NYSE ARCA, INC.

NYSE REGULATION,	
Complainant,	Proceeding No. 2016-12-00089
v.	
MAXIM GROUP LLC,	April 22, 2019
Respondent.	

Maxim Group LLC violated: (i) SEC Rule 15c3-5 by failing to establish, document, and maintain, a system of risk management controls and supervisory procedures reasonably designed to manage the financial and regulatory risk of its business activity; and (ii) NYSE Arca Equities Rule 6.18 and NYSE Arca Rule 11.18, by failing to establish and maintain written supervisory procedures and a supervisory system reasonably designed to detect and prevent potentially manipulative trading and achieve compliance with SEC Rule 15c3-5. Consent to censure, $450,000 fine, and undertaking.

Appearances

For the Complainant: Danielle A. Kantor, Esq. and Adam J. Wasserman, Esq., NYSE Regulation.

For the Respondent: Edward Rose, Esq. and James Siegel, Esq. for Maxim Group LLC.

DECISION

Maxim Group LLC ("Maxim" or "Firm") and NYSE Arca, Inc. ("NYSE Arca") 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 findings referred to in the offer of settlement.[1] The Hearing Officer accepts the Offer of Settlement and Consent and issues this Decision.[2]

FINDINGS OF FACTS AND VIOLATIONS

Overview

1.   This matter involves Maxim's compliance with requirements set forth in Rule 15c3-5 under the Securities Exchange Act of 1934 ("Rule 15c3-5" or "Market Access Rule"), NYSE Arca Equities Rule 6.18, and its successor rule, NYSE Arca Rule 11.18.[3] As stated below, from December 1, 2016, through December 19, 2018 ("Relevant Period"), Maxim failed to establish, document, and maintain a system of risk management controls and supervisory procedures reasonably designed to manage the financial and regulatory risk of its business activity as it related to (a) credit limits, (b) erroneous orders, (c) post-trade reviews, and (d) annual reviews, in violation of Rule 15c3-5; and failed to establish and maintain written supervisory procedures ("WSPs") and a supervisory system reasonably designed to achieve compliance with Securities and Exchange Commission ("SEC") and NYSE Arca rules, in violation of NYSE Arca Equities Rule 6.18 and NYSE Arca Rule 11.18. The Firm consents to a censure, a fine of $450,000, and an undertaking.

Background and Jurisdiction

2.   Maxim became registered as an Equities Trading Permit ("ETP") Holder with NYSE Arca on March 19, 2003.

3.   In a letter dated April 12, 2017, which Maxim received, the Enforcement Section of NYSE Regulation, on behalf of NYSE Arca, notified the Firm it was investigating whether the Firm failed to have risk management controls and supervisory procedures in place reasonably designed to prevent the entry of erroneous orders, in violation of NYSE Arca Equities Rules and/or Rule 15c3-5.

Violative Conduct

4.   On November 3, 2010, the SEC adopted Rule 15c3-5 to address concerns relating to the practice of broker-dealers affording direct market access to customers. The rule became effective on July 14, 2011.

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[1] 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 American LLC (fka NYSE MKT LLC), and FINRA.

[2] *See* NYSE Arca Rule 10.6(e). The facts, allegations, and conclusions contained in this Decision were taken from the executed Offer of Settlement and Consent.

[3] On August 17, 2017, NYSE Equities Rule 6.18 became NYSE Arca Rule 11.18. NYSE Arca Equities Rule 6.18 applied to Maxim's conduct before August 17, 2017, and NYSE Arca Rule 11.18 applied to its conduct on and after that date.

5.   Rule 15c3-5 requires, among other things, that a broker-dealer with market access establish risk management controls and supervisory procedures reasonably designed to limit the financial exposure of the broker-dealer and ensure compliance with all regulatory requirements applicable to market access.

