

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. 2008012233601**

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REGISTRATION & DISCLOSURE

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

RE: Citigroup Global Markets, Inc. – CRD No. 7059

Pursuant to NASD Rule 9216 of the FINRA Code of Procedure, Citigroup Global Markets, Inc. ("Citigroup" 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, FINRA will not bring any future actions against Citigroup alleging violations based on the same factual findings described herein.

I.

ACCEPTANCE AND CONSENT

- A. Citigroup 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

Citigroup (formerly known as Smith Barney Inc. and Salomon Smith Barney Inc.) is a wholly-owned subsidiary of Citigroup Financial Products, Inc. and indirectly a wholly-owned subsidiary of Citigroup, Inc., which is traded on the New York Stock Exchange LLC. The Firm's principal place of business is in New York, New York. The Firm is, and was during the relevant period of June 2002 to December 2007 (the "relevant period"), a FINRA member firm. The Firm provides services including investment banking, underwriting debt and equity securities and advising corporations, governments and institutions, as well as acting as a full-service global broker-dealer engaged in, among other things, retail brokerage of stocks and market making. The Firm continues to use the Smith Barney trade name for its retail brokerage services.

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OVERVIEW

During the relevant period, Citigroup violated NASD Conduct Rules 2110 and 3010 in that it failed to reasonably supervise the commissions, mark-ups, and mark-downs (collectively, "commissions") on equity and option trades. Citigroup had a standard calculated commission rate and generally did not permit its registered representatives to charge more than that amount. However, Citigroup never formally communicated the existence of this standard calculated rate or gave guidance concerning the circumstances in which it was acceptable to charge commissions that were higher than this standard calculated rate to its registered representatives or its branch or regional management. Citigroup did provide its registered representatives and branch and regional management with a Commission Calculator that automatically calculated the standard calculated rate on a prospective trade.

Citigroup's order entry system also did not block commissions that exceeded the standard calculated rate but were less than five percent. As a result, it was possible for registered representatives to charge customers commissions in excess of the Firm's standard calculated rate. Several registered representatives knowingly charged more than the standard calculated rate, including charges substantially in excess of the standard calculated rate. The Firm had inadequate policies or procedures with respect to restrictions on commission charges or with respect to factors to consider when determining if a commission should exceed the standard calculated rate.

The Firm's Compliance Department did review and adjust certain commissions that exceeded five percent, but the Firm did not communicate to the registered representative, branch management, or the customer that a commission had been reduced because it was considered to be too high. In addition, the Compliance Department did not review commissions on options trades. As a result, there was effectively no Firm-imposed limitation on the commissions a registered representative could charge for options trades. A sample of options trades revealed commissions in excess of 20 percent for a small number of option trades.

The Firm also gave no specific guidance to branch management with respect to the supervision of individual commissions. Branch management at two of the three branches investigated by Enforcement was not aware it was possible for a registered representative to charge commissions in excess of the standard calculated rate until the Firm's Compliance Department notified them of investigations of the commission practices of a registered representative at each of those branches. Branch management at all three branches did not supervise for excessive commissions on individual trades on a regular basis.

As a consequence of the Firm's inadequate supervision, during the period from April 2002 to January 2006, one registered representative, Juan Carlos Hernandez ("Hernandez") overcharged approximately 27 customers commissions that in many instances were substantially in excess of the standard calculated rate. He overcharged

one customer approximately \$1,200,000. Branch management detected and stopped Hernandez's misconduct and, in February 2006, the Firm terminated Hernandez's employment. Two other registered representatives in different branch offices also overcharged commissions on a repeated basis, but on a smaller scale. As a sanction for this conduct, Citigroup is being censured and fined \$300,000.

FACTS AND VIOLATIVE CONDUCT

During the relevant period, Citigroup had, and continues to have a standard calculated rate for commissions. In the Firm's electronic order execution system, a Commission Calculator automatically generated this standard calculated rate for prospective trades in equity securities and options based on the trading price of the security and the number of shares (or options) bought or sold. The price of the security and the amount of money involved in a transaction¹ are both listed in IM-2440 as factors relevant to consider in determining the fairness of a commission. During the relevant period, the Firm did not communicate that the Commission Calculator generated a standard calculated rate which commissions generally were not permitted to exceed or otherwise communicate the existence of a standard calculated rate. Nonetheless, it appears to have been commonly understood by Firm employees that it was improper to charge more than the standard calculated rate, absent special circumstances.

