SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

THE PEOPLE OF THE STATE OF NEW YORK By ERIC T. SCHNEIDERMAN, Attorney General of the State of New York,	Index No.:
Plaintiff,	**SUMMONS**
- against -	Plaintiff Designates New York County as the Place of Trial
BARCLAYS CAPITAL, INC., and BARCLAYS PLC,	
Defendants.	

TO THE ABOVE-NAMED DEFENDANTS:

YOU ARE HEREBY SUMMONED to answer in this action and serve a copy of your answer on the Plaintiff's attorney within twenty (20) days after service of this summons, exclusive of the day of service. If this summons is not personally served upon you, or if this summons is served upon you outside of the State of New York, then your answer or notice of appearance must be served within thirty (30) days. In case of your failure to appear or answer, judgment will be taken against you by default, for the relief demanded in the Complaint.

Dated: New York, New York
June 25, 2014

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By: ______________________
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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

THE PEOPLE OF THE STATE OF NEW YORK By ERIC T. SCHNEIDERMAN, Attorney General of the State of New York,		
		Index No.:
Plaintiff,		
- against -		**COMPLAINT**
BARCLAYS CAPITAL, INC., and BARCLAYS PLC,		
Defendants.		

Plaintiff, the People of the State of New York, by Eric T. Schneiderman, Attorney General of the State of New York (the "Attorney General"), alleges the following against Barclays Capital, Inc. and Barclays PLC (together, "Barclays"):

PRELIMINARY STATEMENT

1. This is a case about fraud and deceit by one of the world's largest banks. Barclays operates in fifty countries with particularly large business operations in New York and London. The facts in this case concern a major business division in Barclays' New York office, the Equities Electronic Trading division. In that division, Barclays operates a private securities trading venue known as a "dark pool." From 2011 to the present, Barclays embarked on a business strategy to dramatically increase the market share of its dark pool, with the goal of making it the largest dark pool in the United States. Barclays accomplished this through a series of false statements to clients and the investing public about how, and for whose benefit, Barclays operates its dark pool. In short, contrary to Barclays' representations that it implemented special

safeguards to protect clients from "aggressive," "predatory," or "toxic"[1] high frequency traders, Barclays has operated its dark pool to favor high frequency traders. Barclays has actively sought to attract such traders to its dark pool, and it has given them advantages over others trading in the pool.

2. As discussed in further detail below, Barclays' wrongdoing includes the following:

a) Barclays falsified marketing material purporting to show the extent and type of high frequency trading in its dark pool. That marketing material was false and misleading because, among other things, Barclays intentionally excluded from the material the dark pool's then-largest participant – a high frequency trading firm Barclays knew engaged in predatory behavior in the dark pool. Internally, Barclays acknowledged that it was "taking liberties" with the truth by suppressing the disclosure of this high frequency trading firm, but decided to falsify the analysis in order to "help ourselves";

b) Barclays falsely marketed the percentage of aggressive high frequency trading activity in its dark pool, asserting to clients and to the investing public that less than 10% of the trading activity in the pool was "aggressive," while at the same time secretly indicating to at least one high frequency trading firm that the level of such trading activity was at least 25%;

c) Barclays made a series of false representations to clients about its "Liquidity Profiling" service. Barclays claimed that its Liquidity Profiling service "analyzes

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[1] The descriptive terms used in this Complaint to categorize high frequency trading, including "aggressive," "predatory," or "toxic" are all taken from Barclays' own statements and marketing materials.

