

**BEFORE THE BUSINESS CONDUCT COMMITTEE**  
**OF THE**  
**CHICAGO BOARD OPTIONS EXCHANGE, INCORPORATED**

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In the Matter of:	)	
	)	
Ladenburg Thalmann & Co., Inc.	)	File No. 96-0046
590 Madison Avenue	)	
New York, New York 10022	)	
	)	
Respondent	)	
	)	

**DECISION ACCEPTING OFFER OF SETTLEMENT**

This proceeding was instituted by the Business Conduct Committee (the "Committee") of the Chicago Board Options Exchange, Incorporated (the "Exchange") as a result of an investigation by the staff of the Exchange, which indicated that there was probable cause for finding a violation within the disciplinary jurisdiction of the Exchange. In accordance with that determination, the Committee directed the issuance of a Statement of Charges ("Statement of Charges"). Pursuant to Exchange Rule 17.8, the respondent, Ladenburg Thalmann & Co., Inc. ("Respondent" or "Ladenburg"), submitted an offer of settlement ("Offer of Settlement").

In submitting the Offer of Settlement, the Respondent neither admitted nor denied the violations alleged in the Statement of Charges.

The Respondent has agreed that the determination of the Committee to accept the Offer of Settlement shall constitute a final Decision, and, as provided in Exchange Rule 17.8, the Respondent may not seek review thereof.

The Respondent understands and acknowledges that the Committee's decision in this matter will become part of his disciplinary record and may be considered in any future Exchange proceeding.

With due regard to the particulars of this matter, the Committee believes it is appropriate to accept the Respondent's Offer of Settlement based on the following stipulated facts and findings and thereby to impose the sanction specified below.

**FACTS**

1. During all relevant periods herein, Ladenburg was a member of the Exchange.
2. During all relevant periods herein, Ladenburg was registered with the Exchange to transact business on the Exchange in accordance with Exchange Rules as a member organization approved to conduct a non-member customer business.

3. During all relevant periods herein, a person associated with Ladenburg ("Associated Person") was registered with the Exchange to transact business on the Exchange in accordance with Exchange Rules as an associated person of Ladenburg working as a trader's assistant on Ladenburg's proprietary trading desk. During all relevant periods, Associated Person maintained a personal trading account at Ladenburg.
4. During all relevant periods herein, another person associated with Ladenburg was registered with the Exchange to transact business on the Exchange in accordance with Exchange Rules as an associated person of Ladenburg working as its President, head trader and supervisor of Ladenburg's proprietary trading desk ("Trading Supervisor").
5. During all relevant periods herein, Exchange Rules 4.1 (Just and Equitable Principles of Trade), 4.2 - (Adherence to Law), 4.6 - (False Statements), 6.8(a)(i) - (RAES Operations in Equity Options), 6.24(a) - (Orders Required to be in Written Form), 7.4(a) - (Obligations for Orders), 9.8, 15.1 and File No. SR-CBOE-85-32 - (Order Approving Rule Changes by the CBOE Relating to the Retail Automated Execution System), Securities Exchange Act Release No. 34-23490 dated August 1, 1986, and published in the CBOE Exchange Bulletin dated August 13, 1986 (SR-CBOE-85-32); and Section 17(a)(1) of the Securities Exchange Act of 1934 as amended (the "Act") and Rule 17a-3 thereunder (Accounts and Records, Examinations of Exchanges, Members and Others), were in full force and effect.
6. During the period from in or about December 1991 through in or about May 1995, Ladenburg failed to establish and implement adequate written supervisory procedures and controls relating to, but not limited to, the review of employee trading accounts, the review and reconciliation of Ladenburg's proprietary accounts, the handling and processing of order entry, and the handling and processing of trade corrections.
7. During the period from in or about December 1991 through in or about May 1995, Ladenburg failed reasonably to supervise Associated Person, who engaged in a fraudulent and deceptive course of conduct whereby, through the use of an electronic system that accepted order entry and same-day trade corrections at Ladenburg, Associated Person: a) caused numerous losing Standard Poor's 100 Stock Index Option ("OEX") trades originally effected by Associated Person for his personal trading account and/or the accounts of other Ladenburg employees to be assigned to Ladenburg's proprietary accounts; and b) converted Ladenburg's funds to his own use by causing certain profitable OEX option trades originally effected by Associated Person for Ladenburg's proprietary accounts to be assigned to Associated Person's personal trading account. As a result of Associated Person's conduct described above, Ladenburg experienced an aggregate net loss of approximately \$757,111.
8. During the period from in or about December 1991 through in or about May 1995, Ladenburg failed reasonably to supervise Trading Supervisor in that Trading Supervisor permitted individuals other than firm proprietary account traders, including but not limited to Associated Person, to effect trades in Ladenburg's proprietary accounts and agreed to pay them a percentage of any profits generated as a result of the trades they each effected; however, Trading Supervisor failed to establish and implement adequate procedures to monitor the proprietary trading activities of these individuals even after he gave them the authority to effect proprietary trades.

