

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER, AND CONSENT
NO. 2018059223401**

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

RE: Independent Financial Group, LLC (Respondent)
Member Firm
CRD No. 7717

Pursuant to FINRA Rule 9216, Respondent Independent Financial Group, LLC (IFG) 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

IFG has been a FINRA member since November 1978 and it offers investment products to retail customers. The firm has approximately 660 registered representatives and 370 branch offices. The firm's main office is in San Diego, California. Respondent does not have any relevant disciplinary history.

OVERVIEW

From January 2008 through March 2016, IFG failed to reasonably supervise one of the firm's former registered representatives ("RR 1") who made unsuitable recommendations to customers. RR 1 recommended that his customers concentrate their retirement assets and liquid net worth in speculative and illiquid securities. IFG became aware of red flags indicating that RR 1 was making unsuitable recommendations to his customers yet the firm failed to take reasonable actions to investigate and stop the misconduct.

By reason of the foregoing, IFG violated NASD Rule 3010 and FINRA Rules 3110 and 2010.¹

FACTS AND VIOLATIVE CONDUCT

A. Applicable FINRA Rules and Guidance

FINRA Rule 3110(a) requires that each member 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 FINRA Rules. A firm's duty to supervise its registered representatives includes the responsibility to reasonably investigate "red flags" of potential misconduct. A violation of FINRA Rule 3110 is also a violation of FINRA Rule 2010, which requires FINRA members, in the conduct of their business, to "observe high standards of commercial honor and just and equitable principles of trade."

FINRA Rule 2111 requires member firms or associated persons to have a reasonable basis for believing that a recommended transaction or investment strategy is suitable for a customer based on the customer's investment profile, which includes, among other factors, the customer's age, other investments, financial situation and needs, tax status, investment objectives, investment experience, investment time horizon, liquidity needs and risk tolerance. A recommendation may be unsuitable if it results in an undue concentration in a particular security or category of securities and the correspondent increased risk of loss is inconsistent with the customer's investment profile.

NASD Notice to Members 03-71 (NTM 03-71) reminded members of their duties with respect to Non-Conventional Investments ("NCI"), such as non-traded real estate investment trusts (REITs). A REIT is a corporation, trust or association that owns (and might also manage) income-producing real estate. REITs pool the capital of numerous investors to purchase a portfolio of properties—from office buildings and shopping centers to hotels and apartments—which the typical investor might not otherwise be able to purchase individually. A non-traded REIT does not trade on a national securities exchange.

NTM 03-71 noted that, "NCIs with particular risks may be suitable for recommendation to only a very narrow band of investors capable of evaluating and being financially able to bear those risks." The NTM also stated that, "due to the unique nature of these products, many investors, especially retail investors, may not understand the features of the product, and may not fully appreciate the associated risks of investing in them."

In October 2011, FINRA issued an Investor Alert on non-traded REITs entitled, "Perform a Careful Review Before Investing." In that alert, FINRA explained that "shares of non-traded REITs do not trade on a national securities exchange. For this reason, non-traded

¹ FINRA Rule 3110 superseded NASD Rule 3010 on December 1, 2014. NASD Rule 3010(a) was substantively identical to FINRA Rule 3110(a).

REITs are generally illiquid, often for periods of eight years or more.” The alert further noted that, “[e]arly redemption of shares is often very limited, and fees associated with the sale of these products can be high and erode total return.” In addition, distributions can be heavily subsidized by borrowed funds and include a return of investor principal, which is unlike dividends received from large corporations that trade on national exchanges, which are typically derived solely from earnings.

Concerned that members were not fulfilling their sales practice obligations to retail customers, FINRA issued guidance on structured products in NASD Notice to Members 05-59 (NTM 05-59). Structured products are 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. The note pays interest to the investor at a specified rate and interval. The derivative component establishes the payment at maturity. In NTM 05-59, FINRA outlined many of the risks associated with structured products and reminded members of their obligation to ensure that such products were suitable for particular customers, based on, among other factors, the customer’s investment objectives, financial status and tax status. The notice recommended that members apply the suitability requirements for options trading, which include that “[t]he customer has *such knowledge and experience* in financial matters that he may reasonably be expected to be *capable of evaluating the risks* of the recommended transaction, and is financially able to bear the risks” (Emphasis in original.)

B. IFG’s Failure to Reasonably Supervise RR 1

During the relevant period, the Firm failed to reasonably supervise RR 1’s recommendations of alternative investments to customers, including senior customers, and failed to reasonably investigate red flags. RR 1 solicited dozens of customers who were retiring or had retired to liquidate their 401(k) and pension plans and invest the proceeds with him at IFG. RR 1 then recommended that many of these customers concentrate their retirement assets in non-traded REITs and structured notes. Many of the customers had little or no investment experience and had never purchased alternative investments.² During this period, RR 1 recommended that his customers make hundreds of investments in non-traded REITs and structured products.

The following examples are illustrative of RR 1’s unsuitable recommendations:

- Customer A was 71 years old, retired, had an investment objective of growth and a conservative risk tolerance. Despite the fact that Customer A’s new account documents did *not* allow for speculation, 50% of Customer A’s liquid net worth was invested in non-traded REITs and structured notes. Customer A’s first purchase was a \$141,000 investment in a single non-traded REIT. The suitability questionnaire completed for Customer A similarly indicated that the account did not allow for speculation, but “no” was subsequently

² RR 1 entered into an AWC and agreed to a bar from associating with any FINRA member firm in any capacity. AWC No. 2017052705001 (June 2018). More than three dozen of RR 1’s customers brought arbitration claims against IFG, and the vast majority of the arbitrations were settled.

crossed-out and initialed by RR 1, not the customer, falsely indicating that the customer then wished to speculate.

