

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 10401 / August 18, 2017

SECURITIES EXCHANGE ACT OF 1934
Release No. 81427 / August 18, 2017

ADMINISTRATIVE PROCEEDING
File No. 3-18118

In the Matter of

Banca IMI Securities Corp.,

Respondent.

**ORDER INSTITUTING ADMINISTRATIVE
AND CEASE-AND-DESIST PROCEEDINGS,
PURSUANT TO SECTION 8A OF THE
SECURITIES ACT OF 1933, AND SECTION
15(b) OF THE SECURITIES EXCHANGE
ACT OF 1934, MAKING FINDINGS, AND
IMPOSING REMEDIAL SANCTIONS AND A
CEASE-AND-DESIST ORDER**

I.

The Securities and Exchange Commission (“Commission”) deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 8A of the Securities Act of 1933 (“Securities Act”) and Section 15(b) of the Securities Exchange Act of 1934 (“Exchange Act”), against Banca IMI Securities Corp. (“BISC” or “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 it and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings, Pursuant to Section 8A of the Securities Act of 1933, and Section 15(b) of the Securities Exchange Act of 1934, Making Findings, and Imposing Remedial Sanctions and 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:

Summary

1. These proceedings arise out of BISC's improper practices involving the pre-release of American Depositary Receipts ("ADRs"). ADRs allow U.S. investors to invest in foreign companies without having to purchase the shares in the foreign markets, and allow foreign companies to get increased exposure to U.S. markets.

2. ADR facilities, which provide for the issuance of ADRs, are established by a depositary bank (the "Depositary") pursuant to a depositary agreement ("Depositary Agreement").

3. Typically, a Depositary delivers ADRs to a market participant who delivers the corresponding number of foreign securities to the Depositary's foreign custodian ("Custodian"). However, in certain situations, Depositary Agreements may provide for a "pre-release" transaction, in which an investor can obtain newly-issued ADRs from the Depositary when the foreign securities have been purchased but prior to their delivery to the Custodian.² Such pre-released ADRs can only be obtained by parties, typically brokers, that have entered into pre-release agreements ("Pre-Release Agreements") with the Depositaries. The Pre-Release Agreements, consistent with the Depositary Agreements, require the broker receiving the pre-released ADRs (or its customer on whose behalf the broker is acting) to own the ordinary shares that evidence the ADRs, and to assign all beneficial right, title, and interest in those ordinary shares to the Depositary while the pre-release transaction is outstanding. In effect, the broker or its customer becomes the temporary custodian of the ordinary shares that would otherwise have been delivered to the Custodian.

4. Since at least January 2011, BISC had Pre-Release Agreements with four Depositaries. Contrary to certain provisions in these agreements and how pre-release transactions were supposed to work under the Depositary Agreements, associated persons on BISC's securities lending desk had an ongoing practice of obtaining, and then lending, pre-released ADRs from Depositaries without taking reasonable steps to determine whether the requisite number of ordinary shares was owned and custodied by the person on whose behalf the pre-released ADRs were being obtained. The result of this conduct was the issuance of ADRs that in many instances were not backed by ordinary shares as required by the Depositary Agreements. This conduct violated Section 17(a)(3) of the Securities Act.

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 The deposited securities typically are equity securities, but debt securities may also underlie ADRs.

5. In addition, BISC failed to establish and implement effective policies and procedures to address whether BISC's associated persons complied with the firm's obligations in connection with pre-release transactions, such as determining ownership of the underlying ordinary shares. As a result, BISC's supervisory policies and procedures were not reasonably designed and implemented to provide effective oversight of associated persons to prevent and detect their violations of Securities Act Section 17(a)(3), and BISC failed reasonably to supervise its associated persons within the meaning of Section 15(b)(4)(E) of the Exchange Act.

Respondent

6. BISC, a Delaware corporation, is registered with the Commission as a broker-dealer, and its principal executive offices are in New York, New York. BISC is a wholly-owned subsidiary of IMI Capital Markets USA Corporation, which in turn is a wholly-owned subsidiary of Intesa Sanpaolo SpA, an Italian bank.

