

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 51700 / May 17, 2005

ADMINISTRATIVE PROCEEDING
File No. 3-11924

In the Matter of

**SUNTRUST SECURITIES,
INC.,**

Respondent.

**ORDER INSTITUTING ADMINISTRATIVE
AND CEASE-AND-DESIST PROCEEDINGS,
MAKING FINDINGS, AND IMPOSING
REMEDIAL SANCTIONS AND A CEASE-
AND-DESIST ORDER PURSUANT TO
SECTIONS 15(b) AND 21C OF THE
SECURITIES EXCHANGE ACT OF 1934**

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 15(b) and 21C of the Securities Exchange Act of 1934 (“Exchange Act”) against SunTrust Securities, Inc. (“SunTrust Securities” or “Respondent”).

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 Respondent 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 15(b) and 21C of the Securities Exchange Act of 1934 (“Order”), as set forth below.

III.

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

A. RESPONDENT

SunTrust Securities is a broker-dealer headquartered in Atlanta, Georgia. It has been registered with the Commission pursuant to Section 15(b) of the Exchange Act since July 1986.

B. SUMMARY

Between 2001 and 2002 (the "relevant period"), Respondent sold shares issued by mutual funds without providing certain customers with the reductions in front-end loads, or sales charges, also known as "breakpoint" discounts, described in the prospectuses of the funds. Respondent failed to provide all available breakpoint discounts even after the Commission staff had alerted Respondent to two specific instances where Respondent either had failed to give a customer the appropriate breakpoint discount or had sold to customers mutual fund shares with front-end loads in amounts approximately \$1,000 less than the breakpoint amount that would have entitled the customer to a lower sales charge. According to statistical analysis by NASD of data submitted to NASD by Respondent, Respondent is estimated to have failed to give certain customers at the time of the transactions breakpoint discounts totaling approximately \$201,117. Respondent later became aware of the failure in certain of these transactions and gave the appropriate discounts. By failing to charge these customers the correct sales loads as set forth in the mutual funds' prospectuses, and by failing to disclose in confirmations the remuneration Respondent received from the sales loads charged to these customers in connection with such transactions, Respondent violated Rule 10b-10 under the Exchange Act.

C. FACTS

Background

Mutual fund costs borne by investors generally fall into two categories: sales charges collected directly from shareholders for specific transactions (such as a purchase, redemption, or exchange) and fees and operating expenses imposed continuously on the fund assets.¹ A "front-end load" is an industry term for a sales charge that certain fund

¹ Annual operating expenses are not charged directly to investors but are deducted from fund assets. These expenses include the management fee, an ongoing charge paid to an investment adviser who manages the fund's assets and selects its portfolio of securities. Some funds charge a Rule 12b-1 fee, named for the rule under the Investment Company Act of 1940 that authorizes mutual funds to pay for distribution expenses, including sales charges used to compensate sales professionals for selling fund shares, directly from a fund's assets. In addition, a fund may also pay a service fee to compensate sales

principal underwriters or distributors charge at the time an investor buys shares. When an investor buys shares with a front-end load, the front-end load portion of the offering price is not invested in the fund, but instead is paid to the fund's principal underwriter or distributor. When the purchase is made through a broker-dealer, the fund's principal underwriter or distributor pays a part of the front-end load amount to the broker-dealer that sold the fund shares to the investor. Typically, front-end loads for shares of equity funds start at 4 percent to 5.75 percent.

A fund may offer different classes of shares. Typically, shares denominated as "Class A" charge a front-end load. Other classes (e.g., Class B, Class C, etc.) have differing sales charge and expense characteristics.² "No-load" funds do not have any front-end or deferred sales charges.

Mutual funds that sell shares charging front-end loads usually offer discounts at certain pre-determined levels of investment, which are called "breakpoints." Front-end loads and breakpoints can vary among funds within a fund complex or across fund complexes. For example, a mutual fund might charge an investor 5.75 percent of the sales price for purchases of less than \$50,000, but reduce the sales charge to 4.75 percent for investments between \$50,000 and \$99,999. An investor usually can procure discounts on sales charges at investment levels of \$50,000, \$100,000, \$250,000, and \$500,000. At the \$1 million investment level, generally there is no sales charge.

