

**FINANCIAL INDUSTRY REGULATORY AUTHORITY  
LETTER OF ACCEPTANCE, WAIVER AND CONSENT  
NO. 2016048931101**

TO: Department of Enforcement  
Financial Industry Regulatory Authority ("FINRA")

RE: Citigroup Global Markets Inc.  
CRD No. 7059

Pursuant to FINRA Rule 9216 of FINRA's Code of Procedure, Citigroup Global Markets Inc. ("CGMI" or the "Firm") submits this Letter of Acceptance, Waiver and Consent ("AWC") for the purpose of proposing a settlement of the alleged rule violations described below. This AWC is submitted on the condition that, if accepted, FINRA will not bring any future actions against CGMI alleging violations based on the same factual findings described herein.

**I.**

**ACCEPTANCE AND CONSENT**

- A. CGMI hereby accepts and consents, without admitting or denying the findings, 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, prior to a hearing and without an adjudication of any issue of law or fact, to the entry of the following findings by FINRA:

**BACKGROUND**

CGMI, a FINRA-registered broker dealer since 1936, has its principal place of business in New York, NY. CGMI is a full service firm providing investment banking, asset management, brokerage, securities trading, and advisory services. The Firm trades securities for institutional and individual customers as well as for proprietary accounts. As of September 30, 2017, CGMI had nearly 7,500 registered representatives in over 700 branches, with quarterly revenues averaging \$2 billion, and excess net capital of \$8.48 billion.

**RELEVANT DISCIPLINARY HISTORY**

On June 16, 2006, CGMI executed AWC No. 2005000792101, in which the NASD found that, from July 2002 to May 2005, CGMI, among other things, failed to make various disclosures required under NASD Rule 2711(h) in over 2,500 published research reports. NASD also found that CGMI failed to establish and maintain a supervisory system reasonably designed to detect and prevent violations of NASD Rule 2711(h). CGMI consented to a censure, a \$350,000 fine, and an undertaking to perform a comprehensive review of its research disclosures.

On April 25, 2012, CGMI executed AWC No. 20080123101, in which it consented to a censure and a fine of \$725,000 in connection with violations of NASD Rule 2711 and violations of the Global Research Analyst Settlement. FINRA found that during the period of at least January 2007 through at least March 2010, largely as the result of

programming and technical errors, CGMI failed to comply with various research rating disclosure requirements as well as the prior settlement.

## OVERVIEW

For almost five years (from February 2011 through December 2015, the “Relevant Period”), CGMI displayed to its brokers, customers, and supervisors inaccurate research ratings for over 1,800 equity securities (more than 38 percent of those covered by the Firm). Because of errors in the electronic feed of ratings data that the Firm provided to its clearing firm, the Firm either displayed: (a) the wrong research rating (i.e., a “buy” when the actual rating was a “sell” or “neutral;” a “sell” when the rating was a “buy” or “neutral;” or a “neutral” when the rating was a “sell” or “buy”); (b) a rating when CGMI’s Research Department (“CGMI Research”) did not, in fact, cover the security; or (c) no rating when, in fact, CGMI Research covered the security. The actual research reports, which were available to brokers, and the research ratings appearing in those reports, as published by CGMI Research, were not affected by these errors.

The Firm’s failure to display accurate research ratings caused its brokers to solicit thousands of transactions inconsistent with the Firm’s actual ratings. Brokers also solicited transactions that violated the portfolio guidelines of certain Firm-managed portfolios. Among other guidelines, those portfolios were prohibited from holding “sell”-rated securities. Because brokers relied on the inaccurately displayed research ratings, many customers’ portfolios improperly included “sell”-rated securities. CGMI supervisors, relying on the inaccurate ratings populated in certain of the Firm’s supervisory tools, failed to detect and prevent a substantial number of transactions that were actually inconsistent with CGMI research or transactions that violated portfolio guidelines. The Firm also provided customers with inaccurate ratings on thousands of customer statements and email alerts and displayed inaccurate ratings on online portals available to customers.

The Firm failed to timely correct the inaccurately displayed ratings, despite numerous red flags alerting various individuals across the Firm to ratings inaccuracies for several securities. The Firm also failed to conduct testing reasonably designed to verify the accuracy of research ratings data that it used and distributed.

