

NASD
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. EAF0401010002

TO: Department of Enforcement
NASD

RE: Banc of America Investment Services, Inc., Respondent
BD No. 16361

Pursuant to Rule 9216 of the NASD 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 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 the firm'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.

Banc of America Investment Services, Inc. has been an NASD member since 1985. Its principal offices are located at 101 S. Tryon Street, 33rd Floor, Charlotte, North Carolina 28255. The firm has no recent relevant disciplinary history.

In connection with the sanctions imposed in this AWC, NASD has taken into account certain demonstrable steps undertaken by BAIS, shortly after NASD issued Notice to Members 03-68, to update and enhance its systems and procedures relating to fee-based accounts. NASD also considered BAIS's self-reporting of certain conduct. As discussed below, on its own initiative, BAIS identified the customers affected by the conduct and has reimbursed the customers the amounts they were charged for the transactions at issue.

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

Banc of America Investment Services, Inc. ("BAIS" or the "firm") 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:

Summary

In August 2002, BAIS began offering to its customers a fee-based brokerage account called "Portfolio Edge." Rather than paying a commission on every trade made in the account, customers utilizing Portfolio Edge accounts would pay an annual fee based on the total value of eligible assets in the account.

During the period August 2002 through September 2005 (the "review period"), BAIS failed to establish and maintain a supervisory system, including written procedures, reasonably designed to review and monitor its fee-based brokerage business. While BAIS had procedures relating to the opening of brokerage accounts generally, between August 2002 and December 2003 the firm did not have a supervisory system or written procedures requiring review of the appropriateness of Portfolio Edge accounts for its customers or requiring the monitoring of these accounts after they were opened. For instance, BAIS did not have procedures requiring an initial review or periodic reviews of customers' fee-based brokerage accounts to determine whether those accounts were appropriate for the particular customers. In addition, from August 2002 through September 2005, the firm did not have an adequate system in place to prevent Portfolio Edge accounts from being charged both a fee and a commission on certain trades. The firm also did not have an adequate system in place to ensure that accurate disclosures of the fees charged

were made to customers in connection with certain transactions in Portfolio Edge accounts. As a result, BAIS violated NASD Conduct Rules 3010 and 2110.

As a result of these deficiencies in BAIS's systems and procedures, BAIS allowed customers to open and continue in Portfolio Edge accounts without assessing whether the accounts were appropriate for the customers. Thus, certain Portfolio Edge customers either conducted no trading for an extended period of time or had accounts where the assets in the account averaged significantly below the minimum amount for an extended period of time, or both.

In addition, during the review period, BAIS used written communications regarding its Portfolio Edge account, including advertising and sales literature, that failed to comply with NASD's rules regarding communications with the public. BAIS thereby violated NASD Conduct Rules 2210 and 2110.

Background

Fee-based brokerage accounts

A fee-based brokerage account is an alternative to the traditional commission-based brokerage account. The primary difference is that a fee-based account imposes charges on assets in the account rather than on specific transactions.

In 1995, in response to concerns about potential conflicts of interest in the brokerage industry, the Securities and Exchange Commission (the "SEC") released its Report of the Committee on Compensation Practices, commonly known as the "Tully Report." This report described fee-based accounts as a "best practice" in the securities industry because it aligns the customer's and broker's interests. In this arrangement, the broker and customer both are motivated to build the assets in the customer's account. This is in contrast to the traditional commission-based account, in which there is always the temptation for the income-seeking broker to attempt to increase the trading activity in his customer's account. The report further advised that a fee-based account also may be appropriate "for investors who prefer a consistent and explicit monthly or annual charge for services received, and whose level of trading activity is moderate." The report also pointed out, however, that small and low-activity accounts could endure higher costs as a fee-based account than as a commission-based account because of the imposed fees.

As a result of regulatory initiatives by the SEC in 1999 granting a "safe harbor" from the registration requirements of the Investment Advisers Act of 1940 for broker-dealers based on the form of compensation received,¹ NASD member firms began offering customers fee-based accounts as an alternative to traditional commission-based charges for brokerage services and that trend is increasing.²

¹ See SEC Rel. No. 34-42000, Nov. 4, 1999, *Certain Broker-Dealers Deemed Not to Be Investment Advisers*.

