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## Texas State Securities Board

208 E. 10th Street, 5th Floor  
Austin, Texas 78701-2407  
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MEMBER

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IN THE MATTER OF THE  
DEALER REGISTRATION OF  
LPL FINANCIAL LLC

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**Order No. IC22-CAF-02**

TO: LPL Financial LLC  
1055 LPL Way  
Fort Mill, SC 29715

### DISCIPLINARY ORDER

Be it remembered that LPL Financial LLC ("Respondent"), appeared before the Securities Commissioner of the State of Texas ("Securities Commissioner") solely for the purpose of resolving an investigation by the Texas State Securities Board, and without admitting or denying, consented to the entry of this order ("Order") the Findings of Fact, the Conclusions of Law, and the Undertaking contained herein.

### OVERVIEW

During the period 2016 through 2019, Respondent failed to enforce its written supervisory procedures relating to its prohibition on retail communications regarding structured notes because Respondent's e-mail surveillance tool was not designed to flag e-mails sent to more than twenty-five individuals in a thirty-day period when those individuals were included only by blind carbon copy (BCC). Accordingly, a former Agent of Respondent solicited sales of over \$65,000,000 in structured notes using blast e-mails to generate interest in the product. Respondent also failed to enforce its written supervisory procedures that sales of products be suitable, since certain investors had limited investment experience and invested over 40% of their investable assets in the notes.

Since 2019, Respondent has implemented a new e-mail surveillance tool that incorporates BCC recipients in connection with the detection of unapproved retail communications. Additionally, the structured notes sold by the former Agent that have reached maturity returned full principal to the investors. To resolve this matter with the Securities Commissioner, Respondent has agreed to pay a \$125,000 fine and enter into an Undertaking whereby Respondent agrees to offer to repurchase outstanding structured notes from certain clients of Respondent's and the Agent's.

## FINDINGS OF FACT

1. Respondent has waived (a) Respondent's right to notice and hearing in this matter; (b) Respondent's right to appear and present evidence in this matter; (c) Respondent's right to appeal this Order; and (d) all other procedural rights granted to the Respondent by The Securities Act Tex. Gov't Code §§ 4001.001-4008.105 (the "Securities Act") and the Administrative Procedure Act, Tex. Gov't Code Ann. §§ 2001.001-2001.902.
2. Structured products are securities derived from a single security, a basket of security, indices, or other securities. Some structured products offer full protection of the principal invested, whereas others offer no or limited protection.
3. Structured products typically have two components—a note and a derivative (often an option). The note pays interest to the investor at a specified rate and interval. The derivative component establishes whether interest will be paid and whether the note will return principal at maturity.
4. A structured note with a barrier, or a Barrier Note, is a note that tracks underlying assets or indices and sets a barrier strike rate at a specified time in the future.
5. Specifically, if the value of the underlying assets/indices is at or greater than the reference barrier strike rate at the time the note matures and at periodic points when coupons could be paid, the investor receives their principal amount plus all the coupons paid throughout the life of the note. However, if the value of the underlying assets/indices at maturity is less than the reference barrier strike rate, the investor will lose some or all of his or her principal but will keep the coupons paid, if any.
6. Barrier Notes are principal-at-risk notes. Additionally, investing in Barrier Notes involves liquidity risks and is not the equivalent to investing directly into the indices linked to the note.
7. In recognition of the aforementioned risks of Barrier Notes, Respondent had written supervisory procedures specifically addressing suitability of structured products and principal-at-risk notes like Barrier Notes.
8. In addition to a general requirement that agents must ensure that any recommendation of a Barrier Note is suitable, internal training materials stated that a Barrier Note is suitable for more speculative and experienced investors.
9. From 2016 through 2019 (the "Relevant Period"), a former agent of Respondent (the "Agent") sold more than \$65,000,000 in structured products, most of which were non-principal protected Barrier Notes.

### *The Agent's Barrier Note E-mails*

10. Throughout the Relevant Period, the Agent sent e-mails to clients and potential clients describing one or more Barrier Notes available through Respondent.
11. These e-mails were not customized to specific individuals. Rather, the Agent often addressed the e-mail to himself but included up to twenty-five (25) individuals by blind carbon copy (or "BCC").
12. For example, on July 25, 2017, the Agent sent an e-mail called "[...] Note for Consideration" to himself, with seventeen (17) individuals included by BCC. Two days later, he sent the exact same e-mail, once again to himself, including fifteen (15) individuals by BCC.
13. Respondent's written supervisory procedures addressed communications with the public and defined "retail/Institutional communications" as any written (including electronic) communication distributed to twenty-six or more brokerage retail and/or institutional investors within a 30-day calendar period.
14. The procedures required that all retail communications be reviewed and approved prior to use. For structured products, including Barrier Notes, Respondent prohibited its agents from creating their own communications, but for a bullet-point reference to a structured product.
15. Certain emails sent by the Agent to clients and prospective clients described the Barrier Note as special or great, with excellent risk/reward, and would identify certain features of the Barrier Note: the issuing bank, length of the note, interest rate, the reference indexes, and the downside barrier (i.e., the percentage at which all indexes must remain above for the note to make interest payments and return principal at maturity).
16. The Agent never sought approval for the aforementioned e-mails even while the total number of BCC recipients within the 30-day calendar period was routinely exceeding twenty-five (25) individuals.

