

BEFORE THE SECURITIES COMMISSIONER  
OF THE STATE OF DELAWARE

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4 IN THE MATTER OF: )  
5 MERRILL LYNCH, PIERCE, FENNER ) Case No. 09-9-2  
& SMITH INCORPORATED, )  
6 Respondent. ) **ADMINISTRATIVE CONSENT ORDER**  
7 )

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

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

14 Merrill Lynch has cooperated with regulators conducting the investigations by responding to  
15 inquiries, providing documentary evidence and other materials, and providing regulators with access to  
16 facts relating to the investigations; and

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

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

21 Merrill Lynch elects to waive permanently any right to a hearing and appeal under 6 Del. C.  
22 §7324. with respect to this Order; and

23 Solely for the purpose of terminating the multi-state investigations, and in settlement of the  
24 issues contained in this Order, Merrill Lynch, without admitting or denying the findings of fact or  
25 conclusions of law contained in this Order, consents to the entry of this Order.

26 NOW, THEREFORE, the Delaware Securities Commissioner ("Commissioner"), as  
administrator of the Delaware Securities Act, 6 Del. C. Ch. 73, (the "Act") hereby enters this Order:

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I.

**FINDINGS OF FACTS**

1. Merrill Lynch admits to the jurisdiction of the Commissioner in this matter.

Background on Client Associates (CA)

2. The CAs function 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. It is unlawful for any person to transact business in Delaware as a broker-dealer or agent unless the person is registered with the Commissioner. 6 Del. C. §7313(a).

1 8. Pursuant to the general prohibition under 6 Del. C. §7313(a), a person cannot accept  
2 unsolicited orders in Delaware without being registered with the Commissioner.

3 9. Pursuant to Section 7316(g) of the Act, a broker-dealer may be fined for selling securities in  
4 Delaware through agents other than registered agents.

#### 5 Merrill Lynch Requires Registration of Client Associates

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

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

#### 11 Regulatory Investigations and Findings

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

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

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

- 22 a. After accepting a client order, CAs accessed the electronic trading system to enter the  
23 order;
- 24 b. The CAs did not have to identify themselves during the order entry process. Therefore,  
25 there is no electronic record that identifies which orders were accepted by CAs;
- 26 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

1 entered. Merrill Lynch represented that this daily report was the only record that could  
2 identify who accepted a client order.

3 d. Merrill Lynch's trading system checked the registration of the FA, but did not check the  
4 registration status of the person accepting the order to ensure that the person was  
5 registered in the appropriate jurisdiction.

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

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

#### 11 Merrill Lynch's Remedial Measures and Cooperation

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

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

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

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

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

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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.

1 22. Between October 1, 2008 and January 28, 2009, 267 CAs registered with the Commissioner  
2 as agents of Merrill Lynch. Yet, data as of February 28, 2009 indicated that significant gaps remained  
3 between the registrations of CAs and their FAs.

4 23. However, Merrill Lynch, as a compliance enhancement, also developed an electronic  
5 system that will prevent a person from entering client orders from a state in which the person accepting  
6 the order is not registered. Merrill Lynch has represented to the Staff that the firm began implementing  
7 this new system in June 2009 and expects it to be fully implemented by December 31, 2009.

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

## 12 II.

### 13 CONCLUSIONS OF LAW

14 1. The Commissioner has jurisdiction over this matter. 6 Del. C. Ch. 73.

15 2. Merrill Lynch's failure to establish an adequate system to monitor the registration  
16 status of persons accepting client orders constitutes a failure to establish a reasonably designed  
17 supervisory system pursuant to 6 Del. C. §7316(a)(10).

18 3. Merrill Lynch's failure to require its CAs to be registered in the appropriate  
19 jurisdictions constitutes a failure to enforce its established written procedures, and is a basis for the  
20 issuance of an Order reprimanding; censuring; or assessing a fine against Merrill Lynch.

21 4. Pursuant to 6 Del. C. §7313(a), Merrill Lynch's sales of securities in Delaware through  
22 unregistered CAs constitute bases for the issuance of an Order reprimanding, censuring, assessing a  
23 fine against Merrill Lynch.

24 5. Pursuant to 6 Del. C. §7313(a) and §7325, Merrill Lynch's sales of securities in  
25 Delaware through sales representatives not registered in Delaware constitute bases to order Merrill  
26 Lynch to cease and desist engaging in the sale of securities in Delaware through unregistered sales

1 representatives.