² See SEC Rel. No. 34-50980, Jan. 6, 2005, *Certain Broker-Dealers Deemed Not to Be Investment Advisers*.

In November 2003, NASD released *Notice to Members 03-68* ("NTM 03-68"), which "remind[ed] members that they must have reasonable grounds for believing that a fee-based program is appropriate for a particular customer, taking into account the services provided, cost, and customer preferences." As noted in NTM 03-68, "[i]t generally is inconsistent with just and equitable principles of trade—and therefore a violation of Rule 2110—to place a customer in an account with a fee structure that reasonably can be expected to result in a greater cost than an alternative account offered by the member that provides the same services and benefits to the customer." Before opening a fee-based account for a customer, members must have reasonable grounds for believing that such an account is appropriate for that particular customer. NTM 03-68 stated:

[M]embers should make reasonable efforts to obtain information about the customer's financial status, investment objectives, trading history, size of portfolio, nature of securities held, and account diversification. With that and any other relevant information in hand, members should then consider whether the type of account is appropriate in light of the services provided, the projected cost to the customer, alternative fee structures that are available, and the customer's fee structure preferences. In addition, members should disclose to the customer all material components of the fee-based program, including the fee schedule, services provided, and the fact that the program may cost more than paying for the services separately.³

Firms' supervisory procedures are required to be tailored to their business. For fee-based accounts, firms should implement supervisory procedures that include a periodic review to determine whether the accounts are appropriate for their customers.

BAIS's Portfolio Edge Account

In August 2002, BAIS introduced its fee-based brokerage account called Portfolio Edge. By September 30, 2005, the firm had 11,856 Portfolio Edge accounts, holding over \$4.5 billion in assets.

During the review period, BAIS required a minimum investment of \$100,000 in eligible securities to open a Portfolio Edge account. As set forth in the Portfolio Edge customer addendum, eligible securities included stocks listed on major exchanges, unlisted stocks, preferred stocks, ADRs, mutual funds (A shares), rights & warrants, options, fixed income products, and REITS. The firm allowed customers to exclude from the fee calculation otherwise eligible assets in their account and any trades in those excluded assets were charged a commission.

³ NTM 03-68, 744.

The annual fee charged to Portfolio Edge accounts varied by the total amount and type of assets held in the account. During the review period, the rate schedule for Portfolio Edge accounts was as follows:

\$100,000-\$250,000	2.25%	1.25%	1.00%
\$250,000-\$1,000,000	1.50%	1.00%	0.75%
\$1,000,000-\$3,000,000	0.90%	0.75%	0.50%
Over \$3,000,000	0.75%	0.50%	0.50%

The firm could discount these rates, but the minimum annual fee charged to a Portfolio Edge account was \$1,500.

Violations

A. BAIS Failed to Establish and Maintain a Supervisory System, Including Written Procedures, Reasonably Designed to Review and Monitor its Fee-Based Business

NASD Conduct Rule 3010 requires member firms to establish and maintain a system, including written procedures, to supervise the activities of its registered representatives and associated persons that is reasonably designed to achieve compliance with applicable securities laws and regulations and with NASD Rules. BAIS violated NASD Conduct Rules 3010 and 2110 by failing to establish and maintain a supervisory system, including written procedures, reasonably designed to review and monitor Portfolio Edge accounts.

From August 2002 until December 2003, BAIS did not maintain a supervisory system or written procedures designed to require an initial or periodic supervisory review of customers' fee-based brokerage accounts to determine whether such accounts were appropriate for the particular customers. From August 2002 until December 2003, the firm did not have procedures requiring its brokers to determine whether a Portfolio Edge Account was appropriate for a customer before opening the account. During this period, the firm also did not maintain exception reports to monitor fee-based brokerage accounts for inactivity or for accounts that fell below the \$100,000 minimum account balance level. Although the firm provided information to its brokers outlining the features of the Portfolio Edge account, BAIS did not have procedures specifically requiring brokers to consider whether the fee-based account was appropriate for a particular customer in light of the services provided, the projected cost to the customer, alternative fee structures that were available, or the customer's fee structure preferences and investment objectives.

