

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 10959 / July 30, 2021

SECURITIES EXCHANGE ACT OF 1934
Release No. 92538 / July 30, 2021

ADMINISTRATIVE PROCEEDING
File No. 3-20444

<p>In the Matter of</p> <p>HERBERT J. SIMS & CO., INC.</p> <p>Respondent.</p>
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ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS, PURSUANT TO SECTION 8A OF THE SECURITIES ACT OF 1933 AND SECTION 15(b) OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER

I.

The Securities and Exchange Commission (“Commission”) deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 8A of the Securities Act of 1933 (“Securities Act”) and Section 15(b) of the Securities Exchange Act of 1934 (“Exchange Act”) against Herbert J. Sims & Co., Inc. (“HJS” or “Respondent”).

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the “Offer”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over it and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Section 8A of the Securities Act of 1933 and Section 15(b) of the Securities Exchange Act of 1934, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order (“Order”), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds¹ that:

Summary

1. These proceedings arise out of HJS, a registered broker-dealer, making unsuitable recommendations of certain highly-complex and high-risk variable interest rate structured products ("VRSPs") to certain of its retail brokerage customers from January 2015 through April 2018 (the "relevant period"). Thirteen registered representatives from HJS's Boca Raton, Florida branch office ("HJS RRs") recommended VRSPs to forty-five customers for whom such investments were unsuitable in light of their financial situations and needs ("Customers"). When a broker-dealer recommends an investment to its customers, it must determine, based on each customer's investment profile at the time of a recommended transaction, that the recommended investment is suitable for the customer in light of, among other factors, the customer's specific investment objectives, financial condition, risk tolerance, and age.

2. The VRSPs that HJS recommended and sold to the Customers are structured securities with maturity periods of fifteen years or more.² They contain both a bond component and an embedded derivative component. As a result, the VRSPs share certain characteristics with traditional corporate bonds, including fixed maturity periods and periodic interest payments. The VRSPs also initially pay a high fixed introductory rate, for a period of one to five years. Unlike traditional corporate bonds, however, the VRSPs convert to a variable rate after the initial fixed rate period. The variable rate is based on formulas tied to differences in Constant Maturity Swap ("CMS") rates for long-term and short-term U.S. Treasury obligations, as well as the performance of certain referenced assets such as stock indices. Importantly, during the variable rate period, the VRSPs no longer guarantee interest payments. Furthermore, the VRSPs are "principal-at-risk" securities, which means that investors can also lose some or all of their invested principal at maturity if the VRSPs' derivative components fail to perform within certain pre-determined ranges.

3. Despite these complexities and risks and the Customers' investment profiles, HJS RRs recommended VRSPs to the Customers. HJS RRs made these recommendations even though they knew or should have known, among other factors, that the Customers were at or approaching retirement age, with low or moderate risk tolerance, primary investment objective of income or long term growth, annual income of less than \$250,000, and, in certain cases, net worth of less than \$500,000 and a desire to minimize exposure of invested principal to loss. By making these unsuitable recommendations of VRSPs to the Customers, HJS and the HJS RRs violated Sections 17(a)(2) and 17(a)(3) of the Securities Act.

¹ The findings herein are made pursuant to Respondent's Offer and are not binding on any other person or entity in this proceeding.

² The VRSPs recommended and sold by HJS consisted of so-called "steepeners," "curve accrual notes," and "non-inversion notes."

4. Between January 2015 and April 2018, HJS also failed reasonably to supervise the HJS RRs with a view to preventing and detecting their violations of Sections 17(a)(2) and 17(a)(3) of the Securities Act arising from the unsuitable recommendations. HJS failed reasonably to implement its customer-specific suitability policies and procedures to determine whether registered representatives were making suitable recommendations to their customers, and that HJS branch managers and other supervisory personnel were appropriately supervising those recommendations.

Respondent

5. Herbert J. Sims & Co, Inc., a Delaware corporation with its principal place of business in Fairfield, Connecticut, is registered with the Commission as a broker-dealer.

Background

6. Beginning in January 2015 and continuing through April 2018, HJS RRs recommended and sold VRSPs to the Customers. The VRSPs were structured securities, typically issued by large well-known financial institutions, with stated fixed maturity periods and periodic interest payments. These characteristics made the VRSPs appear to be similar to traditional corporate bonds. The VRSPs, however, differ from traditional corporate bonds in several important ways.

