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UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of: **BEHRUZ AFSHAR, SHAHRYAR AFSHAR, RICHARD F. KENNY, IV, FINELINE TRADING GROUP LLC and MAKINO CAPITAL LLC,** **Respondents.**	**RESPONDENT RICHARD F. KENNY, IV'S ANSWER AND AFFIRMATIVE DEFENSES TO ORDER INSTITUTING PROCEEDINGS**

Respondent, Richard F. Kenny, IV ("Kenny"), by his attorney, for his Answer and Affirmative Defenses to the Commission's Order Instituting Proceedings ("OIP") against Kenny and Behruz Afshar ("Behruz"), Shahryar Afshar ("Shahryar"), Fineline Trading Group LLC ("Fineline") and Makino Capital LLC ("Makino") (collectively, "the Afshar Respondents"), states as follows:

OIP, Paragraph 1:

1. This case involves the perpetration of two fraudulent trading schemes by Behruz, his twin brother, Shahryar, and their close friend, Kenny: the mismarking of option orders to obtain "customer priority" and "spoofing" to generate liquidity rebates. The Afshars are sophisticated options traders and former registered representatives. Kenny, during the relevant time period, was a registered representative at Lightspeed Trading, LLC ("Lightspeed"). The Afshars and Kenny conducted the schemes through two Lightspeed accounts in the name of Fineline and Makino, limited liability companies which the Afshars owned.

Answer, paragraph 1:Kenny admits that during the relevant time period he was a registered representative at Lightspeed. Kenny denies each and every remaining allegation of paragraph 1 of the OIP directed to him.[1]

[1] Many of the allegations of the OIP are not directed to Kenny so that Kenny is not required to respond thereto. To the extent that Kenny is required to respond to allegations directed to other Respondents, Kenny adopts the

OIP, Paragraph 2:

2. The first fraudulent scheme involved the mismarking of option orders to take advantage of the benefits that certain exchanges provide to non-professional, public retail investors. These exchanges, including the Chicago Board Options Exchange, the NYSE AMEX Options, the International Securities Exchange, and NASDAQ OMX PHLX ("PHLX"), require option orders from the accounts of public customers (not broker-dealers or market-makers) to be marked as either "customer" or "professional."

Answer, Paragraph 2:

Kenny admits the allegations of the second sentence of Paragraph 2 of the OIP. Kenny denies each and every remaining allegation of Paragraph 2 of the OIP directed to him.

OIP, Paragraph 3:

3. Orders marked "customer" have priority of execution over, and earn higher rebates and incur lower fees than, orders marked "professional" at the same price. A non-broker-dealer person or entity that places more than 390 orders in listed options per day (on average) - whether executed or not - on any listed options exchange during any calendar month in a quarter will be designated as a "professional" for the next quarter. Conversely, a "customer" is a non-broker-dealer person or entity that does not exceed the 390-order threshold for each calendar month in a quarter.

Answer, Paragraph 3:

Kenny admits the allegations of Paragraph 3 of the OIP.

OIP, Paragraph 4:

4. Despite far exceeding the 390-order threshold for every quarter from October 2010 to December 2012, the Respondents were able to continually place "customer" marked orders throughout this time period by shifting their trading operations on a quarterly basis between the accounts of Fineline and Makino. When Fineline was designated as "professional" for an upcoming quarter, the Afshars' trading operations transitioned that quarter to Makino's account (designated as "customer"), essentially ceasing activity in Fineline's account. Fineline's inactivity would ensure that its account fell below the 390-order threshold, thereby achieving "customer" status for the next quarter, and thus enabling the trading to continue with the benefits of "customer" designation for that subsequent quarter (while trading in Makino essentially ceased).

Answer, Paragraph 4:

The allegations of paragraph 4 of the OIP are not directed to Kenny.

OIP, Paragraph 5:

5. The Afshars and Kenny accomplished this back-and-forth scheme through false representations to Lightspeed that Behruz solely owned Fineline and that Shahryar solely owned Makino, when in fact Behruz had an ownership interest in both companies. Kenny facilitated the

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Answer to the OIP filed by those Respondents.

movement of funds and trading operations between the accounts. He also traded in the Afshars' accounts, received a portion of their trading gains, and shared his commissions with the Afshars.

Answer, Paragraph 5:
Kenny denies that he engaged in the "scheme" alleged in the OIP and therefore denies each and every allegation of Paragraph 5 of the OIP directed to him.

OIP, Paragraph 6:

6. By placing orders improperly marked as "customer," the Respondents deceived several exchanges, reaping over $2 million in transaction fees wrongly avoided and higher rebates wrongly received and unfairly disadvantaged other market participants with orders that received execution priority.

Answer, Paragraph 6:
Kenny denies each and every allegation of Paragraph 6 of the OIP directed to him.

OIP, Paragraph 7:

7. The second fraudulent scheme involved manipulative trading known as "spoofing" to collect rebates from the PHLX. During the relevant time period, the PHLX employed a "maker-taker" fee model that offered rebates for orders that provided or "made" liquidity (i.e., orders that are posted to the exchange's order book before executing against a subsequent incoming order) and charged fees for orders that "took" liquidity (i.e., orders that execute immediately against previously received, liquidity-providing orders).

Answer, Paragraph 7:
Kenny admits the allegations of the second sentence of Paragraph 7 of the OIP. Kenny denies each and every remaining allegation of Paragraph 7 of the OIP directed to him.

OIP, Paragraph 8:

8. Between May 2011 and December 2012, the Respondents placed all-or-none ("AON") orders (undisplayed orders that must be executed in their entirety or not at all) in options on the PHLX to generate liquidity rebates. The Respondents then placed smaller orders in the same option series and price as the larger AON orders, but on the opposite side of the market. These small lot orders, which were displayed, were not bona fide orders because they were not intended to be executed. Instead, they were placed to alter the option's best bid or offer ("BBO") in order to induce, or "spoof," other market participants into submitting orders at the new BBO, which would then execute against the AON orders. Upon execution of those AON orders, any open displayed orders placed by the Respondents were cancelled.

Answer, Paragraph 8:
Kenny denies each and every allegation of Paragraph 8 of the OIP directed to him.

OIP, Paragraph 9:

9. Because the executed AON orders existed prior to the entry of the other market participants' orders, they were deemed to have added liquidity and, thereby, generated rebates. In contrast, the other market participants, tricked into trading against the AON orders, were

assessed a "take" fee. As a result of this manipulative trading scheme, the Afshars reaped over $225,000 in ill-gotten rebates.

Answer, Paragraph 9:
Kenny denies each and every allegation of Paragraph 9 of the OIP directed to him.

OIP, Paragraph 10:

10. **Behruz Afshar**, age 44, of Chicago, IL, worked at Terra Nova Financial, LLC ("Terra Nova"), a registered broker-dealer, from February 1997 to August 2007. While at Terra Nova, Behruz was the firm's head trader, managing and supervising all trading operations of the broker-dealer. Behruz was also associated with another registered broker-dealer from October 2009 to December 2011. In March 2008, Behruz started his own trading company, Fineline, which began trading through a master sub-account at Terra Nova. During the relevant time period, Fineline traded through a master sub-account at Lightspeed. Behruz employed traders on an independent contracting basis to trade in Fineline's sub-accounts. Behruz held Series 3, 4, 7, 24, 53, 55, and 63 licenses.

Answer, Paragraph 10:
The allegations of Paragraph 10 of the OIP are not directed to Kenny.

OIP Paragraph 11:

11. **Shahryar Afshar**, age 44, of Chicago, IL, is the twin brother of Behruz and was registered representative with Terra Nova from 1998 to 1999, and from March 2005 to October 2005, and with various other broker-dealers from 2000 to 2004. In December 2010, together with Behruz and Kenny, Shahryar formed and took an ownership interest in Makino, which traded through a master sub-account at Lightspeed. Makino utilized the same independent contracting traders as Fineline to trade in its sub-accounts. Shahryar held Series 3, 7, 55, and 63 licenses.

