

STATE OF ALASKA  
DEPARTMENT OF COMMERCE, COMMUNITY, AND ECONOMIC DEVELOPMENT  
DIVISION OF BANKING AND SECURITIES

In the matter of:	)	
	)	ORDER NO: 11-000815-01-S
MERRILL LYNCH, PIERCE,	)	
FENNER & SMITH INCORPORATED,	)	<b>ADMINISTRATIVE CONSENT ORDER</b>
Respondent.	)	

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WHEREAS, Merrill Lynch, Pierce, Fenner & Smith Incorporated (“Merrill Lynch”) is a broker-dealer registered in the state of Alaska, with its home office located at One Bryant Park, New York, New York 10036 and Central Registration Depository (“CRD”) number of 7691;

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;

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;

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

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 Alaska Securities Act, Alaska Statutes (“AS”) 45.55, the Administrative Procedures Act, AS 44.62 and the Alaska Administrative Code (“AAC”) 3 AAC 08 Securities Regulations with respect to this Order.

Solely for the purpose of terminating the multi-state investigations, and in settlement of the issues contained in this Order, Merrill Lynch, without admitting or denying the findings of fact or

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conclusions of law contained in this Order, consents to the entry of this Order.

NOW, THEREFORE, the Department of Commerce, Community, and Economic Development, Division of Banking and Securities (the “Division”), as administrator of the Alaska Securities Act, hereby enters this Order:

## I. FINDINGS OF FACT

1. Merrill Lynch admits the jurisdiction of the Division in this matter.

### Background on Client Associates

2. The CAs functions as sales assistants and typically provides administrative and sales support to one or more of Merrill Lynch’s Financial Advisors (“FAs”). There are different titles within the CA position, including Registered Client Associate and Registered Senior Client Associate.

3. The responsibilities of a CA specifically include:

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

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

5. Notably, FAs might have a “primary CA” and a “secondary CA.” As suggested by the designation, the customary practice is that the primary CA would handle the FA’s administrative

matters and client orders. However, if the primary CA was unavailable, the secondary CA would handle the FA's administrative matters and client orders.

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

#### Registration Required

7. Any person transacting securities business in Alaska must be registered as a broker-dealer agent, unless the person is otherwise exempt from registration. AS 45.55.980. Pursuant to the general prohibition under AS 45.55.030, a broker-dealer cannot employ an agent to accept unsolicited orders to buy or sell securities, in or from Alaska without first being registered. .

8. Pursuant to AS 45.55.920 the Division administrator may order that a broker-dealer follows the registration requirements, and impose civil penalties for violation of the Alaska Securities Act.

#### Merrill Lynch Requires Registration of Client Associates

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

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

#### Regulatory Investigations and Findings

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

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

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

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

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

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

## Merrill Lynch's Remedial Measures and Cooperation

16. As a result of the inquiries by state regulators, Merrill Lynch conducted a review of its CA registration practices.

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

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

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

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

21. Between October 1, 2008 and January 28, 2009, 125 CAs registered with Alaska as agents of Merrill Lynch. Yet, data as of February 28, 2009 indicated that significant gaps remained between the registrations of CAs and their FAs.

22. However, Merrill Lynch, as a compliance enhancement, also developed an electronic system that will prevent a person from entering client orders from a state in which the person accepting the order is not registered. This system, which enhanced Merrill Lynch's primary trading systems for bond and equities trading, was fully implemented by December 31, 2009.

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

Further, the firm has engaged in an ongoing assessment of firm processes to determine where additional changes related to the merger with Bank of America or otherwise, may enhance the firm's registration compliance program.<sup>2</sup>

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

## II. CONCLUSIONS OF LAW

1. The Division has jurisdiction over this matter pursuant to AS 45.55.905.
2. Merrill Lynch's failure to establish an adequate system to monitor the registration status of persons accepting client orders does not comply with the supervisory requirements of the FINRA (formerly NASD) Code of Conduct Rule 3010 in violation of AS 45.55.050(k).
3. Merrill Lynch's failure to require its CAs to be registered in the appropriate jurisdictions constitutes a failure to enforce its established written procedures, and failure to reasonably supervise its agents in violation of AS 45.55.060(b)(1) thus repeatedly violating the agent registration provisions of AS 45.55.030(a) and (b).
4. Merrill Lynch's sales of securities in Alaska through unregistered CAs constitute repeated violations of AS 45.55.030(a) and (b).
5. Pursuant to AS 45.55.920 , Merrill Lynch's sales of securities in Alaska through agents/ not registered in Alaska constitute bases to order Merrill Lynch to cease and desist engaging in the

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<sup>2</sup> Note that in late October, 2009, Banc of America Investment Services, Inc. ("BAIS") migrated on the CRD to Merrill Lynch, however, the trading and order entry integration was not completed until the third quarter of 2010. BAIS, whose policies have required sales assistants' state registration to mirror the FAs they serve, continued to use its own order entry system for its existing clients until the integration was completed.

sale of securities in Alaska through unregistered agents.

