

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. 2018057508101**

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

RE: J.P. Morgan Securities LLC, Respondent
Member Firm
CRD No. 79

Pursuant to FINRA Rule 9216 of FINRA's Code of Procedure, Respondent J.P. Morgan Securities LLC ("JPMS" 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 Respondent alleging violations based on the same factual findings described herein.

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

JPMS is currently a FINRA member firm. Headquartered in New York City, it engages in a general securities business, has approximately 27,000 registered representatives, and maintains approximately 5,400 branch offices nationwide.

RELEVANT DISCIPLINARY HISTORY

Respondent does not have any relevant disciplinary history with the Securities and Exchange Commission, any state securities regulators, FINRA, or any other self-regulatory organization.

OVERVIEW

During the period January 1, 2014 to May 24, 2016 (the "Relevant Period"), the Firm failed to establish and maintain a supervisory system reasonably designed to achieve compliance with its obligations under the applicable FINRA rules in connection with its sale of volatility-linked exchange traded products ("Volatility ETPs"). Volatility ETPs are complex products that are typically held for short periods of time as part of a trading

strategy rather than as a buy-and-hold investment. Although the Firm was aware of the unique characteristics of Volatility ETPs, it made these products available for solicited purchases during the Relevant Period, without having a reasonable system in place to ensure that its brokers and customers understood the nature and characteristics of these products or the risks inherent in holding them for long-term periods. During the Relevant Period, certain of the Firm's customers, including those without high risk tolerances or aggressive investment objectives, purchased Volatility ETPs on a solicited basis, held them for lengthy periods of time, and sustained losses. Based on the above conduct, JPMS violated NASD Rule 3010(a),¹ and FINRA Rules 3110(a) and 2010.

FACTS AND VIOLATIVE CONDUCT

A. Background

1. Volatility ETPs

Volatility ETPs attempt to provide exposure to the Chicago Board Options Exchange Volatility Index (the "VIX") by tracking or holding investments in VIX futures, although they do not track the VIX on a one-to-one basis. For Volatility ETPs to maintain continuous exposure to the VIX, a VIX futures position must be rolled over prior to a contract's expiration; therefore, a position with an earlier contract maturity date is sold and replaced by a contract with a more distant maturity date. In the market conditions in which these futures contracts have historically traded, a contract with a more distant maturity date has typically been more expensive than one set to expire sooner. The difference between the proceeds from selling a position and the cost of buying a new one to replace it is called the "roll yield." When an expiring contract is rolled into a more expensive contract, there will be a loss, *i.e.*, a negative roll yield.

In market conditions in which the roll yield is negative, any Volatility ETP that is held for a long period of time is highly likely to lose value. Accordingly, given their complexity and risks, Volatility ETPs are best viewed as short-term products that should be monitored closely.

In January 2009, the iPath Series B S&P 500 VIX Short-Term Futures ETN ("VXX") was introduced as the first Volatility ETP available to retail investors. Other Volatility ETPs subsequently became available. Since their introduction in 2009, Volatility ETP sponsors have warned about the risks associated with such securities. By January 2014, the financial media had long discussed such risks, including the risk of holding the products for long periods of time.

2. JPMS's Sales of Volatility ETPs

JPMS sold Volatility ETPs on a solicited basis through certain lines of business during the Relevant Period. During the Relevant Period, one of those JPMS businesses did not have any restrictions on the sale of Volatility ETPs, and its registered representatives

¹ NASD Rule 3010 was superseded by FINRA Rule 3110 effective December 1, 2014.

could and did solicit customers to purchase VXX and other Volatility ETPs as they were introduced to the marketplace.

Other JPMS businesses used an “approved list” to designate which products its brokers could solicit. A committee at the Firm met regularly to review products and, if deemed appropriate, designate their availability. These JPMS businesses would then decide whether to include a product approved by the committee on their respective approved list. In March 2010, the committee met and considered whether VXX should be made available. A PowerPoint presentation was prepared for the meeting, and contained details on the risks involved with investing in VXX, including negative roll yield. The presentation stated that “VXX seems more appropriate as a tool used by traders than as a buy-and-hold option.” The committee approved VXX for use only in certain non-brokerage accounts, and VXX was added to the “approved list” for those accounts. Then, in June 2011, the committee removed VXX from the “approved list” for the non-brokerage accounts because it believed that VXX had a high tracking error with the VIX, and was being used primarily on an unsolicited basis.

In 2015, a group within the Firm proposed to the committee expanding the availability of VXX and several other products to certain brokerage platforms. The committee in 2015 was not provided with the 2010 PowerPoint related to VXX nor other information about the Firm’s prior approval and then non-approval of VXX. Nor was the committee informed of any reason, from an investment standpoint, why approval for VXX should not be expanded. On April 16, 2015, the committee approved VXX for expansion to certain brokerage platforms. On June 25, 2015, VXX was added to the approved lists for those brokerage customers. Following a FINRA inquiry in a separate investigation, in May 2016 VXX was removed from the approved lists. As noted above, during the Relevant Period, certain of the Firm’s customers purchased Volatility ETPs on a solicited basis and, contrary to their general use as a short-term trading vehicle, held them for lengthy periods of time.

B. JPMS Failed to Establish and Maintain a Supervisory System Reasonably Designed to Achieve Compliance with Its Obligations in Connection with Its Sales of Volatility ETPs.

NASD Rule 3010(a) provided, and FINRA Rule 3110(a) provides, in relevant part that each member shall establish and maintain a system, including written procedures, to supervise the activities of each registered representative, registered principal, and other associated persons that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable NASD and FINRA Rules.

