

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. 2015045713304**

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

RE: Wells Fargo Advisors, LLC (n/k/a Wells Fargo Clearing Services, LLC), Respondent
Member Firm
CRD No. 19616

Pursuant to FINRA Rule 9216 of FINRA's Code of Procedure, Wells Fargo Advisors, LLC (n/k/a Wells Fargo Clearing Services, LLC) 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 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

Wells Fargo Advisors, LLC was a FINRA member from 1987 until November 2016, when it merged with another broker-dealer and became Wells Fargo Clearing Services, LLC, a FINRA member. Headquartered in St. Louis, Missouri, the firm engages in a general securities business. As of June 2020, the firm has approximately 25,807 registered individuals and 6,216 branch offices.

RELEVANT DISCIPLINARY HISTORY

Respondent does not have any relevant disciplinary history with the Securities and Exchange Commission, any state securities regulators, FINRA, or any other self-regulatory organization.

OVERVIEW

Between November 2012 and October 2015, two former firm representatives, Charles Frieda and Charles Lynch, recommended that many of their customers invest a

substantial portion of their assets at Wells Fargo in four high-risk energy securities.¹ The representatives' conduct generated multiple red flags regarding overconcentration in their customers' account that raised suitability concerns that Wells Fargo failed to reasonably investigate. Thus, the firm failed to reasonably supervise the activities of the two representatives, violating NASD Rule 3010(a) and FINRA Rules 3110(a) and 2010.²

FACTS AND VIOLATIVE CONDUCT

NASD Rule 3010(a) (in effect up to December 1, 2014) required each member firm to “establish and maintain a system to supervise the activities of each registered representative . . . that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable NASD Rules.” FINRA Rule 3110(a), which became effective on December 1, 2014, is substantively identical to NASD Rule 3010(a).³ A firm's duty to supervise its registered representatives under both Rules includes the responsibility to reasonably investigate “red flags” of potential misconduct by registered representatives.

Between November 2012 and October 2015, Frieda and Lynch recommended that many of their customers invest a substantial portion of their assets at Wells Fargo in the four high-risk energy securities, including one low-priced security. For example, the representatives' recommendations resulted in a 38-year-old customer holding 92.4% of her total household account value in these four securities and a 54-year-old customer holding 55.7% of her total household account value in these securities. The two representatives sold approximately \$46 million of these securities to their customers, representing about half of their overall sales.

Frieda and Lynch exacerbated risk of investing in these securities by recommending that customers purchase shares of other energy securities. In many instances, their customers' investments in energy-sector securities exceeded 50% of their liquid net worth.

Because of Frieda and Lynch's recommendations, 70 of their customers lost a total of more than \$10 million when prices of energy securities prices plummeted in 2014 and 2015.

Wells Fargo compensated 67 Frieda and Lynch customers more than \$9.7 million based on losses related to these four securities. Three customers were not compensated, and the firm will provide restitution to them pursuant to this AWC.

¹ The firm terminated Lynch in May 2016 and Frieda in September 2017. In December 2017, Frieda and Lynch signed AWCs barring them for making unsuitable recommendations that their customers concentrate in energy securities, in violation of FINRA Rules 2111 and 2010.

² FINRA Rule 3110 superseded NASD Rule 3010 in 2014.

³ FINRA Rule 2010 requires FINRA member firms to observe high standards of commercial honor and just and equitable principles of trade. Conduct that violates NASD Rule 3010(a) or FINRA Rule 3110(a) also violates FINRA Rule 2010.

The Firm Did Not Reasonably Investigate Red Flags Arising From the Representatives' Recommendations

Wells Fargo had multiple red flags about overconcentration in Frieda and Lynch's customers' accounts that raised suitability concerns. Yet, Wells Fargo failed to reasonably investigate certain of these red flags. Between September 2013 and April 2014, the firm's trade-review system issued 28 alerts that four customers of the representatives were concentrated in the same low-priced, energy security. The alerts noted concentration levels ranging between 35.18% and 86.95% for these accounts, which was above the firm's threshold for triggering a security concentration alert.

