

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER, AND CONSENT
NO. 2016051704305**

TO: Department of Enforcement
Financial Industry Regulatory Authority (FINRA)

RE: Aegis Capital Corp. (Respondent)
Member Firm
CRD No. 15007

Pursuant to FINRA Rule 9216, Respondent Aegis Capital Corp. (Aegis) submits this Letter of Acceptance, Waiver, and Consent (AWC) for the purpose of proposing a settlement of the alleged rule violations described below. This AWC is submitted on the condition that, if accepted, FINRA will not bring any future actions against Respondent alleging violations based on the same factual findings described in this AWC.

**I.
ACCEPTANCE AND CONSENT**

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

BACKGROUND

Aegis has been a FINRA member since July 1984. Aegis is headquartered in New York, New York, and currently employs more than 300 registered representatives in its 23 branch offices. Aegis is an introducing broker-dealer and generates more than half of its revenues from commissions or markups and markdowns charged in connection with purchases and sales of securities made on behalf of its retail and institutional customers.¹

OVERVIEW

From July 2014 through December 2018, Aegis failed to establish, maintain, and enforce a supervisory system, including written supervisory procedures (WSPs), reasonably designed to achieve compliance with the suitability requirements of FINRA Rule 2111 as it pertains to excessive trading. As a result, Aegis failed to identify trading in hundreds of customer accounts that was potentially excessive and unsuitable, including trading conducted by eight Aegis registered representatives in the firm's Melville and Wall Street branches whose trading in the accounts of 31 firm customers resulted in an average annualized cost-to-equity ratio (or break-even point) of 71.6%, an average annualized turnover rate of 34.9, combined customer costs (including commissions, markups or

¹ For more information about the firm, including prior regulatory events, visit BrokerCheck® at www.finra.org/brokercheck.

markdowns, margin interest and fees) of more than \$2.9 million, and cumulative losses of \$4.6 million.

Additionally, from July 2014 to June 2019, Aegis failed to establish, maintain, and enforce a supervisory system, including WSPs, reasonably designed to achieve compliance with the suitability requirements of FINRA Rule 2111 when selling leveraged, inverse, and inverse-leveraged Exchange-Traded Funds (Non-Traditional ETFs) to retail customers. As a result, Aegis failed to identify customers who purchased and held Non-Traditional ETFs for extended periods of time, or whose purchase was inconsistent with their recorded investment objective, risk tolerance or finances.

By virtue of the foregoing, Aegis violated NASD Rule 3010 and FINRA Rules 3110 and 2010.²

FACTS AND VIOLATIVE CONDUCT

These matters originated from a firm examination conducted by FINRA Member Supervision and FINRA's review of a customer arbitration filing.

FINRA Rule 3110 and its predecessor, NASD Rule 3010, require FINRA member firms to establish, maintain, and enforce a supervisory system, including WSPs, that is reasonably designed to supervise the activities of each registered representative, registered principal, and other associated person of the firm and achieve compliance with applicable securities laws and regulations, and FINRA and NASD rules.

The duty of supervision imposed by FINRA Rule 3110 and NASD Rule 3010 on firms includes the obligation and responsibility to investigate red flags that suggest misconduct may be occurring and to act upon the results of such investigation.

A violation of FINRA Rule 3110 or NASD Rule 3010 also constitutes a violation of FINRA Rule 2010, which requires member firms and associated persons to observe high standards of commercial honor and just and equitable principles of trade in the conduct of their business.

Suitability, Generally.

FINRA Rule 2111, FINRA's suitability rule, requires member firms and their associated persons to have a reasonable basis to believe that a recommended transaction or investment strategy is suitable for the customer based on the customer's investment profile. A customer's investment profile includes the customer's age, other investments, financial situation and needs, tax status, investment objectives, investment experience, investment time horizon, liquidity needs, and risk tolerance.

