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BEFORE THE ARKANSAS SECURITIES COMMISSIONER

10 MAY 18 PM 2:49

CASE NO. S-10-034

ARKANSAS SECURITIES DEPT.

S-10-034-10-CO01

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3 IN THE MATTER OF:

4 MERRILL LYNCH, PIERCE, FENNER
& SMITH INCORPORATED

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CONSENT ORDER

WHEREAS, Merrill Lynch, Pierce, Fenner & Smith Incorporated ("Merrill Lynch") is a broker-dealer registered in the state of Arkansas, with a Central Registration Depository ("CRD") number of 7691; and

State securities regulators from multiple jurisdictions have conducted coordinated investigations into the registration of Merrill Lynch Client Associates ("CAs") and Merrill Lynch's supervisory system with respect to the registrations of CAs; and

Merrill Lynch 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

Merrill Lynch has advised regulators of its agreement to resolve the investigations pursuant to the terms specified in this Consent Order (the "Order"); and

Merrill Lynch agrees to make certain changes in its supervisory system with respect to the registration of CAs, and to make certain payments in accordance with the terms of this Order; and

Merrill Lynch elects to waive permanently any right to a hearing and appeal under the Arkansas Securities Act, Ark. Code Ann. §§ 23-42-101 through 23-42-509, and the Arkansas Administrative Procedures Act, Ark. Code Ann. §§ 25-15-201 through 25-15-219, with respect to this Order; and

Solely for the purpose of terminating the multi-state investigations, including the investigation by the Arkansas Securities Department, and in settlement of the issues contained in this Order, Merrill Lynch, without admitting or denying the findings of fact or conclusions of law contained in this Order, consents to the entry of this Order.

1 NOW, THEREFORE, the Arkansas Securities Commissioner as administrator of the
2 Arkansas Securities Act hereby enters this Order:

3 I.

4 FINDINGS OF FACTS

5 1. Merrill Lynch admits the jurisdiction of the Arkansas Securities Department in this
6 matter.

7 Background on Client Associates

8 2. The CAs function as sales assistants and typically provide administrative and sales
9 support to one or more of Merrill Lynch's Financial Advisors ("FAs"). There are different titles
10 within the CA position, including Registered Client Associate and Registered Senior Client
11 Associate.

12 3. The responsibilities of a CA specifically include:

- 13 a. Handling client requests;
- 14 b. Resolving client inquiries and complaints;
- 15 c. Determining if client issues require escalation to the FA or the branch management
16 team; and
- 17 d. Processing of operational documents such as letters of authorization and client
18 check requests.

19 4. In addition to the responsibilities described above, and of particular significance to this
20 Order, some CAs are permitted to accept unsolicited orders from clients. As discussed below,
21 Merrill Lynch's written policies and procedures require that any CAs accepting client orders first
22 obtain the necessary licenses and registrations.

23 5. Notably, FAs might have a "primary CA" and a "secondary CA". As suggested by the
24 designation, the customary practice is that the primary CA would handle the FA's administrative
25 matters and client orders. However, if the primary CA was unavailable, the secondary CA would
26 handle the FA's administrative matters and client orders.

1 6. During the period from 2002 to the present, Merrill Lynch employed approximately
2 6,200 CAs (average) per year.

3 Registration Required

4 7. It is unlawful for any person to transact business in Arkansas as a broker-dealer or agent
5 unless he or she is registered under the Act. Ark. Code Ann. § 23-42-301(a).

6 8. Pursuant to the general prohibition under Ark. Code Ann. § 23-42-301(a) a person
7 cannot accept unsolicited orders in Arkansas without being registered as a broker-dealer or agent.

8 9. Pursuant to Ark. Code Ann. § 23-42-308(g)(1), a broker-dealer may be fined for selling
9 securities in Arkansas through agents other than registered agents.

10 Merrill Lynch Requires Registration of Client Associates

11 10. In order for a CA to accept client orders, Merrill Lynch generally required each CA to
12 pass the series 7 and 63 qualification exams and to register in the appropriate jurisdictions.

