FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER, AND CONSENT
NO. 2015047806501

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

RE: Allstate Financial Services, LLC, Respondent
CRD No. 18272

Pursuant to FINRA Rule 9216 of FINRA's Code of Procedure, Allstate Financial Services, LLC ("AFS") 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 AFS alleging violations based on the same factual findings described herein.

I.

ACCEPTANCE AND CONSENT

A. AFS 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

AFS is a retail broker that has been registered with FINRA or its predecessor since 1986. As of November 2016, AFS had 7,411 branches and 8,865 registered persons.

RELEVANT DISCIPLINARY HISTORY

AFS does not have any history of relevant discipline.

OVERVIEW

Due to five systemic problems, some of which lasted as long as fifteen years, AFS failed to supervise certain communications and transactions, retain certain records, and provide customers with certain required notices and information.

First, AFS omitted approximately 3,500 secondary email accounts from the list of email accounts that the firm monitored. As a result, AFS did not review approximately 44 million emails, which included approximately 11,000 emails

with customers or otherwise relating to the firm's securities business.[1] AFS did not retain the emails relating to its securities business.

Second, AFS did not adequately supervise the use of several programs used by its registered persons to create consolidated reports, which are documents that typically combine information about most or all of a customer's financial assets, regardless of where they are held. Nor did AFS appropriately retain the consolidated reports that its registered persons created. Those failures affected approximately several thousand consolidated reports.

Third, AFS's records for approximately 9,000 customer accounts were missing or incomplete, and were not linked to the firm's software system for sending various notices. As a result, AFS did not verify the identity of certain of those accounts' owners, determine whether recommendations were suitable for those customers, and send required periodic account records and notices explaining the firm's privacy policies to those customers.

Fourth, AFS paid commissions totaling $587,000 in connection with securities transactions to approximately 4,400 unregistered persons who either were previously registered with the firm or at the time worked for affiliated insurance companies. Most of the payments were trailing commissions that AFS paid to persons who had been registered with the firm, but no longer were registered when they received the payments.

Fifth, AFS incorrectly labeled approximately 2,900 customers' accounts as closed due to an error during a system conversion. As a result, those customers did not receive required periodic account records and notices explaining AFS's privacy policies.

As a result of those problems, AFS violated several federal securities laws and NASD and FINRA rules.

FACTS AND VIOLATIVE CONDUCT

1. AFS failed to review, retain, and supervise email

AFS's registered persons have a primary business email account and some of those persons also have one or more secondary email accounts. The secondary email accounts were typically created as a result of registered persons' affiliation with a satellite insurance office of AFS's parent company, Allstate Insurance Company.

AFS has allowed its registered persons to use email for communicating with customers about securities in limited ways since August 2007 and generally since April 2009. Before July 2014, however, AFS did not review or retain messages from approximately 3,400 secondary email accounts or supervise the use of those

[1] This number is an extrapolation from emails that AFS recovered.

email accounts. AFS's lack of review affected approximately 44 million messages, and the firm's lack of retention affected approximately 11,000 emails relating to AFS's securities business, including communications with customers.

Those problems occurred because AFS inadvertently did not add the secondary email accounts to the list of email accounts that the firm's email software system monitored, and also because the firm did not employ adequate measures to ensure that its software system captured every relevant email.

Those problems implicated three types of regulatory obligations. First, from December 2007 to November 2014, NASD Rule 3010(d)(2) required every firm to review "incoming and outgoing ... electronic correspondence with the public relating to its ... securities business."

Second, the Securities Exchange Act of 1934 ("Exchange Act") and several rules required AFS to retain email messages. Exchange Act Rule 17a-4(b)(4) requires every registered broker-dealer to preserve for at least three years "all communications ... relating to its business" that the firm receives and sends. During the relevant period, NASD Rule 3010(d)(3) required firms to "retain correspondence of registered representatives relating to its ... securities business." Exchange Act § 17(a) requires every registered broker-dealer to "keep for prescribed periods such records ... as the Commission, by rule, prescribes." Before December 5, 2011, NASD Rule 3110(a) required firms to "preserve ... correspondence in conformity with all applicable laws, rules, regulations and statements of policy promulgated thereunder." Since that date, FINRA Rule 4511 has required firms to "preserve books and records as required under the FINRA rules, the Exchange Act and the applicable Exchange Act rules."

Third, several NASD and FINRA rules required AFS to supervise email. Before December 1, 2014, NASD Rule 3010(a) required firms to "establish and maintain a system to supervise the activities of each registered representative, registered principal, and other associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable NASD Rules" and NASD Rule 3010(b) required firms to "establish, maintain, and enforce written procedures to supervise the types of business in which it engages and to supervise the activities of registered representatives, registered principals, and other associated persons that are reasonably designed to achieve compliance with applicable securities laws and regulations, and with the applicable Rules of NASD." Since December 1, 2014, FINRA Rule 3110(a) and 3110(b) have imposed substantially similar requirements.

