

STATE OF WASHINGTON  
DEPARTMENT OF FINANCIAL INSTITUTIONS  
SECURITIES DIVISION

IN THE MATTER OF DETERMINING  
whether there has been a violation  
of the Securities Act of Washington by:

Order Number S-08-229-09-CO01

CONSENT ORDER

WACHOVIA SECURITIES, LLC;  
WACHOVIA CAPITAL MARKETS, LLC,

Respondents.

**INTRODUCTION**

WHEREAS, Wachovia Securities, LLC<sup>1</sup> (“Wachovia Securities”), is a broker-dealer registered in the State of Washington with its home office at One North Jefferson Avenue, St. Louis, Missouri, and Wachovia Capital Markets, LLC (“Wachovia Capital Markets,” collectively with Wachovia Securities, “Wachovia”<sup>2</sup>), is a broker-dealer with its home office at 301 South College Street, Charlotte, North Carolina; and

WHEREAS, a multi-state task force conducted and coordinated investigations into Wachovia’s marketing and sale of auction rate securities to investors during the period of January 1, 2006, through February 14, 2008; and

WHEREAS, after a books and records inspection by a multi-state task force on July 17, 2008, Wachovia Securities has cooperated fully with regulators conducting the investigations by responding to inquiries, providing documentary evidence and other materials, and providing

<sup>1</sup> In October 2007, Wachovia Corporation acquired the Missouri-based broker dealer A. G. Edwards & Sons, Inc. (“AG Edwards”) which was subsequently combined with Wachovia Securities, LLC.

<sup>2</sup> Factual allegations in this Order may apply to Wachovia Securities and/or Wachovia Capital Markets, but do not necessarily refer to both entities.

1 regulators with access to information relating to the investigations; and

2 WHEREAS, Wachovia has advised regulators of its agreement to resolve the  
3 investigations relating to its marketing and sale of auction rate securities to investors; and

4 WHEREAS, Wachovia agrees to, among other things, reimburse certain purchasers of  
5 auction rate securities, and to make certain payments at the direction of the Securities Division of  
6 the Washington State Department of Financial Institutions; and

7 WHEREAS, Wachovia elects to permanently waive any right to a hearing and appeal  
8 under RCW 21.20.440 and RCW 34.05 with respect to this Consent Order (the “Order”);

9 NOW, THEREFORE, the Securities Administrator, as administrator of the Securities Act  
10 of Washington, RCW 21.20, hereby enters this Order.

11  
12 **I.**

13 **FINDINGS OF FACT**

14 1. Wachovia Securities admits the jurisdiction of the Securities Division of the  
15 Washington State Department of Financial Institutions and Wachovia Capital Markets consents  
16 to the jurisdiction of the Securities Division of the Washington State Department of Financial  
17 Institutions for purposes of this Order. Neither of them admits nor denies the Findings of Fact  
18 and Conclusions of Law contained in this Order, and each consents to the entry of this Order by  
19 the Securities Division of the Washington State Department of Financial Institutions.

20 2. Auction rate securities are long-term debt or equity instruments that include  
21 auction preferred shares of closed-end funds, municipal auction rate bonds, and various asset-  
22 backed auction rate bonds (collectively referred to herein as “ARS”). While ARS are all long-  
23

1 term instruments, one significant feature of ARS (which historically provided the potential for  
2 short-term liquidity) is the interest/dividend reset through auctions that occur in varying  
3 increments of between 7 and 42 days. If an auction is successful, investors are able to exit the  
4 ARS market on a short-term basis. If, however, an auction “fails,” investors are required to hold  
5 all or some of their ARS until the next successful auction in order to liquidate their funds.  
6 Beginning in February 2008, the ARS market experienced widespread failed auctions.

