



**Disciplinary Panel  
NYSE Alternext US LLC<sup>1</sup>**

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IN THE MATTER

of

BKI ASSOCIATES

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:  
: Case No. 07-31 and 07-107  
: [AMXC08030]

:  
: Hearing Officer – DMF

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: **DECISION**

:  
: October 24, 2008  
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Pursuant to Rule 478T, Temporary Procedures Governing Legacy Disciplinary Proceedings, this proceeding came before the Hearing Officer for review of the attached Stipulation and Consent to Penalty (Stipulation), which was entered into by the Parties for the purposes of settling this proceeding and concluding all disciplinary actions by NYSE Alternext US LLC against Respondent based upon or arising out of the facts set forth in the Stipulation. Respondent, without admitting or denying the facts, allegations and conclusions contained in the Stipulation, consented to the entry of findings of violations of the Exchange Constitution, Exchange rules, the Securities Exchange Act of 1934, rules promulgated by the Securities and Exchange Commission pursuant to the Exchange Act (SEC rules), and Regulation X promulgated by the Federal Reserve Board, and the imposition of penalties for such violations, as set forth in the Stipulation.

After considering the stipulated facts, as well as the analysis and authorities set forth in the Memorandum in Support of Proposed Settlement, the Hearing Officer hereby accepts the Stipulation, and accordingly finds that Respondent:

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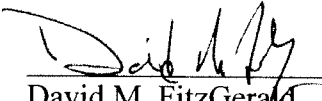
<sup>1</sup> Effective October 1, 2008 the corporate successor to the American Stock Exchange is NYSE Alternext US, LLC.

1. Violated Exchange Rule 958-ANTE(g) by placing options trades in its market making account notwithstanding the fact that it did not initiate any of these trades through the facilities of the Exchange;
2. Violated SEC Rule 11a-1 by effecting options transactions while on the floor of the Exchange for its own account while not acting in the capacity of an options market maker;
3. Violated Regulation X and Article V, Section 4(h) of the Exchange Constitution in that it knew, or should have known, that inappropriately placing options trades in its market making account held at its clearing firm would cause the clearing firm to improperly extend good faith market making margin treatment in contravention of Federal Reserve Board Regulation T;
4. Violated SEC Rules 15c3-1, 17a-3(a)(11), and 17a-5 and Exchange Rule 470 by filing inaccurate net capital computations on its December 31, 2003 and December 31, 2005 FOCUS Reports;
5. Violated SEC Rule 17a-5 and Exchange Rule 443 by failing to file a required Annual Audit Report for the calendar year 2005; and
6. Violated Exchange Rule 320 by failing to establish and maintain appropriate policies, systems and procedures of supervision and control, including written supervisory procedures, with respect to its Annual Audit Report filing and subordinated loan requirements, and by

failing to properly implement its procedures with respect to filing accurate FOCUS Reports.

In accordance with the Stipulation, for these violations, Respondent is censured and fined \$15,000.

**SO ORDERED.**

  
David M. FitzGerald  
Hearing Officer

Copies to: BKI Associates (*via overnight courier and first class mail*)  
Brian F. Sklar, Esq. (*via electronic and first class mail*)  
Jocelyn Thrower (*via electronic and overnight courier*)  
Mary Yeager (*via electronic and overnight courier*)

# **EXHIBIT A**

Disciplinary Panel  
American Stock Exchange LLC

IN THE MATTER  
OF  
BKI ASSOCIATES

STIPULATION OF FACTS  
AND  
CONSENT TO PENALTY  
Case No. 07-31 and 07-107

This proceeding was instituted by the American Stock Exchange LLC (the “Exchange” or “Amex”) against BKI Associates (“BKI” or “the Firm”) (CRD# 32367), a Regular Member Organization of the Exchange. This Stipulation of Facts and Consent to Penalty (“Stipulation”) is entered into with BKI pursuant to Article V, Section 2 of the Exchange Constitution for the sole purpose of settling this disciplinary proceeding, without adjudication of any issues of law or fact, and without admitting or denying the facts, allegations and conclusions contained in this Stipulation, hereby consents to the entry of findings of violations of the Exchange Constitution and Rules, and the Federal securities laws, and the imposition of penalties hereinafter provided. BKI understands that a hearing officer, without conducting a formal hearing, will determine whether BKI has committed the violations set forth herein and may fix and impose the agreed upon penalty or reject the Stipulation. This Stipulation can also be the subject of review by the Amex Adjudicatory Council (“AAC”). BKI understands and acknowledges that the hearing officer’s acceptance of this Stipulation may not be appealed by the parties, will become part of its disciplinary records, and may be considered in any future proceeding brought by the Exchange.

