

UNITED STATES OF AMERICA  
Before the  
COMMODITY FUTURES TRADING COMMISSION

\_\_\_\_\_)  
In the Matter of: )  
 )  
Merrill Lynch, Pierce, Fenner & Smith ) CFTC Docket No. 19-21  
Incorporated, )  
 )  
Respondent. )  
\_\_\_\_\_)



**ORDER INSTITUTING PROCEEDINGS PURSUANT TO  
SECTION 6(C) AND (D) OF THE COMMODITY EXCHANGE ACT, MAKING  
FINDINGS, AND IMPOSING REMEDIAL SANCTIONS**

**I. INTRODUCTION**

The Commodity Futures Trading Commission (“Commission”) has reason to believe that from in or about March 2015 to at least January 2018 (“Relevant Period”), Merrill Lynch, Pierce, Fenner & Smith Incorporated (“Respondent”) violated Section 4g of the Commodity Exchange Act (“Act”), 7 U.S.C. § 4g (2012), and regulations 1.31, 1.35, and 166.3, 17 C.F.R. §§ 1.31, 1.35, and 166.3 (2018) of the Commission Regulations (“Regulations”) promulgated thereunder. Therefore, the Commission deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted to determine whether Respondent engaged in the violations set forth herein and to determine whether any order should be issued imposing remedial sanctions.

In anticipation of the institution of an administrative proceeding, Respondent has submitted an Offer of Settlement (“Offer”), which the Commission has determined to accept. Without admitting or denying any of the findings or conclusions herein, Respondent consents to the entry of this Order Instituting Proceedings Pursuant to Section 6(c) and (d) of the Commodity Exchange Act, Making Findings, and Imposing Remedial Sanctions (“Order”) and acknowledges service of this Order.<sup>1</sup>

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<sup>1</sup> Respondent consents to the use of the findings of fact and conclusions of law in this Order in this proceeding and in any other proceeding brought by the Commission or to which the Commission is a party or claimant, and agrees that they shall be taken as true and correct and be given preclusive effect therein, without further proof. Respondent does not consent, however, to the use of this Order, or the findings or conclusions herein, as the sole basis for any other proceeding brought by the Commission or to which the Commission is a party or claimant, other than: a proceeding in bankruptcy or receivership; or a proceeding to enforce the terms of this Order. Respondent does not consent to the use of the Offer or this Order, or the findings or conclusions in this Order, by any other party in any other proceeding.

## II. FINDINGS

The Commission finds the following:

### A. SUMMARY

For nearly three years, Respondent, a registered futures commission merchant (“FCM”), failed to promptly produce reliable audit trail data requested by the Division of Enforcement (“Division”). These failures substantially delayed a Division investigation and were due in large part to Respondent’s failure to develop and diligently administer adequate procedures for responding to routine regulatory requests.

### B. RESPONDENT

Merrill Lynch, Pierce, Fenner & Smith Incorporated is a subsidiary of BAC North America Holding Company and is headquartered in New York, New York. Respondent is the executing broker for a third-party firm that was the subject of a Division investigation. Respondent is registered with the Commission as an FCM.

### C. FACTS

The Division requested audit trail data, among other records, as part of an ongoing investigation on three separate dates in 2015. Respondent maintained the audit trail data in its capacity as an executing broker for a third-party firm. Respondent was required to maintain and produce this audit trail data pursuant to Section 4g of the Act, 7 U.S.C. § 6g (2012), and Regulations 1.31 and 1.35, 17 C.F.R. §§ 1.31 and 1.35 (2018).

The productions made in response to the requests for audit trail data were both significantly delayed and flawed. Namely, even after the Division agreed to limit the scope of the requests, Respondent did not produce any audit trail data until January 2017—more than eighteen months after the initial requests. Moreover, this production was incomplete and required a supplemental production in February 2017. Thereafter, the Division identified numerous issues with the audit trail data produced, which included unpopulated fields. After numerous discussions and reproduction of data to correct the issues, the Division was led to believe that the production of audit trail data was complete.

