

NYSE AMEX LLC

HEARING BOARD DECISION 09-AMEX-19

July 31, 2009

BNY CONVERGEX EXECUTION SOLUTIONS LLC
MEMBER ORGANIZATION

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Violated AMEX Rules 1000-Commentary .04 and 1000A-Commentary .05 failing to prevent introducing broker-dealer client from entering limit orders into Firm's AMEX order routing system in same Portfolio Depository Receipts and Index Fund Shares for account or accounts of same or related beneficial owner, in such manner that Firm effectively operated as market maker by holding itself out as willing to buy and sell such Portfolio Depository Receipts and Index Fund Shares on regular or continuous basis; violated AMEX Rule 153(a) and Article XI, Section 3 of AMEX Constitution by failing to maintain complete record of every order entered through order management system to buy or sell Portfolio Depository Receipt; violated AMEX Rule 411 by failing to learn essential facts relative to each order accepted by Firm in Portfolio Depository; violated AMEX Rule 320(c) and (e) by failing to provide for appropriate procedures of supervision and control, by failing to establish and maintain appropriate policies, systems and procedures of supervision and control, including written supervisory procedures and by failing to establish separate system of follow-up and review to ensure compliance with AMEX Rules 1000-Commentary .04(a) and 1000A-Commentary .05 – Consent to censure and \$35,000 fine.

Appearances:

For the Division of Enforcement
David Rosenstein, Esq.
Theresa C. Clarkson, Esq.

For Respondent
Robert Virgilio

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A Hearing Officer on behalf of the NYSE Amex LLC ("NYSE Amex") considered a Stipulation of Facts and Consent to Penalty entered into between NYSE Regulation, Inc.'s Division of Enforcement ("Enforcement") and BNY ConvergEx Execution Solutions LLC (f/k/a BNY

Brokerage Inc., “BNY,” the “Firm” or “Respondent”),¹ an NYSE Amex member organization. Without admitting or denying guilt, Respondent consented to a finding by a Hearing Officer that it:

- I. Violated AMEX Rules 1000-Commentary .04 and 1000A-Commentary .05 in that BNY failed to prevent its introducing broker-dealer client from entering limit orders into BNY’s AMEX order routing system in the same Portfolio Depositary Receipts and Index Fund Shares for the account or accounts of the same or related beneficial owner, in such a manner that BNY effectively operated as a market maker by holding itself out as willing to buy and sell such Portfolio Depositary Receipts and Index Fund Shares on a regular or continuous basis during the period June 2004 – October 2004;
- II. Violated AMEX Rule 153(a) and Article XI, Section 3 of the AMEX Constitution in that the Firm failed to maintain a complete record of every order entered through its order management system to buy or sell a Portfolio Depositary Receipt during the period of October 25 – 29, 2004;
- III. Violated AMEX Rule 411 in that the Firm failed to learn the essential facts relative to each order accepted by the Firm in a Portfolio Depositary Receipt during the period of October 25 – 29, 2004;
- IV. Violated AMEX Rule 320(c) and (e) during the period June 2004 through October 2008 in that the Firm failed to provide for appropriate procedures of supervision and control; failed to establish and maintain appropriate policies, systems and procedures of supervision and control, including written supervisory procedures; and failed to establish a separate system of follow-up and review to ensure compliance with AMEX Rules 1000-Commentary .04(a) and 1000A-Commentary .05 during the period June 2004 – October 2008.

For the sole purpose of settling this disciplinary proceeding, without adjudication of any issues of law or fact, and without admitting or denying any allegations or findings referred to in the Stipulation of Facts and Consent to Penalty, Respondent stipulates to certain facts, the substance of which follows:*

¹ According to FINRA’s Central Registration Depository, BNY converted to a Delaware limited liability company on September 27, 2006 and subsequently changed its name to BNY ConvergEx Execution Solutions LLC on December 22, 2006.

* Hearing Officer Note: The facts, allegations, and conclusions contained in paragraphs 1 to 27 are taken from the executed Stipulation of Facts and Consent to Penalty between Enforcement and Respondent. No changes have been made to the stipulated paragraphs by the Hearing Officer.

