Re Independent Trading Group (ITG)

I<small>N THE MATTER OF</small>:

The Rules of the Investment Industry Regulatory Organization of Canada

and

The Universal Market Integrity Rules

and

Independent Trading Group (ITG) Inc.

2015 IIROC 21

Investment Industry Regulatory Organization of Canada
Hearing Panel (Ontario District)

Heard: April 27, 2015
Decision: April 27, 2015
Reasons: June 30, 2015

Hearing Panel:
Thomas J. Lockwood, Q.C. (Chair), Leo Ciccone and Guenther Kleberg
Appearances:
Charles Corlett Enforcement Counsel, IIROC
Kenneth Dekker, Respondent's Counsel

REASONS FOR DECISION

A.   BACKGROUND

¶ 1   On March 23, 2015, IIROC Staff made an Offer of Settlement ("Offer") to Independent Trading Group (ITG) Inc. ("Respondent"). Appendix "A" to the Offer was a Statement of Allegations.

¶ 2   Paragraph 3 of the Offer provided that, if accepted by the Respondent, the resulting Settlement Agreement was conditional upon approval by a duly appointed Hearing Panel.

¶ 3   The Offer was accepted by the Respondent.

¶ 4   On April 27, 2015, the Hearing Panel convened. We carefully reviewed the Settlement Agreement. We also considered the oral submissions of Counsel for Staff as well as Counsel for the Respondent. The parties jointly recommended that the Settlement Agreement be accepted.

¶ 5   After a short period of deliberation, we unanimously accepted the Settlement Agreement. At the time we advised that written Reasons for our Decision would follow. These are those Reasons.

B.   THE SETTLEMENT AGREEMENT

¶ 6   The salient provisions of the Settlement Agreement are as follows:

OFFER OF SETTLEMENT

A.   INTRODUCTION

1.   The Enforcement Department Staff (Staff) of the Investment Industry Regulatory Organization of Canada (IIROC) has conducted an investigation (the Investigation) into the conduct of Independent Trading Group (ITG) Inc. (the Respondent).

2.   The Investigation has disclosed matters for which IIROC seeks certain sanctions against the Respondent pursuant to Rule 10.5 of the Universal Market Integrity Rules (UMIR).

3.   If this Offer of Settlement is accepted by the Respondent, the resulting settlement agreement (the Settlement Agreement), which has been negotiated in accordance with Part 3 of UMIR Policy 10.8, is conditional upon the approval by a hearing panel appointed pursuant to IIROC Transitional Rule No.1, Schedule C.1 (the Hearing Panel).

4.   The Respondent agrees to waive all rights under UMIR to a hearing or to an appeal or review if the Settlement Agreement is approved by the Hearing Panel.

5.   The Respondent consents to be subject to the jurisdiction of IIROC and its relevant disciplinary process and rules in relation to this matter.

6.   Staff and the Respondent jointly recommend that the Hearing Panel accept this Settlement Agreement.

B.   AGREEMENT AS TO REQUIREMENTS CONTRAVENED

7.   The Respondent agrees that it contravened UMIR 7.1(6) and Policy 7.1, Part 7 by failing to adopt, document and maintain a system of risk management and supervisory controls, policies and procedures that was adequate to ensure the management of the financial, regulatory and other risks associated with electronic access to marketplaces.

C.   ADMITTED FACTS

8.   For the purposes of this Settlement Agreement only, Staff and the Respondent agree with and rely upon the admitted facts and conclusions which are set out in the Statement of Allegations attached as Appendix "A" to this Settlement Agreement.

D.   DISPOSITION

9.   For the contraventions in paragraph 7 above, Staff and the Respondent have agreed upon disposition as follows:

    (i)   a fine of $170,000.00 payable by the Respondent to IIROC; and

    (ii)   costs of $5,000.00 payable by the Respondent to IIROC."

STATEMENT OF ALLEGATIONS

I.   REQUIREMENTS CONTRAVENED

1.   Independent Trading Group (ITG) Inc. ("Independent Trading Group") contravened Universal Market Integrity Rule ("UMIR") 7.1(6) and Policy 7.1, Part 7 by failing to adopt, document and maintain a system of risk management and supervisory controls, policies and procedures that was adequate to ensure the management of the financial, regulatory and other risks associated with electronic access to marketplaces.