7 3. In April 2008, Wachovia Securities’ investors, unable to access their ARS funds,  
8 began to submit complaints to the Securities Division of the Washington State Department of  
9 Financial Institutions. Since April 2008, the Securities Division of the Washington State  
10 Department of Financial Institutions has received 2 complaints from Washington residents  
11 concerning the sale of ARS by Wachovia Securities. Those complaints covered ARS holdings  
12 totaling over \$1,500,000.  
13

14 **Marketing and Sales of ARS to Investors**

15 4. In connection with the sale of ARS, some Washington residents state variously  
16 that they were told by Wachovia Securities and its registered agents that ARS were one or more  
17 of the following:

- 18 a. just like cash;
- 19 b. same as cash;
- 20 c. safe as cash;
- 21 d. same as money markets;
- 22 e. safe as money markets;
- 23
- 24

- 1 f. cash equivalents;
- 2 g. short-term adjustable rate securities;
- 3 h. cash alternatives;
- 4 i. completely safe;
- 5 j. liquid at any time; and/or
- 6 k. always liquid at an auction.

7 Although marketed and sold to investors as safe, liquid, cash-like investments, and although the  
8 ARS market had, in fact, functioned for more than twenty years with virtually no auction  
9 failures, ARS are actually long-term instruments subject to a complex auction process that, upon  
10 failure, can lead to illiquidity and lower interest rates.

11  
12 5. Wachovia Securities further fostered the misconception that ARS were cash-like  
13 instruments by providing account portfolio summaries to certain of its customers that listed ARS  
14 as “cash equivalents.” In fact, ARS were not “cash equivalents” and full liquidity was only  
15 available at an auction if the auction was successful.

16 6. Although Wachovia Securities sold ARS as conservative, safe, and liquid  
17 investments to its investors until February 2008, Wachovia had information that several auctions  
18 had failed in August 2007 and early 2008, before the mass failures in February 2008. During  
19 this same period of time, Wachovia failed to inform its customers purchasing ARS after such  
20 auctions began to fail that certain auctions would have failed had Wachovia or another broker-  
21 dealer not entered support bids in those auctions.

22  
23 7. Although Wachovia knew, or should have known, of the inherent risks and the

1 recent volatility of the ARS market, only minimal information regarding the ARS market was  
2 provided to Wachovia Securities' retail ARS customers.

3 8. Wachovia and its registered securities agents were, or should have been, aware  
4 that the ARS market was suffering from increasing failures and liquidity issues, and they should  
5 have disclosed those facts to investors who were purchasing auction rates after such issues arose.  
6 Based on these facts, Wachovia engaged in dishonest and unethical practices in the marketing  
7 and sale of ARS. Pursuant to RCW 21.20.110(1)(g), these practices constitute grounds to revoke  
8 Wachovia's registration. These practices included, among other things, the following:

9 a. Wachovia told some ARS investors purchasing ARS after the market  
10 disruptions began to occur that:

- 11 i. ARS were cash equivalents;
- 12 ii. ARS were completely safe; and/or
- 13 iii. ARS were liquid at any time; and

14 b. Wachovia was or should have been aware that the market for ARS was  
15 becoming illiquid, yet Wachovia Securities continued to market and sell  
16 ARS to investors.  
17

18 **Temporary Maximum Rate Waiver on Certain ARS**

19 9. The interest rates on ARS are reset periodically through the auction process. In  
20 the event that there is insufficient demand for a particular issue and an auction fails, the interest  
21 rate resets to a "maximum rate" or "failure rate" as defined in the offering documents for that  
22 particular issue. Typically, this maximum rate would be higher than prevailing market rates in  
23

1 order to compensate ARS holders who are unable to sell their positions and offer an “incentive”  
2 to induce buyers to return to the market although in some cases, particularly for student loan  
3 auction rates, the maximum rate might be lower than the prevailing rate.

4 10. In December 2007, with the encouragement of its underwriters, the Missouri  
5 Higher Education Loan Authority (“MOHELA”) sought and secured approval to waive its  
6 maximum rate for certain issues of ARS. Absent such waivers, the ARS issued by MOHELA  
7 would not have been allowed to reset at interest rates high enough to clear auctions.