13 11. At all times relevant to this Order, Merrill Lynch's policies and procedures specified
14 that each CA maintain registrations in the same jurisdictions as his or her FA, or broadly required
15 that each CA maintain registrations in all necessary jurisdictions.

16 Regulatory Investigations and Findings

17 12. In May 2008, state regulators received a tip alleging that Merrill Lynch was failing to
18 ensure its CAs were in compliance with jurisdictional registration requirements and its own
19 procedures. The tip alleged that Merrill Lynch CAs were registered in two jurisdictions – the CA's
20 home state and one neighboring state – because Merrill Lynch only paid for registrations in two
21 jurisdictions.

22 13. During the summer of 2008, Merrill Lynch received inquiries regarding CA
23 registrations from a number of state securities regulators.

24 14. Because Merrill Lynch's relevant trade records were maintained in hard copy and only
25 at branch offices across the country, the multi-state investigation focused on systemic issues with
26 Merrill Lynch CA registrations and related supervisory structure instead of attempting to identify
each incidence of unregistered activity. Specifically:

- 1 a. After accepting a client order, CAs accessed the electronic trading system to enter
2 the order;
- 3 b. The CAs did not have to identify themselves during the order entry process.
4 Therefore, there is no electronic record that identifies which orders were accepted
5 by CAs;
- 6 c. Instead, Merrill Lynch maintained a daily report that recorded the identity of the
7 person who accepted and/or entered each order. However, this report was not
8 maintained electronically, and was only maintained at the branch office where the
9 order was entered. Merrill Lynch represented that this daily report was the only
10 record that could identify who accepted a client order.
- 11 d. Merrill Lynch's trading system checked the registration of the FA, but did not check
12 the registration status of the person accepting the order to ensure that the person was
13 registered in the appropriate jurisdiction.

14 15. The multi-state investigation found that many CAs supported FAs registered in
15 Arkansas when the CAs were not registered in Arkansas as agents of Merrill Lynch. This
16 difference in registration status increased the possibility that CAs would engage in unregistered
17 activity.

18 16. The multi-state investigation found that certain Merrill Lynch CAs engaged in the sale
19 of securities in Arkansas at times when the CAs were not appropriately registered in Arkansas.

20 Merrill Lynch's Remedial Measures and Cooperation

21 17. As a result of the inquiries by state regulators Merrill Lynch conducted a review of its
22 CA registration practices.

23 18. Merrill Lynch's review found that as of June 30, 2008, the firm had 3,780 registered
24 CAs. Approximately 2,200, almost 60%, of those registered CAs were only registered in their
25 home state or their home state and one additional state.
26

1 19. Consistent with the fact that many Merrill Lynch CAs were only registered in one or
2 two jurisdictions, Merrill Lynch's review found incidences of trading by CAs not properly state
3 registered.

4 20. In October 2008, Merrill Lynch amended its registration policy to require that each CA
5 mirror the state registrations for the FAs that they support.¹ Merrill Lynch's Registration
6 Compliance personnel participated in calls with branch management to advise the field about this
7 requirement.

8 21. As Merrill Lynch worked on a more permanent solution, it also developed a temporary
9 report intended to identify instances where a CA's registration did not match the FA or FAs the CA
10 supported.

11 22. Between October 1, 2008 and January 28, 2009, 251 CAs registered with the Arkansas
12 Securities Department as agents of Merrill Lynch. Yet, data as of February 28, 2009, indicated that
13 significant gaps remained between the registrations of CAs and their FAs.

14 23. However, Merrill Lynch, as a compliance enhancement, also developed an electronic
15 system that will prevent a person from entering client orders from a state in which the person
16 accepting the order is not registered. Merrill Lynch began implementing this new system in June
17 2009 and fully completed implementation by December 31, 2009.²

18 24. Merrill Lynch provided timely responses and substantial cooperation in connection with
19 the regulatory investigations into this issue. Furthermore, as displayed by the corrective actions
20 described above, Merrill Lynch has acknowledged the problems associated with its CA
21 registrations and supervisory system.

