

MEMO# 20885

February 20, 2007

NASD Sanctions Three Broker-Dealers for Violations of the Non-Cash Compensation Rules that Occurred in 2001-2004

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TO: COMPLIANCE MEMBERS No. 9-07

BROKER/DEALER ADVISORY COMMITTEE No. 13-07

SALES FORCE MARKETING COMMITTEE No. 2-07

SEC RULES MEMBERS No. 22-07

SMALL FUNDS MEMBERS No. 17-07 RE: NASD SANCTIONS THREE BROKER-DEALERS FOR VIOLATIONS OF THE NON-CASH COMPENSATION RULES THAT OCCURRED IN 2001-2004

The NASD has announced the settlement of charges against three broker-dealers involving the payment of non-cash compensation. [\[1\]](#) Though each of the broker-dealers neither admitted nor denied the NASD's allegations, the NASD found that they violated the following rules between 2001-2004:

- NASD Rules 2850(I)(5) (investment company securities) and 2820(g)(4) (variable annuities) governing the payment of non-cash compensation;
- NASD Rule 3010, relating to supervision; and
- Rule 2110, which requires members to adhere to high standards of commercial honor and just and equitable principles of trade.

As a result of the NASD finding that the above violations occurred, each of the broker-dealers agreed to be censured and pay a fine. The amounts of their respective fines and the NASD's finding against each of the broker-dealers are briefly summarized below.

The NASD's Findings

According to the first AWC, in connection with educational meetings involving overnight stays of attendees, the broker-dealer held "spouse breakfasts" and permitted spouses to attend expensive dinners at premier New York City restaurants. The broker-dealer also provided the following entertainment at various points during the relevant period: a Renaissance Festival; a Street Festival, complete with a caricature artist, live music during dinner, and a private concert with a singer; a choice of golf, fishing, or horseback riding followed by dinner with live entertainment; a theme dinner at the Hollywood Entertainment Museum; an elaborate rock-and-roll party that included recreating the "Whisky-A-Go-Go" bar and use of makeup artists "to make attendees 'look the part;'" and theater and sporting events. This broker-dealer also permitted attendees to spend a Saturday night on location at Half Moon Bay, California so they could engage in group entertainment during the day. While the broker-dealer attempted to justify this Saturday night stay based on the potential cost savings, the NASD found the firm's analysis was flawed because it relied on a fully-refundable airfare rather than the less expensive non-refundable fares the firm actually booked. This broker-dealer agreed to a fine of \$475,000.

In the second AWC, the NASD found that the broker-dealer paid for meal and group transportation expenses for guests of registered representatives who attending training and education meetings held between 2001-2004. According to the AWC, two of these meetings were held three weeks after the firm was advised by its outside counsel that such payments were contrary to the NASD's rules. While this broker-dealer had policies during the relevant period that prohibited the payment of "guest expenses," the firm's employees applied the policies only to air travel and lodging expenses and permitted the payment of guest meal and ground transportation expenses. This broker-dealer agreed to a find of \$175,000.

In the third AWC, the NASD found that, until May 2001, the broker-dealer's written non-cash compensation policies and procedures did not address, and in effect permitted, paying for or reimbursing entertainment expenses incurred in connection with training and education meetings. In May 2001, a memo was distributed to all employees of the broker-dealer prohibiting the firm from paying or reimbursing brokers for costs of golf outings, tours, or other entertainment during training or educational meetings. The memo did not, however, address payment of or reimbursement for guest meal expenses. The NASD found that this broker-dealer provided and paid for entertainment for attendees and their guests in conjunction with six educational fora held from January-July 2001. This entertainment took the form of tickets to Broadway plays and tours of the United Nations. The firm also paid for meal expenses "at prominent New York City restaurants" for guests of registered representatives who attended ten fora during the relevant period. This broker-dealer agreed to a fine of \$100,000.

As noted above, in addition to finding that each of the broker-dealers violated the non-cash compensation rules, the NASD also found each to have violated the NASD's supervisory rule

(Rule 3010) and Rule 2110, requiring members to observe just and equitable principles of trade.

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[Attachment](#)

[\[1\]](#) See attached copies of: *Scudder Distributors, Inc.*, NASD Letter of Acceptance, Waiver and Consent (“AWC”) No. EAF0401460001 (Dec. 29, 2006); *Putnam Retail Management Limited Partnership*, NASD AWC No. SAF2004016601 (Dec. 27, 2006); and *AllianceBernstein Investments, Inc.* NASD AWC No. SAF2004016001 (Dec. 27, 2006). This memo’s summary of these settlements follows the order in which these AWCs are listed in this footnote.

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