



**Don't know responses include those from respondents who stated that their organization's policy with respect to instant messages was unclear.*

Of those companies that *forbid* instant messaging, regardless of industry segment, their reasons are shown in Figure 2 on a percentage basis. Risk to the security of the network remains the greatest overall deterrent to wider permissiveness, and not concerns for regulatory compliance, but clearly other concerns are close behind.

Figure 2. Why does your company prevent/forbid the use of instant messaging by employees for business communications and transactions?



**Multiple responses permitted.*

Use of Instant Messaging

For various reasons, a ban on instant messaging does not in and of itself ensure regulatory compliance and in fact may be counterproductive. Regardless of whether or not they have an instant messaging policy in place, its use is already well established within the U.S. Securities and Investments industry. When asked whether or not employees *use* instant messaging in their business today, 68.2% of respondents within the Securities and Investments industry say that employees of their organizations do. The use of instant messaging is even more established within the U.S. than within the U.K. – only 42% of respondents in the U.K. study reported that instant messaging was used within their companies.³

Within the Securities and Investment sector, 57.8% of U.S. respondents indicate that they use instant messaging differently than they do e-mail. Interestingly, 15.4% of U.S. respondents from organizations that have a policy with respect to instant messaging reported that it is used in their organizations *even when they have a policy in place that prohibits it* (Table 2), and another 34.6% don't know whether it is used or now. Results show that having a policy in place impacts usage in the manner in which organizations intend, but either policies are not well-understood, not well-communicated, or employees ignore them in some instances.

These findings further suggest that, even among this subset of respondents whose organizations *have* a policy in place forbidding instant messaging, its use is occurring anyway. It is becoming so mainstream that it may in fact already be viewed as a necessary business tool within this industry. The policy of forbidding instant messaging usage, at least within the Securities and Investments industry, provides little protection for compliance with SEC and NASD regulations. They suggest that it is far better to *permit* the use of instant messaging and provide appropriate tools so that it may be monitored and audited in order to avoid financial penalties. If a Securities and Investments firm elects to forbid the use of instant messaging, management must recognize that they still have a compliance problem that requires them to:

- Explain to registered representatives of their firm that they may not use instant messaging;
- Audit employees to ensure that they are not using instant messaging; and
- Emphasize that violation of this policy may be grounds for dismissal.

The requirements of a policy prohibiting instant messaging may require nearly as much time and IT support as policies supporting it. Other factors to consider, although outside the realm of this White Paper, are the cost issues associated with the use of instant messaging. Like webcasting and other real-time technologies, instant messaging may in fact reduce meeting costs within a company by connecting employees geographically. There are also less tangible costs to consider: Instant messaging has the potential to facilitate improved communications with customers and may go directly to the ability to compete within the industry because instant messaging is ideally suited for time-sensitive communications. If the latter factor is indeed the case, it is also likely that it will be difficult to enforce a “no instant messaging” policy among sales representatives who know that their commissions are based upon timeliness of response and perception as a leader in utilizing technology for business applications. The U.K. study concluded that instant messaging represents a “bottom up” phenomenon in that its usage is driven by the user base upward, not by management downward, and our results would lead us to draw a similar conclusion for the U.S.

³ The question was worded identically, both surveys included approximately the same number of interviews from the Securities and Investment industry (50 in the U.K. versus 68 in the U.S.), and the industry was defined identically in terms of who was included as a ‘Securities and Investment’ firm.

**Table 2. Use of Instant Messaging Among Those With Policies:
Forbidding its Use Makes an Impact***

	Forbid IM	Permit IM	Total
Employees Use IM	4 (15.4%)	42 (100.0%)	46 (67.6%)
Employees Don't Use IM	13 (50.0%)	0 (0.0%)	13 (19.1%)
Don't Know	9 (34.6%)	0 (0.0%)	9 (13.2%)
Total	26 (100.0%)	42 (100.0%)	68 (100.0%)**

*Survey results reflect the entire base of respondents in the financial services industry that have a policy with respect to instant messaging in place, and does not solely reflect the Securities and Investments industry.

