



15 Broker-Dealer Firms Settle SEC Charges Involving Violative Practices in the Auction Rate Securities Market

Firms Ordered to Cease and Desist and to Pay Over \$13 Million in Penalties

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Washington, D.C., May 31, 2006 - Today the Securities and Exchange Commission announced the institution of proceedings against 15 broker-dealer firms for engaging in violative practices in the \$200 billion plus auction rate securities market. Auction rate securities are municipal bonds, corporate bonds or preferred stocks with interest rates or dividend yields that are periodically re-set through Dutch auctions. Simultaneously with the institution of the proceedings, the firms, which neither admit nor deny the findings in the order, consented to the entry of an SEC cease-and-desist order providing for censures, undertakings, and more than \$13 million in penalties.

The SEC, in determining the structure of the settlement and the size of the penalties, considered the amount of investor harm and the firms' conduct in the investigation to be factors that mitigated the serious and widespread nature of the violations. In particular, the firms voluntarily disclosed the practices they engaged in to the SEC, upon the staff's request for information, which allowed the SEC to conserve resources.

Linda Chatman Thomsen, Director of the SEC's Division of Enforcement, said, "This matter highlights both the industry-wide violations that existed in the auction rate securities market and the benefits to firms that cooperate with the SEC to quickly address problems. This case signals that the Commission is willing to take measured sanctions when broker-dealers are cooperative with the SEC in curing industry-wide violations and there is relatively modest investor harm."

The SEC order finds that, between January 2003 and June 2004, each firm engaged in one or more practices that were not adequately disclosed to investors, which constituted violations of the securities laws. The violative conduct included

- allowing customers to place open or market orders in auctions;
- intervening in auctions by bidding for a firm's proprietary account or asking customers to make or change orders in order to
- prevent failed auctions, to set a "market" rate, or to prevent all-hold auctions;
- submitting or changing orders, or allowing customers to submit or change orders, after auction deadlines;

- not requiring certain customers to purchase partially-filled orders even though the orders were supposed to be irrevocable;
- having an express or tacit understanding to provide certain customers with higher returns than the auction clearing rate; and
- providing certain customers with information that gave them an advantage over other customers in determining what rate to bid.

Some of these practices had the effect of favoring certain customers over others, and some had the effect of favoring the issuer of the securities over customers, or vice versa. In addition, since the firms were under no obligation to guarantee against a failed auction, investors may not have been aware of the liquidity and credit risks associated with certain securities. By engaging in these practices, the firms violated Section 17(a)(2) of the Securities Act of 1933, which prohibits material misstatements and omissions in any offer or sale of securities.

The SEC order (1) censures each firm; (2) requires each firm to cease and desist from committing or causing any violations and future violations of Section 17(a)(2) of the Securities Act; (3) requires each firm to pay a penalty; (4) requires each firm to provide certain disclosures of its material and current auction practices and procedures; and (5) requires each firm, not later than six months after the date of the order, to have its CEO or general counsel certify that it has implemented procedures that are reasonably designed to prevent and detect violations in the auction rate securities area.

The order requires the respondents to pay the following penalties based upon their relative market share and conduct: Bear, Stearns & Co., Inc., Citigroup Global Markets, Inc., Goldman Sachs & Co., J.P. Morgan Securities, Inc., Lehman Brothers Inc., Merrill Lynch, Pierce, Fenner & Smith Incorporated, Morgan Stanley & Co. Incorporated/ Morgan Stanley DW Inc., and RBC Dain Rauscher Inc. - \$1,500,000 each; and A.G. Edwards & Sons, Inc., Morgan Keegan & Company, Inc., Piper Jaffray & Co., SunTrust Capital Markets Inc., and Wachovia Capital Markets, LLC - \$125,000 each. Banc of America Securities LLC is required to pay \$750,000 rather than \$1,500,000 based on the quality of its self-monitoring capabilities in the auction rate securities area.

The Commission's investigation is continuing as to other entities that participate in the auction rate securities market.

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▶ Additional materials: [Administrative Proceeding 33-8684](#)

<http://www.sec.gov/news/press/2006/2006-83.htm>