Answer, Paragraph 11:
Kenny denies each and every allegation of Paragraph 11 of the OIP directed to him.

OIP, Paragraph 12:

12. **Richard F. Kenny, IV**, age 45, of Chicago, IL, was a registered representative at Terra Nova from 1996 to 1998 and from January 2005 until October 2010, when he became a registered representative at Lightspeed as a result of Lightspeed's acquisition of Terra Nova. Kenny held Series 3, 7, 24, 55, and 63 licenses. Kenny resigned from Lightspeed in December 2013, due to his refusal to formally attest that he was not sharing his commissions with any customers or non-registered individuals. In October 2014, FINRA filed a complaint against Kenny for repeatedly refusing to respond to informational requests in connection with its investigation of the Afshars' trading activity. In June 2015 FINRA issued a decision against Kenny for his failure to provide information and documents that would have identified the Afshars and bank accounts in their names or under their control. FINRA's decision, which became final in July 2015, barred Kenny from association with any FINRA member firm and ordered him to pay costs.

Answer, Paragraph 12:
Kenny admits the allegations of the first and second sentences of Paragraph 12 of the OIP. Kenny admits that in October 2014, FINRA filed a complaint against him and that in June 2015 FINRA issued a decision in that case. Kenny states that the Complaint and Decision speak for themselves. Kenny denies each and every remaining allegation of Paragraph 12 of the OIP.

OIP, Paragraph 13:

13. **Fineline Trading Group LLC** is a Nevada limited liability company that Behruz formed in December 2007. Fineline is a trading company through which Behruz, during the relevant time period, employed up to four independent contracting traders to trade in its sub-accounts. Behruz and Kenny also traded in Fineline's sub-accounts. Behruz controlled and handled all of Fineline's trading operations, risk management and accounting.

Answer, Paragraph 13:
Kenny admits that at times he entered **orders as directed by the account holder in Fineline's sub-accounts. Kenny denies each and every remaining allegation of Paragraph 13 of the OIP directed to him. The remaining allegations of Paragraph 13 of the OIP are not directed to Kenny.**

OIP, Paragraph 14:

14. **Makino Capital LLC** is a Nevada limited liability company that Shahryar, Behruz, and Kenny formed in December 2010. Makino utilized the same independent contracting traders as Fineline to trade in its master sub-account. Shahryar, Behruz, and Kenny also traded in Makino's sub-accounts. Behruz controlled and handled all trading operations, risk management and accounting for Makino.

Answer, Paragraph 14:
Kenny admits that at times he entered orders as instructed by account holder in Makino's sub-accounts. Kenny denies each and every remaining allegation of Paragraph 14 of the OIP directed to him.

OIP, Paragraph 15:

15. **Lightspeed Trading LLC** is a New York limited liability company that was formed in 1998. Lightspeed is a broker-dealer registered with the Commission pursuant to Section 15(b) of the Exchange Act. Lightspeed's principal place of business is in New York, New York; the firm also has a branch office in Chicago. Lightspeed, which acquired Terra Nova in 2010, is a member of FINRA and various exchanges.

Answer, Paragraph 15:
The allegations of Paragraph 15 of the OIP are not directed to Kenny.

OIP, Paragraph 16:

16. **Third Rail Management, Inc. ("Third Rail")** is a Nevada S corporation that Kenny formed in 2008. During the relevant time period, among other things, Third Rail's bank account facilitated monetary transfers between the checking accounts of Fineline and Makino.

Answer, Paragraph 16:
Kenny admits the allegations of the first sentence of Paragraph 16 of the OIP. Kenny denies each and every remaining allegation of Paragraph 16 of the OIP.

OIP, Paragraph 17:

17. The Afshar brothers and Kenny are close friends. They attended the same middle school and college, and had overlapping tenures at Terra Nova where Behruz was director of the firm's trading operations, and where Kenny and Shahryar were registered representatives.

Answer, Paragraph 17:
Kenny admits the allegations of Paragraph 17 of the OIP.

OIP, Paragraph 18:

18. In October 2010, Kenny became a registered representative at Lightspeed as a result of Lightspeed's acquisition of Terra Nova. Kenny, although a registered representative with Lightspeed, was considered an independent contractor or "external broker" of the firm.

Answer, Paragraph 18:
Kenny admits the allegations of Paragraph 18 of the OIP.

OIP, Paragraph 19:

19. Kenny brought with him to Lightspeed some of the customer accounts he personally serviced while at Terra Nova, including his two largest customers, Behruz and Shahryar and their accounts, most notably, Fineline.

Answer, Paragraph 19:
Kenny admits the allegations of Paragraph 19 of the OIP with the exception of the words "most notably."

OIP, Paragraph 20:

20. During his tenure at Lightspeed, Kenny, as an "external broker," was not required to work at the firm's registered office in Chicago, but operated alongside Behruz at a trading desk they leased on one of the floors of the Chicago Stock Exchange, Inc. Shahryar traded from his home or at one of the terminals at his brother's and Kenny's rented trading desk.

Answer, Paragraph 20:
Kenny admits that during his tenure at Lightspeed he was an "external broker" and was not required to work at the Firm's registered office in Chicago. Kenny further admits that he worked at a trading desk he and Behruz leased on one of the floors of the Chicago Stock Exchange, Inc. Kenny denies each and every remaining allegation of Paragraph 20 of the OIP directed to him.

OIP, Paragraph 21:

21. Kenny helped Behruz form Fineline and Makino by filing the formation documents with the state of Nevada and serving as Fineline's resident agent. Kenny was also

Fineline's registered representative at Terra Nova (and later at Lightspeed) and Makino's registered representative at Lightspeed, earning commissions on trades in their accounts. Kenny, along with Behruz, was also a signer on the companies' checking accounts and a named cardholder of Fineline's business credit card. Kenny also invested in Makino, together with the Afshars.

Answer, Paragraph 21:
Kenny admits that he filed formation documents with the state of Nevada for Fineline and Makino, that he served as Fineline's resident agent, that he was Fineline's registered representative at Terra Nova and later at Lightspeed, that he was Makino's registered representative at Lightspeed, that he earned commission on trades in the accounts of Fineline and Makin, and that he was a signer on the Fineline and Makino checking account and had a Fineline business credit card. Kenny denies each and every remaining allegations of Paragraph 21 of the OIP.

OIP, Paragraph 22:
22. During the relevant time period, Fineline and Makino employed at least four traders on an independent contracting basis to trade in the companies' sub-accounts, using trading capital provided by the Afshars.

Answer, Paragraph 22:
The allegations of Paragraph 22 of the OIP are not directed to Kenny.

OIP, Paragraph 23:
23. Generally, a master sub-account is an account at a broker-dealer where a top-level customer, in most instances a limited liability company or limited liability partnership, is allowed to have subordinate accounts for different trading activities. These subordinate, or sub-accounts, are then typically used by individual traders or groups of traders.

Answer, Paragraph 23:
Kenny admits the allegations of Paragraph 23 of the OIP.

OIP, Paragraph 24:
24. Three of the independent contracting traders of Fineline and Makino traded in the same office space in San Francisco, and the other trader was a friend of the Afshars who traded primarily alongside Behruz and Kenny at their trading desk.

Answer, Paragraph 24:
Kenny admits the allegations of Paragraph 24 of the OIP.

OIP, Paragraph 25:
25. The master sub-account arrangement with portfolio margining afforded the traders increased "buying power" and leverage as each trader could trade on margin against the value of the entire Fineline or Makino master account. The traders agreed to split their respective net gains with the Afshars on a 50/50 basis.

