MEMO# 21164

May 21, 2007

Broker-Dealer Settles SEC Charges Relating to Best Execution

[21164]

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TO: COMPLIANCE MEMBERS No. 17-07
EQUITY MARKETS ADVISORY COMMITTEE No. 29-07
SEC RULES MEMBERS No. 51-07
SMALL FUNDS COMMITTEE No. 17-07 RE: BROKER-DEALER SETTLES SEC CHARGES RELATING TO BEST EXECUTION

The Securities and Exchange Commission has settled an administrative enforcement action against a registered broker-dealer ("Respondent") relating to fraud charges for its failure to provide best execution to certain retail orders for over-the-counter securities. [1] The Respondent neither admitted nor denied the findings.

The Order found that from October 2001 through December 2004, the Respondent embedded undisclosed mark-ups and mark downs on certain retail OTC orders processed by its automated market-making system and delayed the execution of other retail OTC orders for which the Respondent had an obligation to execute without hesitation. As a result of this conduct, the Order found that the Respondent failed to provide best execution to more than 1.2 million executions (3.7 percent of its OTC executions) valued at approximately $8 billion. The SEC's press release, quoting an associate regional director, noted that "[t]he duty of best execution is not a static concept, but rather one that evolves with changes in technology."

Based on the alleged conduct, the Order found that the Respondent willfully violated Section 15(c)(1)(A) of the Securities Exchange Act of 1934, which prohibits broker-dealers from using manipulative, deceptive, or fraudulent devices or contrivances to effect securities transactions.

The Commission censured the Respondent and ordered it to comply with remedial undertakings, including retaining an independent compliance consultant to conduct a comprehensive review and provide a report on its automated retail order handling practices. The Commission also ordered the Respondent to pay $7.9 million in disgorgement, interest, and penalties, which will be distributed according to a distribution plan developed by the Respondent in conjunction with the Commission.

Jane G. Heinrichs
Associate Counsel

endnotes

[1] *See In the Matter of Morgan Stanley & Co. Incorporated,* SEC Release No. 34-55726, Admin. Proc. File No. 3-12631 (May 9, 2007) ("Order"). The Order is available on the SEC's website at http://sec.gov/litigation/admin/2007/34-55726.pdf and the accompanying press release is available at http://sec.gov/news/press/2007/2007-91.htm.