UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 8-K

CURRENT REPORT

Pursuant to Section 13 or 15(d) of the
Securities Exchange Act of 1934

Date of Report (Date of earliest event reported): August 28, 2006

PRUDENTIAL FINANCIAL, INC.
(Exact name of registrant as specified in its charter)

New Jersey	001-16707	22-3703799
(State or other jurisdiction of incorporation)	(Commission File Number)	(I.R.S. Employer Identification No.)

751 Broad Street
Newark, New Jersey 07102
(Address of principal executive offices and zip code)

(973) 802-6000
(Registrant's telephone number, including area code)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions (see General Instruction A.2. below):

¨ Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)

¨ Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)

¨ Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))

¨ Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

Item 1.01 Entry Into a Material Definitive Agreement.

On August 28, 2006, Prudential Equity Group, LLC ("PEG"), a wholly owned subsidiary of Prudential Financial, Inc. (the "Company"), reached a global resolution of the previously disclosed regulatory and criminal investigations into deceptive market timing related activities involving PEG's former Prudential Securities operations. This resolution takes the form of separate settlements between PEG and each of the United States Attorney for the District of Massachusetts ("USAO"), the Secretary of the Commonwealth of Massachusetts, Securities Division ("MSD"), the Securities and Exchange Commission ("SEC"), the National Association of Securities Dealers ("NASD"), the New York Stock Exchange ("NYSE"), the New Jersey Bureau of Securities ("NJBS") and the New York Attorney General's Office ("NYAG").

The investigations of the above named authorities have focused on former Prudential Securities brokers in Boston and certain other branch offices in the U.S., their supervisors, and other members of the Prudential Securities control structure with responsibilities that related to the market timing activities, including certain former members of Prudential Securities senior management. The settlements relate to conduct that generally occurred between 1999 and September 2003. The Prudential Securities operations were contributed to a joint venture with Wachovia Corporation in July 2003, but PEG retained liability for the market timing related activities.

These settlements resolve the investigations by the above named authorities into these matters as to all Prudential entities without further regulatory proceedings or filing of charges so long as the settlement terms are followed and provided, in the case of the settlement agreement reached with the USAO, that the USAO has reserved the right to prosecute PEG if there is a material breach by PEG of that agreement during its five year term and in certain other specified events. Under the terms of the settlements, PEG is paying $270 million into a Fair Fund administered by the SEC to compensate those harmed by the market timing activities. In addition, $330 million will be paid in fines and penalties. In the settlements, PEG has agreed to retain, at PEG's ongoing cost and expense, the services of an Independent Distribution Consultant acceptable to certain of the authorities to develop a proposed distribution plan for the distribution of Fair Fund amounts according to a methodology developed in consultation with and acceptable to certain of the authorities. In addition, as part of these settlements PEG has agreed, among other things, to continue to cooperate with the above named authorities in any litigation, ongoing investigations or other proceedings relating to or arising from their investigations into these matters.

No addition to the Company's existing reserves for estimated settlement costs is required on account of the payment into the Fair Fund, fines and penalties required to be paid under the terms of these settlements.

In connection with the settlements, the Company has agreed with the USAO, among other things, to cooperate with the USAO and to maintain and periodically report on the effectiveness of its compliance procedures.

The settlement documents include findings and admissions that may adversely affect existing litigation or cause additional litigation and result in adverse publicity and other potentially adverse impacts to the Company's businesses.

The foregoing summary does not purport to be complete and is qualified in its entirety by reference to the settlement documents with the USAO, MSD, SEC, NASD, NYSE, NJBS and NYAG, copies of which are attached as Exhibits 10.1, 10.2, 10.3, 10.4, 10.5, 10.6 and 10.7, respectively, and are incorporated herein by reference.

Item 7.01 Regulation FD Disclosure.

A copy of the Company's public statement, dated August 28, 2006, confirming the settlements described in Item 1.01 above is furnished herewith as Exhibit 99.1.

Item 9.01 Financial Statements and Exhibits.

(c) Exhibits

10.1 Agreement, dated August 28, 2006, between Prudential Equity Group, LLC ("PEG") and the United States Attorney for the District of Massachusetts ("USAO") and related letter agreement, dated August 28, 2006, between Prudential Financial, Inc. and the USAO.

10.2 Consent Order, dated August 28, 2006, entered into by PEG with the Secretary of the Commonwealth of Massachusetts, Securities Division.

10.3	Order Instituting Administrative Proceedings, dated August 28, 2006, issued by the Securities and Exchange Commission upon acceptance of the Offer of Settlement made by PEG.
10.4	Letter of Acceptance, Waiver and Consent submitted by PEG and accepted on August 28, 2006 by the National Association of Securities Dealers.
10.5	New York Stock Exchange Hearing Board Decision announced on August 28, 2006, accepting Stipulation of Facts and Consent to Penalty.
10.6	Consent Order, dated August 28, 2006, entered into by PEG with the New Jersey Bureau of Securities.
10.7	Assurance of Discontinuance, dated August 25, 2006, entered into by PEG with the Office of the Attorney General of the State of New York.
99.1	Public statement of Prudential Financial, Inc., dated August 28, 2006, confirming settlements of market timing investigations (furnished and not filed).

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

Date: August 28, 2006

PRUDENTIAL FINANCIAL, INC.

By:	/s/ BRIAN J. MORRIS
Name:	Brian J. Morris
Title:	Assistant Secretary

Exhibit Index

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Exhibit 10.1

AGREEMENT

PRUDENTIAL EQUITY GROUP, LLC (“PEG”), formerly known as Prudential Securities, Incorporated (“PSI”), a wholly owned subsidiary of Prudential Financial, Inc. (“Prudential”), by its undersigned attorneys, pursuant to authority granted by the Board of Directors of PEG and Prudential and the United States Attorney for the District of Massachusetts (the “USAO”), enter into this Agreement (the “Agreement”).

WHEREAS, since November 2003, the USAO has been conducting a criminal investigation into allegations that PEG employees were engaged in deceptive trading in mutual fund shares in violation of federal criminal law, including the following: (a) Title 15, United States Code, Sections 78j(b) and 78ff(a), Title 17, Code of Federal Regulations, Section 240.10b-5; (b) Title 15, United States Code, Sections 78o(c)(1)(A) and 78ff(a), Title 17 Code of Federal Regulations, Section 240.15c(1)-2; (c) Title 18, United States Code, Section 1341; (d) Title 18, United States Code, Section 1343; and (e) Title 18, United States Code, Section 2;

WHEREAS, the U.S. Securities and Exchange Commission (“SEC”), the National Association of Securities Dealers (“NASD”), the New York Stock Exchange (“NYSE”), the Secretary of the Commonwealth of Massachusetts (the “Secretary”), the State of New York Attorney General’s Office (“NYAG”), and the New Jersey Bureau of Securities (“NJBS”) (collectively the “Securities Regulators”) have also conducted investigations of PEG into matters related to the deceptive trading in mutual funds, and those investigations of PEG are now concluded in accordance with the terms of this Agreement;

WHEREAS, the USAO investigation of PEG has established, without limitation, the following:

a. From at least 1999 through June 2003, when PSI transferred its domestic retail broker-dealer assets to Wachovia Securities, LLC (“Wachovia”), certain brokers employed by PSI (the “Timer Brokers”) engaged in deceptive and fraudulent trading in shares of mutual funds. Following the asset transfer, the Timer Brokers continued their fraudulent conduct from July 2003 until approximately September 2003, when their employment was terminated;

b. While at PSI and at Wachovia, the Timer Brokers defrauded mutual fund companies (i.e., organizations that manage mutual funds) and mutual funds by employing various deceptive and fraudulent acts and practices to execute prohibited “market timing” trades on behalf of certain PSI clients. From January 2001 through June 2003, the Timer Brokers generated in excess of $50 million in gross commissions and fees for PEG. From July 2003 through September 2003, the Timer Brokers generated in excess of $7 million in gross commissions and fees for Wachovia; and

c. PSI had supervisory responsibility for the Timer Brokers from at least January 1999 through June 2003. During the period of time the Timer Brokers were employed at Wachovia, from July 2003 through September 2003, former PSI supervisors retained supervisory responsibility for the Timer Brokers;

WHEREAS, the USAO has filed criminal charges against a number of former employees of PSI, and PEG acknowledges and accepts responsibility for the conduct of those former employees.

WHEREAS the USAO has informed Prudential and PEG that the USAO has determined that there is a sufficient basis to seek an indictment of PEG for, without limitation, violations of Title 15, United States Code, Sections 78j(b) and 78ff(a), and Title 17, Code of Federal Regulations, Section 240.10b-5;

WHEREAS, the USAO has determined that an indictment of PEG may cause undue harm to innocent individuals, including current employees of PEG and employees and shareholders of affiliated entities who had no involvement in the criminal conduct under investigation; and

WHEREAS, PEG's parent company, Prudential, by and through its Board of Directors, has undertaken certain remedial actions to ensure better control and compliance over PEG and other Prudential affiliated entities and has agreed to continue those efforts by separate letter agreement with the USAO dated August 28, 2006;

NOW, THEREFORE, the USAO and PEG agree as follows:

1. This Agreement shall be in effect for 60 months from the date of its execution.

2. PEG admits to and accepts responsibility for its conduct and the conduct of the Timer Brokers as described in this Agreement and the Statement of Facts incorporated herein and attached hereto as Exhibit A and agrees that certain PEG employees engaged in conduct that was unlawful and fraudulent. PEG also admits to and accepts responsibility for all conduct described in the Statement of Facts. PEG agrees that the Statement of Facts is accurate and further agrees not to contradict the facts stated therein.

3. PEG agrees that, if it violates any terms of this Agreement, the USAO may file the attached criminal Information (the "Information") in the United States District Court for the District of Massachusetts charging PEG with securities fraud, in violation of Title 15, United States Code, Sections 78j and 78ff(a), Title 17, Code of Federal Regulations, Section 240.10b-5. A copy of the Information is attached hereto as Exhibit B. As is set forth elsewhere in this agreement, PEG waives any rights it may have to proceed by way

of indictment and it waives any and all rights it may have under any applicable statutes of limitations or other legal, equitable or constitutional limitations that may limit the period of time during which the USAO may seek an indictment or other charging document (such as a complaint or information) for the offenses covered by the Information.

4. PEG does not endorse, ratify, or condone illegal conduct and, as set forth below, has taken steps to prevent such conduct from occurring in the future.

5. During the term of this Agreement, PEG agrees to cooperate fully with the USAO and with any other agency designated by the USAO regarding any matter about which PEG has knowledge. Pursuant to this paragraph, PEG agrees that cooperation includes but is not limited to the following:

   a. Completely and truthfully disclosing all information with respect to the activities of PEG and its affiliates, and its present and former officers, agents, and employees, concerning all matters that may be inquired into by the USAO;

   b. Assembling, organizing and providing on request by the USAO all documents, records, or other evidence in PEG's possession, custody or control;

   c. Not asserting, in relation to any request of the USAO, a claim of privilege (such as attorney-client privilege) or immunity from disclosure (such as work product) as to any documents or information requested by the USAO related to the conduct described in the Statement of Facts that pre-date September 4, 2003 and, as to any documents, information or testimony that are dated or post-date September 4, 2003, not asserting the attorney-client privilege or other immunity from disclosure as to any documents or information that primarily contain factual information, analyses or compilations of factual information related to the investigations of the USAO and the Securities Regulators. PEG may assert the attorney client-privilege or immunity from disclosure as to documents, information and testimony that are dated or post-date October 1, 2003 for documents or information relating to legal or settlement advice provided to PEG. In making any production to the USAO of the foregoing documents or information, PEG neither expressly nor implicitly waives its right to assert any privilege or immunity from disclosure with respect to the produced documents or information (or any subject-matter covered by such documents, information, or testimony) as to anyone not a party to this Agreement;

d. Using its best efforts to identify witnesses who, to PEG's knowledge, possess material information regarding the matters covered by this Agreement;

e. Using its best efforts to make available for interviews, or for testimony, present or former PEG officers, directors, and employees as requested by the USAO;

f. Providing testimony and other information deemed necessary by the USAO or the court to establish the original location, authenticity, or other evidentiary foundation to admit into evidence documents in any criminal or other proceeding as requested by the USAO;

g. Complying with any agreements between PEG and the SEC or any other governmental agency as long as such agreements remain in effect; and

h. Maintaining PEG as a lawfully organized and adequately capitalized corporate entity for purposes of this Agreement during the time this Agreement is in effect.

6. PEG further agrees that it will not, through present or future attorneys, board of directors, agents, affiliates, parent, officers or employees, make any public statement or filing, including, without limitation, statements or filings in litigation in which the USAO (or the U.S. Department of Justice by and through the USAO) or the Securities Regulators is a party, contradicting any statement set forth in the Information or in the Statement of Facts. Any such contradictory public statement by PEG, its present or future attorneys, board of directors, agents, affiliates, parent, officers or employees shall constitute a material breach of this Agreement, and PEG thereafter would be subject to prosecution on the Information attached to this Agreement. The decision of whether any public statement by any such person contradicting a statement contained in the Information or Statement of Facts will be imputed to PEG for the purpose of determining whether PEG has breached this Agreement shall be at the sole reasonable discretion of the USAO. Upon the USAO's reaching a determination that such a contradictory statement has been made by PEG, the USAO shall so notify PEG. PEG may avoid a breach of this Agreement by publicly repudiating such statement within forty-eight hours after notification by the USAO. This paragraph is not intended to apply to any statement made by any individual in the course of any criminal, regulatory, or civil matter initiated by the USAO or Securities Regulators against such individual, unless such individual is speaking on behalf of PEG. Consistent with PEG's obligation not to contradict any statement set forth in the Information or the Statement of Facts, PEG may take good faith positions in litigation involving any private party.

7. In light of PEG's remedial actions to date and its willingness to (a) acknowledge responsibility for its behavior, (b) cooperate with the USAO and other governmental regulatory agencies, and (c) demonstrate its future good conduct and full compliance with the securities laws, the USAO agrees that if PEG is in full compliance with all of its obligations under this Agreement, the USAO, will not prosecute PEG on the attached Information or on the matters described in the Statement of Facts.

8. Upon execution of this Agreement, PEG shall pay \$600,000,000, with the following payments to be credited against the \$600,000,000:

   \$270,000,000 paid to the Fair Fund administered by the SEC pursuant to an offer of settlement reached between the Securities Regulators and PEG; and

   \$5,000,000 paid to the Secretary of the Commonwealth of Massachusetts as a monetary penalty.

   The balance, \$325,000,000, shall be paid as a monetary penalty allocated as follows: \$300,000,000 to the United States Treasury and \$25,000,000 to the United States Postal Inspection Service Consumer Fraud Fund.

   The payments set forth above are material terms of this Agreement. Failure to make payment upon execution of this Agreement or within 48 hours of execution of this Agreement renders all remaining terms of this Agreement null and void.

9. The parties further agree that should the USAO, in its sole reasonable discretion, determine that PEG (a) has given deliberately false, incomplete, or misleading information under this Agreement, (b) has committed any federal crimes subsequent to the date of this Agreement, or (c) has otherwise committed a willful and knowing material breach of any provision of this Agreement (these three circumstances, (a), (b) and (c) are collectively referred to herein as "Breach"), PEG shall, in the USAO's sole reasonable discretion, thereafter be subject to prosecution(s) for any federal criminal violation, including, without limitation, the Information. Moreover, with respect to any prosecutions relating to deceptive mutual fund market timing transactions that are not time-barred as of the date of this Agreement by the applicable statute of limitations (or any other legal, equitable or constitutional basis upon which a prosecution may be time-barred), PEG agrees that the applicable statute of limitations period (or any other legal, equitable or constitutional basis for barring prosecution based on the passage of time), shall be tolled for a period of time equal to the term of this Agreement. PEG's agreement to toll any applicable statute of limitation (or of any legal, equitable or constitutional basis for barring prosecution based on the passage of time) for the period of time covered by this Agreement means that the time period covered by this Agreement shall not be included in the computation of any time periods for purposes of determining whether any applicable statute of limitation (or of any legal, equitable or constitutional basis for barring prosecution based on the passage of time) bars prosecution of PEG relating to

deceptive mutual fund market timing transactions, including, without limitation the charges set forth in the Information and the conduct set forth in the Statement of Facts. PEG's agreement herein tolling the statute of limitations (and any other legal, equitable or constitutional basis for barring prosecution based on the passage of time) is knowing and voluntary and in express reliance on the advice of counsel.

10. PEG agrees that in the event that the USAO, in its sole reasonable discretion, determines that PEG has committed a Breach: (a) PEG will not contest the filing of the Information nor the admissibility into evidence of the Statement of Facts as a binding admission of PEG; (b) PEG will not contradict the contents of the Information or the Statement of Facts; (c) all statements made by or on behalf of PEG and any employee (current or former), or any testimony given by PEG and any employee (current or former) before a grand jury, the United States Congress, the SEC, or elsewhere, and any leads derived from such statements and testimony, shall be admissible in evidence against PEG if proffered by the USAO in any and all criminal proceedings brought by the USAO against PEG; (d) PEG shall not assert any claim under the U.S. Constitution, the rules of evidence, common law or any other legal or equitable principle, that statements made by or on behalf of PEG prior to or subsequent to this Agreement, or any leads therefrom, should be suppressed; (e) PEG shall not assert that the conduct set forth in the Statement of Facts fails to provide a sufficient factual or legal basis to support the charge set forth in the Information; and (f) PEG will agree that the conduct set forth in this Agreement, including the conduct set forth in the Statement of Facts, violates federal criminal law, including, without limitation, Title 15, United States Code, Sections 78j(b) and 78ff(a), and Title 17, Code of Federal Regulations, Section 240.10b-5, and that the conduct of the Timer Brokers violates these provisions and is chargeable to PSI (and PEG as successor to PSI).

11. The decision whether conduct and statements of any individual will be imputed to PEG for the purpose of determining whether PEG has committed a Breach shall be in the sole reasonable discretion of the USAO.

12. Should the USAO determine that PEG has committed a Breach, the USAO shall provide written notice to PEG of the alleged breach and provide PEG with a two-week period in which to make a presentation to the USAO to demonstrate (a) that no Breach has occurred, (b) that the Breach is not a willful and knowing material breach, or (c) that the Breach has been cured. The parties hereto expressly understand and agree that should PEG fail to make a presentation to the USAO within a two-week period, it shall be conclusively presumed, at the USAO's option, that PEG has committed a Breach. In the event of a Breach that results in a prosecution of PEG, such prosecution may be premised upon any information provided by or on behalf of PEG to the USAO at any time, unless otherwise agreed when the information was provided.

13. PEG agrees that the consequences for a Breach as set forth in this Agreement, including, without limitation, those set forth in paragraph 10 of this Agreement, are remedies to which the USAO is entitled in the event of a Breach and shall survive in the event of a

Breach. PEG further agrees that the USAO's remedies for a Breach are not limited to those set forth in this Agreement. PEG further agrees that in the event of a Breach, PEG shall nevertheless be bound by its waivers of any legal, equitable or constitutional rights set forth in this Agreement, including, without limitation, its waivers in paragraphs 3, 9 and 15 of this Agreement, and those provisions shall survive even in the event of a Breach.

14. PEG agrees that if it sells or merges all or substantially all of its business operations as they exist as of the date of this Agreement to or into a single purchaser or group of affiliated purchasers during the term of this Agreement, it shall include in any contract for sale or merger a provision binding the purchaser/successor to the obligations described in this Agreement.

15. PEG shall expressly waive any rights it may have to a speedy trial pursuant to the Fifth or Sixth Amendments of the United States Constitution, Title 18, United States Code, Section 3161, Federal Rule of Criminal Procedure 48(b), any applicable local rule of the United States District Court for the District of Massachusetts, or any other applicable legal or equitable principle.

16. It is understood that this Agreement is binding on PEG and the USAO, but specifically does not bind any other federal agencies, or any state or local law enforcement or licensing authorities, although the USAO will bring the cooperation of PEG and its compliance with its other obligations under this Agreement to the attention of state and local law enforcement or licensing authorities, if requested by PEG or its attorneys.

17. Nothing in this Agreement restricts in any way the ability of the USAO from proceeding against any individual or entity not a party to this Agreement.

18. This Agreement expires five years from the date of its execution; provided, however, that if on such date, any investigation, prosecution or proceeding relating to the subject matters is then ongoing and is being conducted by the USAO, the SEC or any other federal or state enforcement or regulatory agency with which PEG has been directed by the USAO to cooperate pursuant this Agreement, then this Agreement shall not expire until such investigation, prosecution or proceeding is concluded. Between 30 and 60 days before the expiration of the 60 month period of this Agreement, PEG shall submit to the USAO a written certification that it is in compliance with this Agreement.

19. PEG and the USAO agree that this Agreement, including Exhibits A and B and the letter agreement with Prudential referenced herein, shall be made available to the public.

20. PEG hereby warrants and represents that the Board of Directors of PEG has duly authorized, in a specific resolution, the execution and delivery of this Agreement by PEG, and that the person signing the Agreement has authority to bind PEG.

21. This Agreement may not be modified except in writing signed by all the parties.

22. This Agreement may be executed in counterparts.

23. PEG agrees that should a dispute between PEG and the USAO arise as to the meaning of any of the provisions of this Agreement, any ambiguities as to the terms of this Agreement shall be construed in the favor of the USAO.

PRUDENTIAL EQUITY GROUP, LLC

/s/ Arthur F. Ryan
Chairman and Chief Executive Officer
Prudential Financial, Inc.
on behalf of Prudential Equity Group, LLC

Date: August 28, 2006

/s/ Susan L. Blount
General Counsel
Prudential Financial, Inc.
on behalf of Prudential Equity Group, LLC

Date: August 28, 2006

MICHAEL J. SULLIVAN

/s/ Michael J. Sullivan
United States Attorney
District of Massachusetts

/s/ Michael Loucks
Michael Loucks
First Assistant, U.S. Attorney
District of Massachusetts

/s/ Diane C. Freniere
Diane C. Freniere
Section Chief
District of Massachusetts

/s/ Michael J. Pineault
Michael J. Pineault
Chief, Economic Crimes
District of Massachusetts

/s/ Jack W. Pirozzolo
Jack W. Pirozzolo
Assistant U.S. Attorney

Date: August 28, 2006

EXHIBIT A

STATEMENT OF FACTS

Background

1. Unless a time period is otherwise stated with more specificity, the relevant period of time for purposes of this statement of facts is from January 1999 through September 2003.

2. Immediately prior to July 1, 2003, Prudential Securities, Incorporated ("PSI") was an indirect wholly owned broker-dealer subsidiary of Prudential Financial, Inc. ("Prudential"). Prudential is a publicly-owned holding company, traded on the New York Stock Exchange, whose operating subsidiaries provide a wide range of insurance, investment management and other financial products and services to retail and institutional customers, including insurance brokers and investment managers. Since July 1, 2003, PSI's former U.S. retail securities brokerage business has operated as part of Wachovia Securities, LLC ("Wachovia Securities"). On July 1, 2003, PSI transferred assets including those relating to its U.S. retail securities brokerage operations to a newly formed holding company, now named Wachovia Securities Financial Holdings, LLC ("WSFH"). Prudential presently owns 38% of WSFH and Wachovia Corporation owns 62% of WSFH, with Wachovia Corporation the controlling owner. Unless otherwise stated, the term PSI as used in this Statement of Facts refers to both PSI and Wachovia Securities.

3. Following the asset transfer, PSI converted from a stock corporation into a limited liability company and was renamed Prudential Equity Group, LLC ("PEG"). PEG is a broker-dealer registered with the Commission pursuant to Section 15(b) of the Exchange Act and is a member of the National Association of Securities Dealers and the New York Stock Exchange. PEG provides equity research, sales and trading to domestic and international institutional customers. Prudential continues to own 100% of the equity interests in PEG.

Market Timing

4. A mutual fund is a regulated investment entity that issues shares to the public and typically invests its shareholders' money in a "basket" of underlying securities (e.g., stocks, bonds, etc.). A mutual fund "share" represents an ownership interest in the fund's "basket" of securities. Mutual fund shares are, themselves, securities regulated by the SEC.

5. Typically, mutual fund shares are designed to be long term, "buy and hold," investments. They are managed so as to maximize returns for long term investors in the fund.

6. "Market timing" refers to the practice of making excessive short term trades in shares of mutual funds. Basically, market timing involves frequent movement in and out of mutual funds to exploit inefficiencies in the way mutual funds calculate the value of fund shares,

called the "net asset value" or "NAV." Often, the NAV of mutual fund shares, which is set once a day, does not fully reflect the value of the underlying assets held by a fund. By trading into a fund on a short term basis, a market timer can purchase a mutual fund share at a price (NAV) below the value of the "basket" of underlying assets. Once the shares are re-priced to reflect the change in value of the underlying assets, the market timer can then redeem the shares at the higher share value. Market timing is sometimes referred to as "excessive trading," "abusive trading," "day trading," or "frequent trading." This type of trading includes not only purchases into and redemptions out of a fund family, but also exchanges within a fund family (e.g., shifting funds from a money market fund to an international fund both managed by the same fund family).

7. Market timing comes in different permutations. These permutations include, among others, "time zone arbitrage" and "momentum investing." In "time zone arbitrage," a market timer exploits inefficiencies in the way mutual funds that hold international stocks price the funds' NAV. Typically, a mutual fund calculates its NAV as of 4:00 p.m. U.S. Eastern Time, which is when the major U.S. stock markets close. In the case of a U.S.-based mutual fund holding international stocks, however, the fund's NAV will often be based on the closing price of the underlying international stocks held by the mutual fund. International stocks, however, are often traded on non-U.S. stock markets, which usually close earlier than the United States markets. Asian markets, for example, close early in the morning, even before the United States markets open. Consequently, the prices of the international stocks do not fully reflect the events occurring while the United States markets are open. When the international markets next open, the stocks traded on those markets will typically follow the direction of the stocks in the United States.

8. Thus, if something significant occurs in the United States following the close of the international markets that causes the United States markets to move up, it is highly likely that the price of international stocks will move up the next trading day. The NAV of the U.S. mutual fund holding those stocks, however, is typically based on the earlier closing prices on the international markets. When the fund's NAV is calculated the next day, it will likely include the gain in the international markets that often occurs following the previous day's gain in the United States markets.

9. By quickly entering and exiting an international fund to take advantage of the delay in pricing of the fund's NAV, a market timer can capture that gain without incurring the risk faced by the long term shareholders in the fund. By capturing that gain and then exiting the fund, the timer takes a percentage of the gain away from the long term, buy and hold shareholders (a concept called "dilution").

10. Another form of mutual fund market timing is "momentum investing." In this type of investing a market timer takes advantage of predictable short term movements in the NAV of mutual fund shares based on market indicators. Often, such momentum investing in mutual fund shares focuses on mutual funds trading in less liquid securities, such as small

capitalization stocks or high yield bonds. In such cases, the NAV of mutual funds holding such securities predictably follows market events that affect the value of the underlying securities held by the fund but are not yet reflected in the NAV. This type of timing activity allows a market timer a similar opportunity to capture a gain in the NAV when the NAV catches up to the market event as exists in time zone arbitrage.

11. Market timing in mutual funds can be a very profitable strategy. Market timing, however, often can be harmful to the majority of fund shareholders, who hold mutual funds as long term investments. Market timing harms long term investors by lowering the long term return of funds: it dilutes the value of long term mutual fund shareholders' shares; it raises transaction costs for funds; and it is disruptive to fund management.

12. From at least 1999, PSI became aware that many fund families objected to market timing. PSI was also aware that mutual fund companies maintained policies and procedures to detect and prevent market timing.

13. During the period of time relevant to this Statement of Facts, mutual fund companies had employees whose responsibilities included identifying and stopping market timers. To identify and stop potential market timing, these employees engaged in surveillance of trade activity in the funds. For example, these employees often looked at the trade frequency and also trade size, scrutinizing more carefully trades made over a certain dollar threshold. They also watched trading in certain funds that typically saw more timing activity than others, such as international funds. They also identified accounts (usually by identifying an account number) associated with market timing. When they detected an account owner market timing, they tried to stop the activity, usually by issuing a warning. If the account owner persisted in market timing, they often blocked the account's trading privileges and, in some cases, barred the account owner from trading in the fund company's funds.

14. The term "hedge fund" is a generic term referring to investment pools, usually run by sophisticated investors. Despite the prohibitions on market timing imposed by many mutual fund companies, a number of hedge funds (the "Hedge Funds") employed mutual fund market timing as an investment strategy and, in doing so, used a variety of deceptive and fraudulent practices to defeat mutual fund companies' efforts to detect and block their activity. These Hedge Funds recognized that market timing was a very profitable investment strategy. They also recognized, however, that a significant impediment to their market timing strategy was that, if detected, many of the fund companies would block their market timing trading. Consequently, Hedge Funds engaged in deceptive and fraudulent trading strategies that Hedge Fund personnel referred to as "undisclosed" or "under the radar" market timing. Basically, "under the radar" market timing consisted of masking or disguising market timing trades from the fund companies so that the fund companies would process timing trades that they otherwise would have blocked.

15. As part of their under the radar strategy, some market timing Hedge Funds employed brokers at PSI. From 1999 through September 2003, PSI employed groups of brokers (the “Timer Brokers”) whose business involved servicing market timing Hedge Funds. As “financial intermediaries” (i.e., brokers standing between the Hedge Funds and the mutual fund companies), the Timer Brokers at PSI were well situated to mask their Hedge Fund clients’ trades in order to have the fund companies process trades they would otherwise have rejected. More specifically, PSI had agreements with a large number of mutual fund companies to sell their mutual funds to PSI clients. Accordingly, the Timer Brokers were able to buy, sell, or exchange for their clients shares in a wide variety of mutual funds, including shares in mutual funds run by PSI’s parent company, Prudential (and its affiliates), and shares in mutual funds independent of Prudential (e.g., American Century, Van Kampen Investments, and many others).

16. In addition, every trading day, PSI received from its clients large volumes of trade instructions for mutual fund shares (i.e., buys, sells, exchanges) for many different fund companies. PSI processed its mutual fund trade information through the National Securities Clearing Corporation (“NSCC”), a centralized information service linking financial intermediaries like PSI to a variety of mutual fund companies. Thus, instead of transmitting the trade instructions to each separate mutual fund company directly, PSI transmitted the trade instruction data for a variety of mutual fund companies in bulk to the NSCC which, in turn, transmitted the PSI data out to each of the different fund companies.

17. The Timer Brokers exploited this mutual fund trading system to disguise their clients’ market timing trading from fund companies. Basically, the Timer Brokers recognized that trades processed from PSI over the NSCC system to fund companies relied on identification numbers. The identification numbers sent from PSI included: (a) a number identifying PSI as the brokerage firm; (b) a number identifying the PSI branch generating the order; (c) a number identifying the PSI account (known as a “BIN number”); and (d) a number identifying the particular broker assigned to the account at the time of the trade, called an FA Number (for “financial advisor number”).

18. To stop timing activity from a PSI client or broker, the fund companies first had to identify the exact account number and/or the FA Number associated with the “timer” client or broker. After doing so, many (but not all) fund companies then had the ability to block or reject trades made in accounts or associated with FA Numbers that they had identified as associated with a timer client or broker. Trades from PSI brokers placed under different account numbers and/or associated with different FA Numbers, however, would continue to be processed.

19. By manipulating the identifying information sent by PSI over the NSCC system to the fund companies, the Timer Brokers deceived fund companies into processing trades that they would otherwise have blocked or rejected. Principally, the two categories of identifying information the Timer Brokers manipulated were the PSI account information and the FA Numbers.

20. The Timer Brokers' manipulation of account number information was relatively straightforward. The brokers, working with the Hedge Fund clients, set up and used multiple accounts. Each account had a different account number (or BIN number). Thus, when a particular fund company identified and stopped market timing in one account, the Timer Brokers and their clients traded in another account under a different BIN number, one that had not yet been identified as a timer's account. When that account was flagged and stopped, the Timer Brokers traded in yet another account, and so on.

21. For example, and without limitation, by September 2003, one group of Timer Brokers in Boston had as many as 183 accounts open for seven Hedge Fund clients. Of those 183 accounts, 79 accounts were for a single client. By September 2003, a Timer Broker in Garden City, New York opened in excess of 400 accounts, with nearly 300 accounts for a single timer client.

22. The multiple accounts were often set up with aliases. More specifically, the Timer Brokers and their clients opened accounts using various shell entities with names that did not contain the clients' names. The Timer Brokers and their clients opened these accounts because on some trades sent over the NSCC system, PSI provided the name of the client assigned to the BIN Number. Sometimes, when fund companies saw timing in one account, they identified other accounts with the same or similar names. The fund companies then monitored those accounts and stopped them more quickly when they began timing. The alias accounts made it more difficult for the fund companies both to see that the accounts were linked to a client that had been stopped before in another account and to see that multiple timing accounts were related to one another.

