

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. 2017053082701**

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

RE: Bay Crest Partners, LLC, Respondent
Broker-Dealer
CRD No. 39944

Pursuant to FINRA Rule 9216 of FINRA’s Code of Procedure, Bay Crest Partners, LLC (“Bay Crest” 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 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 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 since August 31, 2007, and its registration remains in effect. The firm has 68 registered representatives across four branch offices. Its principal place of business is New York, NY.

RELEVANT DISCIPLINARY HISTORY

Bay Crest does not have any relevant disciplinary history with the Securities and Exchange Commission (“SEC”), any state securities regulators, FINRA, or any other self-regulatory organization.

OVERVIEW

The firm failed to properly qualify and register its Chief Compliance Officer (“CCO”) as a Securities Trader Principal, failed to implement reasonably designed market access controls, and failed to publish accurate information about its order routing practices. As a result, the firm violated NASD Rule 1022(a)(6), Rules 15c3-5 and 606, which the SEC promulgated under the Securities Exchange Act of 1934 (“Rule 15c3-5” and “Rule 606”), FINRA Rule 2010, and related supervisory requirements, during the period December 17, 2016 through June 1, 2018 (the “review period”).

FACTS AND VIOLATIVE CONDUCT

Bay Crest Failed to Qualify and Register One Associated Person as a Securities Trader Principal with FINRA

1. During the review period, NASD Rule 1022(a)(6)(A)¹ stated: “Each person associated with a member who is included within the definition of principal in [NASD] Rule 1021 and who will have supervisory responsibility over the securities trading activities described in [NASD] Rule 1032(f)(1) shall become qualified and registered as a Securities Trader Principal.² To qualify for registration as a Securities Trader Principal, such person shall become qualified and registered as a Securities Trader under [NASD] Rule 1032(f) and pass the General Securities Principal qualification examination.”
2. During the review period, the firm’s CCO, who was a firm principal by virtue of her position as an officer of the firm, had supervisory responsibility over the securities trading activities of the firm’s 11 Securities Traders, but was not qualified or registered as a Securities Trader Principal.³ Therefore, the firm violated NASD Rule 1022(a)(6) and FINRA Rule 2010.

Bay Crest’s Market Access Controls and Supervisory Procedures were Unreasonable

3. On November 3, 2010, the SEC adopted Rule 15c3-5 to reduce the risks faced by broker-dealers, as well as the markets and the financial system as a whole, as a result of various market access arrangements, by requiring financial and regulatory risk management controls reasonably designed to limit financial exposure and ensure compliance with applicable regulatory requirements to be implemented on a market-wide basis.
4. Rule 15c3-5(b) requires, in relevant part, that “[a] broker-dealer . . . that provides a customer or any other person with access to an exchange . . . through use of its market participant identifier or otherwise, shall establish, document, and maintain a system of risk management controls and supervisory procedures reasonably designed to manage the financial, regulatory, and other risks of this business activity.”

¹ On October 1, 2018, FINRA Rule 1220 replaced NASD Rule 1022.

² During the review period, NASD Rule 1021(b) defined “principal” to include officers of the firm, and NASD Rule 1032(f)(1) required that registered persons engaged in the following securities trading activities register as Securities Traders: “proprietary trading, the execution of transactions on an agency basis, or the direct supervision of such activities . . .” in equity, preferred, or convertible debt securities.

³ The CCO was properly qualified and registered with FINRA as a General Securities Principal, authorizing her to supervise the firm’s General Securities Representatives. The CCO’s responsibility with respect to supervising Securities Traders was limited to reviewing three reports of their trading activity. The CCO no longer conducts reviews of the securities trading activities of the firm’s Securities Traders.