Background

ADRs and the Pre-Release of ADRs

7. ADRs are negotiable instruments that represent an ownership interest in a specified number of foreign securities that have been deposited with a Depositary by the holder of those securities. ADRs may be traded on U.S. stock exchanges or over-the-counter. The owner of an ADR has the right to obtain the underlying foreign securities by withdrawing them from the ADR facility.³

8. An ADR is either "sponsored" or "unsponsored." If the ADR is sponsored, the Depositary Agreement is among the foreign company whose securities are represented by the ADRs (i.e., the sponsor), the Depositary, and ADR holders. If the ADR is unsponsored, the Depositary Agreement is between the Depositary and the ADR holders.⁴ In either case, the Depositary Agreement will describe fees applicable to the ADRs and the party responsible for paying those fees. In either case, the Depositary establishing the ADR files a Securities Act registration statement on Form F-6 with the Commission, which includes the Depositary Agreement as an exhibit.

³ In a more technical sense, ADRs evidence American Depositary Shares, or ADSs, which represent the specific number of underlying ordinary shares of the same company on deposit with the Custodian in the foreign issuer's home market. In addition, an ADR for a particular company may actually represent one ordinary share, more than one ordinary share, or a fraction of an ordinary share. The ADR-to-ordinary share ratio varies by company, based on pricing in the foreign and U.S. markets.

⁴ An unsponsored ADR is created by the Depositary and does not involve the formal participation (or require the agreement) of the foreign company whose securities the ADRs represent.

9. Typically, when ADRs are issued, a specified number of the ordinary shares represented by the ADRs are contemporaneously delivered to the Custodian. In this way, those ordinary shares (“Deposited Shares”) are removed from the market.

10. In some situations, a person may seek to obtain ADRs through a “pre-release” transaction, which is provided for in the Depositary Agreements and Pre-Release Agreements. In pre-release transactions, a market participant obtains newly issued ADRs from the Depositary (as opposed to purchasing existing ADRs on the market) before that participant delivers the corresponding ordinary shares to the Custodian. The traditional rationale for pre-release transactions was to address settlement timing disparities in jurisdictions that could delay delivery to the Custodian of recently-purchased ordinary shares. In theory, the pre-release transaction would be closed in short order once the ordinary shares were delivered to the Custodian. Once issued, pre-released ADRs are indistinguishable from other ADRs of the same issuer and can be freely traded, even while the pre-release transaction remains open.

11. Depositary Agreements and Pre-Release Agreements govern the terms of pre-release transactions. Brokers with Pre-Release Agreements (“Pre-Release Brokers”) may obtain pre-released ADRs directly from Depositaries.

12. The Depositary Agreement and Pre-Release Agreement typically require a representation that, in connection with each pre-release transaction, the person to whom pre-released ADRs are to be delivered, or that person’s customer, (i) owns the ordinary shares to be remitted, (ii) assigns all beneficial rights, title, and interest in the shares to the Depositary, and (iii) will not take any action with respect to such shares that is inconsistent with the transfer of beneficial ownership (collectively, the “Pre-Release Representations”). In effect, the person, or the customer on whose behalf the person is acting, must agree to custody the ordinary shares for the benefit of ADR holders, similar to how the Depositary custodies the ordinary shares in issuing ADRs that are not pre-released.

13. Depositary Agreements and Pre-Release Agreements also typically include provisions addressing the situation where ADRs have been pre-released over a dividend record date. The provisions typically require the person on whose behalf the pre-released ADR is obtained to ensure withholding taxes to the extent due were paid on the dividend to the foreign jurisdiction at the rate required for ADR holders, to forward to the Depositary all dividends received from their corresponding ordinary shares, net of any withholding tax paid, and to pass through any tax credits or refunds from the dividends to the Depositary. In this way, the rights and obligations of anyone who ends up holding the pre-released ADR will be protected, and the flow of dividend and tax payments will not be altered by the fact that the ordinary shares had not been simultaneously deposited with the Custodian when the pre-released ADR was issued.

14. Significantly, these agreements are intended to ensure that, at all times until the pre-release position is closed by delivery of the ordinary shares (or an equivalent number of ADRs), the Custodian and the Pre-Release Broker (or its customer) are collectively holding in custody, for the benefit of ADR holders, the number of ordinary shares that corresponds to the issued ADRs. This ensures that the total number of ordinary shares plus shares represented by ADRs available on the markets is constant, and that any economic or tax impact related to

holding the ordinary shares flows to the Depository and the ADR holders for whose benefit the Depository custodies ordinary shares.

