

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT**

NO. 2006005179801

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

RE: Lazard Capital Markets LLC, Respondent, CRD No. 134736

Pursuant to FINRA Rule 9216 of FINRA's Code of Procedure, Respondent 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 Respondent alleging violations based on the same factual findings described herein.

I.

ACCEPTANCE AND CONSENT

- A. Respondent 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

Lazard Capital Markets LLC ("LCM" or the "firm" or "Respondent")¹ is headquartered in New York, New York and has been a FINRA-regulated firm since 2005. The firm has approximately 136 registered representatives in four branch offices. The firm provides research, sales and trading, and underwriting to institutional customers in equity, fixed income and convertible securities.

RELEVANT DISCIPLINARY HISTORY

LCM has the following relevant disciplinary history:

1. On October 30, 2008, the SEC issued an administrative order (SEC Admin. Rel. 34-58880) in which LCM was ordered to pay \$1.8 million in disgorgement, \$420,000 in prejudgment interest and a \$600,000 monetary penalty for failing to reasonably supervise and implement policies with respect to monitoring the nature

¹ Lazard Freres & Co., LLC, a FINRA-regulated firm since 1936, transferred its capital market business, which is the subject of this matter, to LCM in 2005.

and extent of individuals' provision of travel, entertainment and gifts to representatives of FMR Co. Inc.

2. On April 4, 2008, FINRA accepted a Letter of Acceptance, Waiver and Consent (No. 2006004092501) in which the firm was censured and fined \$30,000 for violations of SEC Rule 605 of Regulation NMS, SEC Rule 203(b)(1) of Regulation SHO and NASD Rules 2110, 3010, 6955(a) relating to incorrect information on not held orders.
3. On October 25, 2005, NASD accepted a Letter of Acceptance, Waiver and Consent (No. E102004024101) in which the firm was censured and fined \$35,000 for inaccurate reporting in connection with TRACE.
4. On September 28, 2005, the NYSE issued an order (HPD# 05-147) in which the firm was fined \$150,000 for inaccurate bluesheet reporting.

OVERVIEW

From January 2003 to December 2004 (the "relevant period"), LCM improperly engaged in a course of practice of using the firm's error account to effect price adjustments for agency trades done primarily on the floor of the NYSE for its largest institutional client (hereinafter referred to as "the Advisor"), in violation of NASD Rule 2110. The Advisor paid just under \$10 million in net commissions to LCM, representing 7.4 percent of the firm's total net commissions during the relevant period.

LCM executed approximately 2,200 equity orders during the relevant period for the Advisor, the vast majority of which were "not held" orders. A "not held" order is a market or limit order that gives the broker both time and price discretion to attempt to get the best possible execution.² LCM executed these "not held" orders in an agency capacity, generally on the floor of the NYSE. For a significant portion of these trades, LCM adjusted the price in favor of the Advisor, that is, it provided the Advisor with a price that was better than the firm's actual average execution price on the floor of the NYSE. During the relevant period, LCM adjusted the prices on approximately 23 percent of the Advisor's orders (approximately 500 orders) and made these adjustments through the firm's error account even though no bona fide trading error had occurred. The total value of the adjustments made in the firm's error account for price adjustments for this one client during the relevant period was over \$1.3 million.

While executing these orders, on certain trades, LCM provided inaccurate communications to the Advisor concerning the prices it obtained throughout the trading day. LCM also failed to supervise trading and the use of the firm's error account, failed to establish and maintain adequate supervisory systems and written procedures, created inaccurate books and records and failed to maintain required records, in violation of Section 17(a) of the Securities Exchange Act, SEC Rule 17a-3 and 17a-4 thereunder, and NASD Rules 3010, 3110 and 2110.

² A "held" order is a market or limit order that the broker must execute, as instructed, without discretion as to the time of an execution.