JPMS’s supervisory obligations included ensuring compliance with the suitability rule, FINRA Rule 2111. Under the suitability rule, members and associated persons must have a reasonable basis to believe that a recommended transaction involving a security is suitable for the customer. FINRA’s Regulatory Notice 12-03, issued in January 2012, reminded firms of their heightened supervisory obligations with respect to complex products. The notice identified ETPs that offered retail investors exposure to stock market volatility as a type of complex product that may not be well understood by many

investors. The notice reminded firms of their obligations to conduct a reasonable-basis suitability determination prior to recommending a complex product, and engage in post-approval review, and noted that registered representatives who recommended complex products must understand the features and risks associated with those products. The notice further reminded firms of their obligations under the relevant FINRA rules to ensure that the complex product was appropriate for the particular customer involved, including by consideration of a customer's financial sophistication, investment experience, and risk tolerance.²

As discussed above, the Firm had identified the risks associated with VXX as early as 2010 and the Firm had removed the product from availability for certain non-brokerage accounts in 2011. Nonetheless, the Firm permitted solicited purchases of Volatility ETPs during the Relevant Period without taking reasonable steps to enhance its supervision of these complex products, including to ensure that its brokers understood their potential risks. The Firm did not provide any training or guidance to its brokers or supervisors specifically regarding Volatility ETPs; identify the risks associated with Volatility ETPs in its written supervisory procedures; conduct reasonable post-approval review of the products' performance and risk profile; or take other reasonable steps to supervise solicited sales of the products to customers.

By virtue of the foregoing, JPMS violated NASD Rule 3010(a) (for conduct prior to December 1, 2014), FINRA Rule 3110(a) (for conduct on and after December 1, 2014), and FINRA Rule 2010.

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

1. A censure;
2. A fine of \$325,000; and
3. Restitution in the amount of \$333,619.34, plus interest.

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 hereafter, the monetary sanctions imposed in this matter.

Restitution is ordered to be paid to the customers listed on Attachment A hereto in the total amount of \$333,619.34, plus interest at the rate set forth in Section 6621(a)(2) of the Internal Revenue Code, 26 U.S.C. 6621(a)(2), from the date of each customer's sale or redemption of Volatility ETPs, until the date this AWC is accepted by the National Adjudicatory Council (NAC).

² See also Regulatory Notice 17-32 (October 2017) ("Volatility-Linked Exchange Traded Products") (citing Regulatory Notice 12-03).

A registered principal on behalf of Respondent Firm shall submit satisfactory proof of payment of restitution and pre-judgment interest (separately specifying the date and amount of each paid to each customer listed on Attachment A) or of reasonable and documented efforts undertaken to effect restitution. Such proof shall be submitted by email to EnforcementNotice@finra.org, with a copy to elissa.methkestin@finra.org, from a work-related account of the registered principal of Respondent Firm. The email must identify the Respondent and the case number and include a copy of the check, money order or other method of payment. This proof shall be provided by email to EnforcementNotice@finra.org, with a copy to elissa.methkestin@finra.org, no later than 120 days after acceptance of the AWC.

If for any reason Respondent cannot locate any customer identified in Attachment A after reasonable and documented efforts within 120 days from the date the AWC is accepted, or such additional period agreed to by a FINRA staff member in writing, Respondent shall forward any undistributed restitution and interest to the appropriate escheat, unclaimed property or abandoned property fund for the state in which the customer is last known to have resided. Respondent shall provide satisfactory proof of such action to the FINRA staff member identified above and in the manner described above, within 14 calendar days of forwarding the undistributed restitution and interest to the appropriate state authority.

The imposition of a restitution order or any other monetary sanction herein, and the timing of such ordered payments, does not preclude customers from pursuing their own actions to obtain restitution or other remedies.

Restitution payments to customers shall be preceded or accompanied by a letter, not unacceptable to FINRA staff, describing the reason for the payment and the fact that the payment is being made pursuant to a settlement with FINRA and as a term of this AWC.

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

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 acceptance or rejection of this AWC.

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(s); 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 the subject matter thereof 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: (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. 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 or its staff.

The undersigned, on behalf of the Respondent 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 it 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 herein and the prospect of avoiding the issuance of a Complaint, has been made to induce it to submit it.

June 11, 2020
Date

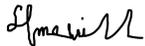
J.P. Morgan Securities LLC
Respondent

By: 

Print Name: William H. Freilich

Title: Managing Director

Reviewed by:



Susan L. Merrill
Counsel for Respondent
Sidley Austin LLP
787 Seventh Avenue
New York, NY 10019
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Accepted by FINRA:

6/22/2020
Date

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



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ATTACHMENT A

SCHEDULE OF RESTITUTION

Customer #	Account #	Restitution Amount (Exclusive of Interest)
1	*6257	\$7,398.52
2	*8997	\$1,409.04
3	*5467	\$8,429.86
4	*2141	\$7,888.88
5	*3042	\$2,037.20
6	*5284	\$26,460.38
7	*4438	\$28,082.88
8	*0445	\$9,641.43
9	*5321	\$22,816.38
10	*2090	\$8,965.70
11	*1516	\$5,654.15
12	*0256	\$28,448.23
13	*8303	\$20,785.11
14	*9509	\$9,030.41
15	*8698	\$46,110.34
16	*5151	\$8,324.27
17	*5827	\$3,715.37
18	*5786	\$3,221.48
19	*2993	\$10,450.44
20	*2750	\$307.72
21	*0405	\$17,699.60
22	*2439	\$3,163.73
23	*2902	\$16,328.47
24	*2206	\$2,867.55
25	*6180	\$5,553.90
26	*9897	\$243.52
27	*5901	\$472.88
28	*0305	\$3,835.00
29	*6006	\$4,309.31
30	*1144	\$19,967.59