each interaction in the dark pool" to "protect [clients] from predatory trading," to "continuously police . . . trading activity" and to "maintain quality flow" in the dark pool. In reality, and undisclosed to clients, Barclays failed to provide those services, because it (i) failed to remove known predatory traders from its dark pool; (ii) failed to regularly profile traders in its dark pool; (iii) granted liberal "overrides" to high frequency trading firms and to Barclays' own internal trading desks (which themselves employ "aggressive" trading strategies), in order to make them appear less "toxic" than they really are; (iv) failed to apply the protections of Liquidity Profiling to a significant portion of the trading in its dark pool; and (v) misled clients as to how Liquidity Profiling actually evaluated traders;

d) Barclays falsely represented that it routed client orders for securities to trading venues in a manner that did not favor Barclays' own dark pool. While representing that Barclays "treat[s] all venues the same based on execution quality," Barclays, in fact, routed a disproportionately high percentage of client orders to its own dark pool. When a detailed analysis of Barclays' order routing practices was conducted for a major institutional investor – showing that Barclays was routing and executing the vast bulk of this client's sampled orders to Barclays' own dark pool – Barclays senior executives directed that a written presentation to that client include falsified information, in an effort to mask Barclays' biased order routing practices; and

e) At the same time that Barclays marketed its dark pool to institutional investors as offering protection from high frequency traders, Barclays secretly gave high frequency trading firms informational and other advantages over other clients trading in the dark pool. For instance, Barclays provided detailed information regarding the structure and composition of its dark pool to high frequency trading firms, including information about the identity and trading activity of other traders in the pool. Such information would allow high frequency trading firms to maximize the effectiveness of their aggressive trading strategies in the dark pool. Barclays did not generally provide such information to its brokerage clients. Barclays also charged high frequency trading firms virtually nothing to trade in its dark pool.

3. The facts described in this Complaint are the result of an investigation by the Office of the Attorney General. The Attorney General's investigation has been aided significantly by a number of high-level former Barclays insiders, each of whom was in a position to observe much of the conduct described in this Complaint. These witnesses provided meaningful assistance to the Attorney General's investigation.

4. As a result of the material misstatements set forth herein and the pattern of fraud and deceit engaged in by Barclays, the Attorney General brings this action pursuant to General Business Law §§ 352 *et seq*. (the "Martin Act") and Executive Law § 63(12).

PARTIES

5. Plaintiff Eric T. Schneiderman is the Attorney General of the State of New York and brings this action on behalf of the People of the State of New York in connection with the Attorney General's role to protect the integrity of the securities markets in the State.

6. Barclays PLC is registered in England. Barclays PLC functions in the United States through Barclays Capital Inc., an affiliate of Barclays PLC. Barclays Capital Inc. is a registered broker dealer and investment adviser with its primary offices at 745 Seventh Avenue, New York, New York.

7. As part of its business in New York, Barclays operates as a registered broker-dealer. Barclays' brokerage clients, serviced out of Barclays' New York offices, include many institutional investors, mutual funds, pension funds, and others ("buy-side" clients). Many of Barclays' buy-side clients manage accounts for individuals and retail investors.

FACTUAL ALLEGATIONS

I. BACKGROUND

8. In the United States, equities securities are traded on eleven public stock exchanges and dozens of privately-owned and operated trading venues, including venues known as "dark pools."

9. Public stock exchanges run on computer systems that match tens of millions of orders to buy and sell every day. Orders are generally visible to participants in these marketplaces, and executions are posted immediately.

10. Dark pools also match buy and sell orders. However, whereas public exchanges immediately display to the market the submission of pending stock orders, dark pools generally do not. There are several dozen dark pools operating in the United States. It is estimated that, today, over forty percent of all U.S. equities trades are executed in dark pools.

11. High frequency trading is a type of trading that uses sophisticated computer programming to conduct stock transactions extremely quickly in order to take advantage of small, momentary changes in stock prices. While not all high frequency traders use the same kinds of trading strategies, certain characteristics are common to high frequency trading firms. These firms tend to trade securities for their own account (as opposed to doing so on behalf of clients), and use high-speed, sophisticated computer programs to generate, route, and execute orders rapidly on multiple exchanges. High frequency trading firms typically maintain their unhedged positions in a given security for a very short period of time (frequently one second or

less) and have a high rate of cancelled orders (in other words, a high rate of orders that are submitted to trading venues, but are cancelled before the order is executed). They typically begin and end each trading day without significant, unhedged positions.

