FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER, AND CONSENT
NO. 2019061765001

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

RE: Securities America, Inc., Respondent
Member Firm
CRD No. 10205

Pursuant to FINRA Rule 9216, Respondent Securities America, 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 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

Securities America, Inc. (SAI), which became a FINRA member firm in 1981, is a full-service broker-dealer. The firm, which operates on an independent contractor model, is headquartered in La Vista, Nebraska. SAI has approximately 4,200 registered representatives and 2,400 branch offices throughout the United States. The firm does not have any relevant disciplinary history.

OVERVIEW

Between August 17, 2016, and February 8, 2018, SAI failed to reasonably supervise representatives' recommendations of an alternative mutual fund—the LJM Preservation & Growth Fund (LJM).[1] SAI permitted the sale of LJM on its platform without conducting reasonable due diligence and without a sufficient understanding of its risks and features, including the fact that the fund pursued a risky strategy that relied, in part, on purchasing uncovered options. SAI also lacked a reasonable supervisory system to

[1] Ticker symbols were LJMIX, LJMCX and LJMAX.

review representatives' LJM recommendations. SAI representatives sold more than $616,000 in LJM to thirty-three customers. LJM's value dropped 80% during an extreme volatility event in February 2018 and the fund ultimately liquidated and closed, resulting in hundreds of thousands in losses for SAI's customers. By virtue of the foregoing, SAI violated FINRA Rules 3110 and 2010.

FACTS AND VIOLATIVE CONDUCT

This matter originated from FINRA's 2019 investigation of firms that sold LJM to retail customers.

Alternative Mutual Funds

Alternative mutual funds are publicly-offered mutual funds that seek to accomplish the funds' objectives through non-traditional investments and trading strategies. In its 2015 National Examination Priorities Letter, FINRA described the features of alternative mutual funds:

> Alternative mutual funds are often marketed as a way for retail customers to invest in sophisticated, actively-managed hedge fund-like strategies that will perform well in a variety of market environments. Alternative mutual funds generally purport to reduce volatility, increase diversification, and produce non-correlated returns and higher yields compared to traditional long-only equity and fixed-income funds, all while offering daily liquidity."[2]

In the same letter, FINRA identified alternative mutual funds as an area of review and noted concerns regarding firms' supervision and sale of such funds:

> Despite their possible benefits, alternative mutual funds raise concerns when compared to conventional funds. In particular, FINRA is concerned that registered representatives and customers will not understand how the funds will respond to various market conditions or even the strategy in which the fund's adviser will engage in various market scenarios. In addition, FINRA has learned that some firms are not reviewing alt funds through their new-product review process, especially if the firm already has an existing agreement with the fund company.

Previously, FINRA issued Regulatory Notices highlighting the risks of "complex products," such as alternative mutual funds, and stressing the need for firms and their

[2] 2015 FINRA Regulatory and Examination Priorities Letter (January 6, 2015) ("2015 Exam Priorities Letter").

representatives to understand their unique risks and features before recommending them, particularly to retail customers.[3]

LJM and the Risks of an Uncovered Options Strategy

LJM was an alternative mutual fund that launched on January 9, 2013. LJM marketed itself as "selling volatility" by seeking to profit from the "volatility premium"—the difference between implied volatility (investors' forecast of market volatility reflected in options pricing) and realized (actual) market volatility. To achieve this goal, LJM invested primarily in purchased (long) and sold (short) call and put options on the S&P 500 futures index. LJM did not hold any underlying stock as a part of its strategy.

In its prospectus, LJM disclosed that "[i]n the aggregate, the Fund is typically 'net short' in the portfolio of contracts that it holds, which means the Fund holds more uncovered option contracts than covered." The prospectus also disclosed the limited upside, and unlimited downside, risk associated with uncovered options.