FACTS AND VIOLATIVE CONDUCT

I. LCM ENGAGED IN A COURSE OF PRACTICE OF ADJUSTING TRADE PRICES FOR THE ADVISOR THROUGH LCM'S ERROR ACCOUNT

1. During the relevant period, the Advisor was LCM's largest institutional customer and accounted for 7.4 percent of the firm's net commissions.
2. The Advisor's traders were responsible for selecting brokerage firms, such as LCM, to execute the Advisor's orders. The Advisor's traders were paid a salary and a bonus. Their bonuses were based, in part, on whether they were able to obtain the AVWAP on the orders they placed with brokerage firms.³
3. The Advisor placed approximately 2200 orders with LCM during the relevant period, the vast majority of which were "not held" orders in NYSE-listed securities. These orders were executed on an agency basis, generally on the floor of the NYSE. There were also a small number of "not held" agency orders in Nasdaq securities, effected through a market maker. Because the orders were "not held," the LCM trader had time and price discretion to execute transactions throughout the day in an effort to obtain the best possible price for the order.
4. LCM executed the Advisor's order in a series of agency transactions during the day by sending the orders to the floor of the NYSE and other exchanges and which were reported to the market and to the regulators as agency trades at the executed prices. For approximately 23 percent of these orders, LCM then made price adjustments at the end of the day and improperly charged these adjustments to its "upstairs" equity error account.
5. During the relevant period, LCM executed agency trades and then made adjustments on 498 orders, resulting in over \$1.3 million in price adjustments in favor of the Advisor.⁴

II. LCM KNEW OR SHOULD HAVE KNOWN THAT THE ENTRIES IN ITS ERROR ACCOUNT WERE PRICE ADJUSTMENTS AND NOT BONA FIDE ERRORS

6. LCM engaged in the course of practice of making these adjustments through its equity error account when it knew or should have known these entries were price adjustments and not bona fide errors. Traders and supervisors received reports detailing the amount of errors for this account.

³ "AVWAP" is a term used by the Advisor to describe the Available Volume Weighted Average Price.

⁴ The total value of the trades on which these adjustments were made was \$2.1 billion, and the weighted average price adjustment was \$0.026 per share.

7. The applicable NYSE rules and guidance in effect during the relevant period provided that an error is an actual mistake in the execution of an order, such as when a "held" or "not held" order: (i) is executed in the wrong security, on the wrong side of the market or at a price outside the limit price of the order; (ii) is over bought or over sold; or (iii) duplicates an execution.⁵
8. In addition, the applicable NYSE guidance in effect during the relevant period provided that an error also occurs when the trader misses the market on a "held" order but that the failure to execute a "not held" order on the NYSE in accordance with the customer's expectations is not an error and a member's error account may not be used to issue reports or prices that customers may be seeking.⁶
9. During the relevant period, and pursuant to their agreement, LCM executed all of the Advisors' trades on an agency basis. As a result, the Advisor received a two-cent rebate on the commissions charged by LCM on such agency trades.
10. In 498 instances during the relevant period, LCM adjusted the Advisor's prices by making equity error account entries.
11. Certain LCM traders assigned to the Advisor's account had discretion to adjust trade prices through the equity error account and were not required to seek any approval or complete any type of documentation to effect such adjustments.
12. In fact, LCM's trading assistant had standing instructions to make such adjustments through the equity error account. During the trading day, the LCM traders reported trade executions and the final average price for each order to the Advisor through the Financial Information Exchange Protocol (FIX) system. At the end of the day, the Advisor's back office confirmed the order to LCM, noting the average price and detailing to which Advisor account(s) the shares were to be allocated. LCM's trading assistant was instructed that when the price communicated from the Advisor's back office differed from the actual execution prices shown on LCM's books and records but matched the price reported by LCM's traders to the Advisor through FIX, she was to make an adjustment through the equity error account and give the Advisor the price reported by LCM's traders. The trading assistant made such adjustments and was not required to seek or obtain approval for such entries.
13. Adjustments for the Advisor during the relevant period accounted for \$1.3 million in the firm's equity error account or 66 percent of the total amount in the equity error account when the Advisor only accounted for 7.4 percent of net commissions. In contrast, the largest dollar amount in adjustments in the firm's

⁵ See NYSE Rule 134; NYSE Information Memo 01-38 (Nov. 6, 2001) and NYSE Information Memo 02-7 (Feb. 5, 2002).