As a result of BAIS's inadequate systems and procedures, BAIS allowed customers to continue in the Portfolio Edge account without adequately assessing whether the accounts were

appropriate for the customers. These customers either conducted no trading for an extended period of time or had accounts where the assets in the account averaged below \$50,000 for at least one full year, or both.

For instance, approximately 129 Portfolio Edge accounts had average daily balances below \$50,000 for more than 12 consecutive months during the review period. Although these accounts remained well below the minimum account balance for Portfolio Edge accounts for over a year, BAIS allowed these accounts to remain open and the accounts continued to incur fees after the 12-month period totaling over \$89,000.

In addition, between August 2002 and September 2005, the firm failed to establish and maintain a supervisory system or procedures reasonably designed to monitor the manual processing of trades to ensure that Portfolio Edge customers were not charged a commission for transactions in eligible assets. As a result, between August 2002 and September 2005, over 2,500 transactions in 1,211 customer accounts were charged both a commission and a fee for transactions in eligible assets in Portfolio Edge accounts, thereby resulting in duplicate charges for the same transaction.⁴

Finally, the firm failed to establish and maintain a supervisory system or procedures reasonably designed to ensure that adequate disclosures were made to customers regarding the fees that would be charged to Portfolio Edge accounts for certain transactions. For example, the firm had no procedures requiring disclosure to Portfolio Edge customers that new issues, including shares purchased in initial public offerings, were eligible assets that would be charged a fee in the Portfolio Edge account. In addition, the addendum to the new account form for Portfolio Edge customers failed to disclose that information and also omitted to state that new issues were subject to an initial sales concession in addition to the Portfolio Edge fee.⁵

As set forth above, BAIS violated NASD Conduct Rules 3010 and 2110 by failing to establish and maintain a supervisory system, including written procedures, reasonably designed to review and monitor its fee-based brokerage business. As a result of these deficiencies, BAIS allowed customers to continue in the Portfolio Edge account without assessing whether the account remained appropriate for those customers.

B. BAIS Used Written Communications Regarding its Portfolio Edge Account That Failed to Comply with NASD Conduct Rule 2210

NASD Conduct Rule 2210(d)(1)(A) provides:

[a]ll communications with the public shall be based on principles of fair dealing and good faith, must be fair and balanced, and must provide a sound basis for evaluating the facts in regard to any particular . . . service. No member may omit

⁴ The manual processing error was discovered by the firm during a routine internal audit. The firm has identified the affected customers and has reimbursed those customers the amounts they were charged as a result of the error.

⁵ The firm identified Portfolio Edge accounts that engaged in new issue transactions during the review period during a routine audit and has reimbursed those accounts any Portfolio Edge fees charged on those transactions.

any material fact or qualification if the omission, in the light of the context of the material presented, would cause the communication to be misleading.

BAIS used advertising and sales literature to market the Portfolio Edge account that omitted material information and failed to provide a sound basis for evaluating the facts in regard to the Portfolio Edge accounts.

For instance, certain brochures and marketing presentations used by the firm failed to disclose that customers could pay more in fees in a Portfolio Edge account than in a traditional commission-based account. Certain client presentations also failed to disclose that \$100,000 in eligible assets were necessary to open a Portfolio Edge account and that there was a minimum annual fee of \$1,500.

A number of the firm's communications with the public also failed to disclose that there could be additional fees and charges associated with the Portfolio Edge account and that customers might pay more in fees than they would pay in commissions in a commission-based account. Moreover, certain of these communications suggested that a customer would receive additional investment services with the Portfolio Edge account such as one-on-one guidance and investment planning from the firm's brokers. However, apart from a quarterly performance report and the ability to trade online, BAIS provided no additional services with the Portfolio Edge account that were not also available through a traditional commission-based account.

By using written communications with the public, including advertising and sales literature, that omitted material information and failed to provide a sound basis for evaluating the facts in regard to the Portfolio Edge account, BAIS violated NASD Conduct Rules 2210(d)(1) and 2110.

