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FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
REGISTRATION & DISCLOSURE NO. 20041000004-01

2008 MAY 13 A 11:47
NASD REGULATION, INC.
MARKET REGULATION

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

RE: UBS Securities LLC, Respondent
Broker-Dealer
CRD No. 7654

Pursuant to NASD Rule 9216 of the FINRA Code of Procedure, UBS Securities LLC (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 the firm alleging violations based on the same factual findings described herein.

I.

ACCEPTANCE AND CONSENT

- A. The firm 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

The firm has been a member of FINRA (f/k/a NASD) since August 17, 1978 and its registration remains in effect. The firm's relevant disciplinary history is as follows:

- On July 3, 2003, FINRA censured and fined the firm \$72,500 for violations of NASD Conduct Rules 2110 and 3320, NASD Marketplace Rules 4613, 6620, and 6955, and SEC Rule 11Ac1-1.
- On September 20, 2004, FINRA censured and fined the firm \$25,000 for violations of NASD Conduct Rule 2110, NASD Marketplace Rules 4632 and 6955, and SEC Rules 10b-10 and 11Ac1-1.
- On July 13, 2005, FINRA, NYSE and the SEC jointly censured and fined the firm \$2.1 million for violations of SEC Rule 17a-4.
- On February 15, 2005, FINRA censured and fined the firm \$20,000 for violations of NASD Marketplace Rules 6954 and 6955 and NASD Conduct Rule 2110.

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- On March 23, 2006, FINRA censured and fined the firm \$22,000 for violations of SEC Rule 11Ac1-4, NASD Marketplace Rule 6955(a), and NASD Conduct Rules 2110 and 3010.
- On January 3, 2007, NYSE fined the firm \$95,000 for violations of SEC Rule 17a-4 and NYSE Rules 123c, 342, 132.30, 123(b) and 440.
- On January 19, 2007, FINRA censured and fined the firm \$65,000 for violations of NASD Marketplace Rule 6955(a).
- On March 29, 2007, FINRA censured and fined the firm \$27,500 for violations of SEC Rule 11Ac1-4, NASD Marketplace Rule 6955(a), and NASD Conduct Rules 2110 and 3010.

OVERVIEW

The staff of the Department of Market Regulation conducted seven reviews of UBSW regarding potentially manipulative short selling activity. The reviews covered periods from December 2003 to September 2004. The reviews are summarized as follows:

- 20041000037, covering the period of May 5, 2004 through June 10, 2004 (the "AOTS review period"), following receipt of an issuer complaint by AeroTelesis, Inc. ("AOTS") regarding potentially manipulative short selling activities;
- 20041000014, covering the period of January through April 2004 (the "ZIXI review period") following receipt of several complaints regarding short selling in Zix Corporation ("ZIXI");
- 20041000029, covering the period of December 4, 2003 through February 13, 2004 (the "BLTI review period") following receipt of a call from Nasdaq Issuer Services reporting an issuer complaint from Biolase Technology, Inc. ("BLTI") regarding possible naked short selling;
- 20041000138, covering the period of June 1, 2004 through August 31, 2004 (the "STEM review period") following receipt of a Nasdaq MarketWatch referral of an issuer complaint from Stemcells, Inc. ("STEM") regarding shares of its stock that had been listed and traded in Berlin;
- 20041000101, covering the period of June 1, 2004 through August 31, 2004 (the "JOSB review period") following receipt of a Nasdaq MarketWatch referral of an issuer complaint from Jos. A. Banks Clothiers, Inc. ("JOSB") regarding short interest in its stock and possible market manipulation;

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- 20050002726, covering the period of May 20, 2004 through July 21, 2004 (the "PGTV review period") following receipt of an issuer complaint from Pegasus Communications Corporation ("PGTV") regarding the level of short interest versus its public float; and
- 20041000166, covering the period of August 1, 2004 through September 30, 2004 (the "TZOO review period") following receipt of a referral from Nasdaq MarketWatch concerning a newspaper article in the New York Post about a "short squeeze" in the stock of Travelzoo Inc. ("TZOO").

In Matter 20041000004, the staff of the Department of Market Regulation initiated a review of USBW during the period of April 1, 2003 through June 30, 2003 (the "Bid Test review period") following a bid test sweep alert.

