

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. 2012034916901**

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

RE: Fidelity Brokerage Services, LLC ("Fidelity" or the "Firm"), Respondent
Firm CRD No. 7784

Pursuant to FINRA Rule 9216 of FINRA's Code of Procedure, Respondent 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 herein.

I.

ACCEPTANCE AND CONSENT

- A. The 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

Fidelity is a Delaware limited liability company based in Smithfield, Rhode Island. It is a large multi-service broker-dealer that provides investment and other services to its customers. Fidelity is registered with the Securities and Exchange Commission as a broker-dealer and has been a FINRA-regulated entity since January 15, 1979. It has more than 12,000 registered representatives and 249 branch offices.

RELEVANT DISCIPLINARY HISTORY

The Firm has no relevant disciplinary history.

OVERVIEW

At various times from January 2006 through September 2013, the Firm overcharged 20,663 customer accounts approximately \$2.4 million. Fidelity did not have reasonable supervisory systems or procedures to ensure that customers were charged accurate fees for accounts managed by third-party investment advisors, which resulted in erroneous and duplicate fees charged in certain

customer accounts utilizing asset-based pricing, duplicate fees in certain customer accounts managed by third-party wrap providers, and erroneous markups on certain fixed income investments. As a result, Fidelity violated NASD Rule 2110, FINRA Rule 2010,¹ and MSRB Rule G-17. The Firm voluntarily reimbursed \$2,418,155, including interest, to the disadvantaged customer accounts.²

During the same period, Fidelity failed to establish an adequate supervisory system and written procedures reasonably designed to ensure that customers received accurate disclosures relating to the Firm's Asset-Based Pricing Program for accounts managed by third-party investment advisors and to monitor billing in these fee-based brokerage accounts to ensure that customers were charged in accordance with the Firm's disclosures. Based upon the foregoing, the Firm violated NASD Rules 3010 and 2110, FINRA Rule 2010, and MSRB Rules G-17 and G-27(b).

FACTS AND VIOLATIVE CONDUCT

Relevant Rules

FINRA Rule 2010 requires that firms observe high standards of commercial honor and just and equitable principles of trade. MSRB Rule G-17 requires that in the conduct of their municipal securities or municipal advisory activities, firms deal fairly with all persons and not engage in any deceptive, dishonest, or unfair practice.

NASD Rule 3010(a) requires that each firm establish and maintain a supervisory systems and written procedures that are reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable NASD Rules. Similarly, MSRB Rule G-27(b) requires that firms establish supervisory systems and written procedures that are reasonable designed to ensure compliance with MSRB rules.

Background on the Firm's Asset-Based Pricing Program

The Firm is an introducing broker-dealer that provides brokerage services to customers, including customers who establish brokerage accounts managed by third-party independent investment advisors ("Advisors"). Through the Firm's Institutional Wealth Services Group ("IWS"), the Firm provides trading and brokerage services to Advisors and their customers. Advisors using IWS's services maintain separate investment management agreements with their customers.

¹ On December 15, 2008, FINRA Rule 2010 replaced NASD Rule 2110. Therefore, conduct occurring prior to that date is a violation of NASD Rule 2110 and conduct occurring on or after that date is a violation of FINRA Rule 2010.

² The Firm has reimbursed customer accounts for overcharges over \$10.

The Firm requires that Advisors on the IWS platform execute an Investment Advisor Representation and Indemnification Agreement, in which the Advisors state that they will disclose the schedule of brokerage fees to their customers. In addition, customers of an Advisor using IWS's services who choose to open a brokerage account with the Firm agree to a Fidelity Customer Agreement. The customer transactions are processed through the customer's brokerage accounts at the Firm.

The Firm offers Advisors and their customers asset-based and transaction-based pricing for Fidelity's brokerage services. Asset-based brokerage accounts charge a fee based on the assets held in the account rather than on a transactional basis. The Firm and the Advisor agree upon the brokerage fee schedule for the Advisor's customers and the Advisor provides notice of the brokerage fees charged by the Firm to its customers. The Firm does not make recommendations to Advisors or their customers as to which pricing model is appropriate. Advisors and their customers make that determination based on the anticipated trading activity.