23. In addition to allowing the brokers to place trades in fund families following a block, the multiple accounts allowed the brokers to break their clients' trades into smaller dollar units. The Timer Brokers knew that fund companies often monitored for market timing activity based on certain dollar thresholds. The Timer Brokers knew that larger trades were more likely to be detected than smaller trades. In order to decrease the chances of detection, and to minimize the consequences if detected, the Timer Brokers used the multiple accounts to divide the trades into smaller units.

24. Often, the use of the multiple accounts required the Timer Brokers to shift funds from one account to another. This was accomplished through a process called "journaling." It was a common practice for the Timer Brokers to journal funds from one account that had been stopped by a fund company to another account that had not been stopped in order to keep trading.

25. The Timer Brokers also manipulated the FA Number information provided with their trades. Often, when fund companies identified repeated market timing in accounts associated with a particular FA Number, the fund companies stopped accepting trades in all accounts associated with that FA Number. When that occurred, the Timer Brokers changed the FA Number associated with the accounts. As with the account numbers, when that FA Number was eventually flagged and stopped, the Timer Broker changed the FA Number again, and so on.

26. One way the Timer Brokers obtained new FA Numbers was by adding brokers to their groups. More brokers meant more FA Numbers that could be used to switch around on accounts after a stop. Thus, the Timer Brokers often worked in teams. In some cases, the members of the teams were located in a single branch. In other cases, the Timer Brokers set up deals with brokers in other branches, which provided an additional layer of camouflage for their trading.

27. Another way the Timer Brokers obtained new FA Numbers was to create "Joint" numbers and "Also" numbers. Each broker at PSI had an "individual" FA Number (i.e., a number assigned just to that broker). PSI, however, allowed brokers working in teams to create Joint FA Numbers, which were numbers assigned to more than one broker. PSI assigned Joint numbers purportedly to allow brokers working as teams to set a commission split. In addition, PSI issued a number to brokers called an Also number. Also numbers represented numbers assigned to brokers purportedly to assist particular clients to access their account information electronically, among other things.

28. While there were facially legitimate reasons for obtaining Joint and Also numbers, the Timer Brokers used the numbers to deceive mutual fund companies into processing trades that the mutual fund companies would otherwise have rejected. More specifically, the Timer Brokers used the Joint and Also numbers to conceal from mutual fund companies the fact that the trades were associated with the Timer Brokers.

29. From 1999 through September 2003, the Timer Brokers obtained multiple Joint and Also numbers. In fact, by mid-2003, one group of Timer Brokers in Boston, Massachusetts had obtained at least 14 FA Numbers, including Joint and Also numbers, that they used in connection with their market timing activities. By mid 2003, the Timer Broker in Garden City, New York had as many as 49 Joint and Also FA Numbers.

30. The Timer Brokers used most of these numbers to process trades in fund companies that had previously stopped their trading under another FA Number.

31. In many cases, the multiple accounts and multiple FA Numbers were created with the assistance and permission of PSI branch managers who knew, or were willfully blind to the fact, that the multiple accounts and FA Numbers were set up to evade mutual fund companies' efforts to detect and stop the market timing activity.

32. In addition, the Hedge Funds (and banks that financed the Hedge Funds) participated in the creation of the multiple accounts to deceive the mutual fund companies. The Hedge Funds were also, in some instances, aware of the Timer Brokers' deceptive use of FA Numbers to process the market timing trades in the multiple accounts owned by the Hedge Funds and banks.

33. In certain instances, when employees of the mutual fund companies contacted the Timer Brokers seeking to stop the market timing trading, the Timer Brokers misled the employees of the mutual fund companies. This included providing the employees of the mutual fund companies false and misleading information about the clients and about the clients' trading activities. At times, this also included concealing from the employees of the mutual fund companies the identities of the Timer Brokers and that various Timer Brokers were working together as a team.

34. At least two dozen brokers employed by PSI engaged in the deceptive market timing during the relevant period of time. Specific Timer Broker groups that engaged in the deceptive activity, included, without limitation, the following:

<u>The Boston Brokers</u>

One group of former PSI brokers based in its Boston, Massachusetts branch office (the "Boston Brokers") repeatedly used deceptive practices to circumvent mutual fund restrictions throughout the relevant period of time. The Boston Brokers consisted of a group of three PSI brokers and registered assistants. The group had seven clients for whom it placed market timing trades.

Many of the mutual funds in which the Boston Brokers traded screened for market timing trades by FA Number and customer account numbers. Many fund companies sent notices to PSI that complained that the Boston Brokers' trades had violated trading limitations. Some mutual funds announced steps they had taken to preclude the Boston Brokers from further trading while others asked that PSI take steps to block further trades by the group in the fund.

During the relevant period, the Boston Brokers used at least fourteen FA numbers and 183 customer accounts (for what were, in reality, only seven clients) to circumvent these blocks and avoid new blocks. The Boston Brokers' use of these devices in connection with market timing allowed group members to continue to place trades in funds that had taken steps to preclude them from further trading. Their scheme created the impression that transactions originated from many brokers and represented many different customers. In fact, what appeared to the mutual funds to be thousands of separate transactions submitted by many brokers for many unrelated customers was actually a systematic pattern of market timing by group members on behalf of their seven Hedge Fund clients.

By 2002 and 2003, the head of the Boston Brokers became the top producing broker for the Boston Branch, and was one of the highest producing brokers throughout PSI.

The Garden City Broker

Another former PSI broker, based in its Liberty Plaza and Garden City, New York branch offices (the "Garden City Broker"), also engaged in deceptive practices throughout the relevant period. The Garden City Broker headed a team of brokers and registered assistants, although he very rarely reported to work at any PSI location. He had five clients for whom he placed market timing trades, each of whom acted on behalf of one or more Hedge Funds.

Like the Boston Brokers, the Garden City Broker traded in mutual funds that screened for market timing by FA Number and client account number. During the relevant period, several mutual funds complained to PSI about the Garden City Broker's trading activity. Many mutual funds specifically identified to PSI the deceptive trading strategies the Garden City Broker used to evade blocks the fund companies had imposed.

To evade these blocks, the Garden City Broker maintained as many as 49 different FA Numbers and as many as 400 accounts (for what were, in reality, only five clients). His use of these devices to market time created the impression that the trades originated from many brokers and many customers. By shifting trades from one FA Number to another, or from one customer account to another, the Garden City Broker concealed his identity and was able to place trades in mutual funds that previously had blocked his trading under his other FA numbers and accounts.

From 2001 through 2003, the Garden City Broker was the top producing broker at PSI.

The Special Accounts Brokers

Another group of former PSI brokers based in a New York office known within the firm as "Special Accounts" (the "Special Accounts Brokers") also engaged in deceptive practices throughout the relevant period. The Special Accounts Brokers consisted of a group of two PSI brokers and several registered assistants. The group had three clients for which it placed market timing trades.

To avoid detection by mutual funds, the Special Accounts Brokers used at least 20 FA numbers and hundreds of client accounts (for what were, in reality, only three clients). The Special Accounts Brokers also used "under-the-radar" trading to disguise their customers' trading in funds that previously had taken steps to stop them. The Brokers' use of these devices in connection with market timing deceived mutual funds into accepting trades they otherwise would have rejected. Like the Boston Brokers and the Garden City Broker, the Brokers' Conduct gave the impression that transactions originated from many brokers and represented many different clients.

From 2001 through 2003, the heads of the Special Accounts Brokers group achieved membership in PSI's Chairman's Club, a select group consisting of only the largest producing brokers within the firm.

PSI's Role In the Deceptive Practices

35. During the relevant period of time, mutual fund companies repeatedly sent letters and emails to PSI imposing blocks on further market timing activity by the Timer Brokers. Typically, these communications notified PSI, in writing, that either a customer, as identified by customer account number, or a broker, as identified by the broker's FA number, was engaged in market timing not permitted by the fund, or that the fund was blocking the account or FA number from future trades in the fund or fund family because of impermissible market timing. PSI received repeated, unambiguous, and clear requests from mutual fund companies informing PSI that the market timing trading from the Timer Broker was unwanted. Some of these communications notified PSI that the Timer Brokers were engaged in deceptive practices to continue placing market timing trades. Despite these communications, PSI:

(a) continued to issue Timer Brokers additional accounts for the clients engaged in timing;

(b) continued to issue additional FA Numbers to Timer Brokers that were used with the market timing clients;

(c) failed to utilize controls that could limit the Timer Brokers' ability to engage in the deceptive practices;

(d) failed to comply with mutual fund companies' requests that the market timing conduct of the Timer Brokers cease;

(e) misled some mutual fund companies by representing to them that PSI could and would stop the Timer Brokers from trading in their funds, and then failing to do so;

(f) failed to implement appropriate policies designed to prevent the Timer Brokers from engaging in the deceptive practices; and

(g) failed to impose any discipline upon any of the Timer Brokers even under circumstances where senior PSI managers were actually aware of the Timer Brokers' deceptive conduct.

PSI Management Was Aware Of The Deceptive Practices

36. During the relevant period, mutual fund companies repeatedly sent letters and e-mails to PSI concerning market timing by the Brokers. Many of these communications asked PSI to take steps to stop further trading by a particular customer account or FA number. Some notified PSI that the Timer Brokers were using trading practices to circumvent the fund companies' blocks.

37. For example, in November 1999, a mutual fund company employee wrote to PSI's Mutual Fund Operations department concerning the Garden City Broker's use of multiple customer account numbers to evade restrictions imposed on his trading privileges. The document notified PSI that the Garden City Broker had used a second customer account number to trade in a mutual fund that had taken steps to preclude another of his customer accounts from further trading. The letter notified PSI that the mutual fund had warned the Garden City Broker that "[the] Funds will place a stop purchase, including exchanges, on [one] account … for which you are the Representative of Record. This account was recently transferred from [another] account … with the same registration. We stopped your market timing by freezing purchases in that account. You have continually tried to circumvent our market timing restrictions. This must stop immediately!" PSI failed to investigate the notification, and did not take action against the Garden City Broker for his use of multiple customer accounts to evade blocks the fund company had imposed.

38. Other notices from mutual fund companies identified the strategies used by Timer Brokers to market time. On March 30, 2001, another mutual fund company employee wrote to PSI executives, including the heads of its Risk Management and Mutual Fund Operations departments, about the Timer Brokers' trading practices. The letter highlighted several strategies used by the Timer Brokers to circumvent blocks that the mutual fund company had imposed. These practices included the Timer Brokers' establishment of new broker identifying numbers, their transferring of positions from account to account, and their lowering of trade tickets below certain dollar amounts to disguise their identities to the fund. Although the letter was forwarded to other PSI senior officers and prompted discussions among those senior officers, PSI failed to discipline or sanction any of the Timer Brokers identified by the fund company or to investigate or terminate the practices the mutual fund company had highlighted.

39. In the spring of 2002, another mutual fund company wrote to PSI's head of Mutual Fund Operations concerning the Brokers' methods of market timing that company's mutual funds. The PSI officer forwarded this letter to other PSI officers. The mutual fund's letter noted "what we have seen [s]cares us. It appears certain representatives are changing account registrations, tax id numbers, and branch and rep numbers in an effort to time the (…) funds. All of these accounts have been stopped, but each day 'new' ones pop up." Although the letter again prompted discussions among PSI's officers, including the head of its Private Client Group and the heads of its Risk Management and Mutual Fund Operations divisions, PSI failed to take action against any of the Timer Brokers for their deceptive practices.

40. Finally, on December 19, 2002, another mutual fund company wrote to an employee in PSI's Mutual Fund Operations division concerning some brokers who used deceptive practices to market time in funds across its complex. The employee forwarded the email to PSI's head of Mutual Fund Operations. The email noted that the mutual fund company had placed blocks on 325 of the Timer Brokers' customer accounts but that employees of the mutual fund company each day identified new PSI customer accounts and broker identifying numbers market timing the funds. A second email from the mutual fund company noted that "these reps have multiple rep ids and have continued to add new ones as we block the ids. for our fund complex." Despite this notification, PSI failed to stop the Timer Brokers' continued trading in that company's funds.

<u>PSI Concluded That The Garden City Broker</u>
<u>Used Deceptive Practices To Market Time</u>

41. In May 2002, an employee of PSI's Risk Management department detailed for at least one senior PSI officer the use of multiple FA numbers by the Garden City Broker. The employee's analysis noted that in one 37-day period, the Garden City Broker had 19 different mutual fund companies request that accounts under the broker's control, or the broker as an FA, be blocked from their funds. The analysis concluded that the Garden City Broker had circumvented these requests by changing his FA Number to an Also or Joint number to avoid

detection by the fund, or by changing customer account numbers and moving the assets from the blocked account to a newly established account. Despite this information, the senior officer failed to recommend that the Garden City Broker be disciplined or sanctioned. As a result, PSI failed to stop the Garden City Broker's deceptive conduct.

PSI Did Not Stop The Brokers' Scheme From Continuing

42. Although PSI officers issued policies and procedures that stated that the Timer Brokers' conduct was not permitted, these policies and procedures were ineffective in scope and were never meaningfully enforced. Moreover, even in situations where these policies and procedures purportedly were enforced, PSI officers granted exceptions for its largest producing brokers. As a result, the Timer Brokers continued their deceptive practices even after the policies and procedures were promulgated.

a. In 2001 PSI Created A System That Could Block The Timer Brokers' Trades, But Implemented It In a Way That Allowed The Timer Brokers' Deceptive Conduct

43. In 2001, following complaints from mutual fund companies, and an audit of PSI by Prudential's internal auditors that identified the Timer Brokers' activities as a control risk for the firm, PSI created a blocking system for its mutual fund trading area. This system allowed PSI to block trades from Timer Brokers in accounts or under FA Numbers in response to complaints from mutual fund companies about the timing. This system allowed PSI to block an account from trading (a) in a specific mutual fund, or (b) in an entire mutual fund family. The system also allowed PSI to block a Timer Broker from trading in a mutual fund family by blocking his FA Number and all FA Numbers associated with him.

44. The block system allowed PSI to block trading from a PSI client or Timer Broker when a mutual fund company notified PSI of its objections to the trading. Often the mutual fund companies raised their objections by supplying the BIN numbers of the accounts that they had been able to identify as engaging in the abusive market timing trading. Similarly, mutual fund companies often raised their objections to a particular Timer Broker by supplying the particular FA Number they had identified as being associated with the offending trading. Under the NSCC system applicable to the trading here, the mutual fund companies were unable, on their own, to identify all accounts associated with a particular timer client. Similarly, they were unable to identify all FA Numbers associated with a particular Timer Broker. At all times, the information regarding account numbers of the PSI timing clients and about the FA Numbers associated with a Timer Broker remained with PSI. PSI did not accurately inform the mutual fund companies of the multiple accounts or multiple FA Numbers employed by the Timer Brokers.

45. The PSI blocking system was never implemented to stop the deceptive practices. Instead, often at the request of the Timer Brokers, the PSI blocking system was intentionally implemented in a narrow and limited way in order to allow the Timer Brokers to continue with their deceptive practices. Specifically,

(a) PSI operations personnel placed blocks only on those accounts the mutual fund companies had identified by BIN number in their communications, even if the mutual fund companies had informed PSI that the trading activity was generally prohibited and that the client – not just the account – was prohibited from trading with the mutual fund because of the abusive market timing. The PSI operations personnel did this while being actually aware that the Timer Brokers were utilizing multiple accounts for the same clients in order to defeat the mutual fund companies' attempts to block the trading.

(b) PSI operations personnel placed blocks only on the FA Numbers the mutual fund companies had identified by number in their communications to PSI, even if it was clear that the mutual fund company wanted to ban the Timer Broker, not just a particular FA Number. Moreover, when discussing blocks with fund companies, PSI operations personnel did not inform the mutual funds requesting blocks on brokers that the Timer Brokers had multiple FA Numbers or worked in teams.

(c) In 2002, PSI operations personnel supplied to Timer Brokers information from the block system. The Timer Brokers used this information to place market timing trades in accounts and FA Numbers that had not yet been identified and stopped by the mutual fund companies.

(d) In 2002, senior PSI operations personnel instructed operations personnel to ignore requests from fund companies to stop all activity from named Timer Brokers and instead to limit the blocks only to the FA Numbers mutual fund companies actually listed on their communications – even if the mutual fund company asked that all business from the Timer Broker be stopped.

(e) In 2002, senior PSI operations personnel instructed PSI operations personnel to remove blocks that had been placed on accounts and Timer Brokers. Such blocks were removed despite instructions from the mutual fund companies that PSI should place the blocks on the accounts and Timer Brokers. Such blocks were removed without informing or consulting with the mutual funds that had requested the blocks. In at least one instance, a senior PSI operations executive instructed PSI operations personnel to remove a block after the Garden City Broker asked the PSI senior operations executive to remove the block. The mutual fund company was not informed that the block was removed.

(f) PSI did not supply PSI operations personnel (nor did the PSI operations personnel obtain) complete lists of FA Numbers for the Timer Brokers, even though such lists were available.

(g) In 2003, even when PSI purportedly issued a policy that required PSI operations to block all FA Numbers associated with a Timer Broker when a mutual fund identified a single FA Number to stop, PSI operations did not do so.

(h) In 2002 and 2003, PSI operations personnel in certain instances simply ignored requests from mutual fund companies that Timer Brokers be banned from their funds and that blocks be placed on all FA Numbers and all accounts.

(i) PSI operations also did not block trades in accounts and FA Numbers the Timer Brokers created after a block request from a mutual fund.

b. <u>In June 2002, PSI Instituted A Control Over The Issuance of FA Numbers That Timer Brokers Evaded With The Assistance of Supervisors</u>

46. In June 2002, PSI instituted a procedure concerning the issuance of FA numbers, purportedly in an effort to hinder the Timer Brokers' ability to obtain Joint numbers and Also numbers to evade limitations on market timing (the "June 2002 Control"). The June 2002 Control provided that requests for Joint and Also numbers would require a documented business request and a Regional Business Manager's ("RBM's") approval. Branch Managers and RBM's were instructed that no new Joint or Also numbers were to be issued for purposes of market timing in mutual funds.

47. The June 2002 Control failed to preclude the Timer Brokers from misusing previously issued Joint and Also numbers to evade blocks imposed by mutual fund companies. Indeed, the Garden City Broker obtained 12 new Joint and Also numbers just days before the procedure took effect, purportedly to assist him in transferring customer accounts from one PSI branch office to another.

48. The June 2002 Control also did not subject the Timer Brokers to any form of discipline or sanction if they continued to use Joint and Also numbers to evade blocks in violation of its terms.

49. The June 2002 Control was also intentionally circumvented by Timer Brokers, in some cases, with the assistance of a Branch Manager. To obtain new FA Numbers, the Timer Brokers provided intentionally false and misleading justifications for why a new Joint or Also number should be issued. In some instances, the Timer Brokers lied and falsely stated that the new Joint numbers were needed for a new client relationship or new commission split arrangement. In fact, once the new FA Numbers were issued, the Timer Brokers used them for deceptive purposes, and did not use them for new clients or for new commission split arrangements.

50. In at least one instance in April 2003, PSI management, including an RBM and a employee in PSI's Risk Management department, became aware that the Boston Brokers had obtained a Joint FA Number in January 2003 by providing misleading and false information on the form. Despite this unambiguous and explicit circumvention of the June 2002 Control, PSI took no disciplinary action against the Boston Brokers. The RBM did, however, instruct the Branch Manager to issue no further FA Numbers to the Boston Brokers. Notwithstanding that explicit instruction, the Branch Manager signed off on request forms requesting issuance of three new Joint FA Numbers to the Boston Brokers for use on accounts set up for a new market timing client. The Boston Brokers and Branch Manager intentionally did not disclose on the request form that the FA Numbers would be used for market timing or for a market timing client. Nor did they present the form to the RBM for signature, instead arranging to have a more senior executive (a "Regional Officer") sign off on the request. The Boston Brokers quickly thereafter used one of the new FA Numbers to place trades in fund companies that had previously banned the Boston Brokers.

c. In January, 2003, PSI Issued – But Never Implemented – A Market Timing Policy

51. As part of the 2001 internal audit process conducted by Prudential, internal auditors from Prudential requested that PSI issue a policy restricting market timing. Internal audit set a deadline for issuance of the policy for the end of 2001. No such policy was issued in 2001, and the internal audit staff agreed to extend the deadline to the end of 2002. During 2002, PSI senior management discussed issuing a policy designed to curtail the deceptive practices associated with market timing by the Timer Brokers.

52. Prior to 2002, PSI had on at least two other occasions issued market timing policies. The first, which was issued in 1999, prohibited brokers from engaging in market timing trades in a PSI trading platform called “PruChoice.” PruChoice was a fee-based (as opposed to transaction-based) mutual fund trading platform, which was abused by market timers and Timer Brokers. The second, which was issued in 2000, prohibited market timing in the mutual funds of PSI’s affiliated mutual fund company, Prudential Investments. Both policies placed explicit limits on the number of exchanges (one “round trip” in 90 days) that a broker could make before being in violation of the policy. The policies provided no sanction for violation, and although the Timer Brokers repeatedly violated the policies, PSI did not take action against any Timer Broker who violated the policies.

53. In mid-2002, after PSI senior management was informed of multiple instances of deceptive conduct on the part of the Timer Brokers and after PSI senior management had advised Prudential internal auditors that PSI would issue a policy on market timing, PSI senior management undertook to create a policy on market timing. In the summer of June 2002, PSI compliance personnel proposed a policy (the “Proposed Policy”) that was similar to that issued in 1999 for PruChoice and in 2000 for Prudential Investments. The Proposed Policy limited the number of exchanges and trades in a mutual fund to one round trip per 90 days and provided for sanctions to the brokers in the case of violations.

54. During the Summer of 2002, PSI senior management met to discuss the Proposed Policy. At that meeting, compliance officers addressed the problems with market timing, including the Timer Brokers’ use of deceptive practices and the fact that the Proposed Policy was similar to that which PSI had issued restricting market timing in the affiliated mutual funds run by Prudential Investments. During that meeting, PSI senior managers expressed concerns that the Proposed Policy would have too great an impact on the Timer Brokers’ revenues. At the time, the Timer Brokers represented several of the highest revenue producers at PSI. A senior PSI manager dismissed reports from compliance officers that other broker-dealers had restricted market timing, expressing the view that even if the other broker-dealers had such policies, the broker-dealers were not following them. That same senior PSI manager then

dismissed the concerns expressed by the compliance officers by saying that restricting the Timer Brokers' business would put PSI at a competitive disadvantage and that he did not want PSI to be the "shiniest ship at the bottom of the sea."

55. No policy was issued in 2002. On January 8, 2003, however, PSI finally issued a market timing policy (the "Market Timing Policy"). PSI rejected the Proposed Policy and intentionally departed from the prior policies it had issued. The Market Timing Policy left monitoring of inappropriate market timing activities to the mutual fund companies themselves. Specifically, it provided that "inappropriate timing activities [would] continue to be monitored" by mutual fund companies and not by PSI itself.

56. The Market Timing Policy provided for the imposition of sanctions, including termination of employment, for the Timer Brokers' use of "manipulative techniques" to evade mutual fund trading restrictions. The Market Timing Policy included within the category of "manipulative techniques" the deceptive practices used by the Timer Brokers (including the use of multiple accounts and multiple FA Numbers) to defraud the mutual fund companies into processing market timing trades that the mutual fund companies otherwise would have rejected. Under the terms of the Market Timing Policy, any imposition of sanctions was to be decided by a committee consisting of members of PSI's Legal, Compliance, and Risk Management divisions.

57. Despite issuing the Market Timing Policy, PSI failed to implement and enforce it. Despite notifications of continuing "manipulative techniques" received by PSI after it issued the Market Timing Policy, PSI failed to form this committee or take action against any of the Timer Brokers to stop their use of "manipulative techniques." Despite repeated violations of the Market Timing Policy by multiple Timer Brokers, including violations explicitly brought to the attention of PSI management, not a single Timer Broker received any sanction or discipline under the policy.

58. PSI also failed to implement the Market Timing Policy in material respects. Specifically, the Market Timing policy provided that, in the event a mutual fund company asked PSI to block any one of a Timer Broker's FA Numbers, all FA Numbers belonging to the Timer Broker similarly would be blocked from trading. PSI never implemented that part of the Market Timing Policy. In fact, despite the policy's clear mandate, PSI continued to interpret mutual fund block requests in the same narrow manner as it had previously – blocking only the specific FA Number or customer account number identified by mutual fund block requests, even if the mutual fund requested a broader block. Indeed, in some instances, PSI failed to implement blocks on FA Numbers specifically identified by mutual fund companies as numbers to be blocked.

59. Thus, even after issuance of the Market Timing Policy, PSI failed to prevent the Timer Brokers from continuing their scheme of switching to unblocked FA numbers or customer accounts to evade blocks imposed by mutual fund companies.

The Timer Brokers' Deceptive Conduct Continued While At Wachovia

60. On July 1, 2003, the Timer Brokers became employees of Wachovia following the transfer of PSI's assets to Wachovia. The Timer Brokers' supervisors also became Wachovia employees, as did PSI senior management. From July 1, 2003, through September 8, 2003, the Timer Brokers continued using the deceptive practices to place market timing trades in mutual funds while under the supervision of the former PSI senior management.

61. On September 8, 2003, Wachovia issued a policy that prohibited market timing. The Timer Brokers' deceptive practices ceased shortly thereafter.

The Timer Brokers' Conduct is Chargeable to PSI

62. PSI accepts responsibility for the Timer Brokers' deceptive and fraudulent conduct. The Timer Brokers' deceptive conduct occurred while they were at PSI. In some instances it occurred with the assistance of the Timer Brokers' supervisors, including their Branch Managers. PSI senior management also either knowingly permitted the Timer Brokers' deceptive conduct or were willfully blind to such conduct and failed to stop the conduct. PSI also profited from the Timer Brokers' conduct. For the period 2001 through 2003, gross commission revenue generated from the timing activities of the Timer Brokers totaled approximately $57 million, with illicit profits to the Timer Brokers' clients of in excess of $100 million.

EXHIBIT B

UNITED STATES DISTRICT COURT
DISTRICT OF MASSACHUSETTS

UNITED STATES OF AMERICA	)	CRIMINAL NO.:
v.	)	VIOLATION: 15 U.S.C. §§ 78j(b) & 78ff(a) (Securities Fraud)
PRUDENTIAL EQUITY GROUP LLC, Defendant.	)	

INFORMATION

The United States Attorney Charges:

COUNT ONE
Securities Fraud

From on or about January 1, 1999 through on or about June 30, 2003, in the District of Massachusetts and elsewhere,

PRUDENTIAL EQUITY GROUP, LLC, a/k/a
PRUDENTIAL SECURITIES, INCORPORATED

defendant herein, did knowingly and willfully, by the use of means and instrumentalities of interstate commerce and of the mails, directly and indirectly aided and abetted others in (a) employing a device, scheme and artifice to defraud, (b) making untrue statements of a material fact and omitting to state a material fact necessary in order to make statements made, in light of the circumstances under which they were made, not misleading, and (c) engaging in acts, practices and courses of business which operated as a fraud and deceit upon persons, in connection with the purchase and sale of securities, all in violation of 15 U.S.C. §§ 78j(b) & 78ff(a) and 17 C.F.R. § 240.10b-5 and 18 U.S.C. § 2.

MICHAEL J. SULLIVAN
UNITED STATES ATTORNEY

Jack W. Pirozzolo
Assistant United States Attorney

DISTRICT OF MASSACHUSETTS

U.S. Department of Justice

Michael J. Sullivan
United States Attorney
District of Massachusetts

Main Reception: (617) 748-3100

John Joseph Moakley United States Courthouse
1 Courthouse Way
Suite 9200
Boston, Massachusetts 02210

Date: August 28, 2006

Robert S. Bennett, Esq.
Skadden, Arps, Slate, Meagher & Flom LLP
1440 New York Avenue, N.W.
Washington, D.C. 20005-2111

Neal E. Sullivan, Esq.
Bingham McCutchen, LLP
2020 K Street, N.W.
Washington, D.C. 20006

Re: Prudential Financial, Inc. and Prudential Equity Group LLC

Dear Mr. Bennett and Mr. Sullivan:

This letter sets forth the agreement ("Compliance Agreement") between the United States Attorneys' Office for the District of Massachusetts (the "USAO") and Prudential Financial, Inc. ("Prudential").

The USAO is conducting a criminal investigation into fraudulent conduct at Prudential Securities, Incorporated ("PSI"), now known as Prudential Equity Group, LLC ("PEG") (unless otherwise stated, PEG and PSI are collectively referred to herein as "PEG"). In connection with that investigation, PEG and the USAO have entered into an Agreement ("Agreement") dated August 28, 2006. The USAO agrees that if PEG complies with its obligations under the Agreement, the USAO will not prosecute PEG or any of its affiliated companies, or their joint venture partners, including Wachovia Securities LLC, for any mutual fund market timing conduct investigated by the USAO or relating to matters described in the Statement of Facts or the Statements of Facts in the agreements related to mutual fund market timing practices between PEG or any of their affiliated companies, or their joint venture partners, including Wachovia Securities LLC and the U.S. Securities and Exchange Commission, the National Association of Securities Dealers, the New York Stock Exchange, the Secretary of the Commonwealth of Massachusetts, the State of New York Attorney General's Office, and the New Jersey Bureau of Securities.

As further set forth in the Agreement, the USAO has entered into the Agreement in part because Prudential has undertaken certain remedial actions to ensure better compliance controls over PEG and other Prudential affiliated entities. By this letter, Prudential agrees to continue its remedial efforts for a period of 60 months from the date of the Agreement. More specifically, Prudential agrees to the following:

1. This Compliance Agreement shall remain in effect for the duration of the Agreement.

2. Prudential will continue to cooperate with the USAO with respect to the activities covered by the Agreement. Prudential's cooperation will include truthful disclosure of all information known to it regarding the matters addressed in the Agreement. Prudential's cooperation will also include making available employees knowledgeable of the subject matter covered by the Agreement. Notwithstanding the provisions of paragraphs 5(h) and 14 of the Agreement, Prudential may cause the sale or merger of PEG or the transfer of all or substantially all of its business operations without binding the acquiring or successor entity to the terms of the Agreement, provided that in no event may Prudential cause PEG to cease to exist such that it could not be subject to the filing of the Information as set forth in paragraph 10 of the Agreement.

3. Prudential agrees to maintain the policies and procedures relating to the integrity of compliance functions ("Compliance Plan") at its various affiliated entities, as set forth in Exhibit A attached to this Compliance Agreement. Nothing in this Compliance Agreement precludes Prudential from amending or changing its Compliance Plan following the date of this Compliance Agreement, so long as such changes or amendment do not diminish the Compliance Plan.

4. Prudential agrees to make periodic reviews of its Compliance Plan to determine the following:

   a) that the Compliance Plan is appropriately designed to accomplish its goals; and

   b) that Prudential is, in fact, implementing the Compliance Plan.

5. Prudential agrees that oversight of the Compliance Plan (as to both design and implementation) shall remain the responsibility of the Prudential General Counsel. The General Counsel shall report on the effectiveness of the Compliance Plan to the Audit Committee of the Prudential Board of Directors on a semi-annual basis. Copies of those reports shall be submitted to the USAO within two weeks of each presentation, along with a certification from the General Counsel that the report contains all material information bearing on the effectiveness of the Compliance Plan. To the extent Prudential determines that any information in those reports is within the scope of the attorney-client privilege, Prudential may redact the portions of the reports it deems privileged from the copies submitted to the USAO.

6. Prudential may, at its option, delegate an audit firm and/or consulting firm and/or outside attorney to assist the General Counsel in assessing the design and implementation of the Compliance Plan. Notwithstanding the preceding sentence, the General Counsel shall continue to be responsible for the effectiveness of the design and implementation of the Compliance Plan and the Audit Committee of the Board of Directors shall be responsible for its oversight.

Very truly yours,

MICHAEL J. SULLIVAN
United States Attorney

/s/ Michael J. Sullivan

Agreed:
PRUDENTIAL FINANCIAL, INC.

By: /s/ Robert S. Bennett
Robert S. Bennett, Esq.
Counsel Prudential Financial, Inc.
Board of Directors
Date: August 28, 2006

/s/ Neal E. Sullivan
Neal E. Sullivan, Esq.
Counsel for Prudential Financial, Inc.
Date: August 28, 2006

PRUDENTIAL FINANCIAL, INC.

