

NASD
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
2004200015601

TO: Market Regulation Department
NASD

RE: Bosc, Inc., Respondent
CRD No. 17530

Pursuant to Rule 9216 of NASD Code of Procedure, Bosc, Inc. ("BOKI" 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 in Part II below. This AWC is submitted on the condition that, if accepted, NASD will not bring any future actions against BOKI alleging violations based on the same factual findings.

BOKI understands that:

1. Submission of this AWC is voluntary and will not resolve this matter unless and until it has been reviewed and accepted by NASD's Department of Market Regulation and National Adjudicatory Council ("NAC") Review Subcommittee or Office of Disciplinary Affairs, pursuant to NASD Rule 9216;
2. If this AWC is not accepted, its submission will not be used as evidence to prove any of the allegations against BOKI; and
3. If accepted:
 - a. *this AWC will become part of BOKI's permanent disciplinary record and may be considered in any future actions brought by NASD or any other regulator against BOKI;*
 - b. *this AWC will be made available through NASD's public disclosure program in response to public inquiries about BOKI's disciplinary record;*
 - c. *NASD may make a public announcement concerning this agreement and the subject matter thereof in accordance with NASD Rule 8310 and IM-8310-2; and*
 - d. *BOKI 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 allegation in this AWC or create the impression that the AWC is without factual basis.*

Nothing in this provision affects BOKI's testimonial obligations or right to take legal or factual positions in litigation or other legal proceedings in which NASD is not a party.

BOKI also understands that its experience in the securities industry and disciplinary history may be factors that will be considered in deciding whether to accept this AWC. That experience and history are as follows:

BOKI entered the securities industry on March 20, 1987 as a member of NASD and its registration remains in effect. BOKI has no relevant disciplinary history.

I.

WAIVER OF PROCEDURAL RIGHTS

BOKI specifically and voluntarily waives the following rights granted under NASD's Code of Procedure:

- A. To have a Formal Complaint issued specifying the allegations against BOKI;
- 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 NAC and then to the U.S. Securities and Exchange Commission and a U.S. Court of Appeals.

Further, BOKI specifically and voluntarily waives 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.

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

II.

ACCEPTANCE AND CONSENT

This matter arose out of the Market Regulation Department staff's review of BOKI's compliance with NASD Rules applicable to trade reporting in the Trade Reporting and Compliance Engine ("TRACE") during the period of July 1, 2003 through September 30, 2003 (the "review period").

- A. BOKI hereby accepts and consents, without admitting or denying the allegations or findings, and solely for the purposes of this proceeding and any other proceeding brought by or on behalf of NASD, or to which NASD 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 NASD:
1. BOKI failed to report to TRACE 491 transactions in TRACE-eligible securities within 75 minutes after execution. These late transactions constituted 43% of all transactions in TRACE securities (1,133) that BOKI was required to report to TRACE during the review period.
 2. The conduct described in paragraph one constitutes separate and distinct violations of NASD Marketplace Rule 6230(a) and a pattern or practice of late trade reporting without exceptional circumstances in violation of NASD Conduct Rule 2110.
 3. The firm's supervisory system did not provide supervision reasonably designed to achieve compliance with respect to applicable securities laws and regulations, and the Rules of NASD concerning TRACE trade reporting. Specifically, the firm's supervisory system did not include written supervisory procedures providing for (i) the identification of the person (s) responsible at the firm to ensure compliance with the applicable rules; (ii) a statement of the step (s) that such person (s) should take to ensure compliance therewith; (iii) a statement as to how often such person (s) should take such step (s); and (iv) a statement as to how enforcement of such written supervisory procedures should be documented at the firm.
 4. The conduct described in paragraph three above constitutes separate and distinct violations of NASD Conduct Rules 2110 and 3010.
- B. BOKI also consents to the imposition, at a maximum, of the following sanctions:

A censure, a fine of \$15,000 (consisting of a \$10,000 fine for trade reporting violations and a \$5,000 fine for inadequate written supervisory procedures), and an undertaking to revise BOKI's written supervisory

procedures with respect to the areas described in paragraph three. Within 30 business days of acceptance of this AWC by the NAC, a registered principal of the Respondent shall submit to the **COMPLIANCE ASSISTANT, LEGAL SECTION, MARKET REGULATION DEPARTMENT, 9509 KEY WEST AVENUE, ROCKVILLE, MD 20850**, a signed, dated letter, providing the following information: (1) a reference to this matter; (2) a representation that the firm has revised its written supervisory procedures to address the deficiencies described in paragraph eight; and (3) the date the revised procedures were implemented.