FINRA Rule 2111 also imposes a "quantitative suitability" obligation that focuses on whether the number of transactions within a given timeframe is suitable in light of the customer's financial circumstances and investment objectives. Excessive trading occurs,

² FINRA Rule 3110 superseded NASD Rule 3010 on December 1, 2014. Respondent's misconduct occurred under both NASD Rule 3010 and FINRA Rule 3110.

and is unsuitable, when a registered representative, while exercising control over a customer's account, recommends a level of trading activity that is inconsistent with the customer's investment needs and objectives. The Supplementary Material to FINRA Rule 2111 at Rule 2111.05(c) states that "[n]o single test defines excessive activity, but factors such as the turnover rate, cost-equity ratio, and the use of in-and-out trading in a customer's account may provide a basis for a finding that a member or associated person has violated the quantitative suitability obligation."

Turnover rate represents the number of times that a portfolio of securities is exchanged for another portfolio of securities. The cost-to-equity ratio measures the amount an account must increase in value just to cover commissions and other trading expenses, or the break-even point where a customer may begin to see a return. A turnover rate of six and a cost-to-equity ratio above 20% are indicators that excessive trading may have occurred.

Aegis failed to establish, maintain and enforce a supervisory system reasonably designed to supervise actively traded accounts and excessive and unsuitable trading.

Between 2014 and 2018, Aegis employed on average more than 350 registered representatives across more than 20 branch offices, with the majority working in the firm's Melville, 40 Wall Street, and Seventh Avenue branches. More than 10% of the firm's registered representatives disclosed personal financial issues, such as outstanding liens, judgments or bankruptcies on FINRA's Central Registration Depository.

During the relevant period, Aegis used boilerplate WSPs prepared by an outside vendor for supervision of registered representatives' trading in customer accounts. Aegis's WSPs instructed its branch managers to monitor trading for suitability issues during their daily review of Aegis's trade blotters, but did not explain how the firm's supervisors should conduct the daily trade review or use the trade blotters and other available customer information to identify potentially unsuitable or excessive trading in Aegis's customers' accounts. The WSPs also did not define, or require supervisors to calculate or consider, turnover rate or cost-to-equity ratio. Additionally, Aegis did not provide its branch and assistant branch managers training to compensate for the lack of guidance in the WSPs.

Aegis's trade blotters were not designed to flag excessive trading activity, as they did not show the trading history in an account, or the holding period between buys and sells in the same security. The blotters also did not include cost-to-equity or turnover, or information regarding the use of margin, even though many of the firm's registered representatives recommended the use of margin to their customers.

Aegis's WSPs also required branch managers to conduct monthly and semi-annual reviews of customer account activity to monitor for suitability and churning, and the firm's chief compliance officer or their designee to review "active accounts" (defined as accounts with more than 20 transactions per month and \$5,000 in commissions), to determine if the type, size, and frequency of trades was consistent with the customer's investment objectives. However, these reviews were not performed for most of the relevant period.

Aegis had access to additional supervisory tools to monitor and identify excessive trading. Aegis received exception reports from its clearing firm specifically designed to identify accounts with turnover rates and commission-to-equity ratios indicative of excessive and

unsuitable trading. The exception reports were triggered when the annualized cost-to-equity ratio in accounts with an aggressive or speculative investment objective exceeded 5% or 6%, respectively, for three or more consecutive days, or the turnover exceeded 500% for five or more consecutive days.

From July 2014 to December 2018, the active, in-and-out trading conducted by Aegis's registered representatives generated thousands of exception reports identifying customer accounts with potentially unsuitable turnover rates and commission-to-equity ratios. Approximately one-third of the exception reports related to trading in accounts held by senior investors, and more than 900 identified potentially unsuitable trading by eight registered representatives who worked in Aegis's Melville and Wall Street branches (the Representatives).

These exception reports were active and viewable in the trade review system that Aegis's supervisors used to conduct their daily trade reviews. However, for most of the relevant period, Aegis's WSPs did not reference the exception reports or require its supervisors to review and address them.

