

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER, AND CONSENT
NO. 2014039952901**

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

RE: E*TRADE Securities LLC (Respondent)
Member Firm
CRD No. 29106

Pursuant to FINRA Rule 9216, Respondent E*TRADE Securities LLC 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 in this AWC.

I.

ACCEPTANCE AND CONSENT

- A. Respondent accepts and consents to the following findings by FINRA without admitting or denying them:

BACKGROUND

E*TRADE has been a FINRA member since February 1992. Its principal place of business is Jersey City, New Jersey. E*TRADE provides brokerage services, primarily online securities investing and trading services, to individual retail customers. The firm has over 2,100 registered persons and 40 branches.¹

OVERVIEW

From February 2016 through November 2021, E*TRADE failed to establish and maintain a supervisory system, including written procedures, reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable FINRA rules, related to detecting potentially manipulative trading by its customers.

As a result, E*TRADE violated FINRA Rules 3110 and 2010.

FACTS AND VIOLATIVE CONDUCT

This matter originated from reviews conducted by FINRA's Market Regulation Department.

¹ For more information about the firm, including prior regulatory events, visit BrokerCheck® at www.finra.org/brokercheck.

E*TRADE failed to establish and maintain a supervisory system reasonably designed to detect manipulative trading.

FINRA Rule 3110(a) requires that FINRA members establish and maintain a system to supervise the activities of each associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable FINRA rules. A violation of FINRA Rule 3110 is also a violation of FINRA Rule 2010, which requires “[a] member, in the conduct of its business, [to] observe high standards of commercial honor and just and equitable principles of trade.”

During the relevant period, E*TRADE’s system for monitoring trading conducted through its platform relied on automated surveillance reports to detect various forms of potentially manipulative trading by its customers. Depending on the nature of the potentially manipulative activity identified, these reports were escalated either to the firm’s compliance or anti-money laundering departments for further investigation. As set forth below, however, this supervisory system was not reasonably designed with respect to detecting potentially manipulative trading involving wash trades, prearranged trading, and marking-the-close.

Wash Sales and Prearranged Trading

During the period December 2016 through November 2021, E*TRADE used multiple surveillance reports to identify potential wash trades and prearranged trades by its customers. Certain of these reports, however, used parameters that significantly restricted their ability to detect such trading, particularly in lower priced and thinly traded securities (which may be more easily affected by manipulative trading). For example, the firm employed a surveillance report to identify potential wash sales, which it defined as “one or more transactions where there is no change in beneficial ownership.” The surveillance system however, flagged trades that met this definition only if the total principal value of the trade was more than \$1,000, regardless of the price of the underlying security. Also, the firm’s surveillance reports would not detect either a potential wash sale or prearranged trade if the two sides of the transaction were executed more than one second apart, even though wash trades and manipulative prearranged trades could be executed more than one second apart.

Marking-the-close

During the relevant period, E*TRADE used several surveillance reports to detect potential marking-the-close activity by its customers. Starting in February 2017, however, the firm modified the surveillance parameters in these reports in a way that rendered them too restrictive to reasonably detect potential marking-the-close activity, especially in lower priced securities.

For example, in February 2017, the firm revised its primary marking-the-close surveillance report to only identify orders and trades that were entered and executed in

the last minute of the trading day. This restriction prevented the firm from identifying instances of potential marking-the-close activity, particularly in lower priced and thinly traded securities, which occurred prior to that time. The firm also added three additional parameters to this surveillance report: (1) an aggregate end-of-day position exceeding \$10,000 for all accounts in a household; (2) a total execution volume greater than one percent of the security's 30-day average daily volume (ADV); and (3) an execution volume of 20 percent or more as a percentage of the customer's position. Importantly, as modified, the surveillance report would only flag a potential instance of marking-the-close if *all* three of these factors were present simultaneously.² As restricted, the surveillance report was not a reasonable method for identifying potential marking-the-close activity.

