

**UNITED STATES OF AMERICA**  
**Before the**  
**SECURITIES AND EXCHANGE COMMISSION**

**SECURITIES EXCHANGE ACT OF 1934**  
**Release No. 67969 / October 3, 2012**

**ADMINISTRATIVE PROCEEDING**  
**File No. 3-15058**

In the Matter of  eBX, LLC  Respondent.
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**ORDER INSTITUTING  
ADMINISTRATIVE AND CEASE-AND-  
DESIST PROCEEDINGS PURSUANT  
TO SECTIONS 15(b) AND 21C 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 Sections 15(b) and 21C of the Securities Exchange Act of 1934 (“Exchange Act”) against eBX, LLC (“eBX” 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 Sections 15(b) and 21C 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 finds that:

A. SUMMARY

1. eBX is a broker-dealer registered with the Commission that operates LevelL ATS (“LevelL”), an alternative trading system (“ATS”), which began operation on October 16, 2006. LevelL is an ATS subject to Regulation ATS under the Exchange Act. eBX marketed LevelL as a “dark pool” trading system and stated that it “maximizes liquidity and provides best execution while minimizing information leakage and market impact.”

2. LevelL outsourced its operation to a third party technology service provider (the “Service Provider”), which signed a contract to build, host, and operate LevelL. The Service Provider also had a separate order routing business unit (the “Order Routing Business”), through which it sold order routing services to its own customers. The Service Provider and its Order Routing Business were distinct from LevelL.

3. Regulation ATS requires an ATS, among other things, to establish adequate safeguards and procedures to protect subscribers’ confidential trading information. Despite this requirement, from at least 2008 through early 2011, LevelL failed to protect the confidential trading information of its subscribers and failed to disclose to all of its subscribers the uses that it allowed an entity outside of the ATS to make of that confidential trading information. In particular, LevelL allowed the Order Routing Business to remember LevelL subscribers’ unexecuted order information and use that information for its own benefit. LevelL did not disclose to all of its subscribers that their confidential order information was being used by the Order Routing Business. There is no evidence that information about LevelL’s unexecuted orders was displayed, or otherwise communicated to, clients of the Order Routing Business or other third parties.

4. From at least 2008 through early 2011, LevelL violated Regulation ATS by permitting the Order Routing Business’s smart order router (the “Router”) to remember information about LevelL subscribers’ unexecuted orders residing within LevelL. The Router then used LevelL subscribers’ order information to make routing decisions for the benefit of its own Order Routing Business. For example, if the Router knew that a buy order had been routed to LevelL, the Service Provider would use that information to route a sell order to LevelL to obtain an execution. Conversely, if the Service Provider knew that no buy order had been routed to LevelL, it would likely route any sell order it subsequently received to another destination. In addition, the Router was aware of the prices and pricing attributes of orders resting in LevelL, and was programmed to use that information in determining whether to send an order to LevelL as opposed to another venue based on where it knew it might get a better price for its own customers’ orders.

5. LevelL did not inform most of its subscribers that their order information was used in this way – outside of the ATS –by the Order Routing Business. Instead, LevelL informed subscribers, in its subscriber agreements and elsewhere, that their order flow would be kept confidential and would not be shared outside of LevelL. These statements were inaccurate. LevelL subscribers other than the Service Provider did not have access to the same type of order information that would have assisted them in making their own routing decisions.

6. Moreover, LevelL was required to file a Form ATS with the Commission that accurately described how it operated. LevelL's Form ATS failed to disclose that it authorized the Service Provider to use data relating to orders routed to LevelL for the benefit of the Order Routing Business.

B. RESPONDENT

7. eBX registered with the Commission as a broker-dealer in or around July 2006 (SEC File No. 8-67145), and is a member of the Financial Industry Regulatory Authority. Since October 16, 2006, eBX has been the registered broker-dealer operating LevelL. eBX is a Delaware limited liability company that is a joint venture among five major registered broker-dealers. Its principal place of business is Boston, Massachusetts. LevelL's subscribers are limited to other registered broker-dealers.

C. FACTS

8. LevelL is an ATS that electronically matches undisplayed buy and sell orders for various equity securities, including NMS stocks and certain OTCBB and Pink Sheet securities.

