

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER, AND CONSENT
NO. 2021069316201**

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

RE: Interactive Brokers LLC (Respondent)
Member Firm
CRD No. 36418

Pursuant to FINRA Rule 9216, Respondent Interactive Brokers 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

Interactive Brokers LLC has been a FINRA member firm since January 1995. The firm, which is headquartered in Greenwich, Connecticut, offers online trading through self-directed accounts and clears transactions for retail and institutional customers, as well as for customers introduced to it by foreign and domestic introducing firms. Interactive Brokers LLC employs more than 350 registered representatives across seven branches.¹

OVERVIEW

Between June and December 2021, Interactive Brokers incorrectly calculated the number of excess shares of stocks listed on European exchanges it had available to return to customers from whom it had borrowed them as part of the firm's fully paid securities lending program. As a result, in more than 800 instances the firm returned borrowed shares when it should not have, which caused the firm to create or increase deficits for the relevant securities, in violation of Exchange Act § 15(c), Exchange Act Rule 15c3-3(b)(1), and FINRA Rule 2010. During the same period, in connection with this activity, Interactive Brokers failed to establish, maintain, and enforce a supervisory system, including written supervisory procedures (WSPs), reasonably designed to comply with

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

the firm's possession and control obligations under Exchange Act § 15 and Exchange Act Rule 15c3-3(b)(1). The firm therefore violated FINRA Rules 3110 and 2010.

Additionally, between January 2021 and December 2023, Interactive Brokers allowed an unregistered associated person to lead and oversee some software development efforts concerning the firm's securities finance business, including the firm's securities lending program. As securities lending is a covered function, that person was required to have been registered with FINRA as an Operations Professional. By allowing an unregistered person to act in a capacity requiring registration, the firm violated FINRA Rules 1210 and 2010.

FACTS AND VIOLATIVE CONDUCT

This matter originated from a cycle examination of Interactive Brokers.

A. The firm violated Exchange Act § 15(c) and Exchange Act Rule 15c3-3(b)(1) when it returned shares to customers and thereby created or increased segregation deficits.

Exchange Act Rule 15c3-3, also known as the Customer Protection Rule, is intended to protect customer assets from improper use by a broker-dealer, and to ensure the prompt return of customer securities in the event of broker-dealer insolvency. Exchange Act Rule 15c3-3(b)(1) requires a broker-dealer to promptly obtain and maintain physical possession or control of fully paid and excess margin securities carried for customer accounts. The number of customers' fully paid and excess margin securities required to be in a firm's possession or control is referred to as its "segregation requirement." If the number of shares in a firm's possession or control exceeds its segregation requirement, the firm has an "excess" of securities. If the number of shares in the firm's possession or control is less than its segregation requirement, the firm has a "deficit" of securities (also referred to as a "segregation deficit").

A violation of Exchange Act § 15(c) and Exchange Act Rule 15c3-3(b)(1) also is a violation of FINRA Rule 2010, which requires firms to observe "high standards of commercial honor and just and equitable principles of trade" in the conduct of their business.

Interactive Brokers engages in securities lending, including a fully paid lending program. In connection with that program, the firm utilizes an algorithm to identify securities for which the firm possesses an excess and are therefore available to be returned to customers from whom it borrowed shares.

Between June and December 2021, the firm updated this algorithm for shares traded on European exchanges in a way that resulted in the firm inadvertently creating or increasing its segregation deficits on multiple occasions. In June 2021, the firm began including anticipated loan return activity—*i.e.* shares the firm expected to have in its possession or control by a specific time—when determining whether and what positions the firm had available to return to customers from whom it had borrowed them. On more than 800

occasions, the firm relied on anticipated loan return activity in calculating the number of shares in its possession or control, but then failed to receive the expected shares. The firm then relied on those calculations to return certain shares to customers from whom it had borrowed them. The firm thereby created or increased existing deficits—the sums of which were approximately \$30 million during the relevant period. In these instances, the firm returned to customers fully paid shares that it had borrowed from them via the firm's fully paid securities lending program (and thus stopped paying those customers the applicable daily rate for borrowing those shares) even though the firm should have continued to borrow those shares to avoid creating or increasing a segregation deficit.