By: /s/ Susan L. Blount
Susan L. Blount
Senior Vice President & General Counsel
Date: August 28, 2006

EXHIBIT A

COMPLIANCE PLAN

A. PRUDENTIAL FINANCIAL, INC. ("PRUDENTIAL") COMPLIANCE ORGANIZATION REPORTING STRUCTURE

1. PURSUANT TO THE JANUARY 2004 COMPLIANCE REORGANIZATION, THE COMPLIANCE FUNCTION IS THE RESPONSIBILITY OF THE SENIOR VICE PRESIDENT AND GENERAL COUNSEL OF PRUDENTIAL

2. PURSUANT TO THE JANUARY 2004 COMPLIANCE REORGANIZATION, ALL REPORTING CHANNELS FLOW TO THE SENIOR VICE PRESIDENT AND GENERAL COUNSEL OF PRUDENTIAL INDEPENDENT OF THE BUSINESS UNITS[1]

3. THE BUSINESS UNITS COVERED BY THIS REPORTING STRUCTURE INCLUDE: (1) INSURANCE DIVISION, (2) INTERNATIONAL DIVISION, (3) INVESTMENT DIVISIONS, AND (4) CORPORATE FUNCTIONS, AS SET FORTH IN THE PRUDENTIAL ORGANIZATIONAL CHART DATED MAY 5, 2006 AND ATTACHED AT TAB [1]

B. SUBSTANTIVE RESPONSIBILITIES OF PRUDENTIAL'S COMPLIANCE ORGANIZATION

1. CORPORATE COMPLIANCE AREA

- AUDIT COMMITTEE REPORTING
- COMPANY POLICIES AND PRINCIPLES
- SECURITIES REGISTRATION, INSURANCE LICENSING AND APPOINTMENTS
- PRE-EMPLOYMENT CREDIT, CRIMINAL AND SALES PRACTICE BACKGROUND CHECKS
- EMPLOYEE SECURITIES ACCOUNT MONITORING

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1 Where required by law or regulation, formal business unit reporting lines are in place in addition to the compliance line. Also, senior business executives sometimes refer to the compliance personnel assigned to a business as reporting to them on an "administrative" or "dotted line" basis to signify the dedication of that resource to that business, while recognizing the reporting relaitonship that ultimately flows to the Senior Vice President/General Counsel.

- CERTAIN SEC FILINGS, E.G., SECTIONS 13 AND 16 AND FORM ADVS
- REGULATORY EXAMINATION MANAGEMENT AND REPORTING
- ERISA MONITORING
- ANTI-MONEY LAUNDERING AND OFAC MONITORING
- PRIVACY MONITORING AND REPORTING
- DESIGN COMPLIANCE TRAINING; DELIVER WHERE APPROPRIATE
- FCPA MONITORING

2. BUSINESS UNITS
    - INTERNAL EXAMINATIONS AND REVIEWS OF BROKER DEALERS, INVESTMENT ADVISORS, INVESTMENT COMPANIES AND INSURANCE COMPANY SEPARATE ACCOUNTS
    - SEC COMPLIANCE PROGRAM RULES, AND NASD BROKER-DEALER TESTING AND REPORTING REQUIREMENTS
    - CUSTOMER ACCOUNT TRANSACTION MONITORING
    - PORTFOLIO AND INVESTMENT GUIDELINE MONITORING
    - GIFT AND ENTERTAINMENT MONITORING AND REPORTING
    - INVESTIGATE AND RECOMMEND DISCIPLINE FOR EMPLOYEE COMPLIANCE MISCONDUCT
    - SALES MARKETING AND ADVERTISING MATERIAL REVIEWS & RELATED INSURANCE AND NASD FILINGS
    - BUSINESS UNIT COMPLIANCE MANUALS OF POLICIES AND PROCEDURES
    - DESIGN AND, IN SOME CASES, DELIVERY OF BUSINESS UNIT COMPLIANCE TRAINING
    - TRACK AND MONITOR IMPLEMENTATION OF NEW LAWS AND REGULATIONS
    - RESPONDING TO REGULATORY INQUIRIES

C. PRUDENTIAL ENFORCEMENT OF COMPLIANCE POLICIES AND PROCEDURES

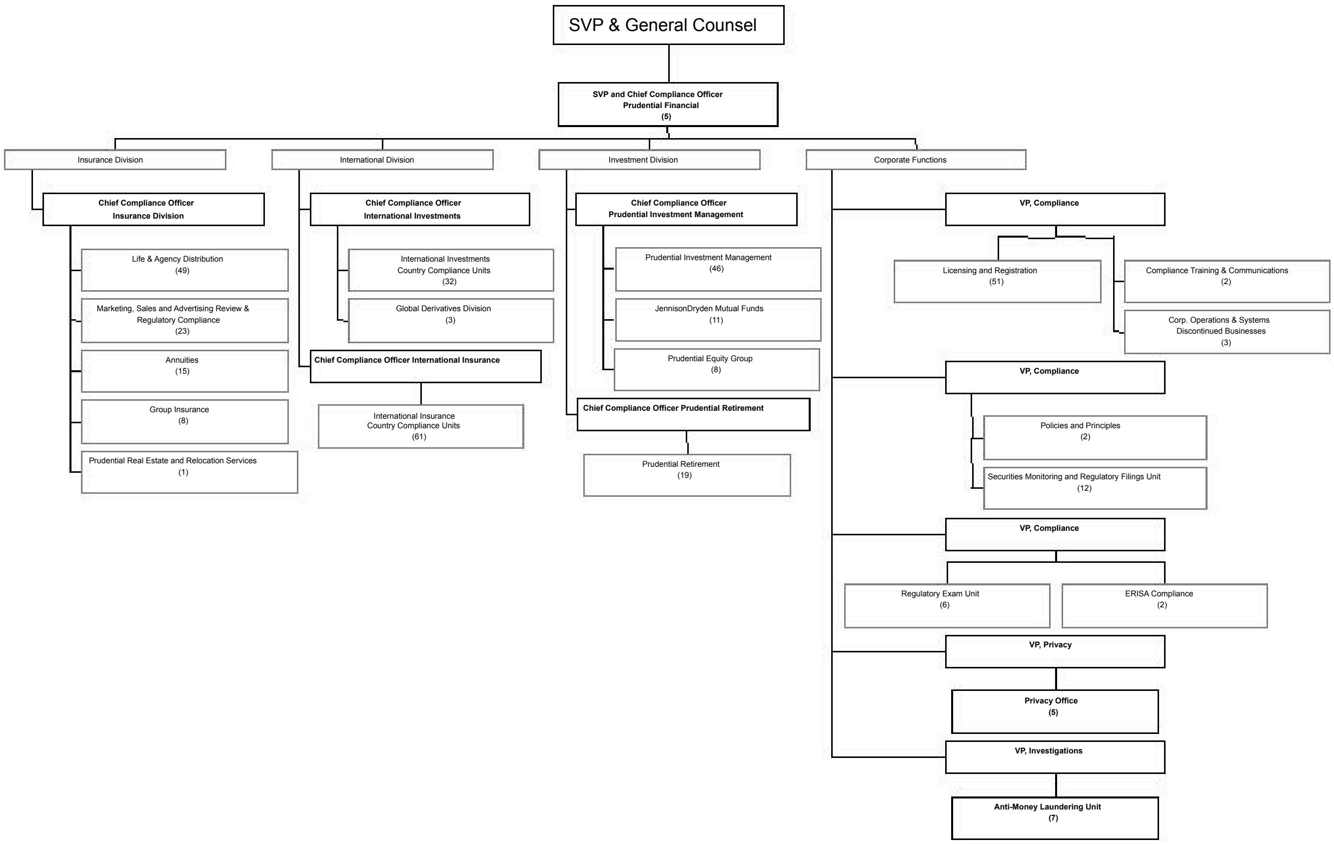
1. PREVENTION OF COMPLIANCE FAILURES AND VIOLATIONS

- BUSINESS ETHICS STATEMENT OF POSITION
- PERFORMANCE REVIEW METRIC INCLUDING "PROMOTION OF COMPLIANCE AND ETHICS" AS METRIC OF EMPLOYEE PERFORMANCE
- ETHICS TRAINING PROGRAMS AS INSTITUTED IN JANUARY 2005
- CONTINUED TRAINING ON ETHICS, ANTI-MONEY LAUNDERING, PRIVACY, AND FRAUD-RELATED ISSUES
- REVISE COMPLIANCE POLICIES AND PROCEDURES MANUAL AS NEEDED TO IMPROVE COMPREHENSION AND EFFECTIVENESS
- MODIFY COMPLIANCE POLICIES AND PROCEDURES AS NEEDED TO ADDRESS DETECTED WEAKNESSES OR FAILURES AND TO ENSURE PROPER CONTROLS OVER EMERGING COMPLIANCE ISSUES
- PERIODIC TESTING OF COMPLIANCE POLICIES AND PROCEDURES TO ASSESS EFFECTIVENESS

2. ACTION TAKEN FOR COMPLIANCE VIOLATIONS AND FAILURES

- RECOMMEND APPROPRIATE DISCIPLINARY ACTION AGAINST ANY EMPLOYEES VIOLATING COMPLIANCE POLICIES OR PROCEDURES
- RECOMMEND APPROPRIATE DISCIPLINARY ACTION AGAINST SENIOR MANAGEMENT, BUSINESS UNIT LEADERS AND SUPERVISORS FOR COMPLIANCE FAILURES OR VIOLATIONS OF COMPLIANCE POLICIES OR PROCEDURES

Distribution of Compliance Personnel



May 5, 2006

Exhibit 10.2

COMMONWEALTH OF MASSACHUSETTS
OFFICE OF THE SECRETARY OF THE COMMONWEALTH
SECURITIES DIVISION
ONE ASHBURTON PLACE, 17TH FLOOR
BOSTON, MASSACHUSETTS 02108

IN THE MATTER OF:	)	
	)	
PRUDENTIAL EQUITY GROUP, LLC, Formerly Known As PRUDENTIAL SECURITIES INCORPORATED	)	DOCKET NO. E-2003-075
	)	
Respondent.	)	

CONSENT ORDER

This Consent Order ("Order") is entered into by the Massachusetts Securities Division ("Division") and Respondent Prudential Equity Group, LLC, formerly known as Prudential Securities Incorporated ("Respondent") with respect to the administrative complaint ("Complaint") filed against Respondent in which the Enforcement Section of the Division alleges that the Respondent has violated the Massachusetts Uniform Securities Act, M.G.L. c. 110A ("Act") and the corresponding regulations promulgated thereunder ("Regulations"). This Order is the final settlement of those allegations set forth in the Complaint.

On August 28, 2006 Respondent submitted an Offer of Settlement (the "Offer") for the purpose of disposing of only those allegations set forth in the Complaint. Solely for the purpose of settlement, the Respondent admits to the Division's Statements of Fact set out in the Offer and consents to the entry of this Order. Therefore, the Division sets forth the following facts and legal conclusions:

I. JURISDICTION AND AUTHORITY

1. The Massachusetts Securities Division is a division of the Office of the Secretary of the Commonwealth with jurisdiction over matters relating to securities, as provided for by the Act.

2. The Act authorizes the Division to regulate: (a) the offers and/or sales of securities; (b) those individuals offering and/or selling securities; and (c) those individuals transacting business as registered agent-dealers and investment advisers within the Commonwealth.

3. The Division brings this action pursuant to the enforcement authority conferred upon it by Section 407A of the Act and M.G.L. c. 30A, wherein the Division has the authority to conduct an adjudicatory proceeding to enforce the provisions of the Act and all corresponding Regulations promulgated thereunder.

II. RESPONDENT

4. Prior to July 1, 2003, Prudential Securities Incorporated ("PSI") was a wholly-owned broker-dealer subsidiary of Prudential Financial, Incorporated ("Prudential Financial"). Prudential Financial is a publicly-owned holding company traded on the New York Stock Exchange ("NYSE"). On July 1, 2003, PSI transferred the assets relating to its U.S. retail securities brokerage operations to a newly formed holding company, now named Wachovia Securities Financial Holdings, LLC ("WSFH"). Prudential Financial presently owns 38% of WSFH and Wachovia Corporation owns 62% of WSFH. Since July 1, 2003, PSI's former U.S. retail securities brokerage business has operated as part of Wachovia Securities, LLC. Following the asset transfer, PSI converted from a stock corporation into a limited liability company and was renamed Prudential Equity Group, LLC ("PEG"). PEG is a broker-dealer registered with the Securities and Exchange Commission ("SEC") pursuant to Section 15(b) of the Securities

Exchange Act of 1934 and is a member of the National Association of Securities Dealers (“NASD”) and the NYSE. Prudential Financial continues to indirectly own 100% of the equity interest in PEG. PEG is a registered broker-dealer in Massachusetts, Central Registration Depository Number 7471, with a main business address of One New York Plaza, 15th Floor, New York, New York 10292-2015.

III. INITIATION OF FORMAL INVESTIGATION

5. In July of 2003, the Division received information from a former PSI registered agent alleging that certain registered agents of the PSI Boston branch office were engaged in market timing of mutual fund shares, PSI management knew of this activity, and PSI failed to take the necessary action to stop it.

6. These PSI registered agents included Martin Druffner, Skifter Ajro and Justin Ficken (the “Druffner Group”).

7. The former registered agent alleged that the Druffner Group made a multi-million dollar business out of trading in and out of mutual funds to make quick profits at the expense of long-term shareholders and on behalf of sophisticated clients, primarily large hedge funds.

8. The former registered agent further indicated that trades and exchanges were routinely placed by these PSI registered agents on a daily basis between 3:30 and 4:00 p.m.

9. The trading volume was so excessive that certain PSI operations employees were instructed to only work on putting these trades through.

10. The former registered agent also alleged that the market timers in the PSI Boston office were given preferential treatment including, re-assigned accounts, assistants and bonuses.

11. Furthermore, the former registered agent alleged that PSI management was not concerned with eliminating market timing at the Boston branch because of the revenue it generated.

12. Based on this initial information and evidence obtained by the Division regarding PSI's Boston branch, on September 3, 2003 the Division forwarded PSI a subpoena duces tecum for records and authorized a formal investigation into PSI to determine whether certain business practices had violated provisions of the Act.

13. Beginning in at least September 1999 and continuing through at least June 2003 ("Relevant Time Period"), the Division uncovered that certain PSI Boston registered agents used deceptive trading practices to conceal their identities, and those of their customers, to evade mutual funds' prospectus limitations on market timing.

IV. STATEMENTS OF FACT

A. <u>PSI's Knowledge of the Disruptive Impact of Market Timing</u>

14. Prior to 1998, PSI did not have a formal market timing policy.

15. PSI understood that market timing and excessive short-term trading could make it difficult for fund managers to implement investment strategies.

16. In 1999, PSI registered agents were prohibited from market timing activity within the PruChoice product that PSI offered.

17. The market timing prohibition applied to all wrap fee programs and defined market timing to include more than one trade per quarter or more than four trades per year.

18. All large purchases and redemptions within the PruChoice product were carefully scrutinized by PSI, and the Druffner Group's market timing accounts within the wrap products were terminated.

19. The policy did not apply to non-proprietary mutual funds unless they were purchased and sold in a wrap fee program.

B. PSI's Obligations to Mutual Fund Companies

20. PSI settled its trades through the National Securities Clearing Corporation's Fund/SERV system ("Fund/SERV").

21. The degree of information that a mutual fund company received from PSI varied depending on the "networking level" chosen by PSI.

22. The information provided via Fund/SERV generally included, among other things, a financial adviser number identifying the registered agent(s) ("FA number"), the registered agent(s) name, the client's account number, and the client's name.

23. During the Relevant Time Period, certain mutual fund companies regularly sought PSI's assistance to stop registered agents from market timing using, in part, the information received via Fund/SERV to identify the registered agent and/or client.

24. The mutual fund companies would submit written requests to PSI directing that a registered agent be stopped by either identifying the registered agent(s) by name or FA number, or by identifying the client by name or account number.

C. PSI's Failure to Supervise the Boston Branch

25. Mutual fund companies identified registered agents within PSI, and specifically the Boston branch, as known market timers.

26. Mutual fund companies sent PSI numerous letters and e-mails advising that they would block certain registered agents from trading shares of mutual funds due to market timing activity or requesting PSI's assistance in blocking such activity.

27. Despite these warning and/or termination letters, PSI registered agents, specifically members of the Druffner Group, engaged in a deceptive scheme and course of business to expand their hedge fund clients' timing capacity in various mutual funds.

28. The Division has evidence that the Druffner Group acquired additional FA numbers, obtained multiple account numbers, utilized different tax identification numbers, and journaled money from one account to another in order to circumvent the mutual funds' market timing defenses.

29. PSI branch management had the capability to stop the market timing activities of the Druffner Group, but failed to take the necessary action to adequately supervise the registered agents.

D. Failure to Prevent the Issuance of New FA numbers for the Purpose of Market Timing

30. Once a mutual fund company blocked a registered agent by FA number for market timing, one way to avoid the block was to trade with a different FA number.

31. Because mutual fund companies were trying to block the market timing trades of the Druffner Group, as identified by their FA numbers, the Druffner Group obtained multiple FA numbers to avoid detection.

32. Prior to June 2002, the Druffner Group could obtain new FA numbers by making an oral request to a PSI branch manager, administrative manager or directly to the commissions department.

33. Boston branch manager(s) approved and delegated approval for the issuance of new FA numbers for the Druffner Group.

34. In addition to individual FA numbers, all three members of the Druffner Group were issued a "Joint" FA number and used these "Joint" FA numbers to execute trades and avoid detection.

35. All three individual members of the Druffner Group were issued an “Also” FA number and used these “Also” FA numbers to execute trades and avoid detection.

36. On June 21, 2002, PSI issued a new policy for obtaining additional FA numbers, Joint FA numbers and “Also” FA numbers.

37. PSI required a “FA Production Number Request/Change Form” to be completed and a business rationale given for such a request.

38. The request for an additional FA number required approval from both the branch manager and the regional business manager.

39. Even after the new 2002 policy, the Boston branch manager approved and delegated approval for the issuance of new FA numbers for members of the Druffner Group.

40. The Division has evidence that the Druffner Group sought to obtain these additional FA numbers as a tool to conceal their identities as market timers.

41. The Druffner Group continued to obtain additional FA numbers by alleging that the new numbers were needed for commission splits.

42. However, at all times the overall commission split for the Druffner Group remained: Druffner 70%, Ficken 20% and Ajro 10% regardless of which FA number the group utilized for an account, an individual trade or an exchange.

43. The Druffner Group created their own pool of FA numbers with which to trade in direct violation and avoidance of the PSI policy that was intended to eliminate the use of multiple FA numbers to evade the mutual funds’ market timing police.

44. The Boston branch manager knew, or should have known, that the Druffner Group’s purpose for requesting new FA numbers was to further the market timing activity.

45. PSI did not make inquiries either during branch audits or at any other time as to the issuance of multiple FA numbers such as: the Ajro/Druffner number, the Druffner/Ajro number, the Druffner/Ficken number, the Ficken/Druffner number, the Ajro/Ficken number, the Ficken/Ajro number, the Druffner/Ficken/Ajro group number, the Druffner "Also" number, the Ficken "Also" number, or the Ajro "Also" number.

46. Moreover, PSI made no formal compliance inquiry into these matters and failed to prevent the Druffner Group from trading in violation of the trading limitations imposed by the mutual fund companies.

E. Failure to Prevent the Use of Different Branch Prefixes for the Purpose of Market Timing

47. The primary account prefixes at PSI's Boston branch were OBB and 041.

48. Many mutual fund companies would initially only block the OBB and 041 prefixes associated with the Boston branch and the Druffner Group's FA numbers.

49. The Druffner Group requested that their market timing clients' accounts be established with different branch prefixes (other than the Boston branch's primary prefixes), such as ERS, TMT, TMU, BTL, and ERE, to effectively expand the number of FA numbers at their disposal.

50. The use of branch prefixes other than OBB and 041 allowed the Druffner Group to multiply the number of available FA numbers and continue excessive short-term trading.

51. PSI received numerous market timing warning and termination letters from mutual fund companies identifying many of the multiple combinations of FA numbers associated with different branch prefixes utilized by the Druffner Group.

52. These communications expressed frustration with PSI registered agents for obtaining multiple FA numbers and the failure of PSI to curtail this activity.

53. PSI branch management was aware that the Druffner Group's multiple FA numbers were used to circumvent mutual funds' market timing restrictions.

54. Through the use of the multiple FA numbers, the Druffner Group was able to continue to engage in the market timing activity that the mutual fund companies sought to block.

55. Although certain mutual fund companies communicated their knowledge of the Druffner Group's tactics to PSI, no formal compliance inquiry resulted.

56. The failure of PSI to take effective action after notification by mutual fund companies allowed the Druffner Group to continue violating mutual fund policies and procedures regarding market timing.

F. Failure to Prevent the Opening of New Accounts for the Purpose of Market Timing

57. If a mutual fund company blocked trading privileges by account number rather than FA number, the Druffner Group often set up new account numbers, journaled money to the new accounts and continued to execute market timing transactions within the new accounts until blocked.

58. The Druffner Group opened new accounts on a regular basis for hedge fund clients.

59. For example, one hedge fund client had approximately 80 different accounts opened by the Druffner Group.

60. The Division has evidence that most of these different accounts were established for the purpose of avoiding detection by mutual fund companies and continuing the market timing activity.

61. Maintaining a large number of accounts gave the Druffner Group the ability to trade after a mutual fund company blocked a particular account number for market timing activity.

62. The opening of new offshore and international hedge fund accounts required multiple approvals from PSI departments above the branch manager.

63. Regional and branch manager personnel did not question the Druffner Group as to the business rationale for opening so many accounts on behalf of one client, particularly in light of mutual fund companies' warning and/or termination letters repeatedly shutting down account numbers previously opened.

64. In order to avoid suspicion, both internally at PSI and with the mutual funds' market timing police, the Druffner Group advised clients to establish new accounts in a different name and, to the extent possible, utilize a different tax identification number for the new accounts.

65. This tactic served to prevent all the accounts from being identified as belonging to the same client, thereby hindering the mutual fund companies from successfully blocking the trading by the client name or a particular tax identification number.

66. While branch management continued to approve multiple account numbers for the Druffner Group, PSI continued to receive numerous warning or block letters from mutual fund companies specifically identifying the use of multiple account numbers by the Druffner Group's clients.

G. Failure to Detect and Prevent the Journaling of Money Between Accounts

67. When a mutual fund company blocked one account, the Druffner Group would often journal the client's money to another account to avoid detection by the market timing police and continue trading, at all times, despite notice from the mutual fund company to stop.

68. Boston branch managers routinely approved the journaling of money between client accounts for the Druffner Group, failing to recognize that the purpose of each request was to fund new accounts in order to avoid detection by the mutual fund market timing police.

69. PSI branch management knew that multiple account numbers were established for each of the Druffner Group's hedge fund clients engaged in market timing and did not make a reasonable inquiry into the frequent journaling of money between those accounts.

H. Failure to Prevent Multiple Accounts Established Under Client Tax Identification Numbers

70. The Division has evidence that the Druffner Group recommended that hedge fund clients utilize different tax identification numbers and establish different account registrations in order to circumvent market timing restrictions.

71. The Druffner Group established multiple accounts for one client and, even though the accounts had the same tax identification number, each account would have a different account registration.

72. For example, a hedge fund client of the Druffner Group had one of its tax identification numbers associated with three different accounts, each with a different registration.

73. The Division has evidence that the Druffner Group facilitated the establishment of different account registrations utilizing the same or different tax identification numbers in order to circumvent market timing restrictions.

74. This served to prevent all the accounts from being identified as belonging to the same client, thereby hindering the mutual fund companies from successfully blocking the trading activity by the client.

75. PSI branch management failed to recognize that the Druffner Group was manipulating registrations to further the market timing activity.

76. Mutual fund companies made PSI aware that registered agents were engaged in this practice, yet PSI took no effective measures to stop it.

I. Failure to Detect and Prevent Trading Below Thresholds

77. While market timing can occur in any mutual fund, attention is drawn to a fund that experiences large and frequent transactions.

78. As a result, the Division has evidence that mutual fund companies established various thresholds for trades, which were dependent on the nature and size of a fund.

79. The mutual fund companies viewed trading at or above these thresholds as a “trigger” to identify potential market timing activity.

80. PSI branch management failed to detect a pattern by the Druffner Group of journaling money between multiple accounts of the same client in order to split transactions into dollar amounts that would fall below the mutual fund companies’ thresholds.

81. PSI branch management failed to identify a pattern employed by the Druffner Group to place multiple trades for one client below certain thresholds to avoid detection.

J. PSI’s Market Timing Policies

82. On November 15, 2000 PSI registered agents received a memo titled “New Policy on Market Timing Based Trading for Prudential Mutual Funds.” Market timing in wrap products was defined to be more than one round trip per quarter or more than four round trips per year.

83. According to the new 2000 PSI policy, market timing was prohibited in PruChoice, Target and Strategic Partners funds and stated: “We will continue to monitor excessive trading activity and may refuse purchase orders or exchanges into our Funds if any person, group or commonly controlled account as described in our Fund prospectuses.”

84. On January 8, 2003, PSI issued a market timing policy stressing “inappropriate timing activities **will continue to be monitored by the product manufacturer**.” (emphasis in the original)

85. PSI will comply with the manufacturer’s restriction requests and such restrictions “will be applied to **all** associated FA numbers, including joint and also numbers.” (emphasis in the original)

86. The January 2003 market timing policy also stated clearly:

i. **Cases involving multiple or subsequent notices, or attempted or actual circumventions of this policy will be reviewed by Law, Compliance and Risk Management for determination of appropriate disciplinary action(s). This includes any attempts to circumvent this policy through the use of manipulative techniques designed to avoid detection of certain trading activity by product manufacturers.** For example, executing transactions through an “also” number or joint production number in order to conceal the identity of the Financial Advisor, or opening new accounts to conceal the identity of the client. **Under any of these circumstances Financial Advisors will be subjected to disciplinary action(s) including, but not limited to, the following:**

- Commission forfeiture,
- Issuance of a Memo of Education,
- Issuance of a Memo of Caution,
- Issuance of a Compliance Directive, and/or
- Termination of Employment.

(emphasis in the original)

K. PSI Failed Effectively to Implement Policy Change

87. Notwithstanding the 2003 market timing policy, members of PSI's mutual fund exchange desk were given no formal compliance training with respect to this or any other market timing policy.

88. The 2003 market timing policy was a continuation of PSI's existing procedure regarding mutual fund companies' requests to block market timing by registered agent FA number and/or by client account number.

89. PSI took the position that the duty of monitoring detection of market timing activities was the responsibility of the mutual fund companies in which the transactions occurred.

90. Certain of PSI branch management continued to approve additional FA numbers, new accounts for existing market timing clients, and the journaling of money between market timing accounts for the registered agents engaged in market timing activity.

91. At no time were any members of the Druffner Group, or any other PSI registered agents, subjected to any of the disciplinary actions set out in the 2003 policy.

92. The Division has evidence that the Druffner Group continued to engage in the acts and practices integral to their market timing strategy, yet prohibited by the 2003 policy.

93. PSI failed to implement an effective compliance inquiry into the acts and practices exhibited by the Druffner Group and failed to meaningfully implement the new market timing policy.

L. Failure to Supervise Market Timing Activity

94. PSI branch management is responsible for the conduct of its registered agents at the Boston branch and the supervision of the registered agents within that office.

95. Branch managers, regional business managers, risk and compliance personnel were made aware of the market timing practices by the Druffner Group.

96. While PSI implemented policies during the relevant time period, PSI branch management failed to effectively stop the market timing practices of the Druffner Group.

97. PSI branch management approved the Druffner Group's requests for additional FA numbers, new account numbers, and the journaling of money that furthered the scheme by the registered agents to continue market timing.

98. As a result, Druffner became the largest producer at the Boston branch and one of PSI's highest producing registered agents.

99. PSI branch management failed to prevent the Druffner Group from utilizing tactics such as those noted above, which allowed them to obscure their identities and conceal the identities of their clients.

100. PSI's branch management failed to make reasonable inquiries in response to red flags and consequently failed to take corrective action allowing the clients of the Druffner Group to continue their market timing activity, which profited both the Druffner Group and PSI.

V. VIOLATIONS OF LAW

A. Count I: Violations of § 101

1. Section 101 of the Act states:

> It is unlawful for any person, in connection with the offer, sale, or purchase of any security, directly or indirectly
>
> (1) to employ any device, scheme, or artifice to defraud;
>
> (2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, or
>
> (3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person.

2. Respondent violated Section 101 of the Act because PSI knowingly failed to detect the fraudulent scheme that Boston branch registered agents were engaged in to circumvent market timing controls for the benefit of the company and to the detriment of long-term shareholders.

3. The Respondent's conduct as described above shows that the Respondent failed to reasonably supervise its registered agents and employees to assure compliance with this chapter.

B. Count II: Violations of § 204(a)(2)(G)

1. Section 204(a)(2)(G) of the Act states:

> (a) The secretary may by order impose an administrative fine or censure or deny, suspend, or revoke any registration or take any other appropriate action if he finds (1) that the order is in the public interest and (2) that the applicant or registrant or, in the case of a broker-dealer or investment adviser, any partner, officer, or director, any person occupying a similar status or performing similar functions, or any person directly or indirectly controlling the broker-dealer or investment adviser:—
>
> (G) has engaged in any unethical or dishonest conduct or practices in the securities, commodities or insurance business;

2. Respondent violated Section 204(a)(2)(G) of the Act because it failed to reasonably supervise its registered agents and employees thereby engaging in unethical and dishonest practices in the securities business.

C. Count III: Violations of § 204(a)(2)(J)

1. Section 204(a)(2)(J)of the Act states:

> The secretary may by order deny, suspend, or revoke any registration if he finds (1) that the order is in the public interest and (2) that the applicant or registrant
>
> (J) has failed reasonably to supervise agents, investment adviser representatives or other employees to assure compliance with this chapter;…

2. Respondent violated Section 204(a)(2)(J) of the Act because PSI failed to reasonably supervise the Druffner Group and failing to prevent its registered agents from utilizing tactics to obscure their identities and conceal the identities of their clients, which furthered the fraudulent market timing scheme.

D. Count IV: Violations of 950 CMR § 12.204(1)(a)(28)

1. 950 CMR § 12.204(1)(a)(28) states in pertinent part:

> (1) Dishonest and unethical practices in the securities business.
>
> > (a) Broker-dealers. Each broker-dealer shall observe high standards of commercial honor and just and equitable principles of trade in the conduct of its business. Acts and practices, including, but not limited to the following, are considered contrary to such standards and constitute dishonest or unethical practices which are grounds for imposition of an administrative fine, censure, denial, suspension or revocation of a registration, or such other appropriate action:
> >
> > > 28. Failing to comply with any applicable provision of the NASD Rules of Fair Practice or any applicable fair practice or ethical standard promulgated by the SEC or by a self-regulatory organization approved by the SEC.

2. NASD Conduct Rule 2110 provides:

> A member, in the conduct of his business, shall observe high standards of commercial honor and just and equitable principles of trade.

3. IM-2310-2. Fair Dealing with Customers provides a guide describing some practices that violate the "responsibility for fair dealing" including among other things:

> (3) Trading in Mutual Fund Shares
>
> > Trading in mutual fund shares, particularly on a short-term basis. It is clear that normally these securities are not proper trading vehicles and such activity on its face may raise the question of Rule violation.

4. NASD Conduct Rule 3010 provides in pertinent part:

> Each member shall establish and maintain a system to supervise the activities of each registered agent and associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable NASD Rules. Final responsibility for proper supervision shall rest with the member.

5. The Respondent violated NASD Rule 2110 and 950 CMR § 12.204(1)(a)(28) by failing to effectively prevent the fraudulent tactics utilized by the Druffner Group in furtherance of the market timing scheme.

6. The Respondent violated NASD Rule 3010 and 950 CMR § 12.204(1)(a)(28) by failing to detect and prevent the Druffner Group from engaging in a fraudulent scheme to market time; failing to have written supervisory procedures that adequately assured compliance with federal and state securities laws; failing to meaningfully enforce existing supervisory policies and procedures; and by failing to take reasonable corrective action in response to repeated warnings by mutual fund companies.

7. Accordingly, by failing to comply with 950 CMR § 12.204(a)(28) and the provisions of the NASD Conduct Rules, Respondent engaged in unethical or dishonest practices in the securities business.

E. Count V: Violations of 950 CMR §12.203(3)(a)

1. 950 CMR § 12.203(3)(a) states in pertinent part:

> Each broker-dealer must comply with the supervision requirements set forth in the NASD's Rules of Fair Practice.

2. The Respondent violated NASD Rule 3010 and 950 CMR § 12. 12.203(3)(a) by failing to detect and prevent the Druffner Group from engaging in a fraudulent scheme to market time; failing to have written supervisory procedures that adequately assured compliance with federal and state securities laws; failing to meaningfully enforce existing supervisory policies and procedures; and by failing to take reasonable corrective action in response to mutual fund company repeated warnings.

VI. ORDER

THEREFORE, it is hereby **ORDERED**, by Consent, as follows:

A. The Respondent shall permanently cease and desist from violations of the Act.

B. The Respondent shall pay an administrative fine in the amount of $5 million dollars. This sum shall be (1) paid within 10 business days of signing the Offer and deposited upon execution of the Division's Order by the Hearing Officer; (2) made by United States postal money order, certified check, bank cashier check, bank money order or wire transfer; and (3) made payable to the Commonwealth of Massachusetts.

C. The Respondent shall not seek or accept, directly or indirectly, reimbursement or indemnification, including, but not limited to any payments made pursuant to any insurance policy, with regard to all amounts that Respondent shall pay to the Division. Respondent further agrees that it shall not claim, assert, or apply for tax deduction or tax credit with regard to any state, federal or local tax for any penalty amounts that Respondent shall pay pursuant to the Division's administrative fine.

