

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. 2011027202401**

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

RE: HSBC Securities (USA), Inc. ("HSI" or the "Firm"), Respondent
CRD No. 19585

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 the Firm alleging violations based on the same factual findings described herein.

I.

ACCEPTANCE AND CONSENT

- A. Respondent 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

HSI has been a FINRA-regulated broker-dealer since July 25, 1987. HSI is a full-service broker-dealer headquartered in New York, and it has approximately 275 active branches and 2,300 registered representatives.

RELEVANT DISCIPLINARY HISTORY

On December 15, 2004, NYSE issued a Hearing Panel Decision in which it found that HSI: (1) violated NYSE Rule 440 and SEC Rule 240.17a-4(b)(4) by failing to preserve for a period of three years electronic communications relating to the business of the Firm; (2) violated Exchange Rule 342(a) and (b) in that the Firm failed to reasonably supervise and control its operational and technological activities, and failed to establish a separate system of follow-up and review to assure compliance with Exchange and federal securities laws governing retention of electronic communications; (3) violated Exchange Rule 351 in that the Firm did not promptly report to the Exchange that it had violated provisions of the

federal securities laws and Exchange Rules by failing to retain electronic communications as required. HSI consented to the sanction of a censure and a \$500,000 fine. See HPD 04-190.

OVERVIEW

At various times over several years, HSI experienced: (1) electronic blue sheet deficiencies, in violation of NASD/FINRA Rules 8211 and 8213; (2) prospectus delivery deficiencies, in violation of NASD Rule 2110 and FINRA Rule 2010; (3) research disclosure deficiencies in violation of NASD Rule 2711(h)(2); and (4) text message retention deficiencies, in violation of SEA Rule 17a-4(b)(4), NASD Rules 3110 and 2110, and FINRA Rule 2010. HSBC has satisfied the criteria necessary to receive credit for extraordinary cooperation.

FACTS AND VIOLATIVE CONDUCT

1. HSI Experienced Blue Sheet Deficiencies, in Violation of Rules 8211 and 8213

FINRA Rules 8211 and 8213 (previously NASD Rules 8211 and 8213¹) require that a firm submit to regulators transaction data in an automated format (i.e., Blue Sheets) with certain designated information, including the indication of whether a transaction was a purchase, sale, or short sale. Firms generate these Blue Sheet submissions at the request of regulators in connection with investigations of questionable trading. Firms have the responsibility to reasonably ensure that the information submitted to regulators via Blue Sheets is accurate.

During the period of September 11, 2006 through August 18, 2010, HSI's middle office system erroneously left off short sale indicators when communicating with its back office system, which reported the Firm's Blue Sheets. As a result, the Firm misreported over 360 short sale transactions as long sales (out of approximately 121,000 transactions in total) on 208 Blue Sheets (out of a total of approximately 3,000 Blue Sheets) during this four-year period, in violation of FINRA/NASD Rules 8211 and 8213.

2. HSI Experienced Prospectus Delivery Deficiencies, in Violation NASD Rule 2110 and FINRA Rule 2010

Section 5(b)(2) of the Securities Act of 1933 (the "Securities Act") prohibits the delivery of certain securities unless such delivery is accompanied by or preceded by a copy of a prospectus that meets the requirements of the Securities Act.

¹ FINRA Rules 8211 and 8213 superseded NASD Rules 8211 and 8213 on December 15, 2008.

FINRA Rule 2010 (formerly NASD Rule 2110)¹ requires that a FINRA-regulated broker-dealer, in the conduct of its business, observe high standards of commercial honor and just and equitable principles of trade. The failure to deliver offering documents to customers as required by Section 5(b)(2) of the Securities Act constitutes a violation of NASD Rule 2110 and FINRA Rule 2010.

From May 28, 2008 through April 30, 2010, HSI failed to deliver over 500 prospectuses or offering memoranda that were required to be delivered in connection with approximately 2,000 fixed income transactions. Such conduct constitutes a violation of NASD Rule 2110 and FINRA Rule 2010.