12. Some estimates place high frequency trading activity at over fifty percent of the total volume in U.S.-listed equities.

13. In order to execute their trading strategies effectively, high frequency traders seek speed advantages. Some of these traders pay to "co-locate" or "cross-connect" their trading computers in the same facilities as public exchanges and dark pools in order to reduce the amount of time it takes to receive market information from those trading venues, and in order to rapidly place or cancel orders. These firms pay a premium for "direct data feeds" from the public exchanges, which are high-speed data feeds that travel faster and contain more information than market data available to ordinary investors by other, less expensive means.

14. Those speed and technology advantages allow high frequency traders to profile the pending orders on an exchange in order to detect the presence of large pending orders, usually from institional investors. This "information leakage," allows high frequency traders to trade ahead of an anticipated stock purchase or otherwise have an impact on price. Speed and technology advantages also allow for strategies that seek to exploit the small, temporary pricing dislocations in a security that occur because of differential and/or delayed access to market data. This strategy is sometimes referred to as "latency arbitrage," because the trader is seeking to exploit the relative slowness, or "latency," in the transmission of market data experienced by other participants. Barclays itself commonly labeled these types of high frequency strategies as "toxic," "predatory," or "aggressive." Ordinary investors generally seek to avoid interactions with high frequency traders because of the effect those sorts of strategies can have on an investor's trading performance.

15. Dark pools have grown in number and market share, at least in part as a means to protect institutional traders with large orders and long-term positions from the potential advantages and strategies used by high frequency trading firms on the public exchanges, as discussed above.

II. **BARCLAYS SOUGHT TO MAKE ITS DARK POOL THE LARGEST IN THE UNITED STATES**

16. In the years following its creation, Barclays' dark pool – known as Barclays LX – did not stand out among the several dozen dark pools operating in the United States. As reflected in Barclays own marketing material in late 2011, Barclays' dark pool was essentially middle-of-the-pack, when measured by average daily volume of share traded.

17. Growing its dark pool to become the largest dark pool in the United States was a principal goal of Barclays' Equities Electronic Trading division, and was central to driving profits for the division. Speaking in 2013, the Head of Barclays' Equities Electronic Trading division (the division that houses the dark pool) recalled that "[w]e laid out a plan two years ago to overhaul our offering end to end, gain market share and provide clients with the best electronic trading tools in the market."

18. In an internal document, Barclays instructed its employees that "[a]ggregating [order] flow into Barclays LX has strategic and economic value for the entire Equities business," including the savings Barclays would realize by not having to pay commissions to execute trades on other venues; fees gained from firms paying to trade in the dark pool; and the "internal trading P&L [profit and loss] opportunities" available to internal Barclays trading desks that trade in the dark pool against brokerage client order flow. Barclays also identified the "market share value of attracting more [order] flow" into its dark pool. In other words, as Barclays' dark pool became bigger, it would become increasingly attractive to additional traders seeking

opportunities to trade. Internal Barclays documents valued this growth opportunity at between $37 and $50 million per year.

19. Besides the profit motive inherent in growing its dark pool, growing Barclays' dark pool to be the largest in the United States was something of a prestige project. Barclays' dark pool was referred to internally as "The Franchise."

20. According to a former senior Director in that division, "[a]t every sales meeting or product meeting, the main goal they were talking about was to grow the size of [Barclays' dark pool] to become the largest pool. All the product team's goals, which would also include their compensation[,] were tied to making the pool bigger. [Barclays had] great incentive at all costs to make the pool bigger."

21. To grow its dark pool, Barclays had to increase the number of orders that Barclays, acting as a broker, executed in the dark pool. This required Barclays to send more of its clients' orders into the dark pool, and to make sure that there was sufficient liquidity in the dark pool to fill those orders. Barclays looked to attract high frequency traders to its dark pool to meet this need.

