

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. 2010022918701**

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

RE: RBC Capital Markets, LLC, Respondent
CRD No. 31194

Pursuant to FINRA Rule 9216 of FINRA’s Code of Procedure, RBC Capital Markets, LLC (“RBC”, “Respondent”, 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 RBC alleging violations based on the same factual findings described herein.

I.

ACCEPTANCE AND CONSENT

- A. RBC 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

RBC has been a FINRA registered broker-dealer since 1993¹ and maintains its principal place of business in New York, NY. The Firm is indirectly owned by the Royal Bank of Canada, which is a publicly listed company on the New York Stock Exchange. The Firm has two main lines of business, a Capital Markets division, which engages in dealing, underwriting, and customer facilitation activities, and a Wealth Management division, which provides private client, asset management, and correspondent brokerage services. The Firm operates approximately 280 branches and has approximately 5,300 registered representatives.

RELEVANT DISCIPLINARY HISTORY

The Firm’s relevant disciplinary history is as follows:

¹ On March 3, 2008, RBC Dain Rauscher Inc. merged with its affiliate, RBC Capital Markets Corporation. In connection with this merger, RBC Dain Rauscher Inc., CRD No. 31194, was renamed RBC Capital Markets Corporation. The name was later amended to RBC Capital Markets, LLC.

- RBC consented to findings that it violated NASD Rules 3010 and 2110 and FINRA Rule 2010 by failing to establish a supervisory system reasonably designed to ensure compliance with its own guidelines and FINRA Rule 2440 regarding permissible markups and markdowns for its Collateralized Mortgage Obligations (“CMO”). Consequently, in 234 CMO transactions with mostly retail customers, the Firm charged markups and markdowns as high as 16.9%. The Firm consented to a sanction consisting of a censure and a \$25,000 fine. *See RBC Capital Markets LLC, Matter No. 200902094501 (AWC, December 2011).*
- RBC consented to findings that it violated Section 5 of the 1933 Securities Act and NASD Rules 3010 and 2110 by executing customer sale orders for more than two billion unregistered shares and eight issuers and by failing to establish, maintain and enforce a system to supervise the activities of its associated persons that was reasonably designed to detect and prevent customers’ sales of more than two billion shares of unregistered securities. The Firm consented to a sanction consisting of a censure and a \$135,000 fine. *See RBC Capital Markets LLC, Matter No. 20090205457 (AWC, December 2009).*

OVERVIEW

Between 2008 and 2012 (the “Relevant Period”), RBC failed to have in place supervisory systems and procedures reasonably designed to ensure compliance with applicable securities laws and regulations and its internal guidelines concerning the suitability of reverse convertibles. The Firm’s supervisory system and procedures did not adequately identify transactions for responsible supervisory personnel when reverse convertibles were sold to customers in violation of the Firm’s suitability guidelines, including those related to customer investment objectives, annual income, net worth and liquid net worth. Consequently, during the Relevant Period, RBC supervisors failed to detect the sale by 99 of its registered representatives of approximately 364 reverse convertible transactions in approximately 218 customer accounts that were unsuitable for those customers. These customers incurred losses totaling at least \$1.1 million.

Accordingly, the Firm violated NASD Rules 3010(a), 2310 and 2110 and FINRA Rule 2010.

FACTS AND VIOLATIVE CONDUCT

Structured products are debt securities derived from or based on a single security, a basket of securities, an index, a commodity, a debt issuance and/or a foreign currency. Structured products typically have two components -- a note and a derivative (often an option). There are many types of structured products. Some structured products offer full protection on the principal invested, whereas others offer limited or no principal protection. Many structured products pay an interest or coupon rate substantially above the prevailing market rate. Structured products also frequently cap or limit the upside participation in the reference asset, particularly if some principal protection is offered or if the security pays an above-market rate of interest.