Aegis also received more than 50 complaints from customers alleging excessive, unsuitable or unauthorized trading in their firm accounts, including at least 13 complaints from customers whose accounts were managed by the Representatives.

Aegis failed to take reasonable steps to investigate these numerous red flags of potentially excessive and unsuitable trading by its registered representatives. Instead, Aegis and its supervisors sent disclosure letters designed to document a customer's general acknowledgement of the trading in their accounts and the trading costs they incurred. However, the letters did not include the actual costs of the trading, the costs incurred due to the use of margin, or explain what trades (or series of trades) prompted Aegis to issue the letter.

During the relevant period, Aegis's compliance department prepared reports documenting the "key compliance issues" identified during its review and testing of Aegis's supervisory systems, procedures, and controls. Aegis's annual testing reported that:

- Aegis lacked specific procedures to monitor turnover and commission-to-equity ratios in customers' accounts.
- Aegis should use exception reports that monitored commission activity and trading velocity (or turnover) to ensure "adequate" commission-to-equity ratios in its customers' accounts.
- Aegis was not utilizing specific alerts provided by its clearing firm that would ensure adequate commission-to-equity ratios.
- Aegis's WSPs did not identify which clearing firm exception reports it would use to conduct supervisory trading reviews, or the principals responsible for reviewing them.
- Aegis needed additional compliance personnel to keep pace with Aegis's rapid hiring and growth.

Although many of these findings carried over from year-to-year, Aegis did not immediately address the deficiencies identified by its annual testing. Aegis did not supplement its daily trade reviews with systems, surveillance, or reviews specifically designed to monitor or calculate commission-to-equity ratios or turnover rates in customer accounts, or require its supervisors to review the exception reports provided by its clearing firm. Aegis also did not update the daily trade blotters to include information that would enable its supervisors to identify patterns of trading, commissions or accumulated losses in customer accounts.

In 2018, Aegis retained a third party vendor to provide new automated trade surveillance and alerts. In 2019, and again in 2020, Aegis also retained independent consultants to conduct comprehensive reviews of its WSPs and supervisory controls, and its remediation is ongoing.

Even so, during the Relevant Period, Aegis failed to identify potentially excessive and unsuitable trading in hundreds of customer accounts. Aegis's unreasonable supervisory system, combined with the failure to respond to the red flags discussed above, also allowed the Representatives to make unsuitable recommendations and excessively trade the accounts of 31 customers. The trading by the Representatives in the accounts of those 31 customers resulted in annualized turnover rates ranging from 4.2 to 199.8 and cost-to-equity ratios ranging from 21.2% to 164.6%, and more than \$2.9 million in costs and \$4.6 million in losses.

Therefore, Aegis violated NASD Rule 3010 and FINRA Rules 3110 and 2010.

Aegis failed to establish, maintain and enforce a system reasonably designed to supervise sales of Non-Traditional Exchange Traded Funds.

Exchange-Traded Funds (ETFs) are typically registered unit investment trusts or open-end investment companies whose shares represent an interest in a portfolio of securities that track an underlying benchmark or index. Shares of ETFs often are listed on national securities exchanges and trade throughout the day at prices established by the market.

Leveraged ETFs seek to return a multiple of the performance of the index or benchmark they track. Some Non-Traditional ETFs are “inverse” or “short” funds, meaning they seek to deliver the opposite of the performance of the index or benchmark they track. Some funds are both inverse and leveraged, meaning that they seek to achieve a return that is a multiple of the inverse performance of the underlying index or benchmark. Most Non-Traditional ETFs reset daily, meaning they are designed to achieve their stated objectives only over the course of one trading session – usually a single day.

In June 2009, FINRA issued Regulatory Notice 09-31. Regulatory Notice 09-31 reminded member firms that the performance of Non-Traditional ETFs over periods of time longer than a single trading session “can differ significantly from the performance ... of their underlying index or benchmark during the same period of time.” Because of these risks, and the complexity of these products, the notice further advised that “[w]hile the customer-specific suitability analysis depends on the investor’s particular circumstances, inverse and leveraged ETFs are not suitable for retail investors who plan to hold them for more than one trading session, particularly in volatile markets.”

