

NASD
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. EAF0301200002

RE: American Express Financial Advisors Inc., Respondent
Member Firm
(BD No. 6363)

Pursuant to Rule 9216 of NASD's Code of Procedure, Respondent American Express Financial Advisors Inc. ("AEFA") 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 it alleging violations based on the same factual findings.

AEFA 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 it; and
3. If accepted:
 - a. this AWC will become part of AEFA's permanent disciplinary record and may be considered in any future actions brought by NASD or any other regulator against it;
 - b. this AWC will be made available through NASD's public disclosure program in response to public inquiries about AEFA's disciplinary records;
 - 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. AEFA 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 AEFA's testimonial obligations or right to take legal or factual positions in litigation or other legal

proceeding in which NASD is not a party.

AEFA 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:

AEFA, which is now named Ameriprise Financial Services, Inc., has been an NASD member since 1972. Its principal offices are located in Minneapolis, Minnesota. It has no relevant formal disciplinary history.

I.

WAIVER OF PROCEDURAL RIGHTS

AEFA 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 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 NAC and then to the U.S. Securities and Exchange Commission ("SEC") and a U.S. Court of Appeals.

Further, AEFA 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.

AEFA 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. Findings

AEFA 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:

Summary

1. This matter involves violations of NASD Rule 2830(k), which prohibits member firms from favoring or disfavoring the sale or distribution of mutual fund shares on the basis of brokerage commissions received by the firm, prohibits member firms from arranging for a specific amount or percentage of brokerage commissions to be directed to the firm conditioned on the firm's sale of mutual fund shares, and prohibits member firms from recommending the purchase of mutual fund shares on the basis of brokerage commissions received or expected to be received by the firm from any source.
2. From January 2001 through December 2003, AEFA maintained two shelf space (or revenue sharing) programs in which participating mutual fund complexes paid a fee in return for preferential treatment by AEFA. That treatment included enhanced access to the firm's sales force and the posting of participant sales materials and information about the participants' funds on AEFA's internal website. Seven of the fund complexes paid their fees for participating in the programs by directing approximately \$41 million in mutual fund portfolio brokerage commissions to AEFA. Those payments violated NASD Conduct Rules 2830(k) and 2110.

AEFA's Shelf Space Programs

3. AEFA maintained a shelf space program called the Preferred Provider program during 2001 through mid-2003. In return for a fee, mutual funds participating in the Preferred Provider program were given preferential treatment over other funds that could be purchased through AEFA. The benefits included enhanced access to AEFA's sales force, including participation in national conferences and regional meetings, distribution and display of marketing materials at AEFA branches, in-office visits with registered representatives (called "advisors"), and participation of AEFA advisors in due diligence meetings organized by the participating fund

complexes.¹ In addition, AEFA promoted the funds offered by the Preferred Providers, but not other fund complexes, on its internal website. The website identified the participating complexes as Preferred Providers, and posted their sales literature and seminar outlines as well as up-to-date information about the funds and fund managers for the Preferred Providers. Finally, AEFA charged its advisors reduced sales ticket charges for the sale of Preferred Provider funds. These benefits were not available to non-participating fund complexes. AEFA sold funds offered by approximately 32 fund complexes, 24 of which were Preferred Providers.

4. In order to participate in the Preferred Provider program, mutual fund complexes were required to pay AEFA between 10 and 16 basis points of assets under management and, in some instances, an additional component based on sales. The fees, which were not shared with the advisors, were in addition to the regular sales concession paid by the fund complexes to AEFA.
5. In approximately June of 2003, AEFA replaced its Preferred Provider program with the Select Group program. Under the Select Group program, funds that paid the required fees would become either Select Group partners or Associate partners. Twelve of the former Preferred Provider fund complexes became Select Group partners, and the remaining complexes became Associate Partners.
6. Select Group partners paid 25 basis points on sales and 10-25 basis points on assets under management and received the same benefits as those available under the Preferred Provider program. In addition, AEFA gave these firms individual pages on its internal website; listed their funds above other funds on AEFA's internal and external websites; put links to their websites on AEFA's internal website; facilitated conference calls with AEFA's advisors; and coordinated the firm's marketing efforts with those of the participating fund complexes.
7. Associate partners paid the same fees as they had under the Preferred Provider program, and received some of the same benefits as the Select Group fund complexes. However, they were not provided space on AEFA's internal or external websites, could not host due diligence events for AEFA advisors, and had a lower priority than the Select Group complexes for participation in AEFA conferences and training events.