BISC's Pre-Release Practices

15. From at least January 2011 until August 2015,⁵ BISC developed a matched book securities lending operation, whereby BISC obtained securities from a bank or broker-dealer and in turn lent them to another broker-dealer. During the relevant period, BISC had Pre-Release Agreements with four Depositories. Pursuant to those agreements, BISC had a practice of obtaining ADRs through pre-release transactions with Depositories and lending those ADRs to broker-dealer counterparties. BISC profited from these transactions by obtaining the pre-released ADRs from Depositories at lower rates than the rates at which they lent them to other brokers. Approximately 63% of BISC's securities lending profits during this period were generated from pre-release transactions.

16. In connection with the Pre-Release Agreements, Depositories A, B and C required BISC to sign certifications ("Certifications") stating that it was complying with the terms of the Pre-Release Agreements. For the period 2006 through 2014, a BISC representative signed a total of 9 such Certifications.

17. Despite the obligations provided for in the Pre-Release Agreements and Certifications, BISC was negligent in failing to take reasonable steps to determine whether it complied with the Pre-Release Representations.

18. BISC itself did not own ordinary shares in connection with any pre-release transaction with a Depository. Nor did BISC take reasonable steps to determine whether the broker-dealer counterparties to whom it lent the pre-released ADRs (or their customers) owned corresponding ordinary shares.

19. Instead, BISC securities lending desk personnel routinely obtained pre-released ADRs through the Pre-Release Agreements and then lent them to counterparties pursuant to standard master securities loan agreements ("MSLAs"). The MSLAs do not address pre-released ADRs, and did not contain any provisions requiring compliance with any of the Pre-Release Representations.

20. Although at various times BISC may have taken some action to inform certain of its counterparties that they should consider the Pre-Release Representations to be incorporated into the MSLAs, BISC's conduct was not sufficient for BISC to operate on the assumption that its counterparties were indeed complying with those Pre-Release Representations in each instance in which BISC lent them pre-released ADRs.

⁵ BISC temporarily suspended its pre-release activity in November 2014 but resumed this activity in March 2015, before it ended in August 2015.

21. In connection with most of its pre-release transactions from at least January 2011 until August 2015, BISC's securities lending desk personnel failed to seek confirmation that its counterparty (or its customer) owned and would appropriately custody ordinary shares, even though the circumstances, including the understanding that counterparties often lent the borrowed ADRs to another third party, as well as the nature of the transactions described below, should have indicated to them the strong possibility that such custody was not occurring.

22. In effect, BISC securities lending desk personnel treated the pre-released ADRs as if they were ordinary shares used in typical securities lending transactions. Accordingly, BISC securities lending desk personnel routinely obtained pre-released ADRs without taking sufficient steps to comply with the Pre-Release Representations. Moreover, given the circumstances in which BISC obtained and lent pre-released ADRs, BISC securities lending desk personnel should have recognized the likelihood that BISC was acting as a conduit through which its counterparties were obtaining and the Depositories were issuing ADRs that were not evidenced by any ordinary shares held for the benefit of the Depository.

23. BISC's securities lending desk personnel typically sought pre-released ADRs from Depositories for two primary reasons.

24. First, from at least January 2011 until August 2015, BISC securities lending desk personnel obtained, on a regular basis, pre-released ADRs of numerous securities and lent them to other broker-dealers that were looking to fulfill settlement obligations. Based on the nature of the broker-dealers' requests to borrow from BISC, and the fact that the requests often were for ADRs that were hard-to-borrow at the time, BISC's securities lending desk personnel should have recognized that the requests at times may have arisen from circumstances involving broker-dealers needing to obtain ADRs in order to make delivery on short sales, avoid fails to deliver, or comply with the close-out requirements in Regulation SHO Rule 204. None of those circumstances would indicate that the broker-dealers to whom BISC was lending the pre-released ADRs owned or had custody of the underlying ordinary shares. As a result, BISC failed to take reasonable steps to comply with the Pre-Release Representations in connection with these transactions.

