

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. 2015047682404**

TO: Department of Enforcement
Financial Industry Regulatory Authority ("FINRA")

RE: Western International Securities, Inc. (BD No. 39262)
Respondent

Pursuant to FINRA Rule 9216 of FINRA's Code of Procedure, Respondent Western International Securities, Inc. ("Western" or the "Firm") submits this Letter of Acceptance, Waiver and Consent ("AWC") for the purpose of proposing a settlement of the alleged rule violations described below. This AWC is submitted on the condition that, if accepted, FINRA will not bring any future actions against Western alleging violations based on the same factual findings described herein.

I.

ACCEPTANCE AND CONSENT

A. Respondent hereby accepts and consents, without admitting or denying the findings, and solely for the purposes of this proceeding and any other proceeding brought by or on behalf of FINRA, or to which FINRA 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 FINRA:

BACKGROUND

Western has been a member of FINRA since 1995. The Firm is a full-service broker-dealer headquartered in Pasadena, California. Western maintains approximately 171 branch offices and has approximately 477 registered personnel.

RELEVANT DISCIPLINARY HISTORY

The Firm has no relevant disciplinary history.

OVERVIEW

From January 1, 2011 to November 5, 2015 (the "Relevant Period"), Western failed to establish, maintain and enforce a supervisory system and written supervisory procedures ("WSPs") reasonably designed to ensure that representatives' recommendations regarding leveraged, inverse, and inverse-leveraged Exchange-Traded Funds ("Non-Traditional ETFs") complied with applicable securities law and regulations, and FINRA

rules. Based on the foregoing, Western violated NASD Rule 3010 and FINRA Rules 3110 and 2010.

In addition, during the Relevant Period, Western allowed its representatives to (1) recommend Non-Traditional ETFs without performing reasonable diligence to understand the risks and features associated with them, and (2) recommend Non-Traditional ETFs that were unsuitable for certain customers based on their ages, investment objectives and financial situations. Based on the foregoing, Western violated NASD Rule 2310 and FINRA Rules 2111 and 2010.

FACTS AND VIOLATIVE CONDUCT

A. Western Failed to Establish, Maintain and Enforce a Reasonably Designed Supervisory System and WSPs Regarding Non-Traditional ETFs

1. Non-Traditional ETFs

Non-Traditional ETFs are designed to return a multiple of an underlying index or benchmark, the inverse of that index or benchmark, or both, over the course of one trading session – usually a single day. As a result, the performance of Non-Traditional ETFs over periods of time longer than a single trading session “can differ significantly from the performance . . . of their underlying index or benchmark during the same period of time.” *FINRA Regulatory Notice 09-31*. Because of these risks and the inherent complexity of these products, FINRA has advised broker-dealers and their representatives that Non-Traditional ETFs “are typically not suitable for retail investors who plan to hold them for more than one trading session, particularly in volatile markets.” *Id.*

2. Western Failed to Adequately Supervise Its Non-Traditional ETF Business

FINRA Rule 3110 and its predecessor, NASD Rule 3010, require that a FINRA member firm establish, maintain, and enforce a supervisory system and written supervisory procedures to supervise the activities of its registered representatives that are reasonably designed to achieve compliance with applicable securities laws, regulations and rules.¹

During the Relevant Period, Western executed about 10,800 solicited Non-Traditional ETF transactions in retail accounts totaling approximately \$197 million. The trading occurred in 1,562 customer accounts, serviced by 182 registered representatives.

Western failed to reasonably supervise these transactions. Western did not have written policies or procedures that addressed the unique features and risks associated with Non-Traditional ETFs, although it provided education regarding these products during annual

¹ FINRA Rule 3110 superseded NASD Rule 3010 effective December 1, 2014.

compliance meetings. In addition, Western lacked any system that enabled supervisory personnel to adequately monitor the risks peculiar to Non-Traditional ETFs, most particularly the risk posed by long-term holding of a product that resets daily. Western had no exception reports or alerts specific to Non-Traditional ETFs, let alone any supervisory tool that could detect the divergence of a Non-Traditional ETF from its linked index, and the Firm had no automated method of calculating and monitoring holding periods.

By virtue of the foregoing, Western violated NASD Rule 3010 and FINRA Rules 3110 and 2010.

B. Unsuitable Non-Traditional ETF Transactions

The reasonable-basis suitability obligation under NASD Rule 2310 and FINRA Rule 2111 requires a broker-dealer and its registered representatives to, *inter alia*, perform reasonable diligence to understand the nature of a recommended security, as well as the potential risks and rewards.¹ As FINRA has stated, “[w]ith respect to leveraged and inverse ETFs, this means that a firm must understand the terms and features of the funds, including how they are designed to perform, how they achieve that objective, and the impact that market volatility, the ETF’s use of leverage, and the customer’s intended holding period will have on their performance.”²

Western, through its registered representatives, failed to perform an adequate reasonable basis suitability analysis of Non-Traditional ETFs to understand the risks and features associated with these products before offering them for sale to retail customers (or, particularly, recommending these products as long-term investments to retail customers).

