

**NYSE AMEX LLC
and
NYSE ARCA, INC.**

NYSE AMEX LLC

HEARING BOARD DECISION 09-AMEX-21

August 4, 2009

**STEVEN M. HAZAN
FORMER MEMBER**

HEARING BOARD DECISION 09-AMEX-22

**HAZAN CAPITAL MANAGEMENT, L.L.C.
FORMER MEMBER ORGANIZATION**

Violated Rule 203(b)(1) of Regulation SHO in that Respondents, who were not acting as bona fide options market makers, improperly utilized the Regulation SHO market maker locate exemption to avoid locating shares prior to effecting short sale transactions in Regulation SHO threshold securities; violated Rule 203(b)(3) of Regulation SHO in that Respondents engaged in a series of transactions that circumvented Respondents' delivery obligations in Regulation SHO threshold securities that had been allocated to Respondents by clearing firm; violated AMEX Rule 958 – ANTE in that Respondents failed to meet their in-person, on-floor, and quoting obligations; violated AMEX Rule 958-ANTE(b) in that Respondents entered into numerous transactions that were not reasonably calculated to maintenance of fair and orderly market – Consent to censure, \$1,500,000 joint and several disgorgement, \$500,000 joint and several fine, and seven-year bar against Hazan.

NYSE ARCA, INC.

HEARING BOARD DECISION 09-ARCA-5

August 4, 2009

**STEVEN M. HAZAN
FORMER OTP HOLDER and MARKET MAKER**

HEARING BOARD DECISION 09-ARCA-6

**HAZAN CAPITAL MANAGEMENT, L.L.C.
FORMER OTP HOLDER and MARKET MAKER**

Violated Rule 203(b)(1) of Regulation SHO in that Respondents, who were not acting as bona fide options market makers, improperly utilized Regulation SHO market maker locate exemption to avoid locating shares prior to effecting short sale transactions in Regulation SHO threshold securities; violated Rule 203(b)(3) of Regulation SHO in that Respondents engaged in a series of transactions that circumvented Respondents' delivery

obligations in Regulation SHO threshold securities that had been allocated to Respondents by clearing firm; violated NYSE Arca Options Rule 6.37A in that Respondents entered into numerous transactions that were not reasonably calculated to maintenance of fair and orderly market; violated NYSE Arca Options Rule 6.37B(c) in that Respondents failed to provide continuous two-sided quotation in their appointed issues for 60% of time NYSE Arca, Inc. was open for trading – Consent to censure, \$1,500,000 joint and several disgorgement, \$500,000 joint and several fine, and seven-year bar against Hazan.

Appearances:

For the Division of Enforcement
Robert A. Marchman, Esq.
Steven Brostoff, Esq.
Kenneth R. Bozza, Esq.
Michael Bautz, Esq.
Sebastian Krawczyk, Esq.
Yen Chan

For Respondents
Michael F. Bachner, Esq.

NYSE Amex LLC

A Hearing Officer, on behalf of 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 Steven M. Hazan (“Hazan”), a former member of the American Stock Exchange (“AMEX”), and Hazan Capital Management, LLC (“HCM”), a former AMEX member organization (collectively, “Respondents”). Without admitting or denying guilt, the Respondents consented to findings by a Hearing Officer that they:

- I. Violated Rule 203(b)(1) of Regulation SHO in that Respondents, who were not acting as bona fide options market makers, improperly utilized the Regulation SHO market maker locate exemption to avoid locating shares prior to effecting short sale transactions in Regulation SHO threshold securities.
- II. Violated Rule 203(b)(3) of Regulation SHO in that Respondents engaged in a series of transactions that circumvented Respondents’ delivery obligations in Regulation SHO threshold securities that had been allocated to Respondents by their clearing firm.
- III. Violated AMEX Rule 958 – ANTE in that Respondents failed to meet their in-person, on-floor, and quoting obligations.
- IV. Violated AMEX Rule 958-ANTE(b) in that Respondents entered into numerous transactions that were not reasonably calculated to the maintenance of a fair and orderly market.

