

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. 2010022962401**

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

**RE: Feltl & Company, Respondent
CRD No. 6905**

Pursuant to FINRA Rule 9216 of FINRA's Code of Procedure, Feltl & Company ("Feltl" 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 Feltl alleging violations based on the same factual findings described herein.

I.

ACCEPTANCE AND CONSENT

- A. Feltl 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

Feltl is headquartered in Minneapolis, Minnesota. It has eight branch offices located in Minnesota and Illinois, and approximately 113 registered representatives. Its revenue is derived from securities commissions, as well as underwriting and investment company activity. Feltl has been a FINRA member since September 1975, and is subject to FINRA's jurisdiction pursuant to Article IV, Section 6 of FINRA's by-laws.

OVERVIEW

Between January 2008 and February 2012 (the "Relevant Period"), Feltl failed to comply with the suitability, disclosure, and record-keeping requirements for broker-dealers who engage in penny stock business. For example, Feltl did not provide certain of its customers with the standardized U.S. Securities and Exchange Commission ("SEC") risk disclosure document two days prior to effecting a penny stock transaction in the customers' accounts and receive a

signed and dated acknowledgement of its receipt. The risk disclosure document describes, among other things, the nature and level of risk in the market for penny stocks, the broker-dealer's duties to the customer, and bid and ask prices for penny stocks.

Feltl also failed to reasonably supervise its penny stock business during the Relevant Period by not monitoring compliance with Sections 15(g) and 15(h) of the Securities Exchange Act of 1934 ("Exchange Act") and the Exchange Act rules thereunder, failing to sufficiently supervise penny stock transactions for compliance with applicable rules and regulations, and failing to establish, maintain, and enforce written supervisory procedures for its penny stock business.

From 2009 to 2012, Feltl also failed to annually test and verify its supervisory procedures, submit the required reports, test results, exceptions, and any additional or amended procedures to senior management, and make the required certifications. Also, Feltl was unable to produce to FINRA certain copies of branch offices' daily trade blotters in response to a FINRA request.

As a result of the foregoing misconduct, during the Relevant Period, Feltl violated Section 15(g) of the Exchange Act (through July 21, 2010); Section 15(h) of the Exchange Act (starting July 22, 2010); SEA Rules 15g-2, 15g-3, 15g-4, 15g-6, and 15g-9¹; NASD Rules 3010(a) and (b); NASD Rule 2110 (through December 14, 2008); and FINRA Rule 2010 (starting December 15, 2008). In addition, from 2009 to 2012, Feltl violated NASD Rule 3012(a)(1); FINRA Rule 3130; and FINRA Rule 2010. Finally, Feltl violated NASD Rule 3110(a), NASD Rule 3010(d)(1), and FINRA Rule 2010.

FACTS AND VIOLATIVE CONDUCT

Feltl Failed To Comply With The Penny Stock Rules

Background. The term "penny stock" generally refers to an equity security that trades below five dollars per share and that was issued by a small company with limited tangible revenue, assets, and/or operations.² Penny stocks often trade infrequently, which may make them difficult to sell and price. Penny stocks are generally considered speculative investments for these and other reasons.

Due to the speculative nature of penny stocks and historic sales practice issues relating to the offering and trading of certain penny stocks, the SEC requires broker-dealers effecting penny stock transactions to make a documented determination that the transactions are suitable for

¹ 17 C.F.R. §§ 240.15g-2, 240.15g-3, 240.15g-4, 240.15g-6, 240.15g-9.

² See SEA Rule 3a51-1, 17 C.F.R. § 240.3a51-1.

those customers and obtain the customers' written agreement to those transactions.³ Congress also amended the Exchange Act to require broker-dealers to provide customers with a risk disclosure document with important information concerning the penny stock market prior to effecting any penny stock transaction and to require the SEC to adopt rules setting forth additional standards for the disclosure by broker-dealers to customers of important information concerning transactions in penny stocks. These requirements are set forth in the SEA rules promulgated under Section 15(g) and 15(h) of the Securities Exchange Act of 1934⁴ (the "Penny Stock Rules").