9. LevelL operates pursuant to Regulation ATS, which was promulgated under the Exchange Act. An ATS is "any organization, association, person, group of persons, or system: (1) [t]hat constitutes, maintains, or provides a market place or facilities for bringing together purchasers and sellers of securities or for otherwise performing with respect to securities the functions commonly performed by a stock exchange within the meaning of Exchange Act Rule 3b-16; and (2) [t]hat does not: (i) [s]et rules governing the conduct of subscribers other than the conduct of subscribers' trading on such [ATS]; or (ii) [d]iscipline subscribers other than by exclusion from trading." Regulation ATS, Rule 300(a).

10. Before beginning operation, an ATS is required to file Form ATS with the Commission. *See* Regulation ATS, Rule 301(b)(2). Form ATS requires the registrant to disclose basic information about the ATS, including the type of subscribers to the ATS, the type of securities that trade on the ATS, other entities that are involved with the ATS, and how the ATS operates. An ATS must file amendments to Form ATS before making material changes to the operation of its system and when information previously filed on Form ATS becomes inaccurate.

**How LevelL Worked – From Initial Operation to March 2008**

11. Since its inception, LevelL has outsourced its operation to the Service Provider. Under a contract signed in May 2006 (the "Original Hosting Agreement"), the Service Provider agreed to operate, host, and maintain LevelL. LevelL's systems were owned and operated by the Service Provider, the personnel involved in the day to day operation of LevelL were employees of the Service Provider, and LevelL employees were not able to access LevelL directly.

12. In addition to, and distinct from, its business of operating LevelL, the Service Provider had an Order Routing Business. The Order Routing Business had its own customers (some of which were also LevelL subscribers, but some of which were not LevelL subscribers). The Order Routing Business used its proprietary technology to send its customers' orders to various market centers. Until certain changes to the parties' agreements that will be described below (*see* ¶¶19-33), the Order Routing Business did not send its customers' orders into LevelL. The Order Routing Business provided its services through the use of the Router – which could adjust its routing strategies to attempt to maximize its customers' executions.

13. When it began to provide technology services to LevelL in 2006, the Service Provider decided to use the Router as the Financial Information eXchange (“FIX”) gateway through which LevelL subscribers were instructed to send their orders into LevelL.<sup>1</sup>

14. LevelL had two principal order types: (1) resting orders (“Intents”), which remained in the system for a subscriber-determined period of time and (2) immediate-or-cancel (“IOC”) orders. LevelL subscribers sent both types of orders into LevelL through the Router.

15. On July 6, 2006, LevelL filed with the Commission an initial operation report on Form ATS. That filing disclosed that the Service Provider would “build and host” LevelL and integrate it with the Router, and that the Router would “sit in front of” LevelL and route orders to LevelL. LevelL also told its subscribers that: LevelL was hosted and operated by the Service Provider; the Router operated by the Service Provider was used as a FIX router to access LevelL; and, for certain purposes, subscribers would communicate with the Service Provider's support personnel.

16. During this initial phase of LevelL's operations, eBX did not permit the Service Provider's Router to remember and utilize LevelL subscribers' confidential trading information.

### **The Service Provider's Order Routing Business and the Router's Memory Feature**

17. In addition to functioning as a FIX gateway for LevelL, the Router also had a memory functionality (the “Memory Feature”) that enabled it to retain a record of any order that the Router had submitted to various market centers, and to use that information to make automated routing decisions. The Memory Feature retained the symbol, side, source, quantity, and received time for these orders. For certain orders, the Memory Feature also remembered pricing information and order attributes. The Router would know if an order it had sent to a market center remained unexecuted, because if it had been executed, the market center would have reported the fill back to the Router. Thus, the Memory Feature maintained a catalog of the orders the Router had sent to all venues.

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<sup>1</sup> The FIX protocol is a series of messaging specifications widely used in the industry for the electronic communication of trade-related messages.

When the Router received a new order, it could consult the Memory Feature to determine the best venue to send the new order to. If the Router knew it had previously sent a contraside order to a particular market center and that order remained unexecuted, the Router could send the new order to that same market center, knowing that there was a high probability that the two orders would execute. The Memory Feature was outside of LevelL and was not necessary to LevelL's functioning.

18. The Service Provider was affiliated with a broker-dealer (the "Routing Broker") that operated an electronic communications network (an "ECN"). As part of its Order Routing Business, the Service Provider used the Router, and in particular, the Router's Memory Feature, to route order flow for its own customers, including the Routing Broker's ECN when contraside interest was not present in the ECN.