5. Rule 15c3-5(c)(1) requires firms that provide market access to establish risk management controls and supervisory procedures that are “reasonably designed to systematically limit the financial exposure of the broker or dealer that could arise as a result of market access.”
6. Specifically, Rule 15c3-5(c)(1)(i) requires that such controls and procedures be reasonably designed to “prevent the entry of orders that exceed appropriate pre-set credit or capital thresholds in the aggregate for each customer . . . by rejecting orders if such orders would exceed the applicable credit or capital thresholds.”
7. Furthermore, the SEC’s Rule 15c3-5 Adopting Release stated that “a broker-dealer will be required to set appropriate credit thresholds for each customer for which it provides market access, including broker-dealer customers,” and that such thresholds will be “determin[ed] based on appropriate due diligence as to the customer’s business, financial condition, trading patterns, and other matters” and that the firm’s decision should be documented.⁴ The Adopting Release also stated that “the Commission expects that the broker-dealer will monitor on an ongoing basis whether the credit thresholds remain appropriate, and promptly make adjustments to them, and its controls and procedures, as warranted.”⁵
8. During the review period, the firm failed to establish risk management controls reasonably designed to prevent the entry of orders that exceeded appropriate pre-set credit thresholds in the aggregate for each customer by rejecting orders if such orders would exceed the applicable credit thresholds.
9. Specifically, the firm had written market access procedures during the review period that described certain due diligence steps supervisors should take to set appropriate customer credit thresholds, including by reviewing “the nature of the customer, the nature of the trading, the capital available to the customer and the customer’s trading history.” Despite the written procedures, the firm could not demonstrate that it performed reasonable due diligence in selecting customer credit thresholds or how the thresholds it selected for customers meaningfully limited the financial exposure generated by the customers’ trading activity. Nor could the firm establish that it monitored the continued appropriateness of those thresholds on an ongoing basis.
10. Instead of evaluating the relevant factors discussed in the Adopting Release, the firm relied solely on customers’ trading activity in selecting customer credit thresholds. The thresholds the firm implemented, however, were not reasonably related to customers’ actual trading activity. For example, for the six-month period from January through June 2017, one of the firm’s customers averaged \$122 million in daily notional trading activity, but the customer’s daily credit limit in one order management system (“OMS”) was \$1.705 billion (about 14 times more than the average activity). During the same

⁴ *Risk Management Controls for Brokers or Dealers with Market Access*, Exchange Act Release No. 63241, 75 Fed. Reg. 69792, 69802 (Nov. 15, 2010).

⁵ *Id.*

period, a second customer averaged \$115,561 in daily notional trading activity, but the customer's daily credit limit in the OMS was \$3 billion (about 25,960 times more than the average activity). These examples illustrate that the firm's customer credit thresholds in the OMS were set at levels not reasonably designed to prevent the entry of orders that exceeded appropriate pre-set credit thresholds in the aggregate for each customer.

11. In a second OMS that one customer was authorized to use, the firm did not implement any customer credit thresholds. Rather, this OMS prevented the entry of single orders greater than \$500 million in notional value. This control threshold was not based on any review conducted by the firm of the customer's business, financial condition, trading patterns, or other matters.
12. In addition, for one customer, the firm failed to aggregate the credit thresholds across the OMSs it utilized to provide the customer with market access. This failure allowed this customer to potentially exceed the OMS-specific thresholds the firm assigned to the customer.
13. Rule 15c3-5(c)(1)(ii) further requires controls and procedures reasonably designed to "[p]revent the entry of erroneous orders by rejecting orders that exceed appropriate price or size parameters, on an order-by-order basis or over a short period of time, or that indicate duplicative orders."
14. Furthermore, the SEC's Rule 15c3-5 Adopting Release stated with respect to preventing erroneous and duplicative orders, "the Commission believes broker-dealers should take into account the type of customer as well as the customer's trading patterns and order entry history in determining how to set such parameters."⁶ In addition, "a system-driven, pre-trade control designed to reject orders that are not reasonably related to the quoted price of the security would prevent erroneously entered orders from reaching the securities markets, which should lead to fewer broken trades and thereby enhance the integrity of trading on the securities markets."⁷
15. During the review period, the firm failed to establish risk management controls and supervisory procedures reasonably designed to prevent the entry of erroneous orders, by rejecting orders that exceeded appropriate price or size parameters, on an order-by-order basis or that indicated duplicative orders.
16. Specifically, the firm implemented order-by-order controls designed to prevent erroneous orders within one of the firm's OMSs. However, two of the four single-order thresholds were set at levels too high to be reasonably designed to prevent erroneous orders from being sent to the market. The firm's maximum quantity per order control and maximum notional value per order control, absent other reasonably designed controls, were not reasonably designed to prevent the entry of erroneous orders that exceeded appropriate price or size parameters on an order-by-order basis. In addition, the firm could not

⁶ 75 Fed. Reg. at 69801.