## STIPULATED FACTS

- 1.0 During all relevant periods herein, BKI was a Regular Member organization of the Exchange acting as a registered options trading firm and was responsible for engaging in options market making activities on the Floor of the Exchange. BKI's principal place of business was located in Great Neck, New York.
- 1.1 As of June 2004, FINRA (f/k/a NASD) Market Regulation - Amex Division (the "Division") was an authorized representative of the Exchange.

## BACKGROUND

- 2.0 The violations in this Stipulation stem from two investigations conducted by the Division. One of the investigations was initiated by the Trading Analysis Department and involved the Firm's compliance with its market making obligations at the Exchange; the other was initiated by the Financial Regulation Department and involved the Firm's compliance with financial books and records and reporting requirements.

### *BKI's Compliance with Market Making Obligations*

- 3.1 During all relevant periods herein, Rule 11a-1 under the Securities Exchange Act of 1934 (the "Exchange Act") provided in relevant part that no member of a national securities exchange, while on the floor of such exchange, shall effect any transaction in any security admitted to trading on such exchange for its own account, but provided an exemption for transactions by a registered specialist in a security in which he is so registered on such exchange.
- 3.2 During all relevant periods herein, Exchange Rule 958-ANTE, Commentary .01(a) provided in relevant part that "[a] registered options trader electing to engage in Exchange options transactions is designated as a Specialist on the Exchange for all purposes under the Securities Exchange Act of 1934 and the rules and regulations thereunder with respect to options transactions (i) initiated and effected by him on the

Floor and through the facilities of the Exchange in his capacity as a registered options trader...” Paragraph (g) of Exchange Rule 958-ANTE also required in relevant part that registered options traders, when entering into an option transaction for any account in which they have an interest, to initiate such transactions on the Floor and through the facilities of the Exchange for those transactions to be considered registered options trader transactions.

3.3 During all relevant periods herein, the Amex operated a hybrid options trading platform known as the Amex New Trading Environment (“ANTE”), which enabled registered options traders and other Amex members, pursuant to applicable rules, to enter electronic and open outcry quotations and orders as well as to effect electronic and open outcry transactions.

3.4 During all relevant periods herein, BKI was registered with the Exchange as a registered options trader, subject to the requirements of Exchange Rule 958-ANTE. As a result thereof, BKI received a market maker ID from Options Clearing Corporation.

3.5 During all relevant periods herein, Part 224 of the Federal Reserve Board Rules (“Regulation X”) required that credit obtained within or outside the United States comply with the limitations of the Federal Reserve Board’s Margin Regulations T and U (12 CFR Parts 220, and 221, respectively), and that any borrower who obtained purpose credit within the United States, unless the borrower willfully caused the credit to be extended in contravention of Regulations T or U, was exempt from the Federal Reserve Board’s margin regulations.<sup>1</sup>

3.6 During all relevant periods herein, Article V, Section 4(h) of the Exchange Constitution provided, in pertinent part, that a member organization which shall be adjudged guilty in

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<sup>1</sup> Part 220.2 of the Federal Reserve Board Rules (“Regulation T”) states: “Good faith with respect to: (1) Margin means the amount which a creditor would require in exercising sound credit judgment; (2) Making a determination or accepting a statement concerning a borrower means that the creditor is alert to the circumstances surrounding the credit, and if in possession of information that would cause a prudent person not to make the determination or accept the notice or certification without inquiry, investigates and is satisfied that it is correct.”

a proceeding of conduct or proceeding inconsistent with just and equitable principles of trade, may be suspended or expelled from membership unless the offense is the violation of a provision, rule or resolution for which a different penalty has been provided, in which case such other penalty may be imposed.

#### Violations

- 4.0 The Trading Analysis Department (“TA”) of the Division opened an investigation into BKI’s options trading activity during the period of July 1, 2005 through June 30, 2006 (the “relevant period”) after BKI and its principal advised Exchange staff that BKI did not have ANTE options class assignments and did not utilize the ANTE platform to conduct options transactions.
- 4.1 During all relevant periods herein, BKI maintained two proprietary accounts at its clearing firm, ABC.<sup>2</sup> One account was an options market making account which was intended for transactions effected by BKI as an Exchange registered options trader in accordance with the Exchange and SEC rules applicable to such transactions, including without limitation that such transactions be initiated and effected by him on the Floor and through the facilities of the Exchange in his capacity as a registered options trader. In agreeing to maintain such options market maker account for BKI, ABC relied on BKI’s status as an Exchange registered options trader as well as BKI’s active OCC market maker ID. The other account was an off-floor trading account which was intended for dealer transactions effected by BKI other than as an Exchange registered options trader. ABC provided good faith margin treatment for trades placed by BKI in the options market maker account.
- 4.2 During all relevant periods herein, BKI effected a total of 1,051 options trades. BKI placed all of the 1,051 options trades in its options market maker account, thereby

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<sup>2</sup> A generic identifier is used throughout the Stipulation to make reference to BKI’s clearing firm.

representing that each such trade was a registered options market maker transaction entitled to good faith margin treatment.