Among other things, the Penny Stock Rules provide that a broker-dealer must: (a) document the customer's suitability for the specific penny stock investment, send a written statement to the customer describing the basis of the suitability determination two days prior to the penny stock transaction, and obtain a written agreement from the customer to purchase the penny stock in a specific quantity prior to the transaction (SEA Rule 15g-9); (b) furnish the customer a standardized risk disclosure document entitled "Important Information on Penny Stocks" (the "Risk Disclosure Document") (that describes among other things the nature and level of risk in the market for penny stocks, the broker-dealer's duties to the customer, and bid and ask prices for penny stocks) two days prior to effecting a penny stock transaction and receive and maintain a signed and dated acknowledgement of its receipt (SEA Rule 15g-2 and Schedule 15G); (c) disclose to the customer the current inside bid and ask market quotations, if any, for the penny stock (SEA Rule 15g-3); (d) disclose to the customer the amount of compensation the broker or dealer will receive for the transaction orally or in writing prior to effecting the transaction and in writing at or prior to the time the written confirmation of the transaction is given (SEA Rule 15g-4); and (e) send to the customer monthly account statements showing certain market and price information for each penny stock held in the customer's account and containing a conspicuous legend containing specified language⁵ (SEA Rule 15g-6).

Feltl's Penny Stock Business. During the Relevant Period, Feltl engaged in thousands of penny stock transactions on behalf of its customers and received significant revenue from its penny stock business. However, because the Firm did not track all penny stock transactions in its books and records, the actual number of penny stock transactions by Feltl's customers and Feltl's total penny stock related revenue are unknown.

Feltl was a market maker in 17 penny stocks at different times during the Relevant Period. With respect to 15 of those penny stocks, Feltl solicited its customers to make at least 2,450 purchases

³ See Sales Practice Requirements for Certain Low-Priced Securities, Exchange Act Release No. 34-27160 (Aug. 22, 1989); 17 C.F.R. § 240.15g-9.

⁴ Dodd-Frank Sec. 929X(c) amended the Exchange Act by, among other things, redesignating Sec. 15(g) to Sec. 15(h), effective July 22, 2010.

⁵ The legend must state: "If this statement contains an estimated value, you should be aware that this value may be based on a limited number of trades or quotes. Therefore, you may not be able to sell these securities at a price equal or near to the value shown. However, the broker-dealer furnishing this statement may not refuse to accept your order to sell these securities. Also, the amount you receive from a sale generally will be reduced by the amount of any commissions or similar charges. If an estimated value is not shown for a security, a value could not be determined because of a lack of information." SEA Rule 15g-6(e).

of penny stocks and received over \$2.1 million from these transactions through markups, markdowns, or commissions. The Firm received additional revenue from selling activity in these penny stocks. While the Firm tracked the activity in these 17 penny stocks in which it was a market maker, it did not track the individual transactions for which a security may have temporarily not met the definition of a penny stock because, for example, the security traded above a price of \$5.00 or the issuer had average revenue of at least \$6 million for the last three years. Further, the Firm failed to track the penny stock transactions in securities in which it did not make a market. Accordingly, while the Firm's penny stock transaction and revenue numbers are substantial, the actual numbers are unknown.

Feltl's Penny Stock Rule Violations. Feltl failed to comply with the Penny Stock Rules during the Relevant Period. For the penny stock transactions that Feltl effected for or with the accounts of its customers during the Relevant Period, Feltl did not:

- 1) document the customer's suitability for the specific penny stock investment, send the customer a written statement describing the basis of the suitability determination two days prior to the penny stock transaction, and obtain a written agreement from the customer to purchase the penny stock prior to the transaction, in violation of SEA Rule 15g-9;
- 2) furnish all customers the standardized Risk Disclosure Document and receive a signed and dated acknowledgement of its receipt two days prior to the penny stock transaction, in violation of SEA Rule 15g-2;
- 3) disclose to the customer the current inside bid and ask market quotations, if any, for the penny stock, in violation of SEA Rule 15g-3;
- 4) disclose to all customers the amount of compensation the Firm would receive for the trade orally or in writing prior to effecting the penny stock transaction, in violation of SEA Rule 15g-4; and/or
- 5) send the customer monthly account statements that showed the market value of each penny stock held in the customer's account and containing the conspicuous legend with the required language concerning penny stock risks, among other things, in violation of SEA Rule 15g-6.

Accordingly, during the Relevant Period, Feltl violated Section 15(g) of the Exchange Act (for conduct through July 21, 2010); Section 15(h) of the Exchange Act (starting July 22, 2010); SEA Rules 15g-2, 15g-3, 15g-4, 15g-6, and 15g-9; NASD Rule 2110 (through December 14, 2008); and FINRA Rule 2010 (starting December 15, 2008).