Reverse convertibles, a complex structured product, are interest-bearing notes in which principal repayment is linked to the performance of a reference asset, often a stock, a basket of stocks or an index. The reference asset is generally unrelated to the issuer of the note. At maturity, if the

value of the reference asset has fallen below a certain level (the “knock-in level”), the investor may receive less than a full return of principal. The diminished principal repayment could be in the form of shares of stock put to the investor or their cash equivalent. Reverse convertibles expose investors not only to the risks traditionally associated with fixed income products, such as issuer risk, but also to the risks of a decline in value in the underlying reference asset, which can lead to loss of principal. Reverse convertibles tend to have limited liquidity and complex payout structures that can make it difficult for registered representatives and their customers to accurately assess their risks, costs, and potential benefits.

Regulatory Guidance

Reverse convertibles are not suitable for every customer and FINRA Notices to Members (“NTM”) regarding structured products generally and reverse convertibles in particular have set forth guidance to the membership regarding their sale. FINRA issued NTM 05-59 as a result of concerns that broker dealers were deficient in fulfilling sales practice obligations when selling structured products, particularly to retail customers. The Notice advised that some structured products present risks similar to that of options and that FINRA members should develop procedures to ensure that the structured products sold to investors matched those investors’ appetite for risk. FINRA reminded firms to perform a reasonable suitability determination on a structured product before recommending the product, as well as a customer specific suitability determination. FINRA also instructed firms that they must train brokers and their supervisors about each type of structured product before the brokers sell the product to investors.

In February 2010, FINRA issued NTM 10-09 that is specific to reverse convertibles and reiterates the need for firms to perform reasonable basis suitability as well as customer specific suitability analyses in connection with the sales of reverse convertibles. The Notice directs firms to make “reasonable efforts to obtain information concerning: (1) the customer's financial status; (2) the customer's tax status; (3) the customer's investment objectives; and (4) such other information used or considered to be reasonable by such member or registered representative in making recommendations to the customer.” In sum, NTM 10-09 seeks to ensure that “[reverse convertibles] are only sold to persons for whom the risk of such products is appropriate.”

The Firm Failed to Establish Reasonable Systems and Procedures to Supervise Sales of Reverse Convertibles

NASD Rule 3010(a) requires members to, among other things, “establish and maintain a system to supervise the activities of each registered representative, registered principal, and other associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable NASD Rules. Final responsibility for supervision shall rest with the member.”

As noted above, NTM 10-09 requires FINRA registered firms that sell reverse convertibles to “have adequate [and reasonably-designed] written supervisory procedures and supervisory controls...to ensure that sales of... [reverse convertibles] comply with federal securities laws and FINRA rules.”

Both NASD Rule 2110 and FINRA Rule 2010 provide that “[a] member, in the conduct of its business, shall observe high standards of commercial honor and just and equitable principles of trade.” Violations of federal securities laws and NASD rules are viewed as violations of NASD Rule 2110 because members of the securities industry are expected and required to abide by the applicable rules and regulations.¹

During the Relevant Period the Firm offered at least 3,000 different reverse convertible products to its customers. The Firm effected through approximately 360 of its registered representatives in excess of 100,000 reverse convertible transactions in at least 5,000 customer accounts during the Relevant Period.

However, during the Relevant Period RBC did not have in place systems and procedures reasonably designed to ensure compliance with applicable securities laws and regulations, NASD/FINRA Rules and its own written supervisory procedures (“WSPs”) in connection with its sale of reverse convertibles.

The Firm’s WSPs for structured product sales set forth suitability requirements and guidelines for sales of reverse convertibles that addressed customer investment objectives and financial profiles as well as requirements for registered representative training. The WSPs prohibited the sale of reverse convertibles to any customer that listed his or her investment objective as “Preservation of Principal/Income.”

Additionally, the applicable WSPs established suitability guidelines for the sale of reverse convertibles pursuant to which investors were expected to have the following profile: (a) \$100,000 annual income; (b) \$100,000 in liquid assets; (c) \$250,000 net worth (collectively, the “Financial Criteria”); and (d) two years of prior investment experience.²

The Firm’s WSPs further required registered representatives to complete a web-based structured products training module prior to soliciting sales of structured products.