6.   Rule 15c3-5 requires that a "broker or dealer with market access, or that provides a customer" with market access, "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."[4]

7.   Rule 15c3-5, in conjunction with the rule's Adopting Release, specifies certain financial and regulatory risks and corresponding requirements, including the requirement to design reasonable controls and supervisory procedures to "[p]revent the entry of orders that exceed" pre-set aggregate credit thresholds for customers, to "[p]revent the entry of erroneous orders, by rejecting orders that exceed appropriate price or size parameters," and to "[a]ssure that appropriate surveillance personnel receive immediate post-trade execution reports."[5]

8.   In addition, Rule 15c3-5 requires broker-dealers to "establish, document, and maintain a system for regularly reviewing the effectiveness" of the above-mentioned controls.[6]

9.   The requirements of Rule 15c3-5 "apply broadly to all forms of market access by broker-dealers that are exchange members or ATS subscribers, including sponsored access, direct market access, and more traditional agency brokerage arrangements with customers, as well as proprietary trading."[7]

10.   Maxim violated Rule 15c3-5 and NYSE Arca's supervisory rules in connection with its calculation and implementation of customer credit thresholds, determination of erroneous order controls, performing post-trade reviews, and conducting of annual reviews.

Rule 15c3-5 Violations with Respect to Customer Credit Limits

11.   Rule 15c3-5(c)(1)(i) requires that broker-dealers' risk management controls and supervisory procedures be reasonably designed to "[p]revent the entry of orders that exceed appropriate pre-set credit or capital thresholds in the aggregate for each customer." The Market Access Rule's Adopting Release explains that these thresholds should be determined "based on appropriate due diligence as to the customer's business,

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[4] Rule 15c3-5(b).

[5] Rule 15c3-5(c)(1)(i), (ii), (iv).

[6] Rule 15c3-5(e).

[7] Risk Management Controls for Brokers or Dealers with Market Access, Exchange Act Release No. 34-63241, 75 Fed. Reg. 69791 (Nov. 3, 2010) (hereinafter "Adopting Release"), at 25.

financial condition, trading patterns, and other matters," and that a broker-dealer must "document that decision."[8]

12. This matter concerns the establishment and implementation of credit limits for institutional customers of Maxim. Although the Firm did not provide these customers direct market access or sponsored access, the Market Access Rule still applies to any customers for whom a broker-dealer provides any market access.[9]

13. Maxim failed to satisfy Rule 15c3-5 credit limit requirements by failing to apply credit limits to any of its institutional customers and failing to maintain any documentation, including WSPs, related to credit limits.

14. Accordingly, Maxim failed to establish, document, and maintain risk management controls and supervisory procedures reasonably designed to prevent the entry of orders exceeding appropriate pre-set credit thresholds, in violation of Rule 15c3-5(b) and Rule 15c3-5(c)(1)(i).

Rule 15c3-5 Violations with Respect to Erroneous Order Controls

15. Pursuant to Rule 15c3-5(b) and 15c3-5(c)(1)(ii), broker-dealers are required to establish, document, and maintain "risk management controls and supervisory procedures . . . 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." Rule 15c3-5 requires such controls and procedures in order to reduce risks to broker-dealers, their customers, and the securities markets.

16. During the Relevant Period, NYSE Regulation identified an order for which Maxim did not file a Clearly Erroneous Execution ("CEE") petition, but which otherwise qualified for treatment as a CEE pursuant to NYSE Arca Rule 7.10.

17. On December 27, 2016, Maxim mistakenly entered a market order to sell 184,162 shares in Company XYZ[10] on NYSE Arca ("December 2016 Order"). The December 2016 Order executed 613 times from 10:02:58.736 through 10:02:59.244, constituting 109,538 shares, ranging in price from $79.68 to $74.92 – at the time of execution, the National Best Bid Offer was $79.68 x $79.70. Within 157 milliseconds, XYZ's price decreased approximately 5.9%. The December 2016 Order accounted for approximately 5.46% of XYZ's average daily volume ("ADV").

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[8] Adopting Release at 39. The SEC reiterated these criteria and documentation obligations on April 15, 2014, in its Response to Frequently Asked Questions Concerning Risk Management Controls for Brokers or Dealers with Market Access.