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

III.

OTHER MATTERS

- A. BOKI understands that BOKI may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. BOKI understands that BOKI 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 NASD, nor does it reflect the views of NASD or its staff.
- B. BOKI agrees to pay any monetary sanctions imposed on BOKI upon notice that this AWC has been accepted and that such payments are due *and payable and has attached an Election of Payment form* showing the method by which BOKI proposes to pay any fine imposed.
- C. BOKI specifically and voluntarily waives any right to claim that BOKI is unable to pay, now or at any time hereafter, any monetary sanction imposed in this matter.

6/30/05

Date

By: Scott B. Grauer
Name: SCOTT B. GRAUER
Title: Pres/CEO

Counsel for Respondent

9/6/05
Date

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



Resource Expenditures and Commitments

We were originally presented with written indications of problems in our TRACE trade reporting in November 2004, as part of Review #MRD200343435 (the "Review"). As indicated in the initial letter received for that Review, our trade reporting fell below the industry average for the quarter ending September 2003. Consequently, we implemented exception tracking and reporting by both Compliance (*see Additional Monitoring and Controls below*) and BOSC Management (*see Additional Supervisory Controls below*). While initial systems corrections resulted in a lower error percentage¹, our primary solution for the reporting issues was our pending conversion to CRI and its ability to provide us with straight-through processing (STP)². Costs for the implementation of CRI were as follows:

Initial CRI Cost:	\$110,419
Accelerant:	\$120,000
Information Systems Labor:	\$78,610
Network Hardware:	\$7,759
TOTAL:	\$316,788

Ultimately, however, CRI was unable to fulfill its commitments and breached its contract with BOSC. We received a reimbursement of the initial cost (\$110,419), but the remaining \$206,369 could not be recouped.

Subsequent to the failure of CRI, we created a project called the Automated Securities Processing Network (ASPN), to do in stages what we would have done all at once with CRI. ASPN includes the Middle Office Manager (fully explained below), the Goldman Cash Portal (which automated all of our activity with Goldman Sachs Money Market trades), BankServ's GFX (which automated the activity we self-clear through the Federal Reserve Book Entry System), the Bloomberg Trading System, and PershingLink. While \$325,000 has been committed for the first three projects listed, the major component of ASPN is InTrader, which will provide a more automated reporting system but which still does not provide STP beyond our internal system (i.e., we would not have STP with respect to Pershing trades). The costs for InTrader may be broken out as follows:

SunGard Professional Services:	\$10,000 ³
Network Hardware:	\$6,358
Information Systems Labor:	\$19,033
Minimum monthly usage fee:	\$40,000

¹ Through the adoption of additional supervisory procedures resulting in the suppression of Pershing's duplicate reporting of our TRACE-eligible trades, we were able to obtain an error rate of 15% for the period December 9, 2003 (the date of implementation of the new procedures) through December 31, 2003.

² Although we indicated in our correspondence dated May 28, 2004 that we were using Bloomberg for automated TRACE reporting instead of CRI, we ultimately returned to the planned CRI conversion due to problems in the planned utilization of Bloomberg.

³ At present, this is actually \$80,000 and increasing.

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An additional component of ASPN is the Middle Office Manager (*see below for functional details*) at a cost of approximately \$30,000, and an annual cost of approximately \$102,000. In addition, there will be approximately 2,000 man-hours for implementation.

In sum, we have expended approximately \$300,000 to resolve the issue, with the bulk of that expense going towards a solution which ultimately proved untenable. Our continuing expenses total over \$500,000 per year, and will increase as the remaining pieces of ASPN are implemented.

