FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. 20100229712

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

RE: Merrill Lynch Professional Clearing Corp., CRD No. 16139, and
Merrill Lynch, Pierce, Fenner & Smith Incorporated, CRD No. 7691, Respondents

Pursuant to FINRA Rule 9216 of FINRA's Code of Procedure, Respondents submit 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 Respondents alleging violations based on the same factual findings described herein.

I.

ACCEPTANCE AND CONSENT

A. Merrill Lynch Professional Clearing Corp. ("MLPRO") and Merrill Lynch, Pierce, Fenner & Smith Incorporated ("MLPFS") hereby accept and consent, 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

MLPRO, a Delaware corporation with its principal executive offices in New York City, has been registered as a broker-dealer with the Securities & Exchange Commission ("SEC") and FINRA since 1985. MLPRO also became registered as an Equities Trading Permit Holder with NYSE Arca, Inc. in 1977. MLPRO is also a fully guaranteed subsidiary of MLPFS. MLPRO provides prime brokerage, securities financing, and clearing and settlement services to broker-dealers, introducing broker-dealers and other professional trading entities on a fully-disclosed basis. MLPRO is also a market maker on several U.S. listed options exchanges. MLPRO has approximately 210 employees including approximately 170 registered representatives.

MLPFS is a Delaware corporation with its principal executive offices in New York City. It has been a registered broker-dealer with the SEC since 1959 and FINRA since 1937. MLPFS is a wholly-owned subsidiary of NB Holdings Corporation and, since January 1, 2009, an indirect wholly-owned subsidiary of Bank of America Corporation. MLPFS is a global investment banking and multi-service brokerage firm that provides retail brokerage, corporate and investment banking services, wealth management, and

commercial lending services. MLPFS has approximately 43,497 employees including approximately 31,784 registered representatives.

Because MLPRO and MLPFS are both FINRA registered broker dealers, FINRA has jurisdiction over each.

RELEVANT DISCIPLINARY HISTORY

MLPFS

In March 2012, MLPFS entered into a Stipulation of Facts and Consent to Penalty with NYSE Amex LLC in which it stipulated to findings that, among other things, it violated Regulation SHO ("Reg SHO") Rule 203(b)(3) by failing to close out 22 fail-to-deliver positions in 4 separate securities that existed between 14 days to 50 days, and violated Amex Rule 320 by failing to implement and maintain adequate procedures of supervision and control, including a separate system for follow-up and review, reasonably designed for compliance with Reg SHO Rule 203(b)(3). MLPFS consented to a sanction consisting of a censure and a $50,000 fine.

OVERVIEW

Between approximately July 1, 2008 through July 2012, MLPRO failed to establish, maintain and enforce adequate supervisory systems and procedures, including in some instances written supervisory procedures, that were reasonably designed to ensure compliance with applicable securities laws and regulations including Regulation SHO, the 2008 Emergency Orders issued by the SEC and anti-money laundering requirements.

From the inception of Rule 204T of Regulation SHO in September 2008 through at least July 2012 ("FTD Relevant Period"), MLPRO failed to close out its fail-to-deliver ("FTD") positions, resulting from a failure in its Intercompany Settlement Process ("ISP") to transfer its clearance and settlement obligations to its affiliated broker-dealer, MLPFS, by purchasing or borrowing securities of like kind and quantity as required by Rule 204T(a) and 204(a) of Regulation SHO. During this period, MLPRO also failed to put in place supervisory systems or procedures, including written supervisory procedures that addressed the requirements of Rule 204 to timely close out FTD positions by purchasing or borrowing securities of like-kind and quantity or the requirement to notify its clients and refrain from effecting or accepting from its clients short sales in securities in which it had an aged FTD position.

Between approximately July 1, 2008 to December 31, 2008, MLPRO also failed to establish supervisory systems and procedures, including written supervisory procedures, that were reasonably designed to ensure compliance with applicable securities laws and rules by dozens of direct market access, sponsored access and naked access customers who traded on US Exchanges using a Firm provided market participant identifier ("MPID"). MLPRO's failure to establish adequate supervisory systems and procedures potentially facilitated these clients' ability to violate various rules and regulations across multiple exchanges.

From at least July 1, 2008 through August 2011, Merrill Lynch, Pierce, Fenner & Smith ("MLPFS") failed to establish, maintain and enforce adequate supervisory systems and procedures, including in some instances written supervisory procedures, that were reasonably designed to ensure compliance with applicable securities laws and regulations including Regulation SHO, Emergency Orders issued by the SEC, customer reserve, and record retention requirements of the Securities Exchange Act of 1934 ("Exchange Act") and anti-money laundering requirements.

From at least September 2008 through at least March 2011, MLPFS failed to establish, maintain and enforce adequate supervisory systems and procedures, including written supervisory procedures, that were reasonably designed to ensure compliance with the requirements of Rule 204 of Regulation SHO by allocating its Continuous Net Settlement ("CNS") FTD positions based on its broker-dealer clients' short positions and without also considering which clients contributed to those positions.

