

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER, AND CONSENT
NO. 2015047322502**

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

RE: Principal Securities, Inc., Respondent ("Principal Securities")
CRD No. 1137

Pursuant to FINRA Rule 9216 of FINRA's Code of Procedure, Principal Securities 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 Principal Securities alleging violations based on the same factual findings described in this AWC.

I.

ACCEPTANCE AND CONSENT

- A. Principal Securities 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

Principal Securities is a retail broker that has been registered with FINRA or its predecessor since 1968. Principal Securities is affiliated with several insurance companies. As of July 2017, Principal Securities had 739 branch offices and 3,292 registered persons.

RELEVANT DISCIPLINARY HISTORY

Principal Securities does not have any relevant disciplinary history.

OVERVIEW

For at least three years, Principal Securities' system for supervising additions to existing variable annuities was not reasonably designed to ensure that they complied with applicable securities laws and rules, including those governing suitability—a problem that affected more than 4,000 transactions. As a result, Principal Securities violated NASD Rule 3010 and FINRA Rules 2010 and 3110.

FACTS AND VIOLATIVE CONDUCT

From October 2013 to September 2016, Principal Securities' customers added money to existing variable annuities on more than 6,000 occasions. Those additions accounted for approximately one-sixth of Principal Securities' revenue from variable products during that period.

While Principal Securities reviewed some of those additions by three exception reports and periodic branch and desk audits, the scope of that supervision was unreasonably limited. First, the exception reports covered only transactions involving one of Principal Securities' affiliates, not all of the existing variable annuities that Principal Securities' customers held. Second, the exception reports covered only additions to existing variable annuities that were funded by surrendering insurance products, not all sources—thus, for example, the exception reports did not cover additions that were funded by rolling over a retirement plan. Third, Principal Securities' supervisors used the exception reports to identify trading trends and patterns, rather than to evaluate the propriety of individual additions. Fourth, Principal Securities' periodic audits covered only selected customers, not additions to existing variable annuities generally or patterns of recommendations to make such additions.

As a result of those and other limitations, Principal Securities' system for supervising additions to existing variable annuities was not reasonably designed to comply with applicable securities laws and rules, including those governing suitability. Principal Securities' system did not capture, so the firm did not review, more than two-thirds of those additions. Nor was Principal Securities' system reasonably designed to focus on the additions that posed the greatest risk to the firm's customers—for example, additions resulting in high concentrations of customers' net worth in variable contracts, or additions by customers whose financial needs and goals had changed since they initially purchased their contracts. As a result, Principal Securities' system was not likely to detect and flag relatively risky transactions—such as a large addition to a contract long after it was purchased, prompted by a recommendation from an associated person—so that the firm could determine whether such recommendations violated any securities laws or rules.

Those gaps in Principal Securities' system resulted in improper transactions escaping detection by the firm, causing harm to contract holders. For example, Principal Securities did not detect recommended in-and-out trading between a customer's variable annuities, which resulted in frequent and unnecessary surrender charges, nor did the firm detect another customer's excessive concentration in a variable annuity resulting from a \$300,000 addition to that contract which more than doubled the customer's initial investment.¹

¹ Principal Securities has remedied the harm to those customers. In November 2016, FINRA barred the associated person who initiated those transactions, Matthew Geiser, from the brokerage industry for failing to cooperate with FINRA's investigation of this matter.

By failing to supervise the majority of additions to variable contracts or to implement a supervisory system focusing on the additions that posed the most risk, Principal Securities violated NASD Rule 3010 and FINRA Rule 3110, and consequently FINRA Rule 2010.

B. Principal Securities also consents to the imposition of the following sanctions:

- Censure
- Fine of \$250,000

Principal Securities agrees to pay that fine upon notice that this AWC has been accepted and that the fine is due and payable. Principal Securities has submitted an Election of Payment form showing the method by which Principal Securities proposes to pay the fine. Principal Securities specifically and voluntarily waives any right to claim that it is unable to pay, now or at any time hereafter, the fine. The sanctions imposed in this AWC shall be effective on a date set by FINRA staff.

II.

WAIVER OF PROCEDURAL RIGHTS

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

- A. To have a Complaint issued specifying the allegations against Principal Securities;
- 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, Principal Securities 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.

Principal Securities 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

Principal Securities 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 Principal Securities; and
- C. If accepted:
 - 1. This AWC will become part of Principal Securities' permanent disciplinary record and may be considered in any future actions brought by FINRA or any other regulator against Principal Securities;
 - 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. Principal Securities 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. Principal Securities 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 Principal Securities' testimonial obligations or right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party.
- D. Principal Securities may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. Principal Securities 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 Principal Securities, certifies that a person duly authorized to act on its behalf has read and understands all of the provisions of this AWC and have been given a full opportunity to ask questions about it; that Principal Securities has agreed to its 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 Principal Securities to submit it.

09.18.2017

Date (mm/dd/yyyy)

Principal Securities, Inc.

By: Kara M. K. Hoogensen
President and CEO

Reviewed by:

John H. Walsh

John Walsh
Counsel for Principal Securities, Inc.
Eversheds Sutherland (US) LLP
700 Sixth Street, NW, Suite 700
Washington, D.C. 2001-3980
202-383-0818

Accepted by FINRA:

Oct. 26, 2017

Date

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

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