Feltl Failed To Reasonably Supervise Its Penny Stock Business. During the Relevant Period, Feltl failed to establish and maintain a system to supervise the activities of its registered representatives, registered principals, and other associated persons that was reasonably designed

to achieve compliance with the applicable rules and regulations relating to its penny stock business, including (a) the Penny Stock Rules, and (b) the rules and regulations designed to deter and detect fraudulent activities and transactions in its penny stock business.

Feltl's supervisory system was not reasonably designed to supervise for compliance with the Penny Stock Rules. Indeed, the Firm did not even track whether customer transactions were penny stock transactions. The Firm did not monitor for compliance with any of the Penny Stock Rules, including whether a Risk Disclosure Document was required or sent to a customer, whether the required suitability analysis was conducted and documented, or whether the other Penny Stock Rules were followed. Additionally, Feltl failed to reasonably supervise penny stock transactions in order to detect potentially fraudulent or otherwise problematic penny stock activity. For example, penny stock transactions routinely were flagged in the Firm's exception reports, but the Firm did not have a reasonable system or procedures to follow up on these transactions.

During the Relevant Period, Feltl also failed to establish, maintain, and enforce written supervisory procedures to supervise the Firm's penny stock business and to supervise the activities of registered representatives, registered principals, and other associated persons that were reasonably designed to achieve compliance with the applicable rules and regulations concerning the Firm's penny stock business, including the Penny Stock Rules. The Firm's written supervisory procedures relating to the Penny Stock Rules merely tracked some of the language of the Penny Stock Rules, and briefly discussed certain requirements under some of the Penny Stock Rules. These procedures therefore were not adequate for a number of reasons.

- The written procedures did not identify the responsible Firm personnel or provide adequate direction to determine whether a particular stock was a penny stock and whether a particular stock was exempt from the Penny Stock Rules.
- The written procedures concerning SEA Rule 15g-2 did not state that the Firm must wait two business days after sending the Risk Disclosure Document to execute the penny stock transaction for the customer account.
- The written procedures concerning SEA Rule 15g-9 did not state that the Firm must (1) receive back from the customer an agreement to the transaction that set forth the identity and quantity of the penny stock to be purchased prior to the transaction, and (2) wait two business days to execute the relevant penny stock transaction after sending the suitability statement and the agreement to the transaction in a penny stock.
- The written procedures failed to sufficiently delineate how to ascertain, and what documents to obtain, regarding whether a customer met the suitability requirements specified under the Penny Stock Rules.
- The written procedures failed to delineate the nature of the disclosures to be made regarding compensation relating to penny stocks, and when and how such disclosures were to be made.

Furthermore, Feltl failed to enforce its existing written supervisory procedures concerning penny stocks, as discussed above. For example, the Firm did not even conduct the steps required by the written procedures as a matter of course.

Accordingly, during the Relevant Period, Feltl violated NASD Rules 3010(a) and (b), NASD Rule 2110 (through December 14, 2008), and FINRA Rule 2010 (starting December 15, 2008).

Feltl Failed To Annually Test Its Supervisory Procedures, Submit Supervisory Reports, And Certify Its Supervisory Processes

NASD Rule 3012(a)(1) requires each member to establish, maintain, and enforce a system of supervisory control policies and procedures that “(A) test and verify that the member’s supervisory procedures are reasonably designed with respect to the activities of the member and its registered representatives and associated persons, to achieve compliance with applicable securities laws and regulations, and with applicable NASD rules and (B) create additional or amend supervisory procedures where the need is identified by such testing and verification.” The member also must annually submit to its senior management a report that details the member’s system of supervisory controls, the summary of the test results and significant identified exceptions, and any additional or amended supervisory procedures created in response to the test results.

FINRA Rule 3130 requires a member’s chief executive officer or similar officer to certify annually that the member has “in place processes to establish, maintain, review, test and modify written compliance policies and written supervisory procedures reasonably designed to achieve compliance with” applicable rules, laws, and regulations and that the chief executive officer met at least once with the chief compliance officer in the preceding 12 months to discuss such processes.

From 2009 through 2012, Feltl failed to test and verify its supervisory procedures and submit the required reports, test results and exceptions, and any additional or amended procedures, to senior management, and make the required certifications. As a result, Feltl violated NASD Rule 3012(a)(1) and FINRA Rules 3130 and 2010 from 2009 through 2012.

