

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER, AND CONSENT
NO. 2021071099404**

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

RE: Western International Securities, Inc. (Respondent)
Member Firm
CRD No. 39262

Pursuant to FINRA Rule 9216, Respondent Western International Securities, Inc. 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 Respondent alleging violations based on the same factual findings described in this AWC.

I.

ACCEPTANCE AND CONSENT

- A. Respondent accepts and consents to the following findings by FINRA without admitting or denying them:

BACKGROUND

Western has been a FINRA member since 1995. It is a full-service broker-dealer headquartered in Pasadena, California. It has approximately 390 registered persons located in its over 100 branch offices and its home office.

In November 2022, Western entered into an AWC with FINRA through which the firm consented to findings that (i) from 2013 to 2017, it failed to establish, maintain, and enforce a supervisory system, including written supervisory procedures, reasonably designed to achieve compliance with its suitability obligations in connection with recommendations of non-traded real estate investment trusts and (ii) between 2015 and 2022, it failed to report or timely report approximately 45 written customer complaints, customer arbitrations, and settlements. It was censured, fined \$400,000, ordered to pay restitution and partial restitution in the amount of approximately \$471,000, and required to certify that it had implemented reasonably-designed supervisory systems and procedures based on these violations of NASD Rule 3010 and FINRA Rule 3110; Article V, Sections 2(c) and 3(b) of FINRA's By-Laws and FINRA Rule 1122; and FINRA Rule 2010.

In January 2021, Western entered into an AWC with FINRA through which the firm consented to findings that from October 2018 through December 2018, it effected opening transactions in a stock option contract that resulted in a customer holding a position in the security that exceeded the applicable position limit for four consecutive

business days. Further, the firm failed to establish and maintain a supervisory system, including written supervisory procedures, that was reasonably designed to achieve compliance with option position limits requirements. It was censured and fined \$20,000 based on these violations of FINRA Rules 2360, 3110(a) and (b), and 2010.

In May 2020, Western entered into an AWC with FINRA through which the firm consented to findings that from October 2011 through June 2018, it failed to (i) timely amend the Uniform Application for Securities Industry Registration or Transfer (Form U4) for 52 registered representatives to disclose 163 liens, judgments, and/or bankruptcies totaling more than \$5.6 million and (ii) establish, maintain, and enforce a supervisory system reasonably designed to ensure the timely reporting of disclosable events. It was censured, fined \$325,000, and ordered to obtain an independent consultant based on these violations of Article V, Section 2(c) of FINRA's By-Laws; NASD Rule 3010 and FINRA Rule 3110; and FINRA Rule 2010.

In July 2019, Western entered into an AWC with FINRA through which the firm consented to findings that from January 2011 and January 2017, it failed to establish and maintain a supervisory system and procedures reasonably designed to ensure that eligible customers who purchased mutual fund shares received the benefit of applicable sales charge waivers. It was censured, fined \$75,000, and ordered to provide remediation to customers, including restitution, based on these violations of NASD Rule 3010 and FINRA Rules 3110 and 2010.¹

OVERVIEW

From January 2016 through June 2020, Western failed to establish, maintain, and enforce a supervisory system, including written supervisory procedures (WSPs), reasonably designed to achieve compliance with the suitability requirements of FINRA Rule 2111 as they pertain to excessive trading. As a result, Western failed to reasonably respond to trading in approximately one hundred accounts that appeared to be potentially excessive and unsuitable. This included trading, between January 2016 and December 2019, in nine customer accounts by four registered representatives that produced an average cost-to-equity ratio of 30%, an average turnover rate of 8, and caused those customers to pay total trading costs of more than \$2.5 million.

By this conduct, Western violated FINRA Rules 3110 and 2010.

FACTS AND VIOLATIVE CONDUCT

This matter originated from an investigation by FINRA's Department of Enforcement.

¹ For more information about the firm, including prior regulatory events, visit BrokerCheck® at www.finra.org/brokercheck.

1. Rules applicable to Western's supervision of actively traded accounts.

FINRA Rule 3110(a) requires member firms to establish and maintain a system to supervise the activities of each associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable FINRA rules. FINRA Rule 3110(b) requires a member firm to establish, maintain, and enforce written procedures to supervise the types of business in which it engages and the activities of its associated persons that are reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable FINRA rules. The duty to supervise under Rule 3110 also includes the responsibility to reasonably investigate red flags that suggest that misconduct may be occurring and to act upon the results of such investigation. A violation of FINRA Rule 3110 is also a violation of FINRA Rule 2010, which requires firms to observe high standards of commercial honor and just and equitable principles of trade in the conduct of their business.