25. Similarly, BISC at times used the ability to obtain pre-released ADRs from Depositories to assist broker-dealers that were seeking to locate shares pursuant to Rule 203 of Regulation SHO, in connection with potential short-selling activity. When providing such assistance, BISC failed to take reasonable steps to determine whether it would have been able to comply with the Pre-Release Representations.

26. As a result of this conduct, BISC, at times, facilitated short selling and enabled the settlement of trades with ADRs that were not actually backed by ordinary shares held for the benefit of the Depository in accordance with the terms of the Pre-Release Agreements.

27. Second, from at least January 2011 until August 2015, BISC securities lending desk personnel engaged in hundreds of pre-release transactions involving the sponsored ADRs of foreign issuers that were scheduled to pay dividends. BISC's counterparties (the brokers to whom BISC lent the pre-released ADRs) and other parties (such as the counterparties' customers

or counterparties' counterparties) sought to profit by holding ordinary shares in a tax advantaged situation if the tax savings were higher than the costs of borrowing or acquiring the ordinary shares at dividend time. BISC, in turn, profited from these transactions by lending the pre-released ADRs at a higher rate than the rate at which it obtained ADRs from the Depositary.

28. Pursuant to the Depositary Agreements and Pre-Release Agreements, the payment of dividends to ADR holders, and tax payments to foreign tax authorities, should have been unaffected by the pre-release of ADRs if all relevant parties were fulfilling their obligations under those agreements. BISC securities lending desk personnel were supposed to have ensured that the dividend payments on ordinary shares that would otherwise have been received by the Depositary's Custodian (i.e., where there was no pre-release transaction) were forwarded from BISC's borrower, to BISC, and on to the Depositary. In addition, the applicable foreign tax withholding on that dividend was supposed to have been calculated as if the Depositary owned and held such shares for the benefit of a U.S. resident holder of ADRs with no other equity interest in the issuer, with BISC representing that the applicable foreign withholding tax would be paid. Thus, all ADR holders on the relevant record date would, despite the existence of pre-released ADRs in the marketplace, (a) receive the dividend the holders were entitled to receive, net of withholding taxes; and (b) receive accurate information concerning the foreign taxes withheld on the dividends paid with respect to the ADRs.

29. BISC forwarded the correct net dividend amounts to the Depositories. However, BISC's securities lending desk personnel should have understood from the circumstances of many of the transactions that those amounts may not have originated from ordinary shares held at the time of the pre-release transaction, and that its borrowers may not have been making tax payments that, under the Pre-Release Agreements, should have been paid to the foreign jurisdiction.

30. For example, BISC securities lending desk personnel were, or should have been, aware that BISC's borrowing counterparties at times returned the pre-released ADRs to the Depositories in exchange for ordinary shares – a fact that could indicate that any forwarding of dividend payments may have come from the ordinary shares obtained from the pre-released ADRs themselves, rather than from any ordinary shares previously owned by the borrower.

31. BISC securities lending desk personnel typically lent pre-released ADRs before record date at rates that, when paid over an agreed upon term, in effect approximated the amount of the dividend that the borrower was willing to pay in order to obtain the ADRs. That is, if a standard U.S. taxpayer would only receive a net 85% of a dividend, with 15% being paid as withholding tax to the foreign jurisdiction, but the borrower (or its customer) qualified for 0% withholding, the borrower might be willing to pay, for example, a rate that when paid over an agreed upon term was roughly equal to a percentage of the dividend that was not withheld in order to borrow the pre-released ADRs. And BISC, in turn, would be willing to lend the pre-released ADRs at that rate if it could obtain them for less from a Depositary.

32. These dividend-related pre-release and corresponding lending transactions were structured by negotiating "all in" rates, which were inputs used to calculate the daily rebate rates

that BISC was willing to pay a Depository and that BISC was seeking to receive from its counterparties.

