

**CBOE BZX EXCHANGE, INC.**  
**LETTER OF ACCEPTANCE, WAIVER AND CONSENT**  
**NO. 2015048008401**

TO: Cboe BZX Exchange, Inc.  
c/o Department of Enforcement  
Financial Industry Regulatory Authority ("FINRA")

RE: Cutler Group, LP, Respondent  
Broker-Dealer  
CRD No. 31730

Pursuant to Rule 8.3 of the Rules of Cboe BZX Exchange, Inc. ("BZX"), Cutler Group, LP (the "firm") 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, BZX will not bring any future actions against the firm alleging violations based on the same factual findings described herein.

**I.**

**ACCEPTANCE AND CONSENT**

- A. The firm hereby accepts and consents, without admitting or denying the findings, and solely for the purposes of this proceeding and any other proceeding brought by or on behalf of BZX, or to which BZX is a party, prior to a hearing and without an adjudication of any issue of law or fact, to the entry of the following findings by BZX:

**BACKGROUND**

The firm became registered as a broker-dealer with the Securities and Exchange Commission ("SEC") in April 1990 and became a member of BZX on April 1, 2010.

**RELEVANT PRIOR DISCIPLINARY HISTORY**

In *Cutler Group, LP*, Enforcement No. 2014-02 (PHLX April 3, 2014), the firm consented to findings that it violated SEC Rule 15c3-5(b) and 15c3-5(c)(2) and PHLX Rule 748 in that it failed to establish and maintain supervisory procedures, and a reasonable system of follow-up and review, designed to prevent and detect excessive message traffic and quotes in real time.

In *Dept. of Market Regulation v. Cutler Group, LP*, Proc. No. 20120321194 (NYSE Arca March 28, 2014), the firm consented to findings that, among other things, it violated SEC Rule 15c3-5(b) and (c) and NYSE Arca Options Rule 11.18(b) and (c) by failing to establish and maintain written supervisory procedures and operational risk control systems reasonably designed with respect to the oversight and operation of algorithmic quoting and trading.

In these actions, the firm consented to censures and fines totaling \$385,000, of which \$230,000 was paid to PHLX and \$155,000 was paid to Arca.

### **SUMMARY**

FINRA's Department of Market Regulation reviewed the firm's compliance with SEC Rule 15c3-5 of the Securities Exchange Act of 1934 and related requirements with respect to the firm's risk management controls and supervisory system, including supervisory procedures, as it pertained to market access for preventing and detecting potentially excessive order message activity, including its quoting, from December 12, 2013, through April 30, 2014. The review was prompted by regulatory alerts in eighty instances of potentially excessive messaging activity by the firm on BZX. As detailed below, the firm's risk management controls and supervisory procedures were not reasonably designed to prevent excessive messaging activity on BZX, in violation of Rule 15c3-5(b) and (c), and BZX Rules 3.1, 3.2, and 5.1.

### **FACTS AND VIOLATIVE CONDUCT**

1. SEC Rule 15c3-5 is designed to reduce the risks faced by broker-dealers, as well as the markets and the financial system as a whole, as a result of various market access arrangements, by requiring effective financial and regulatory risk management controls reasonably designed to limit financial exposure and ensure compliance with applicable regulatory requirements to be implemented on a market-wide basis.
2. Rule 15c3-5(b) requires, among other things, a broker-dealer with market access to "establish, document, and maintain a system of risk management controls and supervisory procedures reasonably designed to manage the financial, regulatory, and other risks" of its market access activity and to preserve a copy of such supervisory procedures and a written description of its risk management controls as part of its books and records.
3. Rule 15c3-5(c)(1)(ii) further provides that the risk management controls and supervisory procedures required by Rule 15c3-5(b) must be reasonably designed to prevent "the entry of erroneous orders, by rejecting orders that exceed appropriate price or size parameters, on an order-by-order basis or over a short period of time, or that indicate duplicative orders." Rule 15c3-5(c)(2) requires that the risk management controls and supervisory procedures shall be reasonably designed to ensure compliance with all regulatory requirements.
4. BZX Rule 3.1 states that a member, in the conduct of its business, shall observe high standards of commercial honor and just and equitable principles of trade. BZX Rule 3.2 prohibits a member from violating the Securities Exchange Act of 1934 or rules and regulations thereunder and BZX's bylaws, rules, or any policy or written interpretation of the bylaws or rules. BZX Rule 5.1 requires a member to establish, maintain, and enforce written procedures that enable it to supervise properly the activities of associated persons and to assure compliance with applicable securities laws, rules, regulations, statements of policy, and BZX rules.