Answer, Paragraph 25:
The allegations of Paragraph 25 of the OIP are not directed to Kenny.

OIP, Paragraph 26:

26. Behruz oversaw all of the activity of the sub-account traders of Fineline and Makino on a real time basis, kept track of their order counts, provided operational, risk management, and technological support, as well as access to trading software to place and route orders to specific exchanges. Behruz also controlled and handled the traders' capital and managed all accounting, including determining the sub-account traders' payouts and expense reimbursements, and ensuring that the companies' trading profits (after compensating the sub-account traders) were split three ways-among himself, Shahryar, and Kenny.

Answer, Paragraph 26:
Kenny denies each and every allegation of Paragraph 26 of the OIP directed to him. The remaining allegations of Paragraph 26 are not directed to Kenny.

OIP, Paragraph 27:

27. Behruz and Kenny also kept track of, on a monthly basis, the exchanges' maker-taker pricing models and fee schedules and informed the sub-account traders of any changes.

Answer, Paragraph 27: Kenny admits the allegations of paragraph 27 of the OIP directed to him.

OIP, Paragraph 28:

28. From October 2010 to December 2013, Kenny earned approximately $2 million in commissions, of which over $1.5 million was earned from the Afshars' accounts. Kenny shared those commissions with the Afshars and personally traded in the sub-accounts of both Fineline and Makino. His conduct, which Kenny failed to disclose to Lightspeed, violated the broker-dealers' written supervisory procedures.

Answer, Paragraph 28:
Kenny admits the allegations of the first sentence of Paragraph 28 of the OIP. Kenny denies each and every remaining allegation of Paragraph 28 of the OIP directed to him.

OIP, Paragraph 29:

29. A "professional order" is defined as an order for the account of a person or entity that: (1) is not a broker or dealer in securities; and (2) places more than 390 orders in listed options per day whether executed or not on any listed options exchange on average during any calendar month of a quarter for its own beneficial account(s) ("390-order threshold"). Three hundred ninety orders is equal to the total number of orders that a person would place in a day if that person entered one order every minute from market open to market close.

Answer, Paragraph 29:
Kenny denies that allegations of the last sentence of Paragraph 29 of the OIP Kenny states that the Exchange rules speak for themselves. To the extent that the allegations of paragraph 29 of the OIP differ therefrom, Kenny denies such allegations.

OIP, Paragraph 30:

30. A "customer priority" order is defined as an order for the account of a non-broker-dealer person or entity that falls below the 390-order threshold for each calendar month in a quarter.

Answer, Paragraph 30:

Kenny states that the Exchange rules speak for themselves. To the extent that the allegations of paragraph 30 of the OIP differ therefrom, Kenny denies such allegations.

OIP, Paragraph 31:

31. All orders for multiple accounts beneficially owned or controlled by the same person or entity, and all sub-accounts of a person or entity's master account, must be aggregated when determining whether the 390-order threshold has been exceeded by that person or entity.

Answer, Paragraph 31:

Kenny states that the Exchange rules speak for themselves. To the extent that the allegations of paragraph 31 of the OIP differ therefrom, Kenny denies such allegations.

OIP, Paragraph 32:

32. A "customer priority" order is given priority of trade execution over "professional" and broker-dealer orders at the same price and, with few exceptions, ***does not incur any transaction fees [is this true]***and receives higher rebates (or pays lower fees) for adding (or removing) liquidity. Options exchanges provide these benefits to customer priority orders to attract retail order flow and level the playing field for retail investors over market professionals.

Answer, Paragraph 32:

Kenny states that the exchange rules speak for themselves. To the extent that the allegations of paragraph 32 of the OIP differ therefrom, Kenny denies such allegations.

OIP, Paragraph 33:

33. Lightspeed coded orders as "customer" or "professional" based on a quarterly counting of its customers' orders. Orders from accounts with the same beneficial ownership (including all sub-accounts under a master account) were aggregated and totaled on a per-month basis to determine whether an account exceeded the 390-order threshold. Because trading activity was reviewed quarterly to determine whether orders for an account should be represented as "professional" or "customer," a professional account one quarter can become a customer account next quarter, and vice versa, depending on the previous quarter's order count.

Answer, Paragraph 33:

The allegations of paragraph 33 of the OIP are not directed to Kenny. Kenny lacks sufficient knowledge or information to frame a response thereto and therefore denies the same.

OIP, Paragraph 34:

34. From at least December 2010 to December 2012, the Afshars and Kenny perpetrated a scheme to fraudulently maintain "customer" designation of all the orders from the Afshars' accounts without interruption despite their order counts at Lightspeed far exceeding the 390-order threshold for every month during that time period.

Answer, Paragraph 34:
Kenny denies each and every allegation of Paragraph 34 of the OIP directed to him.

OIP, Paragraph 35:

35. The scheme was accomplished by having the trading operations at Lightspeed alternate between the Fineline and Makino accounts each quarter, depending on which account was "customer" designated, with the other "professional" account conducting little to no activity.

Answer, Paragraph 35:
Kenny denies that there was any "scheme" and therefore denies each and every allegation of Paragraph 35 of the OIP.

OIP, Paragraph 36:

36. Both Kenny and Behruz knew Lightspeed's quarterly review procedures which required the aggregation of orders for all beneficially owned accounts (and their sub-accounts, if any existed). Kenny also read industry guidance regarding the requirement to aggregate orders and the exchanges' prohibition on avoiding the "professional" designation by spreading trading activity over multiple accounts.

Answer, Paragraph 36:
Kenny denies each and every allegation of Paragraph 36 of the OIP directed to him.

OIP, Paragraph 37:

37. Typically, at the end of each quarter, Kenny or Behruz sought confirmation from Lightspeed that either the Fineline or Makino account would be designated as "professional" and that the other account would "come off pro" and revert back to "customer."

Answer, Paragraph 37:
Kenny denies each and every allegation of Paragraph 37 of the OIP directed to him.

OIP, Paragraph 38:

38. After receiving confirmation from Lightspeed that the mostly dormant "professional" account would return to "customer" status at the start of the next quarter, Behruz alerted the sub-account traders of their upcoming transition to a new account and required them to wind down any open positions. Kenny ensured that the sub-account traders had trading authority and proper access credentials to seamlessly move between accounts. He also assisted the Afshars in transferring sufficient trading capital between the two master sub-accounts to enable the trading operations to continue without interruption.

Answer, Paragraph 38:
The allegations of the first sentence of Paragraph 38 of the OIP are not directed to Kenny. Kenny admits that, as part of his duties as a registered representative of Lightspeed, he ensured that traders had proper trading authority and proper access credentials for the various accounts they traded. Kenny denies each and every remaining allegation of Paragraph 38 of the OIP directed to him.

OIP, Paragraph 39:

39. To avoid account aggregation, the Afshars and Kenny misrepresented to Lightspeed that Fineline and Makino did not share common ownership, representing that Behruz was the sole beneficial owner of the former, and Shahryar was the sole beneficial owner of the latter.

Answer, Paragraph 39:
Kenny denies each and every allegation of Paragraph 39 of the OIP directed to him.

OIP, Paragraph 40:

40. In fact, Behruz had a beneficial interest in both Fineline and Makino. Fineline's account opening documents signed by Behruz and submitted to Lightspeed, listed Behruz as the only individual with a beneficial interest in the Company. Fineline's incorporation documents also reflect that Behruz was the sole managing member of the company during the relevant time period.

Answer, Paragraph 40:
The allegations of Paragraph 40 of the OIP are not directed to Kenny.

OIP, Paragraph 41:

41. For Makino, according to an email from Shahryar to Behruz and Kenny in June 2011, Behruz initially invested $27,500 in the company. At the time, this was at least a third of the total amount invested in Makino.