### **Negotiations to Permit the Router to Utilize the Memory Feature to Make Routing Decisions And Changes After March 2008**

19. In fall 2007, LevelL began negotiating a new hosting agreement with the Service Provider. At around the same time the Order Routing Business also sought to have the Routing Broker become a subscriber to LevelL. During the negotiations, the Service Provider proposed that (1) as part of its Order Routing Business, the Router could send orders to LevelL, and (2) the Order Routing Business could use the Memory Feature and its information about LevelL subscribers' unexecuted orders for the purpose of routing or not routing orders to LevelL. In practice, this would allow the Router to read the LevelL order book by "turning on" the Memory Feature for LevelL. This arrangement would benefit the Service Provider because the Router would know LevelL's order book before it routed orders to LevelL. This arrangement would then increase the Order Routing Business' fill rate significantly, in part because it could route additional orders to LevelL in situations where there was more likely to be a contraside Intent in LevelL.

20. During the negotiations, the Service Provider emphasized to LevelL the importance of the Routing Broker becoming a LevelL subscriber. An executive from the Service Provider emailed a LevelL executive stating that the negotiations needed "to get resolved ASAP" because "if we do not get this agreement done, then [the Order Routing Business]'s flow will not be able to access LevelL." The Service Provider also later wrote the LevelL executive that the Routing Broker wants to "send orders to LevelL. That is all." The LevelL executive replied, "Absolutely. I will make sure it goes through."

21. During the negotiations, the issue was raised internally at LevelL as to whether its user agreements with its subscribers would prohibit the Memory Feature from using those subscribers' unexecuted order information for the Order Routing Business' benefit. A LevelL executive acknowledged that several LevelL subscribers had agreements that explicitly prohibited such use. Though that executive told another LevelL official that he would obtain the consent of those LevelL subscribers whose existing user agreements explicitly would prohibit such information access by the Memory Feature, he failed to do so.

22. Effective February 25, 2008, the Routing Broker signed a user agreement under which it became a subscriber to LevelL (the “Routing Broker User Agreement”). The Routing Broker User Agreement contained specially-negotiated language in the section entitled “restrictions on use: security” that stated it could “use information and or data relating to order entry, order execution, or indications of interest.” This language was not present in LevelL’s standard user agreements. In March 2008, the Memory Feature was turned on for orders submitted to LevelL by entities who were subscribers to both LevelL and to services offered by the Order Routing Business. From that point, the Order Routing Business benefitted from information concerning other LevelL subscribers’ order information. At that time, the Memory Feature was not turned on for the order flow of LevelL subscribers who were not also customers of the Order Routing Business. LevelL did not inform its subscribers of this change in the use of their unexecuted order information.

23. Contemporaneously, the Service Provider was seeking to revise its Original Hosting Agreement with LevelL so that the Memory Feature could be turned on for all LevelL Intent orders. The Original Hosting Agreement required the Service Provider to maintain the confidentiality of all LevelL subscriber information. The Service Provider proposed edits to these confidentiality provisions that permitted it to use LevelL order information “related to unexecuted orders to enable the [Router] application to make routing decisions.”

24. In November 2008, eBX entered into the new hosting agreement with the Service Provider (the “Revised Hosting Agreement”) that expressly authorized the Service Provider to “use that portion of eBX Data that is information related to unexecuted orders to enable the [Router] application to make routing decisions” (the “Information Sharing provision”). Shortly after the Revised Hosting Agreement was signed, the Memory Feature was turned on for all LevelL subscribers. LevelL never advised most of its subscribers about this new use of their order information by the Service Provider and its Order Routing Business.

25. Although LevelL was advised by counsel in connection with negotiating the Revised Hosting Agreement, there is no evidence that LevelL obtained specific legal advice about whether the Information Sharing provision complied with Regulation ATS.

26. On or about December 31, 2009 and unrelated to the execution of the Revised Hosting Agreement, the Service Provider and many of its assets were sold to a third party. As part of this transaction, the Revised Hosting Agreement and certain assets of the Service Provider were assigned to the Routing Broker, which continues to act as LevelL’s technology service provider and to operate the Order Routing Business.

### **Advantages of the Memory Feature to the Order Routing Business**

27. The Memory Feature benefitted the Order Routing Business because it allowed the Router to know the likely result before routing an order to LevelL, increasing the Order Routing Business’ fill rate by enabling the Router to route orders to LevelL in situations where it knew there would be a contraside Intent in LevelL and avoiding routing to LevelL when no contraside was available. In addition, the Router knew the way that

Intents in LevelL were priced and could make routing decisions for its own customers based on that pricing information. While the record shows that the actual execution price received by the LevelL subscriber and the Order Routing Business would be identical to the execution price that would have resulted had the Order Routing Business sent the same orders to LevelL without the benefit of the Memory Feature, knowledge of the pricing information of orders resting in LevelL gave the Order Routing Business the ability to route orders to LevelL in situations where the resulting price could have been better for the Order Routing Business' customer than prices available in other market centers.