D. The Respondent shall, in addition to the payment of an administrative fine called for in Section (b) herein, pay disgorgement in the amount of $270 million dollars as part of a joint administrative settlement with the SEC and other civil regulators.

E. The Respondent shall retain an independent distribution consultant ("Independent Distribution Consultant"), within 60 days of the entry of the final order of the SEC ("SEC Order"), acceptable to the staff of the SEC and the Division. The Independent Distribution Consultant will develop a distribution plan ("Distribution Plan") to distribute fairly and proportionately the total disgorgement outlined in Section (d) above and Section IV.B. of the SEC Order dated August 28, 2006.

F. Respondent shall be responsible for all costs and expenses associated with the development and implementation of the Distribution Plan for the distribution of the disgorgement ordered in Section (d) above and Section IV.B. of the SEC Order. Such costs and expenses shall include, without limitation (i) the compensation of a tax administrator for the preparation of tax returns and/or for seeking any Internal Revenue Service rulings; (ii) the payment of taxes; and (iii) the payment of any distribution or consulting services as may be reasonably required by the Independent Distribution Consultant. Respondent shall cooperate with the tax administrator to see that all tax payments are timely made, and all such tax payments shall be deposited in a Qualified Settlement Fund (as defined by 26 C.F.R. §1.468B-1(c)) upon notice from the tax administrator concerning the amount and the deadline for payment.

G. Respondent shall cooperate fully with the Independent Distribution Consultant to provide all information requested for its review, including providing access to its files, books, records and personnel.

H. The Independent Distribution Consultant shall develop a proposed Distribution Plan for the distribution of disgorgement as specified above in Section (d) above and Section IV.B. of the SEC Order, and any interest or earnings thereon, according to a methodology developed in consultation with and acceptable to the staff of the SEC and the Division.

I. The Division does not object to the proposed procedural deadlines established by the SEC for the Independent Distribution Consultant to develop a proposed Distribution Plan for the distribution of the disgorgement amount as specified in the SEC Order to perform this analysis. For good cause shown, the staff of the SEC and the Division may alter any of the procedural deadlines set forth in the SEC Order.

J. Any proposed Distribution Plan developed by the Independent Distribution Consultant pursuant to Section (d) above and the SEC Order shall be submitted simultaneously to the staff of the SEC and the Division.

K. The Independent Distribution Consultant shall submit to Respondent, the staff of the SEC and the Division the proposed Distribution Plan no more than 180 days after the entry of the Order.

L. The proposed Distribution Plan developed by the Independent Distribution Consultant shall be binding unless, within 210 days after the date of entry of the SEC Order, Respondent, the staff of the SEC, or the Division advises, in writing, the Independent Distribution Consultant of any determination or calculation from the Distribution Plan that it considers to be inappropriate and states in writing the reasons for considering such determination or calculation inappropriate.

M. With respect to any calculation with which Respondent, the staff of the SEC, or the Division do not agree, such parties shall attempt in good faith to reach an agreement within 240 days of the entry of the SEC Order. In the event that Respondent, the staff of the SEC, and the Division are unable to agree on an alternative determination or calculation, the determinations of the Independent Distribution Consultant shall be included in the proposed Distribution Plan.

N. Within 285 days of the date of entry of the SEC Order, the Independent Distribution Consultant shall submit the proposed Distribution Plan for the administration and distribution of disgorgement funds pursuant to the SEC's Rules on Fair Fund and Disgorgement Plans, 17 C.F.R. § 201.1101, *et seq*., (Rule 1101 through Rule 1106). Following an SEC Order approving a final plan of distribution as provided in Rule 1104 (17 C.F.R. § 201.1104) of the SEC's Rules on Fair Fund and Disgorgement Plans, the Independent Distribution Consultant shall take all necessary and appropriate steps to administer the final plan for distribution of disgorgement funds in accordance with the terms of the approved Distribution Plan.

O. For the period of engagement and for a period of two years from completion of the engagement, the Independent Distribution Consultant 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. Any firm with which the Independent Distribution Consultant is affiliated in performance of his or her duties under the SEC Order, or of which he/she is a member, and any person engaged to assist the Independent Distribution Consultant in the performance of his/her duties under the SEC Order, shall not, without prior written consent of the SEC and the Division, enter into any employment, consultant, attorney-client, auditing or other professional relationship with Respondent, or any of

Respondent's present or former affiliates, directors, officers, employees, or agents acting in the capacity as such for the period of the engagement and for a period of two years after the engagement.

P. This Order is not intended by the Massachusetts Securities Division to subject any Covered Person to any disqualifications under the laws of any state, the District of Columbia or Puerto Rico (collectively, "State"), including, without limitation, any disqualifications from relying upon the State registration exemptions or State safe harbor provisions. "Covered Person" means Respondent, or any of its officers, directors, affiliates, current or former employees, or other persons that would otherwise be disqualified as a result of the Orders (as defined below.).

Q. The SEC Final Judgment, the NYSE Stipulation and Consent, the NASD Letter of Acceptance, Waiver and Consent, this Order and the order of any other State in related proceedings against Respondent (collectively, the "Orders") shall not disqualify any Covered Person from any business that they otherwise are qualified, licensed or permitted to perform under the applicable law of the Commonwealth of Massachusetts and any disqualifications from relying upon this state's registration exemptions or safe harbor provisions that arise from the Orders are hereby waived.

R. The Orders shall not disqualify Respondent from any business that they otherwise are qualified or licensed to perform under applicable state law.

S. If after the entry of this Order, the Respondent fails to comply with any of the terms set forth in the Division's Order, the Enforcement Section may institute an action to have the Offer of Settlement and this Order declared null and void.

Upon issuance of an appropriate Order and after a fair hearing, the Enforcement Section may re-institute the action that had been brought against the Respondent.

WILLIAM FRANCIS GALVIN
SECRETARY OF THE COMMONWEALTH

By: /s/ Diane Young-Spitzer
Diane Young-Spitzer
Presiding Officer
Massachusetts Securities Division
One Ashburton Place, 17th Floor
Boston, Massachusetts 02111

Issued: August 28, 2006

Exhibit 10.3

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 54371/August 28, 2006

ADMINISTRATIVE PROCEEDING
File No. 3-12400

In the Matter of

PRUDENTIAL EQUITY GROUP, LLC, formerly known as PRUDENTIAL SECURITIES, INC.,

Respondent.

ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS PURSUANT TO SECTION 15(b) 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 proceedings be, and hereby are, instituted pursuant to Section 15(b) of the Securities Exchange Act of 1934 (“Exchange Act”) against Prudential Equity Group, LLC, formerly known as Prudential Securities Inc. (“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 it and the subject matter of these proceedings, Respondent consents to the entry of this Order Instituting Administrative Proceedings, Making Findings, and Imposing Remedial Sanctions Pursuant to Section 15(b) of the Securities Exchange Act of 1934 (the “Order”), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds[1] that:

A. Respondent

1. Prior to July 1, 2003, Prudential Securities Inc. ("PSI") was an indirect wholly owned broker-dealer subsidiary of Prudential Financial, Inc. ("Prudential Financial"). Prudential Financial is a publicly-owned holding company, traded on the New York Stock Exchange, whose operating subsidiaries provide a wide range of insurance, investment management and other financial products and services to retail and institutional customers including insurance brokers and investment managers. On July 1, 2003, PSI transferred the assets relating to its U.S. retail securities brokerage operations to a newly formed holding company, now named Wachovia Securities Financial Holdings, LLC ("WSFH"). Prudential Financial presently owns 38% of WSFH and Wachovia Corporation owns 62% of WSFH. Since July 1, 2003, PSI's former U.S. retail securities brokerage business has operated as part of Wachovia Securities, LLC. Following the asset transfer, PSI converted from a stock corporation into a limited liability company and was renamed Prudential Equity Group, LLC ("PEG"). PEG is a broker-dealer registered with the Commission pursuant to Section 15(b) of the Exchange Act and is a member of the National Association of Securities Dealers and the New York Stock Exchange. PEG provides equity research, sales and trading to domestic and international institutional customers and is a successor entity to PSI. Prudential Financial continues to own 100% of the equity interests in PEG.

B. Summary

2. This matter concerns a fraudulent market timing scheme perpetrated by PSI registered representatives (collectively, the "Representatives") whose business involved market timing to defraud at least fifty mutual funds and their long-term shareholders. Beginning in at least September 1999 and continuing through at least June 2003 (the "Relevant Period"), the Representatives used deceptive trading practices to conceal their identities, and those of their customers, to evade mutual funds' prospectus limitations on market timing. These practices included the use of multiple broker identifying numbers (known as Financial Advisor, or "FA" numbers) and multiple customer accounts; the use of accounts coded as confidential in PSI's systems; and the Representatives' use of "under the radar" trading to avoid notice by mutual funds. Typically, mutual funds screened for market timing trades only above a designated dollar amount. The practice of "under the radar" trading refers to the Representatives' splitting of one trade into numerous smaller ones to avoid detection by mutual funds.

[1] The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

3. As early as the fourth quarter 1999, several mutual fund companies identified the Representatives' use of deceptive trading practices and notified PSI of the Representatives' conduct. In May 2002, PSI itself determined that its top-producing registered representative used deceptive trading practices to avoid notice by mutual funds. Throughout the Relevant Period, PSI received hundreds of notices from mutual fund companies that identified the Representatives' conduct and asked the firm to take steps to curtail their deceptive market timing practices.

4. Despite PSI's increasing awareness of the Representatives' fraudulent market timing practices, the firm elected to continue the business of market timing. Rather than discipline or sanction any of the Representatives or even curtail their ability to open additional accounts for their market timing customers, PSI failed to prevent their conduct from continuing and actually began to track the Representatives' gross revenues. In 2001, for example, the Representatives generated more than $16 million in gross commission revenues for the firm, most of which was in danger of being eliminated had the firm phased out market timing at that time. Similarly, the Representatives generated approximately $23 million in gross commission revenues in 2002, and continued to generate comparable revenues throughout the Relevant Period.

5. PSI's policies and procedures were ineffective in curtailing the Representatives' fraud and were largely not enforced. Even in situations where PSI purportedly enforced any of these policies, PSI senior officers undermined them by granting exceptions for PSI's largest producing registered representatives. Additionally, PSI repeatedly failed to deprive the Representatives of their inappropriate use of hundreds of FA numbers, even though the use of multiple FA numbers was the primary means by which the Representatives carried out their fraud. PSI finally issued a market timing policy in January 2003, but the firm did not fully enforce procedures in that policy to curtail the Representatives' scheme. PSI also failed to make and keep required records concerning the Representatives' trading practices. As a result of the conduct described above, PSI violated the antifraud and books and records provisions of the federal securities laws.

C. Background

6. Market timing includes frequent buying and selling of shares of the same mutual fund or buying or selling of mutual fund shares in order to exploit inefficiencies in mutual fund pricing. Though not illegal *per se*, market timing can harm mutual fund shareholders because it can dilute the value of their shares, if the market timer is exploiting pricing inefficiencies, or disrupt the management of the mutual fund's investment portfolio and can cause the targeted mutual fund to incur costs borne by other shareholders to accommodate frequent buying and selling of shares by the market timer.

7. Beginning in the late 1990s, many mutual funds determined that market timing

harmed their long-term shareholders. As a result, they began to monitor market timing in their funds' shares and imposed restrictions on excessive trading. Such restrictions limited the number of trades that an account holder could place in a fund's shares and often were set forth in the funds' prospectuses. Many funds monitored trading activity to detect any violations of these prospectus limitations.

8. Most mutual funds received trade instructions from PSI through the National Securities Clearing Corporation ("NSCC"). NSCC is a centralized trade clearance and settlement system that linked the Representatives, PSI, and virtually all mutual fund companies. To place trades that were transmitted through NSCC, the Representatives were required to identify their FA number and a customer account to mutual funds on trade tickets. PSI appended additional information to the Representatives' orders and transmitted the transactions through NSCC to the mutual fund companies.

9. Some mutual funds screened for excessive short-term trading by reviewing FA and customer account numbers that the Representatives transmitted to them via NSCC. Some also monitored for excessive short-term trading by trade size and principal amount and by the branch code attached to a trade.[1] Typically, if a fund concluded that a shareholder had violated its exchange limitations, the fund would attempt to prevent, or "block" additional trades in a fund or fund family by that shareholder. If a fund determined that a particular PSI registered representative or shareholder had violated its exchange limitations, the fund would send a "block letter" to PSI. Block letters varied but generally notified PSI of the mutual fund's intention to block the registered representative's or customer's transaction and often asked PSI to take steps to preclude a particular registered representative or customer account from engaging in additional trades in a particular fund or fund family.

10. Because these mutual funds monitored for excessive trading by FA number and/or customer account number, the Representatives altered their use of these numbers to defraud these funds and the funds' long-term shareholders. By altering their use of these numbers, the Representatives tricked mutual fund companies into accepting trades that the funds otherwise would have rejected.

D. The Representatives' Deceptive Conduct

11. During the Relevant Period, the Representatives engaged in a fraudulent scheme to circumvent blocks imposed by mutual funds on their trading privileges. The Representatives' scheme worked as follows. The Representatives' customers, typically hedge funds, asked the Representatives to purchase and sell mutual funds on a short-term basis on their behalf. The

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2 PSI assigned branch codes to each of its retail branch offices. Branch codes identified to mutual funds the PSI branch office from which a particular market timing trade originated.

Representatives, however, knew that mutual funds tracked their trades by FA number and customer account number, and they knew that if they placed short-term mutual fund trades for their customers using a single FA or account number, the mutual funds would likely determine the number of trades was excessive and would block any further trades by them.

12. The Representatives, therefore, devised a scheme to conduct their customers' trading using dozens of customer accounts, often established under fictitious names, and multiple FA numbers to make it difficult for mutual funds to identify their customers' market timing. When the mutual funds succeeded in blocking certain FA numbers or customer accounts from further trading, the Representatives then used other FA numbers and customer accounts that had not yet been blocked to evade the funds' restrictions and continue to trade.

a. The Boston Registered Representatives

13. For example, one group of PSI registered representatives based in its Boston, Massachusetts branch office (the "Boston Representatives") repeatedly used these deceptive practices to defraud mutual funds throughout the Relevant Period. The Boston Representatives consisted of a group of three PSI registered representatives and several assistants. The group had five customers for whom it placed market timing trades, each of whom acted on behalf of one or more hedge funds. During the Relevant Period, PSI received approximately $8 million from the Boston Representatives' market timing activities, of which group members received approximately $4.6 million. As a result of this business, the head of the group quickly rose to become one of PSI's top producers.

14. Many of the mutual funds in which the Boston Representatives traded screened for market timing trades by FA and customer account numbers. Many fund companies sent notices to PSI that complained that the group's trades had violated prospectus limitations. Some mutual funds announced steps they had taken to preclude the Boston Representatives from further trading while others asked that PSI take steps to block further trades by the group in the fund.

15. During the Relevant Period, the Boston Representatives used at least thirteen FA numbers and hundreds of customer accounts (for what were, in reality, only five customers) to circumvent these blocks and preclude new blocks. The Boston Representatives' use of these devices in connection with market timing allowed group members to continue to place trades in funds that had taken steps to preclude them from further trading. Their scheme created the impression that transactions originated from many registered representatives and represented many different customers. In fact, what appeared to the mutual funds to be thousands of separate transactions submitted by many registered representatives for many unrelated customers was actually a systematic pattern of market timing by group members on behalf of their five hedge fund customers.

b. The Garden City Representative

16. Another PSI registered representative based in its Liberty Plaza and Garden City, New York branch offices (the “Garden City Representative”) used these same deceptive practices to defraud mutual funds throughout the Relevant Period. The Garden City Representative headed a team of registered representatives and assistants, although he very rarely reported to work at any PSI location. He had five customers for whom he placed market timing trades, each of whom acted on behalf of one or more hedge funds. During the Relevant Period, PSI received approximately $9.8 million from the Garden City Representative’s market timing activities (of which the Garden City Representative received approximately $4.7 million). The Garden City Representative was the top producing registered representative at PSI throughout the Relevant Period.

17. Like the Boston Representatives, the Garden City Representative traded in mutual funds that screened for market timing by FA and customer account numbers. During the Relevant Period, approximately fifty mutual funds complained to PSI about the Garden City Representative’s trading activity. Many mutual funds specifically identified to PSI his use of deceptive trading strategies to evade blocks the fund companies had imposed.

18. To evade these blocks, the Garden City Representative maintained 49 different FA numbers and hundreds of customer account numbers (for what were, in reality, only five customers). His use of these devices to market time created the impression that the trades originated from many registered representatives and many customers. By shifting trades from one FA number to another, or from one customer account to another, the Garden City Representative concealed his identity and was able to place trades in mutual funds where PSI previously had blocked his trading under his other FA numbers and accounts.

c. The Special Accounts Representatives

19. Another group of PSI registered representatives based in a New York office known within the firm as “Special Accounts” (the “Special Accounts Representatives”) also used deceptive practices to defraud mutual funds throughout the Relevant Period. The Special Accounts Representatives consisted of a group of two PSI registered representatives and several assistants. The group had three customers for which it placed market timing trades. During the Relevant Period, PSI received gross revenue of approximately $6.5 million from the Special Accounts Representatives’ market timing activities, of which group members received approximately $2.5 million. As a result of this business, the heads of the group quickly achieved membership in PSI’s Chairman’s Club, a select group consisting of the largest producing registered representative within the firm.

20. Like the Boston Representatives and the Garden City Representative, the Special Accounts Representatives knew that most mutual funds identified excessive trading by FA and customer account numbers. They also understood that mutual funds screened for market timing by reviewing only those trades at or exceeding certain dollar amounts. The Special Accounts

Representatives used at least 20 FA numbers and hundreds of customer accounts (for what were, in reality, only three customers) to avoid detection by mutual funds. The Special Accounts Representatives also used “under the radar” trading to disguise their customers’ trading in funds that previously had taken steps to stop them. The Special Accounts Representatives’ use of these devices in connection with market timing deceived mutual funds into accepting trades they otherwise would have rejected. Like the Boston Representatives and the Garden City Representative, their scheme perpetuated the impression that transactions originated from many registered representatives and represented many different customers.

E. PSI Failed to Prevent the Representatives From Obtaining Multiple Broker Identifying and Customer Account Numbers

21. PSI failed to prevent the Representatives from obtaining several different forms of broker identifying numbers. Consequently, the Representatives used these numbers to perpetrate their scheme to defraud. When registered representatives began their employment with PSI, PSI assigned them an FA number. Registered representatives used FA numbers to open customer accounts, execute trades, and track their commissions. When registered representatives worked as a team to service common customers, PSI provided “Joint” numbers. Joint numbers ostensibly represented a commission split between two or more registered representatives. Here, the Representatives acquired and used Joint numbers for improper purposes. The numbers were not used to split commissions, but rather to facilitate the Representatives’ ability to trade after their other broker identifying numbers had been blocked from trading. PSI also provided the Representatives with “Also” numbers. The purported purpose of “Also” numbers was to allow the Representatives’ customers to access only those portions of a given registered representative’s portfolio that belonged to that customer or to provide certain customers with commission discounts. The Representatives, however, used Also numbers improperly in the same manner as they used FA and Joint numbers – to circumvent blocks that had been imposed on their other FA numbers. Indeed, at least one mutual fund became so frustrated by its inability to identify the Representatives that it threatened to curtail the trading privileges of all registered representatives within a PSI branch to remedy the conduct.

22. Each of the Representatives maintained numerous FA, Joint, and Also numbers, and used these numbers interchangeably to execute trades for their customers. For example, the Boston Representatives used 13 broker identifying numbers to place market timing trades and the Garden City Representative used 49 broker identifying numbers. When one of the Representatives’ FA, Joint, or Also numbers was blocked from trading by a particular mutual fund, he used another number assigned to him to place the trade in that fund. Although each Joint number ostensibly represented a unique commission split, in fact each team of Representatives split commissions from mutual fund purchases according to a single ratio, irrespective of which broker identifying number was used to enter the trade.

23. PSI failed to prevent the Representatives from opening hundreds of customer account numbers. The Representatives’ customers maintained multiple accounts with PSI, many

of which bore fictitious names that had no relation to the actual customer's name. The Representatives used these customer accounts interchangeably to execute trades. When one customer account was blocked from trading by a particular mutual fund, the Representatives substituted another account for that same customer to place the trade for that customer, thereby creating the appearance that the trade originated from another customer.

24. PSI failed to prevent the Representatives from obtaining accounts for their customers that were coded as "Confidential." Confidential accounts did not identify the beneficial owner of the account on the transaction data provided to the mutual funds. Although such a designation could have a legitimate purpose, here the Representatives used confidential accounts improperly to impede the mutual funds' ability to identify which PSI registered representative or customer was market timing their funds.

25. PSI also failed to prevent the Representatives from obtaining customer account numbers with multiple branch identifiers. Typically, registered representatives located in one PSI branch office had customer accounts that had a prefix used to identify the branch location. Here, the Representatives established accounts for their hedge fund customers using multiple branch codes, which effectively impeded the mutual funds' ability to identify the particular PSI office location, as well as registered representative, that was market timing their funds. The Representatives used branch identifiers improperly as another mechanism to conceal their identities and the identities of their customers to mutual funds.

F. PSI Received Notifications of the Representatives' Deceptions

26. During the Relevant Period, mutual fund companies sent more than a thousand letters and e-mails to PSI concerning market timing by the Representatives. Many of these communications asked PSI to take steps to stop further trading by a particular customer account or FA number. Others expressly notified PSI that the Representatives used deceptive trading practices to continue placing market timing trades.

27. High level officers of PSI were aware during the Relevant Period that mutual funds were accusing the Representatives of using deceptive practices to evade the mutual funds' attempts to block the Representatives' market timing trades. For example, an individual who joined PSI in 1997 and rose to become the chief administrator of PSI's Private Client Group ("PCG") in January 1999, then to executive director of PCG in November 2000, and finally to president of PCG in December 2002 (the "Senior Officer"), received repeated notices of wrongdoing by the Representatives throughout the Relevant Period, but did not take adequate steps to stop the Representatives' fraud. Among other things, the Senior Officer received the following indications that the Representatives were committing fraud. In some cases, certain other senior managers or high level officers of PSI also received notices that the Representatives were committing fraud.

28. On November 21, 1999, a senior executive in the PSI Mutual Fund Operations

Division forwarded to the Senior Officer a string of e-mails concerning a complaint from a mutual fund complex that the Garden City Representative had evaded a block on two of his accounts by simply opening new accounts. Among other things, the e-mail stated:

> It appears that [the Garden City Representative] circumvented this restriction by requesting new BIN [account] #s and fund accounts be established, funded by transferring shares into these new accounts on 11/8/99. Subsequently on 11/10/99, an exchange out of the money fund into our stock funds was processed, beginning market timing again.

The cover e-mail commented, "[T]his seems to be a serious matter that will only get worse."

29. On January 19, 2000, the manager of PSI's Mutual Fund Operations Division forwarded to the Senior Officer an e-mail from another mutual fund complex complaining that a member of the Boston Representatives had evaded a trading restriction by opening a new account, stating:

> It appears that [the member] set up another account in December for the same client we restricted on 11/22.

30. On March 30, 2001, the head of PCG risk management sent the Senior Officer an e-mail that attached a letter from another mutual fund complex complaining that "excessive trading activity" by PSI registered representatives in its mutual funds "has become detrimental to both the funds and shareholders of the funds involved." The letter described the tactics used by PSI registered representatives to avoid having their trades canceled as follows:

> Since trade cancellation began on February 26th, 2001, we have noticed several types of reactions by Prudential Financial Advisors in order to circumvent our attempts to terminate excessive trading. Originally, your Financial Advisors established new identification numbers so that they would not be recognized as a repeat offender. Secondly, Financial Advisors would transfer a fund(s) position from account to account, in order to disguise their identity. Lastly, your Financial Advisors have attempted to reduce the dollar amount of the exchange orders while simultaneously increasing the number of exchanges (in the same fund and account) in the hopes of not being identified.

31. On June 28, 2001, the Senior Officer received an e-mail from the manager of the Special Accounts branch warning him that the Special Accounts Representatives were obtaining multiple FA numbers in order to conduct their market timing, stating that:

> We will have an issue soon with joint FA numbers: in order to get

> around the MF [mutual fund] timing issue they are starting to request 99/01 split numbers with their junior partners to help them get around being shut down by some MF companies on timing.

32. On April 4, 2002, the manager of PSI's Mutual Funds Operations division sent an e-mail to other senior managers forwarding an e-mail from another mutual fund complex complaining that certain PSI registered representatives were using multiple accounts and FA numbers to evade restrictions on their market timing. The e-mail stated:

> What we have seen scares us. It appears certain representatives are changing account registrations, tax id numbers, and branch and rep numbers in an effort to time the [mutual fund complex's] funds. All of these accounts have been stopped, but each day "new" ones pop up.

When the PSI chief compliance officer saw the above e-mail, he showed it to the Senior Officer. The head of PCG risk management also discussed the e-mail with the Senior Officer.

33. On April 29, 2002, the Senior Officer met with an internal PSI working group that had been analyzing market timing issues. The group described for the Senior Officer the mutual fund companies' restrictions on excessive trading, the fund companies' block letters to PSI, and the deceptive trading strategies used by certain PSI registered representatives, including multiple accounts and FA numbers.

34. On at least two occasions in May 2002, an employee of PSI's risk management division detailed for the Senior Officer several deceptive practices used by the Garden City Representative. The employee's analysis noted that in one 37-day period, the Garden City Representative had 19 different mutual fund companies request that accounts under the representative's control, or the representative as an FA, be blocked from their funds. The analysis concluded that the Garden City Representative had circumvented these requests by changing his FA number to an Also or Joint Number to avoid detection by the fund, or by changing customer account numbers and moving the assets from the blocked account to a newly established account.

35. On February 5, 2003, the director of strategic planning at PCG sent the Senior Officer (then the President and most senior officer of PCG) a string of e-mails from another mutual fund complex complaining that certain PSI registered representatives were using multiple customer accounts and FA numbers for market timing. One of the e-mails stated:

> I have spoken to these reps a few times over the past several months about stopping their timing activity to no avail. Over the past several months, we have placed stops on 325 of their accounts as of 11/30/02 and continue to add accounts daily. We see new

> accounts/rep id combinations being opened and have determined that we are not able to continue chasing them within our funds. We feel our only course of action to protect our fund shareholders is to prohibit the attached list of reps from doing business with [our funds].

Another e-mail in the string stated:

> These reps have multiple rep ids and have continued to add new ones as we block the ids within the NSCC trading system for our fund complex . These reps created close to $3 billion in exchanges last year with $75 million of assets during a time in which we placed stops on 350 of their accounts.

The director of strategic planning added his own warning to the Senior Officer:

> I just wanted to give you a heads up on an issue that is sure to reach your desk in the next day or two. As you can see from the attached string of notes, the senior leadership team at [a mutual fund complex] are completely frustrated with some of the tactics/strategies of FA's [the Garden City Representative and the Boston Representatives]. Previous attempts to curtail timing activity in the [mutual fund complex's] funds by blocking account activity have been thwarted by the establishment of additional FA numbers. It appears that [the mutual fund complex] is now making overtures that continued activity of this nature will threaten the relationship between Prudential and the fund company.

36. On February 11, 2003, a PCG risk officer sent an e-mail to the Senior Officer (then the President and most senior officer of PCG) that forwarded an e-mail from the Garden City branch manager about the Garden City Representative's market timing business. The branch manager questioned the effectiveness of the Mutual Fund Operations Division's internal blocking system and raised several other concerns about the Garden City Representative's activities:

> Blocking of individual accounts by fund companies is extremely short-sighted in consideration of the fact that each "entity" maintains multiple accounts with our Firm.
>
> There have been repeat offenses, at least in spirit . . .
>
> Fund companies have been misled as to the identity of the FA's of record. Recently, [a mutual fund company] was provided with information which was at best misleading to effect the removal [of] a block.

[T]here is frequent journaling of funds between accounts.

At the present time, [the Garden City Representative and an assistant] either have or have had a total of 48 FA #s including single, joint and also numbers.

G. PSI's Procedures to Limit Market Timing Were Ineffective

37. Although PSI senior officers issued policies and procedures ostensibly designed to proscribe the Representatives' conduct, these policies and procedures were ineffective in scope and were never fully enforced. Moreover, even in situations where these policies and procedures purportedly were enforced, PSI senior officers undermined them by granting exceptions for its largest producing registered representatives. As a result, the Representatives' deceptions continued even after these policies and procedures were promulgated.

a. PSI's June 2002 Procedure Concerning Issuance of FA Numbers

38. In June 2002, PSI instituted a procedure concerning the issuance of FA numbers, in a purported effort to hinder the Representatives' ability to obtain "Joint" numbers and "Also" numbers to evade limitations on market timing (the "June 2002 Procedure"). The June 2002 Procedure provided, simply, that requests for "Joint" and "Also" numbers would require a documented business request and a PSI Regional Business Manager's approval. The June 2002 Procedure failed to preclude the Representatives from misusing previously issued Joint and Also numbers to evade blocks imposed by mutual fund companies nor did it preclude them from obtaining new FA numbers to facilitate their fraud. Indeed, the Garden City Representative obtained 12 new Joint and Also numbers just days before the procedure took effect, purportedly to assist him in transferring customer accounts from one PSI branch office to another. The June 2002 Procedure also did not subject the Representatives to any form of discipline or sanction if they continued to use Joint and Also numbers to evade blocks in violation of its terms.

b. PSI's January 2003 Market Timing Policy

39. After protracted discussion involving PSI senior officers during the Fall of 2002, PSI issued a market timing policy on January 8, 2003 (the "Market Timing Policy"). PSI considered, and rejected, defining market timing in the Market Timing Policy as a certain number of trades because of concerns that doing so would have too great an impact on the Representatives' revenues. PSI also rejected an absolute prohibition on the business of market timing. Instead, the Market Timing Policy provided that "inappropriate timing activities [would] continue to be monitored" by mutual fund companies and not by PSI itself.

40. Unlike other PSI policies concerning market timing, the Market Timing Policy expressly provided for the imposition of sanctions, including termination of employment, for the Representatives' use of "manipulative techniques" to evade mutual fund trading restrictions. Any imposition of sanctions was to be decided by a committee consisting of members of PSI's Legal, Compliance, and Risk Management divisions. Despite notifications of continuing deceptive practices received by PSI after it issued the Market Timing Policy, PSI did not form this committee and failed to take action against any of the Representatives to stop their use of "manipulative techniques" to market time.

41. The Market Timing Policy also provided that, in the event a mutual fund company asked PSI to block any one of a registered representative's FA numbers, **all** numbers belonging to the registered representative similarly would be blocked from trading. However, PSI senior officers determined not to implement this critical aspect of the Market Timing Policy. In fact, despite the policy's clear language, PSI interpreted mutual fund block requests after it issued the Market Timing Policy in the same manner as it had previously – as narrowly as possible, blocking only the specific FA number or customer account number identified by mutual fund block requests. Thus, even after issuance of the Market Timing Policy, the Representatives were able to continue their fraudulent scheme of switching to unblocked FA numbers or customer accounts to evade blocks imposed by mutual fund companies.

H. PSI Profited From the Representatives' Deceptive Acts

42. PSI identified the Representatives as early as 2000 and monitored their revenues and ranks within the firm throughout the Relevant Period. The firm's Mutual Fund Operations Division, which processed the Representatives' trades in mutual funds, monitored the Representatives' activity because their rapid trading required the dedication of additional staff within the department to process the trades and strained the firm's trade processing and settlement systems.

43. In 2000, PSI began to track each quarter the gross commission revenues generated by the Representatives. PSI prepared these reports to determine the amount of income that would possibly be reduced if the firm determined to eliminate market timing as a business. In 2001, for example, the Representatives generated more than $16 million in gross commission revenues for the firm, most of which would have been eliminated had the firm phased out market timing at that time. Similarly, the Representatives generated approximately $23 million in gross commission revenues for 2002, and received another $10 million in gross commission revenues during the first half of 2003.

44. As PSI senior officers became increasingly aware of the Representatives' use of deceptions, the firm elected to continue the business of market timing. Indeed, some of the firm's senior officers were aware that the June 2002 Procedure concerning the issuance of multiple FA numbers and the January 2003 Market Timing Policy were wholly ineffective at

eradicating the Representatives' deceptions and the Representatives and their hedge fund customers continued this activity. During the Relevant Period, the Representatives generated approximately $50 million in gross revenues as a result of this conduct.

I. PSI Failed to Make and Keep Required Books and Records

45. PSI was required to make and keep current trade orders and trade tickets concerning the Representatives' mutual fund trading. PSI also was required to make and keep current a trade blotter that reflected the Representatives' mutual fund trading. During the relevant period, PSI failed to maintain these required books and records, and, in instances where PSI did maintain these items, they did not give the actual time at which the orders were received or the time of entry.