Sanctions

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

1. A censure;
2. A fine in the amount of \$500,000; and
3. The payment of restitution to 129 customers, who were allowed to continue in Portfolio Edge accounts without BAIS reassessing whether the accounts remained appropriate for them, as listed on Attachment A (which was provided to BAIS in electronic format), in the total amount of \$89,625, plus interest at the rate set forth in Section 6621(a)(2) of the Internal Revenue Code (26 U.S.C. § 6621), from September 31, 2005 until the date this AWC is accepted by the NAC. NASD is not ordering payment of restitution to additional customers, in the amount of \$27,843.46, because the Firm has previously paid that restitution to those customers. Satisfactory proof of payment of the restitution or of reasonable and

documented efforts undertaken to effect restitution shall be provided to NASD staff no later than 120 days after acceptance of this AWC. If for any reason BAIS cannot locate any customer identified in Attachment A after reasonable and documented efforts within such period, or such additional period agreed to by the staff, BAIS shall forward any undistributed restitution and interest to the appropriate escheat, unclaimed property, or abandoned property fund for the state in which the customer is last known to have resided.

4. In connection with the errors in the manual processing of certain trades and the failure to make certain disclosures, as described above, BAIS shall provide to NASD satisfactory proof of payment.

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

III.

OTHER MATTERS

- A. BAIS 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. BAIS 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. BAIS agrees to pay any monetary sanctions imposed on it upon notice that this AWC has been accepted and that such payments are due and payable, and BAIS has attached an Election of Payment form showing the method by which it proposes to pay any fine imposed.
- C. BAIS 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.

BAIS certifies that it has read and understands all of the provisions of this AWC and has 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 BAIS to submit it.

11/21/2006

Date

Banc of America Investment Services, Inc.
Respondent

By:



Ronald J. Newth
Senior Vice President and
Chief Administrative Officer

Reviewed by:



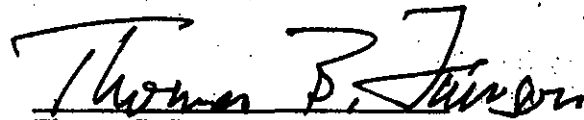
William E. Goydan, Esquire
Wolff & Samson, P.C.
One Boland Drive
West Orange, New Jersey 07052

Accepted by NASD:

12/19/06

Date

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



Thomas B. Lawson
Chief Counsel
NASD Department of Enforcement
1801 K Street, NW
Washington, DC 20006

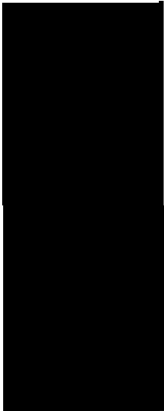
Attachment A - Customer Accounts to Receive Restitution

Account Number	Average Account Size	Number of Qtrs Min Fee Charged	Total Client Remediation
	\$28,292.90	5	\$375.00
	\$41,004.23	6	\$750.00
	\$44,993.08	5	\$375.00
	\$37,590.13	5	\$375.00
	\$32,061.31	5	\$375.00
	\$43,284.94	5	\$375.00
	\$291.47	5	\$375.00
	\$40,578.01	6	\$750.00
	\$17,545.03	8	\$1,500.00
	\$252.32	5	\$375.00
	\$33,707.76	5	\$375.00
	\$43,548.25	5	\$375.00
	\$33,391.25	7	\$1,125.00
	\$46,136.99	5	\$375.00
	\$44,143.76	5	\$375.00
	\$27,348.71	5	\$375.00
	\$27,129.27	6	\$750.00
	\$34,573.36	8	\$1,500.00
	\$25,964.27	8	\$1,500.00
	\$42,023.72	5	\$375.00
	\$42,504.96	5	\$375.00
	\$47,328.18	5	\$375.00
	\$47,756.24	8	\$1,500.00
	\$48,885.42	5	\$375.00
	\$15,083.80	6	\$750.00
	\$20,429.83	5	\$375.00
	\$24,625.25	6	\$750.00
	\$35,167.86	6	\$750.00
	\$45,524.21	6	\$750.00
	\$45,342.14	5	\$375.00
	\$42,339.53	6	\$750.00
	\$12,093.78	5	\$375.00
	\$45,323.62	5	\$375.00
	\$31,346.97	7	\$1,125.00
	\$30,343.83	6	\$750.00
	\$48,179.54	6	\$750.00
	\$43,307.78	6	\$750.00
	\$36,993.18	5	\$375.00
	\$48,023.04	6	\$750.00
	\$24,982.17	5	\$375.00
	\$40,975.98	5	\$375.00
	\$33,219.47	6	\$750.00
	\$23,204.57	6	\$750.00
	\$24,895.96	6	\$750.00
	\$36,091.62	6	\$750.00
	\$45,264.40	5	\$375.00
	\$40,808.36	6	\$750.00
	\$46,878.43	6	\$750.00
	\$47,628.75	6	\$750.00
	\$0.00	5	\$375.00
	\$23,469.03	5	\$375.00
	\$7,631.81	6	\$750.00
	\$46,160.91	5	\$375.00
	\$43,486.18	6	\$750.00
	\$48,803.13	6	\$750.00
	\$22,107.14	6	\$750.00
	\$26,973.54	5	\$375.00