Although the system automatically generated this commission amount, until October 2007, the system permitted registered representatives to increase the commission beyond the Firm's standard calculated rate, so long as the commission was below five percent (as well as to discount the commission). During the relevant period, when a registered representative entered a commission on an equity security that was more than five percent, the system would lower that rate to the highest level the system would process (approximately 4.9 percent).² This block on trades with commissions above five percent was not entirely effective and the system occasionally processed trades with higher commissions. This block also did not apply to options trades. As a result, there was no Firm imposed restriction on the commission a registered representative could charge for an options trade.

A system within the Compliance Department reviewed certain equity trades with commissions that exceeded five percent of the principal amount and the Firm reduced the commissions on any such trades so they were below five percent of the principal amount of the trade. When the Compliance Department identified excessive commissions and reduced them, it did not inform the registered representative, branch management, or the customer of the adjustment to the account. The Compliance Department's review did not include option trades.

¹ The amount of money involved in a transaction is equal to the product of the price of the security and amount of the security purchased.

² As stated in IM-2440, firms are entitled to recover the costs incurred in handling transactions. At Citigroup, transactions with commissions of \$75 or less were exempted from this block.

The Firm also failed to have policies or procedures, pursuant to NASD IM-2440, to identify those situations that would justify commission charges in excess of the standard calculated rates. Although the Firm's system permitted commissions to exceed the standard calculated rate as long as the commissions were below five percent, there were no policies or procedures to address the circumstances when such increases were permissible or to determine the appropriateness of the higher commission. The Firm also had no related supervisory policies or procedures for its branch or regional supervisory employees and the Firm did not make such employees aware that it was possible for a registered representative to charge more than the standard calculated rate.

Although Citigroup's BOM Compliance Manual contains a reference to the need for its BOMs to be sensitive to possible indications of excessive commissions and Citigroup provided its BOMs with reports that contained information about commissions, i.e., the trade blotter and the Compliance Account Evaluation System reports, the Firm did not advise its BOMs that it was technologically possible for commissions to exceed the standard calculated rate on any type of trade, including options. Citigroup also failed to provide any guidance as to how to supervise for excessive commissions on individual trades. As a result, for most trades, it is likely that no one at the Firm was reviewing commissions on equities trades that were greater than the standard calculated rate but were less than five percent plus \$50 and no one was reviewing the commissions on options trades.

Based on extrapolation from a sample of options trades identified by the Firm, the number of trades with commissions above the standard calculated rate as a percentage of overall options trades was less than one percent. Nonetheless, the sample did reveal options trades with commissions of more than 20 percent of the principal amount of the trade.

Enforcement identified these supervisory deficiencies in connection with an investigation of Hernandez, a former registered representative at Citigroup's former branch office in San Juan, Puerto Rico.³ Hernandez engaged in a pattern of charging commissions on equity trades substantially in excess of the Firm's standard calculated commission rate that began several months after the start of his employment with the Firm in 2002 and continued until his conduct was detected and stopped by branch management and he was suspended by the Firm and then fired in early 2006. Hernandez manipulated the Firm's order entry system by entering commissions above five percent that the system reduced to just below five percent. Over the course of approximately four years, Hernandez charged approximately 27 customers commissions that were below five percent but above, and often substantially above, the Firm's standard calculated rate on approximately 1,500 trades. Approximately 20 of those customers were overcharged by at least \$1,000. The customer Hernandez overcharged the most paid commissions that exceeded the Firm's standard calculated rate by a total of approximately \$1,200,000. The customer with the second highest overcharges was overcharged approximately \$73,000. The Firm offered to reimburse all the customers and has reimbursed all those customers

³ Citigroup sold its San Juan Puerto Rico branch office in December 2007.

who signed settlement agreements. In Matter Number 2007009435601, in March 2008, Hernandez entered into, and FINRA accepted, an AWC in which Hernandez consented to findings that he violated NASD Rules 2110 and 2120 and caused a violation of NASD Rule 3070(c). Hernandez was permanently barred.

