

NASD
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
20042000090-01

TO: Department of Market Regulation
NASD

RE: Intercoastal Financial Services Corp., Respondent
Broker-Dealer
CRD No. 45557

Pursuant to Rule 9216 of the NASD Code of Procedure, Intercoastal Financial Services Corp. ("IFSC" or the "firm") submits this Letter of Acceptance, Waiver and Consent ("AWC") for the purpose of proposing a settlement of the alleged rule violations described in Part II below. This AWC is submitted on the condition that, if accepted, NASD will not bring any future actions against IFSC alleging violations based on the same factual findings.

IFSC understands that:

1. Submission of this AWC is voluntary and will not resolve this matter unless and until it has been reviewed and accepted by NASD's Department of Market Regulation and National Adjudicatory Council ("NAC") Review Subcommittee or Office of Disciplinary Affairs, pursuant to NASD Rule 9216;
2. If this AWC is not accepted, its submission will not be used as evidence to prove any of the allegations against IFSC; and
3. If accepted:
 - a. this AWC will become part of IFSC's permanent disciplinary record and may be considered in any future actions brought by NASD or any other regulator against IFSC;
 - b. this AWC will be made available through NASD's public disclosure program in response to public inquiries about IFSC's disciplinary record;
 - c. NASD may make a public announcement concerning this agreement and the subject matter thereof in accordance with NASD Rule 8310 and IM-8310-2; and
 - d. IFSC 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 allegation in this AWC or create the impression that the AWC is without factual basis. Nothing in this provision affects IFSC's testimonial obligations or right to take legal or factual positions in litigation or other legal proceedings in which NASD is not a party.

IFSC also understands that its experience in the securities industry and disciplinary history may be factors that will be considered in deciding whether to accept this AWC. That experience and history are as follows:

IFSC has been a member of NASD since November 30, 1998, and its registration remains in effect. IFSC has the following relevant disciplinary history:

- In an AWC that became final on July 24, 2003, IFSC was censured and fined \$7,500 for violating NASD Marketplace Rules 6620(a) and 6620(a)(3), and NASD Conduct Rule 2110.
- In an AWC that became final on October 1, 2002, IFSC was fined 5,000 for a pattern or practice of late trade reporting in violation of NASD Conduct Rule 2110.

I.

WAIVER OF PROCEDURAL RIGHTS

IFSC specifically and voluntarily waives the following rights granted under NASD's Code of Procedure:

- A. To have a Formal Complaint issued specifying the allegations against IFSC;
- B. To be notified of the Formal 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, IFSC specifically and voluntarily waives any right to claim bias or prejudgment of the General Counsel, 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.

IFSC further specifically and voluntarily waives any right to claim that a person violated the ex parte prohibitions of Rule 9143 or the separation of functions prohibitions of 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.

II.

ACCEPTANCE AND CONSENT

In connection with 20042000090/MRD200341049, the staff of NASD's Department of Market Regulation (the "staff") conducted a review of IFSC's compliance with NASD Marketplace Rules 6100-6190, which are applicable to the Automated Confirmation Transaction Service ("ACT"), during the period January 2, 2003 through April 30, 2003.

In connection with 20042000199/MRD200444172, the 2004 Trading and Market Making Surveillance Examination ("2004 TMMS Exam") of IFSC, the staff reviewed the following items:¹

- Twenty-seven customer sale transactions, for compliance with NASD Rules 3110 and 3370 and SEC Rule 10a-1;
- Twenty-three proprietary sale transactions, for compliance with NASD Rule 3370 and SEC Rule 10a-1;
- Four sales in NNM securities, for compliance with NASD Rule 6180;
- One short sale in CQS securities, for compliance with SEC Rule 10a-1;
- Twenty-seven limit orders in market making securities, for compliance with NASD Rules 2110, IM-2110-2, 6440 and 2320; and SEC Rule 11Ac1-4;
- One marketable order received while holding "non-displayed" limit orders in the same security, for compliance with NASD Rule 2320;
- Twenty-seven limit orders executed in a principal or riskless principal capacity, for compliance with capacity reporting under NASD Trade Reporting and ACT rules;
- Twenty-six customer transactions in OTCBB and/or OTC equity securities, for compliance with NASD Rules 3110(b) and 2320;
- Three persons engaged in the firm's trading and market making activities from trading staff in December 2003, for compliance with NASD Registration rules;
- Fifty order/trade records prepared and maintained for the above samples, for compliance with NASD Rule 3110 and SEC Rules 17a-3 and 17a-4;
- Fifty trades reported to ACT, for compliance with NASD Trade Reporting and ACT rules;

¹ Unless otherwise noted, all such items are for trade dates December 8, 2003 through December 19, 2003.