8 11. As a result of the maximum rate waivers, certain MOHELA ARS issues reset to a  
9 higher rate for a brief period after the waiver was implemented. However, due to a feature of  
10 those issues that caps the average interest rate over any given one-year period, the interest rates  
11 reset to 0% after the expiration of the waiver period. The ramifications of this maximum rate  
12 waiver were not explained to Wachovia Securities’ customers who subsequently purchased  
13 MOHELA ARS.  
14

15 12. Wachovia Securities engaged in dishonest and unethical practices by not  
16 adequately explaining to individual investors who purchased ARS with maximum rate waivers,  
17 among other things, the following:

- 18 a. that the ARS interest rates could not be reset at a level that would prevent  
19 a failed auction absent the maximum rate waiver; and  
20  
21 b. that the high interest rate allowed by the waiver would expire at the end of  
22 the waiver period unless extended by the issuer.

23 Pursuant to RCW 21.20.110(1)(g), these practices constitute grounds to revoke Wachovia  
24

1 Securities' registration.

2 **Failure To Supervise Agents Who Sold ARS**

3 13. Although ARS are complicated and complex products, Wachovia Securities did  
4 not provide its sales or marketing staff with the training and information necessary to adequately  
5 explain these products or the mechanics of the auction process to their customers. During the  
6 course of investigations, on-the-record statements taken from Wachovia Securities' registered  
7 agents demonstrated that these agents lacked a basic understanding of the functionality of the  
8 ARS products and the auction rate market.

9 14. Many of Wachovia Securities' registered agents were not adequately educated in  
10 the ARS products they were selling and did not know where to look for information to bolster  
11 that knowledge. Wachovia Securities failed to provide timely and comprehensive sales and  
12 marketing literature regarding ARS and the mechanics of the auction process. In addition,  
13 Wachovia Securities failed to review account portfolio statements sent to its customers to ensure  
14 that they reflected accurate information regarding ARS.

15 15. Wachovia Securities' failure to provide sufficient training and information  
16 concerning ARS and the market environment in which they were sold was not limited to one or  
17 two agents, and is therefore indicative of Wachovia Securities' failure to ensure that its  
18 registered personnel provided adequate information regarding ARS to its customers.

19 16. Wachovia Securities failed to reasonably supervise its employees, which is  
20 grounds for revocation of its registration under RCW 21.20.110(1)(j). These practices included,  
21 among other things, the following:  
22  
23  
24

- 1 a. failing to provide adequate training to its registered agents regarding ARS  
2 by, among other things:
- 3 i. failing to provide timely and comprehensive sales and marketing  
4 literature regarding ARS and the mechanics of the auction process;
- 5 ii. failing to provide pertinent information concerning the complexity  
6 of the ARS product; and
- 7 iii. failing to ensure that its agents were selling ARS to individual  
8 investors for whom they were suitable; and
- 9 b. failing to review account portfolio statements sent to its customers to  
10 ensure that they reflected accurate information regarding ARS;
- 11 c. failing to review ARS transactions in accounts of customers who needed  
12 liquidity; and
- 13 d. failing to ensure that its registered personnel were providing adequate  
14 information regarding ARS to its customers.  
15

16 **II.**

17 **CONCLUSIONS OF LAW**

18 17. The Securities Division of the Washington State Department of Financial  
19 Institutions has jurisdiction over this matter pursuant to the Securities Act of Washington, RCW  
20 21.20.  
21

22 18. The Securities Division of the Washington State Department of Financial  
23 Institutions finds that Wachovia Securities failed to supervise its employees and engaged in  
24

1 dishonest or unethical practices in the securities business, and that this conduct constitutes  
2 grounds to revoke Wachovia Securities' registration under RCW 21.20.110(1)(j) and RCW  
3 21.20.110(1)(g).

4 19. The Securities Division of the Washington State Department of Financial  
5 Institutions finds this Order and the following relief appropriate, in the public interest, and  
6 consistent with the purposes intended by the Securities Act of Washington.

7 **III.**

8 **CONSENT ORDER**

9 On the basis of the Findings of Fact, Conclusions of Law, and Wachovia's consent to the  
10 entry of this Order,

11 **IT IS HEREBY ORDERED:**

12 1. This Order concludes the investigation by the Securities Division of the  
13 Washington State Department of Financial Institutions and any other action that the Securities  
14 Division of the Washington State Department of Financial Institutions could commence under  
15 applicable Washington State law on behalf of the State of Washington as it relates to Wachovia,  
16 and its marketing and sale of auction rate securities to investors.