Use of Directed Brokerage Commissions

8. Mutual fund complexes generally use a variety of unaffiliated broker-

¹ This last benefit was only available to fund complexes that offered AEFA-sponsored mutual funds through their own retail affiliates.

dealers with institutional trading facilities to execute transactions in the portfolios of the mutual funds they distribute and manage. The selection of executing brokers is generally within the discretion of the mutual fund complex advisor, subject to the requirement of obtaining best execution.

9. Seven of the participants in the Preferred Provider and Select Group programs paid all or part of the fees required to participate in the program by directing brokerage commissions for portfolio transactions to AEFA. This allowed the mutual fund distributors or advisors to avoid using their own funds to pay the fees, instead using assets of the mutual funds.
10. The arrangements for paying the directed brokerage amounts were established by having the mutual fund complex enter into a clearing arrangement with a clearing firm designated or accepted by AEFA. The mutual fund complex, through its investment advisor, would direct some of its trade execution business to the designated clearing firm, identifying AEFA as the introducing broker. The clearing firm would execute mutual fund portfolio trades, retain a pre-determined portion of the commissions (generally 14-25%), and remit the rest to AEFA as the "introducing broker." AEFA would then estimate the amount of revenue sharing it expected each firm to generate over the next year, based on the prior year's results and projected growth, and provide the fund complex with a targeted amount of commission business to be generated with AEFA designated as the introducing broker. This target was set by increasing, or "grossing up," the expected revenue sharing amount by a multiplier sufficient to generate enough revenue to the clearing firm to cover both the revenue sharing obligation to AEFA and the amount retained by the clearing firm.² AEFA would monitor progress towards the goal on a quarterly basis, and would modify the target based on actual results as compared to the projections.
11. AEFA, which did not actually execute any trades for the fund complexes, received approximately \$41 million in shelf space payments through this arrangement.

Resulting Rule Violations

12. Conduct Rule 2830(k) is designed to prevent arrangements in which brokerage commissions, which are fund assets, are used to compensate member firms for selling fund shares. The rule is also designed to ensure that execution of portfolio transactions by brokerage firms is guided by the

² Thus, if a mutual fund complex which used a clearing firm that retained 20% was projected to owe AEFA \$800,000 in revenue sharing, AEFA would set its target commissions at \$1,000,000. If the fund complex met that target, the clearing firm would retain its 20% clearing fee, or \$200,000, and remit the remaining \$800,000 to AEFA.

principle of "best execution" and not by other considerations.³ The rule provides, in pertinent part:

(1) No member shall, directly or indirectly, favor or disfavor the sale or distribution of shares of any particular investment company or group of investment companies on the basis of brokerage commissions received or expected by such member from any source, including such investment company, or any covered account.

* * *

(3) No member shall ... request or arrange for the direction to any member of a specific amount or percentage of brokerage commissions conditioned upon that member's sale or promise of sales of shares of an investment company.

* * *

(6) No member shall, ... (B) recommend specific investment companies to sales personnel, or establish "recommended," "selected," or "preferred" lists of investment companies..., if such companies are recommended or selected on the basis of brokerage commissions received or expected from any source

13. As described above, AEFA received approximately \$41 million in directed brokerage commissions from mutual funds as payment for participation in AEFA's shelf space programs. The mutual fund complexes received a number of benefits by participating in the program, including enhanced access to the firm's sales force, listing on the firm's internal website as a preferred mutual fund, and placement of sales material on that website. These advantages were not available for other funds. By receiving brokerage commissions to pay for the fund complexes' participation in the firm's Preferred Provider and Select Group programs, AEFA violated NASD Conduct Rules 2830(k) and 2110.

B. Sanctions

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

1. A censure; and
2. A fine of \$12,300,000.

³ Proposed Rule Change, file SR-NASD-2004-027, 2004 SEC LEXIS 2488 (Oct. 29, 2004); *Notice to Members* 84-40

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 on it pursuant to the terms of this AWC.
- 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.

The undersigned certifies on behalf of Respondent that I 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 me to submit it.

American Express Financial Advisors Inc.

August 9, 2005
Date

By: [Signature]

Name: James M. Cruchio

Title: Chief Executive Officer

Reviewed by:

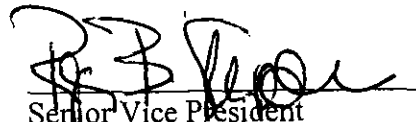
[Signature]
Counsel for Firm

Charles F. Smith

Skadden, Arps, Slate, Meagher & Flom LLP

Accepted by NASD:

11/30/05
Date



Senior Vice President

Department of Enforcement

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