- Twenty-seven customer trade confirmations, for compliance with SEC Rule 10b-10;
- Various documents relating to the firm's establishment and implementation of "regular & rigorous" reviews of the execution quality of orders sent to other market centers for execution during December, 2003, for compliance with NASD Rules 2320 and 3010; and
- Various documents relating to the firm's establishment and implementation of a supervisory system and written supervisory procedures in effect during December 2003, for compliance with NASD Rule 3010.

Finally, in connection with 20050000814/MRD200448983, the staff reviewed IFSC's compliance with the ACT rules during the period July 1, 2004 through September 30, 2004.

- A. IFSC hereby accepts and consents, without admitting or denying the allegations or findings, and solely for the purposes of this proceeding and any other proceeding brought by or on behalf of NASD, or to which NASD 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 NASD:

20042000090/MRD200341049 (First Trimester 2003 Trade Reporting Review)

1. IFSC failed, within 90 seconds after execution, to transmit through Nasdaq Market Center 109 last sale reports of transactions in OTC Equity securities. These transactions constitute 4% percent of the transactions reviewed that IFSC was required to report to Nasdaq Market Center during the review period
2. The conduct described in paragraph one constitutes a pattern or practice of late reporting without exceptional circumstances in violation of NASD Conduct Rule 2110.
3. IFSC failed, within 90 seconds after execution, to transmit through Nasdaq Market Center 63 last sale reports of transactions in OTC Equity securities and failed to designate through Nasdaq Market Center such last sale reports as late.
4. The conduct described in paragraph three constitutes separate and distinct violations of NASD Marketplace Rule 6620(a).
5. IFSC's supervisory system did not provide for supervision reasonably designed to achieve compliance with respect to the applicable securities laws and regulations, and the Rules of NASD, concerning trade reporting. Specifically, the firm's supervisory system did not include written supervisory procedures providing for a statement as to how the completion of the step(s) included in the written supervisory procedures should be documented.

6. The conduct described in paragraph five constitutes a violation of NASD Conduct Rules 2110 and 3010.

20042000199/MRD200444172 (2004 TMMS Exam)

7. During the period December 8, 2003 through December 19, 2003, IFSC failed to report to Nasdaq Market Center the correct symbol indicating whether the transaction was a buy, sell, sell short, sell short exempt or cross for 45 transactions in eligible securities.
8. IFSC failed to report to Nasdaq Market Center the correct symbol indicating whether the transaction was executed in a principal or agency capacity for one transaction in an eligible security.
9. The conduct described in paragraphs seven and eight constitutes separate and distinct violations of NASD Marketplace Rule 6130(d).
10. IFSC incorrectly media reported the second leg of one riskless principal transaction in a Nasdaq National Market security.
11. The conduct described in paragraph ten constitutes a violation of NASD Marketplace Rule 4632(d).
12. IFSC incorrectly media reported the second leg of one riskless principal transaction in an OTC Equity security.
13. The conduct described in paragraph 12 constitutes a violation of NASD Marketplace Rule 6620(d).
14. On six occasions during the period of December 8, 2003 through December 19, 2003, IFSC failed to contemporaneously or partially execute one customer limit order in a Nasdaq security after it traded the subject security for its own market-making account at a price that would have satisfied the customer's limit order.
15. The conduct described in paragraph 14 constitutes separate and distinct violations of NASD Conduct Rule 2110 and IM-2110-2.
16. On four occasions during the period of December 8, 2003 through December 19, 2003, IFSC failed to contemporaneously or partially execute two customer limit orders in an OTC Equity security after it traded the subject security for its own market-making account at a price that would have satisfied the customer's limit order.