17 2. This Order is entered into solely for the purpose of resolving the referenced multi-  
18 state investigation, and is not intended to be used for any other purpose.

19 3. Wachovia shall CEASE AND DESIST from violating the Securities Act of  
20 Washington and shall comply with the Securities Act of Washington.

21 4. Within ten days after the entry of this Order, Wachovia shall pay the sum of  
22

1 \$491,556.71 to the State of Washington as a civil monetary penalty pursuant to RCW 21.20.110,  
2 to be deposited in the Securities Prosecution Fund, pursuant to RCW 21.20.395, which amount  
3 constitutes the State of Washington's proportionate share of the state settlement amount of 50  
4 million dollars (\$50,000,000.00).

5 5. In the event another state securities regulator determines not to accept Wachovia's  
6 state settlement offer, the total amount of the State of Washington's payment shall not be  
7 affected, and shall remain at \$491,556.71.

8 6. Wachovia Securities and Wachovia Capital Markets, respectively, as agents for  
9 one or more affiliated companies and not as principal, shall offer to purchase at par ARS that  
10 are subject to auctions that are not successful and are not subject to current calls or redemptions  
11 ("Eligible ARS") from all investors in the Relevant Class. For purposes of this Order the  
12 Relevant Class shall be defined as all investors who purchased ARS from either Wachovia  
13 Securities or Wachovia Capital Markets, respectively, on or before February 13, 2008 into  
14 accounts maintained at Wachovia Securities or Wachovia Capital Markets, respectively.  
15

16 a. Wachovia Securities and Wachovia Capital Markets, as agents for one or  
17 more affiliated companies and not as principal, shall make an offer to buy the  
18 Eligible ARS from Individual Investors, as defined below, who are in the  
19 Relevant Class. This buy back shall commence no later than November 10,  
20 2008 and conclude no later than November 28, 2008. For purposes of this  
21 Order, Individual Investors shall include natural persons, individual retirement  
22 accounts and the following entities or accounts:  
23  
24

- 1 i. Accounts with the following owners:
- 2 1. non-profit charitable organizations; and
- 3 2. religious corporations.
- 4 ii. Accounts with the following owners and with account values or
- 5 household values up to \$10 million:
- 6 1. trusts;
- 7 2. corporate trusts;
- 8 3. corporations;
- 9 4. employee pension plans/ERISA and Taft Hartley Act plans;
- 10 5. educational institutions;
- 11 6. incorporated non-profit organizations;
- 12 7. limited liability companies;
- 13 8. limited partnerships;
- 14 9. non-public companies;
- 15 10. partnerships;
- 16 11. personal holding companies;
- 17 12. unincorporated associations; and
- 18 13. governmental and quasi-government entities.

19

20

21 b. Wachovia Securities and Wachovia Capital Markets as agent for one or more

22 affiliated companies and not as principal, shall commence a buy back of the

23 Eligible ARS from all other investors in the Relevant Class not otherwise

24

1 covered by subparagraph a, above, no later than June 10, 2009 and conclude  
2 no later than June 30, 2009.

3 7. No later than November 28, 2008, Wachovia shall pay any investor in the  
4 Relevant Class who sold ARS below par between February 13, 2008 and August 15, 2008 and  
5 whom Wachovia can reasonably identify, the difference between par and the price at which the  
6 investor sold the ARS.

7 8. Wachovia shall notify all investors in the Relevant Class of the provisions of this  
8 Order as provided in paragraphs 9 and 10.

