

Notice of Hearing

-1400274-

annuity product (also hereinafter at times referred to as “clients”, “investors” and/or “applicants”) incurring a surrender charge of \$1,000 or more during the period between July 2013 and July 2014.

4. In November 2014, the Department requested additional documentation related to the information provided by Pruco in September 2014. Pursuant to ongoing discussion between the parties, Pruco, by and through its legal counsel, provided the complete customer files through multiple responses between January and November 2015.

COUNT I

FAILURE TO SUPERVISE

5. Pruco utilizes the Protegent system to facilitate review of variable annuity sales made by its agents. This review is conducted by Pruco’s Centralized Transaction Review unit (“CTR”). The Protegent system creates “alerts” that call the CTR reviewer’s attention to items needing further review in the proposed transaction. These alerts generated by the Protegent system include, but are not limited to, messages designed to identify the following purchase scenarios: high concentration in deferred variable annuities, contract in a qualified account, level of education and investment experience, and sub-account allocations that do not match the customer’s risk tolerance on file. Each Protegent alert has a risk-based weighted score assigned to it. Based on the cumulative score given to each transaction, the reviewer must review and address each of the alerts before approving the transaction, in addition to completing a holistic supervisory review of the customer’s application and profile information. Depending on the type of the alert, the reviewer is required to obtain and document additional information from the agent and/or customer.
6. The Department has identified instances or examples where Pruco has failed to reasonably supervise its representatives and reviewers, and enforce its supervisory systems and procedures during the CTR review process for transactions with Illinois customers. These failures caused the approval of certain variable annuity applications which should have required further scrutiny by the reviewer before approval.
7. The Department conducted a review of Pruco’s supervision of variable annuities transactions in Illinois, and conducted compliance exams of certain Pruco Illinois branch offices.
8. Upon review of the information provided by Pruco, the Department noted violations of the Illinois Securities Act of 1953 for failure to reasonably supervise its registered representatives and enforce its systems and procedures as they relate to the CTR review process for variable annuity applications by Illinois residents. In the course of its investigation, the Department observed examples of variable annuity applications for Illinois customers that it believes were reviewed in a manner inconsistent under Pruco’s policies and procedures. These examples include: concurrent or near-concurrent multiple purchases which appear to have been viewed in isolation by the CTR reviewer, transactions which resulted in individual or household concentration in VA products that exceeded 50 percent of the individual or household net worth, citing an applicant’s investment “experience” where

Notice of Hearing
-1400274-

the applicant's investment history was limited to employer-sponsored retirement plans, inconsistent documentation of commission splits between Pruco representatives on certain VA sales, and transaction review documentation which appeared to have listed inconsistent income, net worth, and/or liquid net worth information which was provided and confirmed by the Illinois customer in defined ranges on the VA application.

9. Specifically, with respect to the financial information provided by the Illinois customers, the Department found that Pruco relied on a standardized feature in Protegent which created "mid-points" of the ranges provided by the customer, as referenced in Paragraph 8, and with respect to the applicant's income. In certain instances, Pruco used the "annual household income" figure to conduct suitability review where the income did not apply to the individual applicant. By conducting its supervisory review in this manner, the Department found that Pruco's assessment of an Illinois applicant's actual income, net worth, total assets, or liquid net worth may have been inaccurate in certain circumstances.
10. The Department found that in certain of these instances, Illinois customers partially or fully liquidated their VA holdings within 36 months of purchase, where use of more specific financial information may have yielded a different view of the customer's immediate liquidity needs.
11. Section 8.E(1)(e)(i) of the Act states *inter alia* that subject to the provisions of subsection F of Section 11 of this Act, the registration of a dealer may be denied, suspended or revoked if the Secretary of State finds that the dealer has failed to reasonably supervise the securities activities of any of its salespersons or other employees and the failure has permitted or facilitated a violation of Section 12 of this Act.

COUNT II

FAILURE TO SUPERVISE

12. As stated above, the Department conducted compliance audits of Pruco branches in June 2014 which were located in the State of Illinois. During these compliance audits, Pruco was asked to provide books and records regarding certain transactions with Illinois residents. Subsequently, the Department made additional regulatory requests, relating to variable annuity transactions in Illinois.
13. In its responses to these audit and regulatory requests, Pruco failed to ensure that certain responsive records were provided to the Department in a timely manner.
14. Pruco failed to have the supervisory structure in place to adequately respond to the Department's regulatory requests regarding variable annuity transactions with Illinois residents.
15. Section 8.E(1)(e)(iv) of the Act states *inter alia* that subject to the provisions of subsection F of Section 11 of this Act, the registration of a dealer may be denied, suspended or revoked if the Secretary of State finds that the dealer has failed to maintain and enforce written

Notice of Hearing
-1400274-

procedures to supervise the types of business in which it engages and to supervise the activities of its salespersons that are reasonably designed to achieve compliance with applicable securities laws and regulations.

You are further notified that you are required pursuant to Section 1104 of the Rules to file an answer to the allegations outlined above, or other responsive pleading within 30 (thirty) days of this notice. Your failure to do this within the prescribed time shall be deemed an admission of the allegations contained in the Notice of Hearing and waives your right to a hearing.

Furthermore, you may be represented by legal counsel; may present evidence; may cross-examine witnesses and otherwise participate. A failure to appear shall constitute default by you.

A copy of the Rules and Regulations promulgated under the Illinois Securities Law and pertaining to hearings held by the Office of the Secretary of State, Illinois Securities Department, are available at the Department's website:

<http://www.cyberdriveillinois.com/departments/securities/abtil.html>

Delivery of notice to the designated representative of any Respondent constitutes service upon such Respondent.

Date of Mailing: 20th day of April 2017



JESSE WHITE
Secretary of State
State of Illinois

Attorneys for the Secretary of State:
Frank Loscuito
Office of the Secretary of State
Illinois Securities Department
69 West Washington Street, Suite 1220
Chicago, Illinois 60602
Telephone: (312) 793-7319

Hearing Officer:
James L. Kopecky
203 N. LaSalle Street, Suite 1620
Chicago, IL 60601