In the Asset-Based Pricing ("ABP") model, a customer is charged a basis point fee according to the total "chargeable" assets in the customer's account. As per Firm sales disclosures to customers, chargeable assets include all assets in the account except for cash, cash equivalents, alternative investments, no-transaction-fee mutual funds, mutual funds with a load or sales charge, Fidelity Mutual Funds, Unit Investment Trusts ("UITs"), and international securities that settle in local currency. If ABP is selected, customers are sent a supplement to the Fidelity Customer Agreement (the "Supplement"), which describes the asset classes included as "chargeable" in the pricing calculation. Although, ABP is in lieu of transaction based fees or commissions, customers in an ABP account may pay other account fees as set forth in the Supplement. For instance, depending on the asset type or investment product, the customer may pay transaction based fees on transactions in non-chargeable assets.

Overcharges under Fidelity's Asset-Based Pricing Program

Inaccurate Classification in the ABP Program

From at least 2006 to December 2012, the Firm distributed a version of the Supplement to customers that did not accurately reflect the fees charged to customers in the ABP program. The Supplement identified mutual funds, alternative investments, certificates of deposit ("CDs"), bankers acceptance, collateralized mortgage obligations ("CMOs"), UITs, precious metals and international securities that settle in local currency as non-chargeable; however, these securities were treated by the Firm as chargeable assets to the detriment of certain customers. As a result, from January 2006 until December 2012, customers who purchased these securities were charged fees even though the

Supplement identified the securities as non-chargeable. In connection with this issue, the Firm has remediated 4,944 customer accounts a total of \$1,333,851.

ABP Program Customers Were Not Provided the Supplement and Were Overcharged

From January 2006 to December 2012, the Supplement was not provided to all ABP account customers who were charged under the ABP program. It was provided only to customers who signed the separate account network application. The separate account network application is an account application designed for clients who will have their accounts managed by an Advisor and separate account managers. The separate account network application is the only application that contained the Supplement in the account opening paperwork. Other customers who did not have a separate account structure, but who had selected ABP, should have received the Supplement, but the Firm failed to provide these customers with the Supplement. The Firm did not have a process for sending the Supplement to customers who selected ABP but did not have a separate account structure.

Additionally from January 2006 until December 2012, the Firm charged customers additional fees for certain types of asset classes including mutual funds with loads, UITs, precious metals, and international securities that settled in local currency. The Firm should not have charged customers for securities in these asset classes under ABP because they had already been charged fees when the assets were purchased. The Firm remediated 4,509 customer accounts a total of \$398,685 for any asset based account charges, including interest.

Overbilling Based on Pricing and Billing Set-Up

From January 2006 until December 2012, as a result of pricing and billing errors, the Firm overcharged 375 customer accounts approximately \$137,315 by billing customers in accordance with two fee schedules. As a result, these customers were charged duplicate fees. In light of these errors, the Firm conducted a review of fee schedules designed with both asset-based and transaction-based pricing to ensure fair and reasonable pricing to customers. The Firm determined that the pricing schedules between the Firm and the Advisors, on behalf of customers, were set up incorrectly resulting in pricing and billing errors. The Firm remediated the affected accounts approximately \$137,315, including interest.

Overcharges on Certain Fixed Income Transactions

From January 2008 through June 30, 2013, the Firm erroneously charged a markup, in addition to an asset-based fee, on fixed income transactions initiated by Advisors in accounts set up for ABP through the Firm's online fixed income trading tool. As a result, customers who purchased fixed income securities, including municipal bonds, were assessed an asset-based fee and a markup on the same transaction, resulting in an overcharge. Approximately 1,063 customer

accounts were overcharged due to this error. The Firm remediated the affected accounts approximately \$108,556, including interest.

Additionally, during the same period, the Firm improperly charged markups on block trade orders when Advisors entered block trades through the same online tool. Approximately 751 customer accounts were overcharged due to this error. The Firm remediated the affected accounts approximately \$71,679, including interest.

Overcharges on Accounts Managed by Third-Party Wrap Providers

From December 2008 through September 2013, the Firm did not properly code 497 accounts managed by third-party wrap providers³ in the Firm's systems resulting in the Firm improperly assessing a fee. For accounts managed by a third-party wrap provider, the fees are only assessed by the provider. As a result, these customer accounts were assessed duplicate charges by the Firm.

