

NYSE ARCA, INC.

NYSE REGULATION,

Complainant,

v.

CANTOR FITZGERALD & CO.,

Respondent.

Proceeding No. 2016-07-01081¹

December 21, 2017

Cantor Fitzgerald & Co. violated: (i) Securities Exchange Act Rule Rule 15c3-5(c)(1)(ii) by failing to have controls and supervisory procedures that were reasonably designed to prevent the entry of erroneous orders by rejecting orders that exceed appropriate price or size parameters, on an order-by-order basis or over a short period of time; (ii) Securities Exchange Act Rule Rule 15c3-5(e) by failing to adequately document the Firm’s review of its controls and properly certify compliance with the Market Access Rule and preserve such certifications as required; and (iii) NYSE Arca Equities Rule 6.18(b) and (c) by failing to establish and maintain adequate supervisory systems and written procedures that were reasonably designed to ensure compliance with Rule 15c3-5. Consent to a censure, fine of \$155,000, and an undertaking.

Appearances

For the Complainant: David A. Feldman and Adam J. Wasserman, NYSE Regulation.

For the Respondent: Nicholas Sahadi, Cantor Fitzgerald & Co.

DECISION

Cantor Fitzgerald & Co. (“Cantor” or “Firm”) and NYSE Arca, Inc. entered into an Offer of Settlement and Consent 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

¹ Includes Proceeding No. 2017-02-00071.

findings referred to in the offer of settlement.² The Hearing Officer accepts the Offer of Settlement and Consent and issues this Decision in accordance with NYSE Arca Rules.³

FINDINGS OF FACTS AND VIOLATIONS

Overview

1. This matter involves violations of Securities Exchange Act Rule 15c3-5 (17 C.F.R. § 240.15c3-5) (“Rule 15c3-5” or the “Market Access Rule”) and NYSE Arca Equities Rule 6.18.
2. As set forth below, Cantor violated: (i) Rule 15c3-5(c)(1)(ii) by failing to establish, document, and maintain risk management controls and supervisory procedures that were reasonably designed to prevent the entry of erroneous orders, by rejecting orders that exceed appropriate price or size parameters, on an order-by-order basis or over a short period of time; and (ii) Rule 15c3-5(e) by failing to establish, document, and maintain a system for regularly reviewing the effectiveness of its controls, and failing to properly certify compliance with the Market Access Rule and preserve such certifications.

Background and Jurisdiction

3. Cantor has been registered as an Equities Trading Permit (“ETP”) Holder with NYSE Arca, Inc. (the “Exchange”) since June 2003. The Firm is a registered broker-dealer with its principal place of business in New York, New York.
4. This matter arises from investigations by NYSE Regulation into the circumstances surrounding two orders entered by Cantor. The staff of the New York Equities Section of the Financial Industry Regulatory Authority (“FINRA”) conducted a review of an order entered on August 13, 2014 (the “August 2014 Order”). NYSE Regulation further reviewed the August 2014 Order, as well as an order entered on February 24, 2017 (the “February 2017 Order”). As part of its review, NYSE Regulation investigated the Firm’s compliance with Rule 15c3-5 and NYSE Arca Equities Rule 6.18 from August 1, 2014, through February 28, 2017 (the “Review Period”).
5. In letters dated November 14, 2016, and June 12, 2017, which Cantor received, the Enforcement Section of NYSE Regulation, on behalf of the Exchange, notified the Firm that it was investigating whether Cantor violated Rule 15c3-5 and NYSE Arca Equities Rule 6.18 by failing to establish and maintain risk management controls and supervisory procedures reasonably designed to prevent the entry of erroneous orders. As a result of

² FINRA’s Office of Hearing Officers reviewed the Offer of Settlement and Consent under the terms of a Regulatory Services Agreement (as amended) among NYSE Group, Inc., New York Stock Exchange LLC, NYSE Arca, Inc., NYSE MKT LLC, and FINRA.

³ The facts, allegations, and conclusions contained in this Decision were taken from the executed Offer of Settlement and Consent. Prior to August 17, 2017, the rules involved in this matter were called NYSE Arca Equities rules.

this investigation, the Firm was found to have violated these rules, as described in detail below.