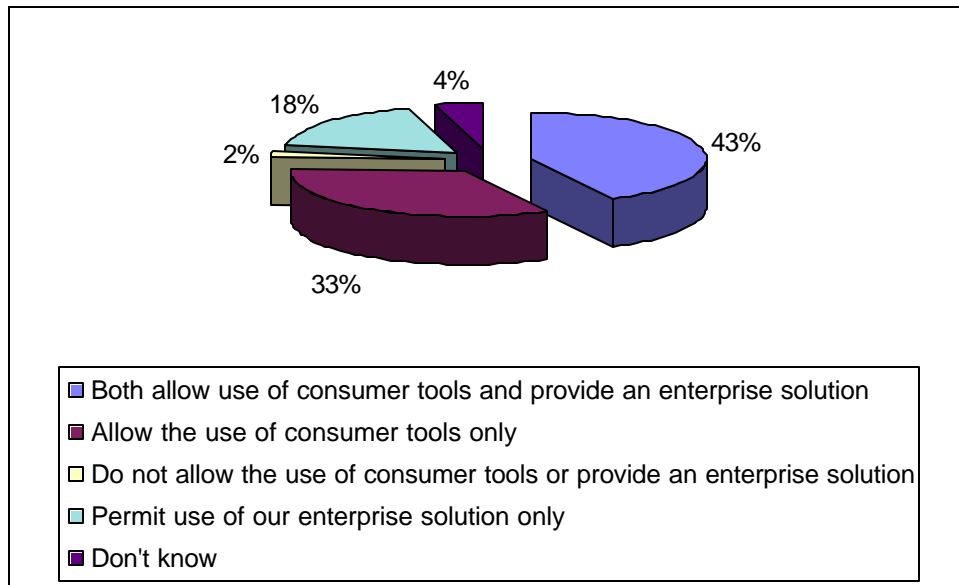
**Rounding error.

Vendor Solutions

Readily available consumer-oriented instant messaging products and services also represent a potential threat to non-compliance. It is difficult for organizations to monitor which of their employees are using any given solution for business reasons. Further, there is no mature standard for instant messaging. This factor complicates communications with external parties and promotes usage of multiple instant messaging solutions by any given individual. Further, no instant messaging platform by itself offers a comprehensive feature set required for logging, archiving, and other capabilities necessary to meet regulatory requirements. For these reasons, in addition to utilizing one or more basic instant messaging platforms, companies may elect to augment their solution with additional software providing security and interoperability among various instant messaging solutions. AOL, Yahoo!, MSN Messenger, Reuters, and Communicator are examples of popular instant messaging software; FaceTime, IMlogic, and Akonix Systems are all examples of security and interoperability software.

Securities and Investments firms are most likely to allow use of both consumer and enterprise solutions in tandem but fully one-third allow the use of consumer tools only (Figure 3), meaning they are utilizing tools which probably offer them the ability to communicate with external parties as needed but are unlikely to meet SEC guidelines for records retention.

Figure 3. Do you allow use of common consumer instant messaging tools such as AOL or Yahoo! or do you provide an enterprise solution?