J. Violations of the Antifraud and Books and Records Provisions of the Federal Securities Laws

46. As a result of the conduct described above, PSI willfully violated Section 17(a) of the Securities Act of 1933, which prohibits fraudulent conduct in the offer or sale of securities.

47. As a result of the conduct described above, PSI also willfully violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, which prohibit fraudulent conduct in connection with the purchase or sale of securities.

48. PSI also willfully violated Section 17(a) of the Exchange Act and Rules 17a-3 and 17a-4 thereunder. Section 17(a) of the Exchange Act and Rules 17a-3 and 17a-4 thereunder required PSI to make and keep certain books and records relating to its business, including trade blotters and trade tickets related to mutual fund trading. Implicit in the Commission's recordkeeping rules is a requirement that information contained in a required book or record be accurate. PSI failed to maintain complete and current copies of trade blotters concerning mutual fund trading and trade tickets related to mutual fund trading in a readily accessible place. In instances where PSI did maintain trade tickets, information included on them did not represent the actual time at which the orders were placed.

K. Undertakings

In determining whether to accept the Offer, the Commission has considered these undertakings:

49. *Cooperation.* Respondent shall cooperate fully with the staff of the Commission in any litigation, ongoing investigation, or other proceedings relating to or arising from the matters described in the This Order. In connection with such cooperation, Respondent has undertaken:

a. to produce promptly, without service of a notice or subpoena, any and all documents and other information requested by the Commission's staff in Respondent's possession and control;

b. to use its best efforts to cause its employees to be interviewed by the Commission's staff at such times as the Commission may reasonably request; and

c. to use its best efforts to cause its employees to appear and testify truthfully and completely without service of a notice or subpoena in such investigations, depositions, hearing or trials as the Commission's staff reasonably may request; and that in connection with any testimony of Respondent to be conducted at deposition, hearing, or trial pursuant to a notice or subpoena, Respondent

i. agrees that any such notice or subpoena for Respondent's appearance and testimony may be served by regular mail on its attorney:

Bingham McCutchen LLP
Attn: Neal E. Sullivan, Esq.
2020 K Street, N.W.
Washington, DC 20006; and

ii. Agrees that any such notice or subpoena for Respondent's appearance and testimony in an action pending in a United States District Court may be served, and may require testimony, beyond the territorial limits imposed by the Federal Rules of Civil Procedure.

50. *Independent Distribution Consultant*. Respondent shall retain, within 60 days of the entry of this Order, the services of an independent distribution consultant ("Independent Distribution Consultant") acceptable to the staff of the Commission.

a. Respondent shall be responsible for all costs and expenses associated with the development and implementation of the Distribution Plan for the distribution of the disgorgement ordered in Section IV.B. of this Order. Such costs and expenses shall include, without limitation (i) the compensation of a tax administrator for the preparation of tax returns and/or for seeking any IRS rulings; (ii) the payment of taxes; and (iii) the payment of any distribution or consulting services as may be reasonably required by the Independent Distribution Consultant. Respondent shall cooperate with the tax administrator to see that all tax payments are timely made, and all such tax payments shall be deposited in the Qualified Settlement Fund upon notice from the tax administrator concerning the amount and the deadline for payment.

b. Respondent shall cooperate fully with the Independent Distribution Consultant to provide all information requested for its review, including providing access to its files, books, records, and personnel.

c. The Independent Distribution Consultant shall develop a proposed Distribution Plan for the distribution of the disgorgement ordered in Section IV.B. of this Order, and any interest or earnings thereon, according to a methodology developed in consultation with and acceptable to the staff of the Commission.

d. The Independent Distribution Consultant shall submit to Respondent and the staff of the Commission the proposed Distribution Plan no more than 180 days after the entry of this Order.

e. The proposed Distribution Plan developed by the Independent Distribution Consultant shall be binding unless, within 210 days after the date of entry of this Order, Respondent or the staff of the Commission advises, in writing, the Independent Distribution Consultant of any determination or calculation from the Distribution Plan that it considers to be inappropriate and states in writing the reasons for considering such determination or calculation inappropriate.

f. With respect to any calculation with which Respondent or the staff of the Commission do not agree, such parties shall attempt in good faith to reach an agreement within 240 days of the entry of this Order. In the event that Respondent and the staff of the Commission are unable to agree on an alternative determination or calculation, the determinations of the Independent Distribution Consultant shall be included in the proposed Distribution Plan.

g. Within 285 days of the date of entry of this Order, the Independent Distribution Consultant shall submit the proposed Distribution Plan for the administration and distribution of disgorgement funds pursuant to the Commission's Rules on Fair Fund and Disgorgement Plans, 17 C.F.R. § 201.1100, *et seq.*, (Rule 1100 through Rule 1106). Following a Commission order approving a final plan of distribution, as provided in Rule 1104 [17 C.F.R. § 201.1104] of the SEC's Rules on Fair Fund and Disgorgement Plans, the Independent Distribution Consultant shall take all necessary and appropriate steps to administer the final plan for distribution of disgorgement funds in accordance with the terms of the approved Distribution Plan.

h. For the period of the engagement and for a period of two years from completion of the engagement, the Independent Distribution Consultant 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. Any firm with which the Independent Distribution Consultant is affiliated in performance of his or her duties under this Order, or of which he/she is a member, and any person engaged to assist the Independent Distribution Consultant in the performance of his/her duties under this 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 Respondent's present or former affiliates, directors, officers, employees, or agents acting in the capacity as such for the period of the engagement and for a period of two years after the engagement.

i. For good cause shown, the staff of the Commission may alter any of the procedural deadlines 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 Respondent's Offer.

Accordingly, pursuant to Section 15(b) of the Exchange Act, it is hereby ORDERED that:

A. Respondent is hereby censured.

B. Respondent shall, within 10 days of the entry of this Order, pay disgorgement of $270 million to the Securities and Exchange Commission. Such payment shall be: (A) made by wire transfer, 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) wired, hand-delivered, or mailed to the Office of Financial Management, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Stop 0-3, Alexandria, VA 22312; and (D) submitted under cover letter that identifies PSI as a Respondent in these proceedings, the file number of these proceedings, a copy of which cover letter, wire transfer instruction, money order, or check shall be sent to David P. Bergers, District Administrator, Securities and Exchange Commission, Boston District Office, 33 Arch Street, 23rd Floor, Boston, Massachusetts 02110.

C. Respondent shall comply with the undertakings enumerated in Section III., paragraph 50 of this Order.

By the Commission.

Nancy M. Morris
Secretary

Exhibit 10.4

NASD
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. E112003067901

TO: Department of Enforcement
NASD

RE: Prudential Securities, Incorporated, n/k/a Prudential Equity Group, LLC,
Respondent
BD No. 7471

Pursuant to Rule 9216 of NASD Code of Procedure, we submit 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 us alleging violations based on the same factual findings.

We understand 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 us; and
3. If accepted:
   a. this AWC will become part of our permanent disciplinary record and may be considered in any future actions brought by NASD or any other regulator against us;
   b. this AWC will be made available through NASD's public disclosure program in response to public inquiries about our 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. We 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 our testimonial obligations or right to take legal or factual positions in litigation or other legal proceedings in which NASD is not a party.

We also understand that our 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:

> Prudential Securities, Incorporated ("PSI"), n/k/a Prudential Equity Group, LLC ("PEG") (BD No. 7471), is a registered broker/dealer under the Securities Exchange Act of 1934 (the "Exchange Act") and has been a member of this Association since November 2, 1939. PEG is wholly owned by Prudential Financial, Inc. ("Prudential Financial"). Prudential Financial is a publicly-owned holding company, traded on the New York Stock Exchange, whose operating subsidiaries provide a wide range of insurance, investment management and other financial products and services to retail and institutional customers including insurance brokers and investment managers. From at least 1998 through July 2003, PSI engaged in retail securities brokerage operations and maintained branch offices in Boston, Massachusetts and elsewhere. On July 1, 2003, Prudential Financial caused PSI to transfer the assets relating to its domestic retail securities brokerage operations to a holding company controlled by an unaffiliated entity. Following this asset transfer, PSI converted from a stock corporation into a limited liability company and was renamed PEG. PEG provides equity research, sales and trading to domestic and international institutional customers.[1] PSI has a prior NASD disciplinary history, including several NASD actions alleging supervisory deficiencies.

I.

WAIVER OF PROCEDURAL RIGHTS

We specifically and voluntarily waive the following rights granted under NASD's Code of Procedure:

A. To have a Formal Complaint issued specifying the allegations against us;

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, we specifically and voluntarily waive any right to claim bias or prejudgment of the General Counsel, the NAC, or any member of the NAC, in connection with such

[1] PEG's principal place of business is in New York, New York. PEG does not have any retail operations and does not sell mutual funds.

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.

We further specifically and voluntarily waive 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. We hereby accept and consent, 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

From at least January 1, 2001 to July 1, 2003 (the "relevant period"), certain of PSI's registered representatives engaged in deceptive activities in order to make improper market timing transactions in mutual funds on behalf of their clients. The registered representatives used multiple customer account numbers and/or representative numbers (also referred to as "FA numbers" at PSI) to evade the trading restrictions ("blocks") that certain mutual funds imposed on market timing transactions. For example, following the imposition of a block, the representatives just placed the market timing trades in another account or, if an FA number had been restricted, the representatives placed trades using another FA number. PSI failed to prevent this activity. As a result, representatives defrauded mutual funds and their shareholders by misrepresenting their identities (through the use of multiple FA numbers) and the identities of their brokerage clients (through the use of multiple customer account numbers) to engage in market timing after the mutual funds had placed blocks attempting to prohibit such trading.

As a result of the violative conduct, at least 1,600 PSI customer accounts were collectively able to purchase and sell mutual fund shares worth more than $116 billion, earning those clients more than $162 million in net profits. Those market timing transactions also earned PSI nearly $50 million in gross commissions.

During the relevant period, PSI failed to maintain accurate books and records related to mutual fund transactions. Certain PSI representatives, despite time being material to the transaction, routinely failed to document the time the customer order was received. For example, there was an absence of time stamps on numerous order tickets in the Boston branch office, making it difficult to determine whether the order was received before the 4:00 p.m. market close on the trade date. As a result, PSI would not have been able to prevent and detect any late trading in mutual fund shares. Indeed, the volume of market timing business in the Boston branch office created significant risk of late trading. Mutual fund orders were often transmitted to PSI's Mutual Fund Operations department after 4:00 p.m. for processing.

Since at least 1998, PSI was aware that its Boston and three of its New York branch offices, among others, had representatives that primarily engaged in market timing transactions. Indeed, beginning in 2002, the firm's Risk Management Department had numerous meetings on the activities of those registered representatives. PSI, however, failed to have an adequate supervisory system and written supervisory procedures relating to market timing activities, mutual fund exchanges, and detecting and preventing any late trading of mutual fund shares.

Background

During the relevant period, PSI maintained branch office locations throughout the United States. Some of those branch office locations, including those located in Boston, Massachusetts, Garden City, New York, and New York, New York, maintained relationships with certain clients, including hedge funds, which engaged in "market timing" of mutual funds. Market timing is essentially the frequent trading of mutual fund shares in order to take advantage of pricing inefficiencies or market movements. Market timing can dilute the value of shares and raise fund transaction costs.

During the relevant period, PSI generally processed hundreds of separate mutual fund transactions weekly for its market timing hedge fund clients. In many instances, the hedge fund clients sent facsimiles to the PSI representative in the morning, which identified hundreds of potential mutual fund trades that the hedge fund clients might want to transact on that day or in the days ahead. Thereafter, typically in the late afternoon, the hedge fund clients would contact the PSI representatives to execute some or all of the trades on the list. The PSI registered representatives would then, often frantically, attempt to enter the trades into PSI's order entry system before the system shut down at the close of the market at 4:00 p.m. Given the number of trades requested by the hedge fund clients, the representatives were often not able to enter all those trades before the close. In that event, the representatives would often fax the remaining orders to PSI's mutual funds operations desk in New York to process the trade as of that day.

Many mutual funds maintain policies and procedures to detect and prevent market timing transactions. Typically, these policies include prohibiting future transactions after a customer has already placed a certain number of trades. To enforce these limits, the funds and/or their distributors track activity by customer account number and/or FA number. Once a customer reaches the limit, the mutual funds and/or their distributors typically send "block letters" to the brokerage firm, indicating that the mutual fund company will no longer accept exchange transactions from that customer and/or the representative. For example, a block letter received by PSI during the relevant period noted that:

> [T]he heightened level of exchange activity in the accounts raises concerns for the funds involved … [i]n light of the amount of recent exchange activity and the funds' concerns, no more exchanges will be allowed on these accounts. Should future exchange requests be submitted, [mutual fund distributor] will not accept them.

During the relevant period, PSI received thousands of communications from various mutual fund companies continually placing blocks on a limited number of representatives and their clients. As further detailed below, those PSI registered representatives engaged in a relatively straightforward scheme to evade the restrictions and continue the market timing activity.

Fraudulent Activities Relating to Mutual Fund Market Timing

During the relevant period, PSI knew, or was reckless in not knowing, that certain of its representatives were engaged in deceptive and manipulative practices in order to continue to make market timing trades for their clients. The firm, however, failed to prevent this misconduct. Those representatives, among other things, obtained successive customer account numbers and multiple FA numbers from PSI in order to evade or circumvent block letter restrictions and otherwise exceed the mutual fund exchange limits. If restrictions were imposed on one account, the representatives would continue market timing by transferring customer funds and placing the prohibited trades in another account. While the use of multiple accounts and FA numbers are not *per se* improper, these techniques were abused at PSI. For example, one group of three representatives in PSI's Boston branch office used 183 accounts for just seven different hedge fund clients engaged in market timing.

The Boston branch representatives also obtained multiple FA numbers in order to continue the market timing strategy. If a mutual fund imposed a block on a representative, the representatives would continue market timing by placing the prohibited trades using another FA number. As a result, clients that were blocked from additional mutual fund transactions were able to continue market timing because of the representatives' ability to obtain a new FA number to circumvent the block.

PSI knew, or was reckless in not knowing, of the following fraudulent activity:

- PSI representatives misrepresented their own identities and the identities of their clients in order to engage in market timing trades after the funds had blocked the representatives and/or their clients from such trading. As noted, PSI received thousands of communications from mutual fund companies relating to blocks placed continually on a limited number of representatives and clients. For example, during the relevant period, PSI received in excess of 1,000 letters and/or e-mails from over 50 different mutual fund companies relating just to the market timing activities of five representatives in its Boston branch office. In numerous cases, PSI did not prevent trading in circumvention of these blocks. To evade the blocks and continue trading, certain representatives were able to set up new accounts for their clients and/or obtain alternate FA numbers to process trades.
- In January 2003, based upon the number of letters PSI received relating to the market timing activities of its representatives, it announced a market timing policy (some two years after it had already stopped market timing in its own proprietary mutual funds). The policy required PSI's representatives to adhere to the restrictions on the frequency of trading set forth in each mutual fund's disclosure documents. The policy also provided that a request from a mutual

fund to block an FA number would be applied to all FA numbers associated with that representative. Notwithstanding this policy, PSI representatives were able to continue to use their pre-existing FA numbers and the numerous client accounts to continue market timing despite the mutual fund blocks. Moreover, certain representatives were able to obtain new FA numbers, which were used to continue the market timing activity.

- PSI representatives used “joint” FA and “also” numbers to evade the mutual fund blocks and defraud the mutual funds into accepting additional transactions. “Joint” FA numbers were generally permitted by PSI for the purpose of splitting commissions, and “also” numbers were permitted by PSI ostensibly to enable certain clients to access their account information electronically. Three Boston representatives, however, obtained 16 “joint” numbers and three “also” numbers that they were able to use to defraud mutual fund companies into accepting additional transactions on behalf of their clients. PSI was aware that the Boston representatives were primarily engaged in market timing transactions.
- In several instances, certain PSI representatives transferred client monies between and among their client’s multiple accounts in order to evade a mutual fund block. PSI knew, or was reckless in not knowing, that the “new” or additional account numbers related to the same client; that the same money was being transferred between accounts; and that that money was being used to continue trading in contravention of mutual fund blocks, or to otherwise exceed prospectus exchange limits. For example, in January 2001, a mutual fund company blocked some of the market timing accounts of a client. The representatives in the Boston branch office contacted the client who then transferred the money from the blocked accounts into other accounts at PSI and continued the market timing trading despite the block.
- Notwithstanding PSI’s knowledge that certain of its registered representatives had engaged in deceptive practices, the firm took no disciplinary action against them.
- Certain of PSI’s customers were able to exchange mutual fund shares beyond the annual limits described in the applicable prospectus. As a result, at least 1,600 PSI customer accounts engaged in market timing transactions and were collectively able to purchase and sell mutual fund shares worth more than $116 billion. Moreover, some of this activity was inconsistent with the terms of certain PSI mutual fund dealer agreements. PSI earned nearly $50 million in gross commissions from the improper market timing transactions and the client accounts made in excess of $162 million in net profits.
- PSI failed to disclose to all of its customers that certain market timing customers were able to exceed the prospectus exchange limits.

This conduct constitutes separate and distinct violations of Section 10(b) of the Exchange Act, Rule 10b-5 promulgated thereunder, and NASD Conduct Rules 2120 and 2110, and IM-2310-2.

PSI Failed To Maintain Accurate Books and Records

From at least January 2001 through August 2003, PSI failed to make, maintain and preserve accurate books and records related to mutual fund transactions. PSI, among other things, failed in numerous instances to make and preserve order tickets, and make, maintain and preserve adequate trade blotters, relating to mutual fund transactions. Moreover, where order tickets had been prepared, PSI failed in numerous instances to document the time the customer order was received by the firm and the time certain orders were executed.[2] For example, there was an absence of time stamps on numerous order tickets, making it difficult to determine whether the order was received before 4:00 p.m. on the trade date or whether the representative engaged in late trading by accepting and processing an order "after hours" in mutual funds. Moreover, certain orders that had time stamps had inaccurate times relating to when they were received at the firm. This conduct constitutes separate and distinct violations of Section 17 of the Exchange Act, Rules 17a-3 and 17a-4 thereunder, and NASD Conduct Rules 3110 and 2110.

Supervisory Violations

Since at least 1998, PSI was aware that its Boston branch office had certain representatives whose primary business was to service clients that engaged in market timing activities. Indeed, the firm's Risk Management Department had numerous meetings on the activities of those representatives. Nevertheless, PSI failed to maintain a reasonable and adequate supervisory system and written supervisory procedures relating to market timing, mutual fund exchanges, and detecting and preventing late trading of mutual fund shares. PSI failed to ensure in those areas that its written supervisory procedures were updated, maintained and enforced; and that they were reasonably designed to achieve compliance with the applicable rules and regulations. The deficiencies in PSI's system and procedures included the following areas:

- PSI's supervisory system and written supervisory procedures were not reasonably designed to prevent and detect representatives from circumventing the block letter restrictions. The firm's written supervisory procedures failed to provide steps reasonably designed to ensure that when the firm received block letters that its representatives could not circumvent those restrictions, thereby enabling certain clients and/or accounts to continue to engage in market timing activities. PSI did not prevent its representatives from obtaining additional FA numbers and establishing multiple customer accounts. In some cases, representatives obtained up to five different FA numbers, which were used to circumvent the trading restrictions placed on accounts and/or clients. As part of their scheme to evade the block letter restrictions, some PSI representatives requested that their clients sign a Letter Of Authorization ("LOA") that authorizes

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2 On November 2, 2001, the SEC amended Rules 17a-3 and 4 and announced that the amendments would become effective on May 2, 2003. Pursuant to those amendments, a broker-dealer is required to record the time the firm received a customer order on the order ticket, even if the order is subsequently transmitted for execution. The SEC intended for these amendments to provide critical trade information to securities regulators to aid their examinations and investigations. *See, Books and Records Requirements for Brokers and Dealers Under the Securities Exchange Act of 1934*, Release No. 34-44992 (November 2, 2001). From at least May 2003 through July 2003, PSI failed to comply with this requirement.

the transfer of money between the client's accounts. The establishment of multiple accounts, the widespread use of LOAs by market timing clients, and the frequent transfer of funds among market timing clients' accounts, were indications to PSI of potential misconduct. The firm, however, failed to establish policies and procedures that were reasonably designed to prevent and detect the misuse of new accounts and LOAs for market timing.

- PSI did not provide for any dedicated personnel or department to be responsible for receiving, tracking and enforcing compliance with the block letters. In addition, the firm's procedures did not require that such communications be forwarded to the firm's compliance department or another centralized location.
- PSI's supervisory system and written supervisory procedures were not reasonably designed to ensure that the firm correctly recorded mutual fund order receipt times in instances where time was material to the execution. The firm's books and records could not show whether certain mutual fund orders, whether for the execution or cancellation of a transaction, were received before or after 4:00 p.m. For example, the volume of market timing business in the Boston branch office created significant risk of late trading. Indeed, in a January 2003 e-mail, a PSI registered representative informed one of his market timing clients that "[y]ou don't realize I have to kick and claw to get trades off for you guys. I even have given you help after the close." Therefore, PSI's supervisory system was not reasonably designed to prevent and detect representatives from engaging in "after-hours" or late trading in mutual funds.
- PSI's supervisory system had inadequate checks and balances to ensure, among other things, that registered representatives and their clients adhered to the mutual fund prospectus restrictions related to market timing activities (e.g., limits on the number of exchanges per year) when alerted by the mutual fund companies that such limitations had been exceeded.

This conduct constitutes separate and distinct violations of NASD Conduct Rules 3010 and 2110.

B. We also consent to the imposition, at a maximum, of the following sanctions:

A censure and $270,000,000 in monetary sanctions. Within ten days of the issuance of this AWC, PSI shall pay the $270,000,000 into an account, not unacceptable to NASD staff, which shall be disbursed in accordance with the independent consultant plan, as further detailed below, to compensate the affected mutual funds and/or shareholders for losses sustained from at least January 1, 2001 to July 1, 2003 as a result of the improper market timing activity in PSI customer accounts and other misconduct described above. Those funds shall be disbursed only pursuant to the undertakings set forth below.

In addition, we shall comply with the following undertakings within the time periods specified (unless otherwise extended by NASD staff):

Retention of an Independent Consultant,
Disbursement of Funds and Certification of Payment

a) PSI shall retain, within 60 days of the issuance of this AWC, an independent consultant ("consultant") not unacceptable to NASD staff. The consultant's compensation and expenses shall be borne exclusively by PSI. The firm shall cooperate fully with the consultant and shall provide the consultant with access to its files, books, records, and personnel as reasonably requested for the review. PSI must not place restrictions on the consultant's communications with NASD staff. Upon request, PSI will make available to NASD any and all communications between the consultant and the firm, and any documents that the consultant reviewed or relied upon in connection with the engagement.

b) PSI shall not terminate the relationship with the consultant without the NASD staff's written approval; PSI shall not be in and shall not have an attorney-client relationship with the consultant and shall not seek to invoke the attorney-client privilege or other doctrine or privilege to prevent the consultant for transmitting any information, reports or documents to NASD.

c) PSI shall require that the consultant develop a written plan ("Plan") for the distribution of the $270,000,000, and any interest or earnings thereon, according to a methodology developed in consultation with the firm and not unacceptable to NASD staff.

d) PSI shall require that the consultant submit the Plan to the firm and NASD no more than 180 days after the issuance of this AWC.

e) The Plan shall be binding unless, within 210 days of the issuance of this AWC, either party advises the consultant, in writing, of any determination, calculation or recommendation from the Plan that it considers to be inappropriate and the reasons for its objection.

f) With respect to any determination, calculation or recommendation with which PSI or NASD staff do not agree, such parties shall attempt in good faith to reach an agreement within 240 days of the issuance of this AWC. In the event that they are unable to agree on an alternative determination, calculation or recommendation, the ultimate determinations, calculations and recommendations of the consultant shall be binding.

g) Within 360 days of the issuance of this AWC, the consultant and the firm shall implement the Plan and take all necessary and appropriate steps to distribute the account's funds.

h) Within ten days thereafter, an officer of PSI shall certify to NASD that the Plan has been implemented and that the $270,000,000, and any interest or earnings thereon, has been disbursed.

i) PSI shall require the consultant to enter into a written agreement that provides that, for the period of engagement and for a period of two years from completion of the engagement, the consultant not enter into any other employment, consultant, attorney-client, auditing or other professional relationship with PSI, or any of its present or former affiliates, directors, officers, employees, or agents acting in their capacity as such. Any firm with which the consultant is affiliated in performing his or her duties pursuant to this AWC, shall not, without the prior written consent of NASD staff, enter into any employment, consulting, attorney-client, auditing or other professional relationship with PSI, 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 thereafter.

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

III.
OTHER MATTERS

A. We understand that we may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. We understand that we 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. We specifically and voluntarily waive any other right to claim that we are unable to pay, now or at any time hereafter, any monetary sanction imposed in this matter.

We certify that we 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 us to submit it.

Prudential Securities, Incorporated, n/k/a Prudential Equity Group, LLC, Respondent

August 9, 2006
Date:

By: /s/ Kenneth Y. Tanji
Print Name: Kenneth Y. Tanji
Title: Senior Vice President

Accepted by NASD:

August 28, 2006
Date

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

/s/ Paul M. Tyrrell
Paul M. Tyrrell
Regional Counsel
NASD Department of Enforcement
99 High Street
Suite 900
Boston, MA 02110
(617) 532-3426

NASD District Director:
Frederick F. McDonald, Jr.
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Boston District Office
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N E W Y O R K S T O C K E X C H A N G E L L C

NYSE HEARING BOARD DECISION 06-156 **August 18, 2006**
PRUDENTIAL EQUITY GROUP, LLC
MEMBER ORGANIZATION

* * *

Violated Section 10(b) of Securities Exchange Act of 1934, Rule 10b-5 thereunder, and NYSE Rule 476(a)(5) by using means or instrumentality of facility on national securities exchange, in connection with purchase or sale of security, to defraud, make untrue statement of material fact, or engage in act, practice, or course of business which operates as fraud or deceit; violated Section 17(a) of Securities Exchange Act of 1934 and Rules 17a-3 and 17a-4 thereunder by failing to make and keep accurate books and records, including trade blotters and trade tickets; violated NYSE Rules 401 and 476(a)(6) by allowing certain brokers to engage in deceptive practices related to market timing of mutual funds; violated NYSE Rule 342 by failing to reasonably supervise its business activities and to establish and maintain appropriate procedures for supervision and control with respect to its business activities involving trading of mutual funds – Consent to censure, $270 million disgorgement, and undertakings.

Appearances:

For the Division of Enforcement
Susan Light, Esq.
Margaret Tolan, Esq.

For Respondent
Gail Marshall-Smith, Esq.
Neil Sullivan, Esq.

* * *

A Hearing Officer on behalf of the New York Stock Exchange LLC ("NYSE") considered a Stipulation of Facts and Consent to Penalty entered into between NYSE Regulation, Inc.'s Division of Enforcement ("Enforcement") and Prudential Equity Group, LLC, formerly known as Prudential Securities, Inc. ("Respondent," "PSI," or the "Firm"), an NYSE member organization. Without admitting or denying guilt, Respondent consented to a finding by the Hearing Officer that it:

I. Willfully violated Section 10(b) of the Securities Exchange Act of 1934 [15 U.S.C. section 78j(b)] (the "Exchange Act"), Rule 10b-5 thereunder [17 C.F.R. section 240.10b-5], and NYSE Rule 476(a)(5) by using any means or instrumentality of interstate commerce or of the mails, or of any facility on any national securities exchange, in connection with the purchase or sale of any security, to employ any device, scheme, or artifice to defraud, to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person.

II. Failed to make and keep required books and records in violation of Section 17(a) of the Exchange Act. Section 17(a)(1) of the Exchange Act required PSI to make and keep current certain specified books and records relating to its business. Implicit in the U.S. Securities and Exchange Commission's (the "Commission") recordkeeping rules is a requirement that information contained in a required book or record be accurate. Rules 17a-3 and 17a-4 enumerate those records required to be maintained, including trade blotters and trade tickets. PSI failed to maintain complete and current copies of trade blotters concerning mutual fund trading and trade tickets related to mutual fund trading in a readily accessible place. In instances where PSI did maintain trade tickets, information included on them did not represent the actual time at which the orders were placed.

III. Violated NYSE Rule 476(a)(6) in that it engaged in conduct inconsistent with just and equitable principles of trade by allowing certain of its brokers to engage in deceptive practices related to the market timing of mutual funds

IV. Violated NYSE Rule 401 in that it failed to adhere to the principles of good business practice by allowing certain of its brokers to engage in deceptive practices related to the market timing of mutual funds.

V. Violated NYSE Rule 342 by failing to reasonably supervise its business activities, and to establish and maintain appropriate procedures for supervision and control with respect to its business activities involving the trading of mutual funds.

For the sole purpose of settling this disciplinary proceeding, Enforcement and Respondent stipulate to certain facts,* the substance of which follows:[1]

Background and Jurisdiction

1. PSI was a member organization of the NYSE and maintained its headquarters and principal place of business in New York. Prior to July 1, 2003, PSI was an indirect wholly-owned broker-dealer subsidiary of Prudential Financial, Inc. ("Prudential

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* Hearing Officer Note: The facts, allegations, and conclusions contained in paragraphs 1 to 45 are taken from the executed Stipulation of Facts and Consent to Penalty between Enforcement and Respondent. No changes have been made to the stipulated paragraphs by the Hearing Officer.

[1] The findings made herein are not binding on Respondent or any other Prudential Financial, Inc. entity in any other forum, nor are the findings binding on any other person or entity.

Financial"). Prudential Financial is a publicly-owned holding company, traded on the New York Stock Exchange, whose operating subsidiaries provide a wide range of insurance, investment management and other financial products and services to retail and institutional customers including insurance brokers and investment managers. On July 1, 2003, PSI transferred the assets relating to its U.S. retail securities brokerage operations to a newly formed holding company, now named Wachovia Securities Financial Holdings, LLC ("WSFH"). Prudential Financial presently owns 38% of WSFH and Wachovia Corporation owns 62% of WSFH. Since July 1, 2003, PSI's former U.S. retail securities brokerage business has operated as part of Wachovia Securities, LLC. Following the asset transfer, PSI converted from a stock corporation into a limited liability company and was renamed Prudential Equity Group, LLC ("PEG"). PEG is a broker-dealer registered with the Commission pursuant to Section 15(b) of the Exchange Act and is a member of the National Association of Securities Dealers and the New York Stock Exchange. PEG provides equity research, sales and trading to domestic and international institutional customers and is a successor entity to PSI. Prudential Financial continues to own 100% of the equity interests in PEG.

2. On or about October of 2003, Enforcement notified Respondent of its investigation into possible violative conduct involving the market timing of mutual funds by certain of Respondent's registered representatives and of its supervision of its mutual fund trading business.

Summary

3. This matter concerns a fraudulent market timing scheme perpetrated by PSI registered representatives (collectively, the "Brokers") whose business involved market timing to defraud at least fifty mutual funds and their long term shareholders. Beginning in at least September 1999 and continuing through at least June 2003 (the "Relevant Period"), the Brokers used deceptive trading practices to conceal their identities, and those of their customers, to evade mutual funds' prospectus limitations on market timing. These practices included the use of multiple broker identifying numbers (known as Financial Advisor, or "FA" numbers) and multiple customer accounts; the use of accounts coded as confidential in PSI's systems; and the Brokers' use of "under the radar" trading to avoid notice by mutual funds. Typically, mutual funds screened for market timing trades only above a designated dollar amount. The practice of "under the radar" trading refers to the Brokers' splitting of one trade into numerous smaller ones to avoid detection by mutual funds.

4. As early as the fourth quarter 1999, several mutual fund companies identified the Brokers' use of deceptive trading practices and notified PSI of the Brokers' conduct. In May 2002, PSI itself determined that its top-producing broker used deceptive trading practices to avoid notice by mutual funds. Throughout the Relevant Period, PSI received hundreds of notices from mutual fund companies that identified the Brokers' conduct and asked the Firm to take steps to curtail their deceptive market timing practices.

5. Despite PSI's increasing awareness of the Brokers' fraudulent market timing practices, the Firm elected to continue the business of market timing. Rather than discipline or sanction any of the Brokers or even curtail their ability to open additional accounts for their market timing customers, PSI failed to prevent their conduct from continuing and actually began to track the Brokers' gross revenues. In 2001, for example, the Brokers generated more than $16 million in gross commission revenues for the Firm, most of which was in danger of being eliminated had the Firm phased out market timing at that time. Similarly, the Brokers generated approximately $23 million in gross commission revenues in 2002, and continued to generate comparable revenues throughout the Relevant Period.