Violations

The August 2014 Order

6. On August 13, 2014, Cantor's Convertibles Desk received an unsolicited client order to sell 205,381 shares of convertible preferred stock in an Exchange-traded security (anonymized hereafter as "XYZ"). The instructions were to work the order on a "market not held" basis. A trader on the Convertibles Desk ("Trader 1") endeavored to fill the order through the Firm's order management system ("OMS").
7. When entering the August 2014 Order in the OMS, Trader 1 unintentionally caused the entire 205,381 share order to be transmitted as a market order for execution. Trade executions occurred immediately upon the Exchange's receipt of the order. After 12 executions for 6,400 shares of XYZ occurred at prices ranging from \$31.25 to \$30.69, another 191,779 shares sold within five seconds, as XYZ's price fell to \$24.66, a decrease of approximately 19.6%. XYZ's 30-day consolidated average daily trading volume ("ADV") was approximately 5,702 shares, and therefore the executions on the August 2014 Order represented approximately 3,475% of XYZ's ADV.
8. Once Trader 1 noticed the high volume of executions in XYZ appearing on his computer desktop, he notified his supervisor. Cantor promptly investigated and determined that Trader 1's transmission of a market order for the entire 205,381 share amount had been caused by an OMS function that mistakenly had been enabled on Trader 1's computer desktop. Cantor then submitted a request for Exchange officials to review the subject trades pursuant to NYSE Arca Equities Rule 7.10 (Clearly Erroneous Executions).⁴ Exchange trading officials declared all transactions at or below \$29.86—a total of 207 executions, totaling 191,779 shares of XYZ and \$4,729,709.14—to be null and void.

The February 2017 Order

9. On February 24, 2017, Cantor's Cash Equities Trading Desk received a "market not held" order from an affiliate to sell 84,950 shares of an Exchange-traded security (anonymized hereafter as "YZA"). At 09:20:17, a trader on the Cash Equities Trading Desk ("Trader 2") created a child order to split 10,000 shares of YZA. While attempting to create an additional child order for 2,000 shares of YZA, Trader 2 inadvertently left an OMS pricing strategy setting to "Order," with the percent of order volume set to 100. This caused the OMS to default the February 2017 Order to "market," the order type of the parent order, instead of defaulting to a best bid/offer or limit price. As a result, Trader

⁴ NYSE Arca Equities Rule 7.10 is currently denominated NYSE Arca Rule 7.10-E.

2 unintentionally caused a market order to sell 73,790 shares of YZA to be transmitted for execution.

10. Trade executions occurred immediately upon the Exchange's receipt of the February 2017 Order. Within 227 milliseconds, the order executed 514 times, with all 73,790 shares of YZA selling at prices ranging from \$284.78 to \$265.50, a decrease of approximately 6.7%. YZA's 30-day consolidated ADV was approximately 1,786,443 shares, and therefore the executions on the February 2017 Order represented approximately 4.1% of YZA's ADV.

Violations of Rule 15c3-5(c)(1)(ii)

11. Rule 15c3-5 states that "a broker or dealer with market access, or that provides a customer or any other person with access to an exchange or alternative trading system . . . shall establish, document, and maintain a system of risk management controls and supervisory procedures reasonably designed to manage the financial, regulatory, and other risks of this business activity." Specifically, Rule 15c3-5(c)(1)(ii) requires that the risk management controls and supervisory procedures "shall be reasonably designed to systematically limit the financial exposure of the broker or dealer that could arise as a result of market access, including being reasonably designed to . . . [p]revent the entry of erroneous orders, by rejecting orders that exceed appropriate price or size parameters, on an order-by-order basis or over a short period of time, or that indicate duplicative orders."
12. During the Review Period, Cantor did not consistently employ maximum share threshold controls to create alerts or block trades when a trader attempted to route a child order to an exchange in excess of a specified number of shares. Instead, the Firm applied such controls only to certain desks, traders, and order types. In this case, Trader 1 and Trader 2 entered market orders for 205,381 shares and 73,790 shares respectively, when each order was intended to be transmitted via substantially smaller child orders.
13. Although Cantor employed procedures and controls that set a maximum notional value for each order, these procedures and controls were inadequate. From the beginning of the Review Period through at least November 2015, the Firm employed a control in the OMS that far exceeded the notional value of even the largest non-erroneous orders that Cantor entered on the Exchange. The parameters were too wide to effectively prevent erroneously entered orders without additional controls.
14. Further, Cantor did not utilize an ADV control during the Review Period. A reasonable ADV control could prevent erroneous orders such as the August 2014 Order, which represented approximately 3,475% of XYZ's ADV.
15. Accordingly, during the Review Period, Cantor's controls were not reasonably designed to prevent the entry of erroneous orders, by rejecting orders that exceed appropriate price

or size parameters, on an order-by-order basis or over a short period. Therefore, the Firm violated Rule 15c3-5(c)(1)(ii).

