

**UNITED STATES OF AMERICA**  
**Before the**  
**SECURITIES AND EXCHANGE COMMISSION**

**INVESTMENT ADVISERS ACT OF 1940**  
**Release No. 2489 / February 21, 2006**

**ADMINISTRATIVE PROCEEDING**  
**File No. 3-12214**

**In the Matter of**

**NEW ENGLAND SECURITIES  
CORP.,**

**Respondent.**

**ORDER INSTITUTING ADMINISTRATIVE  
AND CEASE-AND-DESIST PROCEEDINGS,  
MAKING FINDINGS, AND IMPOSING  
REMEDIAL SANCTIONS AND A CEASE-  
AND-DESIST ORDER PURSUANT TO  
SECTIONS 203(e) AND 203(k) OF THE  
INVESTMENT ADVISERS ACT OF 1940**

**I.**

The Securities and Exchange Commission (“Commission”) deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Sections 203(e) and 203(k) of the Investment Advisers Act of 1940 (“Advisers Act”) against New England Securities Corp. (“Respondent” or “NES”).

**II.**

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the “Offer”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over it and the subject matter of these proceedings, Respondent consents to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order Pursuant to Sections 203(e) and 203(k) of the Investment Advisers Act of 1940 (“Order”), as set forth below.

### III.

On the basis of this Order and Respondent's Offer, the Commission finds that:

#### **SUMMARY**

1. Beginning in 1995, NES marketed and sold the Investment Manager Program ("IM Program") through its field force of approximately 1,800 investment advisory representatives. The program allowed investors to select a model asset allocation portfolio of investments. From the program's inception, NES promised participating clients that it would regularly screen their accounts and identify whether their asset allocation percentages remained within certain predetermined ranges. If the percentages drifted from those ranges, NES promised to notify the clients and rebalance their portfolios upon request. However, from the program's inception and continuing until late 2002, NES failed to provide such rebalancing services to a large number of its IM Program clients. Throughout the period at issue, NES was aware of the rebalancing failures and yet failed to take appropriate corrective action. Instead, the company continued to make representations promising rebalancing services that it was failing to provide.

#### **RESPONDENT**

2. New England Securities Corp., headquartered in Boston, Massachusetts, is a registered investment adviser (File No. 801-47061) and broker-dealer (File No. 8-13910) operating through a nationwide network of offices. NES is owned by MetLife, Inc. via a series of wholly-owned subsidiaries. MetLife merged with New England Mutual Life, then NES' parent company, in 1996. MetLife's common stock is registered with the Commission pursuant to Section 12(b) of the Exchange Act (File No. 001-15787) and principally trades on the New York Stock Exchange.

#### **Facts**

##### ***The IM Program***

3. The Investment Manager ("IM") Program is a non-discretionary wrap investment program in which NES recommends an allocation of clients' assets among a suite of no-load and load-waived mutual funds that the company screens and evaluates for quality, and which it monitors on an ongoing basis. Investments in each client's account are spread among various mutual funds generally based upon one of five basic asset allocation models, with the client selecting a mix of funds for each asset class. The models are comprised of a mix of stock, bond and money market offerings, and offer various levels of risk, with the most aggressive models being more heavily tilted toward stock funds.

4. NES introduced the IM Program as a pilot program in 1995. By 1997, the

company offered the program nationally through its force of approximately 1,800 investment advisory representatives. Clients in the IM Program include ERISA plans, other retirement plans and individual investors with general investment accounts. The minimum initial investment in an IM Program account was \$100,000. NES generally charged IM Program clients an annual management fee from 1 to 1.75 percent of total assets, with fee rates negotiable. NES represented to clients that they would receive various services, including mutual fund screening, assistance in setting up their asset allocation portfolios, quarterly reports, and notice if selected rebalancing parameters were crossed.

### ***NES' Representations to Clients Concerning Rebalancing***

5. From the program's inception in 1995 until March 2003, NES consistently represented to its IM Program clients that it would send them notifications on an agreed schedule if their asset allocation varied by a specified amount from client-chosen allocation or "baseline." NES also distributed numerous marketing materials to both current and prospective clients in which it represented that it would provide such notices as part of the program. NES also instructed its sales representatives to tell their clients that they would receive rebalancing notifications based upon their stated preferences.