9 9. As part of Wachovia's general obligation to notify all investors in the Relevant  
10 Class pursuant to paragraph 8, above, Wachovia shall mail the Required Notification, defined  
11 below, by November 10, 2008, to all investors in the Relevant Class that held ARS positions in  
12 a Wachovia account as of August 31, 2008. For purposes of the Order, "Required Notification"  
13 shall mean a notice that includes general statements and information specific to each investor,  
14 including:  
15

- 16 a. a general notification of all provisions of this Order;
- 17 b. the specific security purchased;
- 18 c. the quantity purchased;
- 19 d. the par value of the holding;
- 20 e. a prominent statement disclosing that at this time the Relevant Class member's  
21 ARS holdings may not be liquid and that there is a possibility that this offer may  
22 be the only opportunity for the investor to liquidate the ARS holdings; and  
23

1 f. a statement that the offer to repurchase the ARS holdings, and other relief  
2 specified in the Order, is being made pursuant to a settlement with state  
3 securities regulators.

4 10. By November 10, 2008, Wachovia shall mail the Required Notification to all  
5 investors in the Relevant Class that transferred ARS positions to a firm other than Wachovia,  
6 prior to the date of this Order, if the initial purchase of the Eligible ARS was on or after January  
7 1, 2003 unless the ARS has been redeemed in full by the issuer.

8 11. Wachovia shall demonstrate that all investors in the Relevant Class received the  
9 Required Notification if Wachovia demonstrates that: 1) Wachovia mailed the Required  
10 Notification via First Class mail at the customer's last known address and did not receive a  
11 return notice, or 2) Wachovia repurchased ARS from the investor.

12 12. Wachovia Securities shall establish and maintain a dedicated telephone assistance  
13 line, with appropriate staff, to respond to questions from investors concerning the terms of this  
14 Order and Wachovia's no net cost loan (nonrecourse, no release) program. Wachovia Securities  
15 shall maintain this dedicated telephone assistance line through June 30, 2009.

16 13. With respect to any claim for consequential damages, to the extent such claims  
17 are not resolved informally by Wachovia, Wachovia shall arbitrate the claim of any Relevant  
18 Class member who elects to arbitrate, pursuant to the following provisions:  
19

- 20 a. the arbitrations will be conducted by a public arbitrator (as defined by section  
21 12100(u) of the NASD Code of Arbitration Procedures for Customer  
22 Disputes, eff. April 16, 2007), under the auspices of FINRA;  
23

- 1           b. the above-referenced public arbitrator will be available for the exclusive  
2           purpose of arbitrating any Relevant Class member's consequential damages  
3           claim;
- 4           c. Wachovia shall pay all applicable forum and filing fees;
- 5           d. any Relevant Class member who chooses to pursue such a claim shall bear the  
6           burden of proving that they suffered consequential damages and that such  
7           damages were caused by investors' inability to access funds consisting of  
8           investors' ARS purchases through Wachovia; and
- 9           e. Wachovia shall be able to defend itself against such claims; provided,  
10          however, that Wachovia shall not contest liability related to the sale of ARS;  
11          and provided further that Wachovia shall not be able to use as part of its  
12          defense an investor's decision not to borrow money from Wachovia.

13  
14           14. Wachovia shall make best efforts to identify Eligible Investors who took out loans  
15          from Wachovia, between February 13, 2008 and the date of this Order, that were secured by  
16          Eligible Auction Rate Securities that were not successfully auctioning at the time the loan was  
17          taken out from Wachovia, and paid interest associated with the auction-rate-securities-based  
18          portion of those loans in excess of the total interest and dividends received on the auction rate  
19          securities during the duration of the loan. Wachovia shall reimburse such customers for the  
20          excess expense, plus reasonable interest thereon. Such reimbursement shall occur no later than  
21          60 days after the entry of this Order.

22  
23           15. By November 28, 2008, Wachovia Securities and Wachovia Capital Markets,

1 respectively and separately, shall refund refinancing fees received by it to municipal auction  
2 rate issuers that issued such securities in the initial primary market between August 1, 2007 and  
3 February 13, 2008, and refinanced those securities through Wachovia after February 13, 2008.

4 16. If Wachovia defaults in any of its obligations set forth in this Order, the Securities  
5 Division of the Washington State Department of Financial Institutions may vacate this Order, at  
6 its sole discretion, upon 10 days notice to Wachovia and without opportunity for administrative  
7 hearing.