[2   Omitted]

II.   RELEVANT FACTS AND CONCLUSIONS

<u>Overview</u>

3.   In 2013, IIROC implemented UMIR 7.1(6) and Policy 7.1, Part 7 – Specific Provisions Applicable to Electronic Access that, among other things, detailed the automated pretrade controls that were expected of Participants to prevent trades from being entered that do not comply with the relevant Requirements or that cause the Participant to exceed predetermined credit or capital thresholds.

4.   While Independent Trading Group did take steps thereafter to put in place some automated pre-trade controls and had an honest belief at the time of the Trading Error (as defined below) that appropriate automated controls were in place, those controls were not in fact calibrated and maintained in a manner that was adequate to prevent the entry of an order that would result in the firm exceeding pre-determined credit or capital thresholds.

5.   On January 21, 2014, at the open of trading on the TSX, Independent Trading Group's failure to employ adequate automated pre-trade controls to limit its financial exposure allowed for the entry of an erroneous order that resulted in an intraday capital deficiency of approximately $8 million (the "Trading Error").

6.   As set out in more detail below, Independent Trading Group's management quickly recognized the Trading Error and took immediate steps to remedy its intraday capital deficiency by covering the short position created by the Trading Error. Independent Trading Group also took immediate steps to notify IIROC staff of the Trading Error.

<u>The Respondent</u>

7.   Independent Trading Group is registered as an investment dealer, is a member and subscriber to IIROC-regulated marketplaces, and therefore is a Participant under UMIR.

8.   Independent Trading Group is engaged in the business of market making and proprietary trading.

<u>The Trading Error</u>

9.   During the TSX pre-opening session on January 21, 2014 at 9:27:07 a.m., the shares of Bank of Nova Scotia ("BNS") showed a calculated opening price ("COP") of $1000 as a result of a large market buy order entered by a Participant that created an imbalance.

10.   In response to these market conditions, a proprietary trader at Independent Trading Group (the "Trader") entered three orders to sell short 1000 shares of BNS at prices above its previous day's closing price.

11.   Shortly before the scheduled open of trading, the Trader entered a fourth order to sell short 825,000 shares of BNS at $66. The Trader inadvertently failed to modify the volume of the order, overrode an alert related to the volume of the order, and submitted the order to the marketplace 4/10ths of a second before the scheduled open of trading. The time from the Trader generating the order to entering it to the marketplace was five seconds.

12.   As a result of the Trader's erroneous order, when the shares of BNS opened for trading at 9:30 a.m., the order was filled for 586,300 shares. The Trading Error caused Independent Trading Group to become capital deficient by approximately $8 million.

<u>The Entry of the Erroneous Order</u>

13.   The Trader entered each of the four orders by double-clicking the displayed volume of the bid on the trade-station. This generated a sell order with a bid volume equal to the displayed volume

(rounded down to the nearest 1000 shares) and a limit price equal to the bid price (during the pre-open equivalent to the COP). After the order was generated, the Trader could modify the price and/or volume before submitting the order to the marketplace.

14. The Trader's trade-station had "soft" controls to prevent the entry of an order that would exceed the Trader's pre-set limits for order value, volume and price differential. If a limit was triggered by the entry of an order, an additional pop up window with the details of the alert would be generated to warn the Trader before entering the order to the marketplace. The Trader was able to override these alerts by a keyboard shortcut on the trade-station.

15. The first three orders generated alerts due to the price differential of the orders from the COP. The fourth order generated an alert due to the volume of the order. All four alerts were overridden by the Trader.

16. The table below sets out the particulars of the Trader's orders culminating in the Trading Error (order #4):

	Order Entry Time	Displayed Bid Volume at time of order	Displayed Bid Price at time of order	Sell Order Generated	Volume Modified	Price Modified	Alert Overridden
1	9:27:55	831,900	$1000	831,000 @ $1000	1000	$75	Yes (price)
2	9:28:06	831,900	$1000	831,000 @ $1000	1000	$95	Yes (price)
3	9:28:17	831,900	$1000	831,000 @ $1000	1000	$69	Yes (price)
	9:29:41	Order for 200,000 @ $69 entered by another Participant COP (displayed bid price) changes to $69						
4	9:29:56	825,300	$69	825,000 @ $69	No	$66	Yes (volume)
	9:29:56	COP (displayed bid price) changes to $66 as a result of the Trader's order						
	9:30:00	BNS opens at $66 Order is partially filled for 586,300 shares @ $66; 238,700 shares left unfilled						
	9:30:13	Trader cancels unfilled order						

Events Subsequent to the Trading Error

17. The Trader immediately cancelled the unfilled portion of the order and contacted Independent Trading Group's Ultimate Designated Person to inform him of the error.