22 II.

23 ¹ It should be noted that Merrill Lynch's policy required CA/FA registration mirroring prior to 2006. In 2006,
24 it amended the relevant policies and procedures to more broadly require that CAs maintain appropriate registrations.

25 ² Note that in late October, 2009, Banc of America Investment Services, Inc. ("BAIS") migrated on the
26 Central Registration Depository to Merrill Lynch, however, the trading and order entry integration will not be
completed until the third quarter of 2010. BAIS, whose policies have required sales assistants' state registration status
to mirror the FAs they serve, will continue to use its own order entry system for their existing clients until the
integration is completed.

1 CONCLUSIONS OF LAW

2 1. The Arkansas Securities Department has jurisdiction over this matter pursuant to
3 Ark. Code Ann. § 23-42-205.

4 2. Merrill Lynch's failure to establish an adequate system to monitor the registration
5 status of persons accepting client orders constitutes a violation of Ark. Code Ann. § 23-42-
6 308(a)(2)(J).

7 3. Merrill Lynch's failure to require its CAs to be registered in the appropriate
8 jurisdictions constitutes a failure to enforce its established written procedures, and is the basis for
9 assessing a fine against Merrill Lynch.

10 4. Pursuant to Ark. Code Ann. § 23-42-301(a) Merrill Lynch's sales of securities in
11 Arkansas through unregistered CAs constitute the basis for the issuance of an Order assessing a
12 fine against Merrill Lynch.

13 5. Pursuant to Ark. Code Ann. § 23-42-308, Merrill Lynch's sales of securities in
14 Arkansas through agents not registered in Arkansas constitute bases to order Merrill Lynch to cease
15 and desist engaging in the sale of securities in Arkansas through unregistered agents.

16 6. Pursuant to Ark. Code Ann. § 23-42-308(g)(1) the violations described above
17 constitute bases for the assessment of an administrative fine against Merrill Lynch.

18 7. The Arkansas Securities Department finds the following relief appropriate and in
19 the public interest.

20 III.

21 UNDERTAKINGS

1 Merrill Lynch, to any claims.

2 3. Merrill Lynch is hereby ordered to cease and desist from engaging in the sale of
3 securities in Arkansas through persons not registered with the Commissioner as agents of Merrill
4 Lynch.

5 4. Merrill Lynch is hereby ordered to pay the sum of three hundred seventy seven
6 thousand, seven hundred twenty five dollars (\$377,725.00) to the Arkansas Securities Department
7 within ten days of the date of this Order. Merrill Lynch shall pay the sum of three hundred seventy
8 seven thousand, seven hundred twenty five dollars (\$377,725.00) in two payments as follows: (1)
9 thirty seven thousand, seven hundred and seventy two dollars and fifty cents (\$37,772.50) in the
10 form of a charitable donation to the Arkansas State Fund at the Investor Protection Trust, a
11 nonprofit organization devoted to investor education; and three hundred thirty nine thousand, nine
12 hundred and fifty two dollars and fifty cents (\$339,952.50) in the form of a fine payable to the
13 Arkansas Securities Department.

14 5. Merrill Lynch shall pay up to a total of Twenty six million, five hundred sixty three
15 thousand, ninety four dollars and fifty cents (\$26,563,094.50) in fines, penalties and any other
16 monetary sanctions among the 50 states, the District of Columbia, Puerto Rico, and the U.S. Virgin
17 Islands pursuant to the calculations discussed with the multi-state working group.

18 6. However, if any state securities regulator determines not to accept Merrill Lynch's
19 settlement offer, the total amount of the payment to the State of Arkansas shall not be affected, and
20 shall remain at three hundred seventy seven thousand, seven hundred twenty five dollars (\$
21 377,725.00).