The fact that LJM was typically "net short" or "short volatility" was also disclosed in various informational and marketing materials provided, or available, to registered representatives and their firms. This material disclosed that there were certain markets in which LJM was designed to do well, namely: (i) flat, (ii) choppy, (iii) eroding, or (iv) slowing rising or falling markets. Conversely, LJM disclosed that there were other markets in which its strategy would be "challenged," namely: (i) sustained upward-trending equity markets, (ii) quick reversals, or (iii) extreme volatility spikes or market moves. LJM employed a risk mitigation strategy through the use of put option spreads that was intended to mitigate the risks associated with the challenging markets, including major market downturns. However, LJM disclosed in its prospectus that "there can be no assurance that the Fund's risk mitigation strategies will reduce risk or will be either available or cost effective."

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[3] In January 2012, FINRA issued Regulatory Notice 12-03 regarding supervisory procedures governing "complex products." In it, FINRA provided guidance to firms on the characteristics of complex products:

> Any product with multiple features that affect its investment returns differently under various scenarios is potentially complex. This is particularly true if it would be unreasonable to expect an average retail investor to discern the existence of these features and to understand the basic manner in which these features interact to produce an investment return.

FINRA provided several examples of complex products, including "exchange-traded products [that] offer retail investors exposure to stock market volatility. … The investable form of volatility may be in the form of futures on the CBOE Volatility Index (VIX) that reflect the market's expectation of volatility." FINRA stated that "complex" products present additional risk to retail investors.

Similarly, in June 2013, FINRA issued an Investor Alert, "Alternative Funds Are Not Your Typical Mutual Funds," noting among other things: (1) in addition to the usual market and investment specific risks mutual funds have, alternative mutual funds carry additional risks from the strategies they use; and (2) many alternative mutual funds have limited performance histories, making it difficult to predict how they will perform in various market conditions, including downturns.

In July 2017, Morningstar issued a Fund Report for LJM that described the fund as "[a]n aggressive option seller with above-average returns and low correlation with equity markets, but high risk." The Report further stated that "[t]he strategy is structured to generate high income but is relatively aggressive and exposed to a steep rise in equity volatility. Even though these volatility spikes and periods of heightened uncertainty are infrequent, they could have significant, negative impact on this fund's future performance."

The Firm Did Not Have a Reasonably Designed Supervisory System with Respect to the Recommendation of Alternative Mutual Funds.

FINRA Rule 3110 sets forth FINRA members' supervisory obligations. Subsection (a) requires that each member shall 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 NASD and FINRA Rules. Subsection (b) requires that each member shall 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 the applicable NASD and FINRA Rules. Violations of FINRA Rule 3110 also constitute violations of FINRA Rule 2010.

FINRA Rule 2111 requires:

> a member or associated person to have a reasonable basis to believe, based on reasonable diligence, that the recommendation is suitable for at least some investors. In general, what constitutes reasonable diligence will vary depending on, among other things, the complexity of and risks associated with the security or investment strategy and the member's or associated person's familiarity with the security or investment strategy. A member's or associated person's reasonable diligence must provide the member or associated person with an understanding of the potential risks and rewards associated with the recommended security or strategy. The lack of such an understanding when recommending a security or strategy violates the suitability rule.[4]

SAI's supervision of its representatives' recommendations of alternative mutual funds was not reasonable in several respects.

First, although the firm had a system for identifying new mutual funds as alternative mutual funds, this system did not result in any heightened review of the fund's strategy, its risks, or its suitability for particular classes of investors. Instead, the firm only required alternative mutual funds to have more assets under management, longer

[4] FINRA Rule 2111.05(a) (Supplementary Material to Rule 2111).

operating histories, and lower expense ratios than ordinary mutual funds. If the alternative fund met these thresholds, then the firm approved it for sale without any additional due diligence.

Second, the firm did not provide reasonable guidance or training to representatives regarding the risks and features of alternative mutual funds and did not have written supervisory procedures advising firm principals how to supervise recommendations of alternative mutual funds. While representatives were required to take special trainings for specific products or categories of alternative investment products prior to selling those products, there was no such required training for LJM at SAI. Similarly, there was no required training for principals regarding alternative mutual funds such as LJM.