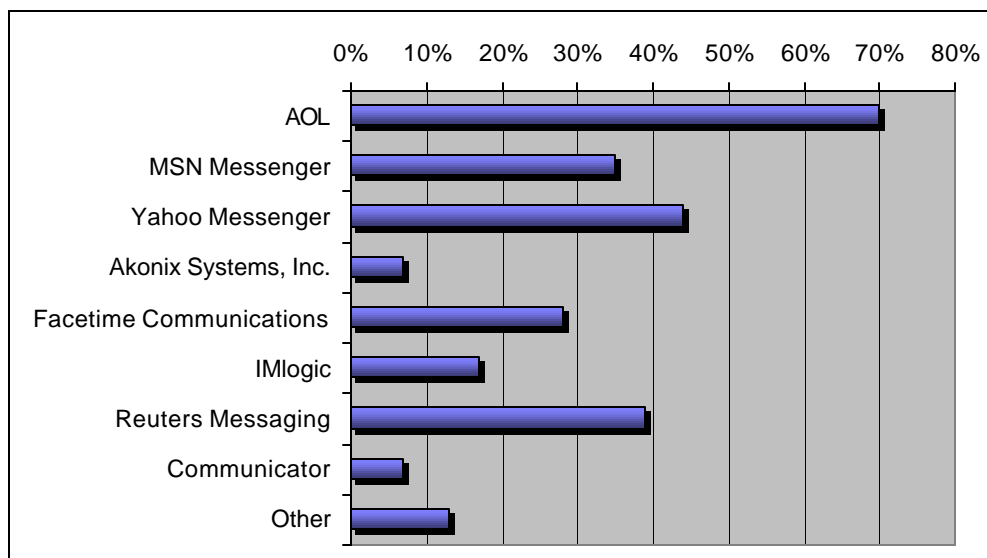


**Multiple responses permitted. Responses represent the Securities and Investments industry solely.*

When respondents from Securities and Investments firms were asked which types of software were used in their organizations, 70% selected one or more consumer-oriented instant messaging solutions (AOL, Yahoo! or MSN Messenger; Figure 4). This fragmentation is to be expected, as few instant messaging solutions interoperate well, if at all. Assuming that the use of instant messaging is driven from the bottom up, representatives will by necessity utilize the solution that their customer uses, or, more likely, the solution(s) that their customer(s) dictate – leaving IT with the responsibility for managing multiple solutions.

To address the need for standards among instant messaging solutions, the financial services industry created FIMA (Financial Services Instant Messaging Association). FIMA is striving to promote the development of protocols for instant messaging within the financial industry, promote adoption of the necessary infrastructure, assist organizations in evaluating solutions, and endorse specific solutions that will meet SEC, NASD, and other regulatory compliance requirements. Until the time that such protocols are in place, however, this fragmentation will exist in many organizations, creating another factor that hinders regulatory compliance.

Figure 4. Which of the following tools do your company's employees use to conduct instant messaging?



**Multiple responses permitted.*

Table 3 shows the percentage of respondents within the Securities and Investments industry that use interoperability software on top of one (or more) of the three most popular consumer messaging protocols. For instance, 62% of respondents report that AOL is used in conjunction with either Akonix, Facetime, or IMlogic. This leaves nearly a third of AOL users, as an example, that do not utilize necessary management software on top of their basic instant messaging solutions.

Table 3. Use of Security/Interoperability Software Among Users of Consumer Instant Messaging Solutions