18. Beginning at 9:30:25, the Trader began covering the short position by purchasing BNS on the marketplace.

19. Independent Trading Group's senior management made the decision to continue covering the short position as quickly as possible while minimizing the disruption to the marketplace. Another trader from ITG, who had access to an algorithmic trading program to handle large orders, was

enlisted to assist in covering the short position in this manner.

20. Approximately twenty minutes after the Trading Error, the firm's senior management notified IIROC's Financial & Operations Compliance department of the capital deficiency and the steps being taken to rectify it. They then notified the Chief Financial Officer of the firm's carrying broker.

21. By 10:20, the capital deficiency was corrected by covering the short position and by 10:30, the position was closed. Independent Trading Group also earned a profit on the trading. IIROC staff is satisfied that the Trading Error and the regulatory breach that allowed it to occur were inadvertent and not calculated or intended by Independent Trading Group or the Trader to earn a profit.

Failure to Employ Automated Controls to Limit Financial Exposure

22. UMIR 7.1(6) and Policy 7.1, Part 7 require a Participant to adopt risk management and supervisory controls, policies and procedures reasonably designed to ensure the management of the financial risks associated with electronic access to marketplaces. The Rule changes implemented in 2013 also require that the risk management and supervisory controls include automated controls to prevent the entry of an order which would result in the Participant exceeding pre-determined credit or capital thresholds.

23. The firm had "soft" controls for each trader at the trade-station level, which could be overridden, once confirmed, by the traders. The firm was required to have "hard" controls on a firm-wide level that could not be modified or overridden by the traders. While the firm did have some automated pre-trade controls in place, the firm did not have in place pre-trade controls sufficient to prevent any order that exceeded pre-determined credit or capital thresholds, in particular an erroneous or "fat-finger" order.

24. Independent Trading Group mistakenly believed that its service provider for its smart order router (the "SOR Provider") had enabled firm-wide pre-trade controls to prevent an order exceeding a maximum order value. The basis for this mistaken belief was a newsletter from the SOR Provider in September 2013 that stated, among other things: "**Please note that on September 5th, 2013, [we] AUTOMATICALLY enabled 'Fat Finger' checking for all our workstation customers to try to prevent orders entered with keystroke errors." The same communication invited customers to contact the SOR Provider to enable and configure other pre-trade controls.

25. Independent Trading Group subsequently received "Fat Finger" alerts through its trading system that orders had been blocked for exceeding a maximum price difference and assumed that this was an indication that broader pre-trade controls had been put into place by its SOR Provider to prevent orders exceeding a maximum order value when this was not in fact the case.

26. Independent Trading Group did not take sufficient further steps to confirm what additional firm-wide pre-trade controls had in fact been enabled by its SOR Provider. It did not consider what capital thresholds would be appropriate based on the firm's risk tolerances and capital position, confirm what thresholds were in place with its SOR Provider, document the thresholds in its policies and procedures, or conduct any testing prior to the Trading Error to ensure that all necessary controls were in place.

Remedial Steps Taken

27. Immediately following the Trading Error, Independent Trading Group reviewed and, where necessary, ensured that automated pre-trade controls were in place at a firm-wide level for orders exceeding pre-determined credit and capital thresholds.

28. Subsequently, Independent Trading Group implemented the following measures:

   (i)   a review of all pre-trade controls and parameters in place at a trade-station and firm-wide level;

   (ii) undertook a process to update its policies and procedures relating to electronic access to marketplaces; and

   (iii) adopted procedures for the regular review of pre-trade controls and parameters in place for its trading systems.

III.   CONCLUSION

29. The Trading Error was inadvertent but resulted in serious financial exposure to Independent Trading Group. The Trading Error could have been prevented had Independent Trading Group taken reasonable additional steps to fulfill its trading supervision obligations under UMIR by employing and verifying that it had in place adequate automated controls to prevent the entry of orders which would result in the firm exceeding pre-determined credit or capital thresholds.