7. The recommended VRSPs initially offer fixed rates for one to five years. After the fixed periods end, however, the VRSPs switch to variable rates, based on formulas tied to the spread between CMS rates for longer term and shorter term U.S. Treasury obligations. Accordingly, during the variable period, depending on the performance of the CMS rates, investors are at risk of receiving little or even no interest payments from the VRSPs. Moreover, certain VRSPs include an additional contingency before investors can be paid interest during the variable rate period. In particular, these VRSPs only make periodic interest payments if one or more referenced assets, such as the S&P 500 and/or Russell 2000 indices, remain above specified levels. Consequently, when the VRSPs no longer are in the fixed rate period, investors are not guaranteed to receive any interest payments. The prospectuses for several of the recommended VRSPs expressly state that there is “no assurance that [investors] will receive a contingent interest payment on any interest payment date” and that “the securities are not a suitable investment for investors who require regular fixed income payments, since the contingent interest payments are variable and might be zero.”

8. The recommended VRSPs are “principal-at-risk” securities, which means that investors can lose some or all of their invested principal if referenced assets, such as the S&P 500 and/or Russell 2000 indices, fail to perform above certain pre-determined ranges at maturity. The prospectuses for several of the recommended VRSPs expressly warn: “There is no minimum payment at maturity. Accordingly, investors may lose up to their entire investment in the securities.”

9. The recommended VRSPs typically lack an active secondary market, in contrast to traditional corporate bonds. The VRSPs that were recommended to the Customers by the HJS RRs are not listed on any securities exchange and, as the prospectus for one of the VRSPs states, “dealers are not likely to make a secondary market for the securities, the price at which [investors] may be able to trade [their] securities is likely to depend on the price, if any, at which [the issuer] (or its affiliates) is willing to buy the securities. If [investors] have to sell [their] securities prior to maturity, [they] may not be able to do so or [they] may have to sell them at a substantial loss.” The lack of an active market for VRSPs is significant in light of their fixed maturity periods of fifteen years or more.

HJS RRs Made Unsuitable Recommendations of VRSPs to the Customers

10. Before recommending a security to a customer, a broker-dealer is required to make a determination that a particular investment is “suitable for the client in light of the client’s investment objectives, as determined by the client’s financial situation and needs.” *See, e.g., Steven E. Muth and Richard J. Rouse*, Exch. Act Rel. No. 52551, at *18 (Oct. 3, 2005) (Comm. Op.). Broker-dealers who make unsuitable recommendations violate the anti-fraud provisions of the federal securities laws, including Sections 17(a)(2) and 17(a)(3) of the Securities Act.

11. During the relevant period, HJS RRs recommended the VRSPs to forty-five customers. Information available to the HJS RRs, which included the Customers’ account opening documents, investment profiles, and other information provided by the Customers, reflected that the Customers were at or approaching retirement age, with low or moderate risk tolerance, primary investment objective of income or long term growth, annual income of less than \$250,000, and, in certain cases, net worth of less than \$500,000. Customer information that was available to the HJS RRs indicated that many of the Customers also sought to minimize exposure of their invested principal to loss.

12. At the time that they recommended the VSRPs, the HJS RRs were, or should have been, familiar with the Customers’ investment profiles, and thus, knew or should have known that these recommendations were unsuitable because they did not align with their particular profiles. For example, HJS RRs recommended VRSPs to the Customers described below, when those products were inconsistent with those Customers’ stated risk tolerances and investment objectives, including, among other things, their desire to minimize exposure of their invested principal to loss:

a. One HJS RR recommended the purchase of over \$30,000 in VRSPs to a 69-year-old customer with a low risk tolerance, an investment objective of income, an annual income of less than \$25,000, and a net worth of less than \$185,000.

b. Another HJS RR recommended the purchase of over \$49,000 in VRSPs to an 87-year-old customer with a moderate risk tolerance, an investment objective of income, an annual income of less than \$25,000, and a net worth of less than \$300,000.

c. A third HJS RR recommended the purchase of nearly \$18,000 in VRSPs to a 68-year-old customer with a low risk tolerance, an investment objective of income, an annual income of less than \$25,000, and a net worth of less than \$455,000.

13. In light of the Customers' stated financial situations and needs, including their risk tolerance, investment objective, financial condition, and age, the VRSPs that were recommended to them by the HJS RRs were unsuitable investments for the Customers.

14. As a result of the conduct described above, HJS and HJS RRs violated Sections 17(a)(2) and 17(a)(3) of the Securities Act.

HJS Failed Reasonably to Supervise the HJS RRs

15. Section 15(b)(4)(E) of the Exchange Act provides that the Commission may sanction a registered broker-dealer for failing reasonably to supervise, with a view to preventing and detecting violations of the federal securities laws, another person subject to their supervision who commits such a violation.

16. HJS's Written Supervisory Procedures ("WSPs") that were in effect during the relevant period included policies and procedures concerning suitability. These policies and procedures required HJS RRs to comply with the customer-specific suitability requirements set forth in FINRA Rule 2111.

17. FINRA Rule 2111 provides that, when making a customer-specific suitability determination, the broker-dealer must consider factors such as its customer's age, other investments holdings, financial condition and needs, tax status, investment objectives, risk tolerance, investment experience, investment time horizon, liquidity needs and any other information provided by the customer.