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, Respondents stipulate to certain facts, the substance of which are set forth below.

NYSE Arca, Inc.

The same Hearing Officer, on behalf of the General Counsel of NYSE Arca, Inc. (“NYSE Arca”), considered an Offer of Settlement and Consent executed by Hazan, a former OTP Holder and Market Maker, and HCM, a former OTP Holder and Market Maker (“Respondents”). Respondents consented to findings that they:

- I. Violated Rule 203(b)(1) of Regulation SHO in that Respondents, who were not acting as bona fide options market makers, improperly utilized the Regulation SHO market maker locate exemption to avoid locating shares prior to effecting short sale transactions in Regulation SHO threshold securities.
- II. Violated Rule 203(b)(3) of Regulation SHO in that Respondents engaged in a series of transactions that circumvented Respondents’ delivery obligations in Regulation SHO threshold securities that had been allocated to Respondents by their clearing firm.
- III. Violated NYSE Arca Options Rule 6.37A in that Respondents entered into numerous transactions that were not reasonably calculated to the maintenance of a fair and orderly market.
- IV. Violated NYSE Arca Options Rule 6.37B(c) in that, throughout the Second Relevant Period they failed to provide a continuous two-sided quotation in their appointed issues for 60% of the time NYSE Arca, Inc. was open for trading.

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 finding referred to in the Offer of Settlement and Consent, Respondents stipulate to certain facts, the substance of which are set forth below. Enforcement does not contest the Offer of Settlement and Consent and recommends its acceptance. With due regard to the stipulated facts and violations and the proposed sanction contained therein, the Hearing Officer believes it is appropriate to accept the Offer of Settlement and Consent and issues this Decision in accordance with NYSE Arca Rules. The Offer of Settlement and Consent is made a part of this Decision by reference herein.

STIPULATION OF FACTS AND VIOLATIONS

1. During all relevant periods herein, HCM, a New York limited liability company, was a duly registered broker-dealer with the Securities and Exchange Commission (“SEC”). During all relevant periods herein, Hazan was the Managing Member of HCM.
2. From on or about January 3, 2005 to on or about July 31, 2006 (the “First Relevant Period”) HCM was a Regular Member Organization of the American Stock Exchange

- (“AMEX”).¹ HCM terminated its AMEX membership effective December 24, 2007. Jurisdiction was retained over HCM in accordance to Article V, Section 6 of the AMEX Constitution, by letter delivered via certified mail/return receipt requested dated January 10, 2008.
3. During the First Relevant Period, Hazan was a Regular Member of the AMEX. Hazan subsequently terminated his Exchange membership effective August 3, 2006. Jurisdiction was retained over Hazan in accordance with Article V, Section 6 of the AMEX Constitution, by a letter delivered via certified mail/return receipt requested dated August 3, 2006.
 4. From in or about June, 2006 to on or about October 20, 2007 (the “Second Relevant Period”), Hazan and HCM were Options Trading Permit (“OTP”) Holders and Market Makers registered with NYSE Arca.
 5. Jurisdiction was retained over Hazan in accordance with NYSE Arca Options Rule 10.1 by letter delivered via certified mail/return receipt requested dated April 11, 2008.
 6. Jurisdiction was retained over HCM in accordance with NYSE Arca Options Rule 10.1 by letter delivered via certified mail/return receipt requested dated April 14, 2008.

Overview

7. Throughout the relevant periods herein, the Respondents violated Rule 203 of Regulation SHO under the Securities Exchange Act of 1934 (“Exchange Act”) by effecting short sales of securities without locating shares to borrow and failing to properly close out fail to deliver positions in Regulation SHO threshold securities. In doing so, the Respondents improperly relied upon an exemption from locating shares granted by Regulation SHO to market makers. The Respondents were not entitled to such exemption since they failed to meet the market maker obligations of the AMEX and NYSE Arca Options rules and federal securities laws.