Answer, Paragraph 41:
The allegations of Paragraph 41 of the OIP are not directed to Kenny.

OIP, Paragraph 42:

42. Had Lightspeed known that Behruz in fact controlled and managed both companies' accounts and had a beneficial interest in Makino, or that both companies' trading profits (after paying the sub-account traders) were divided among the Afshars and Kenny, the accounts of Fineline and Makino would have been marked "professional" for every quarter during the relevant time period.

Answer, Paragraph 42:
Kenny denies each and every allegation of Paragraph 42 of the OIP directed to him.

<u>OIP, Paragraph 43</u>:

43. The scheme took shape in December 2010, when Behruz and Kenny, fully aware of the aggregation requirements of orders from beneficially owned accounts, explored ways to ensure that Fineline's trading continued in a "customer" marked account for the first quarter of 2011. Behruz and Kenny initially sought to open a new master sub-account at another broker-dealer. In mid-December 2010, Behruz forwarded to one of the sub-account traders an email from the other broker-dealer about the availability of a new master sub-account for trading by January 3, 2011, stating, "[b]elow is an email from my guy at the other BD we plan on trading soon.... In case you were wondering, we plan on having accounts open at multiple firms under different names so we can keep trading."

<u>Answer, Paragraph 43</u>:

Kenny denies each and every allegation of Paragraph 43 of the OIP directed to him.

<u>OIP, Paragraph 44</u>:

44. The idea of opening an account at the other broker-dealer was abandoned when Lightspeed's compliance department refused to approve Kenny's dual association with the other broker-dealer.

<u>Answer, Paragraph 44</u>:

Kenny denies each and every allegation of Paragraph 44 of the OIP directed to him.

<u>OIP, Paragraph 45</u>:

45. Behruz, Kenny, and Shahryar ultimately decided to form a new entity, Makino, named after a sushi restaurant in Las Vegas, Nevada that Shahryar frequented, open a master sub-account in its name at Lightspeed, and then make it appear that Makino was not beneficially owned by Fineline and/or Behruz. As Behruz explained to a sub-account trader via instant message:

Behruz:	i'm always about the money, the problem that we face is Monday [January 3, 2011] we are Pro[fessional] ...that doesn't change
Behruz:	I was ready to have a customer account for [sic] to trade in as of last week, but some powers that be may be came in and put some strain on that account so we had to go another route which will still accomplish our goal...
Behruz:	you should see all the s*** we're doing here...too funny
Sub-Account Trader:	costume party? what do you mean?
Behruz:	opening bank accounts, trading accounts, etc...
Behruz:	i think we have about I O lie here all tied to sushi names

Sub-Account Trader:	LOL
Sub-Account Trader:	you and your fish man
Sub-Account Trader:	too funny
Behruz:	i'm not even the one that came up with these damn names
Sub-Account Trader:	haha who made em up
Behruz:	my bro and rich

Answer, Paragraph 45:
Kenny denies each and every allegation of Paragraph 45 of the OIP directed to him.

OIP, Paragraph 46:
46. Kenny filed paperwork with the state of Nevada to form Makino on December 20, 2010. Those formation documents included Shahryar as the only principal of the company despite the fact that Behruz and Kenny also had a beneficial interest in the company all three each initially invested $27,500. One week later, Kenny completed and submitted an application to Lightspeed for a new master sub-account for Makino. That application, signed by Shahryar, falsely stated that Shahryar was the sole beneficial owner of Makino.

Answer, Paragraph 46:
Kenny admits that he filed paperwork with the state of Nevada to form Makino on December 20, 2010. Kenny denies each and every allegation of paragraph 46 of the OIP directed to him.

OIP, Paragraph 47:
47. Once Makino's master sub-account was approved by Lightspeed in mid-January 2011, Fineline's trading, with Behruz managing the operations and Kenny serving as the registered representative (and an unofficial sub-account trader), was able to continue as a "customer" for the first quarter of 2011 in the new Makino account and for all subsequent quarters in the relevant time period as those operations seamlessly alternated between the two accounts.

Answer, Paragraph 47:
Kenny admits that he served as to registered representative on Makino's Lightspeed account beginning in January 2011. Kenny denies each and every remaining allegation of Paragraph 47 of the OIP directed to him.

OIP, Paragraph 48:
48. By the fourth quarter of 2012, Behruz became frustrated with aggregating the sub-account traders' orders for purposes of determining the 390-order threshold, and confided in a former colleague from Terra Nova that it was time to "kill the whole idea of having these master sub setups and having individual traders being just backed and they have to monitor their order

counts. That way we don't -they don't have to f***in' bounce around" between Fineline and Makino.

Answer, Paragraph 48:
The allegations of Paragraph 48 of the OIP are not directed to Kenny.

OIP, Paragraph 49:

49. As a result, starting in January 2013, the Respondents' plan was for each sub-account trader to establish their own LLC, open an account at Lightspeed in the name of that LLC in which to trade, and have Fineline "operate as we always have, but more as a lender of capital," controller of all the "money flow," and recipient of a split of the traders' respective net gains. "The idea," as Behruz wrote, "[was] to function in a capacity where [Fineline] will not have beneficial ownership but will still be able to provide traders with the same service" and with trading capital. Moreover, each trader had to "adhere to the 390 rule or else run the risk of being coded pro-customer."

Answer, Paragraph 49:
Kenny denies that he engaged in any "plan" or "scheme" and denies that he engaged in any unlawful conduct or violated any rule, regulation, law or statute and therefore denies each and every allegation of Paragraph 49 of the OIP.

OIP, Paragraph 50:

50. The Respondents placed the following number of orders in the fourth quarter of 2011:

Month	Account Name	Account Designation	Aggregate Orders	Daily Average
October 2011	Fineline Trading Group LLC	Customer	91,250	4,345
	Makino Capital LLC	Professional	78	4
November 2011	Fineline Trading Group LLC	Customer	76,916	3,663
	Makino Capital LLC	Professional	2	0.10
December 2011	Fineline Trading Group LLC	Customer	80,134	3,816
	Makino Capital LLC	Professional	0	0

Answer, Paragraph 50:
Kenny denies each and every allegation of Paragraph 50 of the OIP directed at him.

OIP, Paragraph 51:

51. In anticipation of Fineline becoming designated as "professional" for the first quarter of 2012 based on the order counts above, Kenny began the process of reactivating the Makino sub-accounts in late December 2011.

Answer, Paragraph 51:
Kenny denies each and every allegation of Paragraph 51 of the OIP.

OIP, Paragraph 52:

52. On December 27, 2011, Kenny emailed a representative in Lightspeed's accounts department requesting log-in credentials for the Makino sub-accounts. In his email, Kenny falsely represented that only Shahryar would be trading in each of the sub-accounts and that Shahryar was the only member of Makino, attaching trade authorization forms signed by Shahryar listing only his name for each sub-account. On December 30, 2011, Kenny received the log-in credentials.

Answer, Paragraph 52:

Kenny admits the allegations of the first and last sentences of paragraph 52 of the OIP but denies each and every remaining allegation of paragraph 52 of the OIP directed to him.

OIP, Paragraph 53:

53. As part of ensuring a seamless transition of trading operations from Fineline to Makino for the start of the first quarter of 2012, Behruz transferred trading capital from Fineline to Makino through an entity owned by Kenny.

Answer, Paragraph 53:

Kenny denies each and every allegation of paragraph 53 of the OIP directed to him.

OIP, Paragraph 54:

54. On December 30, 2011, Behruz submitted a wire request to Lightspeed to transfer $420,000 from Fineline's brokerage account to its checking account. After receiving those funds, on the same day, Fineline's checking account transferred $220,000 to a checking account in the name of Third Rail, an entity Kenny owned and which helped facilitate money transfers between Fineline and Makino, with the remaining $200,000 transferred to Makino's checking account (increasing Makino's account balance to over $400,000).