The Firm improperly overcharged 497 customer accounts. The Firm remediated the affected accounts approximately \$355,935, including interest.

Summary of Overcharging Firm Customers

In total, at various times from January 2006 through September 2013, the Firm overcharged 20,663 customer accounts approximately \$2.4 million and, as a result, violated NASD Rule 2110, FINRA Rule 2010 and MSRB Rule G-17.

Failure to Establish Systems or Procedures to Monitor Charges in Fee-Based Accounts

Failure to Send the Supplement to ABP Customers

Prior to discovering these billing problems in or about April 2012, Fidelity did not have supervisory systems or written policies or procedures to ensure that customers received accurate disclosures relating to its ABP program and to monitor fees charged in fee-based brokerage accounts. Although the Firm had supervisory controls to review the opening of an Advisor's ABP in the billing system and to monitor the monthly fluctuations in asset-based fees charged to the Advisor, these controls did not identify improper duplicate charges to the same assets in an account. The Firm did not clearly delegate responsibility for the supervision of fee-based brokerage accounts. In fact, until 2013, the Firm did not designate a supervisory principal to oversee its IWS asset based pricing program. Given the lack of adequate policies and procedures and proper delegation of

³ Third-party wrap providers are independent investment advisors that service wrap accounts. A wrap account is a managed account that is assessed a flat quarterly or annual fee that covers all administrative and advisory services provided by the investment advisor.

II.

WAIVER OF PROCEDURAL RIGHTS

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

- A. To have a Complaint issued specifying the allegations against the Firm;
- 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, the firm 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 acceptance or rejection of this AWC.

The Firm 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

The Firm 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 the Firm; and
- C. If accepted:

responsibility, the problems with overcharging Firm customers continued for seven years.

The Firm also failed to establish a reasonable supervisory system to periodically test and evaluate the fees charged to customers based on the decentralized supervisory structure of IWS and the lack of adequate policies and procedures to monitor fees charged in fee-based accounts managed by Advisors.

As a result, the Firm violated NASD Rules 3010 and 2110, FINRA Rule 2010 and MSRB Rules G-17 and G-27(b) for failing to develop and implement an adequate supervisory system and written supervisory policies and procedures to: (1) ensure that customers received accurate disclosures relating to account fees; and (2) monitor fees charged in fee-based brokerage accounts to ensure customers received accurate billing.

OTHER FACTORS

In determining the appropriate sanctions, FINRA considered the Firm's internal review through which it self-identified the violations addressed in this AWC, the remedial measures that the Firm took to correct its systems and procedures, and the Firm's voluntary efforts to remediate customers.

B. The Firm also consents to the imposition of the following sanctions:

- Censure; and
- A \$350,000 fine (\$7,153 of which pertains to the violations of MSRB Rules G-17 and G-27(b), which is proportional to the total amount of overcharges by the Firm (\$2,439,262) in relation to overcharges for the sale of municipal securities (\$49,851).

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

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

The Firm specifically and voluntarily waives any right to claim that it is unable to pay, now or at any time hereafter, the monetary sanction imposed in this matter.

1. this AWC will become part of the Firm's permanent disciplinary record and may be considered in any future actions brought by FINRA or any other regulator against the Firm;
 2. this AWC will be made available through FINRA's public disclosure program in response to public inquiries about the Firm's 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. The Firm 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. The Firm 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 the Firm's right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party.
- D. The Firm may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. The Firm 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.

The undersigned, on behalf of the Firm, certifies that a person duly authorized to act on its 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 the Firm 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 the Firm to submit it.

12-11-14
Date

Fidelity Brokerage Services, LLC, Respondent

By: 

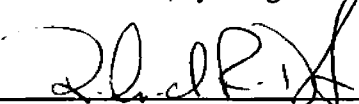
Reviewed by:


David C. Boch
Counsel for Respondent
Morgan, Lewis & Bockius LLP
One Federal Street
Boston, MA 02110-1726
T 617.951.8485, F 617.951.8736
david.boch@morganlewis.com

Accepted by FINRA:

1.15.15
Date

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


Richard R. Best, Chief Counsel
FINRA Department of Enforcement
One World Financial Center
New York, NY 10281
646.315.7308
richard.best@finra.org