In addition, Western representatives solicited and effected Non-Traditional ETF purchases that were unsuitable for specific customers. As noted, Non-Traditional ETFs are complex and speculative securities, but representatives recommended these products (and the long-term holding of these products) to conservative customers with modest financial situations, some of whom were elderly. Moreover, some of these customers held Non-Traditional ETF positions for extended periods. For example:

- a 73-year-old customer with an investment objective of growth, a conservative risk tolerance, and a net worth of \$200,000 held five solicited Non-Traditional ETF positions for an average of 356 days, resulting in a net loss of \$20,232.41.

¹ FINRA Rule 2111 superseded NASD Rule 2310 effective July 9, 2012.

² See Notice 09-31, at 3; see also FINRA Regulatory Notice 12-03, *Complex Products - Heightened Supervision of Complex Products* (January 2012), at 5-6.

- a 71-year-old customer with an investment objective of growth, a conservative risk tolerance, and a net worth of \$200,000 held five solicited Non-Traditional ETF positions for an average of 346 days, resulting in a net loss of \$22,670.14.
- a customer with an investment objective of growth, a conservative risk tolerance, and a net worth of \$200,000 held five solicited Non-Traditional ETF positions for an average of 350 days, resulting in a net loss of \$32,865.

By virtue of the foregoing, Western violated NASD Rule 2310 and FINRA Rules 2111 and 2010.

13. Western consents to the imposition of the following sanctions:

- censure; and
- a fine of \$125,000.

Western is also ordered to pay restitution in the amount of \$521,098.10 to the customers listed in Attachment A hereto, plus interest at the rate set forth in Section 6621(a)(2) of the Internal Revenue Code, 26 U.S.C. 6621(a)(2), from November 5, 2015, until the date this AWC is accepted by the NAC.

A registered principal of Western shall submit satisfactory proof of payment of restitution or of reasonable and documented efforts undertaken to effect restitution. Such proof shall be submitted to David F. Newmun, Senior Regional Counsel, FINRA Department of Enforcement, 1601 Market Street, Suite 2700, Philadelphia, PA, either by letter that identifies Western and the case number or by email from a work-related account of the registered principal of Western to EnforcementNotice@FINRA.org. This proof shall be provided to the FINRA staff member listed above no later than 120 days after acceptance of the AWC.

If for any reason Western cannot locate any customers identified in Attachment A after reasonable and documented efforts within 120 days from the date of the AWC is accepted, or such additional period agreed to by a FINRA staff member in writing, Western shall forward any undistributed restitution and interest to the appropriate escheat, unclaimed property or abandoned property fund in the state in which the customer is last known to have resided. Western shall provide satisfactory proof of such action to the FINRA staff member identified above and in the manner described above, within 14 days of forwarding the undistributed restitution to the appropriate state authority.

The imposition of a restitution order or any other monetary sanction herein, and the timing of such ordered payments, does not preclude customers from pursuing their own actions to obtain restitution or other remedies.

Western agrees to pay the monetary sanctions upon notice that this AWC has been accepted and that such payments are due and payable. Western has submitted an Election

of Payment form showing the method by which it proposes to pay the fine imposed.

Western has specifically and voluntarily waived any right to claim an inability to pay at any time hereafter the monetary sanction imposed in this matter.

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

I.

WAIVER OF PROCEDURAL RIGHTS

Respondent specifically and voluntarily waives the following rights granted under FINRA's Code of Procedure:

- A. To have a Complaint issued specifying the allegations against it;
- B. To be notified of the 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 National Adjudicatory Council ("NAC") and then to the U.S. Securities and Exchange Commission and a U.S. Court of Appeals.

Further, Respondent specifically and voluntarily waives any right to claim bias or prejudgment of the Chief Legal Officer, the NAC, or any member of the NAC, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including acceptance or rejection of this AWC.

Respondent further specifically and voluntarily waives any right to claim that a person violated the ex parte prohibitions of FINRA Rule 9143 or the separation of functions prohibitions of FINRA 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.

III.

OTHER MATTERS

Respondent understands that:

- A. Submission of this AWC is voluntary and will not resolve this matter unless and

until it has been reviewed and accepted by the NAC, a Review Subcommittee of the NAC, or the Office of Disciplinary Affairs ("ODA"), pursuant to FINRA Rule 9216;

B. If this AWC is not accepted, its submission will not be used as evidence to prove any of the allegations against Respondent; and

C. If accepted:

1. this AWC will become part of the Respondent's permanent disciplinary record and may be considered in any future actions brought by FINRA or any other regulator against it;

2. this AWC will be made available through FINRA's public disclosure program in accordance with FINRA Rule 8313;;

3. FINRA may make a public announcement concerning this agreement and the subject matter thereof in accordance with FINRA Rule 8313; and

4. Respondent may not take any action or make or permit to be made any public statement, including in regulatory filings or otherwise, denying, directly or indirectly, any finding in this AWC or create the impression that the AWC is without factual basis. Respondent may not take any position in any proceeding brought by or on behalf of FINRA, or to which FINRA is a party, that is inconsistent with any part of this AWC. Nothing in this provision affects Respondent's: (i) testimonial obligations; or (ii) right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party.