28. The Information Sharing provision was significant to the Order Routing Business because it improved the efficiency of that business. In marketing materials, the Order Routing Business touted the advantages of the Memory Feature, noting that it:

- was a “virtual order book” of known dark orders from various liquidity sources, including other dark pools;
- provided a private market data source, which was known only to the Router;
- allowed the Router to route against a “known contra order”; and
- allowed the Router to use information provided by the Memory Feature for special orders, creating opportunities for price improvement and liquidity enhancement.

29. Internal documents from the Service Provider indicate that it perceived an advantage to the Order Routing Business from being able to “see the LevelL order flow in [the Memory Feature] and be able to efficiently interact with it.” The Service Provider also reacted with enthusiasm to the signing of the Revised Hosting Agreement that allowed it to turn on the Memory Feature for all LevelL orders, stating in internal email, “Yeah! Finally. I will configure key LevelL-only clients for [the Memory Feature] tonight so we can start getting the benefits ASAP.”

30. This arrangement provided the Order Routing Business with an information advantage over other LevelL subscribers, as the Order Routing Business was able to use the knowledge of other LevelL subscribers' orders to increase its execution rate within LevelL, as well as to decide whether to route to LevelL or elsewhere.

31. As a result of its privileged access to information about the orders that were submitted to, and executed in, LevelL, the Order Routing Business was able to obtain a much higher fill rate for its IOC orders than any other LevelL subscriber's IOC orders by increasing orders submitted to LevelL in circumstances where they were likely to be executed and decreasing orders submitted to LevelL in circumstances where they were less likely to be executed. For example, from about May 2008 through June 2009, the Order Routing Business's LevelL IOC orders had a fill rate ranging from about 30 to 70%, while the fill rate for other LevelL subscribers' IOC orders was about 1 to 2%. During this period, the Order Routing Business accounted for approximately 1 to 2 % of all IOC shares directed to LevelL while its executed IOC shares were between 16 and 39% of all IOC shares executed at LevelL, which accounted for between 4 and 11 % of all shares executed in LevelL.

32. In April 2011, after an examination by the Commission, LevelL caused the Order Routing Business to disable the Memory Feature. As a result of disabling the Memory Feature, the Order Routing Business' fill-rate decreased substantially, as it no longer had the benefit of the Memory Feature's knowledge of orders routed to LevelL.

### **LevelL Did Not Have Adequate Policies Concerning Regulation ATS**

33. Rule 301(b)(10) of Regulation ATS requires an ATS to establish adequate safeguards and procedures to protect subscribers' confidential trading information, and to adopt and implement adequate oversight procedures to ensure that the safeguards and procedures adopted under Rule 301(b)(10) are followed. LevelL violated this Rule by entering into the Information Sharing arrangements that allowed the Order Routing Business to remember subscribers' unexecuted order information and to use that information for its own benefit. The subscriber information that was shared with the Order Routing Business is "confidential trading information" where such use was not authorized by, or disclosed to, LevelL subscribers.

34. LevelL also failed to have safeguards and procedures to ensure that its subscribers were informed about how the Router and its Memory Feature were accessing and using their confidential order information.

35. Despite outsourcing its operations, LevelL nonetheless retained the responsibility for ensuring LevelL's compliance with all applicable laws and regulations, including Rule 301(b)(10) of Regulation ATS. Despite these obligations, LevelL failed to adopt or implement adequate oversight procedures to make sure that the Service Provider, and after 2009, the Routing Broker, protected LevelL subscribers' confidential trading information.

### **LevelL Did Not Inform, and Otherwise Failed to Notify, Its Subscribers Concerning the Use of Their Confidential Order Information by the Service Provider and Routing Broker**

36. Before the Commission's investigation into its conduct, LevelL did not disclose to most of its subscribers that the Memory Feature had access to, and used, information about unexecuted orders sent to LevelL to make routing decisions for the benefit of the Order Routing Business.

