

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 34-79579 / December 16, 2016

ADMINISTRATIVE PROCEEDING
File No. 3-17732

In the Matter of

ANTHONY B. KERRIGONE

Respondent.

**ORDER INSTITUTING CEASE-AND-
DESIST PROCEEDINGS PURSUANT TO
SECTION 21C OF THE SECURITIES
EXCHANGE ACT OF 1934, MAKING
FINDINGS, AND IMPOSING A CEASE-
AND-DESIST ORDER**

I.

The Securities and Exchange Commission (“Commission”) deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 21C of the Securities Exchange Act of 1934 (“Exchange Act”), against Anthony B. Kerrigone (“Kerrigone” or the “Respondent”).

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the “Offer”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over him and the subject matter of these proceedings, which are admitted, and except as provided herein in Section V, Respondent consents to the entry of this Order Instituting Cease-And-Desist Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings, And Imposing A Cease-And-Desist Order (“Order”), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds¹ that:

A. SUMMARY

1. This proceeding arises out of the trading practices of the proprietary trading group at Wilson-Davis & Co. ("WDCO") and WDCO's violations of Rule 203 of Regulation SHO.

2. From at least November 2011 through May 2013, WDCO willfully² violated Regulation SHO by taking advantage of the bona-fide market making exception to the "locate" requirement for short sales in Rule 203(b)(2)(iii) without being entitled to rely on the exception. Rule 203(b)(1) of Regulation SHO requires a broker-dealer, prior to effecting a short sale in an equity security for its own account, to "locate" a source of borrowable securities that can be delivered on the date that delivery is due, and document such locate. Rule 203(b)(2)(iii) provides a limited exception to the locate requirement for short sales effected by a market maker in connection with bona-fide market making activities in the securities for which the exception is claimed. During the relevant time, WDCO considered all of its proprietary trading to be bona-fide market making activity, and relied on the bona-fide market making exception in Rule 203(b)(2)(iii). This reliance was improper for certain WDCO trades because WDCO's proprietary trading was not, in fact, bona-fide market making. As a result, WDCO violated Rule 203(b)(1) of Regulation SHO. While improperly availing itself of the bona-fide market making exception, WDCO engaged in numerous short sales in over-the-counter equity securities which resulted in significant and improper trading profits.

3. Kerrigone, a proprietary trader at WDCO, is a WDCO representative who caused WDCO's Regulation SHO violations by executing certain short sales of securities on behalf of WDCO without WDCO being engaged in bona-fide market making activity and without WDCO obtaining a locate prior to effecting the short sales. Kerrigone improperly relied on the bona-fide market making exception for certain short sale trades without having a reasonably sufficient understanding of the rule, without sufficiently discussing with anyone at WDCO whether such trading qualified WDCO for the bona-fide market making exception, and by conducting such trading in a manner that closely resembled examples explicitly identified by the Commission—years before the conduct at issue—as activity that generally is not bona-fide market making.

B. RESPONDENT

¹ The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

² A willful violation of the securities laws means merely "that the person charged with the duty knows what he is doing." *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000) (quoting *Hughes v. SEC*, 174 F.2d 969, 977 (D.C. Cir. 1949)). There is no requirement that the actor "also be aware that he is violating one of the Rules or Acts." *Id.* (quoting *Gearhart & Otis, Inc. v. SEC*, 348 F.2d 798, 803 (D.C. Cir. 1965)).

4. Kerrigone, age 45, lives in Greenwood Village, Colorado. He was associated with and was a proprietary trader at WDCO from approximately September 2008 until approximately June 2013. During that time he was an independent contractor for WDCO and worked out of WDCO's office in Centennial, Colorado. Kerrigone holds, and at all relevant times held, Series 7, 55 and 63 securities licenses, and he was associated with several broker-dealers before he was associated with WDCO, including ones in New Jersey, New York and Florida between 1995 and 2008. Kerrigone has a disciplinary history with the Financial Regulatory Authority ("FINRA"), formerly known as the National Association of Securities Dealers, Inc..

C. FACTS

(1) **Regulation SHO's Locate Requirement**

5. Regulation SHO, the Commission's short sale regulation, was adopted, in part, to address problems associated with persistent "fails to deliver" and potentially abusive "naked" short selling. Short selling involves a sale of a security that the seller does not own or a sale which is consummated by the delivery of a security borrowed by, or for the account of, the seller. In a "naked" short sale, however, the short seller does not borrow securities in time to make delivery to the buyer within the standard T+3 settlement cycle.