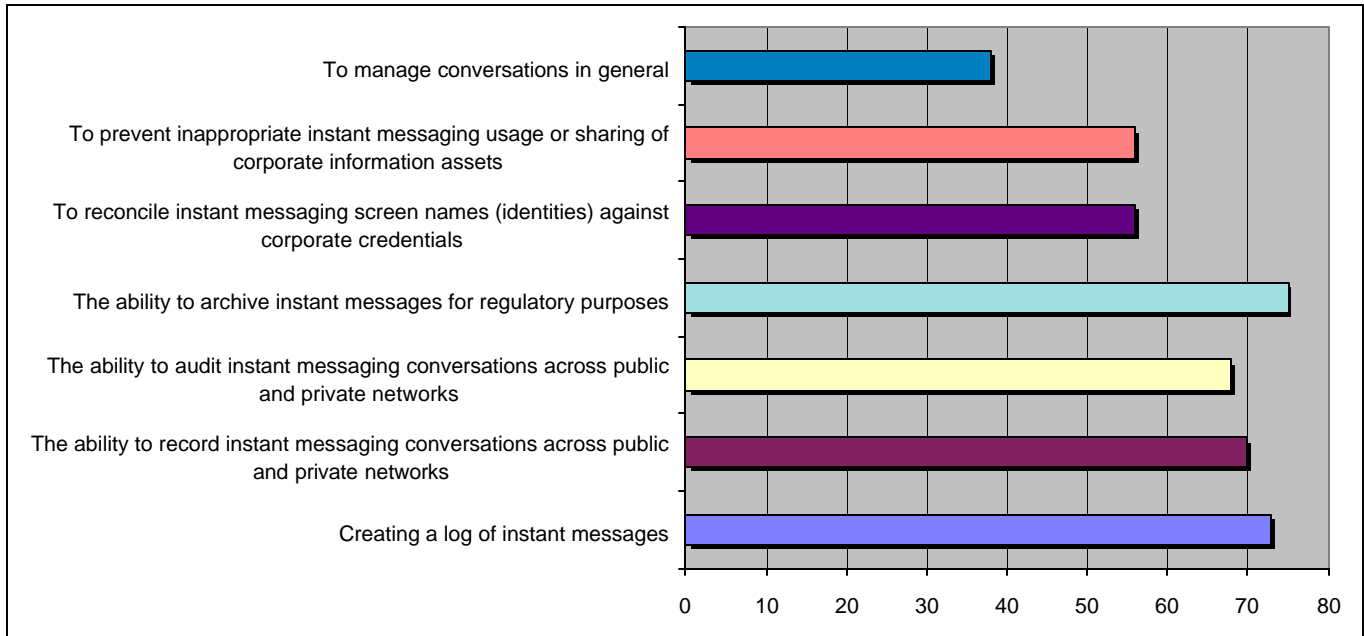
	AOL	MSN Messenger	Yahoo Messenger	Total
Akonix Systems, Inc.	3 (9%)	3 (18%)	3 (15%)	3 (100%)
Facetime Communications	11 (34%)	5 (31%)	7 (35%)	13 (100%)
IMlogic	6 (19%)	5 (31%)	4 (20%)	8 (100%)
Total	32	16	20	46

**Multiple responses permitted.*

Formal evaluation of instant messaging products by the financial services community is more limited than would be expected, further increasing the risk of regulatory non-compliance. In those companies that use instant messaging, 33.3% of Securities and Investments respondents reported that no formal evaluation of vendor solutions occurred. Without this formal evaluation, companies remain at risk in determining whether or not the systems they implement formally comply with all of the various SEC and NASD regulations. The purpose of vendor selection is noted in Figure 5; archiving and the ability to create a log of instant messages are the most commonly required features. These results are shown for all survey respondents and not those exclusively in Securities and Investments, due to the relatively small sample size of Securities

and Investments firms that have formally evaluated instant messaging solutions. However, it may be seen that all features are viewed as necessary by the majority of firms, with the exception of the first one (“to manage conversations in general”).

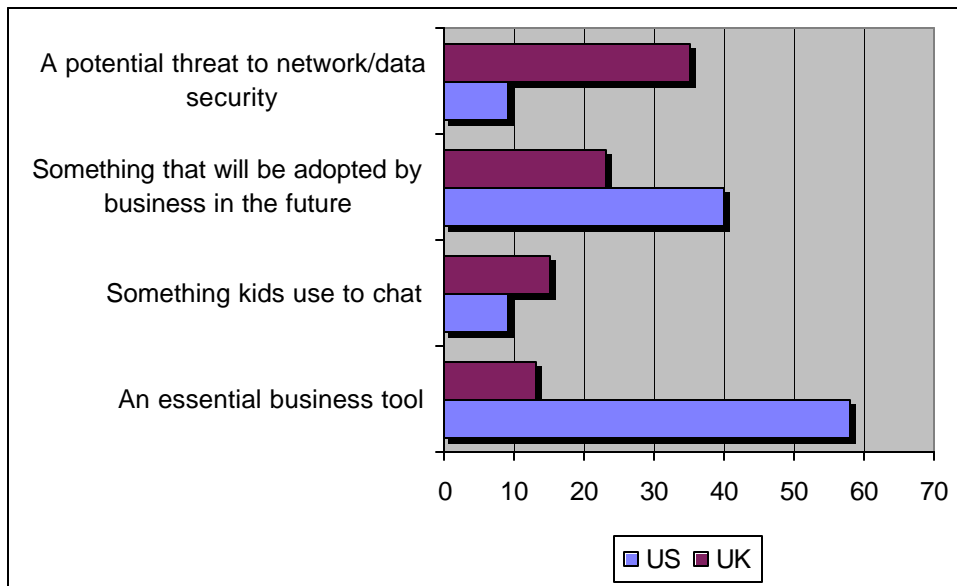
Figure 5. Which of the following features/functions did you seek in an instant messaging solution?