FINRA Rule 2111(a) requires member firms and associated persons to have a reasonable basis to believe that a recommended transaction or investment strategy involving a security or securities is suitable for the customer.² During the relevant period, under FINRA Rule 2111 Supplementary Material .05(c), members and associated persons with actual or *de facto* control over an account were required to have a reasonable basis for believing that a series of recommended transactions, even if suitable when viewed in isolation, was not excessive and unsuitable for the customer in light of the customer's investment profile.

Although no single test defines excessive trading, factors such as the cost-to-equity ratio, turnover rate, and the use of in-and-out trading in a customer's account are relevant to determining whether a member firm or associated person may have excessively traded a customer's account. The cost-to-equity ratio measures the amount an account must increase in value to cover commissions and other trading expenses, or the breakeven point where a customer may begin to see a return. Turnover rate represents the number of times that a portfolio of securities is exchanged for another portfolio of securities. An annualized cost-to-equity ratio above 20% and an annualized turnover rate of six or more is each an indication that excessive trading may have occurred.

2. Western failed to establish, maintain, and enforce a supervisory system reasonably designed to supervise actively traded accounts.

From January 2016 through June 2020, Western failed to have a supervisory system that was reasonably designed to ensure compliance with applicable securities laws and regulations and with FINRA rules prohibiting excessive trading, including FINRA Rule 2111.

² FINRA Rule 2111 is still in effect, but as of June 30, 2020, it no longer applies to recommendations to retail customers that are subject to Regulation BI under the Securities Exchange Act of 1934.

Under Western's WSPs for actively traded accounts, supervisors were supposed to review daily trade blotters and monthly account statements to detect potentially excessive trading.

Western's WSPs and trade-blotter-based surveillance were not reasonably designed to detect excessive trading. The WSPs failed to provide supervisors with guidance for evaluating cost-to-equity ratios, turnover rates, or any other useful indicators of potentially excessive trading. The trade-blotter-based surveillance did not reasonably permit supervisors to incorporate any such indicators into their review.

In addition, Western's WSPs did not require supervisors to take reasonable steps to respond to any potentially excessive trading that they might identify. For example, the firm's WSPs did not require supervisors to determine or document the factual justification for recommending trading in excess of specific cost-to-equity ratios or turnover rate thresholds, to contact customers by phone or in person to confirm the suitability of even the most active trading, or to impose any discipline or heightened supervision on registered representatives in response to potentially excessive trading. Instead, supervisors were only required to notify compliance staff, who were in turn supposed to send activity letters to customers.

Western compliance staff sent activity letters to customers based on notice from supervisors and also based on their own review of certain exception reports. Until early 2019, however, the exception report reviewed by compliance staff for the vast majority of the firm's accounts did not include cost-to-equity ratios, turnover rates, or any other useful indicators of potentially excessive trading. When the firm created a new exception report that included cost-to-equity ratios and turnover rates in early 2019, the firm did not provide it to supervisors. Instead, the firm limited the use of the new report to compliance staff, who used it primarily for the ministerial task of sending activity letters when trading exceeded certain thresholds. In addition, although the new exception report used by compliance staff presented the two indicators above on a trailing twelve-month basis, it did not track other red flag trends or patterns such as, for example, rapidly-accelerating trading.

Initially, Western used so-called "negative consent" activity letters. If customers did not respond to an activity letter about the trading in their accounts, then no additional action was taken. By 2019, Western was generally requiring that customers return a signed "trading acknowledgment" in response to an activity letter. In certain situations—for example, if the customer affirmatively objected to the trading, claimed that it was unauthorized, or failed to return a signed trading acknowledgement, if one was requested—the firm was supposed to restrict the account. Otherwise, generally no additional actions were taken. Even if the firm identified new red flags of potentially excessive trading, it was Western's practice not to send more than one activity letter every six months.