6. PSI's policies and procedures were ineffective in curtailing the Brokers' fraud and were largely not enforced. Even in situations where PSI purportedly enforced any of these policies, PSI senior officers undermined them by granting exceptions for PSI's largest producing brokers. Additionally, PSI repeatedly failed to deprive the Brokers of their inappropriate use of hundreds of FA numbers, even though the use of multiple FA numbers was the primary means by which the Brokers carried out their fraud. PSI finally issued a market timing policy in January 2003, but the Firm did not fully enforce procedures in that policy to curtail the Brokers' scheme. As a result of the conduct described above, PSI violated the antifraud and books and records provisions of the federal securities laws, and NYSE Rules 401, 476(a)(5)-(6), 440 and 342, which relate to good business practices, just and equitable principles of trade, NYSE books and records requirements and failure to supervise.

Background

7. Market timing includes frequent buying and selling of shares of the same mutual fund or buying or selling of mutual fund shares in order to exploit inefficiencies in mutual fund pricing. Though not illegal *per se*, market timing can harm mutual fund shareholders because it can dilute the value of their shares, if the market timer is exploiting pricing inefficiencies, or disrupt the management of the mutual fund's investment portfolio and can cause the targeted mutual fund to incur costs borne by other shareholders to accommodate frequent buying and selling of shares by the market timer.

8. Beginning in the late 1990s, many mutual funds determined that market timing harmed their long-term shareholders. As a result, they began to monitor market timing in their funds' shares and imposed restrictions on excessive trading. Such restrictions limited the number of trades that an account holder could place in a fund's shares and often were set forth in the funds' prospectuses. Many funds monitored trading activity to detect any violations of these prospectus limitations.

9. Most mutual funds received trade instructions from PSI through the National Securities Clearing Corporation ("NSCC"). NSCC is a centralized trade clearance and settlement system that linked the Brokers, PSI, and virtually all mutual fund

companies. To place trades that were transmitted through NSCC, the Brokers were required to identify their FA number and a customer account to mutual funds on trade tickets. PSI appended additional information to the Brokers' orders and transmitted the transactions through NSCC to the mutual fund companies.

10. Some mutual funds screened for excessive short -term trading by reviewing FA and customer account numbers that the Brokers transmitted to them via NSCC. Some also monitored for excessive short -term trading by trade size and principal amount and by the branch code attached to a trade.[2] Typically, if a fund concluded that a shareholder had violated its exchange limitations, the fund would attempt to prevent, or "block" additional trades in a fund or fund family by that shareholder. If a fund determined that a particular PSI broker or shareholder had violated its exchange limitations, the fund would send a "block letter" to PSI. Block letters varied but generally notified PSI of the mutual fund's intention to block the broker or customer's transaction and often asked PSI to take steps to preclude a particular broker or customer account from engaging in additional trades in a particular fund or fund family.

11. Because these mutual funds monitored for excessive trading by FA number and/or customer account number, the Brokers altered their use of these numbers to defraud these funds and the funds' long-term shareholders. By altering their use of these numbers, the Brokers tricked mutual fund companies into accepting trades that the funds otherwise would have rejected.

<u>The Brokers' Deceptive Conduct</u>

12. During the Relevant Period, the Brokers engaged in a fraudulent scheme to circumvent blocks imposed by mutual funds on their trading privileges. The Brokers' scheme worked as follows. The Brokers' customers, typically hedge funds, asked the Brokers to purchase and sell mutual funds on a short-term basis on their behalf. The Brokers, however, knew that mutual funds tracked their trades by FA number and customer account number, and they knew that if they placed short-term mutual fund trades for their customers using a single FA or account number, the mutual funds would likely determine the number of trades was excessive and would block any further trades by them.

13. The Brokers, therefore, devised a scheme to conduct their customers' trading using dozens of customer accounts, often established under fictitious names, and multiple FA numbers to make it difficult for mutual funds to identify their customers' market timing. When the mutual funds succeeded in blocking certain FA numbers or customer accounts from further trading, the Brokers then used other FA numbers and customer accounts that had not yet been blocked to evade the funds' restrictions and continue to trade.

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[2] PSI assigned branch codes to each of its retail branch offices. Branch codes identified to mutual funds the PSI branch office from which a particular market timing trade originated.

The Boston Brokers

14. For example, one group of PSI brokers based in its Boston, Massachusetts branch office (the "Boston Brokers") repeatedly used these deceptive practices to defraud mutual funds throughout the Relevant Period. The Boston Brokers consisted of a group of three PSI brokers and several registered assistants. The group had five customers for whom it placed market timing trades, each of whom acted on behalf of one or more hedge funds. During the Relevant Period, PSI received approximately $8 million from the Boston Brokers' market timing activities, of which group members received approximately $4.6 million. As a result of this business, the head of the group quickly rose to become one of PSI's top producers.

15. Many of the mutual funds in which the Boston Brokers traded screened for market timing trades by FA and customer account numbers. Many fund companies sent notices to PSI that complained that the group's trades had violated prospectus limitations. Some mutual funds announced steps they had taken to preclude the Boston Brokers from further trading while others asked that PSI take steps to block further trades by the group in the fund.

16. During the Relevant Period, the Boston Brokers used at least thirteen FA numbers and hundreds of customer accounts (for what were, in reality, only five customers) to circumvent these blocks and preclude new blocks. The Boston Brokers' use of these devices in connection with market timing allowed group members to continue to place trades in funds that had taken steps to preclude them from further trading. This scheme created the impression that transactions originated from many brokers and represented many different customers. In fact, what appeared to the mutual funds to be thousands of separate transactions submitted by many brokers for many unrelated customers was actually a systematic pattern of market timing by group members on behalf of their five hedge fund customers.

The Garden City Broker

17. Another PSI broker based in its Liberty Plaza and Garden City, New York branch offices (the "Garden City Broker") used these same deceptive practices to defraud mutual funds throughout the Relevant Period. The Garden City Broker headed a team of brokers and registered assistants, although he very rarely reported to work at any PSI location. He had five customers for whom he placed market timing trades, each of whom acted on behalf of one or more hedge funds. During the Relevant Period, PSI received approximately $9.8 million from the Garden City Broker's market timing activities (of which the Garden City Broker received approximately $4.7 million). The Garden City Broker was the top producing broker at PSI throughout the Relevant Period.

18. Like the Boston Brokers, the Garden City Broker traded in mutual funds that screened for market timing by FA and customer account number. During the Relevant Period, approximately fifty mutual funds complained to PSI about the Garden City Broker's trading activity. Many mutual funds specifically identified to PSI his use of deceptive trading strategies to evade blocks the fund companies had imposed.

19. To evade these blocks, the Garden City Broker maintained 49 different FA numbers and hundreds of customer account numbers (for what were, in reality, only five customers). His use of these devices to market time created the impression that the trades originated from many brokers and many customers. By shifting trades from one FA number to another, or from one customer account to another, the Garden City Broker concealed his identity and was able to place trades in mutual funds where PSI previously had blocked his trading under his other FA numbers and accounts.

The Special Accounts Brokers

20. Another group of PSI brokers based in a New York office known within the Firm as "Special Accounts" (the "Special Accounts Brokers") also used deceptive practices to defraud mutual funds throughout the Relevant Period. The Special Accounts Brokers consisted of a group of two PSI brokers and several registered assistants. The group had three customers for which it placed market timing trades. During the Relevant Period, PSI received approximately $6.5 million from the Special Accounts Brokers' market timing activities, of which group members received approximately $2.5 million. As a result of this business, the heads of the group quickly achieved membership in PSI's Chairman's Club, a select group consisting of the largest producing brokers within the Firm.

21. Like the Boston Brokers and the Garden City Broker, the Special Accounts Brokers knew that most mutual funds identified excessive trading by FA and customer account number. They also understood that mutual funds screened for market timing by reviewing only those trades at or exceeding certain dollar amounts. The Special Accounts Brokers used at least 20 FA numbers and hundreds of customer accounts (for what were, in reality, only three customers) to avoid detection by mutual funds. The Special Accounts Brokers also used "under the radar" trading to disguise their customers' trading in funds that previously had taken steps to stop them. The brokers' use of these devices in connection with market timing deceived mutual funds into accepting trades they otherwise would have rejected. Like the Boston Brokers and the Garden City Broker, their scheme perpetuated the impression that transactions originated from many brokers and represented many different customers.

PSI Failed to Prevent the Brokers From Obtaining Multiple Broker Identification and Customer Account Numbers

22. PSI failed to prevent the Brokers from obtaining several different forms of broker identifying numbers. Consequently, the Brokers used these numbers to perpetrate their scheme to defraud. When brokers began their employment with PSI, PSI assigned them an FA number. The Brokers used FA numbers to open customer accounts, execute trades, and track their commissions. When brokers worked as a team to service common customers, PSI provided "Joint" numbers. Joint numbers

ostensibly represented a commission split between two or more brokers. Here, the Brokers acquired and used Joint numbers for improper purposes. The numbers were not used to split commissions, but rather to facilitate the Brokers' ability to trade after their other broker identifying numbers had been blocked from trading. PSI also provided the Brokers with "Also" numbers. The purported purpose of "Also" numbers was to allow the Brokers' customers to access only those portions of a given broker's portfolio that belonged to that customer or to provide certain customers with commission discounts. The Brokers, however, used Also numbers improperly in the same manner as they used FA and Joint Numbers – to circumvent blocks that had been imposed on their other FA numbers. Indeed, at least one mutual fund became so frustrated by its inability to identify the Brokers that it threatened to curtail the trading privileges of all brokers within a PSI branch to remedy the conduct.

23. Each of the Brokers maintained numerous FA, Joint, and Also numbers, and used these numbers interchangeably to execute trades for their customers. For example, the Boston Brokers used 13 broker identifying numbers to place market timing trades and the Garden City Broker used 49 broker identifying numbers. When one of the Broker's FA, Joint, or Also numbers was blocked from trading by a particular mutual fund, he used another number assigned to him to place the trade in that fund. Although each joint number ostensibly represented a unique commission split, in fact each team of Brokers split commissions from mutual fund purchases according to a single ratio, irrespective of which broker identifying number was used to enter the trade.

24. PSI failed to prevent the Brokers from opening hundreds of customer account numbers. The Brokers' customers maintained multiple accounts with PSI, many of which bore fictitious names that had no relation to the actual customer's name. The Brokers used these customer accounts interchangeably to execute trades. When one customer account was blocked from trading by a particular mutual fund, the Brokers substituted another account for that same customer to place the trade for that customer, thereby creating the appearance that the trade originated from another customer.

25. PSI failed to prevent the Brokers from obtaining accounts for their customers that were coded as "Confidential." Confidential accounts did not identify the beneficial owner of the account on the transaction data provided to the mutual funds. Although such a designation could have a legitimate purpose, here the Brokers used Confidential accounts improperly to impede the mutual funds' ability to identify which PSI broker or customer was market timing their funds.

26. PSI also failed to prevent the Brokers from obtaining customer account numbers with multiple branch identifiers. Typically, brokers located in one PSI branch office had customer accounts that had a prefix used to identify the branch location. Here, the Brokers established accounts for their hedge fund customers using multiple branch codes, which effectively impeded the mutual funds' ability to identify the particular PSI office location, as well as broker, that was market timing their funds. The Brokers used branch identifiers improperly as another mechanism to conceal their identities and the identities of their customers to mutual funds.

PSI Received Notifications of the Brokers' Deceptions

27. During the Relevant Period, mutual fund companies sent more than a thousand letters and emails to PSI concerning market timing by the Brokers. Many of these communications asked PSI to take steps to stop further trading by a particular customer account or FA number. Others expressly notified PSI that the Brokers used deceptive trading practices to continue placing market timing trades.

28. High level officers of PSI were aware during the Relevant Period that mutual funds were accusing the Brokers of using deceptive practices to evade the mutual funds' attempts to block the Brokers' market timing trades. For example, an individual who joined PSI in 1997 and rose to become the chief administrator of PSI's Private Client Group ("PCG") in January 1999, then to become executive director of PCG in November 2000, and finally to president of PCG in December 2002 ("the Senior Officer") received repeated notices of wrongdoing by the brokers throughout the Relevant Period, but did not take adequate steps to stop the Brokers' fraud. Among other things, the Senior Officer received the following indications that the Brokers were committing fraud. In some cases, certain other senior managers or high level officers of PSI also received notices that the Brokers were committing fraud.

29. On November 21, 1999, a senior executive in the PSI Mutual Fund Operations division forwarded to the Senior Officer a string of emails concerning a complaint from a mutual fund complex that the Garden City Broker had evaded a block on two of his accounts by simply opening new accounts. Among other things, the email stated:

> It appears that [the Garden City Broker] circumvented this restriction by requesting new BIN [account] #s and fund accounts be established, funded by transferring shares into these new accounts on 11/8/99. Subsequently on 11/10/99, an exchange out of the money fund into our stock funds was processed, beginning market timing again.

The cover email commented, "[T]his seems to be a serious matter that will only get worse."

30. On January 19, 2000, the manager of PSI's Mutual Fund Operations division forwarded to the Senior Officer an email from another mutual fund complex complaining that a member of the Boston Brokers had evaded a trading restriction by opening a new account, stating:

> It appears that [the member] set up another account in December for the same client we restricted on 11/22.

31. On March 30, 2001, the head of PCG risk management sent to the Senior Officer an email that attached a letter from another mutual fund complex complaining that "excessive trading activity" by PSI brokers in its mutual funds "has become detrimental to both the funds and shareholders of the funds involved." The letter described the tactics used by PSI brokers to avoid having their trades canceled as follows:

> Since trade cancellation began on February 26th, 2001, we have noticed several types of reactions by Prudential Financial Advisors in order to circumvent our attempts to terminate excessive trading. Originally, your Financial Advisors established new identification numbers so that they would not be recognized as a repeat offender. Secondly, Financial Advisors would transfer a fund(s) position from account to account, in order to disguise their identity. Lastly, your Financial Advisors have attempted to reduce the dollar amount of the exchange orders while simultaneously increasing the number of exchanges (in the same fund and account) in the hopes of not being identified.

32. On June 28, 2001, the Senior Officer received an email from the manager of the Special Accounts branch warning him that the Special Accounts Brokers were obtaining multiple FA numbers in order to conduct their market timing, stating that:

> We will have an issue soon with joint FA numbers: in order to get around the MF [mutual fund] timing issue they are starting to request 99/01 split numbers with their junior partners to help them get around being shut down by some MF companies on timing.

33. On April 4, 2002, the manager of PSI's Mutual Funds Operations division sent an email to other senior managers forwarding an email from another mutual fund complex complaining that certain PSI brokers were using multiple accounts and FA numbers to evade restrictions on their market timing. The email stated:

> What we have seen scares us. It appears certain representatives are changing account registrations, tax id numbers, and branch and rep numbers in an effort to time the [mutual fund complex's] funds. All of these accounts have been stopped, but each day "new" ones pop up.

When the PSI chief compliance officer saw the above email, he showed it to the Senior Officer. The head of PCG risk management also discussed the email with the Senior Officer.

34. On April 29, 2002, the Senior Officer met with an internal PSI working group that had been analyzing market timing issues. The group described for the Senior Officer the mutual fund companies' restrictions on excessive trading, the fund companies' block letters to PSI, and the deceptive trading strategies used by certain PSI brokers, including multiple accounts and FA numbers.

35. On at least two occasions in May 2002, an employee of PSI's risk management division detailed for the Senior Officer several deceptive practices used by the Garden City Broker. The employee's analysis noted that in one 37-day period, the Garden City Broker had 19 different mutual fund companies request that accounts under the broker's control, or the broker as an FA, be blocked from their funds. The analysis concluded that the Garden City Broker had circumvented these requests by changing his FA number to an Also or Joint Number to avoid detection by the fund, or by changing customer account numbers and moving the assets from the blocked account to a newly established account.

36. On February 5, 2003, the director of strategic planning at PCG sent the Senior Officer (then the President and most senior officer of PCG) a string of emails from another mutual fund complex complaining that certain PSI brokers were using multiple customer accounts and FA numbers for market timing. One of the emails stated:

> I have spoken to these reps a few times over the past several months about stopping their timing activity to no avail. Over the past several months, we have placed stops on 325 of their accounts as of 11/30/02 and continue to add accounts daily. We see new accounts/rep id combinations being opened and have determined that we are not able to continue chasing them within our funds. We feel our only course of action to protect our fund shareholders is to prohibit the attached list of reps from doing business with [our funds].

Another email in the string stated:

> These reps have multiple rep ids and have continued to add new ones as we block the ids within the NSCC trading system for our fund complex… These reps created close to $3 billion in exchanges last year with $75 million of assets during a time in which we placed stops on 350 of their accounts.

The director of strategic planning added his own warning to the Senior Officer:

> I just wanted to give you a heads up on an issue that is sure to reach your desk in the next day or two. As you can see from the attached string of notes, the senior leadership team at [a mutual fund complex] are completely frustrated with some of the tactics/strategies of FA's [the Garden City Broker and the Boston Brokers]. Previous attempts to curtail timing activity in the [mutual fund complex's] funds by blocking account activity have been thwarted by the establishment of additional FA numbers. It appears that [the mutual fund complex] is now making overtures that continued activity of this nature will threaten the relationship between Prudential and the fund company.

37. On February 11, 2003, a PCG risk officer sent an email to the Senior Officer (then the President and most senior officer of PCG) that forwarded an email from the Garden City branch manager about the Garden City Broker's market timing business. The branch manager questioned the effectiveness of the Mutual Fund Operations

division’s internal blocking system and raised several other concerns about the Garden City Broker’s activities:

> Blocking of individual accounts by fund companies is extremely short-sighted in consideration of the fact that each “entity” maintains multiple accounts with our Firm.
>
> There have been repeat offenses, at least in spirit…
>
> Fund companies have been mislead as to the identity of the FA’s of record… Recently, [a mutual find company] was provided with information which was at best misleading to effect the removal [of] a block.
>
> [T]here is frequent journaling of funds between accounts.
>
> At the present time, [the Garden City Broker and an assistant] either have or have had a total of 48 FA #’s including single, joint and also numbers.

PSI’s Procedures to Limit Market Timing Were Ineffective

38. Although PSI senior officers issued policies and procedures ostensibly designed to proscribe the Brokers’ conduct, these policies and procedures were ineffective in scope and were never fully enforced. Moreover, even in situations where these policies and procedures purportedly were enforced, PSI senior officers undermined them by granting exceptions for its largest producing brokers. As a result, the Brokers’ deceptions continued even after these policies and procedures were promulgated.

PSI’s June 2002 Procedure Concerning Issuance of FA Numbers

39. In June 2002, PSI instituted a procedure concerning the issuance of FA numbers, in a purported effort to hinder the Brokers’ ability to obtain “Joint” numbers and “Also” numbers to evade limitations on market timing (the “June 2002 Procedure”). The June 2002 Procedure provided, simply, that requests for “Joint” and “Also” numbers would require a documented business request and a PSI Regional Business Manager’s approval. The June 2002 Procedure failed to preclude the Brokers from misusing previously issued Joint and Also numbers to evade blocks imposed by mutual fund companies. Indeed, the Garden City Broker obtained 12 new Joint and Also numbers just days before the procedure took effect, purportedly to assist him in transferring customer accounts from one PSI branch office to another. The June 2002 Procedure also did not subject the Brokers to any form of discipline or sanction if they continued to use Joint and Also numbers to evade blocks in violation of its terms.

PSI's January 2003 Market Timing Policy

40. After protracted discussion involving PSI senior officers and attorneys during the Fall of 2002, PSI issued a market timing policy on January 8, 2003 (the "Market Timing Policy"). PSI considered, and rejected, defining market timing in the Market Timing Policy as a certain number of trades because of concerns that doing so would have too great an impact the Brokers' revenues. PSI also rejected an absolute prohibition on the business of market timing. Instead, the Market Timing Policy provided that "inappropriate timing activities [would] continue to be monitored" by mutual fund companies and not by PSI itself.

41. Unlike other PSI policies concerning market timing, the Market Timing Policy expressly provided for the imposition of sanctions, including termination of employment, for the brokers' use of "manipulative techniques" to evade mutual fund trading restrictions. Any imposition of sanctions was to be decided by a committee consisting of members of PSI's Legal, Compliance, and Risk Management divisions. Despite notifications of continuing deceptive practices received by PSI after it issued the Market Timing policy, PSI did not form this committee and failed to take action against any of the Brokers to stop their use of "manipulative techniques" to market time.

42. The Market Timing Policy also provided that, in the event a mutual fund company asked PSI to block any one of a broker's FA numbers, **all** numbers belonging to the broker similarly would be blocked from trading. However, PSI senior officers determined not to implement this critical aspect of the Market Timing Policy. In fact, despite the policy's clear language, PSI interpreted mutual fund block requests after it issued the Market Timing Policy in the same manner as it had previously – as narrowly as possible, blocking only the specific FA number or customer account number identified by mutual fund block requests. Thus, even after issuance of the Market Timing Policy, the Brokers were able to continue their fraudulent scheme of switching to unblocked FA numbers or customer accounts to evade blocks imposed by mutual fund companies.

PSI Profited From the Brokers' Deceptive Acts

43. PSI identified the Brokers as early as 2000 and monitored their revenues and ranks within the Firm throughout the Relevant Period. The Firm's Mutual Funds Operations division, which processed the Brokers' trades in mutual funds, monitored the Brokers' activity because their rapid trading required the dedication of additional staff within the department to process the trades and strained the Firm's trade processing and settlement systems.

44. In 2000, PSI began to track each quarter the gross commission revenues generated by the Brokers. PSI prepared these reports to determine the amount of income that would possibly be reduced if the Firm determined to eliminate market timing as a business. In 2001, for example, the Brokers generated more than $16 million in gross

commission revenues for the Firm, most of which would have been eliminated had the Firm phased out market timing at that time. Similarly, the Brokers generated approximately $23 million in gross commission revenues for 2002, and received another $10 million in gross commission revenues during the first half of 2003.

45. As PSI senior officers became increasingly aware of the Brokers' use of deceptions, the Firm elected to continue the business of market timing. Indeed, some of the Firm's senior officers were aware that the June 2002 Procedure concerning the issuance of multiple FA numbers and the January 2003 Market Timing Policy were wholly ineffective at eradicating the Brokers' deceptions and that the Brokers and their hedge fund customers continued this activity. During the Relevant Period, the Brokers generated approximately $50 million in gross revenues as a result of this conduct.

DECISION

The Hearing Officer, in accepting the Stipulation of Facts and Consent to Penalty, found Respondent guilty as set forth above.

PENALTY

In view of the above findings, the Hearing Officer imposed the penalty consented to by Respondent of a censure, the payment of disgorgement in the amount of $270 million,[3] and compliance with the following undertakings:

Independent Distribution Consultant. Respondent shall retain, within 60 days of this Decision's becoming final, the services of an independent distribution consultant (the "Independent Distribution Consultant") acceptable to Enforcement.

a. Respondent shall be responsible for all costs and expenses associated with the development and implementation of a distribution plan (the "Distribution Plan"). Such costs and expenses shall include, without limitation (i) the compensation of a tax administrator for the preparation of tax returns and/or for seeking any IRS rulings; (ii) the payment of taxes; and (iii) the payment of any distribution or consulting services as may be reasonably required by the Independent Distribution Consultant. Respondent shall cooperate with the tax administrator to see that all tax payments are timely made, and all such tax payments shall be deposited in the Qualified Settlement Fund upon notice from the tax administrator concerning the amount and the deadline for payment.

3 Payment of this amount, pursuant to an order issued in a related Commission proceeding involving Respondent and the same underlying facts (the "Commission's Order"), shall be deemed payment in satisfaction of the Hearing Board decision in this matter (the "Decision"). The terms of the payment and the distribution of the disgorgement amounts are set forth in the Commission's Order.

b. Respondent shall cooperate fully with the Independent Distribution Consultant to provide all information requested for its review, including providing access to its files, books, records, and personnel.

c. The Independent Distribution Consultant shall develop a proposed Distribution Plan for the distribution of the total disgorgement ordered in this decision, and any interest or earnings thereon, according to a methodology developed in consultation with and acceptable to the staff of the Commission.

d. The Independent Distribution Consultant shall submit to Respondent and Enforcement the proposed Distribution Plan no more than 180 days after this Decision becomes final.

e. The proposed Distribution Plan developed by the Independent Distribution Consultant shall be binding, unless, within 210 days after the Decision in this matter becomes final, Respondent or Enforcement advises, in writing, the Independent Distribution Consultant of any determination or calculation from the Distribution Plan considered to be inappropriate and states in writing the reasons for considering such a determination or calculation inappropriate.

f. With respect to any calculation with which Respondent or Enforcement do not agree, such parties shall attempt in good faith to reach an agreement within 240 days of this Decision's becoming final. In the event the Respondent and Enforcement are unable to agree on an alternative determination or calculation, the determinations of the Independent Distribution Consultant shall be included in the proposed Distribution Plan.

g. Within 285 days of this Decision's becoming final, the Independent Distribution Consultant shall submit the proposed Distribution Plan for the administration and distribution of disgorgement funds pursuant to the Securities and Exchange Commission's Rules on Fair Fund and Disgorgement Plans, 17 C.F.R. Section 201.1100, et seq., (Rules 1100 through 1106). Following a Commission order approving a final plan of distribution, as provided in Rule 1104 [17 C.F.R. Section 201.1104] of the SEC's Rules on Fair Fund and Disgorgement Plans, the Independent Distribution Consultant shall take all necessary and appropriate steps to administer the final plan for distribution of disgorgement funds in accordance with the terms of the approved Distribution Plan.

h. For the period of the engagement and for a period of two years from completion of the engagement, the Independent Distribution Consultant 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. Any firm with which the Independent Distribution Consultant is affiliated in performance of his or her duties under the this Decision, or of which he or she is a member, and any person engaged to assist the Independent Distribution Consultant in the performance of his or her duties under this Decision, shall not, without prior written consent of Enforcement, enter into any employment, consultant, attorney-client, auditing or other professional relationship with Respondent, or any of Respondent's present of former affiliates, directors, officers, employees, or agents acting in the capacity as such for the period of the engagement and for a period of two years after the engagement.

i. For good cause shown, Enforcement may alter any of the procedural deadlines set forth above.

For the Hearing Board

/s/ Peggy Kuo

Peggy Kuo - Chief Hearing Officer

Exhibit 10.6

STATE OF NEW JERSEY
OFFICE OF THE ATTORNEY GENERAL
DEPARTMENT OF LAW & PUBLIC SAFETY
NEW JERSEY BUREAU OF SECURITIES

P.O. Box 47029
Newark, New Jersey 07101
(973) 504-3600

IN THE MATTER OF	:	**CONSENT ORDER**
PRUDENTIAL SECURITIES Incorporated. n/k/a PRUDENTIAL EQUITY GROUP, LLC	:	

Pursuant to the authority granted to the Chief of the New Jersey Bureau of Securities ("Bureau") by the Uniform Securities Law (1997) N.J.S.A. 49:3-47 *et seq*. (the "Securities Law"), and after investigation and review and due consideration of the facts and statutory provisions set forth below, the Bureau Chief has determined that Prudential Securities, Incorporated ("PSI" or the "Respondent") shall pay disgorgement in the amount of $270 million as part of a joint administrative settlement. Payment of this amount pursuant to an order issued in a related Securities and Exchange Commission proceeding (the "SEC Final Order") shall be deemed payment in satisfaction of this Consent Order. Respondent through counsel (Neal E. Sullivan, Esq. of Bingham McCutchen LLP appearing) now in the interest of avoiding the cost and inconvenience of formal judicial or administrative proceedings, desires to resolve this matter and consent to the form and entry of this order.

WHEREAS, the Bureau is the State agency with responsibility to administer the Securities Law; and

WHEREAS, N.J.S.A. 49:3-68 provides the Bureau Chief with investigative authority necessary to determine whether there exists a violation of the Securities Laws; and

WHEREAS, PSI is a broker-dealer registered in the State of New Jersey; and

WHEREAS, the Bureau has conducted an investigation into the fraudulent trading activities of certain PSI agents in connection with the purchasing, exchanging, and redeeming of mutual funds on behalf of their clients and discovered evidence that PSI failed to supervise the agents; and

WHEREAS, PSI is continuing to cooperate with the Bureau's ongoing investigation into the activities of the agents and others, by responding to inquiries, providing documentary evidence and other materials, and providing the Bureau with access to facts relating to the investigation, books and records, and personnel; and

WHEREAS, N.J.S.A. 49:3-67 authorizes the Bureau Chief from time to time to issue such orders as are reasonably necessary to carry out the provisions of the Securities Law; and

WHEREAS, the Bureau Chief believes that the sanctions imposed herein are in the public interest, for the protection of investors and consistent with the policy and purposes intended by the Securities Laws, as provided in N.J.S.A. 49:3-67(b) thereof; and

WHEREAS, PSI admits the jurisdiction of the Bureau, neither admits nor denies the Bureau's allegations, and solely for the purposes of this consent order, prior to a hearing on the allegations in the consent order and without an adjudication of any issue of law or fact, consents to the entry of this consent order and voluntarily agrees:

a. To waive its opportunity for hearing on the allegations in the consent order after reasonable notice within the meaning of N.J.S.A. 49:3-58(c) (2); and

b. To not seek judicial review of, or otherwise challenge or contest, the validity of this consent order; and

WHEREAS, this consent order concludes the investigation by the Bureau and any civil or administrative action that could be commenced under the Securities Law on behalf of the State of New Jersey as it relates to seeking civil monetary penalties or other relief against PSI for market timing-related activities.[1]

WHEREAS, the Bureau Chief makes the following findings:

BACKGROUND

1. This matter concerns a fraudulent market timing scheme perpetrated by agents of PSI whose business involved market

[1] The findings made herein are not binding on Respondent or any other Prudential Financial entity in any other forum.

timing to defraud at least fifty mutual funds and their long term shareholders. Beginning in at least September 1999 and continuing through at least June 2003 (the "Relevant Period"), the agents used deceptive trading practices to conceal their identities, and those of their customers, to evade mutual funds' prospectus limitations on market timing. These practices included the use of multiple identifying numbers (known as Financial Advisor, or "FA" numbers) and multiple customer accounts; the use of accounts coded as confidential in PSI's systems; and the agents' use of "under the radar" trading to avoid notice by mutual funds. Typically, mutual funds screened for market timing trades only above a designated dollar amount. The practice of "under the radar" trading refers to the agents' splitting of one trade into numerous smaller ones to avoid detection by mutual funds.

2. As early as the fourth quarter 1999, several mutual fund companies identified the agents' use of deceptive trading practices and notified PSI of the agents' conduct. In May 2002, PSI itself determined that its top-producing agent used deceptive trading practices to avoid notice by mutual funds. Throughout the Relevant Period, PSI received hundreds of notices from mutual fund companies that identified the agents' conduct and asked PSI to take steps to curtail their deceptive market timing practices.

3. Despite PSI's increasing awareness of the agents' fraudulent market timing practices, PSI elected to continue the business of market timing. Rather than discipline or sanction any of the agents or even curtail their ability to open additional

accounts for their market timing customers, PSI failed to prevent their conduct from continuing and actually began to track the agents' gross revenues. In 2001, for example, the agents generated more than $16 million in gross commission revenues for PSI, most of which was in danger of being eliminated had PSI phased out market timing at that time. Similarly, the agents generated approximately $23 million in gross commission revenues in 2002, and continued to generate comparable revenues throughout the Relevant Period.

4. PSI's policies and procedures were ineffective in curtailing the agents' fraud and were largely not enforced. Even in situations where PSI purportedly enforced any of these policies, PSI senior officers undermined them by granting exceptions for PSI's largest producing agents. Additionally, PSI repeatedly failed to deprive the agents of their inappropriate use of hundreds of FA numbers, even though the use of multiple FA numbers was the primary means by which the agents carried out their fraud. PSI finally issued a market timing policy in January 2003, but PSI did not fully enforce procedures in that policy to curtail the agents' scheme.

FINDINGS OF FACT

5. Market timing includes frequent buying and selling of shares of the same mutual fund or buying or selling of mutual fund shares in order to exploit inefficiencies in mutual fund pricing. Though not illegal *per se*, market timing can harm mutual

fund shareholders because it can dilute the value of their shares, if the market timer is exploiting pricing inefficiencies, or disrupt the management of the mutual fund's investment portfolio and can cause the targeted mutual fund to incur costs borne by other shareholders to accommodate frequent buying and selling of shares by the market timer.

6. Beginning in the late 1990s, many mutual funds determined that market timing harmed their long-term shareholders. As a result, they began to monitor market timing in their funds' shares and imposed restrictions on excessive trading. Such restrictions limited the number of trades that an account holder could place in a fund's shares and often were set forth in the funds' prospectuses. Many funds monitored trading activity to detect any violations of these prospectus limitations.

7. Most mutual funds received trade instructions from PSI through the National Securities Clearing Corporation ("NSCC"). NSCC is a centralized trade clearance and settlement system that linked the agents, PSI, and virtually all mutual fund companies. To place trades that were transmitted through NSCC, the agents were required to identify their FA number and a customer account to mutual funds on trade tickets. PSI appended additional information to the agents' orders and transmitted the transactions through NSCC to the mutual fund companies.