Regulatory Framework

Regulation SHO²

8. Regulation SHO was adopted to update short sale regulation in light of numerous market developments since short sale regulation was first adopted in 1938. One of the goals of Regulation SHO was to address problems associated with failures to

¹ On October 1, 2008, the AMEX was acquired by NYSE Euronext and was renamed NYSE Amex US LLC. 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 merger date, the violations were of “AMEX Rules.”

² Exchange Act Release No. 34-50103 (July 28, 2004) 69 FR 48008 (August 6, 2004) (“Regulation SHO Adopting Release”).

deliver, including potentially abusive “naked” short selling, by establishing uniform “locate” and “close-out” requirements.³ Fails to deliver, as part of a manipulative naked short could be used to drive down a company’s stock price and undermine the confidence of investors who may be reluctant to commit capital to an issuer they believe to be the subject of such manipulative conduct. Moreover, issuers may suffer unwarranted reputational damage due to such negative perceptions and might have an adverse impact on the security’s price.⁴

9. During all relevant periods herein, Rule 203(b)(1) of Regulation SHO required market participants to locate shares to borrow⁵ prior to effecting a short sale transaction. However, pursuant to an exemption in Rule 203(b)(2) of Regulation SHO, market makers engaged in bona-fide market making activities⁶ in a particular security are exempt from the locate requirements applicable to other market participants. Options market makers in equity options are exempt from the locate requirements of Regulation SHO when selling the underlying equity security short, provided that such short sales hedge options positions established during the course of bona fide options market making activity.⁷
10. During all relevant periods herein, pursuant to Rule 203(b)(3) of Regulation SHO, Respondents’ clearing firm was obligated to immediately close out⁸ any fail to deliver positions in a threshold security that lasted for 13 consecutive settlement days by purchasing securities of like kind and quantity (“Regulation SHO buy-in”). However, pursuant to Rule 203(b)(3)(iv) of Regulation SHO, a clearing firm is permitted to allocate a portion of the fail to deliver position in the subject threshold security to the responsible broker or dealer based on such broker or dealer’s short position and thereby shift the obligation for complying with the mandatory close-out to such broker or dealer.

³ Division of Market Regulation: Key Points About Regulation SHO (April 11, 2005).

⁴ See Exchange Act Release No. 34-58775 (October 17, 2008).

⁵ “Locating shares” requires a market participant to, prior to effecting a short sale in any equity security, borrow the security, enter into an arrangement to borrow the security, or have reasonable grounds to believe that the security can be borrowed so that it can be delivered on the date delivery is due.

⁶ In the Regulation SHO Adopting Release, the SEC provided guidance on bona-fide market making activities. Specifically, the SEC stated, “...bona-fide market making does not include transactions whereby a market maker enters into an arrangement with another broker-dealer or customer in an attempt to use the market maker’s exception for the purpose of avoiding compliance with Rule 203(b)(1) by the other broker-dealer or customer” 69 FR 48008, 48015 (August 6, 2004) (footnote omitted).

⁷ See Section 3(a)(38) of the Exchange Act, Rules 203(b)(2)(iii) and 11a1-3(T) thereunder, and the Regulation SHO Adopting Release.

⁸ A “close out” of a short position involves the purchase of an equivalent number of shares to reduce the short position to zero.

