

NEW YORK STOCK EXCHANGE, INC.

EXCHANGE HEARING PANEL DECISION 05-28

March 8, 2005

FLEET SECURITIES, INC.  
MEMBER ORGANIZATION

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**Violated SEC Rule 15c3-3 in that the Firm improperly computed its Customer Reserve Formula requirements, violated SEC Rule 15c3-1 in that the Firm failed to properly and accurately calculate its Net Capital, violated Exchange Rule 132 in that the Firm failed to submit to the Exchange accurate account type indicators, violated Exchange Rule 342 in that it failed to provide for, establish, and maintain adequate supervisory procedures and controls, including a separate system of follow-up and review, of certain of its business activities in order to ensure compliance with Exchange Rules and federal securities laws relating to proper and accurate computations of Customer Reserve and Net Capital – Consent to censure and a \$100,000 fine.**

**Appearances:**

For the Division of Enforcement  
Matthew L. Moore, Esq.  
Robert Meyers, Esq.

For the Respondent  
Paul F. McCurdy, Esq.

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An Exchange Hearing Panel met to consider a Stipulation of Facts and Consent to Penalty entered into between the Exchange's Division of Enforcement and Fleet Securities, Inc. a Member Organization (the "Firm"). Without admitting or denying guilt, the Firm consented to findings by the Hearing Panel that it:

- I. Violated SEC Rule 15c3-3 in that the Firm improperly computed its Customer Reserve Formula requirements.
- II. Violated SEC Rule 15c3-1 in that the Firm failed to properly and accurately calculate its Net Capital in accordance with the requirements of that regulation.
- III. Violated Exchange Rule 132 in that the Firm failed to submit to the Exchange accurate account type indicators with respect to certain transactions.

- IV. Violated Exchange Rule 342 in that it failed to provide for, establish, and maintain adequate supervisory procedures and controls, including a separate system of follow-up and review, of certain of its business activities in order to ensure compliance with Exchange Rules and federal securities laws relating to proper and accurate computations of Customer Reserve and Net Capital.

For the sole purpose of settling this disciplinary proceeding, the Division of Enforcement and the Firm stipulate to certain facts, the substance of which follows:

### **Background and Jurisdiction**

1. The Firm became a member organization of the Exchange in 1984 and was, at all relevant times, a broker/dealer that executed and cleared transactions for correspondent broker/dealers and affiliated companies. The Firm was a wholly owned subsidiary of Bank of America Corporation until its purchase by Automatic Data Processing, Inc. (ADP) in November 2004. At that time, the Firm became known as ADP Clearing & Outsourcing Services, Inc., which is an ADP business unit and a member firm organization. All matters relevant to this Stipulation occurred prior to November 2004.
2. In 2000, the Exchange's Division of Member Firm Regulation ("MFR") conducted an examination of the Firm's Financial and Operational procedures ("FIN/OP"). Following the examinations MFR issued an Examination Report which identified certain deficiencies in the Firm's financial and operational procedures. Thereafter, MFR referred its findings and the Firm's response to Enforcement for further review.
3. By letter dated June 22, 2001, which the Firm received, Enforcement notified the Firm that it was investigating the findings contained in the Examination Report.

### **Summary of Violative Conduct**

4. As set forth more particularly below, on the date of August 31, 2000, the Firm failed to exercise reasonable supervision with respect to certain required financial reporting calculations. The Firm failed to prepare accurate Net Capital and Customer Reserve computations as a result of, among other things, understating borrowed securities by 144.6 million dollars, failing to include approximately 12.5 million dollars in the PAIB Reserve Formula and including 16.4 million dollars of unsecured receivables as an allowable asset. In addition, the Firm failed to submit to the Exchange accurate account type indicators with respect to specific transactions.

### **Customer Reserve Formula**

5. Pursuant to SEC Rule 15c3-3(e)(1) (the "Rule"), broker/dealers must maintain with a bank a separate account entitled "Special Reserve Bank Account for the Exclusive Benefit of Customers," (the "Reserve Bank Account") into which they

must deposit cash and/or qualified securities in amounts computed in accordance with a specified formula.

6. Under the Rule, broker/dealers are required to utilize this formula to make a weekly computation of the amount to be deposited into the Reserve Bank Account and to make requisite deposits on a timely basis.
7. The Firm's Customer Reserve formula computation during the relevant time understated borrowed securities by 144.6 million dollars, which increased excess debits over credits.
8. In addition, non-customer securities (*i.e.*, the accounts of the Firm's principal officers and directors) had been allocated wrongly by the Firm's processing system in a customer account range.
9. In addition, the Firm failed to include a net debit balance of approximately 12.5 million dollars of Fleet Specialists in the PAIB Reserve Formula the amount was excluded from the Customer Reserve Formula, but not included in the PAIB. (Proprietary Accounts of Introducing Brokers ("PAIB") are covered under SEC Rule 15c-3(e), which requires in pertinent part, that clearing brokers must maintain a separate account for the protection of assets of introducing brokers held by the clearing broker).