[9] *See* Adopting Release, at 25.

[10] The name of the issuer is anonymous in this document.

18. Maxim did not employ controls and procedures reasonably designed to potentially prevent erroneous orders.

19. Maxim did not utilize a reasonable ADV control limit. The Firm's ADV control limit was set at 50% for all symbols and for all customers. Similarly, the Firm's dollar limit, limit away from market, and share limit erroneous controls were not tailored to Maxim's business and were unreasonably high. For example, the Firm's share limit control was set at 4,000,000 during the Relevant Period, despite the fact that the Firm did not receive any orders approaching that number during 2016. Moreover, the Firm failed to provide a reasonable basis or justification for these controls.

20. The erroneous order controls Maxim implemented were soft limits, rather than hard blocks. And, the Firm failed to provide evidence that it trained or supervised its traders with respect to the overriding of such limits, and failed to maintain any records of when Firm traders bypassed such soft blocks.

21. Accordingly, Maxim's controls were not reasonably designed to prevent the entry of erroneous orders by rejecting orders that exceeded appropriate price or size parameters, on an order-by-order basis or over a short period. Therefore, Maxim violated Rule 15c3-5(b) and Rule 15c3-5(c)(1)(ii).

Rule 15c3-5 Violations with Respect to the Firm's Post-Trade Controls

22. Rule 15c3-5(c)(2) provides that the controls and supervisory procedures implemented pursuant to the rule "shall be reasonably designed to ensure compliance with all regulatory requirements, including being reasonably designed to . . . (iv) [a]ssure that appropriate surveillance personnel receive immediate post-trade execution reports that result from market access." The SEC further explained in the rule's Adopting Release that the "regulatory requirements" referenced in subsection (c)(2) include "post-trade obligations to monitor for manipulation and other illegal activity,"[11] and that it "believes that immediate reports of executions will provide surveillance personnel with important information about potential regulatory violations, and better enable them to investigate, report, or halt suspicious or manipulative trading."[12] Accordingly, the Financial Industry Regulatory Authority ("FINRA") made clear to broker-dealers in its 2012 Annual Regulatory and Examination Priorities that members must have post-trade surveillance procedures "reasonably designed to identify various potential trading violations such as wash sales, marking, spoofing, layering, quote stuffing, and other potential violations of" rules of the SEC or applicable self-regulatory organizations.

23. Throughout the Relevant Period, Maxim violated the Market Access Rule by not having a spoofing or layering review during the Relevant Period.

24. Accordingly, Maxim violated Rule 15c3-5(b) and Rule 15c3-5(c)(2).

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[11] Adopting Release at 22–23.

[12] Adopting Release at 48.

Rule 15c3-5 Violations with Respect to the Firm's Annual Reviews

25.   Rule 15c3-5(e) provides that broker-dealers shall "establish, document, and maintain a system for regularly reviewing the effectiveness of the risk management controls and supervisory procedures . . . and for promptly addressing any issues," and shall, among other things, 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."[13] The rule further provides that "[s]uch review shall be conducted in accordance with written procedures and shall be documented," and that such procedures and documentation of review must be preserved in a manner consistent with Exchange Act Rule 17a-4(e)(7).

26.   Throughout the Relevant Period, Maxim's WSPs failed to describe in sufficient detail how the Firm should conduct its mandated annual review.

27.   Moreover, Maxim failed to provide evidence that, during the Relevant Period, it reviewed the effectiveness or the reasonableness of its erroneous order controls or its credit limits. A reasonable Market Access Rule annual review should have identified the deficiencies noted above, including institutional customers trading without pre-trade credit thresholds.

28.   Based on the foregoing, Maxim violated Rule 15c3-5(b) and Rule 15c3-5(e).

NYSE Arca Supervisory Violations

29.   NYSE Arca Rule 11.18(b) states, in pertinent part, that "[e]ach ETP Holder . . . must establish and maintain a system to supervise the activities of its associated persons and the operations of its business. Such system must be reasonably designed to ensure compliance with applicable federal securities laws and regulations and NYSE Arca Rules." NYSE Arca Equities Rule 6.18(b) imposed similar obligations.