By virtue of the foregoing conduct, CGMI violated FINRA Rule 2010 (Just and Equitable Principles of Trade), FINRA Rule 2210(d)(1) and NASD Rule 2210(d)(1) (Communications with the Public), and FINRA Rules 3110(a) and (b) and NASD Rules 3010(a) and (b) (Supervision).

## FACTS AND VIOLATIVE CONDUCT

### **1. CGMI’s Research Ratings**

#### *a. Research Ratings Were Important to Customers, Brokers, and Supervisors*

An equity research rating reflects a firm’s opinion of the future performance of a public security, and a research report sets forth analysis supporting that opinion. Research opinions can materially impact individual investment decisions and market prices.

During the Relevant Period, CGMI Research provided a variety of analyses to both CGMI brokers and clients, including equity research ratings. CGMI research ratings reflected the Firm's forecast of expected total return ("ETR") for equity securities over the following 12 months. The Firm rated equity securities it covered as either "buy," "neutral,"<sup>1</sup> or "sell." A "buy" rating indicated that the Firm expected an ETR of 15% or more (or more than 25% for high risk stocks); "neutral" indicated an expectation of a positive ETR less than 15% (or less than 25% for high risk stocks); and a "sell" rating predicted a negative ETR.

CGMI's customers, brokers, and supervisors relied on the Firm's research and research ratings. The Firm designated CGMI Research as the principal source of security recommendations for the Firm. The Firm's written supervisory procedures ("WSPs") instructed brokers that they should document and justify a suitability rationale if they solicited securities transactions contrary to the ratings of CGMI Research. In certain Firm-managed accounts, brokerage customers paid an asset-based fee (up to 2 percent) and gave discretion to brokers to invest their portfolios consistent with guidelines that relied on CGMI research ratings. Those guidelines prohibited the portfolios from holding sell-rated securities, and limited the percentage of securities not covered by Firm research in some portfolios. To monitor compliance with these policies, the Firm employed exception reports designed to alert supervisors of solicited transactions inconsistent with CGMI research ratings or portfolio guidelines. During the Relevant Period, the Firm also displayed CGMI research ratings on customer account statements, in online customer portals, and through e-mail alerts designed to notify customers immediately of research rating changes.

*b. CGMI Displayed Inaccurate Research Ratings*

When CGMI began using a new clearing firm in early 2011, the Firm created and provided to the clearing firm an electronic feed of CGMI research ratings data. A variety of errors with the electronic feed rendered inaccurate a substantial number of research ratings. These inaccurate ratings were then displayed by the clearing firm, on behalf of CGMI, in three places during the Relevant Period: (1) an internal online platform used by Firm brokers when making securities recommendations to customers; (2) CGMI retail customer communications (account statements, client e-mail alerts, and an external online portal); and (3) certain supervisory tools used by the Firm to monitor for trading inconsistent with CGMI Research opinions.

As a result, over the course of the Relevant Period, the Firm inaccurately displayed ratings for more than 1,800 securities covered by CGMI Research (over 38% of the total equity securities covered by the Firm). The ratings for affected securities were inaccurate in one or more ways. The ratings were inaccurate because the Firm either displayed: (a) the wrong research rating (i.e., a "buy" when the actual rating was a "sell" or "neutral;" a "sell" when the rating was a "buy" or "neutral;" or a "neutral" when the rating was a "sell" or "buy"); (b) a rating when CGMI Research did not, in fact, cover the security; or (c) no rating when, in fact, CGMI Research covered the security.

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<sup>1</sup> Prior to October 8, 2011, the Firm rated securities "hold," rather than "neutral."

The inaccuracies in the research ratings feed had widespread, adverse consequences throughout the Relevant Period, resulting in violations of FINRA and NASD Rules as described below.

## **2. CGMI Negligently Made Inaccurate Statements Concerning Research Ratings**

During the Relevant Period, because of the errors with the electronic feed described above, CGMI, through its brokers, negligently made inaccurate statements to customers concerning CGMI research ratings. When making securities recommendations, CGMI brokers relied on inaccurate ratings that the Firm displayed on its internal online portal. As a result, CGMI customers executed thousands of transactions that, although consistent with the internally displayed ratings, were inconsistent with the actual CGMI research ratings. CGMI brokers also relied on the inaccurate research ratings to construct customers' portfolios in certain Firm-managed accounts, thereby causing a substantial number of these accounts to violate portfolio guidelines by holding sell-rated stocks or holding more than the allowable percentage of non-rated securities.

