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Wells to pay $2M to settle claims broker sold unsuitable investments to seniors

Finra alleged that a broker bought reverse convertible notes for 21 mostly elderly customers

By Liz Skinner

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Wells Fargo Advisors has agreed to pay a $2 million fine to settle regulator allegations that a former broker bilked more than 20 elderly clients by selling them unsuitable investments that generated more than $1 million in commissions for him and losses for many investors.

The firm, known as Wells Fargo Investments LLC before merging with Wachovia Securities LLC in March, also agreed to repay an unspecified amount to clients for losses caused by that broker and, in an unrelated charge, for not giving certain customers a volume discount that they were due.

The Financial Industry Regulatory Authority Inc. alleged that Wells Fargo representative Alfred Chi Chen bought reverse convertible notes for 21 customers, none of whom had ever invested in such a complex product, and most of whom were retired, including many investors in their 80s and 90s.

He built up the concentration of these investments within customers' accounts until most had nearly all their assets in reverse convertible notes, Finra said in its separate complaint against Mr. Chen. The transactions from January 2006 through July 2008 helped him become the firm's highest RCN producer in 2008, the self-regulator said.

In April 2007, Mr. Chen was promoted to senior financial consultant, according to the Finra complaint.

The broker also made trades in the accounts of two dead customers and bought $75,000 worth of the complex structured notes for another customer who specifically told him not to buy anything because she needed the funds in her account to pay quarterly taxes, Finra said.

In July 2008, Wells Fargo told Mr. Chen to reduce his customers' concentrations in the reverse convertible notes, and it fired him four months later after he had worked for the firm for eight years, according to Finra.

In addition to not sufficiently supervising him, Wells Fargo failed to give certain customers who purchased unit investment trusts appropriate discounts on transactions that exceeded certain thresholds between January 2006 and July 2008, the Finra complaint against Wells Fargo said.

Both the firm's breaches were “serious failings that harmed investors,” said Brad Bennett, Finra's enforcement chief.

Wells Fargo neither admitted nor denied the allegations in settling the complaint.

“The issue involves conduct at a legacy firm which has been merged into Wells Fargo Advisors,” the firm said in a statement. “Wells Fargo Advisors will continue to support the processes and procedures in place to prevent this kind of activity from happening.”

Finra is asking for Mr. Chen, who didn't return a phone call or e-mail seeking comment, to return his ill-gotten gains with interest.

Reverse convertible notes are structured products that usually consist of a high-yield, short-term note of the issuer that is linked to the performance of an unrelated asset, which can be a single stock or a basket of equities such as an index.

In this case, the notes were mostly linked to single equities and sold by ABN Amro Bank NV, Barclays PLC and Wells Fargo Bank NA, Finra said.

Wells Fargo To Pay Over $2.7 Million ETF Fine and Restitution

Bill Singer, Contributor 5/01/2012

For the purpose of proposing a settlement of rule violations alleged by the Financial Industry Regulatory Authority (“FINRA”), without admitting or denying the findings, prior to a regulatory hearing, and without an adjudication of any issue, Wells Fargo Advisors, LLC, Wells Fargo Advisors Financial Network, LLC and Wells Fargo Investments, LLC (collectively “Wells Fargo,”) submitted a Letter of Acceptance, Waiver and Consent (“AWC”), which FINRA accepted. In the Matter Wells Fargo Advisors, LLC et al.., *Respondent* (AWC 20090191139**,** May 1, 2012).

Wells Fargo is the retail brokerage and wealth management affiliate of Wells Fargo & Company, headquartered in St. Louis, Missouri. On December 31, 2008, Wells Fargo & Company acquired Wachovia Corporation and its affiliated brokerage businesses, including Wachovia Securities. Wachovia Securities changed its name to Wells Fargo Advisors on May 1, 2009 and Wells Fargo

July 2009 FINRA ETF Notice

As described in “**Non-Traditional ETFs**: *FINRA Reminds Firms of Sales Practice Obligations Relating to Leveraged and Inverse Exchange-Traded Funds*” (FINRA Regulatory Notice 09-31, June 2009), ETFs are typically registered unit investment trusts (UITs) or open-end investment companies whose shares represent an interest in a portfolio of securities that track an underlying benchmark or index.

Leveraged ETFs seek to deliver multiples of the performance of the index or benchmark they track. Some Non-Traditional ETFs are "inverse" or "short" funds (or combinations of both), meaning that they seek to deliver the opposite of the performance of the index or benchmark they track. Such objectives are achieved through the use swaps, futures contracts and other derivative instruments.

The AWC asserts that Non-Traditional ETFs generally "reset" daily, and such a factor can have significant ramifications that distort the performance of the subject ETF and its underlying index or benchmark. For example, the AWC notes that the Dow Jones U.S. Oil & Gas Index, between December 1, 2008 and April 30, 2009, gained two percent, while an ETF seeking to deliver twice the index's daily return fell six percent, and the related ETF seeking to deliver twice the inverse of the index's daily return fell 26 percent.

Despite the risks associated with holding Non-Traditional ETFs for longer periods, the AWC alleges that certain Wells Fargo customers held Non-Traditional ETFs for extended time periods during the relevant period of January 2008 through June 2009. In fact, certain Wells Fargo customers with a primary investment objective of income held Non-Traditional ETFs for periods of several months. The AWC offers these examples:

• A 65-year old conservative customer with a stated net worth under $50,000 held a Non-Traditional ETF for 43 days and sustained losses of over $25,000.

• A 92-year old conservative customer with a stated net worth under $500,000 held a Non-Traditional ETF for 135 days and sustained losses of over $2,000.

During the relevant period from January 2008 through June 2009, FINRA alleged that Wells Fargo failed to establish and maintain a supervisory system, including written procedures, reasonably designed to achieve compliance with applicable NASD and/or FINRA rules in connection with the sale of leveraged, inverse, and inverse-leveraged Exchange-Traded Funds ("Non-Traditional ETFs"). The AWC alleges that Wells Fargo supervised Non-Traditional ETFs the same way it supervised traditional ETFs. Thus, Wells Fargo failed to establish a reasonable supervisory system and written procedures to monitor the sale of Non-Traditional ETFs.

The AWC further alleges that Wells Fargo also failed to establish adequate formal training regarding Non-Traditional ETFs during the Relevant Period.

In addition, certain Wells Fargo registered representatives allegedly did not have an adequate understanding of Non-Traditional ETFs before recommending these products to retail brokerage customers. Certain Wells Fargo registered representatives also made unsuitable recommendations of Non-Traditional ETFs to certain customers with a primary investment objective of income.

As such, the AWC alleged that Wells Fargo violated NASD Rules 3010, 2310, and 2110 and FINRA Rule 2010, and, according to the terms of the AWC, FINRA imposed sanctions of a Censure, a $2.1 million fine, and $641,489 in restitution.