30. Independent Trading Group has recognized that it did financially benefit as a result of the Trading Error and that it should not retain any financial benefit from the Trading Error as a result of its non-compliance with UMIR.

31. The fine that Independent Trading Group has agreed to pay in this Settlement Agreement takes into account the profit earned from the Trading Error while allowing for the deduction of certain costs associated with the event and the remedial steps undertaken.

32. The costs incurred by Independent Trading Group as a result of the breach and the remedial steps that it has undertaken include an assessment paid to the Canadian Investor Protection Fund arising from the capital deficiency, the cost of hiring a consultant to ensure its policies and procedures are properly updated, and execution fees related to covering the short position."

C.   **SUBMISSIONS**

¶ 7   Both Staff and Counsel for the Respondent made extensive oral submissions as to why, in their respective views, the Settlement Agreement should be accepted by the Hearing Panel.

D.   **DISCUSSION**

¶ 8   We find that the trading error was inadvertent. However, it did result in a serious financial exposure to the Respondent, as well as a potential risk to market integrity.

¶ 9   The Respondent is a small firm which did take some steps to put controls in place to prevent the type of error which occurred. However, these were "soft" controls which could be overridden by the traders.

¶ 10   The requirement was to have "hard" controls in place on a firm-wide level which could not be modified or overridden by the traders.

¶ 11   The Respondent does not have any history of non-compliance.

¶ 12   A financial benefit did accrue to the Respondent as a by-product of correcting the error. The proposed settlement was structured to ensure that no net benefit was received by the Respondent.

¶ 13   The Respondent took the following immediate steps once the volume error was discovered:

   (a)   the unfilled portion of the order was cancelled;

   (b)   the Respondent's Ultimate Designated Person was contacted and advised of the error;

   (c)   the Trader began covering the short positon;

(d) IIROC's Financial & Operation Compliance Department was notified of the capital deficiency and the steps being taken to rectify it;

(e) the Chief Financial Officer of the Respondent's carrying broker was notified; and

(f) within the hour, the capital deficiency was corrected and the position closed.

¶ 14 There was no market interruption.

¶ 15 The Respondent also took steps to review all of its pre-trade controls to ensure that a volume error of this nature would not occur in the future.

¶ 16 We were referred to the new IIROC Sanction Guidelines, which became effective as of February 2, 2015. These Guidelines supersede and replace all previous versions of both the Dealer Member Disciplinary Sanction Guidelines and the UMIR Disciplinary Guidelines.

¶ 17 The parties submitted that the Settlement Agreement complied with these Guidelines. For example, Principle No. 1 provides that: "Disciplinary sanctions are preventative in nature and should be designed to protect the investing public, strengthen market integrity, and improve overall business standards and products."

¶ 18 In the narrative, under the Principle, we were referred to the sentence which states: "When considering specific and general deterrence in the imposition of sanctions, consideration should be given to the size of the Dealer Member, including the firm's financial resources, nature of the firm's business, and the number of individuals associated with the firm, with a view toward ensuring that the sanctions imposed are sufficient to achieve deterrence."

¶ 19 We were also referred to Principle No. 4, which states that: "Sanctions should ensure that a registrant does not financially benefit as a result of misconduct."

¶ 20 The parties also relied on the IIROC Decision in BMO Nesbitt Burns (Re) 2012 IIROC 21, which was a settlement agreement case relating to a trading error.

¶ 21 In this case, a BMO Nesbitt Burns ("BMONB") trader inadvertently entered a Market-on-Close Order ("MOC Order") to sell 33,000,000 shares of Bank of Montreal stock when he intended to enter an order to sell 33,000 shares. The BMONB trader did not discover the error until 3:40 p.m., when the TSX published the MOC imbalance. BMONB immediately called IIROC and the TSX to report the error and seek guidance on the appropriate way to correct the error.

¶ 22 At the time of the erroneous order, no pre-trade filters were enabled on the trader's trading application. BMONB admitted in the Settlement Agreement that had an adequate supervision system been in place, the error would have been detected prior to entry in the MOC Facility.

¶ 23 This is to be contrasted with the situation before us, where the Respondent mistakenly believed that the service provider for its smart order router had enabled firm-wide pre-trade controls to prevent an order exceeding a maximum order value.

¶ 24 In the BMO case, the Hearing Panel accepted the joint recommendation for a $50,000 fine and costs in the amount of $5,000.