22 7. Merrill Lynch is hereby ordered to comply with the Undertakings contained herein.

23 8. This order is not intended by the Arkansas Securities Department to subject any
24 Covered Person to any disqualifications under the laws of the United States, any state, the District
25 of Columbia, Puerto Rico, or the U.S. Virgin Islands including, without limitation, any
26 disqualification from relying upon the state or federal registration exemptions or safe harbor
provisions. "Covered Person," means Merrill Lynch or any of its affiliates and their current or

1 former officers or former officers, directors, employees, or other persons that would otherwise be
2 disqualified as a result of the Orders (as defined below).

3 9. The parties admit and acknowledge that the Arkansas Securities Commissioner has
4 no authority or jurisdiction over any other state or federal agency or regulatory authority.
5 Nonetheless, the Arkansas Securities Commissioner does not intend for this Order to serve as a
6 basis for any CA's disqualification from registration exemptions or safe harbor provisions
7 contained in the following:

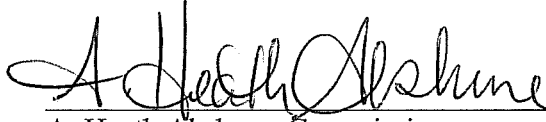
- 8 - Arkansas Securities Act, or rules or regulations thereunder;
- 9 - Federal securities laws, or the rules and regulations thereunder;
- 10 - Rules and regulations of self regulatory organizations; or
- 11 - Various states' or U.S. Territories' securities laws.

12 The Arkansas Securities Commissioner also does not intend for this Order to form a basis for the
13 disqualification of Respondents or any of their affiliates or employees from any business that they
14 are otherwise qualified or licensed to perform.

15 10. This Order shall be binding upon Merrill Lynch and its successors and assigns as
16 well as to successors and assigns of relevant affiliates with respect to all conduct subject to the
17 provisions above and all future obligations, responsibilities, undertakings, commitments,
18 limitations, restrictions, events, and conditions.

19 Dated this 10th day of May, 2010.

20 BY ORDER OF THE ARKANSAS SECURITIES
21 COMMISSIONER

22 

23 A. Heath Abshure, Commissioner

1 CONSENT TO ENTRY OF ADMINISTRATIVE ORDER BY MERRILL LYNCH

2 Merrill Lynch hereby acknowledges that it has been served with a copy of this Consent Order
3 ("Order"), has read the foregoing Order, is aware of its right to a hearing and appeal in this matter, and
4 has waived the same.

5 Merrill Lynch admits the jurisdiction of the Arkansas Securities Department neither admits nor
6 denies the Findings of Facts and Conclusions of Law contained in this Order, and consents to entry of
7 this Order by the Arkansas Securities Department as settlement of the issues contained in this Order.

8 Merrill Lynch agrees that it shall not claim, assert, or apply for a tax deduction or tax credit
9 with regard to any state, federal or local tax for any administrative monetary penalty that Merrill
10 Lynch shall pay pursuant to this Order.

11 Merrill Lynch states that no promise of any kind or nature whatsoever was made to it to induce
12 it to enter into this Order and that it has entered into this Order voluntarily.

13 Joaquin M. Sena represents that he is an Associate General Counsel and, as such, has been
14 authorized to enter into this Order for and on behalf of Merrill Lynch.

15 Dated this 26th day of April, 2010.

16 MERRILL LYNCH, PIERCE, FENNER & SMITH
17 INCORPORATED

18 By: Joaquin M. Sena
19 Joaquin M. Sena
20 Title: Associate General Counsel

21 STATE OF NEW YORK)
22)SS.:
23 COUNTY OF NEW YORK)

24 I certify that Joaquin M. Sena personally known to me, appeared before me this day and
25 acknowledged the due execution of the foregoing instrument.

26 Witness my hand and official seal, this the 26 day of April, 2010.

(Official Seal)

Marianne Bretton-Granatoor
Notary Public
My Commission expires: _____