The specific terms and conditions under which breakpoint discounts may become available are determined by the mutual funds and can vary. Generally, an investor can procure a breakpoint discount through either a single purchase large enough to reach a breakpoint or multiple purchases in a single mutual fund or any of the funds in a fund complex, the aggregate value of which is large enough to reach a breakpoint. In reaching a breakpoint, an investor typically is permitted to aggregate transactions made by certain family members and transactions in certain other related accounts, e.g., retirement accounts. An investor also typically may aggregate purchases over time to meet applicable breakpoint thresholds through "rights of accumulation" ("ROA") or "letters of intent" ("LOI"). An investor may be eligible for a discount through an ROA by aggregating the amount of his or her current purchase with the amount of certain prior purchases. An LOI is a written statement of intent by the investor to purchase a certain amount of mutual fund shares over what is usually a thirteen-month period.

professionals, or other service providers, for ongoing services to investors or their accounts. In addition, all mutual funds incur brokerage and other transaction-related costs that are borne indirectly by the investors in the funds.

² For example, Class B shares generally carry "contingent deferred sales charges," which means that a "load" is charged if shares are redeemed within a certain number of years after purchase. Class B and Class C shares generally impose a sales charge in the form of higher 12b-1 fees, but impose no front-end load.

Mutual funds are required to disclose the schedule of available breakpoints in their prospectuses and disclose how an investor may qualify for breakpoints either in the prospectuses or in their statements of additional information, both of which are filed with the Commission on Form N-1A. Mutual funds generally incorporate by reference into their prospectuses the information included in their statements of additional information.

Broker-dealers who sell fund shares to retail customers must disclose breakpoint discount information to their customers and must have procedures reasonably designed to ascertain information necessary to determine the availability and appropriate level of breakpoints. A failure to do so can result not only in the customer being deprived of a benefit to which he or she is entitled, but also in the broker-dealer and representative receiving increased commissions at the customer's expense. See In the Matter of Application of Harold R. Fenocchio for Review of Disciplinary Action Taken by the NASD, 46 SEC 279 (1976) (registered representatives “had a responsibility to make certain that a letter of intent was filed with the mutual fund or, at the very least, to inform the clients of their rights of accumulation”). Because of the large number of mutual funds offering different discounts and employing different criteria for determining breakpoint eligibility, many broker-dealers have experienced operational challenges and other difficulties in assuring that customers consistently receive the applicable discounts. Nevertheless, each broker-dealer is responsible for exercising due care, based on information reasonably ascertainable by the broker-dealer, to provide the appropriate breakpoint discounts.

Broker-Dealers Perform Self-Assessments

From November 2002 through January 2003, the Commission, NASD, and the New York Stock Exchange reviewed thousands of mutual fund transactions at forty-three broker-dealers that sold shares with front-end loads issued by mutual funds. Examiners found widespread failures to deliver breakpoint discounts to eligible customers among the transactions reviewed.

As a result of the examination findings, in March 2003 NASD directed broker-dealers that processed 100 or more automated purchases of Class A mutual fund shares with front-end loads in either 2001 or 2002 to conduct a “self-assessment” of their record of delivering breakpoint discounts to customers, based on the customers’ accounts and related accounts held at the broker-dealer. The self-assessment was designed to produce a statistically significant sample that would allow NASD to assess the scope of the failure to provide available breakpoint discounts at individual member firms and to gauge the scope of the problem across the industry as a whole.

The self-assessments showed that most firms did not consistently deliver applicable breakpoint discounts to eligible mutual fund share purchasers. Overall,

discounts were not delivered in about one out of five eligible transactions.³ The statistical analysis commissioned by the NASD determined that broker-dealers failed to deliver at least \$86 million in breakpoint discounts to eligible customers in 2001 and 2002.

Respondent's Self-Assessment Results

Based on the self-assessment and other data submitted by Respondent, the statistical analysis commissioned by NASD reflected to a 90 percent level of confidence that (1) at the time of the transactions, Respondent failed to give its customers appropriate breakpoint discounts in 24.13 percent of eligible mutual fund transactions in 2001 and 2002, and (2) this resulted in missed breakpoints that would have reduced customers' charges by an estimated \$201,117 on their purchases of mutual fund shares with front-end loads during the relevant period.

Respondent Had Notice of "Breakpoint" Deficiencies

In 2001, the Commission staff conducted an examination of Respondent and found that Respondent had sold mutual fund shares with a front-end load to a customer and failed to give the customer the appropriate breakpoint discount reduction in the sales charge, resulting in Respondent overcharging the customer on the sale of the mutual fund. Moreover, in that instance and another, Respondent had sold mutual fund shares with front-end loads to customers in amounts approximately \$1,000 less than the breakpoint amount that would have entitled the customers to lower sales charges.