In Matter 20060046163, the staff of the Department Market Regulation conducted an integrated sweep during the period of October 1, 2005 through December 31, 2005 (the "OATS review period") to determine the firm's compliance with applicable OATS rules.

In Matter 20060060328, the staff of the Department of Market Regulation conducted a Trading and Market Making Surveillance Examination (the "2006 TMMS Exam") for trade dates in July 2006 (the "2006 TMMS Exam review period"). For purposes of this examination, the staff reviewed the items contained on Exhibit A attached hereto.¹

The violations contained herein are a result of these reviews.

FACTS

1. The firm accepted 218 customer short sale orders in certain securities (18 during the AOTS review period, six during the STEM review period, eight during the PGTV review period, and 186 during the TZOO review period) and, for each order, failed to make an affirmative determination that the firm would receive delivery of the security on behalf of the customer or that the firm could borrow the security on behalf of the customer for delivery by settlement date. The conduct described in this paragraph constitutes separate and distinct violations of NASD Conduct Rule 3370.
2. The firm effected 34 short sales in certain securities for the firm's proprietary account (32 during the BLTI review period and two during the JOSB review period) and failed to make an affirmative determination that the firm could borrow the securities or otherwise provide for delivery of the securities by settlement date. The conduct

¹ Unless stated otherwise, samples for the 2006 TMMS Exam were from trade dates July 19 - 20, 2006.

described in this paragraph constitutes separate and distinct violations of NASD Conduct Rule 3370.

3. During the ZIXI review period, the firm effected three short sales in certain securities for the firm's proprietary account and failed to annotate an affirmative determination that the firm could borrow the securities or otherwise provide for delivery of the securities by settlement date. The conduct described in this paragraph constitutes separate and distinct violations of NASD Conduct Rule 3370.
4. The firm executed eight short sale orders (eight during the PGTV review period and 186 during the TZOO review period) and failed to properly mark the order tickets as short for those orders. The conduct described in this paragraph constitutes separate and distinct violations of NASD Marketplace Rule 3110.
5. During the Bid Test review period, the firm executed 39 short sale transactions and failed to report each of these transactions to the Nasdaq Market Center with a short sale modifier. The conduct described in this paragraph constitutes separate and distinct violations of NASD Marketplace Rule 6130(d)(6).
6. During the AOTS, STEM, PGTV and TZOO review periods, the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with NASD Conduct Rule 3370. During the PGTV and TZOO review periods, the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with NASD Conduct Rule 3110(b)(1). During the Bid Test review period, the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with NASD Marketplace Rule 6130(d)(6). Specifically, the firm's supervisory system did not include written supervisory procedures providing for one or more of the following: (1) identification of the person(s) responsible for supervision with respect to the applicable rules; (2) a statement of the supervisory step(s) to be taken by the identified person(s); (3) a statement as to how often such person(s) should take such step(s); and (4) a statement as to how the completion of the step(s) included in the written supervisory procedures should be documented. The conduct described in this paragraph constitutes a violation of NASD Conduct Rules 2110 and 3010.
7. During the OATS review period, on five days, the firm submitted to OATS 1,899,045 reportable order events ("ROEs") after the 4:00 AM deadline that were marked late by OATS. These late ROEs represented 4.97 percent of all ROEs (38,175,894) submitted by UBSW to OATS during the review period. The conduct described in this paragraph constitutes separate and distinct violations of NASD Marketplace Rule 6955.