Options Market Maker Obligations

11. Section 3(a)(38) of the Exchange Act defines a market maker as “any specialist permitted to act as a dealer, any dealer acting in the capacity of a block positioner, and any dealer who with respect to a security, holds himself out (by entering quotations in an inter-dealer communications system or otherwise) as being willing to buy and sell such security for his own account on a regular or continuous basis.”
12. During the relevant periods, AMEX Rule 958-Amex New Trading Environment (“ANTE”) set forth the quoting obligation of a market makers, known as a Registered Options Trader (“ROT”), and required, among other things, that ROTs execute a minimum of 25% of their option contract trading volume in person on the Floor of the AMEX and not through the use of orders represented by another member or member organization.
13. AMEX Rule 958-ANTE(b) states, in relevant part, “[AMEX] option transactions of a [ROT] should constitute a course of dealing reasonably calculated to contribute to the maintenance of a fair and orderly market and no [ROT] should enter into transactions or make bids or offers that are inconsistent with such a course of dealing.”
14. NYSE Arca Options Rule 6.37B(c) requires its market makers to “provide continuous two-sided quotations throughout the trading day in its appointed issues for 60% of the time [NYSE Arca Inc.] is open for trading in each issue.”
15. NYSE Arca Options Rule 6.37A states, in relevant part, “[t]ransactions of a Market Maker should constitute a course of dealings reasonably calculated to contribute to the maintenance of a fair and orderly market, and no Market Maker should enter into transactions or make bids or offers that are inconsistent with such a course of dealings.”

Violative Conduct

Respondents’ Failure to Locate Shares Prior to Effecting Short Sale Transactions

16. During the relevant periods Respondents regularly engaged in transactions known as “reverse conversions”⁹ with purchasers of Regulation SHO threshold securities.¹⁰

⁹ A “reverse conversion” is the combination of a “reversal” and a “conversion” between two market participants. A “reversal” is a short stock transaction that is tied to a long options combination. The options position creates a “synthetic long position”, which carries the essential risk/reward characteristics comparable to the instrument it replicates (i.e., long stock). A synthetic long position is created by buying a call option and selling a put option with the same strike price and expiration. The contra side of reversal transaction is called a conversion. A conversion is a long stock transaction that is tied to a short option combination. The options position creates a “synthetic short position”, which carries the essential risk/reward characteristics comparable to the instrument it replicates (i.e., the short sale of stock). The synthetic short position is created by selling a call option and buying a put option with the same strike price and expiration.

¹⁰ A “threshold security” is an equity security for which there is an aggregate “fail to deliver” position

17. In a typical reverse conversion transaction during the relevant periods, a third party acting as agent for a purchaser of stock in a Regulation SHO threshold security (the “converter”) solicited Respondents to take the other side (“contra side”) to a reverse conversion transaction (the “reverser”).
18. The converter, or buyer of the Regulation SHO security, also sold call options and bought put options.
19. Respondents participated in the reverse conversion transactions by taking the contra side of the reverse conversion transaction (i.e., reversing against the conversion). Respondents sold short shares of a Regulation SHO threshold security, bought call options and sold put options on the security at a specific hedge ratio¹¹ equaling the number of shares sold short by the Respondents. Effecting the reverse conversions eliminated directional risk of the market for the Respondents and gave the appearance that the converter complied with Regulation SHO.¹²
20. Respondents did not locate or borrow shares of the security in question prior to entering an order to effect the short sale portion of the reverse conversion transaction as required by Regulation SHO.
21. In certain cases, Respondents were not entitled to the Regulation SHO market maker exemption from the locate requirements since the short sales were not effected in connection with bona-fide options market making activities. During the relevant period, Respondents’ options trades were effected without complying with the applicable options market maker requirements with respect to meeting their quoting obligations as an AMEX ROT and/or Arca options market maker. Further, Respondents did not maintain regular and continuous two-sided quotations or otherwise hold themselves out as willing to buy and sell securities on a regular or continuous basis in the options overlying the equity securities that were sold short as part of the reverse conversion transactions.¹³

exceeding the size criteria as set forth in Regulation SHO for a period of five consecutive settlement days.

¹¹ A “hedge ratio,” also known by the Greek symbol “delta,” is typically defined as the change in price of a call/put option for every one-point move in the price of the underlying security.

¹² Because put sellers hedge their transactions with stock sales, and Regulation SHO threshold securities are hard-to-borrow, the difficulty in delivering the stock causes the puts to trade at a higher price than the corresponding call options.