Violating any securities law or rule before December 15, 2008 also violates NASD Rule 2110, which provides that "[a] member, in the conduct of its business, shall observe high standards of commercial honor and just and equitable principles of trade." Such a violation after December 15, 2008 violates that rule's identical successor, FINRA Rule 2010.

By failing to review approximately 44 million messages in its registered persons' secondary accounts, AFS violated NASD Rules 2110 and 3010 and FINRA Rule 2010. By failing to retain approximately 11,000 emails relating to its securities business, AFS violated Exchange Act § 17, Exchange Act Rule 17a-4, NASD Rules 2110, 3010, and 3110, and FINRA Rules 2010 and 4511. And, by failing to supervise the use of its registered persons' secondary email accounts, failing to test its software system for monitoring email, and by failing to address those issues in its written supervisory procedures, AFS violated NASD Rules 2110 and 3010 and FINRA Rules 2010 and 3110.

2. AFS failed to retain and supervise consolidated reports

Consolidated reports typically combine information about most or all of a customer's financial assets, including those that are held away from the reporting firm, and may also address the assets' performance. Consolidated reports often are highly customized and do not replace required account statements. In Regulatory Notice 10-19, FINRA advised firms that consolidated reports "raise a number of regulatory concerns" and noted that firms "must ensure that the size and complexity of [a] consolidated reporting program does not exceed the firm's ability to supervise the activity and to subject it to a rigorous system of internal controls."

Since 2009, AFS has allowed its registered persons to prepare customized consolidated reports for customers, using one of several programs. The consolidated reports may include assets that the customers do not hold at AFS. From 2009 to January 2015, AFS's registered persons generated an unknown number of, but at least four thousand, consolidated reports.

During that period, AFS did not supervise its registered persons' use of consolidated reports or address them in the firm's written supervisory procedures. For example, AFS did not train its registered persons to use consolidated reports, assign responsibility for reviewing consolidated reports to its supervisors, train its supervisors how to review consolidated reports, or verify information in consolidated reports.

In addition, AFS did not retain copies of all consolidated reports. Although AFS required its registered persons to retain copies of retail communications generally, the firm did not adequately instruct its registered persons that its retention policy applied to consolidated reports. As a result, AFS has very few records of consolidated reports that its representatives distributed to customers from 2009 to January 2015.

By failing to retain its registered persons' consolidated reports, AFS violated Exchange Act § 17 and Rule 17a-4, NASD Rules 2110, 3010, and 3110, and FINRA Rules 2010 and 4511. By failing to supervise its registered persons' use of consolidated reports, AFS violated NASD Rules 2110 and 3010 and FINRA Rules 2010 and 3110.

3. AFS had missing and incomplete account records

From 2001 to 2016, AFS's records for approximately 9,200 customer accounts holding mutual funds and variable products were missing or incomplete, and those accounts were not linked to the firm's software system that generated various notices. That problem resulted from several errors. AFS's registered persons had submitted some of the accounts directly to product sponsors, bypassing the firm's systems; that practice violated a policy that the firm did not consistently enforce. Other accounts were transferred to AFS from other firms without being properly documented. And, information about other accounts was entered incorrectly, due to manual errors.

As a result, AFS did not verify the identity of the owners of approximately 7,000 customer accounts. AFS also did not obtain information about those customers' investment profiles or confirm that recommendations for them were suitable. Finally, AFS did not send approximately 60,000 privacy notices and approximately 11,000 required periodic account records to those customers.

From April 24, 2002 to December 31, 2009, NASD Rule 3011 required firms to "develop and implement a written anti-money laundering program reasonably designed to achieve and monitor the member's compliance with the requirements of the Bank Secrecy Act ... and [its] implementing regulations." Since January 1, 2010, FINRA Rule 3310 has imposed similar requirements. The Bank Secrecy Act requires financial institutions, among other things, to "establish anti-money laundering programs" including "reasonable procedures for [] verifying the identity of any person seeking to open an account to the extent reasonable and practicable; [and] maintaining records of the information used to verify a person's identity, including name, address, and other identifying information."[2] That statute's implementing regulations require firms to "establish, document, and maintain a written Customer Identification Program" that includes, among other things, "procedures for verifying the identity of each customer" that "enable the broker-dealer to form a reasonable belief that it knows the true identity of each customer."[3]

Before July 9, 2012, NASD Rule 2310 required firms to have reasonable grounds for believing that a recommendation to purchase, sell, or exchange a security is suitable for the customer, based on information that the customer disclosed, and also required firms to make reasonable efforts to obtain information about the customer's investment profile. Since that date, FINRA Rule 2111(a) has required firms to have "a reasonable basis to believe that a recommended transaction or investment strategy involving a security or securities is suitable for the customer," based on reasonably diligent efforts to ascertain the customer's investment profile.

[2] *See* 31 U.S.C. § 5318(h), (*l*).

[3] *See* 31 C.F.R. §§ 103.122(a) (before Mar. 1, 2011), 1023.220(a) (since Mar. 1, 2011).