**Multiple responses permitted. Responses represent all respondents surveyed and not exclusively those in the Securities and Investments industry.*

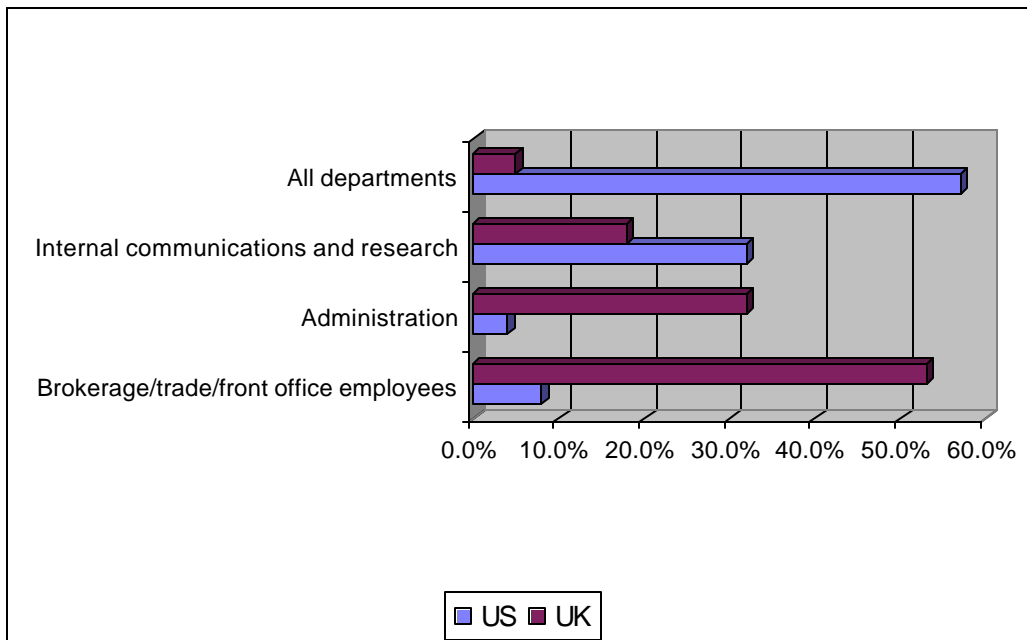
The Securities and Investment industry is more likely than other financial services sectors to see instant messaging as an essential business tool or as something that will be adopted by business in the future and are far more likely to perceive instant messaging as an essential business tool than U.K. firms (Figure 6) while concurrently less likely to show concern about issues related to network and data security. These findings even more conclusively demonstrate that instant messaging is a “bottom up” phenomenon – if initiated at the top or by IT managers there would be considerably greater concern for the threats to data security as well as for regulatory compliance. This points to the grave risk these companies face as they begin to utilize instant messaging – typically starting with highly familiar consumer-oriented services, which may be pervasive even in companies that preclude their usage.

Figure 6. Which of the following describes your perception of instant messaging: The U.S. vs. the U.K.