8. During the TMMS Exam review period, the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with respect to the applicable securities laws and regulations, and the Rules of NASD, concerning Order Handling (multiple MPIDs); Best Execution (customer block-sized orders, not held orders, special pricing terms/conditions, limit orders/non-displayed limit orders, and trade-throughs); Other Trading Rules (identical quotes in multiple systems); Soft Dollar Accounts and Trading (soft dollar credit agreement with member and cost/value of research); and Other Rules (multiple MPIDs, books and records). Specifically, the firm's supervisory system did not include written supervisory procedures providing for one or more of the following: (1) the identification of the person(s) responsible for supervision with respect to the applicable rules; (2) a statement of the supervisory step(s) to be taken by the identified person(s); (3) a statement as to how often such person(s) should take such step(s); and (4) a statement as to how the completion of the step(s) included in the written supervisory procedures should be documented. In addition, during the TMMS Exam review period, the firm failed to enforce its written supervisory procedures with respect to Order Handling (disclosure of Order Routing Information Rule), Soft Dollar Accounts and Trading (monitoring research regarding safe harbor). The conduct described in this paragraph constitutes a violation of NASD Conduct Rules 2110 and 3010.
9. During the TMMS Exam review period, the firm (a) failed to show the time of execution on the memorandum of two brokerage orders, (b) failed to show the correct time of execution on the memorandum of one brokerage order, (c) failed to show the time of cancellation on the memorandum of four brokerage orders, (d) incorrectly showed a cancellation on the memorandum of nine brokerage orders, (e) failed to show the limit price of an order on the memorandum of one brokerage order, (f) failed to show the customer name and account number on the memorandum of two brokerage orders, (g) failed to show the partial execution detail on the memorandum of two brokerage orders, (h) failed to show the short or short exempt notation on the memorandum of one brokerage order, and (i) failed to show the correct price of execution on the memorandum of four brokerage orders. The conduct described in this paragraph constitutes separate and distinct violations of SEC Rule 17a-3 and NASD Conduct Rule 3110.
10. During the TMMS Exam review period, the firm failed to preserve for a period of not less than three years, the first two in an accessible place, the memorandum of 13 brokerage orders, five trading ledgers, and four customer confirmations and/or account statements. The conduct described in this paragraph constitutes a violation of SEC Rule 17a-4 and NASD Conduct Rule 3110.

11. During the TMMS Exam review period, the firm (a) reported to ACT the incorrect capacity for 51 last sale reports of transactions in designated securities. The conduct described in this paragraph constitutes separate and distinct violations of NASD Marketplace 4632(d).
12. During the TMMS Exam review period, the firm failed to report to ACT eight last sale reports of transactions in designated securities. The conduct described in this paragraph constitutes separate and distinct violations of NASD Marketplace Rule 4632(b).
13. During the TMMS Exam review period, the firm reported to ACT the incorrect execution time for four last sale reports of transactions in designated securities and failed to report the correct modifier for two last sale reports of transactions in designated securities. The conduct described in this paragraph constitutes separate and distinct violations of NASD Marketplace 4632(c).
14. During the TMMS Exam review period, the firm reported to ACT 120,317 last sale reports of transactions in designated securities it was not required to report. The conduct described in this paragraph constitutes separate and distinct violations of NASD Marketplace 4632(e).
15. During the TMMS Exam review period, the firm transmitted to OATS 14 reports that contained inaccurate, incomplete, or improperly formatted data. Specifically, the reports omitted handling codes or destination codes in five instances and utilized the incorrect type of report in nine instances. These inaccurate and/or incomplete reports represented 23 percent of the sample of reports reviewed in the TMMS examination that the firm transmitted during the review period. The conduct described in this paragraph constitutes separate and distinct violations of NASD Marketplace Rule 6955(a).
16. During the TMMS Exam review period, on 21 occasions the firm failed to display immediately 21 customer limit orders in Nasdaq securities in its public quotation, when each such order was at a price that would have improved the firm's bid or offer in each such security; or when the order was priced equal to the firm's bid or offer and the national best bid or offer for each such security, and the size of the order represented more than a *de minimis* change in relation to the size associated with the firm's bid or offer in each such security. The conduct described in this paragraph constitutes separate and distinct violations of SEC Rule 604 of Regulation NMS.

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B. The firm hereby consents to the imposition of the following sanctions:

A censure, and a fine of \$116,000 (\$50,000 for the violations of NASD Rules 3370, 3110 and 6130; \$20,000 for the supervision violations; \$16,000 for the OATS violations; \$10,000 for the violations of SEC Rules 17a-3 and 17a-4 and NASD Conduct Rule 3110; \$5,000 for the violations of NASD Marketplace Rule 4632; and \$15,000 for the SEC Rule 604 violations); and an undertaking to revise the firm's written supervisory procedures with respect to the areas described in paragraphs six and eight above.

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

The firm agrees to pay the monetary sanction(s) upon notice that this AWC has been accepted and that such payment(s) are due and payable. The firm has submitted an Election of Payment form showing the method by which the firm proposes to pay the fine imposed.

The firm specifically and voluntarily waives any right to claim that the firm is unable to pay, now or at any time hereafter, the monetary sanction(s) imposed in this matter.

II.