8. Some mutual funds screened for excessive short-term trading by reviewing FA and customer account numbers that the

agents transmitted to them via NSCC. Some also monitored for excessive short-term trading by trade size and principal amount and by the branch code attached to a trade. Typically, if a fund concluded that a shareholder had violated its exchange limitations, the fund would attempt to prevent, or “block” additional trades in a fund or fund family by that shareholder. If a fund determined that a particular PSI agent or shareholder had violated its exchange limitations, the fund would send a “block letter” to PSI. Block letters varied but generally notified PSI of the mutual fund’s intention to block the agent or customer’s transaction and often asked PSI to take steps to preclude a particular agent or customer account from engaging in additional trades in a particular fund or fund family.

9. Because these mutual funds monitored for excessive trading by FA number and/or customer account number, the agents altered their use of these numbers to defraud these funds and the funds’ long-term shareholders. By altering their use of these numbers, the agents tricked mutual fund companies into accepting trades that the funds otherwise would have rejected.

The Agents’ Deceptive Conduct

10. During the Relevant Period, the agents engaged in a fraudulent scheme to circumvent blocks imposed by mutual funds on their trading privileges. The agents’ scheme worked as follows. The agents’ customers, typically hedge funds, asked the agents to purchase and sell mutual funds on a short-term basis on their behalf. The agents, however, knew that mutual funds tracked their

trades by FA number and customer account number, and they knew that if they placed short-term mutual fund trades for their customers using a single FA or account number, the mutual funds would likely determine the number of trades was excessive and would block any further trades by them.

11. The agents, therefore, devised a scheme to conduct their customers' trading using dozens of customer accounts, often established under fictitious names, and multiple FA numbers to make it difficult for mutual funds to identify their customers' market timing. When the mutual funds succeeded in blocking certain FA numbers or customer accounts from further trading, the agents then used other FA numbers and customer accounts that had not yet been blocked to evade the funds' restrictions and continue to trade.

The Boston Agents

12. For example, one group of PSI agents based in its Boston, Massachusetts branch office (the "Boston Agents") repeatedly used these deceptive practices to defraud mutual funds throughout the Relevant Period. The Boston Agents consisted of a group of three PSI agents and several assistants. The group had five customers for whom it placed market timing trades, each of whom acted on behalf of one or more hedge funds. During the Relevant Period, PSI received approximately $8 million from the Boston Agents' market timing activities, of which group members received approximately $4.6 million. As a result of this business, the head of the group quickly rose to become one of PSI's top producers.

13. Many of the mutual funds in which the Boston Agents traded screened for market timing trades by FA and customer account numbers. Many fund companies sent notices to PSI that complained that the group's trades had violated prospectus limitations. Some mutual funds announced steps they had taken to preclude the Boston Agents from further trading while others asked that PSI take steps to block further trades by the group in the fund.

14. During the Relevant Period, the Boston Agents used at least thirteen FA numbers and hundreds of customer accounts (for what were, in reality, only five customers) to circumvent these blocks and preclude new blocks. The Boston Agents' use of these devices in connection with market timing allowed group members to continue to place trades in funds that had taken steps to preclude them from further trading. This scheme created the impression that transactions originated from many agents and represented many different customers. In fact, what appeared to the mutual funds to be thousands of separate transactions submitted by many agents for many unrelated customers was actually a systematic pattern of market timing by group members on behalf of their five hedge fund customers.

The Garden City Agent

15. Another PSI agent based in its Liberty Plaza and Garden City, New York branch offices (the "Garden City Agent")

used these same deceptive practices to defraud mutual funds throughout the Relevant Period. The Garden City Agent headed a team of agents and assistants, although he very rarely reported to work at any PSI location. He had five customers for whom he placed market timing trades, each of whom acted on behalf of one or more hedge funds. During the Relevant Period, PSI received approximately $9.8 million from the Garden City Agent's market timing activities (of which the Garden City Agent received approximately $4.7 million). The Garden City Agent was the top producing agent at PSI throughout the Relevant Period.

16. Like the Boston Agents, the Garden City Agent traded in mutual funds that screened for market timing by FA and customer account number. During the Relevant Period, approximately fifty mutual funds complained to PSI about the Garden City Agent's trading activity. Many mutual funds specifically identified to PSI his use of deceptive trading strategies to evade blocks the fund companies had imposed.

17. To evade these blocks, the Garden City Agent maintained 49 different FA numbers and hundreds of customer account numbers (for what were, in reality, only five customers). His use of these devices to market time created the impression that the trades originated from many agents and many customers. By shifting trades from one FA number to another, or from one customer account to another, the Garden City Agent concealed his identity and was able to place trades in mutual funds where PSI previously had blocked his trading under his other FA numbers and accounts.

The Special Accounts Agents

18. Another group of PSI agents based in a New York office known within PSI as “Special Accounts” (the “Special Accounts Agents”) also used deceptive practices to defraud mutual funds throughout the Relevant Period. The Special Accounts Agents consisted of a group of two PSI agents and several assistants. The group had three customers for which it placed market timing trades. During the Relevant Period, PSI received approximately \$6.5 million from the Special Accounts Agents’ market timing activities, of which group members received approximately \$2.5 million. As a result of this business, the heads of the group quickly achieved membership in PSI’s Chairman’s Club, a select group consisting of the largest producing agents within the firm.

19. Like the Boston Agents and the Garden City Agent, the Special Accounts Agents knew that most mutual funds identified excessive trading by FA and customer account number. They also understood that mutual funds screened for market timing by reviewing only those trades at or exceeding certain dollar amounts. The Special Accounts Agents used at least 20 FA numbers and hundreds of customer accounts (for what were, in reality, only three customers) to avoid detection by mutual funds. The Special Accounts Agents also used “under the radar” trading to disguise their customers’ trading in funds that previously had taken steps to stop them. The agents’ use of these devices in

connection with market timing deceived mutual funds into accepting trades they otherwise would have rejected. Like the Boston Agents and the Garden City Agent, their scheme perpetuated the impression that transactions originated from many agents and represented many different customers.

PSI Failed to Prevent the Agents From Obtaining Multiple Identification and Customer Account Numbers

20. PSI failed to prevent the agents from obtaining several different forms of identifying numbers. Consequently, the agents used these numbers to perpetrate their scheme to defraud. When agents began their employment with PSI, PSI assigned them an FA number. The agents used FA numbers to open customer accounts, execute trades, and track their commissions. When agents worked as a team to service common customers, PSI provided "Joint" numbers. Joint numbers ostensibly represented a commission split between two or more agents. Here, the agents acquired and used Joint numbers for improper purposes. The numbers were not used to split commissions, but rather to facilitate the agents' ability to trade after their other agent identifying numbers had been blocked from trading. PSI also provided the agents with "Also" numbers. The purported purpose of "Also" numbers was to allow the agents' customers to access only those portions of a given agent's portfolio that belonged to that customer or to provide certain customers with commission discounts. The agents, however, used Also numbers improperly in the same manner as they used FA and Joint Numbers – to circumvent blocks that had been imposed on

their other FA numbers. Indeed, at least one mutual fund became so frustrated by its inability to identify the agents that it threatened to curtail the trading privileges of all agents within a PSI branch to remedy the conduct.

21. Each of the agents maintained numerous FA, Joint, and Also numbers, and used these numbers interchangeably to execute trades for their customers. For example, the Boston Agents used 13 identifying numbers to place market timing trades and the Garden City Agent used 49 identifying numbers. When one of the agent's FA, Joint, or Also numbers was blocked from trading by a particular mutual fund, he used another number assigned to him to place the trade in that fund. Although each joint number ostensibly represented a unique commission split, in fact each team of agents split commissions from mutual fund purchases according to a single ratio, irrespective of which agent identifying number was used to enter the trade.

22. PSI failed to prevent the agents from opening hundreds of customer account numbers. The agents' customers maintained multiple accounts with PSI, many of which bore fictitious names that had no relation to the actual customer's name. The agents used these customer accounts interchangeably to execute trades. When one customer account was blocked from trading by a particular mutual fund, the agents substituted another account for that same customer to place the trade for that customer, thereby creating the appearance that the trade originated from another customer.

23. PSI failed to prevent the agents from obtaining accounts for their customers that were coded as "Confidential." Confidential accounts did not identify the beneficial owner of the account on the transaction data provided to the mutual funds. Although such a designation could have a legitimate purpose, here the agents used Confidential accounts improperly to impede the mutual funds' ability to identify which PSI agent or customer was market timing their funds.

24. PSI also failed to prevent the agents from obtaining customer account numbers with multiple branch identifiers. Typically, agents located in one PSI branch office had customer accounts that had a prefix used to identify the branch location. Here, the agents established accounts for their hedge fund customers using multiple branch codes, which effectively impeded the mutual funds' ability to identify the particular PSI office location, as well as agent, that was market timing their funds. The agents used branch identifiers improperly as another mechanism to conceal their identities and the identities of their customers to mutual funds.

PSI Received Notifications of the Agents' Deceptions

25. During the Relevant Period, mutual fund companies sent more than a thousand letters and emails to PSI concerning market timing by the agents. Many of these communications asked PSI to take steps to stop further trading by a particular customer account or FA number. Others expressly notified PSI that the agents used deceptive trading practices to continue placing market timing trades.

26. High level officers of PSI were aware during the Relevant Period that mutual funds were accusing the agents of using deceptive practices to evade the mutual funds' attempts to block the agents' market timing trades. For example, an individual who joined PSI in 1997 and rose to become the chief administrator of PSI's Private Client Group ("PCG") in January 1999, then to become executive director of PCG in November 2000, and finally to president of PCG in December 2002 ("the Senior Officer") received repeated notices of wrongdoing by the agents throughout the Relevant Period, but did not take adequate steps to stop the agents' fraud. Among other things, the Senior Officer received the following indications that the agents were committing fraud. In some cases, certain other senior managers or high level officers of PSI also received notices that the agents were committing fraud.

27. On November 21, 1999, a senior executive in the PSI Mutual Fund Operations division forwarded to the Senior Officer a string of emails concerning a complaint from a mutual fund complex that the Garden City Agent had evaded a block on two of his accounts by simply opening new accounts. Among other things, the email stated:

It appears that [the Garden City Agent] circumvented this restriction by requesting new BIN [account] #s and fund accounts be established, funded by transferring shares into

> these new accounts on 11/8/99. Subsequently on 11/10/99, an exchange out of the money fund into our stock funds was processed, beginning market timing again.

The cover email commented, "[T]his seems to be a serious matter that will only get worse."

28. On January 19, 2000, the manager of PSI's Mutual Fund Operations division forwarded to the Senior Officer an email from another mutual fund complex complaining that a member of the Boston Agents had evaded a trading restriction by opening a new account, stating:

> It appears that [the member] set up another account in December for the same client we restricted on 11/22.

29. On March 30, 2001, the head of PCG risk management sent to the Senior Officer an email that attached a letter from another mutual fund complex complaining that "excessive trading activity" by PSI agents in its mutual funds "has become detrimental to both the funds and shareholders of the funds involved." The letter described the tactics used by PSI agents to avoid having their trades canceled as follows:

> Since trade cancellation began on February 26th, 2001, we have noticed several types of reactions by Prudential Financial Advisors in order to circumvent our attempts to terminate excessive trading. Originally, your Financial Advisors established new identification numbers so that they would not be recognized as a repeat offender. Secondly, Financial Advisors would transfer a fund(s)

position from account to account, in order to disguise their identity. Lastly, your Financial Advisors have attempted to reduce the dollar amount of the exchange orders while simultaneously increasing the number of exchanges (in the same fund and account) in the hopes of not being identified.

30. On June 28, 2001, the Senior Officer received an email from the manager of the Special Accounts branch warning him that the Special Accounts Agents were obtaining multiple FA numbers in order to conduct their market timing, stating that:

> We will have an issue soon with joint FA numbers: in order to get around the MF [mutual fund] timing issue they are starting to request 99/01 split numbers with their junior partners to help them get around being shut down by some MF companies on timing.

31. On April 4, 2002, the manager of PSI's Mutual Funds Operations division sent an email to other senior managers forwarding an email from another mutual fund complex complaining that certain PSI agents were using multiple accounts and FA numbers to evade restrictions on their market timing. The email stated:

> What we have seen scares us. It appears certain representatives are changing account registrations, tax id numbers, and branch and rep numbers in an effort to time the [mutual fund complex's] funds. All of these accounts have been stopped, but each day "new" ones pop up.

When the PSI chief compliance officer saw the above email, he showed it to the Senior Officer. The head of PCG risk management also discussed the email with the Senior Officer.

32. On April 29, 2002, the Senior Officer met with an internal PSI working group that had been analyzing market timing issues. The group described for the Senior Officer the mutual fund companies' restrictions on excessive trading, the fund companies' block letters to PSI, and the deceptive trading strategies used by certain PSI agents, including multiple accounts and FA numbers.

33. On at least two occasions in May 2002, an employee of PSI's risk management division detailed for the Senior Officer several deceptive practices used by the Garden City Agent. The employee's analysis noted that in one 37-day period, the Garden City Agent had 19 different mutual fund companies request that accounts under the agent's control, or the agent as an FA, be blocked from their funds. The analysis concluded that the Garden City Agent had circumvented these requests by changing his FA number to an Also or Joint Number to avoid detection by the fund, or by changing customer account numbers and moving the assets from the blocked account to a newly established account.

34. On February 5, 2003, the director of strategic planning at PCG sent the Senior Officer (then the President and most senior officer of PCG) a string of emails from another mutual fund complex complaining that certain PSI agents were

using multiple customer accounts and FA numbers for market timing. One of the emails stated:

> I have spoken to these reps a few times over the past several months about stopping their timing activity to no avail. Over the past several months, we have placed stops on 325 of their accounts as of 11/30/02 and continue to add accounts daily. We see new accounts/rep id combinations being opened and have determined that we are not able to continue chasing them within our funds. We feel our only course of action to protect our fund shareholders is to prohibit the attached list of reps from doing business with [our funds].

Another email in the string stated:

> These reps have multiple rep ids and have continued to add new ones as we block the ids within the NSCC trading system for our fund complex… These reps created close to $3 billion in exchanges last year with $75 million of assets during a time in which we placed stops on 350 of their accounts.

The director of strategic planning added his own warning to the Senior Officer:

> I just wanted to give you a heads up on an issue that is sure to reach your desk in the next day or two. As you can see from the attached string of notes, the senior leadership team at [a mutual fund complex] are completely frustrated with some of the tactics/strategies of FA's [the

> Garden City Agent and the Boston Agents]. Previous attempts to curtail timing activity in the [mutual fund complex's] funds by blocking account activity have been thwarted by the establishment of additional FA numbers. It appears that [the mutual fund complex] is now making overtures that continued activity of this nature will threaten the relationship between Prudential and the fund company.

35. On February 11, 2003, a PCG risk officer sent an email to the Senior Officer (then the President and most senior officer of PCG) that forwarded an email from the Garden City branch manager about the Garden City Agent's market timing business. The branch manager questioned the effectiveness of the Mutual Fund Operations division's internal blocking system and raised several other concerns about the Garden City Agent's activities:

> Blocking of individual accounts by fund companies is extremely shortsighted in consideration of the fact that each "entity" maintains multiple accounts with our Firm. There have been repeat offenses, at least in spirit… Fund companies have been mislead as to the identity of the FA's of record… Recently, [a mutual find company] was provided with information which was at best misleading to effect the removal [of] a block.
>
> [T]here is frequent journaling of funds between accounts. At the present time, [the Garden City Agent and an assistant] either have or have had a total of 48 FA #'s including single, joint and also numbers.

PSI's Procedures to Limit Market Timing Were Ineffective

36. Although PSI senior officers issued policies and procedures ostensibly designed to proscribe the agents' conduct, these policies and procedures were ineffective in scope and were never fully enforced. Moreover, even in situations where these policies and procedures purportedly were enforced, PSI senior officers undermined them by granting exceptions for its largest producing agents. As a result, the agents' deceptions continued even after these policies and procedures were promulgated.

PSI's June 2002 Procedure Concerning Issuance of FA Numbers

37. In June 2002, PSI instituted a procedure concerning the issuance of FA numbers, in a purported effort to hinder the agents' ability to obtain "Joint" numbers and "Also" numbers to evade limitations on market timing (the "June 2002 Procedure"). The June 2002 Procedure provided, simply, that requests for "Joint" and "Also" numbers would require a documented business request and a PSI Regional Business Manager's approval. The June 2002 Procedure failed to preclude the agents from misusing previously issued Joint and Also numbers to evade blocks imposed by mutual fund companies. Indeed, the Garden City Agent obtained 12 new Joint and Also numbers just days before the procedure took effect, purportedly to assist him in transferring customer accounts from one PSI branch office to another. The June 2002 Procedure also did not subject the agents to any form of discipline or sanction if they continued to use Joint and Also numbers to evade blocks in violation of its terms.

PSI's January 2003 Market Timing Policy

38. After protracted discussion involving PSI senior officers and attorneys during the Fall of 2002, PSI issued a market timing policy on January 8, 2003 (the "Market Timing Policy"). PSI considered, and rejected, defining market timing in the Market Timing Policy as a certain number of trades because of concerns that doing so would have had too great an impact on the agents' revenues. PSI also rejected an absolute prohibition on the business of market timing. Instead, the Market Timing Policy provided that "inappropriate timing activities [would] continue to be monitored" by mutual fund companies and not by PSI itself.

39. Unlike other PSI policies concerning market timing, the Market Timing Policy expressly provided for the imposition of sanctions, including termination of employment, for the agents' use of "manipulative techniques" to evade mutual fund trading restrictions. Any imposition of sanctions was to be decided by a committee consisting of members of PSI's Legal, Compliance, and Risk Management divisions. Despite notifications of continuing deceptive practices received by PSI after it issued the Market Timing policy, PSI did not form this committee and failed to take action against any of the agents to stop their use of "manipulative techniques" to market time.

40. The Market Timing Policy also provided that, in the event a mutual fund company asked PSI to block any one of a agent's FA numbers, all numbers belonging to the agent similarly would be blocked from trading. However, PSI senior officers

determined not to implement this critical aspect of the Market Timing Policy. In fact, despite the policy's clear language, PSI interpreted mutual fund block requests after it issued the Market Timing Policy in the same manner as it had previously – as narrowly as possible, blocking only the specific FA number or customer account number identified by mutual fund block requests. Thus, even after issuance of the Market Timing Policy, the agents were able to continue their fraudulent scheme of switching to unblocked FA numbers or customer accounts to evade blocks imposed by mutual fund companies.

PSI Profited From the Agents' Deceptive Acts

41. PSI identified the agents as early as 2000 and monitored their revenues and ranks within PSI throughout the Relevant Period. PSI's Mutual Funds Operations division, which processed the agents' trades in mutual funds, monitored the agents' activity because their rapid trading required the dedication of additional staff within the department to process the trades and strained PSI's trade processing and settlement systems.

42. In 2000, PSI began to track each quarter the gross commission revenues generated by the agents. PSI prepared these reports to determine the amount of income that would possibly be reduced if PSI determined to eliminate market timing as a business. In 2001, for example, the agents generated more than $16 million in gross commission revenues for PSI, most of which would have been eliminated had PSI phased out market timing at

that time. Similarly, the agents generated approximately $23 million in gross commission revenues for 2002, and received another $10 million in gross commission revenues during the first half of 2003.

43. As PSI senior officers became increasingly aware of the agents' use of deceptions, PSI elected to continue the business of market timing. Indeed, some of PSI's senior officers were aware that the June 2002 Procedure concerning the issuance of multiple FA numbers and the January 2003 Market Timing Policy were wholly ineffective at eradicating the agents' deceptions and the agents and their hedge fund customers continued this activity. During the Relevant Period, the agents generated approximately $50 million in gross revenues as a result of this conduct.

CONCLUSION OF LAW

Solely for the purpose of this consent order and without admitting or denying the findings of fact, PSI consents to the following:

1. PSI failed to reasonably supervise its agents in violation of its duty under N.J.S.A. 49:3-58(a)(2)(xi) to establish or enforce reasonable supervisory procedures for detecting and preventing the deceptive market timing practices described herein;

ORDER

THEREFORE, it is, on this, 28 day of August, 2006, hereby ORDERED that:

1. PSI shall disgorge $270 million, payable to the United States Securities and Exchange Commission or as it otherwise directs as part of a joint administrative settlement.
2. PSI shall CEASE AND DESIST from violating the Uniform Securities Law (1997), L. 1997, c.276, N.J.S.A. 49:3-47 *et seq*.
3. PSI retain an Independent Distribution Consultant subject to the following provisions:
    a. Respondent shall retain, within 60 days of the entry of this consent order, the services of an independent distribution consultant ("Independent Distribution Consultant") acceptable to the staff of Bureau.
    b. Respondent shall be responsible for all costs and expenses associated with the development and implementation of the Distribution Plan, including such costs as further detailed in the SEC Final Order.
    c. Respondent shall cooperate fully with the Independent Distribution Consultant to provide all information requested for its review, including providing access to its files, books, records, and personnel.
    d. The Independent Distribution Consultant shall develop a proposed Distribution Plan for the Distribution of

the total disgorgement ordered in the SEC Final Order and this consent order, and any interest or earnings thereon, according to a methodology developed in consultation with and acceptable to the staff of the Commission and the Bureau.

e. The Independent Distribution Consultant shall simultaneously submit to Respondent and the Bureau the proposed Distribution Plan no more than 180 days after the entry of this consent order.

f. The proposed Distribution Plan developed by the Independent Distribution Consultant shall be binding unless, within 210 days after the date of entry of this order, Respondent, the staff of the SEC or the Bureau advises, in writing, the Independent Distribution Consultant of any determination or calculation from the Distribution Plan that it considers to be inappropriate and states in writing the reasons for considering such determination or calculation inappropriate.

g. With respect to any calculation with which Respondent or the staff of Bureau do not agree, such parties shall attempt in good faith to reach an agreement within 240 days of the entry of this consent order. In the event the Respondent and the Bureau staff are unable to agree on an alternative determination or calculation, the determinations of the Independent Distribution Consultant shall be included in the proposed Distribution Plan.

h. Within 285 days of the entry of this consent order, the Independent Distribution Consultant shall submit the proposed Distribution Plan for the administration and distribution of disgorgement funds to the staff of the Commission and to the Bureau. The Independent Distribution Consultant shall take all necessary and appropriate steps to administer the final plan for distribution of disgorgement funds in accordance with the terms of the approved Distribution Plan.

i. For the period of the engagement and for a period of two years from completion of the engagement, the Independent Distribution Consultant 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. Any firm with which the Independent Distribution Consultant is affiliated in performance of his or her duties under this consent order, or of which he/she is a member, and any person engaged to assist the Independent Distribution Consultant in the performance of his/her duties under this consent order, shall not, without prior written consent of the Bureau, enter into any employment, consultant, attorney-client, auditing or other professional relationship with Respondent, or any of Respondent's present of former affiliates, directors, officers, employees, or acting in the capacity as such for the period of the engagement and for a period of two years after the engagement.

j. For good cause shown, the Bureau may alter any of the procedural deadlines set forth above.

4. PSI shall cooperate fully and in good faith with the Bureau in any investigation or litigation by the Bureau relating to the allegations in this consent order. Such cooperation will include, but is not limited to, voluntarily making employees available for interviews and/or testimony, producing business and other records within its possession, custody, and/or control in a timely manner as requested by the Bureau, and providing other non-privileged information obtained by PSI in connection with its own investigation. PSI will bear the cost of producing documents, information, and/or witnesses requested by either the Attorney General or the New Jersey Bureau of Securities.

5. This consent order, the SEC Final Order, the NASD Administrative Waiver & Consent, the Stipulation and Consent issued by the New York Stock Exchange and the order of any other State in related proceedings against PSI shall not be a ground to deny, suspend or revoke the broker-dealer, agent, investment adviser or investment adviser

representative registration of any Covered Person pursuant to N.J.S.A. 49:3-58, shall not be a ground of denial or revocation of the transactional or securities exemptions from registration in N.J.S.A. 49:3-50, and shall not be a ground to issue a stop order denying effectiveness to, or suspending or revoking the effectiveness of, any securities registration statement pursuant to N.J.S.A. 49:3-64.

THE PARTIES CONSENT TO THE FORM, CONTENT, AND ENTRY OF THIS CONSENT ORDER ON THE DATES UNDER THEIR RESPECTIVE SIGNATURES.

FOR THE BUREAU OF SECURITIES:

By: /s/ Franklin L. Widmann
Franklin L. Widmann
Chief, Bureau of Securities

Dated this 28 day of August, 2006.

FOR PRUDENTIAL EQUITY GROUP, LLC:

By: /s/ Kenneth Y. Tanji
Kenneth Tanji
Senior Vice President

Dated this 23 day of August, 2006.

ATTORNEY GENERAL OF THE STATE OF NEW YORK
BUREAU OF INVESTMENT PROTECTION

--X

In the Matter of

PRUDENTIAL EQUITY GROUP, LLC,
Formerly Known As
PRUDENTIAL SECURITIES INCORPORATED

--X

ASSURANCE OF DISCONTINUANCE
PURSUANT TO EXECUTIVE LAW § 63 (15)

WHEREAS, pursuant to the provisions of Article 23-A of the General Business Law (the "Martin Act"), Eliot Spitzer, Attorney General of the State of New York (the "Attorney General"), commenced an investigation in September 2003 into the practices, procedures and conduct of Prudential Securities Incorporated ("PSI"), during the period 1998 through September 2003 respecting market timing and late trading of mutual funds (the "Investigation");[1]

WHEREAS, the Investigation was conducted in cooperation with investigations of PSI by the U.S. Securities and Exchange Commission ("SEC"), the Commonwealth of Massachusetts, the State of New Jersey, the New York Stock Exchange and NASD Inc.;

WHEREAS, prior to July 1, 2003, PSI was an indirect wholly owned broker-dealer subsidiary of Prudential Financial, Incorporated ("Prudential Financial");

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1 "Market timing" refers to the practice of short-term investing in mutual fund shares and/or the exploitation of pricing inefficiencies in mutual fund share pricing. "Late trading" refers to obtaining a given day's mutual fund share price for orders to buy, sell or exchange shares that were placed after the close of the market on that day.

WHEREAS, on July 1, 2003, PSI transferred the assets relating to its U.S. retail securities brokerage operations to a newly formed holding company, now named Wachovia Securities Financial Holdings, LLC ("WFSH");

WHEREAS, Prudential Financial currently owns 38 percent of WSFH and Wachovia Corporation owns 62 percent of WSFH;

WHEREAS, since July 1, 2003, PSI's former U.S. retail securities brokerage business has operated as part of Wachovia Securities, LLC;

WHEREAS, in the course of the Investigation, numerous witnesses were interviewed and/or deposed and extensive documentary evidence was reviewed;

WHEREAS, Prudential Equity Group, LLC ("PEG") has cooperated in the Investigation by producing documentary evidence and witnesses and identifying evidence relevant to the Investigation;

WHEREAS, the Investigation revealed that certain practices by PSI violated the Martin Act, General Business Law ("GBL") §349, and Executive Law §63 (12);

WHEREAS, PEG has advised the Attorney General of its desire to resolve the Investigation;

WHEREAS, PEG agrees to implement certain changes with respect to securities practices and to make the payment of $270 million as set forth herein;

WHEREAS, PEG has entered into an Agreement with the Office of the United States Attorney for the District of Massachusetts relating to potential criminal charges for violations of the federal Securities Exchange Act of 1934, and PEG has agreed to pay a penalty of $330 million; and

WHEREAS, the Attorney General finds the following sanctions appropriate and in the public interest and PEG agrees to the sanctions provided herein;

NOW, THEREFORE, the Attorney General, based upon the Investigation, makes the following findings:

FINDINGS

1. At all relevant times until on or about July 1, 2003, PSI was a Delaware corporation with its headquarters in New York, New York, was registered with the Department of Law of the State of New York as a securities broker-dealer, and conducted business in and from the State of New York.

2. The Attorney General has jurisdiction over this matter pursuant to the Martin Act, GBL § 349, and Executive Law§ 63 (12).

A. Summary of the Fraud

3. This matter concerns a fraudulent market timing scheme perpetrated by PSI registered representatives (collectively, the “Representatives”) whose business involved market timing to defraud at least 50 mutual funds and their long-term shareholders. Beginning in at least September 1999 and continuing through at least June 2003 (the “Relevant Period”), the Representatives used deceptive trading practices to conceal their identities, and those of their customers, to evade mutual funds’ prospectus limitations on market timing. These practices included the use of multiple broker identifying numbers (known as Financial Advisor, or “FA,” numbers) and multiple customer accounts; the use of accounts coded as confidential in PSI’s systems; and the Representatives’ use of “under-the-radar” trading to avoid notice by mutual

funds. Typically, mutual funds screened for market timing trades only above a designated dollar amount. The practice of “under-the-radar” trading refers to the Representatives’ splitting of one trade into numerous smaller ones to avoid detection by mutual funds.

4. As early as the fourth quarter 1999, several mutual fund companies identified the Representatives’ use of deceptive trading practices and notified PSI of the Representatives’ conduct. In May 2002, PSI itself determined that its top-producing registered representative used deceptive trading practices to avoid notice by mutual funds. Throughout the Relevant Period, PSI received hundreds of notices from mutual fund companies that identified the Representatives’ conduct and asked the firm to take steps to curtail their deceptive market timing practices.

5. Despite PSI’s increasing awareness of the Representatives’ fraudulent market timing practices, the firm elected to continue the business of market timing. Rather than discipline or sanction any of the Representatives or even curtail their ability to open additional accounts for their market timing customers, PSI failed to prevent their conduct from continuing and actually began to track the Representatives’ gross revenues. In 2001, for example, the Representatives generated more than $16 million in gross commission revenues for the firm, most of which was in danger of being eliminated had the firm phased out market timing at that time. Similarly, the Representatives generated approximately $23 million in gross commission revenues in 2002, and continued to generate comparable revenues throughout the Relevant Period.

6. PSI’s policies and procedures were ineffective in curtailing the Representatives’ fraud and were largely not enforced. Even in situations where PSI purportedly enforced any of these policies, PSI senior officers undermined them by granting exceptions for PSI’s largest

producing registered representatives. Additionally, PSI repeatedly failed to deprive the Representatives of their inappropriate use of hundreds of FA numbers, even though the use of multiple FA numbers was the primary means by which the Representatives carried out their fraud. PSI finally issued a market timing policy in January 2003, but the firm did not fully enforce procedures in that policy to curtail the Representatives' scheme. As a result of the conduct described above, PSI violated the Martin Act and Executive Law § 63(12).

B. Background on Market Timing

7. Market timing includes frequent buying and selling of shares of the same mutual fund or buying or selling of mutual fund shares in order to exploit inefficiencies in mutual fund pricing. Market timing can harm mutual fund shareholders because it can dilute the value of their shares, if the market timer is exploiting pricing inefficiencies, or disrupt the management of the mutual fund's investment portfolio and can cause the targeted mutual fund to incur costs borne by other shareholders to accommodate frequent buying and selling of shares by the market timer.

8. Beginning in the late 1990s, many mutual funds determined that market timing harmed their long-term shareholders. As a result, they began to monitor market timing in their funds' shares and imposed restrictions on excessive trading. Such restrictions limited the number of trades that an account holder could place in a fund's shares and often were set forth in the funds' prospectuses. Many funds monitored trading activity to detect any violations of these prospectus limitations.

9. Most mutual funds received trade instructions from PSI through the National Securities Clearing Corporation ("NSCC"). NSCC is a centralized trade clearance and settlement system that linked the Representatives, PSI, and virtually all mutual fund companies.

To place trades that were transmitted through NSCC, the Representatives were required to identify their FA number and a customer account to mutual funds on trade tickets. PSI appended additional information to the Representatives' orders and transmitted the transactions through NSCC to the mutual fund companies.

10. Some mutual funds screened for excessive short-term trading by reviewing FA and customer account numbers that the Representatives transmitted to them via NSCC. Some also monitored for excessive short-term trading by trade size and principal amount and by the branch code attached to a trade.[2] Typically, if a fund concluded that a shareholder had violated its exchange limitations, the fund would attempt to prevent, or "block" additional trades in a fund or fund family by that shareholder. If a fund determined that a particular PSI registered representative or shareholder had violated its exchange limitations, the fund would send a "block letter" to PSI. Block letters varied but generally notified PSI of the mutual fund's intention to block the registered representative's or customer's transaction and often asked PSI to take steps to preclude a particular registered representative or customer account from engaging in additional trades in a particular fund or fund family.

11. Because these mutual funds monitored for excessive trading by FA number and/or customer account number, the Representatives altered their use of these numbers to defraud these funds and the funds' long-term shareholders. By altering their use of these numbers, the Representatives tricked mutual fund companies into accepting trades that the funds otherwise would have rejected.

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[2] PSI assigned branch codes to each of its retail branch offices. Branch codes identified to mutual funds the PSI branch office from which a particular market timing trade originated.