Following the identification of the algorithm-related issue described above, the firm updated the algorithm to correctly account for anticipated loan return activity not settling and made restitution to affected customers.

As a result of the firm creating or increasing its segregation deficits, Interactive Brokers violated Exchange Act § 15(c), Exchange Act Rule 15c3-3(b)(1), and FINRA Rule 2010.

B. Interactive Brokers failed to establish and maintain a supervisory system, including written supervisory procedures, reasonably designed to comply with its possession and control obligations.

FINRA Rule 3110 requires a member firm to establish, maintain, and enforce a system, including WSPs, 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 also is a violation of FINRA Rule 2010.

Between June and December 2021, Interactive Brokers' WSPs failed to address how the firm should identify or resolve deficits caused by early returns. Interactive Brokers also did not have a system to detect issues that might cause early returns or deficits as a result of its stock lending program.

Moreover, as described below, the firm did not have a registered principal or Operations Professional directly supervise the creation, launch, or testing of the algorithm the firm relied on to identify securities available to be returned.

Beginning in December 2021, following the discovery of the failures with respect to the securities lending algorithm, the firm updated its processes and ensured that properly registered persons oversaw the software development for the securities lending program.

As a result of its failure to establish and maintain a supervisory system, including written supervisory procedures, reasonably designed to comply with its possession and control obligations in connection with the failure to receive anticipated loan returns, Interactive Brokers violated FINRA Rules 3110 and 2010.

C. Interactive Brokers allowed an unregistered person to oversee changes made to the securities lending algorithm in violation of FINRA Rule 1210.

FINRA Rule 1210 requires that “[e]ach person engaged in the investment banking or securities business of a member shall be registered with FINRA as a representative or principal in each category of registration appropriate to his or her functions and responsibilities as specified in Rule 1220. . . .” FINRA Rule 1220(b)(3) defines, as one category of registration, an “Operations Professional” being “any person designated by senior management...as a supervisor, manager or other person responsible for approving or authorizing work, including work of other persons, in direct furtherance of each of the covered functions specified in paragraph (b)(3)(A)(ii) of this Rule.” Pursuant to paragraph (b)(3)(A)(ii), covered functions include “receipt and delivery of securities and funds,” “settlement, fail control, buy ins, segregation, possession and control,” “stock loan or securities lending,” and “defining and approving business requirements for sales and trading systems and any other systems related to the covered functions, and validation that these systems meet such business requirements.” A violation of FINRA Rule 1210 also is a violation of FINRA Rule 2010.

Between January 2021 and December 2023, Interactive Brokers allowed an unregistered person to lead and oversee some software development efforts concerning the firm’s securities finance business, including some of the firm’s securities lending program. That unregistered person supervised a team of approximately 20 unregistered individuals, including eight direct reports. The unregistered person had the authority to, in certain circumstances, devise and approve software development projects that modified the code and functioning of the applications used by the firm’s securities finance business without any direct involvement by any registered person.

In particular, the unregistered person devised and—along with other unregistered persons employed by Interactive Brokers—made and approved updates to the securities lending algorithm that went into effect in June 2021. The unregistered person reviewed the changes to the securities lending program algorithm and directed that the changes to the securities lending algorithm be put into effect, which caused the firm to create or increase its segregation deficit in affected securities. Thus, the unregistered person should have been registered with FINRA as an Operations Professional.

In January 2024, Interactive Brokers placed properly registered persons in charge of the supervision of the firm’s software development efforts related to its securities lending program.

As a result of allowing an unregistered person to perform covered functions, Interactive Brokers violated FINRA Rules 1210 and 2010.

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

- a censure, and
- a \$475,000 fine.

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
- 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.

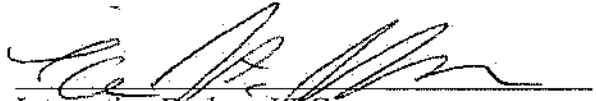
OTHER MATTERS

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.

10/18/24
Date


Interactive Brokers LLC
Respondent

Print Name: Elaine H. Mandelbaum

Title: General Counsel

Accepted by FINRA:

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

10/22/24
Date


Myla G. Arumugam
Principal Counsel
FINRA
Department of Enforcement
581 Main St., 7th Floor
Woodbridge, NJ 07095