Third, the firm utilized an electronic trade review system to assist with the supervision of the trading activity of the firm's financial professionals. However, the firm failed to consider whether the rules of the review system pertaining to traditional mutual funds were reasonable for use in reviewing alternative mutual funds that utilize a more complex strategy, such as LJM, or whether it may be necessary to tailor the tool's rules to address particular risks and characteristics of alternative mutual funds, including LJM. As a result, SAI's LJM transactions were generally not identified for additional suitability review.[5]

SAI approved LJM on its platform in August 2016. SAI followed its review process for alternative mutual funds and did not review LJM's investment and trading strategy. The firm did not impose any limitations on the sale of LJM. SAI's first sale of LJM occurred on August 17, 2016, and the last occurred on February 7, 2018. During that time, one SAI representative sold approximately $616,045 in shares of LJM to thirty-three customers.

On February 5, 2018, the S&P 500 fell 113 points (around 4.1%), which contributed to an unprecedented increase in market volatility, as measured by the CBOE Volatility Index (VIX). On February 5, 2018, the VIX more than doubled from 17 to 37, which at that time was the largest one day rise in its history. As a result of the market's increased volatility, the prices of the short option positions sold by LJM increased dramatically. On February 5 and 6, 2018, LJM lost about 80% of its value. On February 7, LJM announced that it was closing itself to new investors, and on March 29, 2018, LJM was liquidated and dissolved. Investors who held shares as of February 6, 2018 lost approximately 80% of their investment.

Based on the above, SAI violated FINRA Rules 3110 and 2010.

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

- a censure;

[5] SAI's transaction review system applied additional rules for products it deemed "alternative," but the firm determined that LJM was not subject to heightened review for transactions in alternative investments.

- a certification signed by an officer and registered principal of the firm that, as of the date of the certification, SAI has established and implemented policies, procedures, and internal controls reasonably designed to address and remediate the issues;

- a $100,000 fine; and

- restitution of $235,979.77 plus interest as described below.

Respondent agrees to pay the monetary sanction 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.

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 sanction imposed in this matter.

Within 90 days of Notice of Acceptance of this AWC, SAI shall certify to FINRA in a submission signed by an officer and registered principal of the firm that, as of the date of the certification, SAI has established and implemented policies, procedures, and internal controls reasonably designed to address and remediate the issues identified in this AWC. The certification shall be addressed to Miki Tesija, Senior Counsel, 55 W. Monroe St., Ste. 2700, Chicago, Illinois, 60603. Upon written request showing good cause, FINRA staff may extend the procedural date set forth above.

Restitution is ordered to be paid to the customers listed on Attachment A to this AWC in the total amount of $235,979.77, 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 March 29, 2018 until November 27, 2018.

A registered principal on behalf of Respondent shall submit satisfactory proof of payment of restitution and prejudgment 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 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 120 days after the date of the notice of 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 after the date of the notice of acceptance of the AWC, or such additional period agreed to by FINRA 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 FINRA 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 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.

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 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 testimonial obligations or 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.

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.

2/26/21
Date

Securities America, Inc.
Respondent

Print Name: Dori Hammond

Title: Interim Chief Compliance Officer

Reviewed by:

Gregory M. Curley
Counsel for Respondent
Senior Litigation Counsel
Advisor Group
10 Exchange Place, Suite 1410
Jersey City, NJ 07302

Accepted by FINRA:

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

March 29, 2021
Date

Sean Heikkila
Counsel
FINRA Department of Enforcement
Brookfield Place
200 Liberty Street
New York, New York 10281
(212) 416-1756

ATTACHMENT A

SCHEDULE OF RESTITUTION

Account #	Restitution Amount (Exclusive of Interest)
*1292	$8,229.46
*1931	$12,438.60
*8081	$8,287.89
*3970	$20,604.18
*0176	$8,227.83
*2470	$12,438.60
*5708	$8,151.46
*3146	$16,436.55
*8653	$4,152.38
*5089	$16,485.20
*6922	$40,275.04
*7422	$6,570.28
*8585	$8,161.42
*9412	$6,865.28
*4708	$19,538.79
*1613	$5,525.85
*6990	$9,880.65
*6380	$5,146.15
*9259	$2,784.31
*5858	$9,914.06
*2781	$4,662.82
*1190	$1,202.95
Total	**$235,979.77**