- Customer B was 72 years old, retired, had an investment objective of growth and a moderate risk tolerance. Customer B's account documents did *not* allow for speculation, but RR 1 nevertheless recommended 75% of Customer B's liquid net worth be invested in non-traded REITs and structured notes. Despite the fact RR 1 recommended these purchases, he falsely marked the transactions as unsolicited. RR 1 was on heightened supervision when the purchases were made and a supervisor did not pre-approve them, as required by RR 1's heightened supervision plan. The questionnaires for the non-traded REITs indicated that the account did *not* allow for speculation, but RR 1 unilaterally changed the form to indicate the account did allow for speculation and initialed the change himself.

Between January 2008 through November 2014, the firm did not explicitly limit concentration levels of alternative investments in customer accounts. Instead, it required the completion of a suitability questionnaire for each alternative investment purchased to purportedly ensure the customer's purchase was suitable based on the suitability criteria contained in the relevant prospectus, that the investment was consistent with the customer's investment objectives, risk tolerance and financial information as provided on new account forms, and that a summary of the risk disclosures was provided to the customer on separate point of sale forms.

RR 1's supervisors observed and reported certain irregularities and concerns relating to RR 1's recommendations. For example, there were discrepancies with RR 1's customers' new account documents, suitability questionnaires and questionable asset allocations. In addition, numerous complaints and customer arbitrations were filed against RR 1 beginning in 2012 and continuing throughout his association with the firm. Although these events resulted in the Firm twice implementing a heightened supervision plan for RR 1, neither plan was reasonably executed. For example, although the firm performed quarterly office inspections pursuant to the terms of RR 1's heightened supervision plan, including unannounced office inspections, it did not reasonably respond to red flags that were observed in the course of those inspections including potentially altered new account and transaction forms, customer signatures that did not match and ineligible accounts purchasing alternative investments. In addition, the heightened supervision plan required a principal to review and approve RR 1's new account forms before an account was accepted and opened. Although IFG placed calls to certain of RR 1's customers as part of that process, it did so after the accounts were opened and IFG did not reasonably act on the information it learned including that certain forms were completed inaccurately.

One of RR 1's supervisors documented issues relating to RR 1's misconduct in his notes, which he shared with others at the firm including individuals within the firm's Compliance Department (Supervisor 1). Supervisor 1's notes highlighted concerns such as the use of corrective tape and liquid paper on account documents, trades being

potentially mismarked as unsolicited, customer signatures that did not match, questionable changes to customer risk tolerances and potentially unsubstantiated increases in a customer's net worth. Notwithstanding the identification of these issues, the firm permitted RR 1 to continue to sell non-traded REITs and structured products to his customers.

In November 2013, Supervisor 2 began supervising RR 1. Supervisor 2, however, was unaware of RR 1's prior pattern of paperwork irregularities and RR 1's growing number of customer complaints and arbitrations. Supervisor 2 also was responsible for implementing RR1's second plan of heightened supervision, effective April 2015, which the firm imposed due to the filing of two customer arbitrations against RR 1.

In November 2014, the firm implemented certain new policies concerning alternative investments, including establishing concentration guidelines for alternative investments based on a customer's age and net worth, and mandatory product specific training on alternative investments for the firm's registered representatives, which supplemented the firm's general product training. RR 1, however, continued to recommend non-traded REITs to customers. While many of these customer purchases were within the concentration guidelines, at times, RR 1's recommendations of non-traded REITs exceeded IFG's November 2014 guidelines—and Supervisor 2 approved the sales. Although Supervisor 2 would sometimes raise questions related to incomplete or stale paperwork or the suitability of certain of RR 1's recommended transactions, the issues Supervisor 2 raised were typically resolved by gathering or amending transaction documentation and not by reasonably acting upon the red flags suggesting the recommended sales were potentially unsuitable.

Therefore, the firm violated NASD Rule 3010 and FINRA Rules 3110 and 2010.

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

- a censure;
- a \$200,000 fine; and
- the following undertaking:
 - (i) Certification Regarding Implementation of Reasonably Designed Procedures. Within no later than 90 days of the date of this AWC is accepted, a senior officer and principal of IFG shall certify in writing to FINRA that the Firm has implemented supervisory systems and written supervisory procedures reasonably designed to: (i) address all areas of conduct identified in this AWC, and (ii) achieve compliance with suitability requirements for alternative investments. This certification shall be submitted by letter addressed to Ellen Sheridan-Cona, Senior Counsel, FINRA Enforcement Department, Brookfield Place, 200 Liberty Street,

11th Floor, New York, New York 10281 and to ellen.sheridan-
cona@finra.org.

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.

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 National Adjudicatory Council (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.

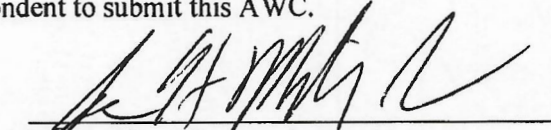
OTHER MATTERS

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.

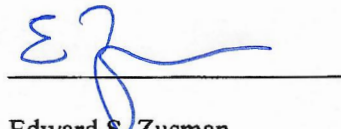
The undersigned, on behalf of Independent Finance Group, LLC, certifies that a person duly authorized to act on Respondent's behalf has read and understands all of the provisions of this AWC and has been given a full opportunity to ask questions about it; that Respondent has agreed to the AWC's provisions 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.

3-29-2021
Date


Independent Finance Group, LLC
Respondent

Print Name: Joe H Miller Jr
Title: CEO

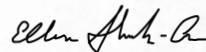
Reviewed by:



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Accepted by FINRA:

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



4/8/2021
Date

Ellen Sheridan-Cona
Senior Counsel
FINRA
Department of Enforcement
Brookfield Place
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