Answer, Paragraph 54:

Kenny admits that he owned Third Rail. Kenny denies each and every remaining allegation of Paragraph 54 of the OIP directed to him.

OIP, Paragraph 55:

55: On January 3, 2012, Third Rail transferred $200,000 to Makino's checking account (increasing its account balance to more than $600,000). Later that day, Makino transferred $600,000 to its brokerage account at Lightspeed and Kenny emailed the sub-account traders their respective log-in credentials received from Lightspeed's accounts department to begin trading in the Makino sub-accounts.

Answer, Paragraph 55:

Kenny admits the allegations of Paragraph 55 of the OIP.

OIP, Paragraph 56:

56. The next day, January 4, Third Rail's checking account transferred $250,000 to Makino's checking account, all of which Makino then transferred to its brokerage account at Lightspeed, providing additional trading funds.

Answer, Paragraph 56:
Kenny denies each and every allegation of Paragraph 56 directed to him or Third Rail.

OIP, Paragraph 57:
Third Rail's involvement in the transfers between Fineline and Makino was intended to avoid raising suspicions that the two companies were affiliated.

Answer, Paragraph 57:
Kenny denies each and every allegation of Paragraph 57 of the OIP directed to him or Third Rail.

OIP, Paragraph 58:
58. The following shows the shifting of trading activity from Fineline's account to Makino's account (now "customer") in the first quarter of 2012:

Month	Account Name	Account Designation	Aggregate Orders	Daily Average
January 2012	Fineline Trading Group LLC	Professional	438	21
	Makino Capital LLC	Customer	97,122	4,625
February 2012	Fineline Trading Group LLC	Professional	16	0.8
	Makino Capital LLC	Customer	100,187	5,009
March 2012	Fineline Trading Group LLC	Professional	12	0.55
	Makino Capital LLC	Customer	107,232	4,874

Answer, Paragraph 58:
The allegations of Paragraph 58 of the OIP are not directed to Kenny.

OIP, Paragraph 59:
59. On March 29, 2012, Kenny requested, and received, confirmation from Lightspeed that Fineline's designation would revert back to "customer" at the start of the second quarter based on the order counts above. Later that day, Kenny requested that Lightspeed "expire" the Makino log-in credentials used by the sub-account traders and "enable" four Fineline log-in credentials, effective Monday, April 2, 2012, the first trading day of the next quarter.

Answer, Paragraph 59:
Kenny admits the allegations of paragraph 59 of the OIP.

OIP, Paragraph 60:
60. As part of transitioning the trading operations from Makino back to Fineline for the start of the second quarter of 2012, Makino transferred trading capital to Fineline. On Friday, March 30, 2012, Makino requested a wire transfer of $730,000 from its Lightspeed account to its checking account. On April 2, 2012, Makino transferred $500,000 and $80,000 to Third Rail's and Fineline's checking accounts, respectively, and Kenny emailed the sub-account traders their new log-in credentials for the re-activated Fineline sub-accounts. On April 4, 2012,

Third Rail transferred $300,000 to Fineline's checking account. Several days later, on April 9, 2012, Fineline transferred $400,000 to its Lightspeed account providing additional trading funds.

Answer, Paragraph 60:
Kenny denies each and every allegation of paragraph 60 of the OIP.

OIP, Paragraph 61:
61. The "customer priority" scheme was intended to deceive, and did deceive, the exchanges which required option orders from public customers to be designated as either "customer" or "professional." On the basis of that order designation, the exchanges determined which orders received priority of execution and the amounts of all related transaction credits and debits, including liquidity rebates, "take" fees, transaction costs, and cancellation fees. Lightspeed passed on the full amount of these credits and debits from the exchanges to the corresponding customers that placed the orders.

Answer, Paragraph 61:
Kenny denies each and every allegation of Paragraph 61 of the OIP directed to him.

OIP, Paragraph 62:
62. As a result, the customer-priority scheme netted the Afshars' accounts over $2 million in exchange fees avoided and additional rebates earned from the exchanges.

Answer, Paragraph 62:
Kenny denies that he violated any rule, regulation, law or statute and therefore denies each and every allegation of Paragraph 62 of the OIP directed to him.

OIP, Paragraph 63:
63. In addition, the scheme unfairly disadvantaged other professional market participants over whom the Respondents' "customer" orders would have wrongly received priority of execution for orders at the same price. Put another way, professional public customers placing orders at the same price as Respondents' orders would have been harmed by the Respondents' advantageous position of execution priority through the customer-priority scheme.

Answer, Paragraph 63:
Kenny denies each and every allegation of Paragraph 63 of the OIP directed to him.

OIP, Paragraph 64:
64. The Respondents' trading operations and the volume and frequency of their orders in no way resembled those of a non-professional, retail customer. The Respondents undermined the purpose of the "professional" order type, which was to level the playing field between public customers and professional traders, by wrongly claiming for themselves the benefits exchanges only offered to non-professional, public customers.

Answer, Paragraph 64:
Kenny denies each and every allegation of Paragraph 64 of the OIP directed to him.

OIP, Paragraph 65:

65. Between May 2011 and December 2012, the Respondents engaged in "spoofing" to generate rebates from the PHLX, which was a maker-taker exchange at the time. In general, spoofing describes a trader's use of "non-bona fide" orders (i.e., orders that the trader does not intend to have executed) in a security on one side of the market, which affect the price and/or volume of that security, for the purpose of inducing other market participants to execute against the trader's orders in the same security but on the opposite side of the market. The spoofing employed by the Respondents focused on options in symbols that were eligible for rebates on the PHLX.

Answer, Paragraph 65:
Kenny denies each and every allegation of Paragraph 65 of the OIP directed to him.

OIP, Paragraph 66:

66. The Respondents, or the sub-account traders under the Respondents' direction and/or supervision, entered a series of non displayed AON orders to buy (or sell) options on the PHLX in these symbols at a price that was a penny more (or less) than the option's current best bid (or offer). AON orders are undisplayed orders to buy or sell securities that must be executed in their entirety, or not executed at all. AON orders continue to remain active (and hidden) until they are executed or cancelled. Because AON orders are undisplayed, their prices do not affect the national best bid or offer ("NBBO").

Answer, Paragraph 66:
Kenny denies each and every allegation of Paragraph 66 of the OIP directed to him.

OIP, Paragraph 67:

67. The Respondents, or the sub-account traders under the Respondents' direction and/or supervision, then placed smaller, non-bona fide sell (or buy) orders typically, for one contract ("a one-lot") - on the PHLX (or a different exchange) at the same price as the AON orders, but on the opposite side of the market (the "small-lot orders"). Because the size of the small-lot orders was less than the AON orders, those orders did not execute against each other. The small-lot orders, which were displayed, were placed for the purpose of lowering (or raising) the option's best offer (or bid) by one penny in order to induce other market participants to send orders on the same side at that price level. Once other market participants joined the small-lot order with sufficient quantity, their orders executed against the AON orders. After the AON orders were filled, any open, non-bona fide, small-lot order was cancelled. Typically, the strategy was repeated on the opposite side of the market to close out the position.

Answer, Paragraph 67:
Kenny denies each and every allegation of Paragraph 67 of the OIP directed to him.

OIP, Paragraph 68:

68. Because the AON orders were posted to the PHLX's order book before executing against subsequently received orders, the PHLX credited them with having provided liquidity and paid rebates that Lightspeed passed on to the Afshars' accounts. Conversely, the orders

from the other market participants, who were "spoofed" into executing against the pre-existing AON orders, were considered to have removed liquidity and charged a "take" fee by the PHLX.