¶ 25 The Respondent is a small company owned by a limited number of individuals. It has no clients. Its capitalization is relatively small. The publicity surrounding this trading error has had a significant impact on the firm's reputation.

¶ 26 While the message has clearly been brought home to the Respondent, it is important, for purposes of general deterrence, that the market participants be reminded of the importance of managing their risk.

¶ 27 At the Settlement Hearing, Counsel for the Respondent indicated the desire on the part of the Respondent to send a strong message to the market participants.

¶ 28   The fine that the parties are jointly recommending takes into account the profits earned on the trading error while allowing for the deduction of certain costs associated with both the events and the remedial steps undertaken by the Respondent to ensure that such an error would not occur in the future. A description of the costs incurred is contained in the Settlement Agreement.

E.   THE LAW

¶ 29   This Hearing Panel must determine whether the proposed sanctions "strike a reasonable balance between fairness to the Respondent in the circumstances and the need to protect the investing public, the industry membership, the integrity of the discipline process, the integrity of the securities markets and prevention of a repetition of the offense."

>   *Re Bereskin* [2010] IIROC No. 37 at para 5.

¶ 30   It is clear that a Hearing Panel should not reject the penalties set out in the Settlement Agreement unless they "clearly fall outside a reasonable range of appropriateness."

>   *Milewski (Re),* [1999] I.D.A.C.D. No. 17 at p. 13-14.

F.   DECISION

¶ 31   After carefully reviewing the Settlement Agreement, the submissions of the parties, the IIROC Sanction Guidelines and previous analogous Decisions, we unanimously concluded that it was in the public interest for the Hearing Panel to accept the Settlement Agreement.

G.   ORDER

¶ 32   We consequently ordered that the Respondent immediately pay to IIROC:

>   (a)   a fine in the amount of $170,000.00; and

>   (b)   costs in the amount of $5,000.00.

DATED at Toronto this 30th day of June, 2015

Thomas J. Lockwood, Q.C., Chair

Leo Ciccone

Guenther Kleberg

OFFER OF SETTLEMENT

A.   INTRODUCTION

1.   The Enforcement Department Staff (Staff) of the Investment Industry Regulatory Organization of Canada (IIROC) has conducted an investigation (the Investigation) into the conduct of Independent Trading Group (ITG) Inc. (the Respondent).

2.   The Investigation has disclosed matters for which IIROC seeks certain sanctions against the Respondent pursuant to Rule 10.5 of the Universal Market Integrity Rules (UMIR).

3.   If this Offer of Settlement is accepted by the Respondent, the resulting settlement agreement (the Settlement Agreement), which has been negotiated in accordance with Part 3 of UMIR Policy 10.8, is conditional upon the approval by a hearing panel appointed pursuant to IIROC Transitional Rule No.1, Schedule C.1 (the Hearing Panel).

4.   The Respondent agrees to waive all rights under UMIR to a hearing or to an appeal or review if the

Settlement Agreement is approved by the Hearing Panel.

5. The Respondent consents to be subject to the jurisdiction of IIROC and its relevant disciplinary process and rules in relation to this matter.

6. Staff and the Respondent jointly recommend that the Hearing Panel accept this Settlement Agreement.

B. AGREEMENT AS TO REQUIREMENTS CONTRAVENED

7. The Respondent agrees that it contravened UMIR 7.1(6) and Policy 7.1, Part 7 by failing to adopt, document and maintain a system of risk management and supervisory controls, policies and procedures that was adequate to ensure the management of the financial, regulatory and other risks associated with electronic access to marketplaces.

C. ADMITTED FACTS

8. For the purposes of this Settlement Agreement only, Staff and the Respondent agree with and rely upon the admitted facts and conclusions which are set out in the Statement of Allegations attached as Appendix "A" to this Settlement Agreement.

D. DISPOSITION

9. For the contraventions in paragraph 7 above, Staff and the Respondent have agreed upon disposition as follows:

  (i) a fine of $170,000.00 payable by the Respondent to IIROC; and

  (ii) costs of $5,000.00 payable by the Respondent to IIROC.

E. PROCEDURES FOR ACCEPTANCE OF OFFER OF SETTLEMENT AND APPROVAL OF SETTLEMENT AGREEMENT

10. The Respondent shall have until the close of business on April 3, 2015 to accept the Offer of Settlement and serve an executed copy thereof on Staff.

