

MEMO# 20262

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NASD Settles with Four Broker-Dealers Relating to Directed Brokerage

©2006 Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice. [20262] August 9, 2006 TO: BROKER/DEALER ADVISORY COMMITTEE No. 28-06 BROKER/DEALER ASSOCIATE MEMBERS No. 4-06 COMPLIANCE MEMBERS No. 34-06 SEC RULES MEMBERS No. 70-06 SMALL FUNDS MEMBERS No. 56-06 RE: NASD SETTLES WITH FOUR BROKER-DEALERS RELATING TO DIRECTED BROKERAGE NASD has announced the settlement of charges against four affiliated broker-dealers in connection with the receipt of directed brokerage in exchange for preferential treatment for certain mutual fund companies.¹ In settling each of these matters, the broker-dealers neither admitted nor denied NASD's allegations or findings. NASD found that from 2001 through 2003, the broker-dealers provided marketing benefits to 10 mutual fund complexes that participated in the shelf-space (or revenue sharing) program, known as the Strategic Partners Program ("Program"). These benefits, most of which were not provided to non- Program participants, included increased access to the broker-dealers' retail brokerage sales forces, placement of materials on the broker-dealers' websites, identification as a Program participant on the broker-dealers' intranet websites, direct links to the websites of the participating fund companies, waiver of ticket charges for retail brokerage sales of participants' funds, and other marketing opportunities. NASD further found that mutual funds paid the broker-dealers millions of dollars to participate in the Program. Eight of the ten participating fund complexes paid a portion of their fees by directing approximately \$25.7 million in mutual fund portfolio brokerage commissions to the broker-dealers, despite the fact that none of the firms executed any trades for the fund complexes. The remaining two funds paid their fees in cash. ¹ See NASD Fines Four ING Broker-Dealers \$7 Million for Directed Brokerage Violations (press release issued by NASD, Aug. 9, 2006), available at http://www.nasd.com/PressRoom/NewsReleases/2006NewsReleases/NASDW_017110; In re Financial Network Investment Corporation, Inc., ING Financial Partners, Inc., Multi-Financial Securities Corporation, Inc., PrimeVest Financial Services, Inc., NASD Letter of Acceptance, Waiver and Consent, No. EAF0400760002 (2006). ² According to NASD, the broker-dealers violated, among other rules, NASD Conduct Rule 2830(k), which prohibits member firms from favoring the sales of shares of particular mutual funds on the basis of brokerage commissions received by the firm. The rule is also designed to ensure that execution of portfolio transactions is guided by the principle of "best execution" and not by other considerations. NASD censured the broker-dealers and imposed fines totaling \$7 million.

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