Regulation S-P § 248.5(a)(1) requires every firm to "provide a clear and conspicuous notice to customers that accurately reflects [the firm's] privacy policies and practices not less than annually during the continuation of the customer relationship." Exchange Act Rule 17a-3(a)(17)(i)(B)(1) requires every registered broker and dealer to make a record indicating that the firm furnished every customer with a copy of his or her account record or an equivalent document within thirty days after the opening of his or her account, and subsequently "at intervals [of] no greater than thirty-six months" unless the firm was not "required to make a suitability determination" about the account during that period. Before December 5, 2011, NASD Rule 3110(a) required firms to "make ... records ... in conformity with all applicable laws, rules, regulations and statements of policy promulgated thereunder...." Since that date, FINRA Rule 4511 has required firms to "make ... records as required under the FINRA rules, the Exchange Act and the applicable Exchange Act rules."

By failing to verify the identity of the owners of approximately 7,000 accounts as the Bank Secrecy Act and its implementing regulations require, AFS violated NASD Rules 2110 and 3011 and FINRA Rules 2010 and 3310. By failing to obtain adequate information about the investment profiles of the owners of approximately 9,200 accounts, precluding any determination whether recommendations about mutual funds and variable products were suitable for those customers, AFS violated NASD Rules 2110 and 2310 and FINRA Rules 2010 and 2111. And, by failing to create and send approximately 60,000 required privacy notices and approximately 11,000 required periodic account records, AFS violated Regulation S-P § 248.5, Exchange Act Rule 17a-3, NASD Rules 2110 and 3110, and FINRA Rules 2010 and 4511.

4. AFS paid commissions to unregistered persons

From 1999 to 2014, AFS paid commissions totaling approximately $587,000 to approximately 4,400 unregistered persons in connection with securities transactions. The recipients were agents of AIC or an affiliated insurance company, and most of the payments were trailing or renewal commissions on mutual funds and variable products.

Approximately 94% of the payments were made to people who had been registered with AFS, but were no longer registered when they received the payments. Those payments resulted from a flaw in AFS's commission processing system, which checked recipients' registration status before remitting types of commissions on new sales but did not do so with respect to trailing commissions.

Approximately 3% of the payments were made to 156 persons who never registered with AFS. The remaining payments were made to 100 persons who registered with AFS at some time after receiving the payments. The latter two groups received payments by virtue of having purchased books of business from registered agents, as AFS's commission processing system did not check the purchaser's registration status before remitting trailing commissions.

Before August 24, 2015, NASD Rule 2420(b) generally prohibited firms from paying commissions from securities transactions to unregistered persons. By paying commissions from securities transactions to approximately 4,400 people who were not registered or associated with any member of FINRA at the time of the payments, AFS violated NASD Rules 2110 and 2420 and FINRA Rule 2010.

5. AFS incorrectly labeled accounts as closed

From 2009 to 2014, AFS incorrectly labeled approximately 2,900 customer accounts as closed in a database. This incorrect labeling occurred when AFS moved the database to a new system, due to user errors and a lack of procedures for identifying such errors. After moving the database, AFS periodically noticed that certain accounts were incorrectly marked as closed, but the firm did not systematically investigate the problem or discover its cause until March 2014, in connection with another system conversion. As a result, AFS did not create or send approximately 6,500 required privacy notices and approximately 2,200 required periodic account records.

Consequently, AFS violated Exchange Act Rule 17a-3, Regulation S-P § 248.5, NASD Rules 2010 and 3110, and FINRA Rules 2010 and 4511.

OTHER FACTORS

In resolving this matter, FINRA recognized AFS's extraordinary cooperation by (1) self-reporting three of its problems—those involving secondary email accounts, payments of commissions to unregistered persons, and missing and incomplete account records—and (2) substantially assisting FINRA with its investigation of the firm's payments of commissions to unregistered persons.

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

Censure
Fine of $1,000,000

AFS agrees to pay the fine imposed in this matter upon notice that this AWC has been accepted and that such payment is due and payable. AFS has submitted an Election of Payment form showing the method by which AFS proposes to pay that fine. AFS specifically and voluntarily waives any right to claim that it is unable to pay, now or at any time hereafter, that fine.

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

II.

WAIVER OF PROCEDURAL RIGHTS

AFS specifically and voluntarily waives the following rights granted under FINRA's Code of

Procedure:

A. To have a Complaint issued specifying the allegations against AFS;

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, AFS 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.

AFS 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

AFS 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 AFS; and

C. If accepted:

1. this AWC will become part of AFS's permanent disciplinary record and may be considered in any future actions brought by FINRA or any other regulator against AFS;

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. AFS 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. AFS 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 AFS'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. AFS may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. AFS 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 AFS's behalf, certifies that a person duly authorized to act on its behalf has read and understood all of the provisions of this AWC and has been given a full opportunity to ask questions about it; that AFS 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 AFS to submit it.

12/12/16
Date (mm/dd/yyyy)

Mary K Nelson
Allstate Financial Services, LLC

By: Mary K Nelson
President & CEO

Reviewed by:

Brian L Rubin

Brian Rubin
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Accepted by FINRA:

12/15/2016
Date

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

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