However, the Firm lacked reasonable systems to ensure that its WSPs for sales of reverse convertibles were followed by RBC registered representatives who sold this product to their retail customers.

Unreasonably Designed Surveillance Systems

The Firm provided its managers with an electronic transaction surveillance system called ProSurv to review all trading activity, including reverse convertible transactions. ProSurv, however, did not generate reports unique to reverse convertible transactions or that measured reverse convertible transactions against applicable requirements and guidelines. For example, ProSurv did not flag reverse convertible transactions where a customer’s annual income, liquid

¹ FINRA Rule 2010 superseded NASD Rule 2110 effective December 15, 2008.

² Until February 2009, the Firm’s WSPs indicated that structured products investors “must” meet the Financial Criteria. Thereafter, the WSPs indicated that structured products investors “should” meet the Financial Criteria.

assets, net worth or investment objective was inconsistent with the requirements and guidelines of the Firm's applicable WSPs. These limitations of the ProSurv system in reviewing reverse convertible transactions continued through the remainder of the Relevant Period and until early 2013. Thus, for a period of at least five years the Firm's electronic surveillance systems did not review transactions for compliance with the requirements and guidelines of its WSPs applicable to reverse convertibles.

Unreasonably Designed and Implemented Exception Reports

Prior to June 2008, the Firm generated and distributed reverse convertible-related exception reports to Complex Directors only sporadically on an "as needed" basis as requested by individual Complex Directors¹ and without the Firm's guidance or direction.

Thereafter, in January 2009, the Firm began issuing to the Firm's Complex Directors a quarterly exception report for reverse convertible transactions (the "Quarterly Report"). However, the Quarterly Report was also an ineffective supervisory tool given that it was created and reviewed only after the transactions had been effected. In addition, this report was issued only on a quarterly basis, thereby allowing potentially non-compliant transactions to remain in effect without review for up to three months after they were effected.

Additionally, the Firm lacked any written escalation procedures requiring notification and/or consultation with the Firm's compliance department when potentially violative transactions were identified.

During the Relevant Period, the Firm effected at least 237 reverse convertible transactions where the customer had an investment objective of Preservation of Principal/Income. In addition, from January 1, 2008 through December 31, 2010, of the 9,200 reverse convertible transactions where the stock hit the knock-in level at or about the time of maturity, more than 5,600 reverse convertible transactions failed to meet one or more of the three Financial Criteria, with at least 127 reverse convertible transactions failing to meet all three criteria. Each of these referenced transactions was effected in violation of the Firm's WSPs without being detected by the Firm's applicable supervisory systems and procedures or being identified as violative by the Firm's supervisory personnel.

The foregoing is demonstrative of the Firm's failure to implement a reasonable system of follow-up and review to ensure that it sold reverse convertibles only to those customers for whom the product was suitable. Specifically, the Firm failed to ensure that it implemented reasonably designed systems and procedures to flag for its supervisory personnel potentially unsuitable transactions in reverse convertibles and ensure that its registered persons were adequately trained regarding the risks associated with reverse convertibles and the customers for whom such investments were suitable.

By the foregoing, the Firm violated NASD Rules 3010 and 2110 and FINRA Rule 2010.

¹ A Complex was composed of various branch offices established in an identified geographical area. The Firm had approximately 35 Complexes during the Relevant Period. Complex Directors had primary responsibility to review all trading activity occurring within their Complexes.

Unsuitable Reverse Convertible Transactions

NASD Rule 2310(a) requires that, in recommending the purchase, sale or exchange of any security, a member have a reasonable basis for believing that the recommendation is suitable for a customer based upon the customer's financial situation and needs. NASD Rule 2310(b) also requires that prior to the execution of a transaction, a member make reasonable efforts to obtain information concerning a customer's financial status.