22. At the same time, Barclays sought to convince its brokerage clients that its dark pool was a safe place to trade, insulated from the kinds of aggressive or predatory high frequency trading practices that are associated with other trading venues, including the public exchanges.

23. In written marketing materials, statements to the media, and in sales meetings with clients, potential clients, and other market participants (hereinafter, "clients"), Barclays represented that it provides a safe, transparent trading environment, and helps to protect its clients from the risks of aggressive high frequency traders.

24. For instance, in March 2013, a Managing Director and Head of Barclays' Equities Electronic Trading division stated that Barclays' dark pool "is an integral part of our electronic

trading offering, providing clients with enhanced execution quality . . . built on transparency and preventing information leakage. We have built in safeguards to manage toxicity, and to help our institutional clients understand how to manage their interactions with high-frequency traders."

25. Barclays' efforts to convince clients, potential clients, and other market participants of the safety of trading in its dark pool relied, in large part, on a service Barclays calls "Liquidity Profiling." This Liquidity Profiling" service purportedly allowed Barclays to monitor the "toxicity" of the trading behavior taking place in its dark pool and, as Barclays claimed, "hold [traders] accountable" if their trading was "aggressive," "predatory," or "toxic."

26. First marketed in 2011, Barclays represents that Liquidity Profiling works by grouping the traders in its dark pool into six categories based on their trading behavior, ranked 0 to 5. In the "0" and "1" categories are those traders conducting the most aggressive, predatory trading activity; in the "4" and "5" categories are those traders conducting the safest, most passive, long-term investor-like trading activity. Participants in Barclays' dark pool were told that they could disable their orders from interacting with traders falling into any of the various categories – in particular, clients could opt-out of trading with traders that were identified by the Liquidity Profiling service as engaging in potentially harmful high frequency trading strategies.

27. Barclays represented Liquidity Profiling as a "sophisticated surveillance framework, helping to protect you from predatory trading . . . our team proactively monitors the behavior of individual participants and quickly responds with corrective action when adverse behavior is detected." Liquidity Profiling, according to Barclays, "improve[s] the overall quality of [Barclays' dark pool because] High-alpha takers [*i.e.*, high frequency traders] can be held accountable . . . transparency means that aggressive flows will be quickly identified by the Barclays ATS team."

28. In various industry publications, Barclays has represented that "Liquidity Profiling analyzes each interaction in the dark pool, allowing us to monitor the behavior of individual participants . . . providing clients with transparency about the nature of counterparties in the dark pool and how the control framework works." "By identifying aggressive behavior, we can take corrective action with clients who exhibit opportunistic behavior in the pool." Barclays' stated that it would "refuse a client access" to the dark pool if they engaged in aggressive or "toxic" high frequency trading strategies.[2]

29. Barclays' Head of Equities Electronic Trading has represented that through the Liquidity Profiling service "we are able to restrict HFTs interacting with our clients [and] we're getting the better half of their order flow (i.e. higher quality liquidity) such as hedges or low impact positions . . . When you're watching behavior to that degree, behavior changes. If an end user has been delivering low-rated flow, we tell them 'Either change it, or don't send it here.'" He further represented that Liquidity Profiling lets Barclays "make sure that we have very good participants in our pool."

30. In response to the recent public, industry-wide discussion about the potential risks of high frequency trading, Barclays has relied heavily on its Liquidity Profiling service to reassure investors and clients that Barclays keeps them safe from aggressive, predatory high frequency traders. On March 28, 2014, Barclays' Head of Equities in the Americas distributed "Internal Q&A and Talking Points on Barclays Electronic Trading and Order Handling Practices." The document, marked "For Internal Use Only," notes that given "recent press on market structure [and the] NY Attorney General's comments on HFT . . . we have an opportunity to engage with clients about how we think about electronic trading and best execution"

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[2] Such statements appeared in, among others, *Traders Magazine*, *Markets Media*, and *HedgeWeek*.