#### **Net Capital Computation**

10. SEC Rule 15c3-1(c)(2)(iv), promulgated pursuant to the Securities Exchange Act of 1934 ("SEA"), requires that when calculating its Net Capital a broker/dealer must deduct fixed assets and assets that cannot be converted into cash, including, among other things, net overall unfavorable bank reconciliation differences.
11. The Firm's Net Capital computation included, as an allowable asset, unsecured receivables from its parent and other aged receivables totaling 16.4 million dollars.
12. SEC Rule 15c3-1(c)(2)(vi) requires that when calculating its Net Capital a broker/dealer must deduct a certain percentage of the market value of all securities, money market instruments or options in the proprietary or other accounts of the broker/dealer. This is known in the securities industry as taking a "haircut". (In making its Net Capital computation, a firm is required to deduct from its net worth certain percentages, known as "haircuts", of the value of the securities and commodities positions in the firm's portfolio. The applicable percentage haircut is designed to provide protection from market risk, credit risk, and other risks inherent in particular positions. Discounting the value of a firm's proprietary positions provides a capital cushion in case the portfolio value of the Firm's positions decline).

13. The Firm was calculating both the unsecured and partly secured debits on one worksheet, with the only distinction being the haircut on the securities collateralizing the debit balances in its partly secured accounts. As the Firm was including the haircut on partly secured debits on the FOCUS Report balance sheet, it was understating the “receivable from Customer” number on the balance sheet by the amount of the haircut on the partly secured debits.
14. The Firm also included the charge related to an affiliate twice, thereby overstating the overall unsecured and partly secured debits by an additional 1.8 million dollars.
15. Moreover, the Firm failed to have procedures in place to calculate the impact of the cash margin deficiency in customer margin accounts (for its impact upon the Net Capital Computation).
16. In addition, the Firm had no procedures to capture aged unfavorable bank charges and had been netting unrelated fail-to-deliver accounts.

#### **Inaccurate Account Type Indicators**

17. Exchange Rule 132 (Comparison and Settlement of Transactions through a Fully-Interfaced or Qualified Clearing Agency), in pertinent part, requires member firms, when making required submissions to a qualified clearing agency, to submit an accurate account type indicator code on every order entered via SuperDot to identify the type of beneficial owner of every trade executed on the Exchange.
18. Submission of accurate account type indicators is critical to the Exchange’s self-regulatory function as this information is among that utilized by the Exchange to monitor trading for surveillance purposes.
19. A review of Audit Trail data submitted to the Exchange for the trade date of August 25, 2000 disclosed that 35 out of 44 transactions had been incorrectly coded as “Code W” (trades submitted by the clearing member organization for the proprietary account of unaffiliated members or member organization including other clearing firms) instead of “Code A” (trades submitted by non-member broker/dealers) as required for trades of non-member broker/dealers.
20. The Firm violated Exchange Rule 132 by submitting to the Exchange inaccurate account type indicators with respect to such transactions.

#### **Failure to Reasonably Supervise**

21. Exchange Rule 342(a) requires, among other things, that “[e]ach office, department or business activity of a member organization shall be under the supervision and control of the member or member organization establishing it and of the personnel delegated such authority and responsibility.” Exchange Rule

342(b)(1) provides that: “general partners or directors of each member organization shall provide for appropriate supervisory control and shall ... delegate ... responsibility and authority for supervision and control of each office, department or business activity, and provide for appropriate procedures of supervision and control.”

22. The Firm violated Exchange Rule 342(a) and (b) in that it failed to provide for appropriate procedures of supervision and control and to establish a system of follow-up and review with respect to certain business activities, as described above.
23. The Firm failed to reasonably supervise and implement appropriate procedures of supervision and control over required financial reports, including, among other things, Customer Reserve and Net Capital calculations, including a separate system of follow-up and review with respect to certain business activities, as described above.
24. Specifically, the Firm lacked adequate internal procedures and controls to ensure that the activities of various departments, which impacted upon the proper and accurate preparation of firm financial regulatory reporting activities, including but not limited to Customer Reserve and Net Capital computations, were monitored and reviewed.

#### **Other Factors Considered**

25. The Firm took steps to address the above matters, including:
  - (a) the Firm made several key management and operational hirings to improve information flow between operations and regulatory reporting;
  - (b) certain procedures and controls over financial and operation systems were enhanced and implemented; and
  - (c) the Firm retained an outside consultant to perform an independent review of the Firm’s regulatory reporting functions.
26. One of the major goals of the independent review was to examine the Firm’s regulatory computations for accuracy, completeness and compliance with SEC Rules 15c3-3 and 15c3-1.
27. The Firm has represented that it adopted many of the report’s recommendations and suggestions and altered Firm policies and procedures in accordance therewith.

#### **DECISION**

The Hearing Panel, in accepting the Stipulation of Facts and Consent to Penalty, found the Firm guilty as set forth above by unanimous vote.

**PENALTY**

In view of the above findings, the Hearing Panel, by unanimous vote, imposed the penalty consented to by the Firm of a censure and a fine of \$100,000.

For the Hearing Panel

Vincent F. Murphy – Hearing Officer

Panelists:

William J. Burke, III

Joseph C. Gawronski