33. In one specific example, in October 2011, Depository A issued the ADRs of a foreign issuer (“Issuer A”) through pre-release transactions with BISC. At this time, the tax treaties with the foreign tax authority provided for a statutory withholding rate of 15% for ADR holders who were U.S. residents. Depository A and BISC entered into pre-release transactions through which BISC obtained 2,300,000 ADRs from Depository A; BISC then loaned those ADRs to a counterparty (“Counterparty A”). As reflected on spreadsheets tracking these transactions, Counterparty A agreed to an “all in” rate of approximately 94.42% over the periods in which the transactions were to remain open, and BISC and Depository A agreed to an “all in” rate of 90.48% over the same periods. In this example, Counterparty A would retain approximately 5.58% of the dividend (or 100% less 94.42%) and pay BISC a rebate rate that approximated 9.42% of the dividend, and BISC would pay Depository A a rebate rate that approximated 5.48% of the dividend (or 90.48% less 85%), such that BISC made a spread that approximated 3.94% of the dividend (or 94.42% less 90.48%). Post-dividend, as was often the case, Counterparty A delivered ADRs to BISC to close out its loan and BISC then delivered the ADRs to Depository A to close out the pre-release transactions. This one set of transactions resulted in \$76,288.80 in revenue for BISC.

34. Under the circumstances described above, BISC’s securities lending desk personnel should have known that BISC’s borrowers may not have been paying withholding taxes that may have been owed to the foreign jurisdiction on dividends received on ordinary shares, and that ordinary shares were not properly custodied for the benefit of ADR holders.

35. BISC failed to establish and implement policies and procedures that would be reasonably expected to determine whether its associated persons on the securities lending desk complied with the Pre-Release Representations in connection with pre-release transactions.

36. Throughout the staff’s investigation, BISC voluntarily highlighted documents likely to be of interest to the staff.

Violations and Failure Reasonably to Supervise

37. As result of the conduct described above, Respondent willfully⁶ violated Section 17(a)(3) of the Securities Act, which prohibits, in the offer or sale of securities, engaging in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

⁶ 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)).

38. Under Section 15(b)(4)(E) of the Exchange Act, broker-dealers are responsible for supervising, with a view to preventing and detecting violations of the federal securities laws, persons subject to their supervision. BISC was responsible for supervising its securities lending desk personnel to address whether they were complying with the Pre-Release Representations. BISC failed reasonably to fulfill such supervisory responsibilities within the meaning of Section 15(b)(4)(E) of the Exchange Act because BISC failed to establish reasonable policies and procedures, and a system for implementing such policies and procedures, that would reasonably be expected to prevent and detect the violations of Section 17(a)(3) of the Securities Act by the associated persons on the securities lending desk described above. If BISC had developed reasonable policies and procedures and systems to implement those procedures, it is likely that the firm would have prevented and detected the violations of its associated persons on the securities lending desk.

BISC's Remedial Efforts

39. In determining to accept the Offer, the Commission considered remedial acts undertaken by Respondent and cooperation afforded the Commission staff.

IV.

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

Accordingly, pursuant to Section 8A of the Securities Act, and Section 15(b) of the Exchange Act, it is hereby ORDERED that:

- A. Respondent cease and desist from committing or causing any violations and any future violations of Section 17(a)(3) of the Securities Act.
- B. Respondent is censured.
- C. BISC shall, within 30 days of the entry of this Order, pay disgorgement of \$18,048,483.38 and prejudgment interest of \$2,362,538.26 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). If timely payment is not made, additional interest shall accrue pursuant to SEC Rule of Practice 600.
- D. BISC shall, within 30 days of the entry of this Order, pay a civil money penalty in the amount of \$15,000,000 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). If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. § 3717.

Payment 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 BISC as a 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 Sanjay Wadhwa, Senior Associate Director, Division of Enforcement, Securities and Exchange Commission, 200 Vesey Street, New York, NY 10281.

E. 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, it shall not argue that it is entitled to, nor shall it 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 it 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.

F. Respondent acknowledges that the Commission is not imposing a civil penalty in excess of \$15,000,000 based upon its cooperation and agreement to cooperate in a Commission investigation and related enforcement action. If at any time following the entry of the Order, the Division of Enforcement ("Division") obtains information indicating that Respondent knowingly provided materially false or misleading information or materials to the Commission, or in a related proceeding, the Division may, at its sole discretion and with prior notice to the Respondent, petition the Commission to reopen this matter and seek an order directing that the Respondent pay an additional civil penalty. Respondent may contest by way of defense in any resulting

administrative proceeding whether it knowingly provided materially false or misleading information, but may not: (1) contest the findings in the Order; or (2) assert any defense to liability or remedy, including, but not limited to, any statute of limitations defense.

By the Commission.

Brent J. Fields
Secretary