9. During the period from in or about December 1991 through in or about May 1995, Ladenburg failed to preserve numerous order tickets representing transactions effected by Associated Person for Ladenburg's proprietary accounts and Associated Person's personal trading account.
10. During the period from in or about December 1991 through in or about May 1995, Ladenburg failed to preserve and retain records of numerous confirmations of trades and trade corrections.<sup>1</sup>
11. During the period from in or about May 1996 through in or about June 1996, Ladenburg permitted numerous firm proprietary option orders to be recorded and entered as customer orders rather than broker-dealer orders, thereby allowing those orders to be entered and executed through the Exchange's Retail Automated Execution System ("RAES") and/or the customer order book, when those orders were not eligible for execution through RAES or the customer order book.

### **FINDINGS**

12. The acts, practices and conduct described in each of Paragraphs 6 through 8 above constitute violations of Exchange Rules 4.2 and 9.8 by Ladenburg, in that Ladenburg failed to establish and implement reasonable supervisory procedures and failed to prevent Associated Person and Trading Supervisor from engaging in the conduct described in Paragraphs 7 and 8 above.
13. The acts, practices and conduct described in each of Paragraphs 9 and 10 above constitute violations of Exchange Rules 4.2 and 15.1 and Section 17(a)(1) of the Act and Rule 17a-3 thereunder by Ladenburg, in that Ladenburg failed to keep current and accurate its books and records.
14. The acts, practices and conduct described in Paragraph 11 above constitute violations of Exchange Rules 4.1, 4.6, 6.8(a)(i), 6.24(a), 7.4(a) and SR-CBOE-85-32 by Ladenburg, in that Ladenburg permitted certain firm proprietary option orders to be recorded and entered as customer orders rather than broker-dealer orders, thereby allowing those orders to be entered and executed through RAES and/or the customer order book, when those orders were not eligible for execution through RAES or the customer order book.

### **SANCTION**

The sanction to be imposed shall consist of:

- 1) a one hundred twenty-five thousand dollar (\$125,000) fine;
- 2) a censure; and

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<sup>1</sup> Ladenburg informed Exchange staff that such confirmations are called "play-backs," which are printed confirmations of orders or trade corrections transmitted over the electronic order entry system in Ladenburg's office.

