

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

	)	
In the Matter of:	)	
	)	
Spear, Leeds & Kellogg, Inc.	)	
120 Broadway	)	
New York, NY 10271	)	File No. 96-0060
	)	
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 ("Respondent"), Spear, Leeds & Kellogg, Inc. ("SLK"), 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, the Respondent, SLK, was a member of the Exchange.
2. During all relevant periods herein, SLK was registered with the Exchange to transact business on the Exchange in accordance with Exchange Rules as a member organization associated with a market-maker and a floor broker, as a member organization authorized to conduct a non-member customer business, as a lessor member and as an Options Clearing Corporation ("OCC") Clearing Member.

3. During all relevant periods herein, First Options of Chicago, Inc. ("FOC") was registered with the Exchange to transact business on the Exchange in accordance with Exchange Rules as a Clearing Member, as a member organization associated with a market-maker and a floor broker, and as a member organization authorized to conduct a non-member customer business. Additionally, during all relevant periods herein, FOC was wholly owned by Spear, Leeds & Kellogg Acquisition Company, a wholly owned subsidiary of SLK.
4. During all relevant periods herein Rockrimmon Securities ("Rockrimmon"), currently known as Rockrimmon Securities L.L.C., was a member organization registered with the Exchange to transact business on the Exchange in accordance with Exchange Rules as an organization associated with a market-maker, floor broker and lessee.
5. During the approximate period from in or about May 1992 through in or about July 1994, Richard Lindar ("Lindar") was registered with the Exchange to transact business on the Exchange in accordance with Exchange Rules as a market maker and as a nominee of Rockrimmon.
6. During the approximate period from in or about October 1991 through in or about July 1993, Kelly Luthringshausen ("Luthringshausen") was an Exchange member registered to transact business on the Exchange in accordance with Exchange Rules as a market-maker and nominee for Rockrimmon.
7. In or about November 1992, certain Rockrimmon nominees established a market-maker joint account ("QJR") pursuant to Exchange Rule 8.9(c).
8. During the approximate period from in or about November 1992 through in or about July 1993, Rockrimmon market-maker nominee Luthringshausen was a member of QJR.
9. During all relevant periods herein, Exchange Rules 4.1 - Just and Equitable Principles of Trade, 4.2 - Adherence to Law, 4.6 - False Statements (including reporting misrepresentations to the Clearing Corporation) and 8.9(c) - Securities Accounts and Orders of Market-Makers and Section 17(a)(1) of the Securities Exchange Act of 1934, as amended (the "Act") - Accounts and Records, Reports, Examinations of Exchanges, Members, and Others and Rule 17a-5 - Reports to be Made by Certain Brokers and Dealers thereunder, were in full force and effect.
10. During the period from on or about May 1, 1992 through on about July 31, 1993, SLK submitted numerous position adjustments to OCC which moved positions that totaled at least 6,350 option contracts from Lindar's Rockrimmon nominee market-maker account into Luthringshausen's Rockrimmon nominee account when SLK knew or had reason to know that those positions resulted from transactions on the Exchange trading floor on behalf of Lindar's Rockrimmon nominee account.
11. During the period from on or about February 25, 1993 through on or about July 31, 1994, SLK submitted numerous position adjustments to OCC which moved numerous positions that totaled at least 55,000 option contracts from Rockrimmon accounts carried in the SLK Customers' Account at OCC to QJR, when SLK knew or had reason to know that those positions resulted from transactions on the Exchange trading floor on behalf of

Rockrimmon's customer account.

12. During the period from on or about October 1, 1991 through on or about July 31, 1993, SLK submitted numerous position adjustments to OCC which moved numerous positions that totaled at least 81,000 option contracts from Rockrimmon accounts carried in the SLK Customers' Account at OCC to Luthringshausen's Rockrimmon market-maker nominee account at OCC, when SLK knew or had reason to know that those positions resulted from transactions on the Exchange trading floor on behalf of Rockrimmon's customer account.
13. During the period from in or about October 1991 through in or about July 1994, SLK failed to establish, implement and maintain adequate procedures for the supervision and control of its activities and operations related to the clearance of trades into appropriate accounts and the verification that option positions were adjusted or moved for the purpose of correcting bona fide errors.
14. During the period from in or about October 1991 through in or about July 1994 and as further described in Paragraphs 10, 11 and 12 above, SLK, on approximately a daily basis, accepted trade information from Rockrimmon regarding the account origin of trades which was different than the account origin information provided by Rockrimmon on floor order tickets and as identified on the Exchange's records and provided by FOC. As a result of this information, SLK submitted numerous position adjustments to OCC, which thereby allowed Rockrimmon associated persons<sup>1</sup> ("Associated Persons") not registered as Exchange market-makers to initiate and enter numerous option orders on behalf of Rockrimmon, the execution of which resulted in transactions that cleared in Rockrimmon's market-maker accounts, when those non-market-maker transactions should have cleared into Rockrimmon's customer or Joint Back Office ("JBO")<sup>2</sup> accounts, and should have been subject to either customer margins or proprietary haircuts.