In January 2012, FINRA issued Regulatory Notice 12-03. Regulatory Notice 12-03 reminded member firms that Non-Traditional ETFs that reset daily are complex products that require heightened supervision. The notice explained that member firms should have: (i) a well-designed system of internal controls; (ii) adequate training so its registered representatives understand how Non-Traditional ETFs are expected to perform in normal market conditions and the risks associated with them; and (iii) monitoring systems or procedures reasonably designed to determine that Non-Traditional ETFs are recommended and sold only to customers who understand their essential features and for whom the product is suitable.

From July 1, 2014 to June 1, 2019, Aegis's registered representatives executed more than 3,000 transactions, with a total principal value of more than \$400 million, in Non-Traditional ETFs that reset daily. The transactions were executed in 524 retail customer accounts and generated approximately \$422,000 in sales compensation for Aegis and its registered representatives.

Consistent with Regulatory Notice 12-03, Aegis's WSPs designated Non-Traditional ETFs as a complex product requiring heightened supervision. For example, Aegis's WSPs required the firm to provide its registered representatives with mandatory training on the features and risks of Non-Traditional ETFs, and clear instructions regarding the types of customers for whom Non-Traditional ETFs were suitable. Aegis's WSPs also required the firm to appoint a product manager responsible for determining the type of investor for whom the purchase or sale of Non-Traditional ETFs was suitable, and tasked the firm's branch managers with reviewing each Non-Traditional ETF transaction for customer-specific suitability.

Aegis failed to conduct the heightened supervision its WSPs required. Aegis did not designate an individual to act as product manager or require its branch managers to perform the heightened suitability review its WSPs mandated for sales of Non-Traditional ETFs. Aegis did not provide its registered representatives with any training on Non-Traditional ETFs until November 2018, or establish guidance regarding the types of customers for whom the purchase of Non-Traditional ETFs was suitable until June 2019.

Aegis's supervisory systems were also not reasonably designed to detect potentially unsuitable transactions involving Non-Traditional ETFs. As discussed in Regulatory Notice 09-31, a primary risk associated with Non-Traditional ETFs is that their performance over longer periods of time can differ significantly from the performance of their underlying index or benchmark, particularly in volatile markets. Aegis relied on its daily trade review to monitor how long customers who purchased Non-Traditional ETFs held the security before selling it. However, the trade blotter did not include information that allowed the branch managers to identify whether a customer held a Non-Traditional ETF for more than one day, and Aegis did not track the holding periods of Non-Traditional ETF positions.

As a result, Aegis failed to identify customers who purchased and held Non-Traditional ETFs for extended periods of time up to and including a year or longer, and customers whose purchase was inconsistent with their recorded investment objective, risk tolerance

or finances. Fifteen of those customers – including seniors and individuals with conservative or moderate risk tolerances – incurred total realized losses of \$132,463.

Therefore, Aegis violated NASD Rule 3010 and FINRA Rules 3110 and 2010.

B. Respondent also consents to the imposition of the following sanctions:

- a censure;
- a fine of \$1,050,000;
- restitution of \$1,692,256.44; and
- an undertaking requiring Aegis to submit, within 30 days of the completion of the firm’s implementation of the recommendations received from the independent consultant retained by the firm on or about January 12, 2021, a certification in writing by Aegis’s Chief Executive Officer that, as of the date of the certification, Aegis has established supervisory systems and WSPs reasonably designed to achieve compliance with the applicable securities laws, regulations, and NASD and FINRA rules addressed in this AWC. The certification should be submitted to Tiffany A. Buxton, Director, at tiffany.buxton@finra.org. All correspondence must identify the respondent and matter number 2016051704305. Upon written request showing good cause, FINRA staff may extend any of the deadlines related to the certification component of the sanction.