In connection with Enforcement's investigation of the commission practices and related supervisory issues of Hernandez, the Firm voluntarily reviewed a sample of trading in 50 branch offices. The Firm determined that a registered representative in another of the Firm's branch offices regularly overcharged commissions, but on a smaller scale and over a shorter period of time than Hernandez. Over the course of more than two years, from December 2004 to March 2007, this registered representative charged approximately 11 customers commissions above, and frequently substantially above, the Firm's standard calculated rate on approximately 150 trades. The Firm has reimbursed all the customers overcharged by at least \$100.

In approximately December 2007, the Firm determined that another registered representative in a third branch office engaged in a similar type of misconduct. Citigroup reviewed this registered representative's trades for the previous five years and determined that he charged approximately 63 customers in excess of the standard calculated rate by approximately \$130,000. The Firm is reimbursing all the customers overcharged by at least \$100.

In October 2007, the Firm implemented a system that blocked commissions on equities and preferred securities from exceeding its standard calculated rate and issued written guidance to BOMs and registered representatives with respect to its commission policies stating that equities and preferred securities commissions in excess of the standard calculated rate would be reduced to the standard calculated rate. Also, in October 2007, Citigroup sent a memo to its BOMs and Operations Managers stating that, effective immediately, this revised policy also applied to options trades, but that the technology required to automatically block option commissions at the standard calculated rate was under development. As an interim solution, the Firm created a weekly report to identify option trades with commissions in excess of the Firm's standard calculated rate. In December 2007, the Firm implemented a system that blocks commissions on options transactions at the Firm's standard calculated rate. Also, as of October 2007, the Firm's Compliance Department reviews any commissions in excess of the Firm's standard calculated rate, looks for patterns by registered representative and by branch involving any commissions above the standard calculated rate, and notifies branch management of any commission adjustments.

NASD Rule 3010 requires that the Firm establish and maintain a system of supervision reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable NASD Rules and that it establish, maintain, and enforce written procedures to supervise the types of business in which it engages and to supervise the activities of its registered and associated persons.

By virtue of the foregoing, Citigroup violated NASD Rules 2110 and 3010.

B. Citigroup also consents to the imposition, at a maximum, of the following sanction:

A Censure and a \$300,000 fine.

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

II.

WAIVER OF PROCEDURAL RIGHTS

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

- A. To have a Formal Complaint issued specifying the allegations against it;
- 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 National Adjudicatory Council ("NAC") and then to the U.S. Securities and Exchange Commission and a U.S. Court of Appeals.

Further, Citigroup specifically and voluntarily waives any right to claim bias or prejudice 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.

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

Citigroup 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 NASD Rule 9216;
- B. If this AWC is not accepted, its submission will not be used as evidence to prove any of the allegations against it; and
- C. If accepted:
 - 1. this AWC will become part of Citigroup's permanent disciplinary records and may be considered in any future actions brought by FINRA or any other regulator against it;
 - 2. this AWC will be made available through FINRA's public disclosure program in response to public inquiries about Citigroup's disciplinary record;
 - 3. FINRA may make a public announcement concerning this agreement and the subject matter thereof in accordance with NASD Rule 8310 and IM-8310-3; and
 - 4. Citigroup 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. Citigroup 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 Citigroup's right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party.
- D. Citigroup may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. Citigroup 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 or its staff.

Citigroup certifies that it has read and understand all of the provisions of this AWC and has been given a full opportunity to ask questions about it; that it 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 it to submit it.

8/26/08
Date

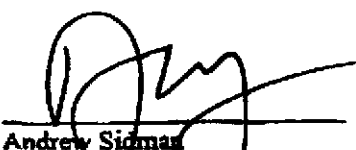
Citigroup Global Markets Inc.

By: 

Melvin Williams, Jr., Director and Counsel

Reviewed By:

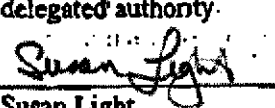
8/27/08
Date


Andrew Sigman
Counsel for Respondent
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Accepted by FINRA:

9/17/08
Date

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


Susan Light
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