37. LevelL expressly represented to certain subscribers in their user agreements that their order information would not be shared with other users. For example, one subscriber's user agreement stated that "eBX acknowledges that the trades, trade related data, trading strategies and other information provided" by that subscriber were proprietary, and that LevelL agreed to keep such information "confidential" and not share it with any other LevelL subscriber. However, LevelL permitted the Router and its Memory Feature to access such order information for routing purposes.

38. From at least 2008 through early 2011, though LevelL disclosed to its subscribers that it obtained technology services from the Service Provider, most LevelL

subscribers were not provided with the additional information that their unexecuted order data was being remembered by the Memory Feature and was being used to make order routing decisions for customers of the Order Routing Business.

**Level Failed To Amend Its Form ATS To Disclose the Information Sharing Arrangements Until 2011 And Did Not Timely Correct Other Inaccuracies In Its Form ATS**

39. LevelL filed its initial operation report with the Commission on Form ATS in July 2006. In Exhibit E to that Form, which requires the disclosure of “the name of any entity, other than the [ATS], that will be involved in operation of the [ATS],” LevelL did not disclose that the Service Provider would be involved in providing technology and support services. In Exhibit F to its July 2006 Form ATS, which described the operation of the ATS, LevelL stated that the Service Provider would “build and host” LevelL and that customers would use the Router to submit orders to LevelL. Exhibit F also stated that “Intents are only viewable by the user that submitted that Intent. The ATS will not provide a data feed that will show in detail or in aggregate, the trading interest of all the Intents resting on the ATS book.” At the time that statement was filed with the Commission, it was accurate because the Router’s Memory Feature had not yet been enabled.

40. Between June 2007 and June 2009, eBX did not file any amendments to its Form ATS. During this time period two relevant events took place. First, in February 2008, LevelL entered into the Routing Broker User Agreement. In March 2008, the Routing Broker began to use the Memory Feature to remember and use certain LevelL subscribers’ unexecuted order information for routing purposes. This was a material change to the operation of LevelL and should have been disclosed in a Form ATS amendment at least 20 days before the change was implemented.

41. In November 2008, LevelL entered into the Revised Hosting Agreement with the Service Provider that permitted the Memory Feature to use all LevelL subscribers’ unexecuted order information to make routing decisions. This was a material change to the operation of LevelL and should have been disclosed in a Form ATS amendment at least 20 days before the change was implemented. This change also rendered inaccurate the Form ATS statement that “[i]ntents are only viewable by the user that submitted that Intent. The ATS will not provide a data feed that will show in detail or in aggregate, the trading interest of all the Intents resting on the ATS book.”

42. In the Form ATS amendment filed on June 10, 2009, LevelL amended Exhibit E to disclose that the Service Provider provided “Technology Services” to LevelL, including the “technology related to the ATS matching system” and “all implementation, hosting, maintenance services” that are “necessary to access and use the Matching Application for eBX’s operations and maintain the operating capability of the Matching Application.” LevelL did not, however, make any relevant changes to Exhibit F. In particular, it did not add a disclosure describing the Information Sharing provision with the Service Provider, and it did not explain how its prior statements about Intents only being viewable by the user that submitted them had been rendered inaccurate.

43. On or about December 31, 2009, the Service Provider assigned its rights and obligations under the Revised Hosting Agreement to the Routing Broker. This change in the identity of Level's service provider was not reported in a timely Form ATS amendment.

D. VIOLATIONS

44. As a result of the conduct described above, eBX willfully<sup>2</sup> violated Rule 301(b)(10) of Regulation ATS which requires an ATS to establish adequate safeguards and procedures to protect subscribers' confidential trading information.

45. As a result of the conduct described above, eBX willfully violated Rule 301(b)(2) of Regulation ATS which requires an ATS to amend its Form ATS before implementing material changes to its operation or when the Form ATS becomes inaccurate.

IV.

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

Accordingly, pursuant to Sections 15(b) and 21C of the Exchange Act, it is hereby ORDERED that:

A. eBX shall cease and desist from committing or causing any violation and any future violation of Rules 301(b)(2) and 301(b)(10) of Regulation ATS;

B. eBX is censured;

C. eBX shall, within 10 days of the entry of this Order, pay a civil money penalty in the amount of \$800,000 to the United States Treasury. 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

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<sup>2</sup> 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)).

identifying eBX, LLC 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 John Dugan, Associate Director of Enforcement, Boston Regional Office, Securities and Exchange Commission, 33 Arch Street, Suite 2300, Boston, MA 02110.

By the Commission.

Elizabeth M. Murphy  
Secretary