In addition, from September 2008 through August 2011 M LPFS failed to establish, maintain and enforce adequate supervisory systems and procedures, including written supervisory procedures, reasonably designed to ensure compliance with the requirements of Rules 204T(b) and (c) and 204(b) and (c) to notify its clients when it had an aged FTD position in a given security and to refrain from effecting or accepting from its clients short sales in securities in which it had an aged FTD position.

MLPRO and MLPFS also failed to establish, maintain and enforce adequate supervisory systems and procedures, including written supervisory procedures that were reasonably designed to surveil the activities of certain of its direct market access, naked access and sponsored access clients for the purpose of detecting and reporting, where appropriate, suspicious and/or manipulative trading.

MLPRO's failure to have in place adequate supervisory systems and procedures resulted in violations of certain provisions of Regulation SHO, the SEC-issued July and September 2008 Emergency Orders, the record keeping requirements of Section 17(a) of the Exchange Act, and the anti-money laundering requirements of NASD Rule 3011(a).

MLPFS failed to establish and implement adequate supervisory processes and procedures, including written supervisory procedures concerning the requirements of Rule 204T and Rule 204 of Regulation SHO. MLPFS also violated the SEC-issued July and September 2008 Emergency Orders, customer reserve and financial filing requirements of Sections 15a and 17a of the Exchange Act, and anti-money laundering requirements of NASD Rule 3011(a).

FACTS AND VIOLATIVE CONDUCT

VIOLATIONS OF REGULATION SHO

Effective September 7, 2004, the SEC adopted 17 CFR Part 42 ("Regulation SHO" or "Reg SHO") under the Exchange Act and designated January 3, 2005, as the commencement date for compliance. On September 17, 2008, the SEC issued an emergency order announcing the creation of new temporary rule 204T,[1] which imposed "enhanced delivery requirements on sales of all equity securities . . . ." In pertinent part, temporary Rule 204T required that a broker dealer deliver securities on long and short sales by settlement date; and that a broker dealer with a FTD resulting from a long or short sale, close out the FTD by no later than the beginning of regular trading hours on the settlement day following settlement date of the transaction.

Effective October 17, 2008, the SEC adopted Rule 204T of Regulation SHO on a temporary basis.[2] On July 31, 2009, Rule 204 of Regulation SHO made permanent Rule 204T, with some modifications.[3] Both Rule 204T and Rule 204 imposed various requirements, including, among other things, that broker dealers: (i) deliver securities on long and short sales by settlement date; (ii) close out FTD positions for short sales on the morning of T+4 by borrowing or purchasing securities of like kind and quantity; and (iii) close out FTD positions for long sales on the morning of T+6 by purchasing securities of like-kind and quantity. In addition, Rule 204 permitted the close out of FTD positions for long sales on the morning of T+6 by borrowing securities of like kind and quantity.

Rule 204T(d) and Rule 204(d) allow a participant of a registered clearing agency to allocate a portion of its FTD position to another registered broker-dealer for which it cleared or from which it received trades for settlement, based on such broker-dealer's short position. The SEC releases accompanying the issuance of Rules 204T and 204 clarified that allocations may be made to other broker-dealers "whose trading activities have caused the [FTD] position provided the allocation is reasonable."

NASD Rule 2110 (for conduct prior to December 15, 2008) and FINRA Rule 2010 (for conduct on or after December 15, 2008) required members, in the conduct of their business, to observe high standards of commercial honor and just and equitable principles of trade.

MLPRO failed to ensure that CNS FTD positions reflected on its books and records were closed out as required by Rules 204T(a) and 204(a) of Regulation SHO

Since the inception of Rule 204T and through at least July, 2012, in certain situations MLPRO took no action to purchase and/or borrow securities of like kind and quantity to close out FTD positions as required by Rule 204T and Rule 204.

[1] Exchange Act Release No. 58572 (September 17, 2008).
[2] Exchange Act Release No. 58773 (October 17, 2008).
[3] Exchange Act Release No. 60388 (July 31, 2009).

During the FTD Relevant Period, MLPRO had in place with MLPFS an ISP through which MLPRO transferred its settlement and clearance obligations to MLPFS. This transfer, conducted through the Correspondent Clearing Service of the National Securities Clearing Corporation, is reflected as a new transaction between MLPRO and MLPFS. The transfer of the positions from MLPRO to MLPFS was recorded on MLPRO's records as buy and sell transactions. The ISP transfer was accompanied by movements of money in corresponding amounts.

The ISP was created as a settlement tool for MLPRO and was put in place prior to the establishment of Regulation SHO. The ISP was not designed to address the close out requirements of Reg SHO and was never altered to ensure compliance with the close out requirements of any of the versions of Rule 204, once those requirements were established.

While the majority of MLPRO's clearance and settlement obligations transferred to MLPFS through the ISP without incident, MLPRO was aware during the FTD Relevant Period that sell transactions between MLPRO and MLPFS in which the corresponding positions did not successfully or properly transfer for clearance and settlement to MLPFS often resulted in FTDs on MLPRO's books and records and at the CNS level.