¹³ Subsequent to the relevant periods, the SEC issued Exchange Act Release No. 34-58775 (October 17, 2008), footnote 99, stating: “[I]f a market maker sells stock (short) together with a synthetic short position (e.g., a conversion) to a client and the client sells the stock (long) retaining the synthetic short position, the effect would be as if the market maker had ‘rented’ its exemption to the client. Such transactions or other transactions that have the same effect will not be considered bona-fide market making activity.”

22. As a result, Respondents failed to meet the requirements to be classified as a market maker under Sections 3(a)(38) and 11(a) of the Exchange Act, Rule 11a-1 under the Exchange Act, AMEX Rule 958-ANTE and NYSE Arca Options Rule 6.37B. Thus, Respondents' short selling activities in the reverse conversion transactions where Respondents were using their locate exemption to provide long stock to another broker-dealer were not related to bona-fide options market making activities and, therefore, Respondents were not entitled to the market maker exemption to the locate rule when selling the stock short.
23. As a result, Respondents, who were not acting as bona fide options market makers, violated Rule 203(b)(1) of Regulation SHO by improperly utilizing the Regulation SHO market maker locate exemption to avoid locating shares prior to effecting short sales in Regulation SHO threshold securities.

Respondents' Failure to Close Out Fail to Deliver Positions in Regulation SHO Threshold Securities

24. The short sale portion of the reverse conversion transaction resulted in a "fail to deliver position"¹⁴ in the security on the books and records of Respondents' clearing firm.
25. Throughout the relevant periods, Respondents' clearing firm routinely notified Respondents of a potential Regulation SHO buy-in by sending Respondents a Regulation SHO Buy-In Notification via email beginning on or about the 10th day of a fail to deliver position.
26. Respondents did not want their fail to deliver position from the reverse conversion transaction to be bought-in since Respondents or their clearing firm would be forced to make large open market purchases of a Regulation SHO threshold security with little or no control as to execution price. Additionally, a buy-in would result in an unhedged synthetic long stock position (long calls and short puts) from the original reversal transaction. This would expose Respondents to directional market risk, which could negatively impact the profit from the reverse conversion transaction.
27. In order to avoid being bought-in, Respondents entered into a series of transactions that circumvented Respondents' obligation to actually deliver securities to close out their short position pursuant to Regulation SHO. Specifically, Respondents, utilizing the services of an options floor broker, executed a series of complex transactions that appeared to close out their fail to deliver position by purchasing securities of like kind and quantity.
28. In an example of one type of such a transaction,¹⁵ Respondents executed a married

¹⁴ A "fail to deliver" position exists when there has been no delivery of the borrowed shares.

¹⁵ Respondents utilized a variety of different types of transactions to circumvent their delivery obligations under Regulation SHO. Examples of other types of transactions utilized by Respondents include,

- put transaction¹⁶ using short term, deep in-the-money put options¹⁷ that had the effect of temporarily resetting the buy-in date. In the transaction, Respondents bought stock from another “market maker” (“married put contra party”)¹⁸ and simultaneously bought short term, deep in-the-money put options for a corresponding number of shares from the same “market maker.”¹⁹ Respondents’ clearing firm reflected the stock purchase transaction in Respondents’ account on the clearing firm’s books and records.
29. Shortly thereafter, the short term put options expired in-the-money and Respondents exercised the put options which required the contra party to purchase stock from Respondents. Respondents delivered to the contra party the purported “long” stock²⁰ they purchased from the contra party in the married put transaction the previous day. Respondents, however, had not received delivery of long stock from the married put contra party. Accordingly, shares were not delivered to close out the short position that was established during the initial reversal transaction. However, based on the execution of the married put transaction, Respondents’ clearing firm reset Respondents’ Regulation SHO close-out obligation to Day 1.
30. Respondents repeatedly engaged in these or other types of transactions after receiving a Regulation SHO Buy-In Notification from their clearing firm and these transactions caused the buy-in date to be reset. These transactions were executed approximately every 13 settlement days until the options positions either expired or were closed out. These transactions enabled Respondents to maintain impermissible short positions in a number of Regulation SHO threshold securities for extended periods of time.
31. Respondents’ transactions, including the married put transactions described above, violated Rule 203(b)(3) of Regulation SHO.²¹

without limitation, buy-writes and one-day FLEX options.