WAIVER OF PROCEDURAL RIGHTS

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

- A. To have a Formal Complaint issued specifying the allegations against the firm;
- B. To be notified of the Formal 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.

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Further, the firm specifically and voluntarily waive any right to claim bias or prejudgment of the General Counsel, 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.

The firm further specifically and voluntarily waives any right to claim that a person violated the ex parte prohibitions of NASD Rule 9143 or the separation of functions prohibitions of NASD 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

The firm 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 NASD Rule 9216;
- B. If this AWC is not accepted, its submission will not be used as evidence to prove any of the allegations against the firm; and
- C. If accepted:
 - 1. this AWC will become part of the firm's permanent disciplinary record and may be considered in any future actions brought by FINRA or any other regulator against the firm;
 - 2. this AWC will be made available through FINRA's public disclosure program in response to public inquiries about the firm's disciplinary record;
 - 3. FINRA may make a public announcement concerning this agreement and the subject matter thereof in accordance with NASD Rule 8310 and IM-8310-3; and

4. The firm 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. The firm 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 the firm's right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party.

- D. The firm may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. The firm understands that the firm 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 firm certifies that the firm has read and understand all of the provisions of this AWC and has been given a full opportunity to ask questions about it; that the firm 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.

5/12/08
Date

Respondent
UBS Securities LLC

By: Judith Romaine
Name: Judith Romaine
Title: Executive Director

Reviewed by:
Counsel for Respondent

Judith Romaine
Name: Judith Romaine
Firm: UBS Securities

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Accepted by FINRA:

June 26, 2008
Date

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

Richard Wallace
~~Thomas R. Gira~~ *Richard Wallace*
Executive Vice President
Department of Market Regulation

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Exhibit A

Samples reviewed by the Staff:

- 31 customer and proprietary sale transactions for compliance with SEC Rules 200(g) and/or Rule 203(b);
- 117 customer and proprietary sales, for compliance with NASD Rule 6130;
- One short sale in CQS securities, for compliance with SEC Rule 10a-1 (Tick Test);
- 362 cancelled trades for compliance with NASD Rules 4632(g), 4642(g), 4652(g), 6130(f), 6420(f), and 6620(f);
- 100 limit and market orders executed for compliance with NASD Rules 2110 (and IM-2110-2), 2111, 6541 and 2320, and SEC Rules 602 and 604;
- 21 Limit and market orders and 36 trades executed in a principal or riskless principal capacity, for compliance with capacity reporting under NASD Trade Reporting and ACT rules;
- Four orders for Nasdaq securities in soft dollar accounts and 60 related executions, for compliance with trade reporting rules and the safe harbor limitations of SEC section 28(e);
- Two open buy limit orders and stop sell limit orders in securities traded ex-dividend, for compliance with NASD Rule 3220;
- Two trades in NNM, SC, or CQS securities reported with a .PRP modifier, for compliance with NASD Rules 4632 and 2320;
- 25 orders in securities for which the firm was a market center, for compliance with the order size/type classification requirements of SEC Rule 605;
- Five security/size/order data statistics published on the firm's monthly order execution report, for compliance with SEC Rule 605;
- Data published on the firm's quarterly order routing report ending June 2006 for compliance with SEC Rule 606;

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- 10 customer transactions in OTCBB and OTC equity securities, for compliance with NASD Rules 3110(b) and 2320;
- 53 persons engaged in the firm's trading and market making activities during June 2006 for compliance with NASD Registration rules;
- 60 orders in NNM or SC securities submitted to OATS, for compliance with NASD Rule 6955;
- 427 order/trade records prepared and maintained in connection with the above samples, for general compliance with NASD Rule 3110 and SEC Rules 17a-3 and 17a-4;
- 1041 trades reported to ACT or TRACS in connection with the above samples, for general compliance with NASD Trade Reporting and ACT rules;
- 27 customer trade confirmations reviewed in connection with the above samples, for compliance with SEC Rule 10b-10;
- The firm's establishment and implementation of "regular & rigorous" reviews of the execution quality of orders sent to other market centers and internalized, for compliance with NASD Rules 2320 and 3010, based upon WSPs in effect during July 2006; and
- The firm's establishment and implementation of a supervisory system and written supervisory procedures, for compliance with NASD Rule 3010, based upon WSPs in effect during July 2006.

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