Nonetheless, during the FTD Relevant Period, MLPRO took no action to purchase and/or borrow securities of like kind and quantity to close out approximately 42,000 CNS FTD positions, representing millions of shares of securities, that were reflected on its books and records during that time as was required by Reg SHO Rule 204T(a) and Rule 204(a). Instead, all actions taken by MLPRO had the single purpose of transferring MLPRO's clearance and settlement obligation to MLPFS regardless of how long a FTD remained open on MLPRO's books.

Consequently, MLPRO violated Reg SHO Rule 204T(a) (from September 18, 2008 through July 30, 2009), Reg SHO Rule 204(a) (from July 31, 2009 and thereafter), NASD Rule 2110 (for conduct prior to December 15, 2008), and FINRA Rule 2010 (for conduct on or after December 15, 2008).

SUPERVISORY VIOLATIONS RELATED TO REGULATION SHO

MLPRO failed to have adequate supervisory systems and procedures for compliance with Reg SHO Rule 204T(a) and Rule 204(a).

NASD Rule 3010(a) requires firms to "establish and maintain a system to supervise the activities of each registered representative, registered principal, and other associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable NASD rules."

NASD Rule 3010(b) requires that each member shall "establish, maintain, and enforce written procedures to supervise the types of business in which it engages and to supervise the activities of registered representatives, registered principals, and other associated

persons that are reasonably designed to achieve compliance with applicable securities laws and regulations, and with the applicable Rules of NASD."

From September 2008 through at least January 2012, MLPRO failed to have in place systems and procedures, including written supervisory policies and procedures for compliance with the close-out requirements of Rules 204T(a) and 204(a) of Regulation SHO. The written supervisory procedures enacted by the Firm in January 2012 were deficient because they allowed FTD positions to be closed out or reduced by netting fail to receive positions or segregated excess positions in the same securities and failed to require MLPRO to close-out FTD positions exclusively by purchasing or borrowing securities of like kind and quantity.

During the FTD Relevant Period, despite the fact that the ISP processes generated certain FTD positions on its books and records, the Firm failed to alter the ISP process or implement systems and procedures reasonably designed to ensure compliance with Rules 204T(a) and 204(a), including systems or procedures to ensure that its FTD positions were investigated to determine whether each was caused by a short or long sale and, if so, to borrow or buy in securities when required.

By the foregoing conduct, from September 2008 through at least July 2012, MLPRO violated NASD Rules 3010(a) and (b) and 2110 (for conduct prior to December 15, 2008) and FINRA Rule 2010 (for conduct on or after December 15, 2008).

MLPRO failed to establish adequate supervisory systems and procedures for compliance with the "notice" and "penalty box" provisions of Rules 204T(b) and (c) and 204 (b) and (c).

Rule 204T(b), and Rule 204(b) of Regulation SHO imposed a penalty on broker-dealers who failed to close out FTD positions as required. Specifically, if the broker dealer had a FTD that was not timely closed pursuant to the provisions of Rule 204T(a) and Rule 204(a) respectively, then that broker-dealer and any client or broker or dealer from which it received trades for clearance and settlement, including any market maker, was prohibited from accepting a short sale order in the equity security from another person, or effecting a short sale in the equity security for its own account, without first borrowing the security or entering into a bona-fide arrangement to borrow the security. This requirement remains in effect until the FTD position is closed out by purchasing securities of like kind and quantity and that purchase has cleared and settled. These provisions are commonly referred to as the "penalty box" provisions.

Further, Reg SHO Rule 204T(c) and Rule 204(c) require that the participant notify any broker or dealer from which it receives trades for clearance and settlement, including any market maker that would otherwise be entitled to rely on the exception provided in §242.203(b)(2)(iii): (i) that the participant has a FTD position in an equity security at a registered clearing agency that has not been closed out in accordance with the requirements of paragraph (a) of this section; and (ii) when the purchase that the

participant has made to close out the FTD position has cleared and settled at a registered clearing agency.

From September 2008 through at least April 2011, MLPRO failed to notify any clients, including broker-dealer clients from which it received trades for clearance and settlement when it had a FTD position in an equity security associated with ISP failures that had not been closed out as required by Reg SHO Rule 204T(a) and Rule 204(a). Moreover, MLPRO continued to accept short sale orders from its broker-dealer and other clients and to itself effect short sale orders in equity securities with respect to which it was in the "penalty box" without ensuring that the client had first borrowed the security or entered into a bona fide arrangement to borrow the security prior to accepting the short sale order.

For example, one of MLPRO's broker dealer sponsored access clients that traded through a service bureau provided by MLPRO entered approximately 1,351 short sale orders in at least eight securities on one day during the FTD Relevant Period, when MLPRO had an aged FTD position and with respect to which MLPRO was in the "penalty box," without first borrowing or arranging to borrow those securities.

In addition to the foregoing, MLPRO also failed to take any action to detect the entry of short sales without pre-borrows in equity securities in which it had an aged FTD due to ISP failures.