⁶ See NYSE Information Memo 02-07 (Feb. 5, 2002) and NYSE Information Memo 02-19 (April 29, 2002).

equity error account for any other client during the relevant period was only \$98,000.

III. LCM FAILED TO MAINTAIN ACCURATE BOOKS AND RECORDS

14. During the relevant period, LCM received “not held orders” from the Advisor and executed the orders in a series of agency transactions, generally on the floor of the NYSE. As LCM executed each transaction, it received information from various sources about the prices obtained on these agency trades.
15. LCM communicated prices electronically to the Advisor through the Advisor’s proprietary FIX system. Some of these communications contained inaccurate information regarding the prices the firm had obtained.
16. In addition, LCM failed to maintain the FIX communications, as required by SEC Rules 17a-3 and 17a-4 and NASD Rule 3110.
17. Section 17(a)(1) of the Exchange Act provides that each member broker or dealer “shall make and keep for prescribed periods such records, furnish copies thereof . . . as the [SEC], by rule, prescribes as necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this title.”
18. Rule 17a-4(b)(4), in turn, requires each broker or dealer to “preserve for a period of not less than 3 years, the first two years in an accessible place [o]riginals of all communications received and copies of all communications sent by such member, broker or dealer (including inter-office memoranda and communications) relating to his business as such.”
19. NASD Rule 3110 requires that “each member shall make and preserve books, accounts, records, memoranda, and correspondence in conformity with all applicable laws, rules, regulations and statements of policy promulgated thereunder and with the Rules of this Association and as prescribed by SEC Rule 17a-3.”
20. During the relevant period, LCM provided inaccurate FIX communications to the Advisor, failed to maintain the FIX communications, and failed to maintain accurate books and records by making error account entries with respect to transactions that did not constitute bona fide errors. As a result, LCM violated SEC Rules 17a-3 and 17a-4 and NASD Rules 3110 and 2110.

IV. LCM FAILED TO SUPERVISE THE USE OF ITS ERROR ACCOUNT

21. LCM’s failure to supervise its equity error account activity was repeated and regular. The volume and dollar amount reflected in the equity error account for the Advisor was substantial, yet no steps were taken to terminate this practice.

22. The firm knew or should have known its traders were misusing the equity error account but failed to stop the practice. The firm also failed to maintain adequate policies and procedures with respect to trading and the use of its equity error account.
23. In addition, the firm had no system to ensure that price adjustments that did not constitute errors were not entered into the equity error account.

VIOLATIONS

In light of the above, LCM violated NASD Rules 2110, 3010, 3110 and Section 17(a) of the Exchange Act and SEC Rules 17a-3 and 17a-4.

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

1. a censure; and
2. a fine in the amount of \$550,000.

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

LCM 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.

I.

WAIVER OF PROCEDURAL RIGHTS

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

- A. To have a Complaint issued specifying the allegations against LCM;
- 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, LCM 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.

LCM 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.

II.

OTHER MATTERS

LCM 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 LCM; and
- C. If accepted:
 - 1. this AWC will become part of LCM's permanent disciplinary record and may be considered in any future actions brought by FINRA or any other regulator against LCM;
 - 2. this AWC will be made available through FINRA's public disclosure program in response to public inquiries about LCM's disciplinary record;
 - 3. FINRA may make a public announcement concerning this agreement and the subject matter thereof in accordance with FINRA Rule 8313; and
 - 4. LCM 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. LCM 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 LCM's right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party.
- D. LCM may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. LCM

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.

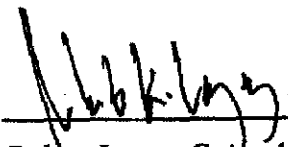
The undersigned, on behalf of the firm, certifies that a person duly authorized to act on its behalf has read and understands all of the provisions of this AWC and has been given a full opportunity to ask questions about it; that it has agreed to its provisions voluntarily; and that no offer, threat, 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.

4 May 2010

Date

Lazard Capital Markets LLC, Respondent

By:



Robert Lagay, General Counsel

Reviewed by:



Louis J. Barash
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Accepted by FINRA:

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

June 2, 2010

Date



Samuel L. Israel
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