Background and Jurisdiction

1. During all relevant periods herein, BNY was a member organization and a registered broker-dealer at the American Stock Exchange (“AMEX”).²
2. BNY executes orders on behalf of its direct customers as well as introducing broker-dealer clients. For certain omnibus clients, BNY provides a sponsored line permitting those brokers to access the AMEX directly rather than through the Firm.
3. After receiving a complaint on or about June 15, 2004, the Trading Analysis Department (“TA”) of FINRA initiated an investigation into the alleged simultaneous/near simultaneous (buy and sell) entry of limit orders in AAA, Index Funds Shares.³
4. TA initiated a separate investigation during the period of October 25 – 29, 2004 after a review of the AMEX Rule 1000 Exception Report revealed possible off-Floor market making activity effected in BBB,⁴ a Portfolio Depository Receipt, through BNY’s trading system linked to the AMEX.

Order Entry and Supervision Violations

5. BNY violated: (1) AMEX Rules 1000-Commentary .04 and 1000A-Commentary .05 by allowing entities to enter simultaneous or near simultaneous buy and sell orders in a Portfolio Depository Receipt and an Index Fund Share for the same beneficial owner during the period June 2004 – October 2004; (2) AMEX Rule 153 and Article XI, Section 3 of the AMEX Constitution, by failing to maintain a record of every order transmitted to the AMEX Floor during October 2004; (3) AMEX Rule 411 by failing to learn the essential facts relative to each order accepted by the Firm during October 2004; and, (4) AMEX Rule 320 by failing to have adequate procedures of supervision and control in place to detect or prevent potential violations of AMEX Rule 1000-Commentary .04 and AMEX Rule 1000A-Commentary .05 during the period June 2004 – October 2008.

Relevant AMEX Rules

6. During all relevant periods herein, AMEX Rule 1000-Commentary .04 (a) provided, in part:

² On October 1, 2008, the AMEX was acquired by the NYSE Euronext and was subsequently renamed NYSE AMEX. Thus, while the rules of NYSE Amex govern the procedural aspects of this Stipulation and Consent, because the conduct referred to herein occurred prior to the acquisition date, the violations were of “AMEX Rules.”

³ “AAA” is a generic identified used throughout this Stipulation for the subject Index Fund Shares.

⁴ “BBB” is a generic identified used throughout this Stipulation for the subject Portfolio Depository Receipt.

Member and member organizations shall not enter orders into the [AMEX's] order routing system, as principal or agent, limit orders in the same Portfolio Depositary Receipts, for the account or accounts of the same or related beneficial owner, in such a manner that the member or beneficial owner(s) effectively is operating as a market maker by holding itself out as willing to buy and sell such Portfolio Depositary Receipts on a regular or continuous basis. In determining whether a member or beneficial owner effectively is operating as a market maker, the [AMEX] will consider, among other things, the simultaneous or near simultaneous entry of limit orders to buy and sell the same Portfolio Depositary Receipts; the multiple acquisition and liquidation of positions in the same Portfolio Depositary Receipts during the same day; and the entry of multiple limit orders at different prices in the same Portfolio Depositary Receipts.

7. During all relevant periods herein, AMEX Rule 1000A-Commentary .05 provided in part:

Member and member organizations shall not enter orders into the [AMEX's] order routing system, as principal or agent, limit orders in the same Index Fund Shares, for the account or accounts of the same or related beneficial owner, in such a manner that the member or beneficial owner(s) effectively is operating as a market maker by holding itself out as willing to buy and sell such Index Fund Shares on a regular or continuous basis. In determining whether a member or beneficial owner effectively is operating as a market maker, the [AMEX] will consider, among other things, the simultaneous or near simultaneous entry of limit orders to buy and sell the same Index Fund Shares; the multiple acquisition and liquidation of positions in the same Index Fund Shares during the same day; and the entry of multiple limit orders at different prices in the same Index Fund Shares.