3. HSI Experienced Research Report Disclosure Deficiencies, in Violation of NASD Rule 2711(h)(2)

NASD Rule 2711(h)(2)(A) requires a broker-dealer to disclose in research reports if it has received any compensation for investment banking services from the subject company in the previous 12 months. Rule 2711(h)(2)(A)(ii) specifically provides that members "must disclose in research reports if the member or affiliate: (a) managed or co-managed a public offering of securities for the subject company in the past 12 months; (b) received compensation for investment banking services from the subject company in the past 12 months; or (c) expects to receive or intends to seek compensation for investment banking services from the subject company in the next 3 months."

HSI experienced a breakdown in its automated feeds from August 2009 through June 2010, resulting in the Firm's failure to append certain investment banking disclosures to its research reports during this period. In addition, HSI learned that it had also failed to include certain debt offerings in the definition of investment banking that was used to determine the appropriate disclosures for its research reports up until that time. As a result of these deficiencies, from March 2007 through June 2010, HSI issued over 1,000 equity research reports without over 2,100 required disclosures (out of approximately 13,600 equity research reports with 75,000 disclosures in total). Moreover, due to incorrect mapping of company identifiers, during the period from August 4, 2011 through October 13, 2011, at least 70 of HSI's research reports initially failed to contain proper disclosures (out of approximately 1,600 research reports in total). By virtue of all of this conduct, HSI violated NASD Rule 2711(h)(2).

4. HSI Experienced Text Message Retention Deficiencies, in Violation of SEA Rule 17a-4(b)(4), NASD Rules 3110 and 2110, and FINRA Rule 2010

According to SEA Rule 17a-4(b)(4), every member, broker, and dealer subject to SEA Rule 17a-3 must preserve for a period of not less than three years, the first two years in an easily accessible place, "[o]riginals of all communications received and copies of all communications sent (and any approvals thereof) by the

¹ FINRA Rule 2010 superseded NASD Rule 2110 on December 15, 2008.

member, broker or dealer (including inter-office memoranda and communications) relating to its business as such, including all communications which are subject to rules of a self-regulatory organization of which the member, broker or dealer is a member regarding communications with the public.”

NASD Rule 3110¹ stated, in part, that “[e]ach 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. The record keeping format, medium, and retention period shall comply with Rule 17a-4 under the Securities Exchange Act of 1934.”

Despite HSI’s policy of disabling text messaging on employee Blackberries, certain non-technology employees had Blackberries with inbound texting functionality before November 2009. Around November 2009, HSI took steps to eliminate this functionality. However, 10 registered employees out of approximately 100 sampled still had Blackberries with texting capability from November 2009 through May 2010. HSI failed to retain Blackberry text messages received by certain employees prior to May 2010. As a result, the Firm violated SEA Rule 17a-4(b)(4), NASD Rules 3110 and 2110, and FINRA Rule 2010.

OTHER FACTORS

HSI satisfied the criteria necessary to receive credit for extraordinary cooperation. *See* Regulatory Notice 08-70 (*FINRA Investigations: FINRA Provides Guidance Regarding Credit for Extraordinary Cooperation*, November 2008).

Although HSI experienced deficiencies in electronic blue sheet reporting, prospectus delivery, research report disclosures, and text message retention over the course of several years, HSI detected these violations on its own, initiated internal investigations upon discovery of the violations, identified the causes of the violations, and ensured that the identified problems were not broader in scope. HSI then remediated its systems, procedures, and controls to prevent future violations in each of these areas -- all prior to FINRA’s involvement. Moreover, HSI took the additional step of verifying that its remediation efforts were fully effective. In addition, HSI provided information, documents, and data to FINRA staff. HSI also provided substantial access and assistance to FINRA staff months later when FINRA evaluated the remediation HSI had put in place. In light of its extraordinary cooperation, HSI has received a reduced fine.

¹ NASD Rule 3110 was effective during the period of HSI’s violation.

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

- a. A censure; and
- b. A fine of \$250,000.

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

HSI 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

Respondent 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, Respondent 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.

Respondent 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

Respondent 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 it; and
- C. If accepted:
 - 1. this AWC will become part of HSI'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 FINRA Rule 8313; and
 - 4. HSI 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. HSI 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. HSI 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 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 HSI 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.

12/28/2012
Date (mm/dd/yyyy)


Respondent HSBC Securities (USA), Inc.

By: ANTHONY VERGA

Title: DEPUTY CHIEF COMPLIANCE OFFICER

Reviewed by:


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Accepted by FINRA:

1/7/2013
Date

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



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