Structured products generally and reverse convertibles in particular are not suitable for every customer and FINRA NTMs have provided guidance to members regarding the parameters for suitability as noted above. As noted above, FINRA NTM 05-59, in effect during the Relevant Period provides guidance on member obligations when selling structured products. These include the requirements to: (1) ascertain accounts eligible to purchase structured products; (2) perform a reasonable-basis suitability determination; (3) perform a customer specific suitability determination; (4) supervise and maintain a supervisory control system; and (5) train associated persons. Further, FINRA recognized in NTM 10-09 the unique nature of reverse convertibles and directed firms to perform a reasonable basis, as well as customer specific suitability analysis, for each recommended reverse convertible purchase in order to ensure that "[reverse convertibles] are only sold to persons for whom the risk of such products is appropriate."

From January 1, 2008 through December 31, 2010, of all the reverse convertible sales where the stock price dropped below the knock-in level at or about the time of maturity, 127 were recommended and sold by RBC in 100 customer accounts that listed an annual income below \$100,000, liquid assets of less than \$100,000 and a net worth below \$250,000. In addition, from January 1, 2008 through December 31, 2012, RBC permitted its registered representatives to recommend and sell 237 unsuitable reverse convertibles in more than 100 customer accounts that listed the conservative investment objective of "Preservation of Principal/ Income." Losses incurred by these customers totaled at least \$1.1 million.

Given the nature of the reverse convertible product, these transactions exposed the referenced customers to a risk of loss that was inconsistent with their risk tolerance, investment objectives and financial status and RBC did not have reasonable grounds to believe that the recommendation and sale of reverse convertibles were suitable for these customers. Moreover, the guidelines articulated in the Firm's own WSPs establish that reverse convertibles should not have been sold to these customers.

By virtue of the forgoing conduct, RBC violated NASD Rules 2310 and 2110 and FINRA Rule 2010.

- B. The Firm also consents to the imposition of the following sanctions:
 - a. A censure;
 - b. A fine in the amount of \$ 1 million; and

c. Restitution in the amount of \$433,898.10.¹

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

RBC specifically and voluntarily waives any right to claim that it is unable to pay, now or at any time hereafter, the monetary sanction(s) imposed in this matter.

Restitution is ordered to be paid to the customers listed on Attachment A hereto in the total amount of \$433,898.10, 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 respective dates indicated, until the date this AWC is accepted by the NAC.

A registered principal on behalf of Respondent firm shall submit satisfactory proof of payment of restitution or of reasonable and documented efforts undertaken to effect restitution. Such proof shall be submitted to Josefina Martinez at One World Financial Center, 200 Liberty Street, New York, NY 10281 either by letter that identifies the Respondent and the case number or by e-mail from a work-related account of the registered principal of Respondent firm 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 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 the FINRA staff member identified above and in the manner described above, within 14 days of forwarding the undistributed restitution and interest to the appropriate state authority.

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

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.

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

¹ The Firm made payments to more than 100 of customers pursuant to the settlement of a class action law suit brought against the Firm in the Superior Court of the State of California, County of Los Angeles. Enforcement will not require the payment of restitution to those customers that received a payout pursuant to the settlement of that lawsuit.

II.

WAIVER OF PROCEDURAL RIGHTS

RBC 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, RBC specifically and voluntarily waives any right to claim bias or prejudice of the General Counsel, 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.

RBC further specifically and voluntarily waive 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

RBC 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 RBC; and

C. If accepted:

1. this AWC will become part of RBC's permanent disciplinary record and may be considered in any future actions brought by FINRA or any other regulator against the Firm;
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. RBC 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. RBC 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 the Firm'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. RBC may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. RBC 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 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 RBC 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 RBC to submit it.

February 27, 2015
Date: _____, 2015

Daniel L. Turberson
RBC Capital Markets, LLC

Reviewed by:
E. S. Seltzer
Eric S. Seltzer
Counsel for Respondent
Sidley Austin LLP
85 Exchange Street
Portland, ME 04101
(207) 780-8272

By: Daniel L. Turberson
General Counsel, ABC Wealth
Management, a division of
RBC Capital Markets, LLC

Accepted by FINRA:

April 23 2015
Date

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

Susan Light
Susan Light
Senior Vice President & Chief Counsel
FINRA Department of Enforcement
One World Financial Center
200 Liberty Street
New York, NY 10281
(646) 315-7333