8. During all relevant periods herein, AMEX Rule 153(a) provided in part:

Every member or member organization shall maintain a record of every order and every modification and cancellation of such order transmitted to the Floor of the [AMEX], which record shall include the name, amount and price of the security and the time when such order, modification or cancellation was so transmitted.

9. During all relevant periods herein, AMEX Rule 411 provided in part:

Every member or member organization shall use due diligence to learn the essential facts relative to every customer and to every order or account accepted.

10. During all relevant periods herein, AMEX Rule 320(c) and (e) provided in part:

(c) A general partner, principal executive officer, or trustee should be designated to assume overall authority and responsibility for internal supervision and control of the organization and compliance with securities laws and regulations. This person shall reasonably: (1) delegate to qualified principals or employees responsibility and authority for supervision and control of each office, department or business activity, and provide for appropriate procedures of supervision and control; and (2) establish a separate system of follow-up and review to verify that the delegated authority and responsibility is being properly exercised.

(e) Members and member organizations who have employees shall establish, maintain, enforce and keep current a system of compliance and supervisory controls, reasonably designed to achieve compliance with applicable securities laws and regulations and [AMEX] rules, that are appropriate to their business size, structure, customer accounts, transactions and business activities.

11. During all relevant periods herein, Article XI, Section 3 of the AMEX Constitution provided:

Members and Member organizations shall keep true and complete books of account and records adequately setting forth the transactions of such members and member organizations in accordance with the requirements of the Constitution and rules of the [AMEX] and the Securities Exchange Act of 1934 and the rules thereunder.

Effectively Acting as a Market Maker by Allowing the Simultaneous/Near Simultaneous Entry of Limit Orders into the AMEX Order Entry System

Review of Trading in AAA

12. Through TA's review, TA determined that there were 45 instances in which the same customer simultaneously entered both buy and sell limit orders in AAA, Index Fund Shares, through BNY's trading system linked to the AMEX's order routing system on June 9, 2004 and June 10, 2004. Thus, BNY effectively was operating as a market maker in AAA by holding itself out as willing to buy or sell AAA on a regular or continuous basis.
13. On or about June 17, 2004, TA sent correspondence to BNY and requested the identity of the customer(s) or Firm trader(s) effecting the subject order activity in AAA. BNY reported in correspondence dated June 22, 2004 that the subject order

activity was effected by BNY's customer, ("Entity A"),⁵ a non-AMEX member. Entity A had an omnibus brokerage account with BNY and routed orders on behalf of customers through BNY's trading system linked to the AMEX for execution.

14. On or about December 10, 2004, BNY sent correspondence to TA, stating that one proprietary trader at one of Entity A's broker/dealer customers ("Entity B")⁶ placed the subject simultaneous buy limit and sell limit orders in AAA for the account of one beneficial owner.
15. On or about January 12, 2005, BNY sent correspondence to TA, informing it that a system problem at Entity B resulted in the activity conducted by its trader in AAA. BNY contacted Entity A who in turn informed Entity B about the subject violative activity, and Entity B was made aware that it was not permitted to enter simultaneous buy and sell limit orders in Index Fund Shares in such a manner such that it was effectively operating as a market maker by holding itself out as willing to buy and sell such Index Fund Shares on a regular or continuous basis.

Review of Trading in BBB

16. Through TA's review of the AMEX Rule 1000 Exception Report, TA determined that on trade date October 28, 2004, BNY had 46,467 instances of potential violations involving the simultaneous or near simultaneous buy and sell of limit orders of BBB, a Portfolio Depository Receipt. Thus, BNY effectively was operating as a market maker in BBB by holding itself out as willing to buy or sell BBB on a regular or continuous basis.
17. On or about November 18, 2004, TA sent correspondence to BNY and requested the identity of the customer(s) or Firm trader(s) effecting the subject order activity in BBB.
18. On or about December 2, 2004, BNY sent correspondence to TA, providing the execution information for the BBB orders on October 28, 2004, and indicating that the subject order activity was effected by BNY's customer, Entity A. BNY, however, did not provide the identity of the customer(s) or any other order details. BNY indicated that Entity A only provided BNY with execution information, and thus, it was not able to receive or maintain a record of essential order information which would include the name, amount and price of the security as well as the name or designation of the account for which the order had been entered.
19. On or about January 4, 2005, BNY sent TA correspondence, informing TA that various day traders at one of Entity A's broker/dealer customers ("Entity C")⁷ (a non-AMEX member) entered the subject trades. These day traders traded Entity C's

⁵ "Entity A" is a generic identifier used throughout this Stipulation for this entity.