Attachment A - Customer Accounts to Receive Restitution

Account Number	Average Account Size	Number of Qtrs Min Fee Charged	Total Client Remediation
	\$18,799.61	5	\$375.00
	\$23,677.99	5	\$375.00
	\$10,083.81	8	\$1,500.00
	\$20,717.90	11	\$2,625.00
	\$28,559.98	5	\$375.00
	\$16,793.10	6	\$750.00
	\$32,826.66	6	\$750.00
	\$24,530.65	7	\$1,125.00
	\$28,497.26	6	\$750.00
	\$1,425.86	6	\$750.00
	\$23,362.91	5	\$375.00
	\$45,833.86	7	\$1,125.00
	\$40,920.06	7	\$1,125.00
	\$532.30	5	\$375.00
	\$19,100.94	7	\$1,125.00
	\$23,304.20	5	\$375.00
	\$34,028.82	5	\$375.00
	\$38,752.96	6	\$750.00
	\$16,631.10	6	\$750.00
	\$13,323.06	6	\$375.00
	\$26,422.55	8	\$1,500.00
	\$33,424.43	5	\$375.00
	\$38,025.21	5	\$375.00
	\$42,938.41	6	\$750.00
	\$29,794.33	6	\$750.00
	\$43,307.72	9	\$1,875.00
	\$49,319.73	5	\$375.00
	\$45,905.82	6	\$750.00
	\$46,909.52	5	\$375.00
	\$41,686.88	6	\$750.00
	\$16,262.11	6	\$750.00
	\$16,485.30	6	\$750.00
	\$24,167.09	5	\$375.00
	\$41,207.79	7	\$1,125.00
	\$44,434.69	7	\$1,125.00
	\$21,752.04	6	\$750.00
	\$10,963.65	6	\$750.00
	\$35,324.24	5	\$375.00
	\$34,863.83	5	\$375.00
	\$12,172.55	5	\$375.00
	\$29,548.33	5	\$375.00
	\$33,755.41	5	\$375.00
	\$5,454.49	6	\$750.00
	\$24,854.79	5	\$375.00
	\$49,347.66	5	\$375.00
	\$29,441.29	5	\$375.00
	\$32,291.74	7	\$1,125.00
	\$20,364.57	7	\$1,125.00
	\$41,259.51	6	\$750.00
	\$16,046.95	6	\$750.00
	\$32,500.42	5	\$375.00
	\$14,715.68	6	\$750.00
	\$35,108.07	5	\$375.00
	\$35,923.75	6	\$750.00
	\$48,927.75	6	\$750.00
	\$34,771.17	6	\$750.00
	\$47,303.20	8	\$1,500.00

Attachment A - Customer Accounts to Receive Restitution

Account Number	Average Account Size	Number of Qtrs Min Fee Charged	Total Client Remediation
	\$30,464.80	6	\$375.00
	\$3,110.13	6	\$750.00
	\$46,782.79	6	\$750.00
	\$35,195.52	5	\$375.00
	\$42,032.31	6	\$750.00
	\$47,573.26	5	\$375.00
	\$21,200.78	9	\$1,125.00
	\$33,306.92	7	\$1,125.00
	\$10,407.40	6	\$750.00
	\$24,905.32	7	\$1,125.00
	\$9,057.70	9	\$1,875.00
	\$25,678.08	6	\$750.00
	\$6,124.92	5	\$375.00
	\$32,056.82	5	\$375.00
	\$41,248.70	5	\$375.00
			\$89,625.00