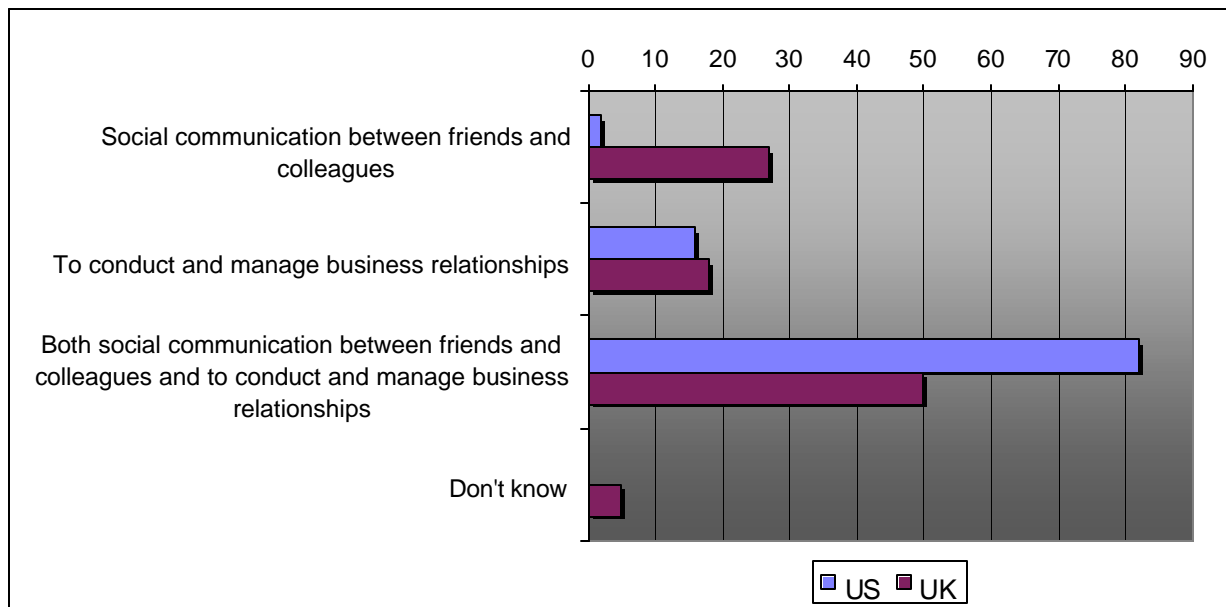
When asked “Which, if any, particular departments use instant messaging more than others?” Securities and Investments respondents most frequently indicated that “all departments” use instant messaging (Figure 7) and that it is used predominantly for both business and social (personal) communications (Figure 8). Once again the challenge to regulatory compliance officers and IT management increases, as there is no single group of individuals that they can single out for monitoring as creating the greatest risk of exposure. In the U.K., front office workers (primarily broker reps) were believed to be the primary users of instant messaging – providing a more focused monitoring and auditing effort for management – but in the U.S. usage is clearly widespread across the organization.

Figure 7. Which, if any, particular departments use instant messaging more than others?



Widespread usage within an organization and perception as a critical business tool will continue to add challenges to organizations that try to control how instant messaging is used. Furthermore, the U.S. Securities and Investments industry is more likely to utilize instant messaging for *both* social and business purposes than the U.K. (Figure 8). While the U.K. study findings show a higher propensity to use instant messaging *exclusively* for business purposes than in the U.S., a full 82% of respondents in the U.S. report that instant messaging is being used for dual purposes. Already instant messaging is perceived as a high critical business tool among organizations that are existing users, with 43.5% of respondents reporting that instant messaging is as equally useful or essential as the telephone, while 56.5% reported that the telephone is not as useful or essential. These findings are not significantly different than in the U.K., where 47% believe that instant messaging is as equally useful or essential as the telephone, and 53% report that it is not as useful or essential.

Figure 8. For which of the following do you think your employees use instant messaging?