### ***October 1999: An Internal Audit Identifies Control Problems with Rebalancing***

6. In 1999, a member of New England Financial's internal audit department conducted a routine audit of the IM Program as part of a larger audit of NES' investment wrap products. The auditor concluded that NES did not have effective controls in place to ensure adherence to IM Program clients' original asset allocation preferences, to maintain those preferences over time, or to generate rebalancing notifications either if accounts drifted by more than 5% or when annual anniversaries occurred. The auditor also concluded that there was no system of review or follow-up in place to determine whether IM Program clients had been properly informed that their accounts needed rebalancing.

7. The auditor prepared a report dated October 26, 1999, specifically identifying the systems failure with respect to the IM Program's rebalancing component as follows:

Client Wrap accounts do not always remain within the portfolio allocation percentages originally set by NES and the client. Without an effective system to re-balance client accounts to their original allocation percentages, NES may not meet its clients' investment objectives.

8. Immediately following this entry, the audit report identified the following "management action plan" to address the problem:

We are currently testing software from Fidelity that will allow us to identify accounts requiring rebalancing and process the necessary trades. The testing should be complete by the first week of November. We do not expect to find anything that will prevent us from using the software at this point. Once a final decision is made, we will notify the NES field force and contact clients seeking their consent. Those that opt out of the automatic rebalancing feature will assume responsibility for their asset allocation and tracking.

9. The 1999 audit report also stated that the software testing would be completed by November 5, 1999, that a system of automatic rebalancing would be implemented by December, and that a direct report to NES' vice president of product origination would be accountable for implementing this plan.

10. The 1999 audit report was distributed to various executives at NES, including the company's vice president of product origination and its president. No one at NES, however, took sufficient steps to implement the management action plan. Neither the original auditor nor anyone else in the audit department followed up to determine whether the management action plan actually was implemented prior to the next internal audit of the IM Program in 2001.

#### ***September 2000 to March 2001: Worsening Problems with Rebalancing***

11. From the inception of the IM Program in 1995 through September 2000, NES did not have an automated system for identifying the IM Program accounts that required a rebalancing notice, or for checking accounts' current asset allocation against original asset allocation baseline. Instead, NES' product origination group produced a quarterly report that listed the current holdings of each client, and an assistant to the vice president of product origination visually scanned that report each quarter and determined which accounts required a rebalancing notice. By 1999 or 2000, as the program grew larger, this "manual" method of determining who should receive rebalancing notices had become essentially unmanageable.

12. In September 2000, for reasons unrelated to the rebalancing program, NES changed clearing firms. As a result of the shift, the stable flow of data that NES had been receiving was replaced by inadequate data coming from the successor firm. Consequently, NES' ability to reconcile IM Program accounts was severely impaired. During the period from September 2000 to March 2001, an account was rebalanced only when a client or sales representative actually requested that the account be rebalanced.

13. As of September 2000 personnel at NES, including the company's president, were aware that the company was not sending rebalancing notices. NES, however, did not take

sufficient steps to investigate or address the problem. During this period, NES made no changes to the continuing references to rebalancing in the IM Program client questionnaires and marketing materials, and the company continued to accept new IM Program clients.

*January - May 2001: Compliance Department Review of IM*

14. In the spring of 2001, New England Financial's chief compliance officer directed a member of her staff to conduct a general review of all of the IM Program's procedures. During this review, NES' vice president of product origination left the chief compliance officer a voice mail in which he told her, among other things, that there was a "gap" in rebalancing IM Program accounts and that NES had purchased new software to address the rebalancing issue.

15. The chief compliance officer subsequently brought to the attention of NES' in-house legal counsel several IM Program-related issues, including rebalancing, and she set up a meeting on May 9, 2001, between the vice president of product origination, herself and other members of NES' compliance, legal and operations departments to discuss those issues. During this meeting, the vice president of product origination told the meeting participants that he had purchased software to address the rebalancing problem.

*Summer 2001: An Internal Audit Identifies the Rebalancing Failure*

16. Approximately two years after the 1999 internal audit, the same auditor conducted another routine audit of the IM Program in the summer of 2001, with the vice president of product origination acting as NES' "point person." Of twenty accounts tested, the auditor found three instances where the client's originally selected asset allocation percentages had drifted by more than 5%. Of the remaining seventeen accounts, the auditor concluded that only two showed some effort at rebalancing, but that the remaining accounts appeared to be in compliance due only to "luck" or "market conditions." In his work papers for the 2001 audit, the auditor noted that "[t]his was an issue in the past [1999] audit and continues to be an issue here as the procedures in place for rebalancing in the past (none) have not changed." The auditor concluded that no formal rebalancing procedures existed at NES, and that the company was not monitoring IM Program accounts to determine whether they were out of balance.