11. This Settlement Agreement shall be presented to a Hearing Panel at a public hearing (the Approval Hearing) held for the purpose of approving the Settlement Agreement, in accordance with the procedures described in UMIR Policy 10.8 in addition to any other procedures as may be agreed upon between the parties. The Respondent acknowledges that IIROC shall notify the public and media of the Approval Hearing in such manner and by such media as IIROC sees fit.

12. Pursuant to Part 3.4 of UMIR Policy 10.8, the Hearing Panel may accept or reject this Settlement Agreement.

13. In the event the Settlement Agreement is accepted by a Hearing Panel, the matter becomes final, there can be no appeal or review of the matter, the disposition of the matter agreed upon in this Settlement Agreement will be included in the permanent record of IIROC in respect of the Respondent and IIROC will publish a summary of the Requirements contravened, the facts, and the disposition agreed upon in the Settlement Agreement.

14. In the event the Hearing Panel rejects the Settlement Agreement, IIROC may proceed with a hearing of the matter before a differently constituted Hearing Panel pursuant to Part 3.7 of UMIR Policy 10.8 and this Settlement Agreement may not be referred to without the consent of both parties.

15. The Respondent agrees that, in the event it fails to comply with any of the terms of the Settlement Agreement, IIROC may enforce this settlement in any manner it deems appropriate and may, without limiting the generality of the foregoing, suspend the Respondent's access to marketplaces regulated by IIROC until IIROC determines that the Respondent is in full compliance with all terms of the Settlement Agreement.

16. The Respondent agrees that neither it, nor anyone on its behalf, will make a public statement inconsistent with this Settlement Agreement.

IN WITNESS WHEREOF the parties have signed this Settlement Agreement as of the dates noted below.

DATED at Toronto, Ontario on the 1st day of April, 2015.

"Witness"   "Independent Trading Group"
Witness   **Per: Independent Trading Group Inc.**

DATED at Toronto, Ontario on the 23rd day of March, 2015.

Per: "Elsa Renzella"

Elsa Renzella

Vice-President, Enforcement

Investment Industry Regulatory Organization of Canada

Suite 2000, 121 King Street West

Toronto, Ontario M5H 3T9

This foregoing Settlement Agreement is hereby approved this 27th day of April, 2015, by the following hearing panel constituted to review the terms thereof:

Per: "Thomas Lockwood"

Panel Chair

Per: "Guenther Kleberg"

Panel Member

Per: "Leo Ciccone"

Panel Member

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APPENDIX "A"

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IN THE MATTER OF:
**The Rules of the Investment Industry Regulatory Organization of Canada
and
The Universal Market Integrity Rules
and
Independent Trading Group (ITG) Inc.**

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STATEMENT OF ALLEGATIONS

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I.   REQUIREMENTS CONTRAVENED

1. Independent Trading Group (ITG) Inc. ("Independent Trading Group") contravened Universal Market Integrity Rule ("UMIR") 7.1(6) and Policy 7.1, Part 7 by failing to adopt, document and maintain a

system of risk management and supervisory controls, policies and procedures that was adequate to ensure the management of the financial, regulatory and other risks associated with electronic access to marketplaces.

2.   Schedule "A" sets out the text of the relevant UMIR Requirements.

II.   RELEVANT FACTS AND CONCLUSIONS

Overview

3.   In 2013, IIROC implemented UMIR 7.1(6) and Policy 7.1, Part 7 – Specific Provisions Applicable to Electronic Access that, among other things, detailed the automated pre-trade controls that were expected of Participants to prevent trades from being entered that do not comply with the relevant Requirements or that cause the Participant to exceed pre-determined credit or capital thresholds.

4.   While Independent Trading Group did take steps thereafter to put in place some automated pre-trade controls and had an honest belief at the time of the Trading Error (as defined below) that appropriate automated controls were in place, those controls were not in fact calibrated and maintained in a manner that was adequate to prevent the entry of an order that would result in the firm exceeding pre-determined credit or capital thresholds.

5.   On January 21, 2014, at the open of trading on the TSX, Independent Trading Group's failure to employ adequate automated pre-trade controls to limit its financial exposure allowed for the entry of an erroneous order that resulted in an intraday capital deficiency of approximately $8 million (the "Trading Error").