<u>**Answer, Paragraph 68**</u>**:**
Kenny denies that he engaged in any "spoofing" or otherwise violated any law, statute, rule or regulation and therefore denies each and every allegation of Paragraph 68 directed to him.

<u>OIP, Paragraph 69</u>:

69. Once the PHLX removed their maker-taker pricing schedule for "customer" marked orders effective January 2013, the AON spoofing scheme came to an end, or as Behruz summed it up, "bye bye AON fun." As a result of this scheme, the Afshars' accounts generated over $225,000 in rebates from the PHLX.

<u>**Answer, Paragraph 69**</u>**:**
Kenny denies that he engaged in any "spoofing" or otherwise violated any law, statute, rule or regulation and therefore denies each and every allegation of Paragraph 69 directed to him.

<u>OIP, Paragraph 70</u>:

70. The use of small-lot orders to spoof other market participants into executing against the non-displayed AON orders was described by Behruz as the "hidden X-A," referring to the coding of orders that earned rebates from the PHLX and "A" for adding liquidity) and described by Kenny as "bringing in the offer" (to fill AON buy orders) or "bringing in the bid" (to fill AON sell orders), as reflected in instant messages:

Behruz:	i love getting em with the hidden x-a anyhow ... bring me such pleasure and joy ... at times I roll over laughing
Sub-Account Trader:	haha
Sub-Account Trader:	yes
Sub-Account Trader:	it's a nice feeling
Sub-Account Trader:	I love it when you use NASD [to place the small-lot order] to bring the bid/offer in and then get em
Sub-Account Trader:	did you see the [Microsoft trade] [last] month?
Sub-Account Trader:	yday
Sub-Account Trader:	no liquidity
Kenny:	I didn't ... you get some?

Sub-Account Trader:	but i offered em on phlx aon and brought the bid in on phlc [sic]
Sub-Account Trader:	i LOVE doin that lol…
Kenny:	that is the finest …bringing in the bid or offer
Kenny:	makes you feel proactive!
Sub-Account Trader:	makes me feel like i was smarter than the computer haha
Kenny:	true dat

Answer, Paragraph 70:
Kenny denies that he engaged in any "spoofing" or otherwise violated any law, statute, rule or regulation and therefore denies each and every allegation of Paragraph 70 directed to him.

OIP, Paragraph 71:

71. On October 15, 2012, between 9:52:50 and 9:52:54, Kenny himself placed twelve AON orders, each to sell ten call option contracts of Ford, with November 2012 expiration and a strike price of $11.00, for $.08 on the PHLX (for a total of 120 contracts).

- At the time, the inside bid for this option series was $.07 and the inside offer was $0.09 and the bid size was over 2,400 contracts.
- The AON orders did not change the national best offer because they were not displayed to other market participants.
- Kenny placed the AON orders in one of the sub-accounts of Fineline, which was designated "customer" because its activity in the prior quarter fell below the 390-order threshold.

Answer, Paragraph 71:
Kenny admits the allegations of Paragraph 71 of the OIP. However, Kenny denies that he engaged in any "spoofing" or otherwise violated any law, statute, rule or regulation and therefore denies each and every allegation of Paragraph 71 directed to him.

OIP, Paragraph 72:

72. At 9:52:56, Kenny placed a one-lot order to purchase the same call option series in Ford for $0.08 on the PHLX from one of the sub-accounts of Makino, which at the time was designated "professional," presumably to avoid raising any suspicions of a wash trade and to decrease the likelihood of an execution (due to the lower priority of "professional" orders).

- The one-lot order raised the national best bid from $0.07 to $0.08-narrowing the NBBO spread from two cents ($0.07 x $0.09) to one cent ($0.08 x $0.09). At that one-cent spread, the bid size was only one contract-reflecting the one-lot order.

- That order was guaranteed not to execute against the AON orders because the quantity of the AON orders exceeded the one-lot.

- At 9:52:59, Kenny cancelled the one-lot order, which lowered the national best bid back to $0.07 (at which price the bid size was more than 2,300 contracts).

Answer, Paragraph 72:
Kenny denies that he engaged in any "spoofing" or otherwise violated any law, statute, rule or regulation and therefore denies each and every allegation of Paragraph 72 directed to him.

OIP, Paragraph 73:
73. At 9:56:01, Kenny placed another one-lot buy order at $0.08 in the same call option series.

- The one-lot order increased the best bid to $0.08 (at which price the bid size was again one contract).

- At 9:56:03, Kenny placed six more AON sell orders in the same call option series at $0.08 (increasing the AON sell orders to 180 total contracts).

- Between 9:56:03 and 9:56:43, other market participants submitted buy orders at $0.08 in sufficient quantities to completely fill all eighteen AON orders.

- At 9:56:43, all eighteen AON orders were executed, resulting in $46.80 in liquidity rebates for the Fineline account ($0.26 per contract).

- At 9:56:45, Kenny cancelled the open one-lot order, dropping the best bid back to $0.07.

Answer, Paragraph 73:
Kenny denies that he engaged in any "spoofing" or otherwise violated any law, statute, rule or regulation and therefore denies each and every allegation of Paragraph 73 directed to him.

OIP, Paragraph 74:
74. Behruz developed the scheme, sometimes referred to as "AON-ing," or simply "AON," after he observed non-marketable orders from the Afshars' accounts-which he believed were eligible for rebates upon their execution-executed immediately and were charged a "take" fee for removing liquidity. After learning that the orders executed against hidden orders, Behruz began testing AON orders on the PHLX.

Answer, Paragraph 74:
The allegations of paragraph 74 of the OIP are not directed to Kenny.

OIP, Paragraph 75:

75. Behruz later learned that "customer" marked AON orders were not assessed cancellation fees by the PHLX (unlike "professional" AON orders). This made the spoofing strategy economically viable because the Afshars' accounts could post AON orders and cancel them without penalty if they were not filled. As a result, in early May 2011, Behruz introduced the AON strategy to Kenny and the sub-account traders.

Answer, Paragraph 75:

Kenny denies that he engaged in any "spoofing" or otherwise violated any law, statute, rule or regulation and therefore denies each and every allegation of Paragraph 75 directed to him.

OIP, Paragraph 76:

76. On some occasions, Behruz and Kenny placed small-lot orders on the PHLX to assist the sub-account traders in filling their AON orders, typically using a different sub-account (or the account designated as "professional" at the time). Kenny told one of the sub-account traders that "as far as AON goes, [Behruz] and i love to help. i love to positions [sic] get closed."

Answer, Paragraph 76:

Kenny denies that he engaged in any "spoofing" or otherwise violated any law, statute, rule or regulation and therefore denies each and every allegation of Paragraph 76 directed to him.

OIP, Paragraph 77:

77. At times, the sub-account traders requested this assistance and other times, Behruz and Kenny proactively offered it. For example, Kenny wrote one sub-account trader: "that you AONing in MSFT? i'm gonna prop it up and get u filled" and, on another occasion, wrote: "lemme help you out. Load up your aons." Similarly, Behruz corresponded with a trader:

Behruz:	i'd rather do the phlx aon on that and bring the offer in
Sub-Account Trader:	ok...
Sub-Account Trader:	10 50 lots
Behruz:	yes
Sub-Account Trader:	ok done
Behruz:	when you're done we'll cancel the lot
Behruz:	that's my offer
Sub-Account Trader:	k

Behruz: come here kitty kitty

Behruz: they are afraid :)

Answer, Paragraph 77:
Kenny denies that he engaged in any "spoofing" or otherwise violated any law, statute, rule or regulation and therefore denies each and every allegation of Paragraph 77 directed to him.

OIP, Paragraph 78:

78. Market participants were deceived when they interpreted the small-lot orders as reflecting genuine demand or supply and joined those orders with hopes of offering liquidity and earning rebates. Instead, their orders often executed against the hidden AON orders and resulted in "take" fees. These market participants were deceived into executing against AON orders placed from the Afshars' accounts at prices that had been artificially raised (or lowered) by those same accounts.