⁷ *Id.* at 69802.

demonstrate that the other two single-order thresholds in the OMS—its limit price control and average-daily volume thresholds—absent other reasonable controls, were set at levels reasonably designed to prevent the entry of erroneous orders that exceeded appropriate price or size parameters on an order-by-order basis.

17. In a second OMS that one customer was authorized to use, the only order-by-order control the firm applied to prevent the entry of erroneous orders was a maximum single-order notional value threshold of \$500 million. This threshold, without other meaningful erroneous order controls, was not reasonably designed to prevent the entry of erroneous orders that exceeded appropriate price or size parameters on an order-by-order basis.
18. The firm did not implement any controls in either of the two OMSs discussed herein designed to prevent the entry of duplicative orders.
19. The firm's failure to implement customer credit thresholds reasonably related to the business, financial condition, or trading patterns of its customers, implementation of unreasonably designed order-by-order erroneous order controls, and its failure to implement any controls to prevent the entry of duplicative orders violated Rule 15c3-5(b) and (c)(1) and FINRA Rule 2010.
20. As a result of the deficiencies described above, the firm also violated FINRA Rules 3110 and 2010.

Bay Crest Failed to Publish Accurate and Complete Reports Regarding its Routing of Customer Orders and Failed to Conduct Supervisory Reviews of the Reports

21. During the review period, Rule 606(a) required broker-dealers to “make publicly available for each calendar quarter a report on its routing of non-directed orders in NMS securities during that quarter.” Specifically, Rule 606(a)(1) required the following information be included on the reports:
 - (i) The percentage of total customer orders for the section that were non-directed orders, and the percentages of total non-directed orders for the section that were market orders, limit orders, and other orders;
 - (ii) The identity of the ten venues to which the largest number of total non-directed orders for the section were routed for execution and of any venue to which five percent or more of non-directed orders were routed for execution . . . and the percentage[] of . . . total non-directed other orders for the section that were routed to [each] venue; and
 - (iii) A discussion of the material aspects of the broker's or dealer's relationship with each venue identified pursuant to paragraph (a)(1)(ii) of this section, including a description of any arrangement for payment for order flow and any profit-sharing relationship.
22. Rule 606(b)(2) required: “A broker or dealer shall notify customers in writing at least annually of the availability on request of the [identity of the venue to which the customer's orders were routed for execution in the six months prior to the customer's

request, whether the orders were directed orders or non-directed orders, and the time of the transactions, if any, that resulted from such orders].”

23. For at least the second calendar quarter of 2017, the firm made publicly available a report on its routing of non-directed orders in covered securities during that quarter. But the report included incomplete information as to the percentage of non-directed customer market orders and limit orders that the firm *routed* for execution. Instead, for each section of the report, the firm listed the “percent of executed volume.” This information would not include customer orders that were routed but not executed.
24. In addition, the firm’s second quarter 2017 report did not list any information regarding the percentage of the total non-directed “other” orders for each section that the firm routed to each venue listed in the report.
25. The firm’s second quarter 2017 report also failed to disclose the “material aspects” of its relationship(s) with its significant execution venues regarding payment for order flow arrangements. The firm was required to describe the material terms of such arrangements, such as any amounts per share or per order that the firm receives.⁸ The firm received payment for order flow in the form of rebates from exchanges, which the firm was required to disclose on the firm’s quarterly 606 report, including the amounts per share or per order.
26. The firm also failed to notify its customers in writing at least annually of the availability of the firm’s order routing statistics.
27. The conduct described in paragraphs 23 through 26 violated Rule 606(a) and (b)(2) and FINRA Rule 2010.
28. During the review period, certain aspects of the firm’s written supervisory procedures with respect to Rule 606 were not reasonably designed to achieve compliance with the rule. Specifically, the written supervisory procedures did not include any steps that supervisors should take to review the accuracy of the information published on the firm’s Rule 606 reports. This conduct violated FINRA Rules 3110 and 2010.