18. HJS's WSPs required the firm's "designated supervising principals" for retail sales to supervise registered representatives for compliance with the firm's suitability requirements, including determining whether the registered representatives were aware of and considered a customer's investment profile information when recommending investments to the customer. HJS's WSPs also required the firm and the supervisors to review all transactions for suitability during "regular and random reviews of client accounts." Moreover, HJS's branch managers or their designees specifically were tasked with promptly reviewing every transaction on the daily trade blotters for suitability.

19. During the relevant period, HJS failed reasonably to implement its customer-specific suitability policies and procedures. Specifically, HJS failed reasonably to determine whether HJS RRs and supervisory personnel were complying with these policies and procedures. For example, for significant periods of time in the Boca Raton branch office, HJS failed to implement its own requirement that daily trade blotters be reviewed for, among other things, suitability. For weeks, and sometimes months, during this period, there is no indication that daily transactions were

reviewed for suitability. Indeed, for various periods totaling more than eight months, there is no record of any supervisory personnel reviewing trade blotters for HJS's Boca Raton branch office. As a result of these supervisory failures, HJS failed reasonably to prevent and detect the HJS RRs' unsuitable recommendations of VRSPs to the Customers, as described above. When supervisory personnel did review trade blotters for HJS's Boca Raton branch office, they failed reasonably to identify any of the unsuitable recommendations of VRSPs that the HJS RRs had made to the Customers.

20. As a result of the conduct described above, HJS failed reasonably to supervise the HJS RRs with a view to preventing and detecting their violations of Sections 17(a)(2) and (a)(3) by making unsuitable recommendations of VRSPs. If HJS had reasonably supervised the HJS RRs, it is likely that the firm would have prevented and detected the HJS RRs' violations of Sections 17(a)(2) and 17(a)(3) of the Securities Act

Undertakings

21. HJS has undertaken to:

a. Retain, within thirty (30) days of the date of entry of the Order, at its own expense, the services of an Independent Consultant not unacceptable to the Division of Enforcement of the Commission ("Division of Enforcement"), to review: (i) HJS's policies and procedures designed to prevent and detect unsuitable recommendations of structured products; and (ii) HJS's systems to implement these policies and procedures.

b. Provide to the Division of Enforcement staff, within thirty (30) days of retaining the Independent Consultant, a copy of an engagement letter detailing the Independent Consultant's responsibilities, which shall include the review described above in Paragraph 21(a).

c. Require the Independent Consultant, at the conclusion of the review, which in no event shall be more than one hundred eighty (180) days after the date of entry of the Order, to submit to HJS and the Division of Enforcement a report of the Independent Consultant. The report shall address the supervisory issues described above and shall include (i) a description of the review performed, (ii) the Independent Consultant's recommendations for any changes or improvements to the policies, procedures, and practices of HJS, and (iii) a procedure for implementing the recommended changes or improvements to such policies, procedures, and practices.

d. Adopt, implement, and maintain all policies, procedures, and practices recommended in the report of the Independent Consultant, provided however, that within thirty (30) days after the date of the applicable report, Respondent shall in writing advise the Independent Consultant and the Commission staff of any recommendations that it considers to be unduly burdensome, impractical, or inappropriate. With respect to any recommendation that the Respondent considers to be unduly burdensome, impractical, or

inappropriate, Respondent need not adopt that recommendation at that time but Respondent shall instead propose in writing to the Independent Consultant and Commission staff an alternative policy or procedure designed to achieve the same objective or purpose as that recommended by the Independent Consultant. As to any of the Independent Consultant's recommendations about which HJS and the Independent Consultant do not agree, such parties shall attempt in good faith to reach agreement within two hundred forty (240) days of the date of the entry of the Order. In the event that HJS and the Independent Consultant are unable to agree on an alternative proposal, HJS and the Independent Consultant shall jointly confer with the Division of Enforcement staff to resolve the matter. In the event that, after conferring with the Division of Enforcement staff, HJS and the Independent Consultant are unable to agree on an alternative proposal, HJS will abide by the recommendations of the Independent Consultant.

e. Cooperate fully with the Independent Consultant in its review, including making such information and documents available as the Independent Consultant may reasonably request, and by permitting and requiring HJS's employees and agents to supply such information and documents as the Independent Consultant may reasonably request.

f. That, in order to ensure the independence of the Independent Consultant, HJS (i) shall not have the authority to terminate the Independent Consultant without prior written approval of the Director of the Division of Enforcement; and (ii) shall compensate the Independent Consultant, and persons engaged to assist the Independent Consultant, for services rendered pursuant to the Order at their reasonable and customary rates.