Answer, Paragraph 78:
Kenny denies that he engaged in any "spoofing" or otherwise violated any law, statute, rule or regulation and therefore denies each and every allegation of Paragraph 78 directed to him.

OIP Paragraph 79:

79. In fact, one market participant alerted the PHLX about being deceived by such trading. On October 31, 2012, a trader at a registered broker-dealer, market-maker, and proprietary trading firm, notified her supervisor, the head of the firm's U.S. options market making ("Head Trader #1"), that "[t]oday we saw in GE us remove large size on PHLX using quotes. We join a 1-lot bid and end up removing liquidity via 10-lot trades (the 1-lot remains). Last time we saw this behavior the exchange verified that we had crossed with an ALL-or-NONE order. I am curious if it is the same case here and if the counterparty we execute against is the same firm that has a 1-lot bid in the depth."

Answer, Paragraph 79:
Kenny denies that he engaged in any "spoofing" or otherwise violated any law, statute, rule or regulation and therefore denies each and every allegation of Paragraph 79 directed to him.

OIP Paragraph 80:

80. Unbeknownst to the firm, on October 31, 2012, from 12:29:31 to 12:29:43, Kenny, in one of Fineline's sub-accounts, placed twenty-four AON orders on the PHLX, each to sell ten contracts of GE (with November 2012 expiration and strike price of $22.00) for $0.07 (for a total of 240 contracts). At the time, the inside bid for this option was $0.06 (with a size of 1,897 contracts) and the inside ask was $0.08 (at 5,291 contracts). At 12:29:47, Kenny, from one of Makino's sub-accounts, placed a one-lot order on the PHLX to buy the same option at $0.07. That one-lot order raised the inside bid from $0.06 to $0.07 (with a bid size of one contract).

<u>Answer, Paragraph 80</u>:
Kenny denies that he engaged in any "spoofing" or otherwise violated any law, statute, rule or regulation and therefore denies each and every allegation of Paragraph 80 directed to him.

<u>OIP, Paragraph 81</u>:

81. In response to that price movement, at 12:34:38, the firm's trading algorithm joined the one-lot order with an order to buy 130 contracts of the November 2012 GE option at $0.07 to provide liquidity at the new bid and potentially earn rebates. However, rather than providing liquidity, the firm's order immediately executed in full against thirteen of the preexisting twenty-four AON orders placed by Kenny. The firm's order thus removed liquidity and was charged a "take" fee by the PHLX. At 12:36:36, Kenny cancelled the one-lot order, moving the inside bid back to $0.06 (with a size of 602 contracts).

<u>Answer, Paragraph 81</u>:
Kenny denies that he engaged in any "spoofing" or otherwise violated any law, statute, rule or regulation and therefore denies each and every allegation of Paragraph 81 directed to him.

<u>OIP, Paragraph 82</u>:

82. Several hours later, after being informed of these findings, Head Trader #1 emailed individuals at the PHLX about his concerns: "[W]e have encountered some strange trading behavior recently on PHLX. It appears like we are trading against hidden AON orders, and we believe that someone might be manipulating the market. Here is one example from today that we found in GE, all timestamps are CST. Before the trades happened, the PHLX BBO was .07 bid at .08. The volume on the .07 bid was 1 contract. We tried to join the .07 bid for a size of 130 contracts, and we immediately traded 13 times, each trade was for 10 contracts. We are particularly concerned that a market participant is entering an order to buy at .07 (not AON), and then they are layering many orders to sell at .07 using an AON contingency."

<u>Answer, Paragraph 82</u>:
Kenny denies that he engaged in any "spoofing" or otherwise violated any law, statute, rule or regulation and therefore denies each and every allegation of Paragraph 82 directed to him.

<u>OIP, Paragraph 83</u>:

83. As a result of the conduct described above, Behruz and Kenny willfully violated, and Shahryar, Fineline, and Makino violated, Sections 17(a)(l) and 17(a)(2) of the Securities Act as well as Section 10(b) of the Exchange Act and Rules 10b-5(a), 10b-5(b), and 10b-5(c) thereunder, which prohibit fraudulent conduct in the offer and sale of securities and in connection with the purchase or sale of securities.

<u>Answer, Paragraph 83</u>:
Kenny denies each and every allegation of Paragraph 83 directed to him.

OIP, Paragraph 84:

84. As a result of the conduct described above, alternatively, Behruz willfully aided and abetted and caused Shahryar's, Fineline's, and Makino's violations of Sections l7(a)(1) and l 7(a)(2) of the Securities Act as well as Section IO(b) of the Exchange Act and Rules 10b-5(a),Ob-5(b), and I5(c) thereunder.

Answer, Paragraph 84:
The allegations of Paragraph 84 of the OIP are not directed to Kenny.

OIP, Paragraph 85:

85. As a result of the conduct described above, alternatively, Kenny willfully aided and abetted and caused Behruz's, Shahryar's, Fineline's, and Makino's violations of Sections l7(a)(l) and 17(a)(2) of the Securities Act as well as Section l0(b) of the Exchange Act and Rules 10b-5(a), 10b-5(b), and 10b-5(c) thereunder.

Answer, Paragraph 85:
Kenny denies each and every allegation of Paragraph 85 of the OIP directed to him.

OIP, Paragraph 86:

86. As a result of the conduct described above, alternatively, Shahryar caused Makino's violations of Sections 17(a)(l) and 17(a)(2) of the Securities Act as well as Section l0(b) of the Exchange Act and Rules 10b-5(a), 10-5(b), and 10b-5(c) thereunder.

Answer, Paragraph 86:
The allegations of Paragraph 86 of the OIP are not directed to Kenny.

OIP, Paragraph 87:

87. As a result of the conduct described above, alternatively, Behruz, Shahryar, and Kenny acted through or by means of Fineline and Makino, as well as Lightspeed, and as a result, Behruz and Kenny willfully violated, and Shahryar violated, Section 20(b) of the Exchange Act, which prohibits a person, directly or indirectly, from doing any act or thing which it would be unlawful for such person to do under the Exchange Act or any rule or regulation thereunder, through or by means of any other person, and Section 10(b) of the Exchange Act and Rules 10b-5(a), 10b-5(b), and 10b-5(c) thereunder.

Answer, Paragraph 87:
Kenny denies each and every allegation of Paragraph 87 directed to him.

OIP, Paragraph 88:

88. As a result of the conduct described above, Behruz and Kenny willfully violated, and Shahryar, Fineline, and Makino violated, Sections 17(a)(l) and 17(a)(3) of the Securities Act as well as Sections 9(a)(2) and IO(b) of the Exchange Act and Rules 10b-5(a) and 10b-5(c) thereunder, which prohibit fraudulent conduct in the offer and sale of securities and in connection with the purchase or sale of securities.

Answer, Paragraph 88:
Kenny denies each and every allegation of Paragraph 88 directed to him.

OIP, Paragraph 89:

89. As a result of the conduct described above, alternatively, Behruz willfully aided and abetted and caused Shahryar's, Fineline's, and Makino's violations of Sections l7(a)(l) and 17(a)(3) of the Securities Act as well as Sections 9(a)(2) and l0(b) of the Exchange Act and Rules 10b-5(a) and 10b-5(c) thereunder.

Answer, Paragraph 89:
The allegations of Paragraph 89 of the OIP are not directed to Kenny.

OIP, Paragraph 90:

90. As a result of the conduct described above, alternatively, Kenny willfully aided and abetted and caused Behruz's, Shahryar's, Fineline's, and Makino's violations of Sections 7(a)(l) and 17(a)(3) of the Securities Act as well as Sections 9(a)(2) and 10(b) of the Exchange Act and Rules 10b-5(a) and 10b-5(c) thereunder.

