FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER, AND CONSENT
NO. 2021071994802

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

RE: Paulson Investment Company, LLC (Respondent)
Member Firm
CRD No. 5670

Pursuant to FINRA Rule 9216, Respondent Paulson Investment Company, LLC 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 accepts and consents to the following findings by FINRA without admitting or denying them:

BACKGROUND

Paulson Investment Company, LLC (Paulson) has been a member of FINRA since 1971. The firm is headquartered in Lake Oswego, Oregon, and has approximately 65 registered persons and 8 registered branch offices.[1]

OVERVIEW

From January 2016 through May 2019, Paulson failed to reasonably supervise unsuitable recommendations to purchase variable interest rate structured products that three firm representatives made to approximately 70 customers. As a result, the firm violated FINRA Rules 3110 and 2020.

FACTS AND VIOLATIVE CONDUCT

A. Applicable Rules

FINRA Rule 3110(a) requires a member firm to 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. FINRA Rule 3110(b) requires a member firm to establish, maintain, and enforce

[1] For more information about the firm, including prior regulatory events, visit BrokerCheck® at www.finra.org/brokercheck.

written procedures to supervise the types of business in which it engages and the activities of its associated persons that are reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable FINRA rules. A violation of FINRA Rule 3110 also is a violation of FINRA Rule 2010, which requires member firms to "observe high standards of commercial honor and just and equitable principles of trade" in the conduct of their business.

FINRA Rule 2111 requires member firms and their associated persons to have a reasonable basis to believe that a recommended securities transaction or investment strategy is suitable for a customer, based on information obtained through the reasonable diligence of the firm or associated person to ascertain the customer's investment profile. A customer's investment profile includes, but is not limited to, the customer's age, other investments, financial situation and needs, investment objectives, investment experience, investment time horizon, liquidity needs, and risk tolerance. A recommended securities transaction or investment strategy may be unsuitable if it is inconsistent with a customer's investment profile, or if it results in a concentration in a particular security or category of securities that creates a risk of loss inconsistent with the customer's investment profile.

B. Variable Interest Rate Structured Products

Variable interest rate structured products (VRSPs) are a category of complex structured products that initially pay interest at a fixed, above-market "teaser" rate for a short period of time, typically one year, before switching to a floating interest rate that is based on a reference index or asset. VRSPs typically have long maturities, generally between 10 and 30 years.

A "steepener" is one type of VRSP that pays a high teaser interest rate, usually between 8% and 10% for the first year, and then resets to a floating interest rate based on the spread between longer- and shorter-term interest rates (*i.e.*, the steepness of the yield curve), commonly the spread between the 30-Year Constant Maturity Swap (CMS) rate and 2-Year CMS rate. Because the spread between longer- and shorter-term interest rates can compress—meaning that the yield curve can flatten—investors holding steepeners can earn little or zero interest for years.

Additionally, there is no guaranteed secondary market for steepeners and thus—as non-conventional investments, which are discussed in FINRA Notice to Member 03-71—the products tend to have less market liquidity, less transparency as to their pricing and value, and may entail significant credit risks. During periods when the yield curve flattens, investors seeking to sell the products before maturity in the secondary market may incur losses of principal. As an additional risk, certain VRSPs—including all of the VRSPs discussed below—do not guarantee a return of the investor's principal at maturity. Therefore, depending on the performance of the underlying reference index or asset, customers who purchase such products could lose some or all of their principal at maturity.

C. Paulson Failed To Reasonably Supervise Recommendations To Purchase VRSPs

Between January 2016 and May 2019, three Paulson representatives made unsuitable recommendations that their customers purchase VRSPs. First, the representatives recommended that 42 customers with either low or moderate risk tolerances, or with a "growth" investment objective (*i.e.*, not an "aggressive" or "speculative" investment objective) purchase VRSPs. Such recommendations were unsuitable for those customers in light of the substantial risks of VRSPs, including the potential for long periods of earning potentially little or zero interest and loss of principal. In fact, during the relevant period, Paulson considered VRSPs to be "non-conventional investments," and the firm's written supervisory procedures (WSPs) restricted the sale of VRSPs to customers with aggressive or speculative investment objectives and risk tolerances higher than moderate. In fact, the WSPs required that customers who purchased VRSPs complete a disclosure form attesting that they had either an aggressive or speculative investment objective and a high risk tolerance. Paulson failed to enforce these requirements, and the firm did not obtain disclosure forms from the 42 customers. Paulson also did not take any steps to determine that the securities were suitable for the customers. Collectively, the 42 customers paid more than $58,000 in sales charges for these unsuitable purchases, and 21 of the customers suffered total realized losses exceeding $50,000, even after accounting for income earned while they held the VRSPs.