¹⁶ A married put is a combination transaction in which stock is purchased and an equivalent number of puts are purchased and executed simultaneously to protect against depreciation in the stock’s price.

¹⁷ A “deep-in-the-money put option” is where the market price of a security is well below the strike price of the option.

¹⁸ Respondents generally bought stock from other market makers that were also selling short hard to borrow Regulation SHO threshold securities and utilizing the market maker exemption from the Regulation SHO locate requirements.

¹⁹ Because the payment received by the other “market maker” is generally less than the interest payment that such “market maker” could have received by lending the same number of shares, Respondents should have been reasonably able to infer that such “market maker” selling stock within the married put transaction was also short stock.

²⁰ While Respondents appeared to have purchased stock on the books and records of Respondents’ clearing firm, the counterparty to the married put did not deliver stock to Respondents.

²¹ Regulation SHO prohibits a broker-dealer from “entering into an arrangement with a counterparty to purchase securities for purposes of closing out a failure to deliver position and the broker-dealer knows

32. In addition, Respondents also acted as counterparties to assist other “market makers” to circumvent their Regulation SHO delivery obligations in threshold securities for extended periods of time. For example, Respondents would sell short shares of threshold securities and sell short term, deep-in-the-money put options. Respondents’ conduct in acting as a counterparty to married put transactions for other “market makers” further violated Rule 203(b)(3) of Regulation SHO.²²

Respondents’ Trading Activity On The AMEX

33. Throughout the First Relevant Period the Respondents, who were not acting as bona fide options market makers and failed to meet their in-person, on-floor and quoting obligations, improperly utilized the Regulation SHO market maker exemption to avoid locating shares prior to effecting short sale transactions as part of effecting reverse conversion transactions and circumvented their delivery obligations in Regulation SHO threshold securities that had been allocated to them by their clearing firm.
34. Although the manner of effecting the reverse conversion transactions, as well as the close-out transactions, varied depending on the particular transaction, the following example is representative of Respondents’ actions that violated the Regulation SHO locate and delivery obligations.
35. On Trade Date, Floor Broker A, acting as agent for Entity B purchasing shares of ABCD, a Regulation SHO threshold security, solicited Respondents to be the contra party to a reverse conversion transaction. In the transaction, Respondents bought ABCD calls, sold ABCD puts and sold short ABCD shares without first locating ABCD stock as required by Regulation SHO. Entity B appeared to have received purported “long” stock by executing the conversion side of the transaction. Specifically, Entity B sold ABCD calls, bought ABCD puts and bought ABCD shares. The transaction is summarized below:

	Respondents – Reversal Transaction	Entity B – Conversion Transaction
Trade Date	HCM buys 286 ABCD Dec 35 calls @ 3.20.	Entity B sells 286 ABCD Dec 35 calls @ 3.20.
Trade Date	HCM sells 286 ABCD Dec 35 puts @ 4.25.	Entity B buys 286 ABCD Dec 35 puts @ 4.25.
Trade Date	HCM sells short 28,600 shares of ABCD @ 34.60.	Entity B buys 28,600 shares of ABCD @ 34.60.

or has reason to know that the counterparty will not deliver the securities, and which thus creates another failure to deliver position” [footnote omitted]. Securities Exchange Act Release No.34-54154 (July 14, 2006) 71 FR 41709, 41711 n.13 (July 21, 2006).

²² Respondents utilized a variety of different types of transactions in assisting other market makers to circumvent their delivery obligations under Regulation SHO. Examples of other types of transactions utilized by Respondents include, without limitation, buy-writes and one-day FLEX options.