6. Rule 203(b)(1) of Regulation SHO prohibits a broker-dealer from accepting a short sale order in an equity security from another person (or effecting a short sale in an equity security for its own account), unless the broker-dealer has "(i) [b]orrowed the security, or entered into a bona-fide arrangement to borrow the security; or (ii) [r]easonable grounds to believe that the security can be borrowed so that it can be delivered on the date delivery is due; and (iii) [d]ocumented compliance with this [requirement]." ³ This is generally referred to as the "locate" requirement.

7. Rule 203(b)(2)(iii) of Regulation SHO provides an exception from the "locate" requirement for short sales effected by a market maker in connection with bona-fide market making activities in the security for which this exception is claimed. ⁴ The bona-fide market making exception under Rule 203(b)(2)(iii) of Regulation SHO is available only to U.S.-registered broker-dealers that are market makers engaged in bona-fide market making activities. This narrow exception is provided because market makers engaged in market making activities may need to facilitate customer orders in a fast moving market without possible delays associated with complying with the locate requirement. ⁵

8. Section 3(a)(38) of the Exchange Act defines the term "market maker" as "any specialist permitted to act as a dealer, any dealer acting in the capacity of block positioner, and any dealer who, with respect to a security, holds himself out (by entering quotations in an inter-dealer

³ 17 CFR 242.203(b)(1).

⁴ 17 CFR 242.203(b)(2)(iii).

⁵ See Exchange Act Release No. 50103 (July 28, 2004), 69 Fed. Reg. 48008, 48015 (Aug. 6, 2004) ("Regulation SHO Adopting Release").

communications system or otherwise) as being willing to buy and sell such security for his own account on a regular or continuous basis.” The Commission has stated, “a market maker engaged in bona-fide market making is a ‘broker-dealer that deals on a regular basis with other broker-dealers, actively buying and selling the subject security as well as regularly and continuously placing quotations in a quotation medium on both the bid and ask side of the market.’”⁶

9. For purposes of claiming the bona-fide market maker exception to the locate requirement, a market maker must be a market maker in the security being sold, and must also be engaged in bona-fide market making in that security at the time of the short sale. Determining whether or not a market maker is engaged in bona-fide market making “depends on the facts and circumstances of the particular activity.”⁷

10. In the adopting release to the 2008 Amendments to Regulation SHO, which the Commission issued approximately three years prior to the trading by WDCO that is at issue in this Order, the Commission provided examples of the types of activities that indicate that a market maker is engaged in bona-fide market making activities for purposes of claiming the bona-fide market making exception to the locate requirement in Rule 203(b)(1). Indicia that a market maker is engaged in bona-fide market making include: (i) if a market maker incurs economic or market risk with respect to the securities (e.g., by putting their own capital at risk to provide continuous two-sided quotes in markets); (ii) a pattern of trading that includes both purchases and sales in roughly comparable amounts to provide liquidity to customers or other broker-dealers; and (iii) continuous quotations that are at or near the market on both sides and that are communicated and represented in a way that makes them widely accessible to investors and other broker-dealers.⁸

11. Indicia that a market maker is not engaged in bona-fide market making include: (i) activity that is related to speculative selling strategies or investment purposes of the broker-dealer and is disproportionate to the usual market making patterns or practices of the broker-dealer in that security; (ii) where a market maker posts continually at or near the best offer, but does not also post at or near the best bid; and (iii) where a market maker that continually executes short sales away from its posted quotes.⁹

12. For purposes of qualifying for the locate exception in Regulation SHO, a market maker must also be a market maker in the security being sold, and must be engaged in bona-fide market making in that security at the time of the short sale.¹⁰ Further, it is incumbent on the person asserting an exemption to demonstrate eligibility for the exemption.

(2) Improper Use of the Bona Fide Market Making Exception

⁶ See, e.g., Exchange Act Release No. 58775 (Oct. 17, 2008), 73 Fed. Reg. 61690 (Oct. 17, 2008) (“2008 Amendments to Regulation SHO”).

⁷ See 2008 Amendments to Regulation SHO at 61699.

⁸ *Id.*

⁹ *Id.*

¹⁰ *Id.*

13. During the relevant time period, WDCO was comprised of two trading groups: a retail trading group and a proprietary trading group. The activity that is the subject of this Order pertains to trading that was within WDCO's proprietary trading group. Traders in the proprietary trading group had agreements with WDCO under which the traders were allowed to use WDCO funds for proprietary trades of securities and would split their profits with WDCO in accordance with their agreements. From 2008-2013, WDCO had an Independent Contractor Agreement with Kerrigone, under which Kerrigone received a portion of the net trading profits generated from his trades on behalf of WDCO and with WDCO funds.

