FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER, AND CONSENT
NO. 2017053437701

TO: Department of Enforcement
Financial Industry Regulatory Authority (FINRA)

RE: Merrill Lynch, Pierce, Fenner & Smith Incorporated (Respondent)
Member Firm
CRD No. 7691

Pursuant to FINRA Rule 9216, Respondent Merrill Lynch, Pierce, Fenner & Smith Inc. submits this Letter of Acceptance, Waiver, and Consent (AWC) for the purpose of proposing a settlement of the alleged rule violations described below. This AWC is submitted on the condition that, if accepted, FINRA will not bring any future actions against Respondent alleging violations based on the same factual findings described in this AWC.

I.

ACCEPTANCE AND CONSENT

A. Respondent hereby accepts and consents, without admitting or denying the findings and solely for the purposes of this proceeding and any other proceeding brought by or on behalf of FINRA, or to which FINRA is a party, prior to a hearing and without an adjudication of any issue of law or fact, to the entry of the following findings by FINRA:

BACKGROUND

Merrill Lynch has been a FINRA member since 1937. The firm is a full-service broker-dealer that is headquartered in New York, New York. Merrill Lynch employs approximately 30,500 registered representatives in approximately 4,200 branch offices.

RELEVANT DISCIPLINARY HISTORY

On August 29, 2012, Merrill Lynch entered into an AWC through which it consented to findings that it violated NASD Rules 3010 and 2110, and FINRA Rule 2010, for failing to "maintain an adequate supervisory system and written procedures to monitor [Unit Investment Trusts] transactions" and failing to reasonably supervise a registered representative that was "recommending unsuitable short-term transactions" in Unit Investment Trusts and Closed End Funds between October 2006 and February 2009.[1]

OVERVIEW

From January 2011 through December 2015, Merrill Lynch failed to establish and maintain a supervisory system that was reasonably designed to achieve compliance with

[1] *Merrill Lynch, Pierce, Fenner & Smith Inc.*, Case No. 2009018601702 (AWC 2012).

FINRA's suitability rule as it pertains to early rollovers of UITs. Merrill Lynch therefore violated NASD Rule 3010 (for conduct before December 1, 2014), FINRA Rule 3110 (for conduct on or after December 1, 2014), and FINRA Rule 2010.

FACTS AND VIOLATIVE CONDUCT

A. Unit Investment Trusts

A Unit Investment Trust (UIT) is a SEC-registered investment company that offers investors shares or "units" in a fixed portfolio of securities in a one-time public offering. A UIT terminates on a specified maturity date, often after 15 or 24 months, at which point the underlying securities are sold and the resulting proceeds are paid to the investors. Generally, a UIT's portfolio is not actively managed between the trust's inception and its maturity date.

UIT sponsors typically offer UIT product lines in successive "series," with the offering periods for new series usually coinciding with the maturity date of prior series. Successive series of UITs often have the same or similar investment objectives and investment strategies as the prior series, even if the portfolio of securities held by the UIT changes from series to series.

UITs impose a variety of upfront sales charges. For example, during the relevant period, a typical 24-month UIT contained three separate charges: (1) an initial sales charge, which was generally 1% of the purchase price; (2) a deferred sales charge, which was generally up to 2.5% of the offering price; and (3) a creation and development fee (C&D fee), which was generally 0.5% of the offering price.[2] If the proceeds from the sale of a UIT were "rolled over" to fund the purchase of a new UIT, UIT sponsors often waived the initial sales charge, but still applied the deferred sales charge and C&D fee.[3]

A registered representative who recommended the sale of a customer's UIT before its maturity date and used the sale proceeds to purchase a new UIT would cause the customer to incur greater sales charges than if the customer had held the UIT until maturity. For example, a hypothetical customer who purchased a 24-month UIT and held it until maturity would have paid a sales charge of about 3.95%. However, if after six months, the customer rolled over the UIT into a new UIT, he or she would have paid an additional 2.95% in sales charges. And, if the customer repeatedly rolled over the existing UIT into a new UIT every six months, he or she would have paid total sales charges of approximately 12.8% over a two-year period.

Because of the long-term nature of UITs, their structure, and their costs, short-term trading of UITs may be unsuitable.

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[2] In addition to these charges, most UITs charged annual operating expenses that were paid to the sponsor out of the assets of the UIT.

[3] The deferred sales charge and C&D fee are generally charged during months three through six of the UIT. After those charges are paid, typically by month six, there are no sales charges applied for the life of the UIT.

B. Merrill Lynch Failed to Reasonably Supervise Short-Term Trading of UITs

FINRA Rule 3110 and its predecessor, NASD Rule 3010, require that each member firm establish and maintain a supervisory system, and establish, maintain, and enforce written supervisory procedures (WSPs), that are reasonably designed to supervise the activities of each registered representative, registered principal, and other associated person of the firm and achieve compliance with applicable securities laws and regulations, and with applicable NASD and FINRA rules. A violation of FINRA Rule 3110 or NASD Rule 3010 is also a violation of FINRA Rule 2010.