By virtue of the foregoing conduct, the Firm violated FINRA Rule 2010.

## **3. CGMI's Customer Communications Contained Materially Inaccurate Information Concerning Research Ratings**

During the Relevant Period, CGMI made materially inaccurate statements and omissions regarding CGMI research ratings in three types of customer communications: (1) customer account statements, which displayed CGMI research ratings for stocks held by the customer, (2) online portals, through which customers could view CGMI research ratings, and (3) e-mails that alerted subscribed clients to changes in CGMI research ratings for selected securities. These communications, at various points during the Relevant Period, displayed the wrong rating for covered securities, displayed ratings for securities that CGMI Research did not cover at the time, or failed to display ratings for securities that CGMI Research actually rated. The errors affected thousands of customers throughout the Relevant Period who held one or more of over 1,800 securities for which the displayed research rating was inaccurate, or who accessed the Firm portal to review an affected security's rating. Over 19,000 inaccurate ratings were displayed on customer statements alone due to the defective feed. The errors also affected customers who subscribed to receive alerts for 353 affected securities during the Relevant Period, totaling over 1,000 affected alerts, each of which was sent to a significant number of customers.

By virtue of the foregoing conduct, the Firm violated FINRA Rules 2210(d)(1) and 2010 and NASD Rule 2210(d)(1).<sup>2</sup>

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<sup>2</sup> FINRA Rule 2210 became effective February 4, 2013. Communications used prior to February 4, 2013 were subject to substantially similar standards under NASD Rule 2210(d)(1)(B).

#### **4. CGMI's Supervisory Failures**

During the Relevant Period, CGMI failed to establish and maintain a supervisory system and WSPs reasonably designed to ensure that the Firm disseminated accurate and complete research ratings to customers, brokers, and supervisors.

First, CGMI failed to have systems in place reasonably designed to ensure that the Firm displayed accurate and complete ratings information in (1) internal web portals used by brokers in connection with solicited transactions in managed and non-managed accounts, (2) customer web portals, (3) customer account statements, (4) client e-mail ratings alerts, and, (5) supervisory tools used to monitor solicited trades and portfolio transactions. In particular, the Firm failed to conduct testing reasonably designed to verify that its clearing firm obtained and distributed accurate and complete CGMI research ratings information, which the Firm knew would be disseminated to, and relied upon by, customers, brokers, and supervisors. As a result, the Firm solicited transactions that were inconsistent with Firm research ratings or portfolio guidelines, and made materially inaccurate statements and omissions to customers. For the same reasons, the Firm was unable to effectively monitor and identify solicited transactions inconsistent with research ratings or portfolio guidelines.

Second, the Firm failed to timely address red flags regarding research rating accuracy issues. Throughout various points during the Relevant Period, the Firm had in its possession information concerning potentially significant problems with its dissemination and use of research ratings data. This information included ratings accuracy issues reported by brokers and other employees across the Firm. Firm personnel, however, failed to timely or adequately address those issues. Even in those instances in which Firm personnel escalated issues with particular CGMI research ratings, the Firm failed to take appropriate action. As a result, Firm management failed to recognize timely that several individual research rating issues were not isolated, but rather were, in fact, related and stemmed from a larger problem.

For example, in the fall of 2011, various Firm personnel were aware that certain research ratings displayed on customer statements were inaccurate. Although the issue was escalated, the Firm failed to recognize that the issue was part of a larger problem affecting the ratings information feed provided to its clearing firm. Also, in October 2012 a broker notified a Firm help desk that he could not locate a research report to support a rating displayed on the Firm's internal portal. In fact, CGMI Research did not cover the security at that time. The help desk escalated the issue to various individuals throughout the Firm. However, the Firm did not correct the issue regarding that particular security until over twelve months later and the Firm failed to recognize that the issue was part of a much larger problem.

The Firm discovered the entire scope of the ratings display issues in December 2015, following a report from a broker who could not reconcile the ratings displayed on the Firm's internal portal with the Firm's actual research reports. After recognizing the broader ratings display issues, the Firm fixed the ratings display issues and self-reported those issues to FINRA.