### **FINDINGS**

15. The acts, practices, and conduct described in each of Paragraphs 10, 11 and 12 above constitute violations of Exchange Rules 4.1 and 4.6 by SLK, in that SLK submitted position adjustments to OCC which moved numerous positions from Rockrimmon accounts carried in SLK Customers' Account at OCC to Luthringshausen's Rockrimmon market-maker nominee account at OCC or QJR, when SLK knew or had reason to know that those positions resulted from transactions on the Exchange floor on behalf of Rockrimmon's customer account and those position were not adjusted or moved for the purpose of correcting bona fide errors. In addition, SLK submitted position adjustments to OCC which moved numerous positions from Lindar's Rockrimmon nominee market-maker account into Luthringshausen's Rockrimmon nominee account when those positions resulted from transactions on the Exchange trading floor on behalf of Lindar's

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<sup>1</sup> Person associated with a broker or dealer as defined in the Securities Exchange Act of 1934, as amended, Section 3(a)(18).

<sup>2</sup> A JBO participant maintains a nominal ownership interest in its clearing firm. As a result, the clearing firm may finance the transactions of its JBO "owner" on a more beneficial margin basis than required under Regulation T of the Federal Reserve Board. A JBO participant's activity remains subject to the net capital rule under the Act.

Rockrimmon nominee account, and when those positions were not effected through market-maker transactions initiated by Luthringshausen or qualified members of QJR, respectively and those position were not adjusted or moved for the purpose of correcting bona fide errors.

16. The acts, practices, and conduct described in Paragraph 13 above constitute violations of Exchange Rules 4.1 and 4.2 by SLK, in that SLK failed to establish, implement and maintain adequate procedures for the supervision and control of its activities and operations related to the clearance of trades into appropriate accounts and the verification that option positions were adjusted or moved for the purpose of correcting bona fide errors. As a result, SLK facilitated persons not registered as Exchange market-makers to initiate and enter numerous option orders on behalf of Rockrimmon, the execution of which resulted in transactions that cleared in Rockrimmon's market-maker accounts, when those non-market-maker transactions should have cleared into Rockrimmon's customer account.
17. The acts, practices, and conduct described in Paragraph 14 above constitute violations of Exchange Rules 4.1, 4.2 and 4.6 and Section 17(a)(1) of the Act and Rule 17a-5 by SLK, in that SLK on numerous occasions, accepted trade information from Rockrimmon regarding the account origin of trades which was different than the account origin information provided by Rockrimmon on floor order tickets and as identified on the Exchange's records and provided by FOC. As a result of this information, SLK submitted numerous position adjustments to OCC, which thereby allowed persons not registered as Exchange market-makers to initiate and enter numerous option orders on behalf of Rockrimmon, the execution of which resulted in transactions that cleared or were adjusted into Rockrimmon's market-maker accounts, when those option transactions resulted from non-market-maker activity, which is subject to greater margin/capital requirements than the same transactions if qualified for market-maker treatment. As a result of the aforementioned conduct, SLK failed to accurately compute and report its net capital to the Securities and Exchange Commission or other regulatory bodies, in that the improper clearance or adjustment of non-market-maker transactions to market-maker accounts would inherently result in inaccurate margin deficiency calculations for such accounts. SLK's net capital was at no time during the relevant period below the minimum required by Rule 15c3-1.

### **SANCTION**

The sanction to be imposed shall consist of:

- 1) a fifty thousand dollar (\$50,000) fine;
- 2) a censure; and
- 3) undertakings that
  - a) SLK will retain an outside consultant acceptable to the Exchange (the "Consultant") within 30 days after the issuance of the Decision in this matter. The independent consultant shall attest that the procedures set forth in Paragraph b below shall be effective; and

- b) The Consultant will conduct an analysis to enable SLK to establish, implement, and maintain adequate procedures for the supervision and control of its activities and operations related to the clearance of trades into appropriate accounts and the verification that option positions are adjusted only for proper purposes. A copy of the procedures described herein shall be furnished to the Exchange's Department of Market Regulation within 120 days after the issuance of the Decision in this matter.

**ORDER**

ACCORDINGLY IT IS ORDERED THAT, the Respondent, Spear, Leeds & Kellogg, Inc., shall be and hereby is censured and fined in the amount of fifty thousand dollars (\$50,000). The Respondent is also hereby ordered to complete the following undertakings:

- 1) SLK will retain an outside consultant acceptable to the Exchange (the "Consultant") within 30 days after the issuance of the Decision in this matter. The independent consultant shall attest that the procedures set forth in Paragraph b below shall be effective; and
- 2) The Consultant will conduct an analysis to enable SLK to establish, implement, and maintain adequate procedures for the supervision and control of its activities and operations related to the clearance of trades into appropriate accounts and the verification that option positions are adjusted only for proper purposes. A copy of the procedures described herein shall be furnished to the Exchange's Department of Market Regulation within 120 days after the issuance of the Decision in this matter.

SO ORDERED  
FOR THE COMMITTEE

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

June 4, 1997  
Date