From September 2008 when Rule 204T took effect until July 2012, MLPRO's supervisory systems and procedures, including written supervisory procedures, did not provide for supervision reasonably designed to achieve compliance with Reg SHO Rules 204T(a) and 204(a), as well as compliance with the penalty box or notice requirements of Reg SHO Rules 204T(b) and (c) and 204(b) and (c).

By the foregoing conduct, from September 2008 through at least July 2012, MLPRO violated NASD Rules 3010(a) and (b) and 2110 (for conduct prior to December 15, 2008) and FINRA Rule 2010 (for conduct on or after December 15, 2008).

MLPFS failed to have adequate supervisory systems and procedures regarding its allocation methodology

As noted above, under certain circumstances Rule 204T(d) and Rule 204(d) allow a clearing firm to allocate the obligation to close out FTDs to broker-dealers that clear or settle trades through the clearing firm. From September 2008 through at least March 2011, MLPFS failed to establish and maintain systems and procedures reasonably designed to ensure compliance with Rules 204T(a) and (d) and Rules 204(a) and (d) of Regulation SHO. During this time period, MLPFS' supervisory systems and procedures, including its written supervisory procedures regarding the allocation of FTDs considered its broker-dealer clients' short positions without also considering their trading activities as stated in the Rule 204T and Rule 204 adopting releases. Specifically, during this period, MLPFS allocated its CNS FTD positions to its broker-dealer clients without

ascertaining whether the allocated broker-dealers caused or contributed to those positions.

Specifically, during this period, MLPFS employed a two-tiered methodology to address all its CNS FTD positions. Tier I consisted of MLPFS' broker-dealer clients. Tier II consisted of MLPFS' non-broker dealer clients. Under its procedures, MLPFS first allocated its FTD position in a given security to its broker-dealer clients with a short position in that security on the stock record on the settlement date the FTD arose. Allocations were done on a pro rata basis relative to the cumulative short position of all its broker-dealer clients in the subject security.

If MLPFS' CNS FTD position in a security exceeded the number of shares that could be allocated to its broker-dealer clients under its procedures, then MLPFS closed-out all other clients and proprietary accounts with a short position in the subject security on a pro rata basis relative to the cumulative non-broker-dealer clients short position on the stock record on the settlement date the FTD arose. The costs associated with closing out the short positions of MLPFS' non-broker-dealer clients were passed to those clients. MLPFS' two-tiered methodology did not also consider whether its clients contributed to the FTD position in that security.

In addition, from September 2008 through at least March 2011, MLPFS' written procedures, including its written supervisory procedures were deficient in that they were consistent with the two-tiered methodology set forth above. The foregoing resulted in a significant number of improper allocations.

Further, MLPFS maintained trading accounts for four distinct but affiliated broker-dealer entities. Since at least 2005 through at least May 2012, the Firm consolidated these four legal entities' trading account positions into one "family account" and netted the positions of the four separate broker-dealer entities to determine the net position of the family account. The Firm improperly based its allocations on the net family account position instead of separately considering the positions of the four individual broker dealer entities. The Firm made only one allocation to the family account and sent only one allocation notice. Thus, the Firm did not consider the position of each legal broker-dealer entity when allocating its FTD positions.

By netting the short positions of the four related but separate and distinct broker dealer entities when allocating its FTD positions, MLPFS' processes failed to ensure that its allocations were made to the specific entity that contributed to its FTD position as required.

Based on the foregoing, MLPFS' supervisory systems and procedures, including its written supervisory procedures regarding Rules 204T and 204 violated NASD Rules 3010(a), 3010(b) and 2110 (for conduct prior to December 15, 2008), and FINRA Rule 2010 (for conduct on or after December 15, 2008).

MLPFS failed to have adequate supervisory systems and procedures for compliance with the "notice" and "penalty box" provisions of Rules 204T(b) and (c) and 204 (b) and (c)

From at least September 2008 through at least August 2011, MLPFS did not have in place adequate systems and procedures, including written supervisory procedures, to ensure compliance with Rules 204T (b) and (c) and Rule 204 (b) and (c) of Regulation SHO. Specifically, during this time period, MLPFS' supervisory systems and procedures failed to ensure that its broker dealer clients were notified in certain situations when it had a FTD position in an equity security that had not been timely closed out pursuant to Rule 204T(a) and 204(a). In those situations, MLPFS also continued to accept short sale orders from its broker dealer and other clients and to itself effect short sale orders in equity securities with respect to which it was in the "penalty box" without ensuring that the client had first borrowed the security or entered into a bona fide arrangement to borrow the security prior to accepting the short sale order. During the referenced time period, MLPFS' supervisory systems and procedures were not reasonably designed to detect the entry of short sales without pre-borrows in equity securities in which it had an aged FTD.

Based on the foregoing, MLPFS violated NASD Rules 3010(a), 3010(b) and 2110 (for conduct prior to December 15, 2008), and FINRA Rule 2010 (for conduct on or after December 15, 2008).