Other Potentially Manipulative Activity

During the relevant period, E*TRADE's surveillance system was not reasonably designed to detect certain types of potentially manipulative trading. Specifically, E*TRADE did not have surveillance reasonably designed to detect trading that artificially increased or decreased the price of thinly traded stocks, such as when a customer attempted to artificially influence the price of a security by effecting a series of buy transactions within a short period of time to create the false appearance of trading interest and activity in the security, followed shortly thereafter by transactions on the opposite side of the market to reap profits from an artificially increased price. Further, while E*TRADE used surveillance reports to detect potential intraday manipulative trading, the parameter settings of these reports were not reasonably designed to detect the aforementioned activity. For example, the reports would only flag a pattern of trading for review if the trades executed on both sides of the market were executed within a one-second window and only if the accounts involved held at least ten percent of the shares outstanding at E*TRADE in that security at the end of the trading day. However, this type of potentially manipulative trading activity could occur over several minutes and in accounts that had reduced their positions below the ten percent threshold during the day. Additionally, E*TRADE's surveillance reports only flagged such a trading pattern as potentially manipulative if the pattern included cancelled orders, even though customers can manipulate the price of a security without cancelling orders.

* * *

As a result of the foregoing, E*TRADE failed to establish and maintain a supervisory system that was reasonably designed to achieve compliance with applicable federal securities laws and regulations and FINRA rules relating to potentially manipulative trading, in violation of FINRA Rules 3110 and 2010.

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

- a censure;

² After the firm added these new parameters, the average number of trades identified by its marking-the-close surveillance report decreased more than 98 percent.

- a total fine of \$350,000, of which \$144,500 is payable to FINRA;³ and
- Within 180 days of the Notice of Acceptance of the AWC, or such additional period based on a showing of good cause as agreed to by a FINRA staff member in writing, a principal of the firm shall submit to the COMPLIANCE ASSISTANT, DEPARTMENT OF ENFORCEMENT, 15200 OMEGA DRIVE, SUITE 300, ROCKVILLE, MD 20850, a signed, dated letter, or an email from a work-related account of the registered principal to MarketRegulationComp@finra.org providing the following information: (1) a reference to this matter; and (2) a representation that the firm has implemented a supervisory system reasonably designed to detect the potentially manipulative trading activity described in this AWC.

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

Respondent specifically and voluntarily waives any right to claim an inability to pay, now or at any time after the execution of this AWC, the monetary sanction imposed in this matter.

The sanctions imposed in this AWC shall be effective on a date set by FINRA.

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

³ The remainder of the fine shall be allocated to The Nasdaq Stock Market LLC, NYSE Arca, Inc., Investors Exchange, LLC; and Cboe EDGX Exchange, Inc. for similar violations.

- 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 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 its acceptance or rejection.

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 Respondent; and
- C. If accepted:
 - 1. this AWC will become part of Respondent's permanent disciplinary record and may be considered in any future action brought by FINRA or any other regulator against Respondent;
 - 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 its subject matter in accordance with FINRA Rule 8313; and
 - 4. Respondent 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. Respondent 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 Respondent's right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party. Nothing in this provision affects Respondent's testimonial obligations in any litigation or other legal proceedings.

- D. Respondent may attach a corrective action statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. Respondent 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.

The undersigned, on behalf of Respondent, certifies that a person duly authorized to act on Respondent's 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 Respondent has agreed to the AWC's provisions voluntarily; and that no offer, threat, inducement, or promise of any kind, other than the terms set forth in this AWC and the prospect of avoiding the issuance of a complaint, has been made to induce Respondent to submit this AWC.

December 31, 2021

Date

S. Anthony Taggart

E*TRADE Securities LLC
Respondent

Print Name: S. Anthony Taggart

Title: Managing Director and Counsel

Reviewed by:

John Sakhleh

John Sakhleh
Counsel for Respondent
Sidley Austin LLP
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Accepted by FINRA:

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

January 10, 2022

Date

Doria Bachenheimer

Doria G. Bachenheimer
Principal Counsel
FINRA
Department of Enforcement
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