4.3 BKI did not initiate and/or effect any of the 1,051 options trades through the facilities of the Exchange. Instead, BKI, using a proprietary trading system operated by ABC, directed all of the trades to options exchanges other than the Amex. ABC's trading system did not constitute a facility of the Amex.

4.4 Amex registered options traders may classify transactions in specific assigned securities effected through a proprietary trading system such as ABC's as registered options trader transactions provided they meet all of their Exchange market maker requirements in those specific assigned securities, as provided in Exchange Rule 958-ANTE. However, none of the options trades described in paragraphs 4.2 and 4.3 above met the requirements to be considered registered options trader transactions since such transactions were not effected through the facilities of the Exchange, and did not otherwise meet the requirements of Exchange Rule 958-ANTE.

4.5 As a result thereof, BKI caused ABC to inappropriately extend good faith margin treatment to such options transactions in contravention of Regulation T, which BKI knew, or should have known, was improper.

#### *BKI's Financial Books and Records Violations*

5.0 At all relevant times herein, SEC Rule 15c3-1 and Exchange Rule 470 required brokers or dealers to compute their net capital pursuant to the requirements as prescribed in SEC Rule 15c3-1.<sup>3</sup>

5.1 During all relevant times herein, Rule 17a-3(a)(11) under the Exchange Act ("SEC Rule 17a-3"), in part, required broker-dealers to make and keep current a record of the computation of net capital, pursuant to Rule 15c3-1.

<sup>3</sup> BKI, as a broker-dealer, was subject to SEC Rule 15c3-1 and required to maintain a minimum net capital requirement of \$100,000.

- 5.2 During all relevant periods herein, Rule 17a-5 under the Exchange Act (“SEC Rule 17a-5”), in part, required members of a national securities exchange to file Part IIA of Form X-17A-5 (“FOCUS Report”) with said exchange in accordance with the requirements described in SEC Rule 17a-5. The FOCUS Report requires that broker-dealers include a computation of net capital under SEC Rule 15c3-1.
- 5.3 During all relevant periods herein, SEC Rule 17a-5, in part, required certain specified registered brokers or dealers to file annually with the Securities and Exchange Commission (“SEC”) and the principal office of the designated examining authority for the broker or dealer, a report audited by an independent public accountant that is prepared in accordance with the requirements specified in SEC Rule 17a-5, and to file the Annual Audit Report not more than 60 days after the date of the financial statements.
- 5.4 During all relevant periods herein, Exchange Rule 443 required member organizations to file an annual audit of its financial statements (“Annual Audit Report”) prepared by an independent public accountant in accordance with the requirements of the Exchange Act and the rules thereunder. Broker-dealers that operate primarily as an on-floor specialist, market maker or a floor broker and execute 75% or more of their transactions directly relating to their primary business on the floor of the Exchange are exempt by the Exchange from the requirement to file an Annual Audit Report.
- 5.5 During all relevant periods herein, Exchange Rule 320 required member organizations to develop, maintain and implement a supervisory system, including written supervisory procedures (“WSPs”), reasonably designed to ensure compliance with respect to applicable securities rules and regulations.

#### Violations

- 6.0 On or about March 28, 2006, the Financial Regulation Department (“FRD”) of the Division commenced a routine examination of BKI’s financial books and records, covering the period of October 1, 2005 through December 31, 2005.

- 6.1 At the conclusion of FRD's review, FRD determined that several of the deficiencies identified were similar to deficiencies previously uncovered by FRD in connection with FRD's prior routine examination of the Firm's financial books and records covering the period of October 1, 2003 through December 31, 2003. FRD notified the Firm of these deficiencies in a deficiency letter to the Firm dated April 30, 2004 (the "April 2004 deficiency letter").
- 6.2 FRD determined that BKI filed an inaccurate FOCUS Report as of December 31, 2005, in that it included an inaccurate net capital computation. Specifically, BKI:
- (1) took an unnecessary haircut of \$1,620 for undue concentration for a security position on its net capital computation, even though the security's market value (\$10,800) did not exceed 10% of BKI's tentative net capital (\$19,856);
  - (2) failed to include the accurate book (cost) value and market value for its Exchange membership seat; and
  - (3) failed to properly classify \$484,068 under the securities owned at market value section of the FOCUS Report.
- 6.3 The deficiencies noted in paragraph 6.2 were similar to the deficiencies that the Firm was previously advised of in the April 2004 deficiency letter.
- 6.4 On or about November 1, 2005, FRD requested that BKI complete a Survey of Annual Audit Filings ("Survey").
- 6.5 On or about December 1, 2005, BKI returned a completed Survey indicating that it claimed an exemption from the requirement to file an Annual Audit Report for the calendar year 2005, because it operates primarily as a market maker and executes 75% or more of its transactions directly relating to its primary business on the floor of the Exchange.
- 6.6 As noted in paragraphs 4.2 through 4.4, however, none of BKI's options trades during the period of July 1, 2005 through December 31, 2005 were initiated and/or effected through

the facilities of the Exchange, and they did not otherwise meet the requirements of Exchange Rule 958-ANTE. Thus, BKI was not entitled to an exemption from the requirement to file an Annual Audit Report.