Respondent agrees to pay the monetary sanctions upon notice that this AWC has been accepted and such payments are due and payable. Respondent has submitted an Election of Payment form showing the method by which the firm proposes to pay the fine imposed.

Respondent specifically and voluntarily waives any right to claim an inability to pay, now or at any time hereafter, the monetary sanctions imposed in this matter.

Restitution is ordered to be paid to the customers listed on Attachment A to this AWC in the total amount of \$1,692,256.44.³

A registered principal on behalf of Aegis shall submit satisfactory proof of payment of restitution (separately specifying the date and amount paid to each customer listed on Attachment A) or of reasonable and documented efforts undertaken to effect restitution. Such proof shall be submitted by email to EnforcementNotice@FINRA.org from a work-related account of the registered principal of Aegis. The email must identify Aegis and the case number and include a copy of the check, money order, or other method of payment. This proof shall be provided by email to EnforcementNotice@FINRA.org no later than 365 days after the date of the notice of acceptance of the AWC.

If for any reason Aegis cannot locate any customer identified in Attachment A after reasonable and documented efforts within 365 days after the date of the notice of acceptance of the AWC, or such additional period agreed to by FINRA in writing, Aegis

³ The amount of restitution Aegis is required to pay has been reduced by sums that Aegis previously paid to customers.

shall forward any undistributed restitution to the appropriate escheat, unclaimed property, or abandoned property fund for the state in which the customer is last known to have resided. Aegis shall provide satisfactory proof of such action to FINRA in the manner described above, within 14 calendar days of forwarding the undistributed restitution to the appropriate state authority.

The imposition of a restitution order or any other monetary sanction in this AWC, and the timing of such ordered payments, does not preclude customers from pursuing their own actions to obtain restitution or other remedies.

Restitution payments to customers shall be preceded or accompanied by a letter, not unacceptable to FINRA, describing the reason for the payment and the fact that the payment is being made pursuant to a settlement with FINRA and as a term of this AWC.

The sanctions imposed in this AWC shall be effective on a date set by FINRA.

II.

WAIVER OF PROCEDURAL RIGHTS

Respondent specifically and voluntarily waives the following rights granted under FINRA's Code of Procedure:

- A. To have a complaint issued specifying the allegations against the firm;
- B. To be notified of the complaint and have the opportunity to answer the allegations in writing;
- C. To defend against the allegations in a disciplinary hearing before a hearing panel, to have a written record of the hearing made, and to have a written decision issued; and
- D. To appeal any such decision to the NAC and then to the U.S. Securities and Exchange Commission and a U.S. Court of Appeals.

Further, Respondent specifically and voluntarily waives any right to claim bias or prejudgment of the Chief Legal Officer, the NAC, or any member of the NAC, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including its acceptance or rejection.

Respondent further specifically and voluntarily waives any right to claim that a person violated the ex parte prohibitions of FINRA Rule 9143 or the separation of functions prohibitions of FINRA Rule 9144, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including its acceptance or rejection.

III. OTHER MATTERS

Respondent understands that:

- A. Submission of this AWC is voluntary and will not resolve this matter unless and until it has been reviewed and accepted by the NAC, a Review Subcommittee of the NAC, or the Office of Disciplinary Affairs (ODA), pursuant to FINRA Rule 9216;
- B. If this AWC is not accepted, its submission will not be used as evidence to prove any of the allegations against Respondent; and
- C. If accepted:
 - 1. this AWC will become part of Respondent's permanent disciplinary record and may be considered in any future action brought by FINRA or any other regulator against Respondent;
 - 2. this AWC will be made available through FINRA's public disclosure program in accordance with FINRA Rule 8313;
 - 3. FINRA may make a public announcement concerning this agreement and its subject matter in accordance with FINRA Rule 8313; and
 - 4. Respondent may not take any action or make or permit to be made any public statement, including in regulatory filings or otherwise, denying, directly or indirectly, any finding in this AWC or create the impression that the AWC is without factual basis. Respondent may not take any position in any proceeding brought by or on behalf of FINRA, or to which FINRA is a party, that is inconsistent with any part of this AWC. Nothing in this provision affects Respondent's right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party. Nothing in this provision affects Respondent's testimonial obligations in any litigation or other legal proceedings.
- D. Respondent may attach a corrective action statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. Respondent understands that it may not deny the charges or make any statement that is inconsistent with the AWC in this statement. This statement does not constitute factual or legal findings by FINRA, nor does it reflect the views of FINRA.