Although the firm was aware that the representatives were recommending that certain of their customers concentrate in energy securities and these alerts raised red flags regarding the customers' concentrations, specifically in a low-priced security, Wells Fargo failed to reasonably investigate certain of these alerts. The firm's written supervisory procedures (WSPs) addressed how to investigate these alerts, but the firm did not follow its procedures in responding to them. The WSPs advised that accounts with high concentrations in a few securities, a sector, or industry have an increased risk of loss, and thus required a detailed review. Specifically, the WSPs required reviewers to: (1) look for any trends of concentration issues in other accounts serviced by the account's representative; (2) review the representative's suitability determination, which the WSPs say the representative "should document"; and (3) consider client contact. But the firm did not review the representatives' other customer accounts for concentration trends, and in certain instances, did not consider contacting customers despite the number of alerts or concerns about whether the customers were aware of the risks associated with concentration. Rather, it resolved alerts based on the representatives' uncorroborated assurances that their customers were aware of the concentrations in their accounts.

In addition, the firm was aware that Frieda and Lynch had not documented the concentration-suitability determination for certain customers, as the firm's WSPs required, raising a concern regarding the underlying suitability of their recommendations.

The firm knew, but did not investigate, that Frieda and Lynch were moving energy securities from customers' advisory accounts into brokerage accounts to avoid the firm's concentration limits in advisory accounts. This attempt to circumvent the firm's own limits was a red flag that the representatives might be unsuitably overconcentrating customer accounts in energy securities.

The firm's WSPs required a daily blotter review to detect "unusual trading activity or patterns" and "[c]oncentration." The trade blotters for Frieda and Lynch consistently evidenced that they were effecting a high volume of sales of the four high-risk energy securities in certain of their customers' accounts. Yet the firm failed to follow-up on this red flag concerning the representatives' trading.

By virtue of the foregoing, Wells Fargo violated NASD Rule 3010(a) and FINRA Rules 3110(a) and 2010.

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

- a censure;
- a fine of \$350,000; and
- restitution to the customers listed on Attachment A in the total amount of \$201,498, plus interest as further described below.

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

Respondent specifically and voluntarily waives any right to claim an inability to pay, now or at any time hereafter, the monetary sanction imposed in this matter.

Restitution is ordered to be paid to the customers listed on Attachment A hereto in the total amount of \$201,498, 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 October 31, 2015, until the date this AWC is accepted by the National Adjudicatory Council (NAC).

A registered principal on behalf of the firm shall submit satisfactory proof of payment of restitution and pre-judgment interest (separately specifying the date and amount of each paid to each customer listed on Attachment A) 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 the firm. The email must identify the firm 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 120 days after acceptance of the AWC.

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

Restitution payments to customers shall be preceded or accompanied by a letter, not unacceptable to FINRA staff, 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.

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

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 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 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 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 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 or its staff.

The undersigned, on behalf of the Respondent 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 it 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 herein and the prospect of avoiding the issuance of a Complaint, has been made to induce it to submit it.

August 27, 2020

Date

Wells Fargo Clearing Services, LLC
Respondent

By: Jim Hays

Print Name: Jim Hays

Title: CEO wells Fargo Advisors

Reviewed by:

Brian L. Rubin

Brian Rubin, Esq.
Counsel for Respondent
Eversheds Sutherland (US) LLP
700 Sixth Street, NW
Suite 700
Washington, DC 20001

Accepted by FINRA:

August 28, 2020

Date

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

Mitka Baker

Mitka Baker
Senior Counsel
FINRA
Department of Enforcement
15200 Omega Drive
Third Floor
Rockville, MD 20850



ATTACHMENT A

1. Customer 1 – \$84,964
2. Customer 2 – \$94,725
3. Customer 3 – \$21,809