VIOLATIONS OF SECTION 12(k)(4) OF THE EXCHANGE ACT

The Firms failed to comply with the July 2008 Emergency Order

On July 15, 2008, the SEC issued an emergency order (the "July Emergency Order")[4]. The July Emergency Order provided, in pertinent part that no person could effect a short sale in the publicly traded securities of certain "Substantial Financial Firms" unless such person or its agent borrowed or arranged to borrow the security or otherwise had the security available to borrow in its inventory prior to effecting such short sale. An appendix to the July Emergency Order specifically identified 19 financial firms as "Substantial Financial Firms."

The July Emergency Order was effective on Monday, July 21, 2008 through Tuesday, July 29, 2008. On Tuesday, July 29, 2008, the SEC amended the July Emergency Order. The amendment extended the effective period of the order through Tuesday, August 12, 2008 (the "July Order Period").

MLPRO and MLPFS were the originating broker-dealers for short sale orders entered by its non-broker dealer direct market access and sponsored access customers.

[4] *See* Exchange Act Rel. No. 58166, as amended by Exchange Act Rel. No. 58190 (July 18, 2008) and Exchange Act Rel. No. 58248 (July 29, 2008).

Consequently, during the July Order Period, MLPRO and MLPFS were responsible to determine that a required pre-borrow was obtained and documented for these clients' short sale orders in the Substantial Financial Firms.

MLPRO

During the July Order Period, MLPRO effected through its internal systems for its non-broker-dealer direct market access clients hundreds of short sale orders in the common stock of six Substantial Financial Firms identified in the July Emergency Order without first having borrowed or arranged to borrow shares prior to effecting such short sales. The foregoing resulted in hundreds of thousands of executed shares violative of the July Emergency Order.

During the July Order Period, MLPRO effected for two non-broker dealer sponsored access clients, less than 20 short sale orders in the common stock of five Substantial Financial Firms identified in the July Emergency Order without first having borrowed or arranged to borrow shares. The foregoing resulted in tens of thousands of executed shares violative of the July Emergency Order.

MLPFS

During the July Order Period, MLPFS released for execution or allowed to be entered for it and its non-broker dealer clients, including its sponsored access clients, hundreds of thousands of short sale orders in the securities of at least 17 Substantial Financial Firms identified in the July Emergency Order. The foregoing resulted in full or partial executions of millions of executed shares violative of the July Emergency Order.

The Firms failed to comply with the September 2008 Emergency Order

On September 18, 2008,[5] the SEC issued another Emergency Order (the "September Emergency Order") which provided, among other things, that "all persons are prohibited from short selling any publicly traded securities of any "Included Financial Firm." An appendix to the September Emergency Order specifically identified 799 financial firms as "Included Financial Firms." The September Emergency Order was effective on September 19, 2008 through October 8, 2008 (the "September Order Period").

As the originating broker dealer for short sale orders entered by its non-broker dealer direct market access and sponsored access clients, MLPRO and MLPFS were also responsible during the September Order Period to prevent the entry of short sale orders in the Included Financial Firms and the Covered Securities by these clients.

[5] *See* Exchange Act Rel. No. 58592, as amended by Exchange Act Rel. No. 58611 (Sept 21, 2008); Exchange Act Rel. No. 58723 (Oct. 2, 2008).

MLPRO

During the September Order Period, MLPRO effected through its internal systems for its non-broker dealer direct market access clients hundreds of short sale orders in the securities of 30 Included Financial Firms and Covered Securities. The foregoing resulted in the full or partial executions of hundreds of thousands of shares in violation of the September Emergency Order.

During the September Order Period, MLPRO effected for three non-broker dealer sponsored access clients less than 20 violative short sale orders in the securities of 11 Included Financial Firms and Covered Securities identified in the September Emergency Order. Although these orders were entered, they resulted in no executions.

MLPFS

During the September Order Period, MLPFS released for execution or allowed to be entered for it and its non-broker dealer clients, including direct market access and sponsored access clients, thousands of short sale orders in the securities of at least 326 Included Financial Firms identified in the September Emergency Order. The foregoing resulted in millions of executed shares in securities subject to the September Emergency Order.

By effecting short sales in the securities restricted by the July and September Emergency Orders MLPRO and MLPFS violated Section 12(k)(4) of the Exchange Act of 1934 and violated NASD Rule 2110.

The Firm failed to have adequate supervisory systems and procedures for compliance with the July and September Emergency Orders

During the July and September Order Periods, MLPFS and MLPRO failed to have in place reasonable systems, procedures and, in some instances, written policies and procedures, including WSPs, to ensure compliance with July and September Emergency Orders by its' non-broker dealer direct market access and sponsored access clients.

Inadequate Pre-Execution Controls

Regulation SHO allows for broker-dealers to create and maintain a daily list of equity securities which it deems easy to borrow ("ETB Lists"). The inclusion of securities on a firm's ETB List indicates the firm's ability to easily supply shares of the identified securities, thereby providing the reasonable grounds for a locate necessary for effecting a short sale in those securities. Short sales entered in reliance upon a firm's ETB List do not require that a separate documented locate be otherwise obtained first.