FINRA Rule 2111 and its predecessor, NASD Rule 2310, require member firms or their associated persons to have a reasonable basis to believe that a recommended securities transaction is suitable for the customer, based on the information obtained through the reasonable diligence of the firm or associated person. A firm's or associated person's reasonable diligence must provide the firm or associated person with an understanding of the potential risks and rewards associated with the recommended security.

Between January 1, 2011 and December 31, 2015, Merrill Lynch executed approximately $32 billion in UIT transactions across more than 185,000 accounts. The $32 billion in UIT transactions included approximately $2.5 billion in transactions in which UITs were sold more than 100 days before their maturity dates and some or all of the proceeds were used to purchase one or more new UITs (early UIT rollovers). In approximately $389 million of these early UIT rollover transactions, some or all of the proceeds were used to purchase a subsequent series of the same UIT, often with the same or similar investment objectives and strategies as the prior series (early series to series rollovers).

During the relevant period, Merrill Lynch's WSPs recognized that UITs are "generally intended as long-term investments" and therefore provided that representatives, as a general matter, should not solicit short-term trading of UITs because of "sales practice concerns." The WSPs also required "oversight" of short-term UIT transactions to "avoid unnecessary costs incurred to clients in fees and commissions." Moreover, a document that a market surveillance and monitoring specialist circulated to Merrill Lynch's surveillance team stated that 24-month UITs "should probably be held for at least 15 months" and that 15-month UITs should "probably be held for at least one year." That same guidance also specified that representatives should not solicit early series to series rollovers.

Nonetheless, Merrill Lynch did not establish a supervisory system that was reasonably designed to identify certain early UIT rollovers. The firm used automated reports that flagged UIT sales within 120 days of the end of the offering period, *i.e.*, approximately seven months after the UIT was first issued, as well as representatives who, within the preceding month, executed three or more UIT sales within four months of purchase. But the firm did not have any report that identified when a representative recommended an early rollover of a UIT that had been held for more than seven months. Merrill Lynch also did not have any report that identified when representatives recommended patterns of early UIT rollovers after the initial seven-month period.

As such, the firm failed to detect that on thousands of occasions during the relevant period, its representatives recommended potentially unsuitable early series to series rollovers. The firm failed to detect thousands of other occasions when its representatives repeatedly recommended other potentially unsuitable early UIT rollovers, even if not series to series, which caused customers to pay unnecessary sales charges. For example, during the relevant period, a representative at Merrill Lynch recommended approximately 75 early UIT rollovers, the majority of which were held between 4.5 and 9 months, and the firm's automated reports did not flag any of the rollovers.

Collectively, these early UIT rollovers may have caused customers to pay $8,437,223.38 in sales charges that they would not have incurred had they held the UITs until their maturity dates.

Since the relevant period, Merrill Lynch has enhanced its controls relevant to the UIT business, including by implementing new automated reports to identify patterns of UIT liquidations prior to maturity and by prohibiting early series to series rollovers.

Therefore, Merrill Lynch violated NASD Rule 3010, FINRA Rule 3110, and FINRA Rule 2010.[4]

B. Respondent also consents to the imposition of the following sanctions:

- a censure;
- a fine of $3,250,000; and
- restitution to the customers listed on Attachment A in the total amount of $8,437,223.38, plus interest as further described below.

Respondent agrees to pay the monetary sanction upon notice that this AWC has been accepted and that such payment is due and payable. Respondent has submitted an Election of Payment form showing the method by which it proposes to pay the fine imposed.

Respondent specifically and voluntarily waives any right to claim an inability to pay, now or at any time after the execution of this AWC, the monetary sanction imposed in this matter.

Restitution is ordered to be paid to the customers listed on Attachment A to this AWC in the total amount of $8,437,223.38, plus interest at the rate set forth in Section 6621(a)(2) of the Internal Revenue Code, 26 U.S.C. § 6621(a)(2), from December 31, 2015 until the date this AWC is accepted by the National Adjudicatory Council (NAC).

[4] FINRA Rule 3110 superseded NASD Rule 3010 on December 1, 2014.

A registered principal on behalf of Respondent shall submit satisfactory proof of payment of restitution and prejudgment interest (separately specifying the date and amount of each paid to each customer listed on Attachment A) or of reasonable and documented efforts undertaken to effect restitution. Such proof shall be submitted by email to EnforcementNotice@FINRA.org from a work-related account of the registered principal of Respondent. The email must identify Respondent and the case number and include a copy of the check, money order, or other method of payment. This proof shall be provided by email to EnforcementNotice@FINRA.org no later than 120 days after the date of the notice of acceptance of the AWC.

If for any reason Respondent cannot locate any customer identified in Attachment A after reasonable and documented efforts within 120 days after the date of the notice of acceptance of the AWC, or such additional period agreed to by FINRA in writing, Respondent shall forward any undistributed restitution and interest to the appropriate escheat, unclaimed property, or abandoned property fund for the state in which the customer is last known to have resided. Respondent shall provide satisfactory proof of such action to FINRA in the manner described above, within 14 calendar days of forwarding the undistributed restitution and interest to the appropriate state authority.

