FINANCIAL INDUSTRY REGULATORY AUTHORITY
OFFICE OF HEARING OFFICERS

Department of Market Regulation, Complainant, v. **GFI Securities LLC** (CRD No. 19982), Respondent.	Disciplinary Proceeding No. 20060051583 Hearing Officer: RSH **ORDER ACCEPTING OFFER OF SETTLEMENT** Date: February 27, 2012

INTRODUCTION

Disciplinary Proceeding No. 20060051583 was filed on September 27, 2010, by the Department of Market Regulation of the Financial Industry Regulatory Authority (FINRA or Complainant). Respondent GFI Securities LLC (GFI) submitted an Offer of Settlement (Offer) to Complainant on February 21, 2012. Pursuant to FINRA Rule 9270(e), the Complainant and the National Adjudicatory Council (NAC), a Review Subcommittee of the NAC, or the Office of Disciplinary Affairs (ODA) have accepted the uncontested Offer. Accordingly, this Order now is issued pursuant to FINRA Rule 9270(e)(3). The findings, conclusions and sanctions set forth in this Order are those stated in the Offer as accepted by the Complainant and approved by the NAC.

Under the terms of the Offer, Respondent has consented, without admitting or denying the allegations of the Complaint, and solely for the purposes of this proceeding and any other proceeding brought by or on behalf of FINRA, or to which FINRA is a party, to the entry of findings and violations consistent with the allegations of the Complaint, and to the imposition of

the sanctions set forth below, and fully understands that this Order will become part of Respondent's permanent disciplinary record and may be considered in any future actions brought by FINRA.[1]

BACKGROUND

Origin of Disciplinary Action

1. As alleged in the Complaint, this case involves collusive interactions in 2005 and 2006 (the "relevant period") among FINRA-registered brokers whereby the brokers sought to frustrate their customers' efforts to obtain competitive brokerage rates on credit default swap (CDS) transactions. A CDS is a derivative contract between two counterparties by which the buyer obtains "risk protection" associated with a specified "credit event," such as bankruptcy, default, or credit downgrade, relating to an underlying instrument (*e.g.*, a debt security). Typically the buyer pays the seller a periodic fee in exchange for the seller's agreement to make a specified payment to the buyer if the credit event occurs while the CDS is in force.

2. During the period in issue, GFI was one of a relatively small number of firms that brokered inter-dealer CDS transactions. In earlier years, the opacity and illiquidity of the market enabled the firms handling such transactions to charge commission rates for their services that were attractive to GFI and other inter-dealer brokers. As the trading volume in CDSs rose, however, the market became more liquid with an increasing number of market participants. The customers — typically major investment and commercial banks — accordingly sought lower commission rates on their CDS transactions. Typically, customers would propose rate reductions to brokers like GFI; the brokers could agree, or negotiate with their customers for a more favorable rate.

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[1] One charge against GFI in the Complaint has been dropped. The provisions in this paragraph relate to the remaining charges in the Complaint against GFI.

3. In response to certain commission reduction proposals, and unbeknownst to the customers, persons associated with GFI and their counterparts at competing firms colluded with one another in an effort to keep the customers from obtaining CDS brokerage services at more favorable rates. By engaging in anticompetitive conduct through which it benefitted at its customers' expense, GFI violated NASD Rule 2110 and IM-2110-5.

4. In violation of NASD Rules 3010 and 2110, GFI lacked reasonable supervisory procedures to prevent misconduct of the kind alleged here, and GFI principals failed adequately to supervise the activities of the firm's CDS brokers so as to prevent such misconduct.

ALLEGED ACTS OR PRACTICES AND VIOLATIONS BY RESPONDENT

As alleged in the Complaint, Respondent engaged in the following acts, or failed to act as follows:

Respondents

5. Respondent **GFI** has been an NASD/FINRA-registered broker-dealer since 1987. It is an indirect subsidiary of GFI Group, Inc. ("GFIG"), a Delaware corporation headquartered in New York City whose stock is listed for trading on the New York Stock Exchange. Among other businesses, GFI acts as a broker in transactions between other securities dealers in over-the-counter products, including CDSs.