36. The sale of the December 35 puts and the purchase of the December 35 calls by the Respondents created a synthetic long position. The sale of ABCD shares by Respondents created a short position. Therefore, the overall reversal transaction was delta neutral²³ for the Respondents because the synthetic long options position was hedged against the short stock position, effectively eliminating market risk for the Respondents.
37. In the reversal transaction described above, Respondents netted \$1.05 on the execution of the options combination.²⁴ Respondents paid \$.40 per share on the execution of the short stock related to the \$35 strike price of the options combination.²⁵ In sum, Respondents netted on this reverse conversion transaction a total of \$18,590.²⁶
38. Since Respondents did not locate or borrow shares of ABCD prior to effecting the short sale, Respondents created a fail to deliver position in the Respondents' account on the books and records of Respondents' clearing firm.
39. Ten settlement days after the initial reverse conversion transaction, Respondents received a Regulation SHO Buy-In Notification from their clearing firm for a total of 28,432 shares of ABCD, which was the Firm's total short position in ABCD, including the 28,600 shares Respondents had failed to deliver for a period of 10 settlement days. Respondents thereafter contacted Floor Broker A to solicit a contra party ("Contra party C") to engage in a married put transaction in order to satisfy Respondents' Regulation SHO close-out obligation. Floor Broker A brokered a transaction in which Respondents bought 28,500 shares of ABCD from Contra party C, an Exchange market maker who sold short such stock, and simultaneously bought 285 short term²⁷ ABCD Nov 45 put options from Contra party C.
40. Shortly thereafter, Respondents' clearing firm reflected this transaction in the Respondents' account and eliminated Respondents' short position created by the reverse conversion on the clearing firm's books and records.

²³ Since delta measures the exposure of a derivative to changes in the value of the underlying, a portfolio that is delta neutral is effectively hedged. That is, its overall value will not change for small changes in the price of its underlying instrument.

²⁴ Respondents received: \$4.25 (sell puts) – \$3.20 (buy calls) = \$1.05. Note: in an options contract, each contract represents 100 shares; when an options contract refers to a price of 3.20 its cost is \$320 (3.20 x 100).

²⁵ Respondents paid: \$35.00 (strike price) - \$34.60 (short sale) = \$.40.

²⁶ Respondents received: \$1.05 - \$.40 = \$.65. \$.65 x 28,600 shares = \$18,590. Generally, in a security that is not a Regulation SHO threshold security, the Respondent would have to pay to reverse as opposed to receiving payment as is the case in hard-to-borrow securities such as in this example. The amount that Respondents received does not take into account certain fees such as transaction costs and clearance fees.

²⁷ In this particular example, the short term put options were set to expire in three days.

41. Three days later, the 285 ABCD Nov 45 short term put options expired in-the-money and Respondents exercised the options and caused the appearance of the delivery of shares they bought three days earlier to Contra party C. As a result of the transaction, Respondents reestablished their previous short position and the fail to deliver position was reset to Day 1 on the books and records of Respondents' clearing firm. The married put transaction is summarized below:

Married Put Transaction

Trade Date + 10	HCM receives a Regulation SHO Buy-In Notification for 28,432 shares of ABCD, which has failed to deliver for 10 days.
Trade Date + 13	HCM buys 285 ABCD Nov 45 puts (3 days until expiration) @ 12.20.
Trade Date + 13	HCM buys 28,500 shares of ABCD common stock @ 32.83.
Trade Date + 16	HCM exercises 285 ABCD Nov 45 puts, causing the appearance of delivery of 28,500 shares of ABCD.