Then in December 2017—more than two-and-a-half years after the initial document requests were made—Respondent identified a significant gap in the audit trail data that had been produced. Respondent ultimately located and produced the missing audit trail data in January 2018. This substantially delayed the Division’s investigation.

The Division subsequently learned that Respondent failed to develop and diligently administer adequate procedures to properly respond to the Division’s requests for required audit trail data, and otherwise lacked an adequate supervisory system to ensure the required records were properly kept and promptly produced. For example, Respondent did not have a process in place to locate account numbers or order entry operator identification numbers; instead, operations personnel simply worked from memory when searching for the data.

### III. LEGAL DISCUSSION

#### A. Failure to Promptly Produce Reliable Records

As an FCM, Respondent is required to comply with the obligations set forth in Section 4g of the Act, 7 U.S.C. § 6g (2012), and Regulations 1.31 and 1.35, 17 C.F.R. §§ 1.31 and 1.35 (2018). Section 4g of the Act requires FCMs, among other registrants, to “keep books and records pertaining to transactions and positions of their customers and commodities for future delivery, and shall make such records available for inspection by the Commission.” 7 U.S.C. § 6g(a).

Before August 28, 2017, Regulation 1.31 stated that persons required to maintain books and records under the Act or Regulations shall produce such records “promptly” to a Commission representative upon request. 17 C.F.R. § 1.31(a)(2) (2017); *see also In re IKON Glob. Mkts., Inc.*, CFTC No. 17-23, 2017 WL 3868976, at \*2 (Aug. 31, 2017) (consent order finding violations of Regulation 1.31 when FCM failed to produce documents over a two-year period); *In re Barclays Bank PLC*, CFTC No. 16-30, 2016 WL 5582339, at \*2 (Sept. 22, 2016) (consent order finding violations of Regulation 1.31 when FCM failed to produce trade confirmation for fourteen months).

On August 28, 2017, Regulation 1.31 was amended to read: “a records entity must produce such regulatory records in the form and medium requested promptly, upon request, unless otherwise directed by the Commission representative.” 17 C.F.R. § 1.31(d)(3)(ii) (2018). Revised Regulation 1.31 also states that if records are maintained electronically, registrants must “establish appropriate systems and controls that ensure the authenticity and reliability of electronic regulatory records” and “ensure the records entity is able to produce electronic regulatory records in accordance with the Regulations.” 17 C.F.R. § 1.31(c)(2) (2018).

Regulations 1.35 further elaborates that FCMs, among other registrants, must:

[k]eep full, complete, and systematic records . . . of all transactions relating to its business of dealing commodity interests . . . which shall include all orders (filled, unfilled, or canceled), trading cards, . . . journals, ledgers, . . . copies of confirmations . . . and all other records, which have been prepared in the course of its business of dealing in commodity interests . . . .

17 C.F.R. § 1.35(a)(1)(i) (2018). These records include audit trail data. *See In re ABN AMRO Clearing Chicago LLC*, CFTC No. 18-31, 2018 WL 4502261, at \*4 (Sept. 14, 2018) (consent order finding violation of Section 4g of the Act and Regulations 1.31 and 1.35 for failures regarding audit trail data); *In re E\*Trade Sec. LLC*, CFTC No. 17-07, 2017 WL 413517, at \*4 (Jan. 26, 2017) (same).

The facts set forth above demonstrate that Respondent failed to promptly produce reliable audit trail data to the Division during the Relevant Period. The Commission considers the particular facts and circumstances of each case when assessing potential violations resulting from production delays. The facts and circumstances here, where for nearly three years Respondent failed to produce reliable required records to the Division, are sufficient for the Commission to

determine that a violation occurred. These failures substantially delayed the Division's investigation, and thus illustrate the importance of complying with the production requirements of the Act and Regulations. On these facts, Respondent violated Section 4g of the Act and Regulations 1.31 and 1.35.