17. When the auditor completed the 2001 audit, he prepared an audit report dated July 31, 2001 that, in part, stated:

**NES does not have an effective system in place to rebalance IM accounts.** As a result, client accounts do not always remain within the portfolio allocation percentages originally set by NES and the client. Without an effective system to re-balance client accounts, NES may not meet its clients' investment objectives.

(Emphasis in original).

18. Immediately following the above entry, the report identified the following “management action plan” to address the rebalancing issue:

NES has already begun implementation of an automated rebalancing system that uses the Advent “MOXY” rebalancing engine as a central element. That software has been installed and tested, and is functional. NES has begun a mailing to reps and clients to inform them of certain changes to our rebalancing policies, and to notify them that out-of-balance accounts will be rebalanced shortly after they receive the notices.

19. The report also noted that October 2001 would be the target date for “all accounts to be rebalanced,” and that the vice president of product origination would be accountable for implementing it.

20. The auditor distributed the 2001 audit report to various executives at NES.

21. NES knew that as of July 31, 2001 (the audit report’s date), there was no effective system in place to rebalance IM Program accounts. In early 2001, NES’ vice president of product origination decided to purchase the Advent “MOXY” software program to automate rebalancing. As of July 31, NES had installed and tested the new software and determined that it could identify the drift between an account’s baselines and its current positions. Several weeks after issuance of the July 31 report, the vice president of product origination discovered that the MOXY software would not save NES time in processing rebalancing notifications.

22. NES also knew that – contrary to what had been noted in the 2001 audit report – the company had not, by the end of July, commenced a mailing to sales representatives and clients informing them of changes to NES’ rebalancing policies. NES also knew that the October 2001 target date set in the July 31 report for all accounts to be rebalanced was inaccurate because, in July 2001, the company’s expectation was only that all notifications would be sent by October – and not that all clients would respond to such notifications and that all rebalancing would be completed by then.

### ***Summer 2001 – Fall 2002: NES Fails to Rectify Rebalancing Problems***

23. Major problems with rebalancing continued from the summer of 2001 through the fall of 2002. Between November 2001 and March 2002, despite the fact that NES still had not

installed a final automated solution to the rebalancing problem, NES sent to most of its IM program clients information packages about new automated options that supposedly would soon be available, together with rebalancing notifications. NES sent out three batches of such mailings in November 2001, and January and March 2002. By June 2002, NES had sent mailings to approximately 2,500 IM Program clients out of the approximately 3,500 clients that had been in the program as of October 2001. NES sent no further notices after June 2002.

24. Even after these mailings, NES never provided the automated rebalancing services that it told its clients they could select. Furthermore, from December 2001 through the end of 2002, NES did not monitor new IM Program accounts for asset allocation drift. By February 2002, NES had ceased making substantial efforts to address the rebalancing problem. Nevertheless, during the entire period from the summer of 2001 to the fall of 2002, no one at NES ever recommended or ordered that the IM Program be closed to new clients, that notices be sent to IM Program clients notifying them of the rebalancing problem, or that the rebalancing representations contained in the IM Program client questionnaires and marketing materials be changed.

***Late 2002 – Early 2003: NES Closes the  
IM Program to New Clients and Self-Reports***

25. In October 2002, a MetLife official became concerned that there may be rebalancing problems with the IM Program during discussions related to switching NES' clearing firm. In November, that official communicated his concerns to NES' chief compliance officer, who arranged a conference with the company's vice president of product origination. During that conference, the vice president of product origination told the chief compliance officer that the MOXY software that he had installed in 2001 had not accomplished automated rebalancing, and that he had not sent out the vast majority of the rebalancing notices by October 2001, as required by the 2001 audit report's management action plan. He also advised that he had periodically reported the problems to the company's president. The chief compliance officer subsequently reported these issues to in-house legal counsel. As a result, in December, NES closed the IM Program to new clients (although the program remained open for existing IM Program clients). In March 2003, NES sent a letter to existing IM Program clients that stated that, "It has come to our attention that you may not have been consistently notified if the allocation of your assets varied over time ('drifted') from the allocation base line that you had selected and that your account may not have been rebalanced automatically after you chose that option." The letter went on to state that NES was in the process of developing a new technology platform and that during the transition to the new platform, "NES will not actively monitor drift, notify you of the possible need to rebalance due to drift, or rebalance your account automatically."

26. In March 2003, NES self-reported to the Commission staff the company's failure to rebalance IM Program accounts in accordance with its representations to its clients. Thereafter, NES fully cooperated with the staff's investigation.