### *Respondent's E-mail Surveillance*

17. During the Relevant Period, Respondent used a lexicon and rule-based surveillance system to enforce its written supervisory procedures related to e-mail reviews.
18. One of the rules in place during the Relevant Period was a Blast E-mail flag that identified e-mails that met the definition of retail communication: an e-mail sent to twenty-six (26) or more recipients.

19. However, the rule parameters were limited to calculating the number of recipients in the "To" field. The system would not flag for a similar number of recipients listed in the "BCC" field.
20. At various times throughout the Relevant Period, certain of the Agent's e-mails were flagged and reviewed by Respondent's supervisors to assess the content of the e-mail and its compliance with Respondent's content standards. Specifically, the requirement that marketing materials regarding structured products balance the features, like the interest rate, with adequate risk disclosures.
21. On three (3) separate occasions, Respondent disciplined the Agent for the contents of his e-mails regarding Barrier Notes. Sanctions included letters of caution, a requirement to take additional training, and multiple fines.
22. However, given the limitations of Respondent's surveillance tool at the time, the Respondent was unaware of the extent of the problematic e-mails.
23. During the Relevant Period, Respondent's e-mail surveillance system flagged about 350 of the Agent's e-mails for review by supervisors. However, more than 1,000 e-mails with BCC recipients went undetected.

#### *Unsuitable Barrier Note Recommendations*

24. Many of the Agent's clients had no or very limited investment experience prior to investing in a Barrier Note.
25. The Agent recommended that certain of these inexperienced clients invest more than 40% of their liquid net worth in Barrier Notes.
26. Although Respondent had procedures in place to flag such transactions, Respondent nevertheless approved them.

#### *Mitigating Facts*

27. In November 2019, Respondent implemented a new e-mail surveillance system. This system flags blind-copy e-mails sent to multiple recipients.
28. All notes recommended by the Agent that reached maturity as of the date of this Order were above their respective barrier and returned full principal to investors.
29. Respondent cooperated fully with the Texas State Securities Board's ("TSSB") investigation.

## CONCLUSIONS OF LAW

1. Respondent's inability to detect certain of the Agent's retail communications regarding Barrier Notes was a failure to enforce Respondent's written supervisory procedures requiring approval of retail communications and prohibiting the creation of retail communications regarding structured products.
2. Respondent's approval of the Agent's unsuitable recommendations of Barrier Notes to certain clients was a failure to enforce Respondent's procedures requiring suitable recommendations of structured products.
3. Respondent's failures to enforce its written supervisory procedures are violations of §115.10 of the Board Rules.

Pursuant to Section 4007.106(a)(3) of the Texas Securities Act, Respondent's violations of §115.10 of the Board Rules constitute a basis for the assessment of an administrative fine against Respondent.

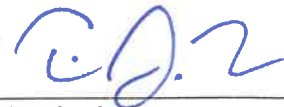
## UNDERTAKING

1. Respondent undertakes and agrees to offer restitution, including an offer to repurchase structured notes that have not yet matured, to certain clients mutually agreed upon by the staff of the TSSB ("Staff") and Respondent.
2. Respondent further undertakes and agrees that the restitution offer will be made within thirty (30) days of this Order.
3. Respondent further undertakes and agrees that the restitution offer will remain open for a period of thirty (30) days from the date the offer is made.
4. Respondent further undertakes and agrees that Respondent will provide evidence and records of the offer and the acceptance of the offer by any client within seventy-five (75) days of this Order to the Staff.

## ORDER

1. It is therefore ORDERED that LPL Financial, Inc. shall pay ADMINISTRATIVE FINE in the amount of One-Hundred and Twenty-Five Thousand Dollars (\$125,000.00) to the general fund of the State of Texas within ten (10) business days of the entry of this Order.
2. It is further ORDERED that LPL Financial, Inc. COMPLY with the terms of the Undertaking contained herein.

SIGNED AND ENTERED BY THE SECURITIES COMMISSIONER this 28<sup>th</sup> day  
of September, 2022.



Travis J. Iles

Respondent:

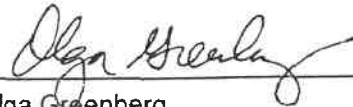


LPL Financial LLC  
By: Matthew K. Enyedi, MD

Approved as to Form:



Clinton Edgar,  
Deputy Securities Commissioner



Olga Greenberg,  
Eversheds Sutherland (US) LLP



Cristi Ochoa,  
Attorney, Inspections & Compliance Division