Feltl Failed To Maintain And Make Branch Office Trade Blotters Available

NASD Rule 3010(d)(1) requires members to establish procedures for the principal review and endorsement in writing, on an internal record, of all securities transactions. In addition, members are required to maintain evidence that these procedures have been implemented and carried out and must make them available to FINRA upon request.

During FINRA’s investigation in this matter, on October 3, 2013, FINRA Staff requested pursuant to FINRA Rule 8210 that Feltl produce “the designated supervisor’s initialed copies of the daily trade blotter for the Firm’s Minnetonka branch office for November 2009 and December 2009 and for the Firm’s Inner Grove Heights branch office for January 2009 and September 2009.” The Firm was unable to produce the requested documents for the Inner Grove

Heights branch office and was not able to produce the requested documents for the Minnetonka branch office until July 23, 2014.

By not maintaining these copies of the daily trade blotters and not providing them, or not promptly providing them, to FINRA upon request, Feltl violated NASD Rule 3010(d)(1), NASD Rule 3110(a), and FINRA Rule 2010.

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

1. A censure; and
2. A fine of \$1,000,000.

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

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

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

II.

WAIVER OF PROCEDURAL RIGHTS

Feltl specifically and voluntarily waives the following rights granted under FINRA's Code of Procedure:

- A. To have a Complaint issued specifying the allegations against Feltl,
- 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, Feltl 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.

Feltl 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

Feltl 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 Feltl; and
- C. If accepted:
 - 1. this AWC will become part of my permanent disciplinary record and may be considered in any future actions brought by FINRA or any other regulator against Feltl;
 - 2. this AWC will be made available through FINRA's public disclosure program in response to public inquiries about my disciplinary record;
 - 3. FINRA may make a public announcement concerning this agreement and the subject matter thereof in accordance with FINRA Rule 8313; and
 - 4. Feltl 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. Feltl 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 Feltl'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. Feltl may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. Feltl understands that Feltl 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 Feltl 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 the Firm to submit it.

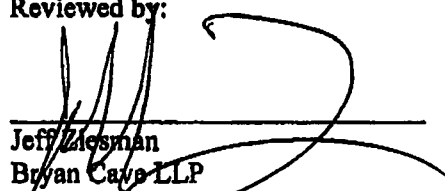
08/14/2014

Date (mm/dd/yyyy)

Feltl & Company

By: 
Thomas F. Steichen
General Counsel, Feltl & Company

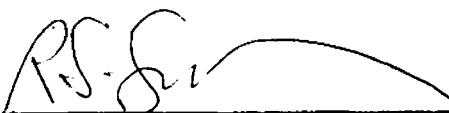
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Accepted by FINRA:

09/02/2014
Date (mm/dd/yyyy)

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


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Corrective Action Statement of Feltl & Company

This matter concerns certain historical practices by Feltl & Company (Feltl) regarding certain penny-stock transactions conducted during the relevant period (January 2008-February 2012), and certain other issues identified in the AWC.¹ Feltl ceased recommending penny stocks to any of its customers in February 2012, over 2 ½ years ago. Feltl ceased being a market maker for any penny-stock in 2012. Consequently, the firm would be exempt from compliance with the penny stock rules since at least February 2012.

Since February 2012, Feltl has allowed customers to trade penny-stocks through Feltl only on a non-solicited basis. To do so, the customers have been required to sign certain paperwork attesting that they understand the nature and risks of penny-stocks, and their desire to continue to place non-solicited transactions through Feltl.

A separate issue in this matter concerns the Chief Executive Officer certification and supervisory controls processes. Since 2012 the firm has formalized meetings between the Chief Executive Officer and Chief Compliance Officer and the commensurate processes, along with providing the annual certification, such that the processes are in compliance with FINRA Rule 3130. The firm has also revised its supervisory controls processes so that they are consistent with the terms and spirit of NASD Rule 3012.

Finally, the firm has replaced the General Counsel, Chief Compliance Officer, Head Trader and a Branch Manager from the relevant period. The current Feltl employees occupying these positions will further enhance a culture of compliance at the firm.

This Statement of Corrective Action is submitted by Feltl. It does not constitute factual or legal findings by FINRA, nor does it reflect the views of FINRA or FINRA Staff.

¹ This Corrective Action Statement is submitted by Feltl & Company. It does not constitute factual or legal findings by FINRA, nor does it reflect the view of FINRA, or its staff.