⁶ "Entity B" is a generic identifier used throughout this Stipulation for this entity.

⁷ "Entity C" is a generic identifier used throughout this Stipulation for this entity.

capital.

20. On or about January 12, 2005, BNY informed TA that it advised Entity A to cease transmitting all orders in all ETFs, including the subject Portfolio Depositary Receipt, on behalf of Entity C.

Supervision

21. On or about December 6, 2004, BNY informed TA during a conference call that the Firm did not have written supervisory procedures (“WSPs”) to ensure compliance with AMEX Rule 1000 and 1000A during the applicable review periods.
22. Subsequent to BNY and TA’s December 6, 2004 discussion, on December 10, 2004, BNY supplied TA with a copy of the WSPs it had since drafted and implemented regarding AMEX Rule 1000-Commentary .04. A review of the WSPs indicated that the WSPs simply provided a definition of the rule and were not reasonably designed to detect or prevent violations of the rule. BNY’s procedures failed to delegate an individual with supervision and control of activity related to Amex Rules 1000-Commentary 04, or 1000A-Commentary .05, and failed to have a separate system of follow-up and review to ensure that the delegated authority and responsibility were being exercised properly.
23. From approximately Fall 2005 throughout 2006, BNY regularly updated TA about its work with its technology department to create a system of exception reports that would detect potential violations of AMEX Rule 1000 or 1000A. Due to system limitations of Entity A, BNY was unable to implement such a system.
24. On or about February 28, 2008, Enforcement sent BNY correspondence, requesting that BNY submit any and all updates to its WSPs pertaining to AMEX Rule 1000-Commentary .04 and 1000A-Commentary .05.
25. On or about March 11, 2008, BNY supplied Enforcement with WSPs pertaining to AMEX Rule 1000-Commentary .04. These WSPs were the same as those WSPs previously submitted in December 2004, and consequently resulted in the same inadequacies as described in above paragraph 22.
26. On or about December 8, 2008 in response to discussions with Enforcement, BNY submitted documentation outlining the Firm’s efforts over the immediate four year period to develop appropriate surveillance for the subject activity. The documentation demonstrates that after TA contacted the Firm in November 2004 regarding the subject activity, the Firm actively engaged in a process to develop and implement necessary procedures and surveillance, including an exception report, to detect potential violative market-making activity. BNY ceased making these efforts when the venue for trading Index Funds and Portfolio Depositary Receipts moved from the AMEX and surveillance for the subject AMEX Rules was determined to be no longer necessary.

Other Factors Considered

27. In determining to resolve this matter on the basis set forth herein, Enforcement took into consideration the following: (1) BNY developed technology to ensure that it would receive all necessary order information rather than just trade execution information that it was receiving; (2) Index Funds and Portfolio Depositary Receipts are not being traded at the AMEX or NYSE AMEX, and therefore it is unlikely that these rules will be violated in the future; (3) the number of violative orders as compared to total amount of orders that BNY effected in these issues without violations as well as no finding of manipulative activity; and, (4) BNY actively took steps to try to develop and implement an exception report to surveil for violative market-making activity.

DECISION

The Hearing Officer, in accepting the Stipulation of Facts and Consent to Penalty, found that Respondent committed the offenses as set forth above.

PENALTY

In view of the above findings, the Hearing Officer, imposed the penalty consented to by Respondent of a censure and a \$35,000 fine.

For the Hearing Board

Peggy Kuo - Chief Hearing Officer