- 3) Respondent agrees to the following undertakings:
- a) Ladenburg's outside counsel will complete the revision of Ladenburg's compliance manual within six months of the date of this Decision;
  - b) Ladenburg will ensure that a compliance certification form is delivered to each employee for signature annually;
  - c) CBOE Staff will be allowed to review and approve those compliance procedures that Ladenburg has implemented to prevent the misconduct at issue from occurring again. These procedures include those that Ladenburg has already implemented, copies of which have been provided to CBOE Staff, and the procedures adopted pursuant to paragraphs e) and f) below. CBOE Staff will be provided with those procedures adopted pursuant to paragraphs e) and f) below within one month of their adoption by Ladenburg's Compliance Department. CBOE Staff will also be provided with a copy of Ladenburg's revised compliance manual within six months of the date of this Decision; however, CBOE Staff will be allowed to review and approve only those compliance procedures that Ladenburg has implemented to prevent the misconduct at issue from occurring again, and those procedures that relate specifically to the supervision of Ladenburg's options business;
  - d) The Compliance Committee of Ladenburg's Board of Directors will conduct an audit, within 6 months of the date of this Decision, of those compliance procedures implemented to prevent the misconduct at issue from occurring again and will generate a report to be submitted to both Ladenburg's Board of Directors and the CBOE Staff regarding the Committee's findings. The audit, which may be performed by the Compliance Department under the Committee's direction, will include but not be limited to an examination of the Trading Desk, which will, in turn, include a review of the compliance procedures implemented since the discovery of Associated Person's wrongdoing. Further, if the audit report recommends that any revisions or additions to Ladenburg's procedures be implemented to prevent the misconduct at issue from occurring again, Ladenburg shall furnish such recommendations to the Exchange's Department of Compliance;
  - e) Ladenburg will establish a policy requiring employees to disclose any arrangements for sharing in the profits and losses of retail accounts or firm proprietary accounts prior to establishing such arrangements; and
  - f) Ladenburg will establish a procedure whereby supervisors are made aware of active account reports for employee personal accounts after three consecutive active account reports have been issued for a particular account in a given calendar year.

In accepting the offer of settlement, the Committee considered that the Respondent has voluntarily expended to date approximately \$525,000 to improve its systems of supervision and compliance since the discovery of the wrongdoing perpetrated by Associated Person, and of that amount, approximately \$425,000 is an annually-recurring cost for increased staffing and compensation in the legal and compliance areas.

### **ORDER**

ACCORDINGLY IT IS ORDERED THAT, the Respondent, Ladenburg Thalmann & Co., Inc., shall be and hereby is censured and fined in the amount of one hundred twenty five thousand dollars (\$125,000). It is further ordered that:

- a) Ladenburg's outside counsel will complete the revision of Ladenburg's compliance manual within six months of the date of this Decision;
- b) Ladenburg will ensure that a compliance certification form is delivered to each employee for signature annually;
- c) CBOE Staff will be allowed to review and approve those compliance procedures that Ladenburg has implemented to prevent the misconduct at issue from occurring again. These procedures include those that Ladenburg has already implemented, copies of which have been provided to CBOE Staff, and the procedures adopted pursuant to paragraphs e) and f) below. CBOE Staff will be provided with those procedures adopted pursuant to paragraphs e) and f) below within one month of their adoption by Ladenburg's Compliance Department. CBOE Staff will also be provided with a copy of Ladenburg's revised compliance manual within six months of the date of this Decision; however, CBOE Staff will be allowed to review and approve only those compliance procedures that Ladenburg has implemented to prevent the misconduct at issue from occurring again, and those procedures that relate specifically to the supervision of Ladenburg's options business;
- d) The Compliance Committee of Ladenburg's Board of Directors will conduct an audit, within 6 months of the date of this Decision, of those compliance procedures implemented to prevent the misconduct at issue from occurring again and will generate a report to be submitted to both Ladenburg's Board of Directors and CBOE Staff regarding the Committee's findings. The audit, which may be performed by the Compliance Department under the Committee's direction, will include but not be limited to an examination of the Trading Desk, which will, in turn, include a review of the compliance procedures implemented since the discovery of Associated Person's wrongdoing. Further, if the audit report recommends that any revisions or additions to Ladenburg's procedures be implemented to prevent the misconduct at issue from occurring again, Ladenburg shall furnish such recommendations to the Exchange's Department of Compliance;

- e) Ladenburg will establish a policy requiring employees to disclose any arrangements for sharing in the profits and losses of retail accounts or firm proprietary accounts prior to establishing such arrangements; and
- f) Ladenburg will establish a procedure whereby supervisors are made aware of active account reports for employee personal accounts after three consecutive active account reports have been issued for a particular account in a given calendar year.

SO ORDERED  
FOR THE COMMITTEE

June 16, 1997  
Date

By: /s/ Bruce I. Andrews  
Bruce I. Andrews  
Chairman  
Business Conduct Committee