By virtue of the foregoing conduct, the Firm violated FINRA Rules 3110(a) and (b), and 2010, and NASD Rule 3010(a) and (b).<sup>3</sup>

### **OTHER FACTORS**

In resolving this matter and determining the appropriate sanction, FINRA has considered that CGMI: (1) self-reported the foregoing research rating issues to FINRA; (2) engaged outside counsel to conduct an internal forensic investigation of the relevant issues; (3) took steps to prevent the display and use of inaccurate research ratings information; (4) provided substantial assistance to FINRA's investigation by sharing the results of its internal investigation; and (5) proposed and developed a substantial remediation plan designed to compensate affected customers.

B. CGMI also consents to the imposition of the following sanctions:

1. Censure;
2. A fine of \$5,500,000; and,
3. The Firm agrees to comply with the following undertaking:
  - a. Within 60 days of the Notice of Acceptance of this AWC, CGMI is ordered to pay compensation totaling at least \$6 million to customers who were solicited to purchase or sell equity securities affected by the Firm's ratings display issues described within this AWC. These payments shall be made to the customers, and in the amounts, specified in a written plan of remediation not unacceptable to FINRA Staff.
  - b. Compensation payments to customers shall be preceded or accompanied by a letter, not unacceptable to FINRA staff, describing the reason for the payment and the fact that it is being made pursuant to a settlement with FINRA and as a term of this AWC.
  - c. Within 90 days of the Notice of Acceptance of this AWC, a designated officer of CGMI shall submit, on behalf of CGMI, satisfactory proof of reasonable and documented efforts undertaken to effect the restitution and notice described above. Such proof shall be submitted to James E. Day, Vice President and Chief Counsel, FINRA Enforcement, 15200 Omega Drive, Suite 300, Rockville, MD 20850.
  - d. If, for any reason, CGMI cannot locate a customer to whom compensation is owed after reasonable and documented efforts within 90 days of the Notice of Acceptance of this AWC, or such additional period provided for under applicable state unclaimed property laws or otherwise agreed to by FINRA staff in writing, CGMI shall forward any undistributed compensation amount to the appropriate escheat, unclaimed property or abandoned property fund for the state in which the customer is last known to have resided. CGMI shall provide satisfactory proof of such action to

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<sup>3</sup> FINRA Rule 3110 superseded NASD Rule 3010, effective December 1, 2014.

the FINRA staff member identified above and in the manner described above, within 14 days of forwarding the undistributed compensation to the appropriate state authority.

- e. CGMI shall pay all costs and expenses associated with the administration of the payments described herein.
- f. FINRA staff may, in its discretion, upon a showing of good cause and upon written request, extend the dates for compliance with any of the terms of the undertaking.
- g. The imposition of this compensation order or any other monetary sanction herein, the timing of such payments, and the acceptance of compensation by the customer, shall not preclude any customer from pursuing a separate action to obtain restitution or other remedies.

CGMI agrees to pay the monetary sanction upon notice that this AWC has been accepted and that such payment is due and payable. CGMI has submitted an Election of Payment form showing the method by which it proposes to pay the fine imposed.

CGMI specifically and voluntarily waives any right to claim that it is unable to pay, now or at any time hereafter, the monetary sanction imposed in this matter.

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

## II.

### WAIVER OF PROCEDURAL RIGHTS

CGMI specifically and voluntarily waives the following rights granted under FINRA's Code of Procedure:

- A. To have a Complaint issued specifying the allegations against it;
- B. To be notified of the Complaint and have the opportunity to answer the allegations in writing;
- C. To defend against the allegations in a disciplinary hearing before a hearing panel, to have a written record of the hearing made and to have a written decision issued; and
- D. To appeal any such decision to the National Adjudicatory Council ("NAC") and then to the U.S. Securities and Exchange Commission and a U.S. Court of Appeals.

Further, CGMI specifically and voluntarily waives any right to claim bias or prejudgment of the Chief Legal Officer, the NAC, or any member of the NAC, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including acceptance or rejection of this AWC.

CGMI further specifically and voluntarily waives any right to claim that a person violated the ex parte prohibitions of FINRA Rule 9143 or the separation of functions prohibitions of FINRA Rule 9144, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including its acceptance or rejection.