Additional Monitoring and Controls

As indicated above, our original understanding was that the CRI conversion would address the error rate. With the delays resulting from CRI's breach of contract, BOSC Management had to implement an interim manual process. To that end, the Traders became the primary control point for trade reporting, and trading management has increased supervisory responsibilities to ensure timely reporting (*see Additional Supervisory Controls below*). In addition to the actual reporting of trades required by TRACE, i.e. the actual placement of the data on the system, BOSC Management also addressed secondary sales issues which resulted in delayed reporting. To address them, we developed supplemental control procedures which are designed to hold accountable those salespersons whose actions may result in late trade reporting. These procedures have already been communicated to Sales Managers and Traders, and are reinforced with our internal Trade Reporting Training Module to be completed by all such individuals. The module has been incorporated into our Firm Element Training Program, and completion will be monitored both by Compliance and by Senior BOSC Management. Failure to complete the module may result in a suspension of trading activity and/or loss of sales compensation, as appropriate.

However, these steps were not fully effective in reducing our error rate. BOSC self-clears fixed income transactions through BOSC Operations, and also clears fixed income trades through Pershing, LLC ("Pershing"). Both of these entities were responsible for reporting TRACE-eligible transactions. Due to the nature of our clearing relationship with Pershing, Pershing categorizes BOSC as a counterparty when clearing transactions with our customers (even though the transactions are internal). As a result, Pershing sends the TRACE-eligible trades from their side via the NSCC interface and thus enters two trades on their end in addition to the one input by BOSC. One trade represents the transaction with BOSC as counterparty, and one represents the transactions between Pershing and the customer. As a result, one late trade posted by BOSC resulted in three late trades being posted altogether. Through reconciliation of trade reports, BOSC Management discovered this and was able to implement the most significant improvement: the suppression of the dealer trades reported by Pershing. Even after this significant improvement, BOSC Management continued to review the process and discovered over a period of weeks that most late trades continued to be those reported by Pershing. Most of these trades were late due to the customer and CUSIP setup processes required by Pershing. Ultimately, BOSC Management worked with Pershing and determined that all Pershing trades could be suppressed. This allowed TRACE reporting to be centralized in BOSC Operations.

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giving BOSC more direct control over the TRACE reporting process. The combination of these efforts resulted in a lowering of our error rate from 54.21% in July 2004 to 11.54% in October 2004.

Additional Supervisory Controls

Although as indicated above our processes and corrections for the period in question have been oriented towards Operations, our reporting of the exceptions themselves included any trends noted; this report is provided quarterly to BOSC Senior Management. In addition, a summary of the reporting was provided no less frequently than annually to our parent company's Risk Oversight and Audit Committee of the Board of Directors. However, as we understood our monthly monitoring and quarterly reporting to be sufficient, there was no mechanism in place for BOSC Management to address the exceptions as they occurred (on a daily basis).

In recognition of the significance of the issue, and in preparation for the thirty- (and ultimately fifteen-) minute reporting requirement, we restructured our supervisory efforts to ensure ground-level supervision of trade errors and provide for immediate attention to issues which may be systematic.

As primary day-to-day supervisory responsibility resided in Michael Ciabocchi as the Manager of Corporate Trading ("MCT"), once our internal Regulatory Reporting System was established in 2005 he began monitoring the explanations provided on that system for late trades. The MCT is responsible for responses to inquiries from Compliance (as indicated above), but more importantly serves as the primary control point for the various issues which may result in TRACE trade reporting errors. To reconcile front and back office issues, and also to reinforce this control, we created a new position, "Middle Office Manager" (the "MM"). Dorlinda Dill, who serves as the MM, provides an additional control and supervisory point for the explanation process, independent from the MCT, and serves as a communications liaison between the back-office Operational function and the front office Trading function. With the addition of these positions, we have centralized TRACE reporting and issue resolution to allow for a much quicker response time. Ultimately, we expect a more proactive approach to be adopted by these positions as a buildup of institutional memory with respect to TRACE issues will allow them to anticipate and resolve issues before our reporting is impacted.

In addition to the immediate efforts of the MCT and MM, analytical supervisory controls have been incorporated to ensure that the significance of issues is properly communicated (including any trends), and that effective corrective actions are taken in a timely fashion. The TRACE results as reported on our internal Regulatory Reporting System ("RRS") are reviewed by Risk Management and communicated by Management to Traders on a daily basis.

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