6.   As set out in more detail below, Independent Trading Group's management quickly recognized the Trading Error and took immediate steps to remedy its intraday capital deficiency by covering the short position created by the Trading Error. Independent Trading Group also took immediate steps to notify IIROC staff of the Trading Error.

The Respondent

7.   Independent Trading Group is registered as an investment dealer, is a member and subscriber to IIROC-regulated marketplaces, and therefore is a Participant under UMIR.

8.   Independent Trading Group is engaged in the business of market making and proprietary trading.

The Trading Error

9.   During the TSX pre-opening session on January 21, 2014 at 9:27:07 a.m., the shares of Bank of Nova Scotia ("BNS") showed a calculated opening price ("COP") of $1000 as a result of a large market buy order entered by a Participant that created an imbalance.

10.   In response to these market conditions, a proprietary trader at Independent Trading Group (the "Trader") entered three orders to sell short 1000 shares of BNS at prices above its previous day's closing price.

11.   Shortly before the scheduled open of trading, the Trader entered a fourth order to sell short 825,000 shares of BNS at $66. The Trader inadvertently failed to modify the volume of the order, overrode an alert related to the volume of the order, and submitted the order to the marketplace 4/10ths of a second before the scheduled open of trading. The time from the Trader generating the order to entering it to the marketplace was five seconds.

12.   As a result of the Trader's erroneous order, when the shares of BNS opened for trading at 9:30 a.m., the order was filled for 586,300 shares. The Trading Error caused Independent Trading Group to become capital deficient by approximately $8 million.

The Entry of the Erroneous Order

13. The Trader entered each of the four orders by double-clicking the displayed volume of the bid on the trade-station. This generated a sell order with a bid volume equal to the displayed volume (rounded down to the nearest 1000 shares) and a limit price equal to the bid price (during the pre-open equivalent to the COP). After the order was generated, the Trader could modify the price and/or volume before submitting the order to the marketplace.

14. The Trader's trade-station had "soft" controls to prevent the entry of an order that would exceed the Trader's pre-set limits for order value, volume and price differential. If a limit was triggered by the entry of an order, an additional pop up window with the details of the alert would be generated to warn the Trader before entering the order to the marketplace. The Trader was able to override these alerts by a keyboard shortcut on the trade-station.

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17. The Trader immediately cancelled the unfilled portion of the order and contacted Independent Trading Group's Ultimate Designated Person to inform him of the error.

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ITG, who had access to an algorithmic trading program to handle large orders, was enlisted to assist in covering the short position in this manner.

20. Approximately twenty minutes after the Trading Error, the firm's senior management notified IIROC's Financial & Operations Compliance department of the capital deficiency and the steps being taken to rectify it. They then notified the Chief Financial Officer of the firm's carrying broker.

21. By 10:20, the capital deficiency was corrected by covering the short position and by 10:30, the position was closed. Independent Trading Group also earned a profit on the trading. IIROC staff is satisfied that the Trading Error and the regulatory breach that allowed it to occur were inadvertent and not calculated or intended by Independent Trading Group or the Trader to earn a profit.

Failure to Employ Automated Controls to Limit Financial Exposure

22. UMIR 7.1(6) and Policy 7.1, Part 7 require a Participant to adopt risk management and supervisory controls, policies and procedures reasonably designed to ensure the management of the financial risks associated with electronic access to marketplaces. The Rule changes implemented in 2013 also require that the risk management and supervisory controls include automated controls to prevent the entry of an order which would result in the Participant exceeding pre-determined credit or capital thresholds.

23. The firm had "soft" controls for each trader at the trade-station level, which could be overridden, once confirmed, by the traders. The firm was required to have "hard" controls on a firm-wide level that could not be modified or overridden by the traders. While the firm did have some automated pre-trade controls in place, the firm did not have in place pre-trade controls sufficient to prevent any order that exceeded pre-determined credit or capital thresholds, in particular an erroneous or "fat-finger" order.

24. Independent Trading Group mistakenly believed that its service provider for its smart order router (the "SOR Provider") had enabled firm-wide pre-trade controls to prevent an order exceeding a maximum order value. The basis for this mistaken belief was a newsletter from the SOR Provider in September 2013 that stated, among other things: "**Please note that on September 5th, 2013, [we] AUTOMATICALLY enabled 'Fat Finger' checking for all our workstation customers to try to prevent orders entered with keystroke errors." The same communication invited customers to contact the SOR Provider to enable and configure other pre-trade controls.