⁸ The SEC’s Rule 606 Adopting Release stated that a description of the material aspects of a payment for order flow arrangement “does not require an estimate of the aggregate dollar amount of payment for order flow[.]” but “would include a description of the terms of the arrangement, such as any amounts per share or per order that the broker receives.” See *Disclosure of Order Execution and Routing Practice*, Exchange Act Release No. 43590, 65 Fed. Reg. 75414, 75427 (Dec. 1, 2000). Furthermore, the term “payment for order flow” is “broadly defined in Exchange Act Rule 10b-10(d)(9) . . . [to include] ‘any monetary payment, service, property, or other benefit that results in remuneration, compensation, or consideration’ to a broker-dealer in return for the routing of orders...” See SEC Division of Market Regulation, Staff Legal Bulletin No. 13A (Frequently Asked Questions About SEC Rule [Rule 606]), Q. 13 (Oct. 16, 2001). The “definition would include, for example . . . direct monetary payments for orders (such as a market maker’s payments for marketable orders and an ECN’s payments for non-marketable limit orders)... *Id.*

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

- A censure;
- a total fine of \$67,000⁹ (consisting of \$2,000 for the registration violation; \$35,000 for the Rule 15c3-5 and related supervisory violations; and \$20,000 for the Rule 606 and \$10,000 for the Rule 606 supervisory violations); and
- an undertaking to revise the firm's written supervisory procedures with respect to the areas described in paragraphs I.A.8 through 20 and paragraph I.A.28. Within 30 days after this AWC becomes final, a registered principal of the Respondent shall submit to the COMPLIANCE ASSISTANT, DEPARTMENT OF ENFORCEMENT, 15200 OMEGA DRIVE, SUITE 300, ROCKVILLE, MD 20850-3241, a signed, dated letter, or an e-mail from a work-related account of the registered principal to MarketRegulationComp@finra.org, acknowledging that the firm revised its written supervisory procedures, and the date the revised procedures were implemented.

Respondent agrees to pay the monetary sanctions upon notice that this AWC has been accepted and that such payments are due and payable. It 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 that it is unable to pay, now or at any time hereafter, the monetary sanctions 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 the firm;
- 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.

⁹ Related disciplinary actions on behalf of Cboe BZX Exchange, Inc. ("BZX"), Cboe EDGX Exchange, Inc. ("EDGX"), The NASDAQ Stock Market LLC ("Nasdaq"), the New York Stock Exchange LLC ("NYSE"), NYSE American LLC ("NYSE American") (collectively, the "SROs") for violations of each exchange's registration rules are being taken concurrently in conjunction with this matter. The NYSE disciplinary action also includes violations of Rule 15c3-5(c)(1)(i).

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 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 Respondent; 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 accordance with FINRA Rule 8313;
 - 3. FINRA may make a public announcement concerning this agreement and the subject matter thereof 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 the firm's: (i) testimonial obligations; or (ii) right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party.

- D. Respondent 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.

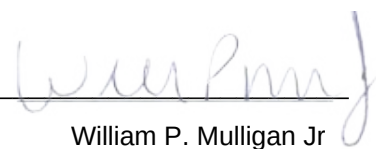
The undersigned, on behalf of the firm, certifies that a person duly authorized to act on its behalf has read and understands all of the provisions of this AWC and has been given a full opportunity to ask questions about it; that it has agreed to the AWC's provisions voluntarily; and that no offer, threat, inducement, or promise of any kind, other than the terms set forth herein and the prospect of avoiding the issuance of a Complaint, has been made to induce the firm to submit it.

March 17, 2020

Date

Respondent

Bay Crest Partners, LLC

By: 

Name: William P. Mulligan Jr

Title: CEO

Reviewed by:

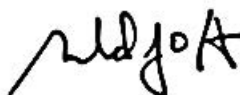
Madelyn Calabrese, Esq.
Haynes and Boone, LLP
Counsel for Respondent

Accepted by FINRA:

March 18, 2020

Date

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



Gerald J. O'Hara
Senior Counsel
FINRA Department of Enforcement