5. From May 2013 through October 2014, the firm's risk management controls and supervisory procedures were not reasonably designed to manage the financial, regulatory, and other risks associated with its business activity involving market access, as required by Rule 15c3-5. In addition, the firm did not establish and maintain written procedures that would enable it to supervise properly the activities of associated persons to assure compliance with applicable securities rules and BZX rules. In particular, the firm's risk management controls and supervisory procedures were not reasonably designed to timely detect and prevent excessive quotation message activity on BZX. As a result, in 80 instances from December 2013 through April 2014, the firm generated surveillance alerts in BZX's systems for excessive messaging.
  6. For example, regulatory surveillance alerts show that in one instance on December 12, 2013, in a one-second period between 10:13:02 and 10:13:03, the firm repeatedly entered and deleted, 258 times, the bids for one option with the same size and price (\$4.70 for one contract), and, in the same second, repeatedly entered and deleted, 259 times, the offers for the same option for the same size and price (\$6.30 for one contract).
  7. The firm's controls and supervisory procedures required by Rule 15c3-5(b) and (c) were not reasonably designed. With respect to one quoting platform, the firm had not fully implemented its controls to prevent excessive messaging on BZX from May 2013 until January 2014. With respect to a second quoting platform, the firm had not fully implemented its controls to prevent excessive messaging on BZX or implemented relevant exception reports from May 2013 until October 2014.
  8. In addition, although the firm had certain reports to review excessive messaging generally and had written supervisory procedures that required regular reviews of those exception reports, by failing to have reasonably designed controls to prevent excessive messaging on BZX specifically, the firm's procedures were not designed to enable the firm to supervise its activities properly and to assure compliance with Rule 15c3-5. Accordingly the firm violated Rule 15c3-5(b), (c)(1)(ii), and (c)(2).
  9. The conduct in paragraphs 5 through 8 also violated BZX Rules 3.1, 3.2, and 5.1.
- B. The firm also consents to a censure and a fine of \$62,500.

The firm agrees to pay the monetary sanction upon notice that this AWC has been accepted and that such payment is due and payable. It has submitted an Election of Payment form showing the method by which it proposes to pay the fine imposed.

The firm specifically and voluntarily waives any right to claim that it is unable to pay, now or at any time hereafter, the monetary sanction imposed in this matter.

The sanctions imposed herein shall be effective on a date set by BZX.

## II.

### WAIVER OF PROCEDURAL RIGHTS

The firm specifically and voluntarily waives the following rights granted under BZX Rules:

- A. To have a Statement of Charges issued specifying the allegations against the firm;
- B. To be notified of the Statement of Charges 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 Appeals Committee of the BZX's Board of Directors and then to the U.S. Securities and Exchange Commission and a U.S. Court of Appeals.

Further, the firm specifically and voluntarily waives any right to claim bias or prejudgment of the Chief Regulatory Officer ("CRO"), in connection with the CRO's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including acceptance or rejection of this AWC.

The firm further specifically and voluntarily waives any right to claim that a person violated the ex parte prohibitions of BZX Rule 8.16, 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

The firm 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 CRO, pursuant to BZX Rule 8.3;
- B. If this AWC is not accepted, its submission will not be used as evidence to prove any of the allegations against the firm; and
- C. If accepted:
  - 1. this AWC will become part of the firm's permanent disciplinary record and may be considered in any future actions brought by BZX or any other regulator against the firm;
  - 2. this AWC will be published on a website maintained by BZX in accordance with BZX Rule 8.18; and

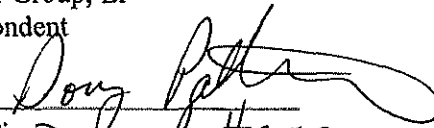
3. The firm may not take any action or make or permit to be made any public statement, including in regulatory filings or otherwise, denying, directly or indirectly, any finding in this AWC or create the impression that the AWC is without factual basis. The firm may not take any position in any proceeding brought by or on behalf of BZX, or to which BZX is a party, that is inconsistent with any part of this AWC. Nothing in this provision affects the firm's: (i) testimonial obligations; or (ii) right to take legal or factual positions in litigation or other legal proceedings in which BZX is not a party.

D. The firm may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. The firm 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 BZX, nor does it reflect the views of BZX or its staff.

The undersigned, on behalf of the firm, certifies that a person duly authorized to act on its 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 it 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 herein and the prospect of avoiding the issuance of a Complaint, has been made to induce the firm to submit it.

12/6/2018  
Date


Cutler Group, LP  
Respondent

By:   
Name: Doug Patterson  
Title: CEO

Reviewed by:

\_\_\_\_\_  
Counsel for Respondent  
Firm Name  
Address  
City/State/Zip  
Phone Number

12/13/2018  
Date

  
Greg Hoogasian  
Senior Vice President & Chief Regulatory Officer  
Cboe BZX Exchange, Inc.

**ELECTION OF PAYMENT FORM**

The firm intends to pay the fine proposed in the attached Letter of Acceptance, Waiver and Consent by the following method (check one):

- A firm check or bank check for the full amount; or
- Wire transfer.

Respectfully submitted,

12/6/2018

Date

Respondent

Cutler Group, LP

By: Doug Patterson

Name: Doug Patterson

Title: CEO