C. The Representatives' Deceptive Conduct

12. During the Relevant Period, the Representatives engaged in a fraudulent scheme to circumvent blocks imposed by mutual funds on their trading privileges. The Representatives' scheme worked as follows. The Representatives' customers, typically hedge funds, asked the Representatives to purchase and sell mutual funds on a short-term basis on their behalf. The Representatives, however, knew that mutual funds tracked their trades by FA number and customer account number, and they knew that if they placed short-term mutual fund trades for their customers using a single FA or account number, the mutual funds would likely determine the number of trades was excessive and would block any further trades by them.

13. The Representatives, therefore, devised a scheme to conduct their customers' trading using dozens of customer accounts, often established under fictitious names, and multiple FA numbers to make it difficult for mutual funds to identify their customers' market timing. When the mutual funds succeeded in blocking certain FA numbers or customer accounts from further trading, the Representatives then used other FA numbers and customer accounts that had not yet been blocked to evade the funds' restrictions and continue to trade.

a. Representatives Martin Druffner, Justin Ficken, and Skifter Ajro

14. For example, one group of PSI registered representatives based in its Boston, Massachusetts, branch office repeatedly used these deceptive practices to defraud mutual funds throughout the Relevant Period. The group consisted of PSI registered representatives Martin Druffner, Justin Ficken, Skifter Ajro and several assistants (the "Druffner Group"). The Druffner Group had five customers for whom it placed market timing trades, each of whom acted on behalf of one or more hedge funds. During the Relevant Period, PSI received approximately $8 million from the Druffner Group's market timing activities, of which group members received approximately $4.6 million. As a result of this business, the head of the group, Martin Druffner, quickly rose to become one of PSI's top producers.

15. Many of the mutual funds in which the Druffner Group traded screened for market timing trades by FA and customer account numbers. Many fund companies sent notices to PSI that complained that the group's trades had violated prospectus limitations. Some mutual funds announced steps they had taken to preclude the Druffner Group from further trading while others asked that PSI take steps to block further trades by the group in the fund.

16. During the Relevant Period, the Druffner Group used at least thirteen FA numbers and hundreds of customer accounts (for what were, in reality, only five customers) to circumvent these blocks and preclude new blocks. The Druffner Group's use of these devices in connection with market timing allowed group members to continue to place trades in funds that had taken steps to preclude them from further trading. Their scheme created the impression that transactions originated from many registered representatives and represented many different customers. In fact, what appeared to the mutual funds to be thousands of separate transactions submitted by many registered representatives for many unrelated customers was actually a systematic pattern of market timing by group members on behalf of their five hedge fund customers.

b. Representative Frederick O'Meally

17. Another PSI registered representative based in its Liberty Plaza, New York, New York, and its Garden City, New York, branch offices, Frederick O'Meally, used these same deceptive practices to defraud mutual funds throughout the Relevant Period. O'Meally headed a team of registered representatives and assistants, although he very rarely reported to work at any PSI location. He had five customers for whom he placed market timing trades, each of whom

acted on behalf of one or more hedge funds. During the Relevant Period, PSI received approximately $9.8 million from O'Meally's market timing activities (of which O'Meally received approximately $4.7 million). O'Meally was the top producing registered representative at PSI throughout the Relevant Period.

18. Like the Druffner Group, O'Meally traded in mutual funds that screened for market timing by FA and customer account numbers. During the Relevant Period, approximately 50 mutual funds complained to PSI about O'Meally's trading activity. Many mutual funds specifically identified to PSI his use of deceptive trading strategies to evade blocks the fund companies had imposed.

19. To evade these blocks, O'Meally maintained 49 different FA numbers and hundreds of customer account numbers (for what were, in reality, only five customers). His use of these devices to market time created the impression that the trades originated from many registered representatives and many customers. By shifting trades from one FA number to another, or from one customer account to another, O'Meally concealed his identity and was able to place trades in mutual funds where PSI previously had blocked his trading under his other FA numbers and accounts.

c. Representatives Jason Ginder and Lawrence Kalish

20. Another group of PSI registered representatives based in a New York office known within the firm as "Special Accounts" also used deceptive practices to defraud mutual funds throughout the Relevant Period. The group consisted of Jason Ginder, Lawrence Kalish and several assistants (the "Ginder/Kalish Group"). The Ginder/Kalish Group had three customers for which it placed market timing trades. During the Relevant Period, PSI received gross revenue of approximately $6.5 million from the Ginder/Kalish Group's market timing

activities, of which group members received approximately $2.5 million. As a result of this business, the heads of the group quickly achieved membership in PSI's Chairman's Club, a select group consisting of only the largest producing registered representatives within the firm.

21. Like the Druffner Group and O'Meally, the Ginder/Kalish Group knew that most mutual funds identified excessive trading by FA and customer account numbers. They also understood that mutual funds screened for market timing by reviewing only those trades at or exceeding certain dollar amounts. The Ginder/Kalish Group used at least 20 FA numbers and hundreds of customer accounts (for what were, in reality, only three customers) to avoid detection by mutual funds. The Ginder/Kalish Group also used "under the radar" trading to disguise their customers' trading in funds that previously had taken steps to stop them. The registered representatives' use of these devices in connection with market timing deceived mutual funds into accepting trades they otherwise would have rejected. Like the Druffner Group and O'Meally, their scheme perpetuated the impression that transactions originated from many registered representatives and represented many different customers.

D. PSI Failed to Prevent the Representatives From Obtaining Multiple Broker Identifying and Customer Account Numbers

22. PSI failed to prevent the Representatives from obtaining several different forms of broker identifying numbers. Consequently, the Representatives used these numbers to perpetrate their scheme to defraud. When registered representatives began their employment with PSI, PSI assigned them an FA number. Registered representatives used FA numbers to open customer accounts, execute trades, and track their commissions. When registered representatives worked as a team to service common customers, PSI provided "Joint" numbers. Joint numbers ostensibly represented a commission split between two or more registered representatives. Here, the Representatives acquired and used Joint numbers for improper purposes. The numbers were

not used to split commissions, but rather to facilitate the Representatives' ability to trade after their other broker identifying numbers had been blocked from trading. PSI also provided the Representatives with "Also" numbers. The purported purpose of "Also" numbers was to allow the Representatives' customers to access only those portions of a given registered representative's portfolio that belonged to that customer or to provide certain customers with commission discounts. The Representatives, however, used Also numbers improperly in the same manner as they used FA and Joint numbers – to circumvent blocks that had been imposed on their other FA numbers. Indeed, at least one mutual fund became so frustrated by its inability to identify the Representatives that they threatened to curtail the trading privileges of all registered representatives within a PSI branch to remedy the conduct.

23. Each of the Representatives maintained numerous FA, Joint, and Also numbers, and used these numbers interchangeably to execute trades for their customers. For example, the Druffner Group used 13 broker identifying numbers to place market timing trades and O'Meally used 49 broker identifying numbers. When one of the Representatives' FA, Joint, or Also numbers was blocked from trading by a particular mutual fund, he used another number assigned to him to place the trade in that fund. Although each Joint number ostensibly represented a unique commission split, in fact each team of Representatives split commissions from mutual fund purchases according to a single ratio, irrespective of which broker identifying number was used to enter the trade.

24. PSI failed to prevent the Representatives from opening hundreds of customer accounts. The Representatives' customers maintained multiple accounts with PSI, many of which bore fictitious names that had no relation to the actual customer's name. The Representatives used these customer accounts interchangeably to execute trades. When one

customer account was blocked from trading by a particular mutual fund, the Representatives substituted another account for that same customer to place the trade for that customer, thereby creating the appearance that the trade originated from another customer.

25. PSI failed to prevent the Representatives from obtaining accounts for their customers that were coded as "Confidential." Confidential accounts did not identify the beneficial owner of the account on the transaction data provided to the mutual funds. Although such a designation could have a legitimate purpose, here the Representatives used confidential accounts improperly to impede the mutual funds' ability to identify which PSI registered representative or customer was market timing their funds.

26. PSI also failed to prevent the Representatives from obtaining customer account numbers with multiple branch identifiers. Typically, registered representatives located in one PSI branch office had customer accounts that had a prefix used to identify the branch location. Here, the Representatives established accounts for their hedge fund customers using multiple branch codes, which effectively impeded the mutual funds' ability to identify the particular PSI office location, as well as registered representative, that was market timing their funds. The Representatives used branch identifiers improperly as another mechanism to conceal their identities and the identities of their customers to mutual funds.

E. PSI Received Notifications of the Representatives' Deceptions

27. During the Relevant Period, mutual fund companies sent more than a thousand letters and e-mails to PSI concerning market timing by the Representatives. Many of these communications asked PSI to take steps to stop further trading by a particular customer account or FA number. Others expressly notified PSI that the Representatives used deceptive trading practices to continue placing market timing trades.

28. High level officers of PSI were aware during the Relevant Period that mutual funds were accusing the Representatives of using deceptive practices to evade the mutual funds' attempts to block the Representatives' market timing trades. For example, Michael Rice, who joined PSI in 1997 and rose to become the chief administrator of PSI's Private Client Group ("PCG") in January 1999, then to executive director of PCG in November 2000, and finally to president of PCG in December 2002, received repeated notices of wrongdoing by the Representatives throughout the Relevant Period, but did not take adequate steps to stop the Representatives' fraud. Among other things, Rice received the following indications that the Representatives were committing fraud. In some cases, certain other senior managers or high level officers of PSI also received notices that the Representatives were committing fraud.

29. On November 21, 1999, a senior executive in the PSI Mutual Fund Operations division forwarded to Rice a string of e-mails concerning a complaint from a mutual fund complex that O'Meally had evaded a block on two of his accounts by simply opening new accounts. Among other things, the e-mail stated:

> It appears that [O'Meally] circumvented this restriction by requesting new BIN [account] #s and fund accounts be established, funded by transferring shares into these new accounts on 11/8/99. Subsequently on 11/10/99, an exchange out of the money fund into our stock funds was processed, beginning market timing again.

The cover e-mail commented, "[T]his seems to be a serious matter that will only get worse."

30. On January 19, 2000, the manager of PSI's Mutual Fund Operations Division forwarded to Rice an e-mail from another mutual fund complex complaining that a member of Druffner Group had evaded a trading restriction by opening a new account, stating: "It appears that [the member] set up another account in December for the same client we restricted on 11/22."

31. On March 30, 2001, the head of PCG risk management sent Rice an e-mail that attached a letter from another mutual fund complex complaining that "excessive trading activity" by PSI registered representatives in its mutual funds "has become detrimental to both the funds and shareholders of the funds involved." The letter described the tactics used by PSI registered representatives to avoid having their trades canceled as follows:

> Since trade cancellation began on February 26th, 2001, we have noticed several types of reactions by Prudential Financial Advisors in order to circumvent our attempts to terminate excessive trading. Originally, your Financial Advisors established new identification numbers so that they would not be recognized as a repeat offender. Secondly, Financial Advisors would transfer a fund(s) position from account to account, in order to disguise their identity. Lastly, your Financial Advisors have attempted to reduce the dollar amount of the exchange orders while simultaneously increasing the number of exchanges (in the same fund and account) in the hopes of not being identified.

32. On June 28, 2001, Rice received an e-mail from the manager of the Special Accounts branch warning him that the Ginder/Kalish Group were obtaining multiple FA numbers in order to conduct their market timing, stating that:

> We will have an issue soon with joint FA numbers: in order to get around the MF [mutual fund] timing issue they are starting to request 99/01 split numbers with their junior partners to help them get around being shut down by some MF companies on timing.

33. On April 4, 2002, the manager of PSI's Mutual Funds Operations division sent an e-mail to other senior managers forwarding an e-mail from another mutual fund complex complaining that certain PSI registered representatives were using multiple accounts and FA numbers to evade restrictions on their market timing. The e-mail stated:

> What we have seen scares us. It appears certain representatives are changing account registrations, tax id numbers, and branch and rep numbers in an effort to time the [mutual fund complex's] funds. All of these accounts have been stopped, but each day "new" ones pop up.

When the PSI chief compliance officer saw the above e-mail, he showed it to Rice. The head of PCG risk management also discussed the e-mail with Rice.

34. On April 29, 2002, Rice met with an internal PSI working group that had been analyzing market timing issues. The group described for Rice the mutual fund companies' restrictions on excessive trading, the fund companies' block letters to PSI, and the deceptive trading strategies used by certain PSI registered representatives, including multiple accounts and FA numbers.

35. On at least two occasions in May 2002, an employee of PSI's risk management division detailed for Rice several deceptive practices used by O'Meally. The employee's analysis noted that in one 37-day period, O'Meally had 19 different mutual fund companies request that accounts under the registered representative's control, or the registered representative as an FA, be blocked from their funds. The analysis concluded that O'Meally had circumvented these requests by changing his FA number to an Also or Joint Number to avoid detection by the fund, or by changing customer account numbers and moving the assets from the blocked account to a newly established account.

36. On February 5, 2003, the director of strategic planning at PCG sent Rice (then the President and most senior officer of PCG) a string of e-mails from another mutual fund complex complaining that certain PSI registered representatives were using multiple customer accounts and FA numbers for market timing. One of the e-mails stated:

> I have spoken to these reps a few times over the past several months about stopping their timing activity to no avail. Over the past several months, we have placed stops on 325 of their accounts as of 11/30/02 and continue to add accounts daily. We see new accounts/rep id combinations being opened and have determined that we are not able to continue chasing them within our funds. We feel our only course of action to protect our fund shareholders is to prohibit the attached list of reps from doing business with [our funds].

Another e-mail in the string stated:

> These reps have multiple rep ids and have continued to add new ones as we block the ids within the NSCC trading system for our fund complex... These reps created close to $3 billion in exchanges last year with $75 million of assets during a time in which we placed stops on 350 of their accounts.

The director of strategic planning added his own warning to Rice:

> I just wanted to give you a heads up on an issue that is sure to reach your desk in the next day or two. As you can see from the attached string of notes, the senior leadership team at [a mutual fund complex] are completely frustrated with some of the tactics/strategies of FA's [O'Meally and the Druffner Group]. Previous attempts to curtail timing activity in the [mutual fund complex's] funds by blocking account activity have been thwarted by the establishment of additional FA numbers. It appears that [the mutual fund complex] is now making overtures that continued activity of this nature will threaten the relationship between Prudential and the fund company.

37. On February 11, 2003, a PCG risk officer sent an e-mail to Rice that forwarded an e-mail from the Garden City branch manager about O'Meally's market timing business. The branch manager questioned the effectiveness of the Mutual Fund Operations Division's internal blocking system and raised several other concerns about O'Meally's activities:

> Blocking of individual accounts by fund companies is extremely short-sighted in consideration of the fact that each "entity" maintains multiple accounts with our Firm.
> There have been repeat offenses, at least in spirit . . .
> Fund companies have been misled as to the identity of the FA's of record... Recently, [a mutual fund company] was provided with information which was at best misleading to effect the removal [of] a block.
>
> [T]here is frequent journaling of funds between accounts.
> At the present time, [O'Meally and an assistant] either have or have had a total of 48 FA #s including single, joint and also numbers.

F. PSI's Procedures to Limit Market Timing Were Ineffective

38. Although PSI senior officers issued policies and procedures ostensibly designed to proscribe the Representatives' conduct, these policies and procedures were ineffective in scope and were never fully enforced. Moreover, even in situations where these policies and procedures purportedly were enforced, PSI senior officers undermined them by granting exceptions for its largest producing registered representatives. As a result, the Representatives' deceptions continued even after these policies and procedures were promulgated.

a. PSI's June 2002 Procedure Concerning Issuance of FA Numbers

39. In June 2002, PSI instituted a procedure concerning the issuance of FA numbers, in a purported effort to hinder the Representatives' ability to obtain "Joint" numbers and "Also" numbers to evade limitations on market timing (the "June 2002 Procedure"). The June 2002 Procedure provided, simply, that requests for "Joint" and "Also" numbers would require a documented business request and a PSI Regional Business Manager's approval. The June 2002 Procedure failed to preclude the Representatives from misusing previously issued Joint and Also numbers to evade blocks imposed by mutual fund companies and it failed to preclude the Representatives from obtaining new FA numbers to facilitate their fraud. Indeed, O'Meally obtained 12 new Joint and Also numbers just days before the procedure took effect, purportedly to assist him in transferring customer accounts from one PSI branch office to another. The June 2002 Procedure also did not subject the Representatives to any form of discipline or sanction if they continued to use Joint and Also numbers to evade blocks in violation of its terms.

b. PSI's January 2003 Market Timing Policy

40. After protracted discussion involving PSI senior officers during the Fall of 2002, PSI issued a market timing policy on January 8, 2003 (the "Market Timing Policy"). PSI

considered, and rejected, defining market timing in the Market Timing Policy as a certain number of trades because of concerns that doing so would have too great an impact on the Representatives' revenues. PSI also rejected an absolute prohibition on the business of market timing. Instead, the Market Timing Policy provided that "inappropriate timing activities [would] continue to be monitored" by mutual fund companies and not by PSI itself.

41. Unlike other PSI policies concerning market timing, the Market Timing Policy expressly provided for the imposition of sanctions, including termination of employment, for the Representatives' use of "manipulative techniques" to evade mutual fund trading restrictions. Any imposition of sanctions was to be decided by a committee consisting of members of PSI's Legal, Compliance, and Risk Management divisions. Despite notifications of continuing deceptive practices received by PSI after it issued the Market Timing Policy, PSI did not form this committee and failed to take action against any of the Representatives to stop their use of "manipulative techniques" to market time.

42. The Market Timing Policy also provided that, in the event a mutual fund company asked PSI to block any one of a registered representative's FA numbers, **all** numbers belonging to the registered representative similarly would be blocked from trading. However, PSI senior officers determined not to implement this critical aspect of the Market Timing Policy. In fact, despite the policy's clear language, PSI interpreted mutual fund block requests after it issued the Market Timing Policy in the same manner as it had previously – as narrowly as possible, blocking only the specific FA number or customer account number identified by mutual fund block requests. Thus, even after issuance of the Market Timing Policy, the Representatives were able to continue their fraudulent scheme of switching to unblocked FA numbers or customer accounts to evade blocks imposed by mutual fund companies.

G. PSI Profited From the Representatives' Deceptive Acts

43. PSI identified the Representatives as early as 2000 and monitored their revenues and ranks within the firm throughout the Relevant Period. The firm's Mutual Fund Operations Division, which processed the Representatives' trades in mutual funds, monitored the Representatives' activity because their rapid trading required the dedication of additional staff within the department to process the trades and strained the firm's trade processing and settlement systems.

44. In 2000, PSI began to track each quarter the gross commission revenues generated by the Representatives. PSI prepared these reports to determine the amount of income that would possibly be reduced if the firm determined to eliminate market timing as a business. In 2001, for example, the Representatives generated more than $16 million in gross commission revenues for the firm, most of which would have been eliminated had the firm phased out market timing at that time. Similarly, the Representatives generated approximately $23 million in gross commission revenues for 2002, and received another $10 million in gross commission revenues during the first half of 2003.

45. As PSI senior officers became increasingly aware of the Representatives' use of deceptions, the firm elected to continue the business of market timing. Indeed, some of the firm's senior officers were aware that the June 2002 Procedure concerning the issuance of multiple FA numbers and the January 2003 Market Timing Policy were wholly ineffective at eradicating the Representatives' deceptions and the Representatives and their hedge fund customers continued this activity. During the Relevant Period, the Representatives generated approximately $50 million in gross revenues as a result of this conduct.

H. Violations of the Martin Act, GBL § 349 and Executive Law § 63 (12)

46. By virtue of the acts and practices set forth hereinabove, PSI violated the Martin Act, GBL § 349, and Executive Law § 63 (12).

AGREEMENT

IT NOW APPEARING THAT PEG desires to settle and resolve the Investigation without admitting or denying the Attorney General's Findings, the Attorney General and PEG hereby enter into this Assurance of Discontinuance ("Assurance"), pursuant to Executive Law § 63 (15), and agree as follows:

I. Affirmative Relief

A. Disgorgement and/or Restitution

1. PEG shall pay $270 million in disgorgement and/or restitution. The $270 million payment shall be remitted and administered in accordance with the SEC's Order Instituting Administrative Proceedings, Making Findings, and Imposing Remedial Sanctions Pursuant to Section 15(b) of the Securities Exchange Act of 1934 in *In the Matter of Prudential Equity Group, LLC, Formerly Known As Prudential Securities Incorporated*, issued on or near the date hereof (the "SEC Order").

2. The provisions in the SEC Order relating to the payment, administration and distribution of the $270 million referred to in this section are incorporated herein by reference, and such terms are agreed to as part of this Assurance by PEG.

3. PEG agrees that it shall not seek or accept, directly or indirectly, reimbursement or indemnification, including, but not limited to, payment made pursuant to any insurance policy, with regard to any or all of the amount payable pursuant to this Assurance, provided that nothing in this Assurance shall: (a) prevent PEG from bringing claims (including

claims for indemnity and/or contribution) against persons or entities for injuries sustained by, or for amounts paid in disgorgement by, PEG as a result of such persons' or entities' engagement or involvement in, agreement to permit or failure to prevent market timing; or (b) limit or impair the rights of persons other than PEG under any applicable insurance policy.

B. Incorporation of Undertakings in the SEC Order

As part of this Assurance, PEG agrees to the terms of and shall comply with the provisions of Section K, "Undertakings," of the SEC Order, which section is incorporated herein by reference.

C. General Relief

1. PEG admits the jurisdiction of the Attorney General. PEG will cease and desist from engaging in any acts in violation of the Martin Act, GBL § 349 and/or Executive Law § 63(12) and will comply with the Martin Act, GBL § 349 and Executive Law § 63(12).

2. Evidence of a violation of this Assurance by PEG shall constitute prima facie proof of violation of the Martin Act, GBL § 349 and Executive Law § 63(12) in any civil action or proceeding hereafter commenced by the Attorney General against PEG.

II. Other Provisions

A. Scope Of This Assurance

1. This Assurance concludes the Investigation brought by the Attorney General and any action the Attorney General could commence against PEG arising from or relating to the subject matter of the Investigation; provided however, that nothing contained in this Assurance shall be construed to cover claims of any type by any other state agency or any claims that may be brought by the Attorney General to enforce PEG's obligations arising from or relating to the provisions contained in this Assurance.

2. If PEG does not make the payment as provided in Section I.A. of this Assurance (*i.e.*, pursuant to the SEC Order), or PEG defaults on any obligation under this Assurance, the Attorney General may terminate this Assurance, at his sole discretion, upon 10 days' written notice to PEG and PEG agrees that any statute of limitations or other time related defenses applicable to the subject of the Investigation and any claims arising from or relating thereto are tolled from and after the date of execution of this Assurance. In the event of such termination, PEG expressly agrees and acknowledges that this Assurance shall in no way bar or otherwise preclude the Attorney General from commencing, conducting or prosecuting any investigation, action or proceeding, however denominated, related to the Investigation, against PEG or from using in any way any statements, documents or other materials produced or provided by PEG after commencement of the Investigation, including, without limitation, any statements, documents or other materials provided for purposes of settlement negotiations.

3. Nothing herein shall preclude New York State, its departments, agencies, boards, commissions, authorities, political subdivisions and corporations, other than the New York State Attorney General and only to the extent set forth in paragraph II.A.2 above (collectively, "State Entities") and the officers, agents or employees of State Entities, from asserting any claims, causes of action, or applications for compensatory, nominal and/or punitive damages, administrative, civil or criminal or injunctive relief against PEG arising from or relating to the subject of the Investigation.

4. Except as provided in Section I.C.2., above, or in an action by the Attorney General to enforce the obligations of PEG in this Assurance, neither this Assurance nor any acts performed or documents executed in furtherance of this Assurance: (a) may be deemed or used as an admission of, or evidence of, the validity of any alleged wrongdoing, liability or lack of

wrongdoing or liability; or (b) may be deemed or used as an admission of or evidence of any such alleged fault or omission of PEG or any other Prudential Financial entity in any civil, criminal or administrative proceeding in any court, administrative agency or other tribunal. This Assurance shall not confer any rights upon persons or entities who are not a party to this Assurance. This Assurance also does not limit or prohibit any defenses of PEG or its current or former affiliates to claims asserted by a person or entity not a party hereto. Nothing herein shall be construed to prohibit the use of any e-mails or other documents of PEG or of others.

5. This Assurance is not intended by the Attorney General to subject PEG or any of its affiliates to any disqualifications under the laws of any state, the District of Columbia, Puerto Rico or territory (collectively, “State”), including, without limitation, any disqualifications from relying upon the State registration exemptions or State safe harbor provisions.

6. The SEC Order, this Assurance and any order of any other State in a proceeding based upon the acts, practices and procedures of PEG which are the subject of this Investigation (collectively, the “Settlement Documents”) shall not disqualify PEG or its affiliates from any business that they otherwise are qualified, licensed or permitted to perform under the applicable laws of the State of New York and any disqualifications from relying upon this state’s registration exemptions or safe harbor provisions that arise from the Settlement Documents are hereby waived.

B. Cooperation

1. PEG and its current affiliates have cooperated to date in the Investigation. If requested to do so by PEG, the Attorney General agrees to bring the cooperation of PEG and its current affiliates to the attention of any other governmental agencies or jurisdictions, provided that PEG, its current affiliates, and its successors, assigns and/or purchasers of all or substantially all the assets of any of the foregoing (collectively, the “Prudential Entities”) continue to cooperate to the satisfaction of the Attorney General.

2. The Prudential Entities shall cooperate fully and promptly with the Attorney General with regard to any investigation, litigation or other proceeding initiated by the Attorney General or to which the Attorney General is a party, whether pending or subsequently initiated, relating to market timing or late trading. The Prudential Entities shall use their best efforts to ensure that all the current and former officers, directors, trustees, agents and employees of the Prudential Entities also fully and promptly cooperate with the Attorney General.

3. Such cooperation shall include, without limitation:

(a) production, voluntarily and without service of subpoena, of all documents or other tangible evidence requested by the Attorney General and any compilations or summaries of information or data that the Attorney General requests be prepared, with the exception of any information or documents with respect to which the Prudential Entities have a statutory or currently existing written contractual obligation of confidentiality to persons or entities who are not parties to this Assurance ("Confidential Information") and information or documents protected by the attorney-client and/or work product privileges to the extent to which such information or documents are not subject to the privilege waiver provided for in subsection B.3. (e), below ("Privileged Information");

(b) without the necessity of a subpoena, having the current officers, directors, and employees of the Prudential Entities attend any Proceedings (as hereinafter defined) in New York State or elsewhere at which the presence of any such persons is requested by the Attorney General and having such current officers, directors, and employees answer any and all inquiries that may be put by the Attorney General to any of them at any Proceedings or otherwise

(“Proceedings” include, but are not limited to, any meetings, interviews, depositions, hearings, trials, grand jury proceedings or other proceedings), except to the extent to which such inquiries call for the disclosure of Confidential Information or Privileged Information;

(c) the Prudential Entities using their best efforts to cause former officers, directors, trustees, agents and employees of the Prudential Entities and the then-current trustees and agents of the Prudential Entities to attend any Proceedings in New York State or elsewhere at which the presence of any such persons is requested by the Attorney General and to answer any and all inquiries that may be put by the Attorney General to any of them at any Proceedings or otherwise, except to the extent to which such inquiries call for the disclosure of Confidential Information or Privileged Information;

(d) fully, fairly and truthfully disclosing all information and producing all records and other evidence in the possession, custody or control of the Prudential Entities relevant to all inquiries made by the Attorney General, except to the extent to which such inquiries call for the disclosure of Confidential Information or Privileged Information;

(e) waiving, upon request by the Attorney General, all privileges relating to any internal investigations concerning matters in the Investigation including, without limitation, production of all interview notes taken in connection with any internal investigations; and

(f) making the Prudential Entities’ outside counsel reasonably available to provide comprehensive presentations concerning any internal investigation relating to all matters in this Assurance and to answer questions, except to the extent to which such presentations or questions call for the disclosure of Confidential Information or Privileged Information.

4. All communications relating to cooperation pursuant to this Assurance may be made to the Prudential Entities' attorneys as follows: Bingham & McCutchen LLP, Attention: Neal E. Sullivan, Esq., 2020 K Street, NW, Washington, DC 20006.

5. In the event that any of the Prudential Entities fails to comply with any provision of this Section II.B. of this Assurance, the Attorney General shall be entitled, in addition to any other remedies in this Assurance or otherwise, to specific performance.

C. Miscellaneous Provisions

1. This Assurance and any dispute related thereto shall be governed by the laws of the State of New York without regard to any conflicts of laws principles.

2. No failure or delay by the Attorney General in exercising any right, power or privilege hereunder shall operate as a waiver thereof nor shall any single or partial exercise thereof preclude any other or further exercise thereof or the exercise of any other right, power or privilege. The rights and remedies provided herein shall be cumulative.

3. PEG consents to the jurisdiction of the Attorney General in any proceeding or action to enforce this Assurance.

4. PEG enters into this Assurance voluntarily and represents that no threats, offers, promises, or inducements of any kind have been made by the Attorney General or any member, officer, employee, agent or representative of the Attorney General to induce PEG to enter into this Assurance.

5. This Assurance may be changed, amended or modified only by a writing signed by all parties hereto.

6. This Assurance constitutes the entire agreement between the Attorney General and PEG and supersedes any prior communication, understanding or agreement, whether written or oral, concerning the subject matter of this Assurance.

7. If any provision of this Assurance is found to be unenforceable, such finding shall not affect the enforceability of the remaining provisions hereof.

8. This Assurance shall be binding upon PEG and its successors and assigns.

9. This Assurance shall be effective and binding only when this Assurance is signed by all parties. This Assurance may be executed in one or more counterparts, each of which shall be deemed an original but all of which together shall constitute one instrument.

WHEREFORE, the following signatures are affixed hereto on the dates set forth below.

Dated: August 24, 2006

PRUDENTIAL EQUITY GROUP, LLC

By: /s/ Kenneth Y. Tanji
Kenneth Y. Tanji
Senior Vice President

Reviewed August 25, 2006, by:

/s/ Neal E. Sullivan by S. Turvey
Neal E. Sullivan
Bingham McCutchen LLP
Attorneys for Prudential Equity Group, LLC

Dated: August 25, 2006

ELIOT SPITZER
Attorney General of the State of New York

By: /s/ Gary R. Connor
Gary R. Connor
First Deputy Bureau Chief

ACKNOWLEDGMENT

STATE OF NEW JERSEY)

COUNTY OF ESSEX)

On this 24th day of August, 2006, before me personally came Kenneth Y. Tanji, known to me, who, being duly sworn by me, did depose and say that he is Senior Vice President of Prudential Equity Group, LLC, the entity described in the foregoing Assurance of Discontinuance, is duly authorized by Prudential Equity Group, LLC, to execute the same, and that he signed his name in my presence by like authorization.

/s/ Maryann Critchley

Notary Public
My commission expires: 2-17-2010

Exhibit 99.1

News Release

Prudential Financial

Prudential Financial, Inc.
751 Broad Street
Newark, NJ 07102-3777
www.prudential.com

<u>**For Immediate Release**</u>
August 28, 2006

Contact: **Bob DeFillippo**
(973) 802-4149

PRUDENTIAL EQUITY GROUP, LLC SETTLEMENT IN MARKET TIMING INVESTIGATIONS

NEWARK, N.J. – Prudential Financial, Inc. (NYSE: PRU) today confirmed that Prudential Equity Group, LLC has reached a settlement with the United States Attorney for the District of Massachusetts, the Secretary of the Commonwealth of Massachusetts, the Securities and Exchange Commission, the National Association of Securities Dealers, the New York Stock Exchange, the New Jersey Bureau of Securities and the New York Attorney General's Office in connection with their investigations into market timing related activities involving the former retail broker-dealer business at Prudential Securities, Inc. In 2003, Prudential Securities contributed that business to a joint venture with Wachovia Corporation. However, Prudential Equity Group, LLC retained liability for the market timing related activities at issue in the investigations.

Under the terms of the settlement, Prudential Equity Group, LLC has agreed to pay $270 million into a Fair Fund administered by the SEC to compensate those harmed by the market timing related activities. In addition, $330 million will be paid as fines and penalties. The settlement resolves these investigations as to all Prudential companies without further proceedings, as long as the terms of the settlement are followed. Prudential Equity Group, LLC has previously reserved sufficient funds to cover these payments.

Prudential Chairman and CEO Arthur F. Ryan said: "We take these matters very seriously and deeply regret the conduct of some former employees that led to these problems. Let me assure you that as part of our ongoing review of business practices, we have strengthened our compliance programs. Prudential cooperated with the authorities throughout the process. This settlement represents our desire to do the right thing and to put this matter behind us, which we believe is in the best interests of our customers, shareholders and employees."

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Prudential Financial companies, with approximately $568 billion in total assets under management as of June 30, 2006, serve individual and institutional customers worldwide and include The Prudential Insurance Company of America, one of the largest life insurance companies in the United States. These companies offer a variety of products and services, including life insurance, mutual funds, annuities, pension and retirement-related services and administration, asset management, banking and trust services, real estate brokerage franchises, relocation services and, through a joint venture, retail securities brokerage services. For more information, visit www.prudential.com.

Prudential Financial