6. At all relevant times, each of the following individual Respondents was associated with GFI as a general securities representative and served in the capacity described:

(a) **SF,** 42, was a senior CDS broker. SF has worked in the financial services industry for approximately seventeen years.

(b) **LS,** 45, was a CDS broker. She has worked in the financial services industry for approximately twenty-three years.

(c) **MB,** 44, was a senior CDS broker. He was also a registered principal of GFI and supervisor of its CDS desks, in which capacity he supervised Respondents SF and LS, and Broker G1. MB has worked in the financial services industry for approximately twenty-two years.

(d) **DF,** 48, was GFI's Senior Managing Director and a registered principal of the firm. He has worked in the financial services industry for more than twenty-five years.

(e) In April 2008, DF, MB, LS and SF left GFI and migrated as a group to another FINRA broker-dealer member where they each remain registered.

7. **SS,** 38, was at all relevant times a CDS broker at a non-FINRA member (not associated with GFI) and a general securities representative of a FINRA member firm.

Other Inter-Dealer Brokers and Associated Individuals

8. **IDB A** was at all relevant times a FINRA member firm. **Broker A1** was at all relevant times a broker and manager of IDB A's CDS desk.

9. **IDB B** was at all relevant times a FINRA member firm. At all relevant times, **Broker B1** and **Broker B2** were CDS brokers at IDB B.

10. **IDB C** was at all relevant times a FINRA member firm. **Broker C1** was at all relevant times a broker and co-manager of IDB C's CDS desk. **Broker C2** was at all relevant times a broker and co-manager of IDB C's CDS desk.

11. **IDB D** was at all relevant times a FINRA member firm. **Broker D1** was at all relevant times an associated person of IDB D and served as a CDS broker for IDB D.

12. **IDB E** was at all relevant times a non-FINRA registered broker. **Broker E1** was at all relevant times a CDS broker of IDB E and an associated person of an affiliated FINRA-registered member.

13. **IDB F** was at all relevant times a non-FINRA-registered private entity whose CDS activities were conducted by FINRA-registered associated persons of a FINRA member. **Broker F1** was at all relevant times a broker and co-manager of IDB F's CDS desk.

14. **Broker G1** was at all relevant times a CDS broker at Respondent GFI.

15. Some of the firms and individuals identified in paragraphs 8–14 above (or their successors) have entered into letters of acceptance, waiver, and consent (AWC) with FINRA to settle claims related to the events alleged in this proceeding.

FINDINGS AND CONCLUSIONS

It has been determined that the Offer be accepted and that findings be made as follows:[2]

Anti-Intimidation/Coordination (NASD Rule 2110 and IM-2110-5)

16. Paragraphs 1–15 are incorporated by reference.

Collusive Resistance by GFI and IDB A to Fee Schedule Proposed by Client A

17. In July 2005, Client A sought to reduce its brokerage costs by proposing that the brokers it used to effect certain CDS transactions forgo charging Client A commissions when it was the "non-aggressor" on the CDS transactions (*i.e.*, the counterparty whose bid has been hit or whose offer has been lifted by the other counterparty).

18. Through a series of communications, GFI broker LS and Broker A1 at IDB A coordinated their respective firms' responses to the proposal. On July 26, 2005, they shared with each other their reactions to the proposal and discussed an alternative fee schedule that might be proposed to Client A.

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[2] The findings herein are pursuant to Respondent GFI's Offer of Settlement and are not binding on any other person or entity named as a respondent in this or any other proceeding.

19. On Friday, August 5, Broker A1 wrote to LS, "[I]f we go aggressor only on brazil . . u know what is next. we can't do that."[3] Within the hour, LS forwarded to Broker A1 the response GFI's broker SF had sent Client A regarding the proposal:

> I cannot agree to aggressor only. You are asking to cut the bro[kerage] by more than half then. Please do not take my answer as any sign of disrespect. . .