27. In addition to NES' problems with the IM Program's rebalancing component, the staff's investigation also determined that NES had failed to properly impose Rule 12b-1 fees<sup>1</sup> and sales commission charges in connection with the program. Pursuant to the terms of the IM Program, NES agreed not to charge IM Program clients sales commissions for the purchase or sale of mutual funds that were included in the program, and NES also agreed to rebate all Rule 12b-1 fees that it received from mutual funds that were purchased in ERISA and IRA accounts participating in the IM Program. However, during the life of the IM Program, NES systematically failed to rebate Rule 12b-1 fees to ERISA and IRA accounts in an amount equal to \$2,257,169. Furthermore, NES also improperly charged mutual fund sales commissions to some IM Program clients in an amount equal to \$116,316. After commencement of the staff's investigation, NES refunded all the unrebated Rule 12b-1 fees and refunded all improperly charged sales commissions, plus interest in the total amount of \$178,649, to the appropriate IM Program ERISA and IRA accounts.

28. After the commencement of the staff's investigation, NES retained an independent consultant to analyze the impact upon IM Program client accounts of the company's failure to provide promised rebalancing services. The independent consultant calculated the investment returns that each IM Program client would have received during the life of the program, had he or she received all of the rebalancing notices that the company failed to provide, based upon the assumption that all clients would have opted to rebalance their portfolios upon the receipt of such notices. The independent consultant concluded that, in some instances, the actual performance of an account was lower than the performance of a hypothetical account that was rebalanced each time it received a drift notice and that, in some instances, the actual performance in an account was higher than the performance of a hypothetical account that was rebalanced each time it received a drift notice. According to the analysis, the total amount of harm to investors from the reduced returns and increased losses was \$7,531,999. During 2004, NES distributed this amount to those IM Program investors whose accounts had lower returns or greater losses, together with interest in the total amount of \$425,765.

### *NES' Remedial Efforts*

29. In determining to accept the Offer, the Commission has considered that, as remedial efforts, NES voluntarily: (i) halted new sales of the IM Program; (ii) notified existing

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<sup>1</sup> Rule 12b-1 fees are paid by certain mutual funds to broker-dealers out of fund assets for distribution-related costs, and are deducted before NAV is calculated. These fees are disclosed in the mutual fund prospectus.



IM Program clients; (iii) self-reported the rebalancing problem to the Commission's staff; (iv) retained a consultant to determine what existing IM Program clients' portfolios would have been worth had they received the rebalancing notices to which they were entitled; (v) paid the difference in portfolio value to clients whose accounts earned reduced returns or suffered losses, plus interest, in the total amount of \$7,957,764; (vi) rebated to clients Rule 12b-1 fees and sales commissions, with interest, in the total amount of \$2,552,134; and (vii) retained a major accounting firm to review IM Program procedures for generating rebalancing notices, rebating Rule 12b-1 fees to appropriate accounts, and complying with contractual provisions regarding commissions for purchase or sale of mutual fund shares.

### **VIOLATIONS**

30. As a result of certain of the conduct described above, NES willfully<sup>2</sup> violated Section 206(2) of the Advisers Act, which makes it unlawful for any investment adviser, directly or indirectly, to engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client.

### **UNDERTAKINGS**

31. **Independent Consultant.** Respondent shall retain, within 30 days of the date of entry of the Order, the services of an Independent Consultant not unacceptable to the staff of the Commission. The Independent Consultant's compensation and expenses shall be borne exclusively by Respondent.

- a. Respondent shall cooperate fully with the Independent Consultant and shall provide the Independent Consultant access to its files, books, records, and personnel as reasonably requested for review.
- b. Respondent shall require, within 60 days of the entry of this Order, that the Independent Consultant conduct a review of: (i) Respondent's operations and procedures to effect rebates of Rule 12b-1 fees received with respect to fund

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<sup>2</sup> "Willfully" as used in this Order means intentionally committing the act which constitutes the violation, *see Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000); *Tager v. SEC*, 344 F.2d 5, 8 (2d Cir. 1965). There is no requirement that the actor also be aware that he is violating one of the Rules or securities Acts. *Id.*

shares held by accountholders in qualified ERISA plans participating in the IM Program and 12b-1 fees received with respect to fund shares held in affiliated funds owned by IRA accountholders participating in the IM Program, and the implementation of those procedures; (ii) Respondent's operations and procedures to prevent payment of a load or commission by accountholders participating in the IM Program who purchase fund shares, and the implementation of those procedures; and (iii) Respondent's operations and procedures to monitor periodically IM Program accounts for drift of the accountholder's portfolio away from the baseline allocation established in the account's proposal and to notify customers of the need to rebalance their account to reestablish the portfolio allocation, and the implementation of those procedures.