Western's activity letters did not provide customers with notice explaining the firm's concerns about the trading in their account. The letters were not part of a larger system of

supervisory procedures reasonably designed to investigate red flags of potentially excessive trading, determine the relevant facts, and then take appropriate action. Under its procedures, the firm could conclude its reviews of potentially excessive trading based on customers' responses to these letters without taking additional steps to actually determine if the customers fully appreciated the trading activity. As a result, the activity letter process did not provide the firm with a reasonable basis to believe that customers fully understood the risks presented by the active trading, that customers had knowingly accepted those risks, and that the trading was otherwise suitable for them, in light of their investment profile.

In one example, by 2018, the firm had become concerned about indicia of potentially excessive trading in one of two accounts held by a senior customer. Despite its concerns, Western wrote an activity letter to this customer stating in substance only that the firm "recently reviewed your account and noted the account has been actively trading securities" and that "[i]f you are in agreement with the activity reflected on your trade confirmations and monthly account statements, please sign this letter and return it to our office." Because the customer signed and returned the letter, Western's follow-up ended there. The trading in this account continued for the next 18 months. By this point, trading in the customer's other account was producing a cost-to-equity ratio of approximately 44% and a turnover rate in excess of 12. In response, the firm sent the customer a similar activity letter. This time Western asked the customer to sign and return a firm-prepared statement that "all activity in my account are [sic] consistent with my risk tolerance," which the customer signed and returned. But the firm again took no additional actions to further review or investigate the potentially excessive trading.

Western also failed to consistently enforce its activity letter procedures. If individual compliance staff failed to send activity letters, keep track of deadlines, or restrict accounts when required, there was no failsafe. For example, a sample from the first half of 2020 showed that most compliance staff did not always record if and when an activity letter was sent and returned for a flagged account. Also, in multiple instances trading continued for a period after trading was supposed to have been restricted, in one case for more than six months.

As a result of all of the above, Western failed to reasonably review trading that appeared to be potentially excessive in approximately one hundred accounts. During the relevant period, four former Western registered representatives in particular traded excessively in certain of their customers' accounts:³

- During 2017 and 2018, a former Western registered representative excessively traded the accounts of a senior customer by directing hundreds of in-and-out trades. This registered representative recommended a series of transactions that produced a total cost-to-equity ratio of 30%. In all, this customer paid more than \$1.5 million in commissions and trading costs as a result of the trading activity.

³ These former Western registered representatives are the subjects of prior disciplinary actions.

- During 2018 and 2019, another former Western registered representative excessively traded the accounts of a senior customer after changing the customer's fee-based account to a commission-based account. This registered representative recommended a series of transactions that produced a total cost-to-equity ratio of 28%. In all, this customer paid more than \$750,000 in commissions and trading costs as a result of the trading activity.
- During 2018 and 2019, another former Western registered representative excessively traded the accounts of six customers. This registered representative directed over 3,200 trades in their accounts during this period and in one account these transactions produced a cost-to-equity ratio as high as 55% and a turnover rate exceeding 22. In all, these customers paid more than \$195,000 in commissions and trading costs as a result of the trading activity.
- During 2016 to 2019, another former Western registered representative excessively traded the account of a customer. This registered representative recommended a series of transactions that in 2019 produced a cost-to-equity ratio of 54% and a turnover rate of 12. In all, this customer paid more than \$110,000 in commissions and trading costs as a result of the trading activity.

Therefore, Western violated FINRA Rules 3110 and 2010.

B. Respondent also consents to the imposition of the following sanctions:

- a censure;
- a \$475,000 fine;
- restitution of \$1,057,632.70 plus interest as described below;⁴
- an undertaking that within 90 days of the date of the notice of acceptance of this AWC, a member of Respondent's senior management who is a registered principal of the firm shall certify in writing that, as of the date of the certification, the firm has implemented and will maintain, for not less than one year, a reasonable plan of heightened supervision for the current registered representatives identified in Attachment B to this AWC; and
- an undertaking that within 90 days of the date of the notice of acceptance of this AWC, a member of Respondent's senior management who is a registered principal of the firm shall certify in writing that, as of the date of the certification, the firm has remediated the issues identified in this AWC and implemented a supervisory system, including written supervisory procedures, reasonably designed to address the

⁴ The amount of restitution Western is required to pay has been reduced by sums that Western previously paid to affected customers.

violations described above, including identifying and responding to red flags of potentially excessive trading.