### III.

#### OTHER MATTERS

CGMI understands that:

- A. Submission of this AWC is voluntary and will not resolve this matter unless and until it has been reviewed and accepted by the NAC, a Review Subcommittee of the NAC, or the Office of Disciplinary Affairs ("ODA"), pursuant to FINRA Rule 9216;
- B. If this AWC is not accepted, its submission will not be used as evidence to prove any of the allegations against CGMI; and
- C. If accepted:
  - 1. this AWC will become part of CGMI's permanent disciplinary record and may be considered in any future actions brought by FINRA or any other regulator against me;
  - 2. this AWC will be made available through FINRA's public disclosure program in accordance with FINRA Rule 8313;
  - 3. FINRA may make a public announcement concerning this agreement and the subject matter thereof in accordance with FINRA Rule 8313; and
  - 4. CGMI may not take any action or make or permit to be made any public statement, including in regulatory filings or otherwise, denying, directly or indirectly, any finding in this AWC or create the impression that the AWC is without factual basis. CGMI may not take any position in any proceeding brought by or on behalf of FINRA, or to which FINRA is a party, that is inconsistent with any part of this AWC. Nothing in this provision affects CGMI's: (i) testimonial obligations; or (ii) right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party.
- D. CGMI may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. CGMI understands that it may not deny the charges or make any statement that is inconsistent with the AWC in this Statement. This Statement does not constitute factual or legal findings by FINRA, nor does it reflect the views of FINRA or its staff.



The undersigned, on behalf of the Firm, certifies that a person duly authorized to act on its behalf has read and understands all of the provisions of this AWC and have been given a full opportunity to ask questions about it; that it has agreed to its provisions voluntarily; and that no offer, threat, inducement, or promise of any kind, other than the terms set forth herein and the prospect of avoiding the issuance of a Complaint, has been made to induce the Firm to submit it.

12/21/2017

Date (mm/dd/yyyy)

  
\_\_\_\_\_  
Respondent  
Citigroup Global Markets Inc.

By: Joshua E. Levine

Title: Managing Director

Reviewed by:

\_\_\_\_\_  
Susan L. Merrill  
Counsel for Respondent  
Sidley Austin LLP  
787 Seventh Avenue  
New York, NY 10019  
(212) 839-8558

Accepted by FINRA:

\_\_\_\_\_  
Date (mm/dd/yyyy)

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

\_\_\_\_\_  
James E. Day  
Vice President and Chief Counsel  
FINRA Department of Enforcement  
15200 Omega Drive  
Rockville, MD 20850  
(301) 258-8520

The undersigned, on behalf of the Firm, certifies that a person duly authorized to act on its behalf has read and understands all of the provisions of this AWC and have been given a full opportunity to ask questions about it; that it has agreed to its provisions voluntarily; and that no offer, threat, inducement, or promise of any kind, other than the terms set forth herein and the prospect of avoiding the issuance of a Complaint, has been made to induce the Firm to submit it.

12/21/2017

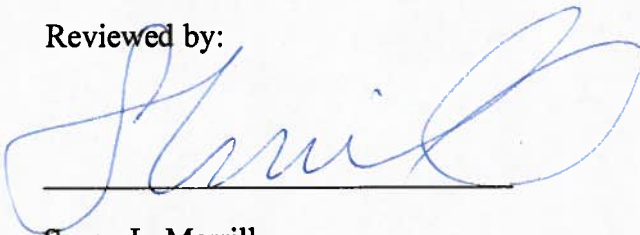
Date (mm/dd/yyyy)

\_\_\_\_\_  
Respondent  
Citigroup Global Markets Inc.

By: \_\_\_\_\_

Title: \_\_\_\_\_

Reviewed by:



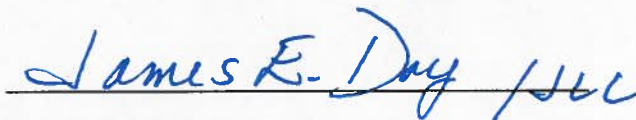
Susan L. Merrill  
Counsel for Respondent  
Sidley Austin LLP  
787 Seventh Avenue  
New York, NY 10019  
(212) 839-8558

Accepted by FINRA:

12/28/2017

Date (mm/dd/yyyy)

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



James E. Day  
Vice President and Chief Counsel  
FINRA Department of Enforcement  
15200 Omega Drive  
Rockville, MD 20850  
(301) 258-8520