Broker A1 replied, "[W]ill do the same." Later, LS passed along thanks to Broker A1 from SF: SF's "looking over at my bbg [Bloomberg] and thanks you for this/conversing/etc. . ." Broker A1 concluded the communication by telling LS she would inform LS of her response to Client A, adding, "i am in agreement with u."

20. The following Monday, Respondent LS sought an update from Broker A1 about the latter's negotiations with Client A. Broker A1 replied,

> i told [the Client A representative] that i couldn't do aggressor only . . . my negotiations are not complete with her – as she wants something so b/n u and me – maybe brazil 5Y aggressor only. but only the 5Y and nothing else.

21. Consistent with Broker A1's suggested limited concession, Client A ultimately got IDB A to agree to aggressor-only terms only as to CDSs based on debt issued by Brazil or Argentina. GFI agreed to give Client A aggressor-only terms only on CDS index (CDX) transactions and CDSs associated with Mexico, rather than the blanket concession Client A had requested for the non-aggressor side of CDS transactions.

Coordinated Responses to Fee Schedule Proposed by Client B

22. In November 2005, Client B also sought aggressor-only terms on CDS transactions from GFI and other CDS brokers. As they had done in responding to Client A's

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[3] For ease of reading, some of the matter quoted in this Offer of Settlement has been modified from the original ALLCAPS format. A number of additional quotations contained a multi-character, computer-generated code representing an apostrophe in Bloomberg messages; in place of that code this Offer of Settlement uses apostrophes, again for ease of reading.

proposal, LS and SF coordinated GFI's response to Client B with Broker A1's response on behalf of IDB A.

23. Over a period of days, and unbeknownst to Client B, each firm kept the other apprised of their respective communications with Client B. Each assured the other they would not broadly accept aggressor-only terms and discussed specific alternative terms they would propose. For example, Broker A1 suggested a counter-response to Client B's proposal involving one-half basis point charges for both aggressor and non-aggressor transactions. SF responded "that's the best i will do as well. i would give him aggressor only in cdx though." The next day, Broker A1 confirmed to LS that IDB A had not agreed to aggressor-only pricing and stated "i don't think that i will." LS replied "We wont."

24. As GFI's and IDB A's separate negotiations with Client B progressed, the coordination between GFI and IDB A became ever more overt. On December 2, 2005, LS told Broker A1 that SF was about to agree to Client B's "Bro[kerage] schedule but not the agressor/non part at all . . .." Broker A1 asked GFI to "hold on" and then suggested a counter-proposal: "what if we say like 3/8 on brazil and arg 5Y? but ½ on everything else or something? or u don't want to try? 3/8 so low."

25. That same day, SF informed DF of GFI of the coordination with Broker A1. In response to DF's asking whether SF trusted Broker A1, SF told DF that Broker A1 had never lied; that she had laid everything "on the table and made [him] comfortable to do the same"; and that they had a "good, open . . . dialogue," with each understanding that they were "in it together" and that neither would benefit if either "screw[ed]" the other.

26. In addition to coordinating with IDB A, SF also discussed GFI's response to Client B with another competitor, Broker E1 of IDB E. On December 7, 2005, Broker E1 sent a

Bloomberg message to SF that the Client B representative "says u gave him the 3/8 crap." SF responded that the Client B representative was a "tool" and that he had said he would "try to give him it as long as he would stop the aggressor only crap."

27. Ultimately Client B did not get the blanket aggressor-only terms it had sought from GFI or IDB A.

Coordinated Efforts to Resist Client C's Fee Proposal

28. In January 2006 Client C proposed a new fee schedule to a number of the firms with which it did CDS business to reduce the brokerage fees it paid on such transactions. The proposal precipitated a flurry of communications among brokers at the affected firms in which they informed each other of their intentions regarding how they would respond to the proposed fee reductions. Those communications included exchanges between GFI's MB and Broker A1 of IDB A, between GFI's Broker G1 and brokers at IDB C and IDB D, and between SS and Broker C1 of IDB C. Among other communications, in one call Broker A1 summarized the "market consensus," based on her conversation with MB, that Client C's proposal was "ridiculous" and "a fifth of what everyone else pays." Within days of the Client C proposal, Respondent SS and other brokers, including Broker C1, Broker C2, Broker F1, Broker A1 and Broker B1, planned a meeting to coordinate a response.