42. Respondents' reestablished fail to deliver position continued to age on the books and records of Respondents' clearing firm. After approximately 10 days, Respondents once again received a Regulation SHO Buy-In Notification from their clearing firm for 165,292 shares of ABCD.²⁸ Respondents again engaged in a transaction that was substantially similar to the transaction described above. Respondents repeated this process to reset their Regulation SHO obligation periodically until the options positions in the reversal transaction expired.
43. Specifically, on the options expiration date, ABCD closed at 36.76. As a result, the 286 ABCD Dec 35 puts expired worthless and the 286 ABCD Dec 35 calls expired at parity²⁹ with the short stock position.
44. For their part of the reverse conversion. Respondents received a total realized gross profit of approximately \$18,590. Respondents effectively locked in this profit at the time the reversal transaction was executed and at no point were Respondents subject to market risk based on the directional movement of the underlying ABCD stock. If the price of ABCD moved down, Respondents covered the ABCD short stock when they were assigned on the ABCD puts that Respondents sold in the reversal transaction. If the price of ABCD moved up, Respondents covered the ABCD short stock position by exercising the ABCD calls that Respondents bought in the reversal transaction. In either scenario, Respondents would lose \$.40 per share on this portion of the transaction. This loss was offset by the \$1.05 that Respondents initially received when they effected the options portion of the reversal transaction.

²⁸ Respondents received a Regulation SHO Buy-In Notification from their clearing firm for a total 165,292 shares of ABCD, which included 28,600 that Respondents had failed to deliver as part of the initial reverse conversion transaction.

²⁹ The intrinsic value of the put was equal to the difference between the stock price and the exercise price of the option.

45. For its part in the married put transaction, the Respondents paid \$.03 per share on 28,500 shares for a total of \$855. Thus, the Respondents realized a net profit of \$17,735 from the reverse conversion and married put transactions noted herein.
46. During the First Relevant Period, the Respondents engaged in reverse conversion transactions on the AMEX in numerous securities which generated a total profit of over \$1.5 million.

Respondents' Trading Activity On NYSE Arca

47. Throughout the Second Relevant Period the Respondents, who were not acting as bona fide options market makers and failed to meet their quoting obligations, improperly utilized the Regulation SHO market maker exemption to avoid locating shares prior to effecting short sale transactions as part of effecting reverse conversion transactions on the NYSE Arca market and circumvented their delivery obligations in Regulation SHO threshold securities that had been allocated to them by their clearing firm.
48. Although the manner of effecting the reverse conversion transactions, as well as the close-out transactions, that circumvented the Regulation SHO locate and delivery obligations, varied depending on the particular transaction, the Respondents' actions on the NYSE Arca market were similar to their actions on the AMEX market. For a representative example of this activity see above paragraphs 35-45.
49. During the Second Relevant Period, the Respondents engaged in reverse conversion transactions on NYSE Arca in numerous securities which generated a total profit of over \$1.5 million.

DECISION

NYSE Amex LLC

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

NYSE Arca, Inc.

The Hearing Officer accepted the NYSE Arca Offer of Settlement and Consent as set forth above, and Respondents are found to have committed the violations contained therein.

PENALTY

NYSE Amex LLC

In view of the above findings in the Stipulation of Facts and Consent to Penalty, the Hearing Officer imposed the penalty consented to by the Respondents of a censure; disgorgement to be paid jointly and severally by Hazan and HCM of \$1,500,000 in trading profits resulting from the circumvention of the Regulation SHO locate and delivery obligations while a Member of the AMEX; and a fine in the amount of \$500,000 to be paid jointly and severally by Hazan and

HCM to NYSE Amex.

The Hearing Officer also imposed the additional penalty consented to by Respondent Hazan of a seven-year bar from membership, allied membership, approved person status, and from employment or association in any capacity with any NYSE Amex member or member organization.

NYSE Arca, Inc.

In accordance with the Offer of Settlement and Consent to Penalty, the Respondents are hereby censured; required to pay, jointly and severally, a disgorgement of \$1,500,000 in trading profits resulting from the circumvention of the Regulation SHO locate and delivery obligations while OTP Holders with NYSE Arca; and fined in the amount of \$500,000 to be paid jointly and severally by Hazan and HCM to NYSE Arca.

In addition, Hazan is hereby barred for seven years from membership, allied membership, approved person status, and from employment or association in any capacity with any NYSE Arca OTP Holder or OTP Firm.

For the Hearing Board

Peggy Kuo – Chief Hearing Officer