

**NASD**  
**LETTER OF ACCEPTANCE, WAIVER AND CONSENT**  
**NO. EAF0400770002**

Re: Commonwealth Financial Network, Respondent  
Member Firm  
(CRD No. 8032)

Pursuant to Rule 9216 of NASD's Code of Procedure, Respondent, Commonwealth Financial Network ("CFN") 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.

CFN 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 CFN'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 CFN'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. CFN 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 CFN's testimonial obligations or

right to take legal or factual positions in litigation or other legal proceedings in which NASD is not a party.

CFN 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.

Commonwealth Financial Network has been a member of NASD since November 1979. The firm's main office is in Waltham, Massachusetts and it has 801 branch offices across the country. It has no relevant disciplinary history within the past five years.

## **I.**

### **WAIVER OF PROCEDURAL RIGHTS**

CFN 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, CFN 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.

CFN 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

CFN 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, among other things, member firms from favoring or disfavoring the sale or distribution of mutual fund shares on the basis of brokerage commissions received by the firm, 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. CFN maintained a revenue sharing (or "shelf space") program between January 2001 and December 2003 pursuant to which, in return for a fee, participating mutual fund complexes received preferential treatment from CFN in the marketing of funds. The benefits provided to the mutual fund complexes included enhanced visibility with CFN's sales force; ticket charge reimbursement; participation in firm conferences; placement of materials and links, and identification as a Strategic Partner, on the firm's intranet website; and inclusion of information about the funds in the firm's monthly newsletter. The program included six non-proprietary mutual fund complexes during the period in question. Four fund complexes paid some or all of their fees for participating in the program by directing approximately \$5.41 million in mutual fund portfolio brokerage commissions to CFN through two clearing brokers. Those payments violated NASD Conduct Rules 2830(k) and 2110.
3. In addition, CFN failed to retain e-mails for the time period required by the books and records rules. As a result, CFN violated Section 17(a) of the Securities Exchange Act of 1934, Rule 17a-4 thereunder, and NASD Conduct Rules 3110 and 2110.

#### **The Strategic Partner Program**

4. From 2001 through 2003, CFN maintained a revenue sharing program called the Strategic Partner Program. In return for a fee, participants' funds were given preferential treatment over other funds in the form of benefits that were not generally available to other funds offered by CFN.

The benefits included ticket charge reimbursement; enhanced visibility with CFN's sales force; additional speaking opportunities and prime booth space at the firm's educational and sales conferences for its representatives; a hyperlink from the firm's intranet website, CommUnityLink, to the Fund Sponsor's website; identification as a Strategic Partner on the firm's intranet website; ability to log on to the non-public side of the intranet site reserved for CFN representatives; more frequent receipt of lists of registered representatives; and inclusion of information about the funds in the firm's monthly newsletter.

5. The cost for the mutual fund complexes to participate in the Strategic Partner program varied by partner, with fees being charged either based on assets under management (up to approximately 10 basis points) or based on sales (up to 25 basis points) or based on a combination of assets under management and sales.

#### **Use of Directed Brokerage Commissions**

6. Mutual fund complexes generally use a variety of unaffiliated broker-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.
7. Four of the participants in the Strategic Partner program paid all or part of their fees for participating in the program through directed brokerage arrangements. 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.
8. In order to pay the directed brokerage amounts to CFN, the mutual fund complexes entered into an arrangement with one or both of CFN's clearing firms. Under that arrangement, the participating fund complexes directed some of their portfolio trade executions to one of the designated clearing firms, and indicated to the clearing firm that the trade was for the benefit of CFN. As part of the arrangement, CFN was deemed to be an introducing broker by the clearing firms. A portion of the commission – generally 70% – from trades made under this arrangement was then deposited into CFN's trading account.
9. CFN received approximately \$5.41 million in commissions from the fund complexes through these directed brokerage commission payments, which were made through its clearing firms. CFN did not actually execute any trades for the fund complexes.

### Resulting Rule Violations

10. 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 principle of “best execution” and not by other considerations.<sup>1</sup> 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.

\* \* \*

(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 ....

11. By virtue of the directed brokerage commission payments to CFN described above, involving the use of trading commissions to pay for participation in the Strategic Partner program, CFN violated NASD Conduct Rules 2830(k) and 2110.

### E-Mail Retention

12. Until at least April 2003, CFN failed to retain e-mails for the required time period, and thus failed to comply with the record-keeping requirements under the federal securities laws and NASD rules.
13. Beginning in 2000, CFN stored internal e-mails on monthly backup tapes, which contained all e-mails on the firm’s server when the tape was created. The monthly backup tapes were kept for one year and then reused until April 2003, when the firm stopped reusing the backup tapes. Nonetheless, the firm did retain backup tapes for March, May and September 2002. The monthly tapes failed to capture e-mails that had been “double deleted” from the system by individual users. In July 2003, CFN began using a second backup system that eliminated the ability of a user to remove e-mails from the firm’s system by double deleting.

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<sup>1</sup> Proposed Rule Change, file SR-NASD-2004-027, 2004 SEC LEXIS 2488 (Oct. 29, 2004); Notice to Members 84-40

14. Rule 17a-4(b)(4), promulgated pursuant to Section 17(a)(1) of the Securities Exchange Act of 1934, requires broker-dealers to preserve, for three years, all communications sent and received by them relating to their business. This rule applies to electronic communications. *Reporting Requirements for Broker or Dealers under the Securities Exchange Act of 1934*, Rel. No. 34-38245 (Feb. 5, 1997). Moreover, NASD Rule 3110 requires members to comply with Rule 17a-4. Thus, by failing to retain e-mails for the required period, CFN violated Section 17(a) of the Securities Exchange Act, Rule 17a-4 thereunder, and NASD Conduct Rules 3110 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 \$1,400,000.

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

III.

OTHER MATTERS

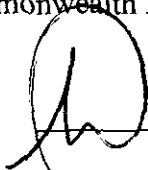
- A. Respondent understands that it may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. Respondent understands that it may not deny the charges or make any statement that is inconsistent with the AWC in this Statement. 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 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.

8/5/05  
Date

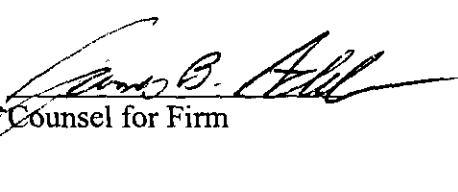
Commonwealth Financial Network

By: 

Name: Peter Wheeler

Title: President

Reviewed by:

  
Counsel for Firm

Accepted by NASD:

8/26/05  
Date

  
~~Director and Chief Counsel~~  
Department of Enforcement  
Signed on behalf of the Director of ODA,  
by delegated authority