Securities Regulation Daily Wrap Up, ENFORCEMENT—New York AG charges Barclays with fraud in operation of dark pool, (Jun. 25, 2014)

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New York Attorney General Eric Schneiderman has charged Barclays with fraud in connection with the operation of the international bank's dark pool and other aspects of its electronic trading division. The attorney general alleges that Barclays falsified marketing material that purported to show the extent and type of high frequency trading in its dark pool. Rather than implementing special safeguards to protect clients from predatory high-frequency traders, the attorney general claims Barclays operated its dark pool to attract and favor high-frequency traders.

Pool of predators. "The facts alleged in our complaint show that Barclays demonstrated a disturbing disregard for its investors in a systematic pattern of fraud and deceit," said Attorney General Schneiderman in a news release. "Barclays grew its dark pool by telling investors they were diving into safe waters. According to the lawsuit, Barclays' dark pool was full of predators – there at Barclays' invitation."

Toxic traders. The suit alleges that Barclays promoted a service called Liquidity Profiling, which the firm represented as a "surveillance" system that tracked every trade in Barclays' dark pool in order to identify predatory traders, rate them based on their trading behavior, and hold them accountable for engaging in predatory practices. Instead, the complaint alleges, Barclays never prohibited any trader from participating in its dark pool, did not regularly update the ratings of high-frequency trading firms, and "overrode" certain Liquidity Profiling ratings by assigning safe ratings to traders that were otherwise determined to be toxic.

Moreover, the complaint alleges, Barclays actively sought to attract high frequency traders by giving them systematic advantages over others trading in the pool. Among other things, the attorney general claims that Barclays told investors that the firm does not favor its own dark pool when routing client orders to trading venues, while doing just that, and also falsified an analysis of how it routed a major client's orders.

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