17. The conduct described in paragraph 16 constitutes separate and distinct violations of NASD Conduct Rule 6541.
18. IFSC failed to indicate whether the sale of a security was long or short on the memorandum of two brokerage orders.
19. IFSC failed to show the correct time of execution on the memorandum of 27 brokerage orders.
20. IFSC failed to show the correct time of entry on the memorandum of six brokerage orders.
21. IFSC failed to show the correct price of execution on the memorandum of two brokerage orders.
22. The conduct described in paragraphs 18 through 21 constitutes separate and distinct violations of SEC Rule 17a-3 and NASD Conduct Rule 3110.
23. IFSC's supervisory system did not provide for supervision reasonably designed to achieve compliance with respect to the applicable securities laws and regulations, and the Rules of NASD, concerning 15 areas of securities regulation.² Specifically, the firm's supervisory system did not include written supervisory procedures providing for one or more of the following: (1) identification of the person(s) responsible for supervision with respect to the applicable rules; (2) a statement of the supervisory step(s) to be taken by the identified person(s); (3) a statement as to how often such person(s) should take such step(s); and (4) a statement as to how the completion of the step(s) included in the written supervisory procedures should be documented.
24. The conduct described in paragraph 23 constitutes a violation of NASD Conduct Rules 2110 and 3010.

² The specific 15 areas of regulation are: Regular & Rigorous Assessment of Quality of Markets; Limit Order Display & Quote Rule; Limit Order Protection; SEC Rule 11Ac1-6; Best Execution – Principal, Agency, Crossing, 3 Quote Rule; SEC Rule 11Ac1-5; 21(a) Issues; Trade Reporting – Riskless Principal, Trade Modifiers, Long/Short Indicator; Customer Sales – Affirmative Determination; Short Sales – Affirmative Determination (non-market making), Bid Test, Tick Test; Locked or Crossed Markets; One Percent Rule; Backing Away; OATS Clock Synchronization; and Books & Records.

20050000814/MRD200448983 (Third Quarter 2004 Trade Reporting Review)

25. During the period July 1, 2004 through September 30, 2004, IFSC failed to accept or decline in Nasdaq Market Center 124 transactions in eligible securities within twenty minutes after execution, approximately 14 percent of all transactions that IFSC had an obligation to accept or decline in Nasdaq Market Center as the OEID.
26. The conduct described in paragraph 25 constitutes separate and distinct violations of NASD Marketplace Rule 6130(b) and a violation of NASD Conduct Rule 2110.

B. IFSC also consents to the imposition, at a maximum, of the following sanctions:

A censure, a fine of \$48,000 (comprised of \$7,500 for the trade reporting violations and \$5,000 for the supervisory violations pursuant to the First Trimester 2003 Trade Reporting Review, \$5,000 for the trade reporting and ACT-reporting violations, \$5,000 for the Limit Order Protection violations, \$12,000 for the recordkeeping and maintenance violations and \$7,500 for the supervisory violations pursuant to the 2004 TMMS Exam, and \$6,000 for the trade reporting violations pursuant to the Third Quarter 2004 Trade Reporting Review), and an undertaking to revise the firm's written supervisory procedures with respect to the areas described in paragraphs five and 23. Within 30 business days of acceptance of this AWC by the NAC, a registered principal of the Respondent firm shall submit to the **COMPLIANCE ASSISTANT, LEGAL SECTION, MARKET REGULATION DEPARTMENT, 9509 KEY WEST AVENUE, ROCKVILLE, MD 20850**, a signed, dated letter, providing the following information: (1) a reference to this matter; (2) a representation that the firm has revised its written supervisory procedures to address the deficiencies described in paragraphs five and 23; and (3) the date(s) on which such revised written supervisory procedures were implemented.

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

III.

OTHER MATTERS

- A. IFSC understands that IFSC may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. IFSC understands that IFSC 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 NASD, nor does it reflect the views of NASD or its staff.**
- B. IFSC agrees to pay any monetary sanctions imposed on IFSC upon notice that this AWC has been accepted and that such payments are due and payable and has attached an Election of Payment form showing the method by which IFSC proposes to pay any fine imposed.**
- C. IFSC specifically and voluntarily waives any right to claim that IFSC is unable to pay, now or at any time hereafter, any monetary sanction imposed in this matter.**