During the July and September Order Periods, MLPRO and MLPFS used and distributed to certain of its sponsored access and naked access clients ETB Lists generated by MLPFS. During this period, MLPFS' order entry, acceptance and routing systems and

MLPRO's order router were programmed to permit the routing for execution of orders for any securities on the MLPFS ETB lists. As a means to prevent the entry of short sales in the Substantial Financial Firms and Included Financial Firms during the July and September Order Periods, MLPFS attempted to remove these securities from its ETB Lists. However, the ETB Lists generated by MLPFS were ineffective in preventing short sales in the Substantial Financial Firms and the Included Financial Firms during the July and September Order Periods because those securities were not timely removed from the ETB Lists. Moreover, during the September Order Period, additions and deletions of restricted securities made daily the list of Included Financial Firms were not contemporaneously added to and deleted from MLPFS' ETB List. The foregoing rendered the ETB Lists inaccurate.

A review of 350 ETB Lists created by MLPFS during the July Order Period revealed that one or more of the Substantial Financial Firms appeared on 41 of the 350 ETB Lists reviewed. Similarly, a review of 170 ETB Lists created by MLPFS during the September Order Period revealed that one or more of the Included Financial Firms and/or Covered Securities appeared on 110 of the 170 ETB Lists reviewed.

MLPFS' and MLPRO's use and distribution of the inaccurate ETB Lists during the July and September Order Periods allowed orders in the restricted securities to be automatically routed for execution in contravention of the July and September Emergency Orders.

In addition, during the September Order Period, MLPFS, on its own and on MLPRO's behalf, placed a technology block in its systems and MLPRO's order router to prevent short sale executions in the securities of Included Financial Firms and Covered Securities. However, the technology block was ineffective in blocking the execution of short sale orders in the Included Financial Firms and Covered Securities during that period.

Although MLPFS instructed its Securities Lending Desk – used both by MLPRO and MLPFS – not to grant locates in the Included Financial Firms and Covered Securities during the September Order Period, MLPFS' Securities Lending Desk in fact granted locates in these securities during the September Order Period. For example, on September 23, 2008 and September 29, 2008, MLPFS' Securities Lending Desk granted locates in 82 and 129 Included Financial Firms respectively.

Moreover, although, MLPRO's order router was programmed to reject short sale orders if the security was not on the MLPFS ETB List, the mere entry by the client of an affirmative locate/pre-borrow indicator, typically in the form of a "Y" for yes and "N" for no, prevented the order from being rejected. Moreover, because the MLPRO order router did not interact with any MLPFS locate/pre-borrow record to determine whether MLPFS had actually provided a locate/pre-borrow, customer entries were accepted at face value without requiring the client to identify the source of the third party locate/pre-borrow and with no check on whether such had actually been granted.

Based on the foregoing, MLPFS and MLPRO lacked sufficient controls to prevent the release for execution of short sale orders violative of the July and September Emergency Orders including by its direct market access, naked access and sponsored access clients.

Inadequate Post-Trade Reviews

MLPRO and MLPFS used End-of-Day Reports to conduct post trade reviews for compliance with the July Emergency Order. However, these reports did not encompass order data and/or records of short sale orders, executed or unexecuted. Because the End-of-Day Reports referenced only positions, not transactions, and included only those accounts that had an end of day increase in its overall short position in one of the securities subject to the July Emergency Order, they were insufficient to ensure compliance with the July Emergency Order.

MLPRO relied on MLPFS to conduct post-trade reviews on its behalf for compliance with the September Emergency Order. MLPFS, however, did not conduct any post trade reviews of the trading activity of MLPRO's direct market access clients whose trades passed through MLPRO's order router or MLPRO's sponsored access clients trading through certain service bureaus for compliance with the September Emergency Order. Thus, no post-trade review of these MLPRO clients' trading was conducted for compliance with the September Emergency Order.

MLPFS' post trade reviews of certain exception reports were likewise insufficient for adequate surveillance because they either excluded transactions that were released for execution but not actually executed in violation of the Emergency Orders or they excluded short sale transactions in securities on the Firm's ETB List and short sale orders in which locate information was provided.

Lack of Written Policies and Procedures

During the September Order Period, MLPRO did not establish and maintain written policies and procedures, including written supervisory policies and procedures that addressed compliance with the September Emergency Order.

MLPFS' written policies and procedures regarding the July Emergency Order describe the above-referenced, inadequate End-of-Day Reports as the primary means to review for compliance with the July Emergency Order.

Based on the above-referenced shortcomings of the Firms' pre-execution controls, post-trade reviews and deficient policies and procedures, MLPFS and MLPRO lacked systems and procedures reasonably designed to ensure compliance with the July and September Emergency Orders. Accordingly, MLPRO and MLPFS each violated NASD Rules 3010(a) and (b) and 2110.