Answer, Paragraph 90:
Kenny denies each and every allegation of Paragraph 90 directed to him.

OIP Paragraph 91:

91. As a result of the conduct described above, alternatively, Shahryar caused Makino's violations of Sections 17(a)(l) and 17(a)(3) of the Securities Act as well as Sections 9(a)(2) and l0(b) of the Exchange Act and Rules 10b-5(a) and 10b-5(c) thereunder.

Answer, Paragraph 91:
The allegations of Paragraph 91 of the OIP are not directed to Kenny.

OIP, Paragraph 92:

92. As a result of the conduct described above, alternatively, Behruz, Shahryar, and Kenny acted through or by means of Fineline and Makino, and as a result, Behruz and Kenny willfully violated, and Shahryar violated, Sections 20(b), 9(a)(2), and 1 0(b) of the Exchange Act and Rules 10b-5(a) and 10b-5(c) thereunder.

Answer, Paragraph 92:
Kenny denies each and every allegation of Paragraph 92 directed to him.

Wherefore, Respondent Richard F. Kenny, IV, requests that the OIP be dismissed with prejudice against him and that judgment be entered on the OIP in his favor and against the Commission.

AFFIRMATIVE DEFENSES

I.
AFFIRMATIVE DEFENSES RELATING TO THE "CUSTOMER-PRIORITY SCHEME"

First Affirmative Defense
(Rule Not Applicable to Customers)

1. An alleged violation of the 390-order rule cannot support a claim for fraud against Kenny when the 390-order rule does not place any affirmative obligation on customers, but instead requires members to mark orders as customer or professional.

Second Affirmative Defense
(No Violation of 390-Order Rule)

2. Kenny at no time violated the 390-order rule or aided or abetted such a violation.

Third Affirmative Defense
(Rule Violation Not Fraudulent)

3. Even if the Commission could somehow show that Kenny violated an exchange rule, which it cannot, this alleged violation does not support a claim for securities fraud.

4. The Commission in its OIP conflates an exchange rule violation with fraud, but the Second Circuit has explicitly rejected this reasoning in *U.S. v. Finnerty*, 533 F.3d 143 (2nd Cir. 2008), precedent to which the Commission adhered in subsequent administrative proceedings.

5. The 390-order rule amounted to simply a regulatory change, and accordingly, violation of the rule does not equate to securities fraud.

Fourth Affirmative Defense
(390-Order Rule Not Applicable to Accounts With Differing Ownership)

6. There was no violation of the 390-order rule because there was no common beneficial ownership between Fineline and Makino.

7. The 390-order rule requires members to aggregate accounts with common "beneficial ownership" when counting orders. The trading here was done by independent traders, in different subaccounts, in turn owned by two different master accounts, owned by two different entities (Fineline and Makino), with each such entity having different ultimate ownership. Additionally, the Commission has not shown and cannot show any profit sharing between these entities that might suggest common beneficial ownership.

Fifth Affirmative Defense
(390-Order Rule Impermissibly Vague As Applied)

8. The 390-order rule is impermissibly vague and therefore cannot be used as a basis for imposing liability on Kenny.

Sixth Affirmative Defense
(Lack of Notice of New Interpretation of the Rule)

9. There can be no finding of customer liability and no imposition of any sanction based on the novel interpretation of the 390-order rule offered by the Commission when there has been no formal Commission precedent or official guidance that would put customers on notice. *See WHX Corp. v. SEC*, 362 F.3d 854, 860 (D.C. Cir. 2004).

Seventh Affirmative Defense
(Limited Enforcement of Exchange Rules)

10. The Commission has no authority to enforce exchange rules against non-members.

11. Section 8A of the Securities Act and Section 21C of the Securities Exchange Act allow the Commission to institute cease-and-desist administrative proceedings only for violation of the Acts and Commission rules and regulations thereunder, not for violation of an exchange rule.

12. To the extent Congress has given the Commission any authority to enforce exchange rules, Congress has carefully limited such authority in Section 21(d)(1) to allow civil actions only against exchange members and associated persons, that is, for violation of "the rules of a national securities exchange ... of which such person is a member or a person associated with a member."

13. Congress has further restricted Commission action in Section 21(f) by providing that the Commission may only enforce the rules of a self-regulatory organization where the organization appears "unable or unwilling to take appropriate action against" the violator of its own rule, or where some other particular circumstance makes such action necessary or appropriate.

Eighth Affirmative Defense
(Duplicative Damage Calculation)

14. The Commission in pursuing disgorgement damages seeks to collect both avoided fees, implying that the trades in question would still have occurred even had the orders been marked professional, as well as assessed commissions, implying that the trades would not have occurred had the orders been marked professional.

15. Calculating damages in such a way is duplicative and at odds with basic tenets of disgorgement damages.

II.

AFFIRMATIVE DEFENSES RELATING TO THE "SPOOFING SCHEME"

Ninth Affirmative Defense

(At-Risk Trading Not Manipulative)

16. The trading allegedly constituting a "spoofing scheme" was not manipulative when Kenny properly participated in a sophisticated market and utilized common, well-known trading strategies, such as price discovery, "all-or-none" orders, and fee and rebate analysis. Lawful at-risk orders that can or do result in actual trades do not become manipulative based simply on the fact that the trader is motivated by economic self-interest and pursuing some trading strategy.

Tenth Affirmative Defense

(No Spoofing)

17. Trading by Kenny does not constitute manipulative spoofing based on the Commission's own interpretation of market manipulation rules and regulations.

III.

AFFIRMATIVE DEFENSES RELATING TO ALL CLAIMS

Eleventh Affirmative Defense

(No Scienter)

18. Kenny did not act with the requisite scienter to support a securities fraud claim.

Twelfth Affirmative Defense

(Procedural Due Process)

19. Use of the administrative forum for a case of this nature will severely prejudice Kenny and deny him due process of law in violation of the Fifth Amendment to the Constitution.

Thirteenth Affirmative Defense

(Executive Power and Appointments)

20. SEC administrative proceedings violate Article II of the Constitution because SEC ALJs have not been appointed by the SEC Commissioners.

Fourteenth Affirmative Defense
(Right to Jury Trial)

21. Where the government seeks a civil penalty, the Supreme Court has held in *Tull v. U.S.*, 481 U.S. 412 (1987), that the Seventh Amendment guarantees the citizen the right to trial by jury.

Fifteenth Affirmative Defense

22. At all times, Kenny entered orders for customer accounts only at the direction of the customer.

Sixteenth Affirmative Defense

23. Kenny's actions as a registered representative for his customers' accounts cannot be the basis of complaint against him under the securities laws.

Seventeenth Affirmative Defense

24. The Division of Enforcement cannot prove the amount of disgorgement damages it seeks from Kenny.

Wherefore, Respondent Richard F. Kenny, IV, requests that the OIP be dismissed with prejudice against him and that judgment be entered on the OIP in his favor and against the Commission.

Dated: January 15, 2016.

RICHARD F. KENNY, IV

By: Howard Stein
His Attorney

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[redacted]

CERTIFICATE OF SERVICE

Howard J. Stein hereby certifies that on January 15, 2016, he served the original and three copies of the foregoing Respondent Kenny's Answer and Affirmative Defenses to the Order Instituting Proceedings upon Brent J. Fields, Secretary, Securities and Exchange Commission, 100 F Street, N.E. Washington, D.C. 20549 by facsimile and by Federal Express overnight delivery; with a copy thereof served by electronic delivery to the Honorable Cameron Elliot, Administrative Law Judge, Securities and Exchange Commission, 100 F Street, N.E., Washington, D.C. 20549; and with copies electronic delivery (by agreement of the parties) to the following attorneys of record:

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