The imposition of a restitution order or any other monetary sanction in this AWC, and the timing of such ordered payments, does not preclude customers from pursuing their own actions to obtain restitution or other remedies.

Restitution payments to customers shall be preceded or accompanied by a letter, not unacceptable to FINRA, describing the reason for the payment and the fact that the payment is being made pursuant to a settlement with FINRA and as a term of this AWC.

The sanctions imposed in this AWC shall be effective on a date set by FINRA.

II.

WAIVER OF PROCEDURAL RIGHTS

Respondent specifically and voluntarily waives the following rights granted under FINRA's Code of Procedure:

A. To have a complaint issued specifying the allegations against it;

B. To be notified of the complaint and have the opportunity to answer the allegations in writing;

C. To defend against the allegations in a disciplinary hearing before a hearing panel, to have a written record of the hearing made, and to have a written decision issued; and

D. To appeal any such decision to the NAC and then to the U.S. Securities and Exchange Commission and a U.S. Court of Appeals.

Further, Respondent specifically and voluntarily waives any right to claim bias or prejudgment of the Chief Legal Officer, the NAC, or any member of the NAC, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including its acceptance or rejection.

Respondent further specifically and voluntarily waives any right to claim that a person violated the ex parte prohibitions of FINRA Rule 9143 or the separation of functions prohibitions of FINRA Rule 9144, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including its acceptance or rejection.

III.

OTHER MATTERS

Respondent understands that:

A. Submission of this AWC is voluntary and will not resolve this matter unless and until it has been reviewed and accepted by the NAC, a Review Subcommittee of the NAC, or the Office of Disciplinary Affairs (ODA), pursuant to FINRA Rule 9216;

B. If this AWC is not accepted, its submission will not be used as evidence to prove any of the allegations against Respondent; and

C. If accepted:

1. this AWC will become part of Respondent's permanent disciplinary record and may be considered in any future action brought by FINRA or any other regulator against Respondent;

2. this AWC will be made available through FINRA's public disclosure program in accordance with FINRA Rule 8313;

3. FINRA may make a public announcement concerning this agreement and its subject matter in accordance with FINRA Rule 8313; and

4. Respondent may not take any action or make or permit to be made any public statement, including in regulatory filings or otherwise, denying, directly or indirectly, any finding in this AWC or create the impression that the AWC is without factual basis. Respondent may not take any position in any proceeding brought by or on behalf of FINRA, or to which FINRA is a party, that is inconsistent with any part of this AWC. Nothing in this provision affects Respondent's testimonial obligations or right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party.

D. Respondent may attach a corrective action statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. Respondent understands that it may not deny the charges or make any statement that is inconsistent with the AWC in this statement. This statement does not constitute factual or legal findings by FINRA, nor does it reflect the views of FINRA.

The undersigned, on behalf of Respondent, certifies that a person duly authorized to act on Respondent's behalf has read and understands all of the provisions of this AWC and has been given a full opportunity to ask questions about it; that Respondent has agreed to the AWC's provisions voluntarily; and that no offer, threat, inducement, or promise of any kind, other than the terms set forth in this AWC and the prospect of avoiding the issuance of a complaint, has been made to induce Respondent to submit this AWC.

June 4, 2021
Date

Mark L. Keene
Merrill Lynch, Pierce, Fenner & Smith, Inc.
Respondent

Print Name: Mark L. Keene

Title: Associate General Counsel

Reviewed by:

Matthew T. Martens
Counsel for Respondent
Wilmer Cutler Pickering Hale and Dorr LLP
1875 Pennsylvania Avenue, NW
Washington, DC 20006

D. Respondent may attach a corrective action statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. Respondent understands that it may not deny the charges or make any statement that is inconsistent with the AWC in this statement. This statement does not constitute factual or legal findings by FINRA, nor does it reflect the views of FINRA.

The undersigned, on behalf of Respondent, certifies that a person duly authorized to act on Respondent's behalf has read and understands all of the provisions of this AWC and has been given a full opportunity to ask questions about it; that Respondent has agreed to the AWC's provisions voluntarily; and that no offer, threat, inducement, or promise of any kind, other than the terms set forth in this AWC and the prospect of avoiding the issuance of a complaint, has been made to induce Respondent to submit this AWC.

June 4, 2021
Date

Merrill Lynch, Pierce, Fenner & Smith, Inc.
Respondent

Print Name: Mark L. Keene

Title: Associate General Counsel

Reviewed by:

Matthew T. Martens
Counsel for Respondent
Wilmer Cutler Pickering Hale and Dorr LLP
1875 Pennsylvania Avenue, NW
Washington, DC 20006

Accepted by FINRA:

Signed on behalf of the
Director of ODA, by delegated authority

June 25, 2021
Date

Melissa J. Turitz
Director
FINRA
Department of Enforcement
581 Main St., Suite 710
Woodbridge, NJ 07095