ANTI-MONEY LAUNDERING

NASD Rule 3011, in effect during from July 1, 2008 through December 31, 2008 (the AML Relevant Period),[6] required FINRA members to develop and implement a written AML program reasonably designed to achieve and monitor compliance with the requirements of the Bank Secrecy Act, 31 U.S.C. §5311, et seq., and the regulations promulgated thereunder. Section (a) of Rule 3011 directs member firms to establish and implement procedures reasonably designed to detect and cause the reporting of certain suspicious transactions. FINRA's predecessor NASD reminded firms in NTM 02-21 that a member firm's AMLCP must "fit its business models and needs" and "consider factors such as its size, location, business activities, the type of accounts it maintains, and the types of transactions in which its customers engage."

From July 1, 2008 through December 31, 2008 (the "AML Relevant Period"), suspicious activity monitoring for both MLPRO and MLPFS was primarily conducted through two surveillance reviews – the Mantas AML Platform and various Compliance Department reviews (the "Compliance Reviews") that served as a supplement to Mantas.

Information fed into the Mantas tool consisted of securities transactions that were executed by MLPRO or MLPFS respectively and/or cleared and settled by MLPRO or MLPFS. Thus, any client orders, including naked access and sponsored access client orders that were executed and cleared and settled away from the Firms were not subject to Mantas review.

Similarly, not all sponsored access and naked access client transactions executed away from the Firms were subject to the Compliance Reviews. In addition, during the AML Relevant Period, the trading of some MLPRO sponsored access clients was not captured at all by the Compliance Reviews, regardless of where those clients' trades were executed.

Thus, because MLPRO's and MLPFS' programs for suspicious activity monitoring failed to capture certain trading data necessary to monitor for suspicious activity, the firms failed to implement and establish procedures and internal controls reasonably designed to detect and cause the reporting of suspicious transactions in violation of NASD Rules 3011(a) and 2110 (for conduct prior to December 15, 2008) and FINRA Rule 2010 (for conduct on or after December 15, 2008).

MLPRO BOOKS AND RECORDS VIOLATIONS

The Firm failed to maintain and/or preserve for a period of at least three years records of orders for trades placed by its naked access and sponsored access clients during at least the September Order Period.

Section 17(a) of the Exchange Act and Rules 17a-3 and 17a-4 thereunder, require broker dealers to preserve for a period of not less than three years a memorandum of each

[6] NASD Rule 3011 was superseded by FINRA Rule 3310 in January 2010.

brokerage order, and of any instruction given or received for the purchase or sale of securities, whether executed or unexecuted. NASD Rule 3110(a) requires members to make, preserve and retain books and records in conformity with SEC Rules 17a-3 and 17a-4.

Prior to April 18, 2011, Enforcement requested that the Firm provide records of orders entered by its clients, including its naked access and sponsored access clients, in the Substantial Financial Firms and Covered Securities during the September Order Period. As of at least April 18, 2011, MLPRO was not in possession of order tickets for its sponsored access clients. Consequently, MLPRO did not provide order tickets or any other order information for orders placed in the securities of the Substantial Financial Firms and Covered Securities by certain of its naked access and sponsored access clients.

By the foregoing, MLPRO violated Section 17(a) of the Exchange Act and Rules 17a-3 and 17a-4 thereunder, NASD Rule 3110 (a) and FINRA Rule 2010.

MLPRO'S INADEQUATE SUPERVISORY SYSTEMS AND PROCEDURES REGARDING ITS NAKED AND SPONSORED ACCESS CLIENTS

From July 1, 2008 through at least December 31, 2008, MLPRO did not have systems and procedures in place to ensure that the electronic trading of its naked access and sponsored access clients was properly reviewed and reasonably supervised.

During this period, MLPRO had an obligation to monitor all order flows it routed to a market center regardless of whether the Firm is the order entry firm. During this time period, electronic trading data of MLPRO's sponsored access and naked access clients was received by MLPFS' Electronic Trading Desk on MLPRO's behalf. Staff of the MLPFS Electronic Support Group was charged with performing reviews of MLPRO sponsored access and naked access client electronic order flow.

From July 1, 2008 through at least December 31, 2008, MLPFS's Electronic Trading Desk did not receive records of brokerage orders or executions for certain of MLPRO's naked access clients. Further, From July 1, 2008 through at least December 31, 2008, MLPFS' Electronic Trading Desk did not receive records of brokerage orders or executions for MLPRO's sponsored access clients that traded through certain service bureaus. Consequently, from July 1, 2008 through at least December 31, 2008, MLPRO failed to establish, maintain and enforce adequate supervisory systems and procedures, including written supervisory procedures, reasonably designed to monitor the electronic trading of MLPRO's referenced sponsored access and naked access clients in violation of NASD Rules 3010(a) and 2110 (for conduct prior to December 15, 2008) and FINRA Rule 2010 (for conduct on or after December 15, 2008).

MLPFS' INACCURATE RESERVE FORMULA COMPUTATIONS AND FOCUS REPORTS

Section 15(c) of the Exchange Act authorizes the SEC to promulgate Rules relating to the financial responsibility of broker-dealers. Rule 15c3-3, known as the "customer protection rule," includes a requirement that every broker-dealer perform a weekly computation (the "reserve formula") to determine what amount, if any, the broker dealer must deposit on behalf of customers in a bank account entitled Special Reserve Bank Account for the Exclusive Benefit of Customers (the "Reserve Bank Account").