The undersigned, on behalf of Aegis, certifies that a person duly authorized to act on Aegis's behalf has read and understands all of the provisions of this AWC and has been given a full opportunity to ask questions about it; that Aegis has agreed to the AWC's provisions voluntarily; and that no offer, threat, inducement, or promise of any kind, other than the terms set forth in this AWC and

the prospect of avoiding the issuance of a complaint, has been made to induce Aegis to submit this AWC.

October 29, 2021

Date

Timothy Treble

Aegis Capital Corp.
Respondent

Print Name: Timothy Treble

Title: Chief Compliance Officer

Reviewed by:



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Accepted by FINRA:

Signed on behalf of the
Director of ODA, by delegated authority

November 8, 2021

Date

Tiffany Buxton

Tiffany A. Buxton
Director
FINRA Department of Enforcement
One Brookfield Place, 200 Liberty Street, 11th Floor
New York, New York 10281

ATTACHMENT A

Customer Name	Restitution Amount
Customer A	\$83,353.11
Customer B	\$3,780.50
Customer C	\$9,244.50
Customer D	\$57,612.05
Customer E	\$15,105.79
Customer F	\$47,800.87
Customer G	\$9,125.00
Customer H	\$22,665.50
Customer I	\$86,302.05
Customer J	\$11,768.75
Customer K	\$28,659.24
Customer L	\$14,395.60
Customer M	\$27,742.60
Customer N	\$48,214.61
Customer O	\$114,790.16
Customer P	\$6,705.23
Customer Q	\$96,155.00
Customer R	\$41,053.00
Customer S	\$18,915.00
Customer T	\$10,405.00
Customer U	\$30,460.50
Customer V	\$87,266.00
Customer W	\$14,685.00
Customer X	\$11,968.11
Customer Y	\$11,450.00
Customer Z	\$10,005.25
Customer AA	\$20,348.25
Customer BB	\$44,627.46
Customer CC	\$22,736.05
Customer DD	\$12,773.00
Customer EE	\$16,796.34
Customer FF	\$18,535.30
Customer GG	\$12,004.50
Customer HH	\$21,016.80
Customer II	\$10,538.25
Customer JJ	\$19,638.50
Customer KK	\$11,420.00

ATTACHMENT A

Customer Name	Restitution Amount
Customer LL	\$8,749.10
Customer MM	\$39,860.50
Customer NN	\$56,230.40
Customer OO	\$10,490.00
Customer PP	\$8,392.50
Customer QQ	\$12,400.00
Customer RR	\$112,532.65
Customer SS	\$13,336.17
Customer TT	\$11,618.50
Customer UU	\$13,309.00
Customer VV	\$53,528.42
Customer XX	\$9,446.00
Customer YY	\$20,275.50
Customer ZZ	\$10,243.00
Customer AAA	\$41,493.27
Customer BBB	\$7,826.15
Customer CCC	\$1,943.18
Customer DDD	\$19,464.43
Customer EEE	\$6,527.10
Customer FFF	\$769.93
Customer GGG	\$630.05
Customer HHH	\$167.07
Customer III	\$321.41
Customer JJJ	\$128.61
Customer KKK	\$22,183.00
Customer LLL	\$5,683.75
Customer MMM	\$16,122.20
Customer NNN	\$3,160.80
Customer OOO	\$15,557.08
Customer PPP	\$2,818.60
Customer QQQ	\$10,472.00
Customer RRR	\$26,513.20
TOTAL	\$1,692,256.44