2 6. Pursuant to 6 Del. C. §7316(g), the violations described above constitute bases for the  
3 assessment of an administrative fine against Merrill Lynch.

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

5 **III.**

6 **UNDERTAKINGS**

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

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

14 3. For the period from the date of this Order through December 31, 2010, Merrill Lynch  
15 further undertakes and agrees to notify the Commissioner if it finds that any person associated with  
16 Merrill Lynch accepted a client order in Delaware without being registered, or exempt from  
17 registration, with the Commissioner as an agent of Merrill Lynch.  
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19 **IV.**

20 **ORDER**

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

23 **IT IS HEREBY ORDERED:**

24 1. This Order concludes the investigation by the Commissioner and any other action that the  
25 Commissioner could commence against Merrill Lynch under applicable Delaware law on behalf of  
26 Delaware as it relates to unregistered activity in Delaware 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.

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

6           3.       Merrill Lynch is hereby censured.

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

9           5.       Merrill Lynch is hereby ordered to pay the sum of two hundred eighty six thousand and  
10 six hundred dollars (\$286,600.00) to the State of Delaware Investor Protection Fund by delivering  
11 within ten days of the date of this Order, a check drawn on good and sufficient funds made payable to  
12 the "State of Delaware" in the amount of \$286,600.00.

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

17           7.       However, if any state securities regulator determines not to accept Merrill Lynch's  
18 settlement offer, the total amount of the payment to the State of Delaware shall not be affected, and  
19 shall remain at \$286,600.00.

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

21           9.       This order is not intended by the Commissioner to subject any Covered Person to any  
22 disqualifications under the laws of the United States, any state, the District of Columbia, Puerto Rico,  
23 or the U.S. Virgin Islands including, without limitation, any disqualification from relying upon the state  
24 or federal registration exemptions or safe harbor provisions. "Covered Person," means Merrill Lynch  
25 or any of its affiliates and their current or former officers or former officers, directors, employees, or  
26 other persons that would otherwise be disqualified as a result of the Orders (as defined below).

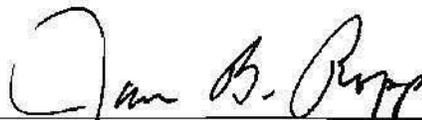
          10.       This Order and the order of any other State in related proceedings against Merrill Lynch  
(collectively, the "Orders") shall not disqualify any Covered Person from any business that they

1 otherwise are qualified, licensed or permitted to perform under applicable securities laws of Delaware  
2 and any disqualifications from relying upon this state's registration exemptions or safe harbor  
3 provisions that arise from the Orders are hereby waived.

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

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9 Dated this 20<sup>th</sup> day of October, 2009.

10 BY ORDER OF

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15 James B. Kopp  
16 Delaware Securities Commissioner for the State of Delaware  
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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 has  
4 waived the same.

5                   Merrill Lynch admits the jurisdiction of the Delaware Securities Commissioner neither admits nor  
6 denies the Findings of Facts and Conclusions of Law contained in this Order, and consents to entry of this  
7 Order by the Delaware Securities Commissioner 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 with  
9 regard to any state, federal or local tax for any administrative monetary penalty that Merrill Lynch shall  
10 pay pursuant to this Order.

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

13                   Teresa M. Brenner represents that she is Associate General Counsel of Merrill Lynch and that, as  
14 such, has been authorized by Merrill Lynch to enter into this Order for and on behalf of Merrill Lynch.

15                   Dated this 14<sup>th</sup> day of October, 2009.

16                   MERRILL LYNCH, PIERCE, FENNER & SMITH  
17 INCORPORATED

18                   By: Teresa M. Brenner  
19                   Teresa M. Brenner  
20                   Title: Associate General Counsel

21                   STATE OF NORTH CAROLINA

22                   COUNTY OF MECKLENBURG

23                   I certify that Teresa M. Brenner personally known to me, appeared before me this day and  
24 acknowledged the due execution of the foregoing instrument.

25                   Witness my hand and official seal, this the 14th day of October, 2009.

26                   (Official Seal)



27                   James E. Dwiggin  
28                   James E. Dwiggin, Notary Public  
29                   My Commission Expires: May 2nd, 2010.