In response to being notified by the Commission staff of these deficiencies, Respondent stated that it would "enhance its supervisory system by designing an exception report that will identify Investment Company transactions at or near breakpoints." Respondent also stated that it would undertake an immediate training effort to reinforce its employees' awareness of the specific rules in question regarding the sale of mutual fund shares. It also represented that it was working on additional written procedures for processing mutual fund share transactions.

Notwithstanding this notice from the Commission staff and implementation of these corrective actions, Respondent, during the relevant period, continued to sell mutual fund shares with front-end loads without providing certain customers with the breakpoint discounts to which they were entitled under the terms of the individual funds, as set forth above.

³ For the purposes of the self-assessment, "eligible transactions" were automated purchases of Class A shares of at least \$2,500 in which a sales charge of one percent or more was charged to the customer and a breakpoint discount was applicable.

IV.

LEGAL ANALYSIS

Rule 10b-10 Under the Exchange Act

Rule 10b-10 provides, in relevant part, that it is unlawful for a broker-dealer to effect any transaction for the customer's account unless the broker-dealer, at or before completion of the transaction, provides the customer with written notification disclosing "[t]he amount of any remuneration received or to be received by the broker from such customer in connection with the transaction..." 17 C.F.R. 240.10b-10(a)(2)(i)(B). The confirmations Respondent sent to customers for purchases of mutual fund shares during the relevant period did not disclose the remuneration Respondent received from front-end sales loads. Further, in those situations in which Respondent failed to apply the applicable breakpoint discount, disclosures in fund prospectuses concerning sales loads and the availability of breakpoint discounts were not, by themselves, sufficient to fully inform customers what they were paying for their shares.⁴ As a result, Respondent violated Rule 10b-10 under the Exchange Act.

Conclusion

As a result of the conduct described above, Respondent willfully violated Rule 10b-10 under the Exchange Act.⁵

V.

On the basis of the foregoing, the Commission deems it appropriate, and in the public interest to impose the sanctions specified in Respondent SunTrust Securities Inc.'s Offer of Settlement.

⁴ When it adopted Rule 10b-10 in 1977, the Commission stated that if information regarding the "source and amount" of the remuneration is contained in a prospectus delivered to a customer, then broker-dealers do not have to repeat the information in a confirmation. Of course, if a broker-dealer received remuneration which was not disclosed in the prospectus, that remuneration would be required to be separately disclosed on a confirmation. See Securities Exchange Act Release No. 13508 (May 5, 1977). The funds' prospectuses disclosed that the customers were entitled to certain breakpoint discounts, which they did not receive. The confirmations did not correct this prospectus representation and, therefore, failed to disclose the remuneration as required.

⁵ "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 Acts.

Accordingly, it is hereby ORDERED:

- A. Pursuant to Section 15(b)(4) of the Exchange Act, that Respondent is hereby censured;
- B. Pursuant to Section 21C of the Exchange Act, that Respondent shall cease and desist from committing or causing any violations and any future violations of Rule 10b-10 under the Exchange Act;
- C. Respondent shall pay disgorgement and prejudgment interest as follows: (1) Respondent shall make a refund within 30 days of the entry of this Order to each customer it identified in the self-assessment as having not received the breakpoint discount to which the customer was entitled; (2) Respondent shall provide written notification (the language of which is to be not unacceptable to the staff of the Commission) within 30 days of the entry of this Order to each customer who purchased Class A mutual fund shares through SunTrust from January 1, 1999 through December 31, 2003 that SunTrust may not have provided breakpoint discounts to which the customer was entitled and that as a result, the customer may be entitled to a refund; (3) Respondent shall make a refund within 30 days after receiving a reply from each customer who did not receive the breakpoint discount to which the customer was entitled; and (4) Respondent shall pay prejudgment interest on all such refunds paid to customers; and
- D. Respondent shall, within six months of the entry of this Order, unless otherwise extended by the staff of the Commission for good cause shown, have its Chief Executive Officer certify in writing to the staff that SunTrust Securities, Inc. has complied with the terms of this Order. The certification in writing to the staff shall include that SunTrust has paid disgorgement and prejudgment interest to customers (listing all customers who received payments and amounts paid to such customers and providing proof of payment thereof) pursuant to Section V.C. of this Order. The certification in writing to the staff also shall include that SunTrust has implemented procedures, and a system for applying such procedures, that reasonably can be expected to prevent and detect failures to provide appropriate breakpoint discounts for which customers are eligible on purchases of front-end load mutual funds, based on information reasonably ascertainable by Respondent.

By the Commission.

Jonathan G. Katz
Secretary