

NASD
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. E1020046050-01

TO: Department of Enforcement
NASD

RE: Bear, Stearns & Co., Inc., Respondent
BD No. 79

Pursuant to Rule 9216 of NASD Code of Procedure, Bear, Stearns & Co., Inc., ("Bear Stearns" or "Respondent") 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 Respondent alleging violations based on the same factual findings.

Respondent 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 Enforcement and National Adjudicatory Council ("NAC") Review Subcommittee or Office of Disciplinary Affairs ("ODA"), 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 Respondent; and
3. If accepted:
 - a. this AWC will become part of Respondent's permanent disciplinary record and may be considered in any future actions brought by NASD or any other regulator against Respondent;
 - b. this AWC will be made available through NASD's public disclosure program in response to public inquiries about Respondent'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. Respondent 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. Nothing in this provision affects Respondent's testimonial obligations or right to take legal or factual

positions in litigation or other legal proceedings in which NASD is not a party.

Respondent 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:

Bear Stearns has been a member of NASD since December 17, 1936. Bear Stearns has no relevant formal disciplinary history with NASD, the Securities and Exchange Commission, any self-regulatory organization or any state securities regulator.

I.

WAIVER OF PROCEDURAL RIGHTS

Respondent 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 Respondent;
- 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, Respondent 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.

Respondent 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

A. 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 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:

1. Options communications are governed by NASD Conduct Rule 2220. Options are sophisticated and potentially risky products. Rule 2220 sets forth a number of detailed regulations concerning the dissemination and content of options communications. Rule 2220 requires, *inter alia*, that:
 - i. all advertisements, sales literature, and educational material issued by a member concerning options have to be approved in advance by the firm's Compliance Registered Options Principal ("CROP") or an appropriate designee;
 - ii. all options related advertisements and educational material be submitted to NASD's Advertising/Investment Companies Regulation Department or another self-regulatory organization at least ten days prior to use; and
 - iii. options communications meet certain general standards. For example, Rule 2220 requires that options communications be free of false and misleading information, contain specific risk disclosures and advise that options are not suitable for all investors.

A review of the options communications with the public distributed by Bear Stearns between January 1, 2003, and July 27, 2004, revealed violations of Rule 2220.

- a. Bear Stearns failed to submit twenty-one of twenty-three options communications for review by a CROP or an appropriate designee as required by Rule 2220.
- b. In addition, five of the twenty-three items were educational material and were not submitted to NASD or another self-regulator for review and approval prior to use by Bear Stearns as required by Rule 2220.
- c. The content of twenty-three options communications revealed additional violations of Rule 2220. In the communications:

1. Two of the items violated Rule 2220(d)(1)(A) by omitting material facts that made them false and/or misleading. For example, one piece of educational material failed to explain the components of an illustrative options calculation and failed to explain the possible outcome of the illustration if the market moved unfavorably for the transaction;
2. Six of the items violated Rule 2220(d)(1)(C) by using hedge clauses or disclaimers that attempted to disclaim responsibility for the communications. For example, some communications included a statement that "Bear Stearns makes no representation as to the accuracy or completeness of any information contained" in the document;
3. Sixteen of the items violated Rule 2220(d)(2)(A) by failing to include the required warning that options are not suitable for all investors and containing inadequate explanation of the potential risks associated with options;
4. Fourteen of the items violated Rule 2220(d)(2)(A)(i) by including a discussion of the advantages and opportunities presented by option investments without a counterbalancing disclosure regarding the risks of options investments. For example, one communication discussed strategies for using swaps and options but did not disclose risks inherent in those strategies;
5. Five of the items violated Rule 2220(d)(2)(C)(v) by failing to disclose the name and address of a person who could provide an Options Disclosure Document;
6. Seven of the items violated Rule 2220(d)(2)(D)(i) by failing to state that the supporting documentation for any claims made in the communication would be supplied upon request; and
7. One item violated Rules 2220(d)(2)(D)(ii)(a) and (c) by suggesting a certainty of future performance and failing to disclose relevant costs. For example, the communication implied that using a specific strategy would likely achieve favorable, long-term results and did not disclose costs associated with implementing the strategy.

Based on the foregoing, Bear Stearns violated NASD Conduct Rules 2220 and 2110.

2. One item of options communication, which was also a research report as defined by NASD Conduct Rule 2711, failed to define the meaning of the ratings used in the report, in violation of Rule 2711. In addition, the report failed to disclose the distribution of ratings used in the Firm's rating system and failed to provide required disclosures, or references to where the disclosures could be found, on the front page of the research report. Through this conduct, Bear Stearns violated NASD Conduct Rules 2711 and 2110.
3. Bear Stearns failed to establish, maintain, and enforce a supervisory system and procedures reasonably designed to achieve compliance with certain federal securities laws and NASD Rules. Specifically, Bear Stearns failed to consistently monitor and enforce policies and procedures relating to the content standards and principal approval of options communications with the public. This failure resulted in the violations described above. Accordingly, Bear Stearns violated NASD Conduct Rules 3010 and 2110.

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

- A censure, and
- A fine of \$150,000.

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

III.

OTHER MATTERS

- A. Respondent understands that it may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. Respondent 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 NASD, nor does it reflect the views of NASD or its staff.
- B. Respondent agrees to pay any monetary sanctions imposed upon notice that this AWC has been accepted and that such payments are due and payable and have attached an Election of Payment form showing the method by which Respondent proposes to pay any fine imposed.

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

We certify that we have read and understand all of the provisions of this AWC and have been given a full opportunity to ask questions about it, and that no offer, threat, inducement, or promise of any kind, other than the terms set forth herein, has been made to induce us to submit it.

6/27/06
Date

Bear Stearns & Co., Inc.

By: 
Michael Solender
General Counsel

Reviewed by:



Mike Wolk, Esq.
Counsel for Respondent
Foley & Lardner LLP
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Accepted by NASD:

~~July 5, 2006~~
Date

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



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