29. As reflected in these communications and others, MB and SS, along with GFI's Broker G1, were aware of how firms other than their own were responding to Client C's proposal, as well as of the impropriety of their acting in concert to frustrate it. Soon after Client C sent out its proposal, for example, MB checked with Broker A1 to find out if IDB A had received it and then arranged to discuss the situation with Broker A1 on her personal, unrecorded cell phone. When MB spoke the next day with Client C's Client Trader C1, the latter remarked,

> I'm . . . gonna caution if we do find out . . . that people are talking . . . we'll treat it very seriously . . . We do not, and no one on this desk discusses commissions with other dealers.

MB responded, "OK. That's fair enough, I mean we hope not. . . ." Client Trader C1 added that he knew discussions had occurred and that "it's against the law . . . and we do take it pretty seriously, but we also expect on the other side that it's taken seriously as well."

30. Client Trader C1 made similar comments to SS when he called to give SS a "heads-up" that Client C would be seeking to reduce its per-transaction fees on CDS transactions.

31. SS nonetheless proceeded to talk to his counterparts at other firms about the fee proposal and to express a desire to act in concert with them to defeat it. When Broker C1 of IDB C told SS that IDB C would not accept the proposed fee schedule, SS replied that he was in favor of getting other brokers involved in resisting it. Broker C1 and SS again talked about calling a meeting among brokers from various firms to discuss Client C's proposal. They also agreed that Client C's traders should get no more "looks" – i.e., bid or ask information on CDSs – once Client C started paying fees that were a fraction of what others paid.

32. GFI's Broker G1's communications with counterparts at IDB C and IDB D reflect GFI's willingness to collaborate with competitors to defeat Client C's proposal. When Broker C2 of IDB C told Broker G1 that IDB C was going to "fight it," Broker G1 responded, "[W]e have to . . . its fukking outrageous," underscoring the point by adding, "Im serious. We have to really fight this one." When Broker C2 texted Broker G1 that Client C's "traders are going to be fukked" and "wont get any looks or calls on anything" if Client C implemented the proposed fee reductions, Broker G1 responded, "[S]ame here . . . trying to set up a meeting with them tmrrw . . . we said the same thing . . they will get the last call on everything."

33. On January 9, 2006, Client C circulated a modified proposal that provided for higher commissions than did its original proposal. SS thereafter texted Broker C1 that the modified proposal was "certainly better" but that there were still "a couple of spots where it is ridiculous." SS and Broker C1 then exchanged messages about coordinating their counterproposals to Client C and doing so in such a way as to avoid detection.

34. In the ensuing days, Broker C2, co-manager of IDB C's CDS desk, exchanged messages with Broker G1 at GFI and CDS brokers at IDB B and IDB E regarding their respective efforts to resist Client C's proposed fee reductions.

35. On January 17, 2006, Client C advised its CDS brokers that it would postpone implementation of its fee proposal to February 1. A week later, SS texted Broker C1, "I am all for a unified front so should we all meet up? Have u spoken to anyone else?" Broker C1 replied, "I have a feeling people are going to accept it . . . that is what it sounded like GFI is doing. . . . Lets ask around."

36. Ultimately, GFI and the other firms involved in the communications referred to above accepted Client C's modified proposal.

Coordinated Resistance to Client D's Proposed Fee Schedule

37. In the fall of 2006, Client D circulated a proposed reduction of the fees it paid on CDS transactions to its CDS brokers. Once again, MB at GFI, SS, GFI's Broker G1, and their counterparts at other firms communicated among themselves their respective thoughts regarding the proposal and strategies for defeating it.