14. At all relevant times, WDCO self-cleared the trading by its proprietary trading group. Kerrigone used firm funds to trade securities, including over-the-counter securities on OTC Link (formerly known as Pink Sheets). WDCO gave Kerrigone an undocumented guideline on the total market exposure that Kerrigone could have in his proprietary trading account at any given time and that guideline was adjusted from time to time by the WDCO principals.

15. When trading at least some over-the-counter securities, Kerrigone would post quotations for the securities on OTC Link and would then trade the securities on OTC Link and other trading venues. For at least some of his proprietary trading, Kerrigone targeted over-the-counter securities that exhibited high price volatility. Short selling was a critical aspect of his trading strategy for certain stocks and allowed him and WDCO to make large profits.

16. Before proprietarily trading in a security, Kerrigone submitted a one-page, internal market maker application that had to be approved by a firm principal. After this application was approved, Kerrigone could trade that security through his WDCO proprietary trading account.

17. Without further analysis, WDCO and Kerrigone considered his proprietary trading activity to be bona-fide market making activity under Regulation SHO and relied upon the bona-fide market making exception to the locate requirement.

18. WDCO and Kerrigone took no steps to confirm that Kerrigone's trading was, in fact, bona-fide market making activity.

19. While WDCO's policies and practices required its proprietary traders to have two-sided quotations and to engage in trading activity in the securities for which they were registered as a market maker, neither WDCO nor Kerrigone took steps to ensure that Kerrigone's quoting activity constituted bona-fide market making activity. For example, WDCO did not review Kerrigone's quotations to determine whether Kerrigone's activities indicated that he was engaged in bona fide market making activities for purposes of claiming the exception to Regulation SHO's locate requirement (e.g., quotations were continuous and at or near both the best bid and the best offer), and Kerrigone did not sufficiently discuss or otherwise review his quotation activity with anyone to ensure that it qualified for the bona-fide market making exception.¹¹ Nor did WDCO or

¹¹ See 2008 Amendments to Regulation SHO at 61699.

Kerrigone review the short sales that he executed away from his posted quotes to determine if they affected whether Kerrigone's trading qualified for the bona-fide market making exception.¹²

20. For some of his most profitable proprietary trading, Kerrigone posted quotations on the OTC Link for, sent and received trade messages regarding, and traded in, various over-the-counter equity securities. However, some of his quoting and trading activity did not comport with the Regulation SHO indicia that a market maker is engaged in bona-fide market making as set forth in the adopting release to the 2008 Amendments to Regulation SHO.¹³ Furthermore, the adopting release to the 2008 Amendments to Regulation SHO provide guidance on trading activity that does not qualify as bona-fide market making and Kerrigone's short sale trading in certain stocks conformed to some of the factors describing non-bona-fide market making activity.¹⁴ Specifically, Kerrigone posted quotations on behalf of WDCO on OTC Link for a security. However, contrary to the guidance in the Commission's Regulation SHO Adopting Release and the 2008 Amendments to Regulation SHO, those quotations were often not at or near the market on both sides. Furthermore, on many days, Kerrigone posted a bid quotation for WDCO at or near the market for that security, but failed to post an offer quotation at or near the market. In addition, while he was updating his bid quotation for the security during the trading day, Kerrigone made few or no changes to his offer quotation throughout the entire trading day, at times not changing an offer quotation that was far away from the market, despite substantial movement in the price of the security. Finally, while purportedly making a market for some securities, Kerrigone executed numerous short sales away from his posted offer quotations.

21. Neither WDCO nor Kerrigone ever located a security before Kerrigone executed a short sale, improperly relying on the bona-fide market making exception to Rule 203(b)(1)'s locate requirement for numerous short sales.

22. As an experienced trader who has been in the industry since before Regulation SHO was adopted, Kerrigone knew about the bona-fide market making exception to the locate requirement in Regulation SHO and knew he and WDCO were relying on the exception to execute his short sales without obtaining a locate. However, he did not have a sufficiently accurate understanding of what the exception required and he did not make reasonably sufficient efforts to make sure that he understood the Rule. Furthermore, he did not make reasonably sufficient efforts to discuss his trading activity with others or ensure that others were reviewing his trading activity so that he could reasonably believe that he was using the exception appropriately. In fact, some of Kerrigone's trading activity did not match the examples of types of trading activity that is bona-fide market making and/or did match the examples of types of trading activity that is not bona-fide market making from the adopting release to the 2008 Amendments to Regulation SHO: continuous quotations that are at or near the market on both sides is an indicia that a market maker is engaged in bona-fide market making activity; and continually executing short sales away from its posted quotes is indicia that market maker is not engaged in bona-fide market making.