Violations of Rule 15c3-5(e)

16. Rule 15c3-5(e) states that broker-dealers providing market access “shall establish, document, and maintain a system for regularly reviewing the effectiveness of the risk management controls and supervisory procedures required by [the Market Access Rule] and for promptly addressing any issues.”
17. Rule 15c3-5(e)(1) requires that broker-dealers “shall review, no less frequently than annually, the business activity of the broker or dealer in connection with market access to assure the overall effectiveness of such risk management controls and supervisory procedures,” and that “such review shall be conducted in accordance with written procedures and shall be documented.”
18. Rule 15c3-5(e)(2) requires that the Chief Executive Officer (or equivalent officer) of the broker-dealer certify, on an annual basis, that such risk management controls and supervisory procedures comply with paragraphs (b) and (c) of Rule 15c3-5, and that the broker-dealer conducted the review described in Rule 15c3-5(e)(1). Rule 15c3-5(e)(2) also requires that such certifications be preserved by a broker-dealer as part of its books and records for not less than three years, in accordance with Securities Exchange Act Rule 17a-4(b) (17 C.F.R. § 240.17a-4(b)).
19. During the Review Period, Cantor did not document its system for regularly reviewing the effectiveness of its risk management controls and supervisory procedures as Rule 15c3-5(e) requires. Although the Firm’s written procedures stated that “[b]roker-dealers with market access must review, no less frequently than annually, the overall effectiveness of its risk management controls and supervisory procedures,” and that “[s]uch review must be conducted in accordance with written procedures and must be documented,” the written procedures prior to September 2016 did not describe the Firm’s controls to prevent the entry of erroneous orders, nor did the written procedures indicate how such controls should be reviewed. Moreover, the Firm did not document regular review of its maximum share threshold, maximum notional value, or ADV controls across desks and order types each year during the Review Period.
20. During the Review Period, Cantor’s Chief Executive Officer signed annual certifications that the Firm had in place “risk management controls and supervisory procedures designed to comply with the requirements of [the Market Access Rule], and conducted reviews of those controls and procedures to test their efficacy for compliance purposes for the applicable coverage period.” The certifications did not satisfy Rule 15c3-5(e)(2) because they did not state that the risk management controls and supervisory procedures actually complied with paragraphs (b) and (c) of Rule 15c3-5.

21. Cantor further violated Rule 15c3-5(e)(2) by failing to preserve an executed copy of its certification for the year 2014 for the period required under Securities Exchange Act Rule 17a-4(b).
22. As a result of the deficiencies described in paragraphs 6 through 21 above, Cantor violated NYSE Arca Equities Rule 6.18(b) and (c).⁵

Relevant Disciplinary History

23. Cantor has no relevant disciplinary history.

Other Factors Considered

24. In determining to resolve this matter on the basis set forth herein, Enforcement took into consideration that Cantor, upon discovery of the August 2014 Order and February 2017 Order, took steps promptly to correct certain OMS functions that contributed to the entry of the orders. Enforcement also took into consideration that during and after the Review Period, the Firm implemented additional and modified controls relating to the entry of erroneous orders, including single-order quantity controls that, had they been operative during the Review Period, could have flagged or prevented the orders described above. As set forth below, the Firm has undertaken to address any remaining deficiencies.

ORDER

Cantor Fitzgerald & Co. violated: (i) Rule 15c3-5(c)(1)(ii) by failing to have controls and supervisory procedures that were reasonably designed to prevent the entry of erroneous orders by rejecting orders that exceed appropriate price or size parameters, on an order-by-order basis or over a short period of time; (ii) Rule 15c3-5(e) by failing to adequately document the Firm's review of its controls and properly certify compliance with the Market Access Rule and preserve such certifications as required; and (iii) NYSE Arca Equities Rule 6.18(b) and (c) by failing to establish and maintain adequate supervisory systems and written procedures that were reasonably designed to ensure compliance with Rule 15c3-5.

SANCTIONS


Cantor Fitzgerald & Co. is censured and fined \$155,000.

Cantor shall address any remaining Market Access Rule deficiencies to ensure it has implemented controls and procedures that are reasonably designed to achieve compliance with the rules and regulations cited herein pertaining to market access requirements. Within 120 days of this Decision, a registered principal of the Respondent shall submit to David A. Feldman, Senior Enforcement Counsel, NYSE Regulation, New York Stock Exchange, 11 Wall Street, New York, NY 10005, a signed, dated letter, or an email from a work-related account of the

⁵ NYSE Arca Equities Rule 6.18 is currently denominated NYSE Arca Rule 11.18.

registered principal to david.feldman@theice.com, providing the following information: a reference to this matter; a representation that the Firm has addressed any remaining Market Access Rule deficiencies described in this Decision to ensure that it has implemented controls and procedures that are reasonably designed to achieve compliance with the rules and regulations cited herein pertaining to market access requirements; and the date(s) the deficiencies were addressed.⁶

These sanctions are effective immediately.


Richard E. Simpson
Hearing Officer

⁶ NYSE Regulation may, upon a showing of good cause and in its sole discretion, extend the time for compliance with these provisions.