In order for such deposits to be bona fide, they cannot create overdrafts or increase existing overdrafts in the accounts from which the funds are drawn; and the broker dealers' agreement on the account from which the funds are drawn must expressly state that overdrawn amounts are unsecured loans and that the bank agrees to look only to the overdrawn account for payment.

Pursuant to Section 17(a) of the Exchange Act and Rule 17a-5 promulgated thereunder, the Firm is required to file periodic reports of financial information known as FOCUS Reports. Such reports include reserve formula computations prepared as of the month-end reporting date.

During January 2009 and through December 2009, the Firm made 13 cash deposits to its Reserve Bank Account at one bank ("Bank A") drawn from an account it held at another bank ("Bank B") that were not bona fide because (1) they created or increased an overdraft in the bank account at Bank B from which the funds were drawn and (2) the Firm's written agreement concerning the account at Bank B failed to acknowledged that withdrawals were unsecured loans or contain certain other language regarding cross liens. The exclusion of these non bona fide deposits resulted in 13 hindsight deficiencies.

Six of the above referenced 13 hindsight deficiencies occurred in connection with a month-end reserve formula computation reported in a Firm FOCUS Report filing. Thus, the Firm submitted six inaccurate FOCUS Reports in that they contained inaccurate reserve formula computations.

By the foregoing, the Firm violated Section 15(c) of the Exchange Act and Rule 15c3-3(e) thereunder, Section 17(a) of the Exchange Act and Rule 17a-5 thereunder, and FINRA Rule 2010.

In addition, by failing to have systems and procedures in place reasonably designed to ensure compliance with Sections 15(c) and 17(a) of the Exchange Act as described above, MLPFS violated NASD Rules 3010(a) and FINRA Rule 2010.

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

a. A censure; and

b. A fine in the total amount of $5 million to be paid to FINRA and NYSE Arca, Inc., of which $3.5 million of that total amount shall be paid to FINRA.

MLPFS also consents to the imposition of the following sanctions:

a. A censure;

b. A fine of $2.5 million; and

c. An undertaking requiring MLPFS, within 120 days of the issuance of a Notice of Acceptance of this AWC, to adopt and implement supervisory systems and written procedures reasonably designed to achieve compliance with the current requirements of Rule 204 of Reg SHO. MLPFS shall, within the time period specified, notify the Department of Enforcement in writing when it has adopted and implemented the supervisory systems and written procedures described above. The Department of Enforcement may, upon showing of good cause and at its sole discretion, extend the time for compliance with this provision.

Respondents agree to pay the monetary sanction upon notice that this AWC has been accepted and that such payment is due and payable. Respondents have each submitted an Election of Payment form showing the method by which each proposes to pay the respective fines imposed.

Respondents specifically and voluntarily waive any right to claim that they are unable to pay, now or at any time hereafter, the monetary sanction(s) imposed in this matter.

The sanctions imposed herein shall be effective on a date set by FINRA staff.

II.

WAIVER OF PROCEDURAL RIGHTS

Respondents specifically and voluntarily waive the following rights granted under FINRA's Code of Procedure:

A. To have a Complaint issued specifying the allegations against them;

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 National Adjudicatory Council ("NAC") and then to the U.S. Securities and Exchange Commission and a U.S. Court of Appeals.

Further, Respondents specifically and voluntarily waive 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 acceptance or rejection of this AWC.

Respondents further specifically and voluntarily waive 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

Respondents understand 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 Respondents; and

C. If accepted:

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

2. this AWC will be made available through FINRA's public disclosure program in response to public inquiries about Respondents' disciplinary record;

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

4. Respondents 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. Respondents 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 Respondents': (i) testimonial obligations; or (ii) right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party.

D. Respondents may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. Respondents understand that they 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 or its staff.

The undersigned, on behalf of the MLPRO, certifies that a person duly authorized to act on MLPRO'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 MLPRO has agreed to its provisions voluntarily; and that no offer, threat, inducement, or promise of any kind, other than the terms set forth herein and the prospect of avoiding the issuance of a Complaint, has been made to induce MLPRO to submit it.

10/21/2014
Date

Merrill Lynch Professional Clearing Corp.

By: Gary E Gilton CEO

Reviewed by:

Attorney Name
Counsel for Respondent

The undersigned, on behalf of the MLPFS, certifies that a person duly authorized to act on MLPFS' 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 MLPFS has agreed to its provisions voluntarily; and that no offer, threat, inducement, or promise of any kind, other than the terms set forth herein and the prospect of avoiding the issuance of a Complaint, has been made to induce MLPFS to submit it.

October 20, 2014
Date

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

By: T. Daniel Montague
Associate General Counsel + Senior Vice President

Reviewed by:

Attorney Name
Counsel for Respondent

Accepted by FINRA:

October 27, 2014
Date

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

Richard Chin
Chief Counsel
FINRA Department of Enforcement
One World Financial Center
200 Liberty Street
New York, NY 10281
(646) 315-7322