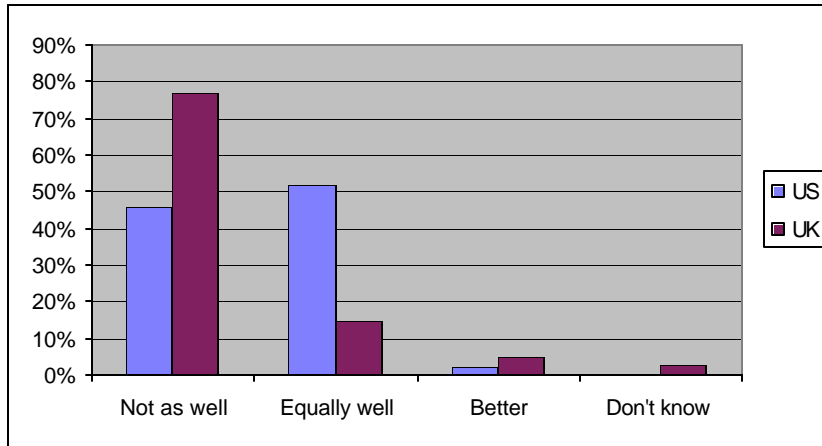


Managing Instant Messaging

The bottom line for all organizations is how well they manage instant messaging. All technologies face similar management issues as they are initially used, and management improves as products mature and implementation becomes more widespread. U.S. companies are significantly more likely than U.K. companies to believe that instant messaging is managed “equally well” as e-mail (perhaps a bad omen for e-mail management), with 54% of respondents reporting that it is managed equally well or better than e-mail (Figure 9). There is a great deal of cross-over between the use of e-mail and instant messaging for various applications: in the U.S., 70% of respondents believe that instant messaging will replace the use of e-mail in some circumstances. As some e-mail migrates to instant messaging, it is more than likely cannibalizing many corporations’ efforts to monitor and audit to ensure compliance. These findings also suggest that a common monitoring and auditing utility is desirable so that communications may be tracked independently of *mode* of communication – since it is unlikely that an individual will be

able to recall the precise mode of communication for retrieval of archived communications at some distant point in the future.

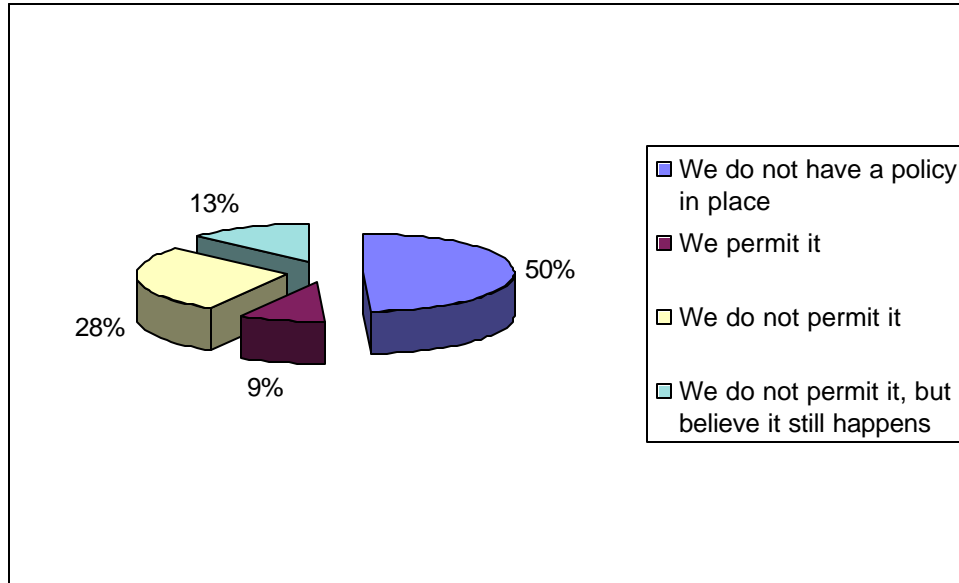
Figure 9. Compared with how your company manages e-mail usage, would you say that instant messaging usage is managed ...