8 17. This Order is not intended to indicate that Wachovia or any of its affiliates or  
9 current or former employees shall be subject to any disqualifications contained in the federal  
10 securities law, the rules and regulations thereunder, the rules and regulations of self regulatory  
11 organizations or various states' securities laws including any disqualifications from relying  
12 upon the registration exemptions or safe harbor provisions. In addition, this Order is not  
13 intended to form the basis for any such disqualifications.  
14

15 18. This Order may not be read to indicate that Wachovia or any of its affiliates or  
16 current or former employees engaged in fraud or violated any federal or state laws, the rules and  
17 regulations thereunder, or the rules and regulations of self regulatory organizations.

18 19. For any person or entity not a party to this Order, this Order does not limit or create  
19 any private rights or remedies against Wachovia including, without limitation, the use of any e-  
20 mails or other documents of Wachovia or of others for the marketing and sale of auction rate  
21 securities to investors, limit or create liability of Wachovia, or limit or create defenses of Wachovia  
22 to any claims.  
23

1           20.     This Order shall not disqualify Wachovia or any of its affiliates or current or  
2 former employees from any business that they otherwise are qualified or licensed to perform  
3 under applicable state law and this Order is not intended to form the basis for any  
4 disqualification.

5           21.     Nothing herein shall preclude the State of Washington, its departments, agencies,  
6 boards, commissions, authorities, political subdivisions and corporations, other than the Securities  
7 Division of the Washington State Department of Financial Institutions and only to the extent set  
8 forth in paragraph 1 above, (collectively, "State Entities") and the officers, agents or employees of  
9 State Entities from asserting any claims, causes of action, or applications for compensatory,  
10 nominal and/or punitive damages, administrative, civil, criminal, or injunctive relief against  
11 Wachovia in connection with the marketing and sale of auction rate securities at Wachovia.  
12

13           22.     Wachovia shall pay its own costs and attorneys' fees with respect to this matter.

14 Dated and Entered this 24th day of March , 2009.

15 By:

16 

17 \_\_\_\_\_  
18 MICHAEL E. STEVENSON  
19 Securities Administrator

20 Approved by:

21 

22 \_\_\_\_\_  
23 Suzanne Sarason  
24 Chief of Enforcement

Presented by:

25 

26 \_\_\_\_\_  
Bridgett Fisher  
Enforcement Attorney

**CONSENT TO ENTRY OF ADMINISTRATIVE ORDER BY WACHOVIA**

1  
2 Wachovia hereby acknowledges that it has been served with a copy of this Consent Order,  
3 has read the foregoing Order, is aware of its right to a hearing and appeal in this matter, and has  
4 waived the same.

5 Wachovia Securities admits the jurisdiction of the Securities Division of the Washington  
6 State Department of Financial Institutions and Wachovia Capital Markets consents to the  
7 jurisdiction of the Securities Division of the Washington State Department of Financial Institutions  
8 for purposes of this Order. Neither Wachovia Securities nor Wachovia Capital Markets admits or  
9 denies the Findings of Fact and Conclusions of Law contained in this Order; and each consents to  
10 entry of this Order by the Commissioner as settlement of the issues contained in this Order.  
11

12 Wachovia states that no promise of any kind or nature whatsoever was made to it to induce  
13 it to enter into this Order and that it has entered into this Order voluntarily.

14 Doug Kelly represents that he/she is General Counsel of Wachovia  
15 Securities, LLC and that, as such, has been authorized by Wachovia Securities, LLC to enter into  
16 this Order for and on behalf of Wachovia Securities, LLC.

17 Vincent Altamura represents that he/she is SVP of  
18 Wachovia Capital Markets, LLC and that, as such, has been authorized by Wachovia Capital  
19 Markets, LLC to enter into this Order for and on behalf of Wachovia Capital Markets, LLC.  
20

21 Wachovia agrees that it shall not claim, assert, or apply for a tax deduction or tax credit  
22 with regard to any state, federal or local tax for any administrative monetary penalty that  
23 Wachovia shall pay pursuant to this Order.  
24