Respondent agrees to pay the monetary sanctions upon notice that this AWC has been accepted and that such payment is due and payable. Respondent has submitted an Election of Payment form showing the method by which it proposes to pay the fine imposed.

Restitution is ordered to be paid to the customers listed on Attachment A to this AWC (Eligible Customers) in the total amount of \$1,057,632.70 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 the date of each commission and trading cost until January 31, 2024.

A registered principal on behalf of Respondent shall submit satisfactory proof of payment of restitution (separately specifying the date and amount paid to each Eligible Customer) or of reasonable and documented efforts undertaken to effect restitution. Such proof shall be submitted by email to EnforcementNotice@FINRA.org from a work-related account of the registered principal of Respondent. The email must identify Respondent and the case number and include a copy of the check, money order, or other method of payment. This proof shall be provided by email to EnforcementNotice@FINRA.org no later than 60 days after the date of the notice of acceptance of the AWC.

The restitution amount plus interest to be paid to each Eligible Customer shall be treated by the Respondent as the Eligible Customer's property for purposes of state escheatment, unclaimed property, abandoned property, and similar laws. If after reasonable and documented efforts undertaken to effect restitution Respondent is unable to pay all Eligible Customers within 60 days after the date of the notice of acceptance of the AWC, Respondent shall submit to FINRA in the manner described above a list of the unpaid Eligible Customers and a description of Respondent's plan, not unacceptable to FINRA, to comply with the applicable escheatment, unclaimed property, abandoned property, or similar laws for each such Eligible Customer.

Respondent specifically and voluntarily waives any right to claim an inability to pay, now or at any time after the execution of this AWC, the monetary sanctions imposed in this matter.

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

Restitution payments to customers shall be preceded or accompanied by a letter, not unacceptable to FINRA, describing the reason for the payment and the fact that the payment is being made pursuant to a settlement with FINRA and as a term of this AWC.

Each certification that Respondent has undertaken to submit shall include a narrative description and supporting exhibits sufficient to demonstrate Respondent's compliance

with the actions that are the subject of each certification. FINRA staff may request further evidence of Respondent's compliance and Respondent agrees to provide such evidence. Respondent shall submit the certifications and these materials to Andrew Boldt, Senior Counsel (Andrew.Boldt@FINRA.org), with copies to EnforcementNotice@FINRA.org.

Upon written request showing good cause, FINRA may extend any of the procedural dates set forth above.

The sanctions imposed in this AWC shall be effective on a date set by FINRA.

II.

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 its acceptance or rejection.

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 Respondent's permanent disciplinary record and may be considered in any future action brought by FINRA or any other regulator against Respondent;
 - 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 its subject matter 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 right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party. Nothing in this provision affects Respondent's testimonial obligations in any litigation or other legal proceedings.
- 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 it 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.

The undersigned, on behalf of Respondent, certifies that a person duly authorized to act on Respondent's 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 Respondent has agreed to the AWC's provisions voluntarily; and that no offer, threat, inducement, or promise of any kind, other than the terms set forth in this AWC and the prospect of avoiding the issuance of a complaint, has been made to induce Respondent to submit this AWC.

4/15/24
Date

WIPM
Western International Securities, Inc.
Respondent

Print Name: William Morrissey

Title: President

Reviewed by:

Brian M. Feldman
Brian M. Feldman
Aurelian Law PLLC
3445 Winton Place, Suite 228
Rochester, NY 14623
*Counsel for the Special Committee
of the Board of Directors of
Western International Securities, Inc.*

Accepted by FINRA:

7/29/24
Date

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

Andrew Boldt
Andrew Boldt
Senior Counsel
FINRA
Department of Enforcement
55 West Monroe Street, Suite 2600
Chicago, Illinois 60603-5001

ATTACHMENT A
AWC No. 2021071099404

Eligible Customer	Restitution Amount
A	\$110,425.17
B	\$87,532.18
C	\$25,362.38
D	\$33,208.96
E	\$18,206.30
F	\$27,341.34
G	\$4,789.91
H	\$750,766.46
TOTAL	\$1,057,632.70

ATTACHMENT B
AWC No. 2021071099404

Individuals for Heightened Supervision
Registered Representative 1
Registered Representative 2
Registered Representative 3
Registered Representative 4
Registered Representative 5