**B. Supervision Failures**

Respondent violated Regulation 166.3 because it failed to develop and diligently administer adequate procedures to ensure compliance with the production requirements of Section 4g of the Act and Regulations 1.31 and 1.35.

Regulation 166.3 requires each registered FCM to “diligently supervise the handling by its partners, officers, employees, and agents . . . of all commodity interests carried, operated, advised or introduced by the registrant and other activities . . . relating to its business as a Commission registrant.” 17 C.F.R. § 166.3 (2018). “A violation of Regulation 166.3 is demonstrated by showing that either: (1) the registrant’s supervisory system was generally inadequate; or (2) the registrant failed to perform its supervisory duties diligently.” *See ABN AMRO Clearing Chicago*, 2018 WL 4502261 at \*4 (collecting cases).

Under Section 4g of the Act and Regulations 1.31 and 1.35, FCMs have an obligation to keep and promptly produce required records, including audit trail data. During the Relevant Period, Respondent lacked an adequate system to properly respond to the Division’s requests for required audit trail data, and otherwise failed to adequately supervise its employees and agents to ensure the required records were properly kept and promptly produced. As a result of this failure, Respondent did not promptly produce reliable data to the Division, and thus failed to meet its production responsibilities under the Act and Regulations. Accordingly, Respondent violated Regulation 166.3.

**IV. FINDINGS OF VIOLATIONS**

Based on the foregoing, the Commission finds that, during the Relevant Period, Respondent violated Section 4g of the Act, 7 U.S.C. § 6g (2012), and Regulations 1.31, 1.35, and 166.3, 17 C.F.R. §§ 1.31, 1.35, and 166.3 (2018).

**V. OFFER OF SETTLEMENT**

Respondent has submitted the Offer in which it, without admitting or denying the findings and conclusions herein:

- A. Acknowledges service of this Order;
- B. Admits the jurisdiction of the Commission with respect to all matters set forth in this Order and for any action or proceeding brought or authorized by the Commission based on violation of or enforcement of this Order;
- C. Waives:
  - 1. The filing and service of a complaint and notice of hearing;

2. A hearing;
  3. All post-hearing procedures;
  4. Judicial review by any court;
  5. Any and all objections to the participation by any member of the Commission's staff in the Commission's consideration of the Offer;
  6. Any and all claims that it may possess under the Equal Access to Justice Act, 5 U.S.C. § 504 (2012), and 28 U.S.C. § 2412 (2012), and/or the rules promulgated by the Commission in conformity therewith, Part 148 of the Regulations, 17 C.F.R. pt. 148 (2018), relating to, or arising from, this proceeding;
  7. Any and all claims that it may possess under the Small Business Regulatory Enforcement Fairness Act of 1996, Pub. L. No. 104-121, tit. II, §§ 201–253, 110 Stat. 847, 857–74 (codified as amended at 28 U.S.C. § 2412 and in scattered sections of 5 U.S.C. and 15 U.S.C.), relating to, or arising from, this proceeding; and
  8. Any claims of Double Jeopardy based on the institution of this proceeding or the entry in this proceeding of any order imposing a civil monetary penalty or any other relief, including this Order;
- D. Stipulates that the record basis on which this Order is entered shall consist solely of the findings contained in this Order to which Respondent has consented in the Offer; and
- E. Consents, solely on the basis of the Offer, to the Commission's entry of this Order that:
1. Makes findings by the Commission that Respondent violated Section 4g of the Act, 7 U.S.C. § 6g, and Regulations 1.31, 1.35, and 166.3, 17 C.F.R. §§ 1.31, 1.35, and 166.3 (2018);
  2. Orders Respondent to cease and desist from violating Section 4g of the Act and Regulations 1.31, 1.35, and 166.3;
  3. Orders Respondent to pay a civil monetary penalty in the amount of three-hundred thousand dollars (\$300,000), plus, if applicable, post-judgment interest; and
  4. Orders Respondent and its successors and assigns to comply with the conditions and undertakings consented to in the Offer and as set forth in Part VI of this Order.
- F. Represents that it has already taken the following steps to revise its internal process for responding to regulatory data requests, including, but not limited to designating personnel to:

1. Interpret regulatory data requests, the source of the information, and the timing for the response;
2. Locate and provide the data; and
3. Independently assess the data extraction process and results.