Second, the representatives unsuitably recommended that 27 other customers concentrate their accounts in VRSPs. Each such customer held positions in VRSPs that were equal to at least 50 percent of their account value as a result of those recommendations. Because VRSPs can potentially earn little or zero interest for years and subjected customers to a risk of loss of principal, such concentrated positions were unsuitable. In fact, given the risks posed by VRSPs, Paulson's supervisory system generated alerts whenever a customer's account became more than 40% or 50% concentrated in certain high-yield products, including VRSPs, depending on the customer's risk tolerance. Despite receiving hundreds of these concentration alerts for these customers, Paulson, did not take steps to prevent the three representatives from soliciting additional VRSP purchases after their customers' accounts already were concentrated in VRSPs. Collectively, the 27 customers paid more than $78,000 in sales charges for unsuitable VRSP purchases, and six of the customers suffered total realized losses exceeding $123,000, even after accounting for income earned while they held the VRSPs.

Therefore, Respondent violated FINRA Rules 3110 and 2010.

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

- a censure;
- a $150,000 fine; and

- restitution of $185,215.35 plus interest as described below.[2]

The sanctions imposed in this AWC shall be effective on a date set by FINRA.

Respondent agrees to pay the monetary sanctions 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.

Restitution is ordered to be paid to the customers listed on Attachment A to this AWC (Eligible Customers) in the total amount of $185,215.35, 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 June 1, 2019 until the date this AWC is accepted by the National Adjudicatory Council (NAC).

A registered principal on behalf of Respondent shall submit satisfactory proof of payment of restitution and interest (separately specifying the date and amount of each paid to each Eligible Customer) or of reasonable and documented efforts undertaken to effect restitution. Such proof shall be submitted by email to EnforcementNotice@FINRA.org from a work-related account of the registered principal of Respondent. The email must identify 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 no later than 120 days after the date of the notice of acceptance of the AWC.

The restitution amount plus interest to be paid to each Eligible Customer shall be treated by the Respondent as the Eligible Customer's property for purposes of state escheatment, unclaimed property, abandoned property, and similar laws. If after reasonable and documented efforts undertaken to effect restitution Respondent is unable to pay all Eligible Customers within 120 days after the date of the notice of acceptance of the AWC, Respondent shall submit to FINRA in the manner described above a list of the unpaid Eligible Customers and a description of Respondent's plan, not unacceptable to FINRA, to comply with the applicable escheatment, unclaimed property, abandoned property, or similar laws for each such Eligible Customer.

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

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[2] Paulson previously paid restitution to nine customers for unsuitable VRSP recommendations described in this AWC. This AWC orders Paulson to pay restitution to the remaining 60 customers—realized losses to those customers who experienced realized losses while their accounts were at Paulson and sales charges to the remaining customers, including those whose accounts at Paulson have unrealized losses in the unsuitable VRSP positions or whose accounts had unrealized losses in the VRSP positions at the time they closed their accounts at Paulson.

Restitution payments to customers shall be preceded or accompanied by a letter, not unacceptable to FINRA, 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.

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 right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party. Nothing in this provision affects Respondent's testimonial obligations in any litigation or other legal proceedings.

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 Respondent, 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.

1/3/2023
Date

Paulson Investment Company, LLC
Respondent

Print Name: Trent Davis

Title: CEO

Accepted by FINRA:

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

1/20/2023
Date

Amanda Fein
Principal Counsel
FINRA
Department of Enforcement
99 High St., 9th Fl.
Boston, MA 02110

SCHEDULE A

Customer	Restitution Amount
Customer 1	$1,905.50
Customer 2	$2,936.90
Customer 3	$54.00
Customer 4	$1,364.50
Customer 5	$1,628.50
Customer 6	$2,345.80
Customer 7	$1,118.00
Customer 8	$41,360.06
Customer 9	$692.00
Customer 10	$6,562.15
Customer 11	$14,975.24
Customer 12	$204.00
Customer 13	$54.00
Customer 14	$580.71
Customer 15	$90.00
Customer 16	$1,181.00
Customer 17	$150.50
Customer 18	$210.00
Customer 19	$1,847.50
Customer 20	$233.00
Customer 21	$3,177.00
Customer 22	$36.00
Customer 23	$5,718.50
Customer 24	$209.00
Customer 25	$2,054.50
Customer 26	$1,147.00
Customer 27	$1,227.50
Customer 28	$14,483.66
Customer 29	$36.00
Customer 30	$18.00
Customer 31	$572.54
Customer 32	$1,466.50
Customer 33	$298.50
Customer 34	$426.00
Customer 35	$150.50
Customer 36	$506.72
Customer 37	$174.00
Customer 38	$2,358.34
Customer 39	$1,291.00

Customer 40	$61.50
Customer 41	$18.00
Customer 42	$218.00
Customer 43	$112.00
Customer 44	$506.72
Customer 45	$7,499.50
Customer 46	$120.00
Customer 47	$5,133.03
Customer 48	$1,495.50
Customer 49	$6,871.00
Customer 50	$68.00
Customer 51	$14,108.70
Customer 52	$22,894.35
Customer 53	$807.50
Customer 54	$177.00
Customer 55	$809.00
Customer 56	$136.00
Customer 57	$36.00
Customer 58	$2,327.00
Customer 59	$540.93
Customer 60	$6,431.00