Wireless Networks Add Another Degree of Complexity

A further challenge beyond instant messaging may be wireless communications – specifically Short Message Service (SMS) and other forms of instant messaging. While SMS is currently a worldwide standard, it is evolving into disparate multimedia solutions (Multimedia Message Service or MMS), which will pose many of the same problems as existing instant messaging solutions in that communications between various systems will be incompatible. Worse yet, archiving and other functionality available with landline networks is far more likely to be lacking with users of wireless instant messaging. Tracking wireless instant messaging is further complicated by the fact that many employees may use personally owned devices and services to communicate with customers, and if a company wishes to manage messages, they may need to centralize procurement of wireless services and bring them under corporate billing. As compared to 73.5% of Securities and Investment firms that have a policy in place for instant messaging on fixed networks, fully 50% do not have a policy in place for instant messaging on wireless networks (Figure 10), and, in a trend that belies instant messaging overall, 13% of respondents believe employees are using instant messaging *even when a policy forbidding it is already in place*. Clearly, the challenges for regulatory compliance are just beginning. The wireless environment is a larger reflection of what is taking place in the overall instant messaging market.

**Figure 10. Instant messaging may also be used on cell phones and wireless networks.
How does your company treat instant messaging on wireless devices?**



Conclusions and Recommendations

While many companies are well underway in seeking to comply with industry regulations pertaining to managing instant messages as records, underlying market conditions and usage patterns are creating the perfect storm – a storm that threatens to undermine record keeping practices within the Securities and Investments industry. More than one-quarter of Securities and Investments firms either lack a stated policy with regard to instant messaging or have failed to adequately communicate that policy to their employees, and where a policy does not exist a lack of monitoring and archiving is likely to follow. *Most* companies that have a policy permit the use of instant messaging, but 30% of those with a policy do not permit it, and a policy forbidding instant messaging may be effective only in the short term within this industry. Although motivated by concerns for network security and an inability to manage and control instant messaging, in fact usage appears to take place anyway and, in one-third of companies, without formal product evaluation.

In one-third of companies, only consumer tools are used – and these tools lack the feature/functionality necessary to comply with industry regulations. Nearly 70% of respondents reported that instant messaging is already being used in their organizations – and 15% of those companies banning instant messaging have employees who use it anyway. Most importantly, however, is the underlying behavior of employees. The majority of respondents already view instant messaging as an essential business tool – suggesting they will use it when and if they need to – and the majority believe that it is already widely used by all departments within an organization for both business and social communications. This groundswell support for instant messaging at the bottom represents a movement much like e-mail, in which instant messaging is a strategic enterprise application supporting all operations of the organization. Added to this perfect storm is the final tsunami – wireless instant messaging, already moving into the mainstream. Here, half of Securities and Investments firms do not have a policy in place.

The challenge lies in adopting a balanced position that encourages use of technologies as they migrate to the mainstream and to support necessary customer interactions, while controlling risks in network and data security as well as regulatory compliance. Regardless of policy or environment, regular communication with employees as well as periodic audits of messages of all types is required to maintain compliance.

Securities and Investments firms need to apply records management controls to electronic messages of all types in order to effectively comply with regulation. This requires adoption of a comprehensive approach to records management that includes policy, technology, communication and training, and compliance monitoring.

- Policy Development: An instant messaging policy should be clearly stated and put in place organization-wide together with procedures that heighten employee awareness, project an image of good faith, and can withstand the scrutiny of litigation, audits, and other investigations.
- Technology Selection: Technology solutions should be put through the same selection process the organization would give any other type of software and should support seamless implementation of organizational policies.
- Communication and Training: An organization must take steps to ensure that employees are made aware of its requirements and are provided training to properly use the technology(ies) selected.
- Compliance: Monitoring and audits should be conducted regularly to ensure that employees are carrying out policies and procedures, *even when a policy precludes the use of a particular technology such as instant messaging*. Where areas of non-compliance are discovered, the organization should take action to address them in order to bring the company into compliance.