D. Respondent may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. Respondent understands that they 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 FINRA, nor does it reflect the views of FINRA or its staff.

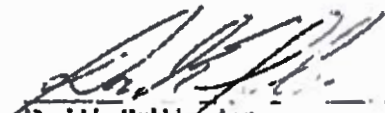
The undersigned, on behalf of the Firm, certifies that a person duly authorized to act on its behalf has read and understands all of the provisions of this AWC and has been given a full opportunity to ask questions about it; that the Firm has agreed to its provisions voluntarily; and that no offer, threat, inducement, or promise of any kind, other than the terms set forth herein and the prospect of avoiding the issuance of a Complaint, has been made to induce the Firm to submit it.

Western International Securities, Inc.

2/13/2018
Date (mm dd,yyyy)

By 
Bradley C. Kaiser
Chief Compliance Officer

Reviewed by:


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Accepted by FINRA:

2/29/2018
Date

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



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Attachment A
AWC No. 2015047682404

Customer Initials	Amount of Restitution
ACB	\$1,151.20
AYL	\$5,429.39
AB	\$1,875.95
AVG	\$1,915.60
AGB	\$4,463.62
AGB	\$294.00
AHG	\$4,734.56
AHG	\$1,324.22
BD	\$16,477.11
BJ	\$490.24
BVP	\$3,029.11
BW	\$20,898.11
BK	\$1,474.76
BV	\$2,149.15
BTE	\$669.96
CR	\$544.41
CA 1	\$2,164.45
CA 2	\$527.46
CC	\$5,298.15
CCF	\$941.90
CCF	\$485.73
DC	\$24,522.45
DDRB	\$2,931.34
DD	\$11,721.68
DVF	\$635.36
DEH	\$856.40
DJI	\$3,644.49
DEO	\$43,151.45
D FAMILY TRUST	\$32,865.61
DB	\$565.36
EHW	\$1,233.37
EAM	\$706.46
EH	\$147.90
EM	\$2,220.58
GC	\$609.43
GKJ	\$970.90
GHG	\$1,305.55
GW	\$1,630.07
HMC	\$493.50
IS_1	\$652.33
IS_2	\$349.01
JG	\$4,028.22
JD_1	\$1,967.29
JJ_2	\$876.31
JEP_1	\$454.07
JTS	\$9,383.32
JMS	\$573.40
JB	\$1,004.25
J TRUST	\$881.37

Attachment A
AWC No. 2015047682404

Customer Initials	Amount of Restitution
JL	\$4,049.05
JSB	\$10,462.18
JJ_1	\$296.22
JPA	\$1,191.81
JF	\$11,270.12
JD_2	\$20,232.41
JD_2	\$382.39
JD_2	\$17,208.89
JGP	\$934.33
JGP	\$2,806.43
JGA	\$1,149.38
JGA	\$18,903.57
JEP_2	\$527.17
KWD	\$1,024.76
LJ	\$1,200.46
LMM	\$3,028.77
LE	\$529.76
LM	\$1,668.49
LLM	\$1,042.85
LVA	\$130.71
MES	\$1,666.41
MAL	\$542.15
MAL	\$1,842.92
MAT	\$240.00
MEF	\$861.11
MEF	\$511.04
MH	\$8,224.35
MAV	\$319.85
MMD	\$4,247.26
MS	\$255.52
MCH	\$2,525.59
MC	\$125.09
MDR	\$1,019.26
MJ	\$1,705.18
MJ	\$5,271.33
MJF	\$7,301.61
MJF	\$22,670.14
MLK	\$599.81
MLK	\$13,559.12
MS	\$6,667.72
MT	\$554.60
MT	\$2,131.68
M TRUST	\$2,873.74
MJK	\$2,123.97
NA	\$349.09
RWH	\$6,286.93
RJM	\$939.44
REC_2	\$8,441.97
REC_1	\$972.15

Attachment A
AWC No. 2015047682404

Customer Initials	Amount of Revision
RVA	\$3,305.29
HBA	\$4,037.48
RW	\$4,172.44
REM	\$207.07
RL	\$2,125.69
RDB	\$1,498.28
RDB	\$10,316.62
RA	\$321.21
RA	\$227.04
RJN	\$2,844.27
RM	\$20,815.85
SKS	\$448.48
SC	\$8,322.68
SGS	\$4,321.75
SD	\$947.04
SR	\$539.87
TPJ	\$715.39
TRO	\$141.56
TSCC	\$14,140.36
W TRUST	\$539.74
TBW	\$2,378.25
TNL	\$595.46
TNL	\$258.91
TNL	\$389.85
WH	\$7,529.41
YT	\$368.83
	<u>\$521,098.10</u>