g. That no later than twelve (12) months after the date of entry of the Order, HJS shall direct the Independent Consultant to conduct a review of HJS's efforts to implement each of the recommendations made by the Independent Consultant and, upon the completion of the Independent Consultant's follow-up review, HJS shall direct the Independent Consultant to submit a report to the staff of the Division of Enforcement no later than fifteen (15) months after the date of the entry of the Order. HJS shall direct the Independent Consultant to describe in the follow-up report the details of HJS's efforts to implement each of the Independent Consultant's recommendations and state whether HJS has fully complied with each of the Independent Consultant's recommendations.

h. Require the Independent Consultant to enter into an agreement that provides that for the period of engagement and for a period of two years from completion of the engagement, the Independent Consultant shall not enter into any employment, consultant, attorney-client, auditing or other professional relationship with HJS, or any of its present or former affiliates, directors, officers, employees, or agents acting in their capacity. The agreement will also provide that the Independent Consultant will require that any firm with which he/she is affiliated or of which he/she is a member, and any person engaged to assist the Independent Consultant in performance of his/her duties under this Order shall not, without prior written consent of the Director of the Division of Enforcement enter into any employment, consultant, attorney-client, auditing or other professional relationship with

HJS, or any of its present or former affiliates, directors, officers, employees, or agents acting in their capacity as such for the period of the engagement and for a period of two years after the engagement.

i. The reports by the Independent Consultant will likely include confidential financial, proprietary, competitive business or commercial information. Public disclosure of the reports could discourage cooperation, impede pending or potential government investigations or undermine the objectives of the reporting requirement. For these reasons, among others, the reports and the contents thereof are intended to remain and shall remain non-public, except (1) pursuant to court order, (2) as agreed to by the parties in writing, (3) to the extent that the Commission determines in its sole discretion that disclosure would be in furtherance of the Commission's discharge of its duties and responsibilities, or (4) is otherwise required by law.

j. Certify, in writing, compliance with the undertakings set forth above. The certification shall identify the undertaking(s), provide written evidence of compliance in the form of a narrative, and be supported by exhibits sufficient to demonstrate compliance. The Division of Enforcement staff may make reasonable requests for further evidence of compliance, and HJS agrees to provide such evidence. The certification and report material shall be submitted to Yuri B. Zelinsky, Assistant Director, Division of Enforcement, with a copy to the Office of the Chief Counsel of the Division of Enforcement, no later than sixty (60) days from the date of the completion of the undertakings.

k. For good cause shown and upon timely application by the Independent Consultant or HJS, the Division of Enforcement staff may extend any of the deadlines set forth above.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in Respondent HJS's Offer.

Accordingly, pursuant to Section 8A of the Securities Act and Section 15(b)(4) of the Exchange Act, it is hereby ORDERED that:

A. Respondent HJS cease and desist from committing or causing any violations and any future violations of Sections 17(a)(2) and 17(a)(3) of the Securities Act.

B. Respondent HJS is censured.

C. Respondent HJS shall, within ten (10) days of the entry of this Order, pay a civil money penalty in the amount of \$250,000 to the Securities and Exchange Commission for transfer to the general fund of the United States Treasury, subject to Exchange Act Section 21F(g)(3). If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. § 3717. Payment must be made in one of the following ways:

- (1) Respondent may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;
- (2) Respondent may make direct payment from a bank account via Pay.gov through the SEC website at <http://www.sec.gov/about/offices/ofm.htm>; or
- (3) Respondent may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center
Accounts Receivable Branch
HQ Bldg., Room 181, AMZ-341
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying Herbert J. Sims & Co., Inc. as a Respondent in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to Jennifer Leete, Associate Director, Division of Enforcement, Securities and Exchange Commission, 100 F St., N.E., Washington, DC 20549-5720B.

D. Amounts ordered to be paid as civil money penalties pursuant to this Order shall be treated as penalties paid to the government for all purposes, including all tax purposes. To preserve the deterrent effect of the civil penalty, Respondent HJS agrees that in any Related Investor Action, it shall not argue that it is entitled to, nor shall it benefit by, offset or reduction of any award of compensatory damages by the amount of any part of Respondent's payment of a civil penalty in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, Respondent agrees that it shall, within 30 days after entry of a final order granting the Penalty Offset, notify the Commission's counsel in this action and pay the amount of the Penalty Offset to the Securities and Exchange Commission. Such a payment shall not be deemed an additional civil penalty and shall not be deemed to change the amount of the civil penalty imposed in this proceeding. For purposes of this paragraph, a "Related Investor Action" means a

private damages action brought against Respondent by or on behalf of one or more investors based on substantially the same findings in this Order instituted by the Commission in this proceeding.

E. Respondent HJS shall comply with the undertakings enumerated in Section III, above.

By the Commission.

Vanessa A. Countryman
Secretary