30.   NYSE Arca Rule 11.18(c) states, in pertinent part, that "[e]ach ETP Holder . . . must establish, maintain, and enforce written procedures to supervise the business in which it engages and to supervise the activities of its associated persons that are reasonably designed to ensure compliance with applicable federal securities laws and regulations, and with the NYSE Arca Rules." NYSE Arca Equities Rule 6.18(c) imposed similar obligations.

31.   During the Relevant Period, Maxim did not have written procedures related to credit limits, and failed to apply credit limits to any of its customers.

32.   During the Relevant Period, Maxim failed to document its process for setting its erroneous order controls or the methodology used to determine functional and appropriate erroneous order controls, and failed to detail its process for evaluating and reviewing control limits and procedures.

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[13] Rule 15c3-5(e)(1).

33. During the Relevant Period, Maxim's WSPs did not include methods for supervising client trading. While the Firm did have certain post-trade surveillances in place, the WSPs did not in all instances state how each review associated with trading activity should be conducted or how issues should be escalated. The WSPs also failed to document the basis for particular control limits, and failed to detail the Firm's process for evaluating and reviewing control limits and procedures. Additionally, the Firm's WSPs failed to specify the controls and procedures the Firm undertook to ensure post-trade execution reports were available immediately to surveillance personnel, and failed to detail the Firm's process for evaluating and reviewing control limits and procedures. And, as previously discussed, the Firm failed to conduct any supervision for spoofing and layering.

34. During the Relevant Period, Maxim's WSPs did not specify the manner in which annual review of market access controls should be conducted. The Firm did not review whether the controls were appropriate or effective given the Firm's business, and the Firm did not conduct a review related to credit limits.

35. The Firm thus violated NYSE Arca Equities Rule 6.18 and NYSE Arca Rule 11.18.

Relevant Disciplinary History

36. On June 19, 2013, FINRA issued Maxim a cautionary action letter noting that the Firm's controls to prevent CEEs were unreasonable as they did not provide for the rejection of orders exceeding appropriate price or size parameters on an order by order basis. Specifically, the Firm's parameters at the time did not cause a soft or hard block to be activated on the basis of the security's average daily volume.

37. On October 9, 2013, in connection with FINRA's 2013 examination of Maxim, FINRA issued the Firm a cautionary action letter for violations of Rule 15c3-5 related to the Firm's failure to establish automated pre-trade capital and credit thresholds, failure to establish reasonable erroneous order controls, and failure to evidence that it performed a reasonable review of its risk management controls.

Other Factors Considered

38. In addition to other personnel changes, the Firm has undertaken to hire a trading compliance specialist and/or independent consultant to address its compliance with Market Access Rule requirements.

ORDER

Maxim Group LLC violated: (i) Rule 15c3-5 by failing to establish, document, and maintain a system of risk management controls and supervisory procedures reasonably designed to manage the financial and regulatory risk of its business activity, and (ii) NYSE Arca Equities Rule 6.18 and NYSE Arca Rule 11.18, by failing to establish and maintain written supervisory procedures and a supervisory system reasonably designed to detect and prevent potentially manipulative trading and achieve compliance with Rule 15c3-5.

SANCTIONS

Maxim Group LLC is censured and fined $450,000.

Maxim shall undertake to revise its WSPs and supervisory system to address the deficiencies described in the paragraphs above, including hiring a trading compliance specialist and/or independent consultant. Within 90 days of this Decision (or such other time as may be mutually agreed to with NYSE Regulation staff), Maxim shall provide: (i) a certification that the Firm has revised its written supervisory procedures and supervisory system to address the deficiencies described in the paragraphs above, including hiring a trading compliance specialist and/or independent consultant; and (ii) the date the revised procedures were implemented.

These sanctions are effective immediately.

SO ORDERED.

David R. Sonnenberg
Hearing Officer