6.7 BKI failed to file an Annual Audit Report for the calendar year 2005 with the SEC or the Exchange.

6.8 FRD's review of BKI's WSPs revealed that the Firm did not have procedures to address regulatory requirements with respect to Annual Audit Report filings, and subordinated loans. Furthermore, although BKI's WSPs addressed FOCUS Report filing responsibilities, the deficiencies noted in the Firm's December 31, 2005 FOCUS Report were similar to the deficiencies that the Firm was previously advised of in the April 2004 deficiency letter.

#### CONCLUSION:

By reason of the foregoing Stipulated Facts, a Hearing Officer may conclude that:

7.0 BKI violated Exchange Rule 958-ANTE(g) by placing options trades in its market making account notwithstanding the fact that it did not initiate any of these trades through the facilities of the Exchange, as set forth in paragraphs 4.1 through 4.5.

7.1 BKI violated Rule 11a-1 of the Exchange Act by effecting options transactions while on the floor of the Exchange for its own account while not acting in the capacity of an options market maker, as set forth in paragraphs 4.1 through 4.5.

7.2 BKI violated Regulation X and Article V, Section 4(h) of the Exchange Constitution in that it knew, or should have known, that inappropriately placing options trades in its market making account held at ABC would cause ABC to improperly extend good faith market making margin treatment in contravention of Regulation T, as set forth in paragraphs 4.1 through 4.5

- 7.3 BKI violated SEC Rules 15c3-1, 17a-3(a)(11), 17a-5 and Exchange Rule 470 by filing inaccurate net capital computations on its December 31, 2003 and December 31, 2005 FOCUS Reports, as set forth in paragraph 6.2 and 6.3.
- 7.4 BKI violated SEC Rule 17a-5 and Exchange Rule 443 by failing to file a required Annual Audit Report for the calendar year 2005, as set forth in paragraphs 6.4 through 6.7.
- 7.5 BKI violated Exchange Rule 320 by failing to establish and maintain appropriate policies, systems and procedures of supervision and control, including WSPs, with respect to its Annual Audit Report filing and subordinated loan requirements, and by failing to properly implement its procedures with respect to filing accurate FOCUS Reports, as set forth in paragraph 6.8.

**DISCIPLINARY ACTION:**

By reason of the foregoing Stipulated Facts and violations, a Hearing Officer may impose the following penalties against the Respondent:

- (a) a censure; and
- (b) a fine in the amount of \$ 15,000.

The Respondent hereby acknowledges that it has read carefully this Stipulation and understands all of the provisions contained herein; that it has agreed to its provisions voluntarily; and that no offer, promise, threat or inducement of any kind has been tendered to the Respondent by the Exchange, its staff or representatives to induce the Respondent to enter into this Stipulation, aside from the prospect of settling this disciplinary proceeding based on the terms and conditions set forth in this Stipulation rather than adjudicating this matter by way of a hearing on a Charge Memorandum as provided by Exchange rules.

Further, the Respondent hereby agrees that it 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 Stipulation or create the impression that the Stipulation is without factual basis. Nothing in this provision affects the Respondent's testimonial obligations or right to take legal or factual positions in litigation or other legal proceedings in which the Exchange is not a party.

Further, the Respondent understands and agrees that the Exchange may make a public announcement concerning this Stipulation and the subject matter thereof in a manner consistent with those specified in Rule 12 of the Rules and Procedures Applicable to Exchange Disciplinary Proceedings.

Finally, it is understood and agreed that in any written submission to or proceeding before any person reviewing and/or body convened to consider this Stipulation of Facts and Consent to Penalty (including any reviewing person or body authorized by the Amex Constitution and/or Rules), neither Enforcement nor the Respondent, shall offer any argument that is inconsistent with the stipulated facts or the agreed-upon penalty, nor shall either party ask for the imposition of any penalty (including arguing that no penalty should be imposed) other than that agreed upon in this Stipulation of Facts and Consent to Penalty.

AMERICAN STOCK EXCHANGE LLC

By: Claudia Crowley

Claudia Crowley  
Senior Vice President  
Chief Regulatory Officer  
American Stock Exchange LLC

Agreed to this 18 day of August, 2008.

[Signature]  
On behalf of BKI Associates