- c. One year after the completion of the review described in the preceding paragraph, Respondent shall require that the Independent Consultant conduct a second review of the same operations and procedures.
- d. Within 60 days after the completion of each of the reviews described in paragraphs (b) and (c) above, Respondent shall require that the Independent Consultant submit a written report of its findings to it and the staff of the Commission.
- e. Respondent shall require that the Independent Consultant, for the period of the engagement and for a period of two years from completion of the engagement, shall not enter into any employment, consultant, attorney-client, auditing or other professional relationship with Respondent or any of its present or former affiliates, directors, officers, employees, or agents acting in their capacity as such. Respondent shall require that any firm with which the Independent Consultant is affiliated in performance of its duties under the Order shall not, without prior written consent of the staff of the Commission, enter into any employment, consultant, attorney-client, auditing or other professional relationship with Respondent or any of its present or former affiliates, directors, officers, employees, or agents acting in their capacity as such for the period of the engagement and for a period of two years after the engagement.

32. Disgorgement. Respondent shall be responsible to distribute the sums ordered as disgorgement in Paragraph IV.D. Respondent shall pay to IM Program clients and former IM Program clients the Disgorgement Amount of \$2,042,865 plus interest of \$572,000, proportionally to the IM Program advisory fees paid by such client between 1995 and 2002. Within ninety (90) days of the entry of this Order, NES shall certify to the staff that it has made such payments, and provide to the staff records of the payments, including the identities of the

recipients, their addresses and the amounts that they received. If a former or present account holder in the IM Program requests a distribution or disputes the amount of a distribution made pursuant to this paragraph, then the Respondent shall respond to the request or dispute and report the account holder's communication and Respondent's response to the staff of the Commission's Boston District Office, 73 Tremont Street, Suite 600, Boston, MA 02108. If NES is unable to pay any client due to factors beyond its control, any portion of the \$2,614,865 which is not paid to such client shall be paid to the United States Treasury within one-hundred and twenty (120) days of the date on which NES initially sends payment to such client. Such payment shall be: (A) made by United States postal money order, certified check, bank cashier's check or bank money order; (B) made payable to the Securities and Exchange Commission; (C) hand-delivered or mailed to the Office of Financial Management, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Alexandria, Stop 0-3, VA 22312; and (D) submitted under cover letter that identifies NES as a respondent in these proceedings, the file number of these proceedings, a copy of which cover letter and money order or check shall be sent to David Bergers, Associate District Administrator, Securities and Exchange Commission, 73 Tremont Street, Boston, Massachusetts, 02108.

33. Within ninety (90) days of entry of the Order, NES will provide a copy of the Order to all clients who purchased the IM Program at any time prior to April 1, 2003, together with a cover letter in a form not unacceptable to the Commission's staff. Within one-hundred and twenty (120) days of entry of the Order, NES will file an affidavit with the Commission's staff, addressed to the attention of Gregory S. Gilman of the Commission's Boston District Office, 73 Tremont Street, Suite 600, Boston, MA 02108, setting forth the details of its compliance with this provision.

34. No later than twenty-four months after the date of entry of the Order, Respondent's chief executive officer shall certify to the Commission in writing that Respondent has fully adopted and complied in all material respects with the undertakings set forth in this section and with the recommendations of the Independent Consultant or, in the event of material non-adoption or non-compliance, shall describe such material non-adoption and non-compliance.

35. Respondent shall preserve for a period not less than six years from the end of the fiscal year last used, the first two years in an easily accessible place, any record of Respondent's compliance with the undertakings set forth herein.

36. For good cause shown, the Commission's staff may extend any of the procedural dates set forth above.

#### IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in the Offer of Settlement of Respondent. Accordingly, pursuant to Section 203(e) and 203(k) of the Advisers Act, it is hereby ORDERED that:

- A. Respondent is hereby censured.
- B. Respondent shall cease and desist from committing or causing any violations and any future violations of Section 206(2) of the Advisers Act.
- C. Respondent shall comply with the undertakings enumerated in Section III above.
- D. Disgorgement. Respondent shall pay, within 90 days of the entry of this Order, disgorgement in the total amount of \$2,042,865 plus prejudgment interest in the amount of \$572,000, consistent with the provisions of Paragraph 32 above.
- E. Other Obligations and Requirements. Nothing in this Order shall relieve Respondent of any other applicable legal obligation or requirement, including any rule adopted by the Commission subsequent to this Order.

By the Commission.

Nancy M. Morris  
Secretary