Upon consideration, the Commission has determined to accept the Offer.

## VI. ORDER

### Accordingly, IT IS HEREBY ORDERED THAT:

- A. Respondent shall cease and desist from violating Section 4g of the Act, 7 U.S.C. § 6g, and Regulations 1.31, 1.35, and 166.3, 17 C.F.R. §§ 1.31, 1.35, and 166.3 (2018).
- B. Respondent shall pay a civil monetary penalty in the amount of three-hundred thousand dollars (\$300,000) (“CMP Obligation”) within ten (10) days of the date of entry of this Order. If the CMP Obligation is not paid in full within ten (10) days of the date of entry of this Order, then post-judgment interest shall accrue on the CMP Obligation beginning on the date of entry of this Order and shall be determined by using the Treasury Bill rate prevailing on the date of entry of this Order pursuant to 28 U.S.C. § 1961 (2012).

Respondent shall pay the CMP Obligation and any post-judgment interest by electronic funds transfer, U.S. postal money order, certified check, bank cashier’s check, or bank money order. If payment is to be made other than by electronic funds transfer, then the payment shall be made payable to the Commodity Futures Trading Commission and sent to the address below:

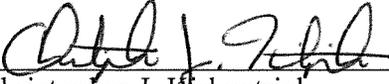
MMAC/ESC/AMK326  
Commodity Futures Trading Commission  
Division of Enforcement  
6500 S. MacArthur Blvd.  
HQ Room 181  
Oklahoma City, OK 73169  
(405) 954-6569 office  
(405) 954-1620 fax  
9-AMC-AR-CFTC@faa.gov

If payment is to be made by electronic funds transfer, Respondent shall contact Marie Thorne or her successor at the above address to receive payment instructions and shall fully comply with those instructions. Respondent shall accompany payment of the CMP Obligation with a cover letter that identifies the paying Respondent and the name and docket number of this proceeding. The paying Respondent shall simultaneously transmit copies of the cover letter and the form of payment to the Chief Financial Officer, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW, Washington, D.C. 20581.

- C. Respondent its successors and assigns shall comply with the following conditions and undertakings set forth in the Offer:
1. Public Statements: Respondent agrees that neither it nor any of its successors and assigns, agents or employees under its authority or control shall take any action or make any public statement denying, directly or indirectly, any findings or conclusions in this Order or creating, or tending to create, the impression that this Order is without a factual basis; provided, however, that nothing in this provision shall affect Respondent's: (i) testimonial obligations; or (ii) right to take legal positions in other proceedings to which the Commission is not a party. Respondent and its successors and assigns shall comply with this agreement, and shall undertake all steps necessary to ensure that all of its agents and/or employees under its authority or control understand and comply with this agreement.
  2. Cooperation, in General: Respondent shall cooperate fully and expeditiously with the Commission, including the Commission's Division of Enforcement, in this action, and in any current or future Commission investigation or action related thereto. Respondent shall also cooperate in any investigation, civil litigation, or administrative matter related to, or arising from, this action.
  3. Partial Satisfaction: Respondent understands and agrees that any acceptance by the Commission or the Monitor of any partial payment of Respondent's Restitution Obligation, Disgorgement Obligation, or CMP Obligation shall not be deemed a waiver of its obligation to make further payments pursuant to this Order, or a waiver of the Commission's right to seek to compel payment of any remaining balance.
  4. Change of Address/Phone: Until such time as Respondent satisfies in full its CMP Obligation as set forth in this Order, Respondent shall provide written notice to the Commission by certified mail of any change to its telephone number and mailing address within ten calendar days of the change.

The provisions of this Order shall be effective as of this date.

By the Commission.

  
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Christopher J. Kirkpatrick  
Secretary of the Commission  
Commodity Futures Trading Commission

Dated: September 10, 2019