¹² *Id.*

¹³ *Id.*

¹⁴ *Id.*

23. WDCO violated, and Kerrigone caused WDCO's violations of, Rule 203(b)(1) of Regulation SHO during the relevant period, resulting in substantial trading profits from the short sales.

D. UNDERTAKINGS

Respondent has undertaken to:

24. Kerrigone shall cooperate fully with the Commission in any and all investigations, litigations or other proceedings relating to or arising from the matters described in this Order.

25. In connection with such cooperation, Kerrigone shall (a) produce, without service of a notice or subpoena, any and all non-privileged documents and other information requested by the Commission's staff; (b) be interviewed (with the presence of counsel) by the Commission's staff at such times as the staff reasonably may request and to appear and testify without service of a notice or subpoena in such investigations, litigations, hearings or trials as may be requested by the Commission's staff; and (c) in connection with any testimony of Kerrigone to be conducted at deposition, hearing or trial pursuant to a notice or subpoena, agree that any such notice or subpoena for Kerrigone's appearance and testimony may be served by regular mail on his counsel.

In determining whether to accept the Offer, the Commission has considered these undertakings.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent's Offer.

Accordingly, it is hereby ORDERED that:

A. Pursuant to Section 21C of the Exchange Act, Respondent Kerrigone cease and desist from committing or causing any violations and any future violations of Rule 203(b) of Regulation SHO.

B. Respondent Kerrigone shall pay disgorgement of \$486,840, prejudgment interest of \$63,160.50 and civil penalties of \$50,000, to the Securities and Exchange Commission for transfer to the general fund of the United States Treasury, subject to Exchange Act Section 21F(g)(3). Payment shall be made in the following installments:

- (1) \$300,000.50 within 10 days of the entry of the Order;
- (2) \$75,000 within 90 days of the entry of the Order;
- (3) \$75,000 within 180 days of the entry of the Order;
- (4) \$75,000 within 270 days of the entry of the Order; and
- (5) \$75,000 within 360 days of the entry of the Order.

If any payment is not made by the date the payment is required by this Order, the entire outstanding balance of disgorgement, prejudgment interest, and civil penalties, plus any additional interest accrued pursuant to SEC Rule of Practice 600 and pursuant to 31 U.S.C. 3717, shall be due and payable immediately, without further application.

Payments must be made in one of the following ways:

- (1) Respondent may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;
- (2) Respondent may make direct payment from a bank account via Pay.gov through the SEC website at <http://www.sec.gov/about/offices/ofm.htm>; or
- (3) Respondent may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center
Accounts Receivable Branch
HQ Bldg., Room 181, AMZ-341
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying Kerrigone as the Respondent in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to Jay Scoggins, Assistant Director, Division of Enforcement, Securities and Exchange Commission, Denver Regional Office, Byron G. Rogers Federal Building, 1961 Stout Street, Suite 1700, Denver, CO 80294-1961.

C. Amounts ordered to be paid as civil money penalties pursuant to this Order shall be treated as penalties paid to the government for all purposes, including all tax purposes. To preserve the deterrent effect of the civil penalty, Respondent agrees that in any Related Investor Action, he shall not argue that he is entitled to, nor shall he benefit by, offset or reduction of any award of compensatory damages by the amount of any part of Respondent's payment of a civil penalty in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, Respondent agrees that he shall, within 30 days after entry of a final order granting the Penalty Offset, notify the Commission's counsel in this action and pay the amount of the Penalty Offset to the Securities and Exchange Commission. Such a payment shall not be deemed an additional civil penalty and shall not be deemed to change the amount of the civil penalty imposed in this proceeding. For purposes of this paragraph, a "Related Investor Action" means a private damages action brought against Respondent by or on behalf of one or more investors based on substantially the same facts as alleged in the Order instituted by the Commission in this proceeding.

V.

It is further Ordered that, solely for purposes of exceptions to discharge set forth in Section 523 of the Bankruptcy Code, 11 U.S.C. §523, the findings in this Order are true and admitted by Respondent, and further, any debt for disgorgement, prejudgment interest, civil penalty or other amounts due by Respondent under this Order or any other judgment, order, consent order, decree or settlement agreement entered in connection with this proceeding, is a debt for the violation by Respondent of the federal securities laws or any regulation or order issued under such laws, as set forth in Section 523(a)(19) of the Bankruptcy Code, 11 U.S.C. §523(a)(19).

By the Commission.

Brent J. Fields
Secretary