38. On October 17, Broker C1 of IDB C proposed to SS that the brokers should "all give them a counter proposal . . .something like [the Client E] schedule . . . [Client D] will have to listen." Broker C1 followed up with SS the next day, informing him that GFI and IDB A were

making counterproposals to Client D. "If we all say no," Broker C1 suggested, Client D would "have to change it." SS replied, "I agree. . . We have to take a true stand sometime, seems like this is the right time." Later that day, Broker C1 advised Broker F1 that IDB C had rejected Client D's proposal and informed Broker F1 of specific pricing components of IDB C's counterproposal to Client D.

39. In late October, SS informed Broker C1 that SS's firm was still executing CDS transactions for Client D at the "old" rates. Broker C1 reciprocated by telling SS the specific rates Client D was paying IDB C on such transactions, which were higher than the rates Client D had proposed.

40. As IDB C negotiated with Client D, Broker C1 kept SS apprised of the terms on which IDB C was executing transactions for Client D.

41. Client D ultimately agreed to accept price reductions which were smaller than it had originally proposed.

42. Respondents and other brokers for inter-dealer transactions engaged in many additional improper communications in 2005 and 2006.

43. NASD Rule 2110 and IM-2110-5 prohibit any member or person associated with a member from, among other things, coordinating pricing with, or attempting to influence pricing by, another member or person associated with such member, or otherwise attempting improperly to discourage the competitive activities of another market participant. Through the communications discussed above, GFI sought to frustrate its customers' efforts to obtain brokerage services at rates reflecting a bona fide competitive market. By doing so, GFI violated IM-2110-5 and NASD Rule 2110.

SUPERVISORY FAILURE (NASD Rules 3010 AND 2110)

44. Paragraphs 1-43 are incorporated by reference.

45. MB and DF knew, or ignored red flags indicating, that GFI registered representatives (such as Broker G1, LS and SF) under their supervision were engaging in improper communications with GFI's competitors regarding CDS brokerage rates, but nonetheless failed to take adequate steps to prevent them from doing so. In addition, MB personally participated in such improper communications.

46. By reason of the foregoing, GFI violated NASD Rules 3010(a) and 2110.

INADEQUATE WRITTEN SUPERVISORY PROCEDURES (NASD Rules 3010 AND 2110)

47. Paragraphs 1–46 are incorporated by reference.

48. GFI's written supervisory procedures were not reasonably designed to ensure compliance with IM-2110-5 and other securities law requirements concerning anti-competitive conduct. GFI's written supervisory procedures during the relevant period included a section concerning anti-competitive or collusive conduct, but that section lacked any specificity about how, how often, or by whom supervisory reviews were to be conducted to ensure that such conduct was not occurring. Nor did the written supervisory procedures provide for ongoing and systematic reviews of brokers' electronic and telephonic communications for that purpose.

49. GFI failed to review employees' Bloomberg messages until at least mid-2006 and failed to document such reviews until at least August 2006; and failed to document that it conducted any supervisory reviews of other instant-messaging forms of communications during the relevant period.

50. By reason of the foregoing, GFI violated NASD Rules 3010(b) and 2110.

Based on these considerations, the sanctions hereby imposed by the acceptance of the Offer are in the public interest, are sufficiently remedial to deter Respondent from any future misconduct, and represent a proper discharge by FINRA, of its regulatory responsibility under the Securities Exchange Act of 1934.

SANCTIONS

It is ordered that Respondent be

censured and fined $2,100,000 for violations of NASD Rule 2110 and IM-2110-5 and for supervision violations.

Respondent agrees to pay the monetary sanction(s) upon notice that the Offer has been accepted and that such payments are due and payable. Respondent has submitted an Election of Payment form showing the method by which it proposes to pay the fine imposed.

The sanctions imposed herein shall be effective on a date set by FINRA staff.

SO ORDERED.

FINRA

Signed on behalf of the
Director of ODA, by delegated authority

Thomas R. Gira
Executive Vice President
Department of Market Regulation