6. Pursuant to AS 45.55.920, the violations described above constitute bases for the assessment of a civil penalty against Merrill Lynch.

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

### III. UNDERTAKINGS

1. Merrill Lynch hereby undertakes and agrees to immediately establish and maintain a trade monitoring system that prevents any person from entering client orders that originate from jurisdictions where the person accepting the order is not appropriately registered.

2. Merrill Lynch further undertakes and agrees to file with the Division within sixty days of the date of this Order, a report describing Merrill Lynch's improvements in its ability to monitor the identity and registration status of each person who accepts a client order entered on Merrill Lynch's trading system.

### IV. ORDER

On the basis of the Findings of Fact, Conclusions of Law, and Merrill Lynch's consent to the entry of this Order,

IT IS HEREBY ORDERED:

1. This Order concludes the investigation by the Division and any other action that the Division could commence against Merrill Lynch under applicable law on behalf of Alaska as it relates to unregistered activity in Alaska by Merrill Lynch's CAs and Merrill Lynch's supervision of CA registrations during the period from January 1, 2004 through the date of this Order.

2. This Order is entered into solely for the purpose of resolving the referenced multi-state investigation, and is not intended to be used for any other purpose. For any person or entity not a party to the Order, this Order does not limit or create any private rights or remedies against Merrill Lynch including, limit or create liability of Merrill Lynch, or limit or create defenses of

Merrill Lynch, to any claims.

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

4. Merrill Lynch is hereby ordered to pay the sum of two hundred ninety five thousand, four hundred fifty dollars (\$295,450) to the State of Alaska within ten days of the date of this Order.

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

6. However, if any state securities regulator determines not to accept Merrill Lynch's settlement offer, the total amount of the payment to the State of Alaska shall not be affected, and shall remain at \$295,450.

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

8. This Order is not intended by the Division to subject any Covered Person to any disqualifications under the laws of the United States, any state, the District of Columbia, Puerto Rico, or the U.S. Virgin Islands including, without limitation, any 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 former officers or former officers, directors, employees, or other persons that would otherwise be disqualified as a result of the Orders (as defined below).

9. This Order and the order of any other State in related proceedings against Merrill Lynch (collectively, the "Orders") shall not disqualify any Covered Person from any business that they otherwise are qualified, licensed or permitted to perform under applicable securities laws 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.

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

SO ORDERED this 30<sup>th</sup> day of January, 2011.

SUSAN BELL, Commissioner  
Department of Commerce, Community, and  
Economic Development  
Division of Banking and Securities

/s/ Lorie L. Hovanec  
Lorie L. Hovanec, Director  
Division of Banking and Securities

## CONSENT TO ENTRY OF ADMINISTRATIVE ORDER BY MERRILL LYNCH

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

Merrill Lynch admits the jurisdiction of the Department of Commerce, Community, and Economic Development, Division of Banking and Securities (the “Division”), neither admits nor denies the Findings of Fact and Conclusions of Law contained in this Order, and consents to entry of this Order by the Division as settlement of the issues contained in this Order.

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

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

J. David Montague represents that he is an Associate General Counsel of Merrill Lynch and that, as such, has been authorized by Merrill Lynch to enter into this Order for and on behalf of Merrill Lynch.

Dated this 29<sup>th</sup> day of December, 2011

MERRILL LYNCH, PIERCE, FENNER & Smith  
INCORPORATED

By: /s/ J. David Montague

J. David Montague  
Associate General Counsel

STATE OF ALASKA  
DEPARTMENT OF COMMERCE, COMMUNITY, AND ECONOMIC DEVELOPMENT  
DIVISION OF BANKING AND SECURITIES  
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STATE OF NEW YORK                    )  
                                                  ) SS.:  
COUNTY OF NEW YORK                )

I certify that J. David Montague personally known to me, appeared before me this day and acknowledged the due execution of the foregoing instrument.

Witness my hand and official seal, this the     29<sup>th</sup>   day of December, 2011.

(Official Seal)

/s/ Marianne Bretton-Granatoor  
Notary Public  
My Commission expires: May 02, 2014