25. Independent Trading Group subsequently received "Fat Finger" alerts through its trading system that orders had been blocked for exceeding a maximum price difference and assumed that this was an indication that broader pre-trade controls had been put into place by its SOR Provider to prevent orders exceeding a maximum order value when this was not in fact the case.

26. Independent Trading Group did not take sufficient further steps to confirm what additional firm-wide pre-trade controls had in fact been enabled by its SOR Provider. It did not consider what capital thresholds would be appropriate based on the firm's risk tolerances and capital position, confirm what thresholds were in place with its SOR Provider, document the thresholds in its policies and procedures, or conduct any testing prior to the Trading Error to ensure that all necessary controls were in place.

Remedial Steps Taken

27. Immediately following the Trading Error, Independent Trading Group reviewed and, where necessary, ensured that automated pre-trade controls were in place at a firm-wide level for orders exceeding pre-determined credit and capital thresholds.

28. Subsequently, Independent Trading Group implemented the following measures:

    (i)   a review of all pre-trade controls and parameters in place at a trade-station and firm-wide level;

    (ii)   undertook a process to update its policies and procedures relating to electronic access to

marketplaces; and

    (iii)   adopted procedures for the regular review of pre-trade controls and parameters in place for its trading systems.

III.   CONCLUSION

29.   The Trading Error was inadvertent but resulted in serious financial exposure to Independent Trading Group. The Trading Error could have been prevented had Independent Trading Group taken reasonable additional steps to fulfill its trading supervision obligations under UMIR by employing and verifying that it had in place adequate automated controls to prevent the entry of orders which would result in the firm exceeding pre-determined credit or capital thresholds.

30.   Independent Trading Group has recognized that it did financially benefit as a result of the Trading Error and that it should not retain any financial benefit from the Trading Error as a result of its non-compliance with UMIR.

31.   The fine that Independent Trading Group has agreed to pay in this Settlement Agreement takes into account the profit earned from the Trading Error while allowing for the deduction of certain costs associated with the event and the remedial steps undertaken.

32.   The costs incurred by Independent Trading Group as a result of the breach and the remedial steps that it has undertaken include an assessment paid to the Canadian Investor Protection Fund arising from the capital deficiency, the cost of hiring a consultant to ensure its policies and procedures are properly updated, and execution fees related to covering the short position.

March 23, 2015

INVESTMENT INDUSTRY REGULATORY ORGANIZATION OF CANADA

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SCHEDULE "A"

EXCERPTS FROM THE UNIVERSAL MARKET INTEGRITY RULES

7.1   Trading Supervision Obligations

    (6)   Notwithstanding any other provision of this Rule, a Participant or Access Person shall adopt, document and maintain a system of risk management and supervisory controls, policies and procedures reasonably designed, in accordance with prudent business practices, to ensure the management of the financial, regulatory and other risks associated with:

        (a)   access to one or more marketplaces; and

        (b)   if applicable, the use by the Participant, any client of the Participant or the Access Person of an automated order system.

Policy 7.1, Part 7 – Specific Provisions Applicable to Electronic Access

Trading supervision related to electronic access to marketplaces must be performed by a Participant or Access Person in accordance with a documented system of risk management and supervisory controls, policies and procedures reasonably designed to ensure the management of the financial, regulatory and other risks associated with electronic access to marketplaces.

The risk management and supervisory controls, policies and procedures employed by a Participant or Access

Persons must include:

- *automated controls to examine each order before entry on a marketplace to prevent the entry of an order which would result in:*

  o *the Participant or Access Person exceeding pre-determined credit or capital thresholds,*

  o *a client of the Participant exceeding pre-determined credit or other limits assigned by the Participant or to that client, or*

  o *the Participant, Access Person or client of the Participant exceeding pre-determined limits on the value or volume of unexecuted orders for a particular security or class of securities;*

- *provisions to prevent the entry of an order that is not in compliance with Requirements;*

- *provision of immediate order and trade information to compliance staff of the Participant or Access Person; and*

- *regular post-trade monitoring for compliance with Requirements.*

A Participant or Access Person is responsible and accountable for all functions that they outsource to a service provider as set out in Part 11 of Companion Policy 31-103CP Registration Requirements and Exemptions.