(emphasis omitted). Barclays instructed its employees to represent to clients that Barclays "[i]nvented Liquidity Profiling to police trading behaviour" in the dark pool, and Barclays "can deny access to predatory participants." Employees were instructed to represent that "Liquidity Profiling encourages passive/benign liquidity provision," and that Liquidity Profiling "manages toxicity within the pool without limiting access to potentially beneficial liquidity."

31. By late 2013, independent analysts reported that Barclays operated one of the two largest dark pools in the United States, as measured by reported average daily shares traded. According to one industry publication, Barclays, "which was barely among the 10 biggest U.S. dark pools as recently as 2009, moved into second place in January 2013, and later in the year ascended to the top of the heap."[3] Barclays marketing material dated April 2014 touted the market share of its dark pool:

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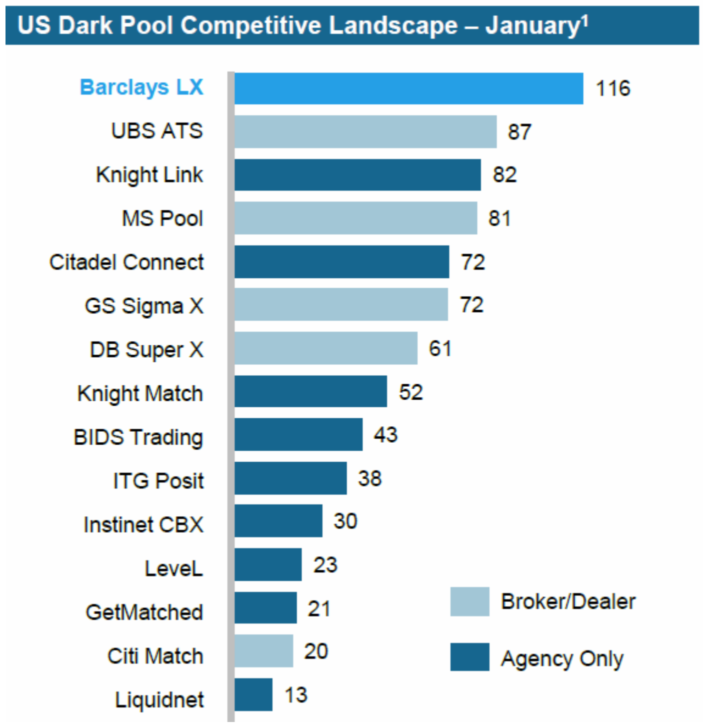
[3] Certain published reports suggested that Barclays was the second largest dark pool operator in the United States, given that one other dark pool operator had declined to report its volumes. Barclays has marketed itself as the largest, based on reported volumes. In either event, Barclays has become one of the two largest dark pools in the United States.



32. In February 2014, Barclays' dark pool was named the "Best Dark Pool" by an industry publication. In commenting on the award in marketing material labeled "for institutional investors only," Barclays' Head of Equities Electronic Trading attributed its growth to Barclays' commitment to being transparent with its institutional investor clients regarding how Barclays operates, how Barclays routes client orders, and the kinds of counterparties traders can expect to deal with when trading in the dark pool. Transparency was "the one issue that we really took a stance on . . . We always come back to transparency as the key driver — letting [clients] know how we're interacting with their flow and what type of flow they're interacting with." "Transparency on multiple levels is a selling point for our entire equities franchise."

III. BARCLAYS COMMITTED FRAUD IN CONNECTION WITH THE MARKETING AND OPERATION OF ITS DARK POOL

33. Far from being transparent regarding trading activity in its dark pool, Barclays made material misrepresentations regarding the extent of aggressive or predatory high frequency trading activity in the pool, and the level of protection Barclays provided from such activity.

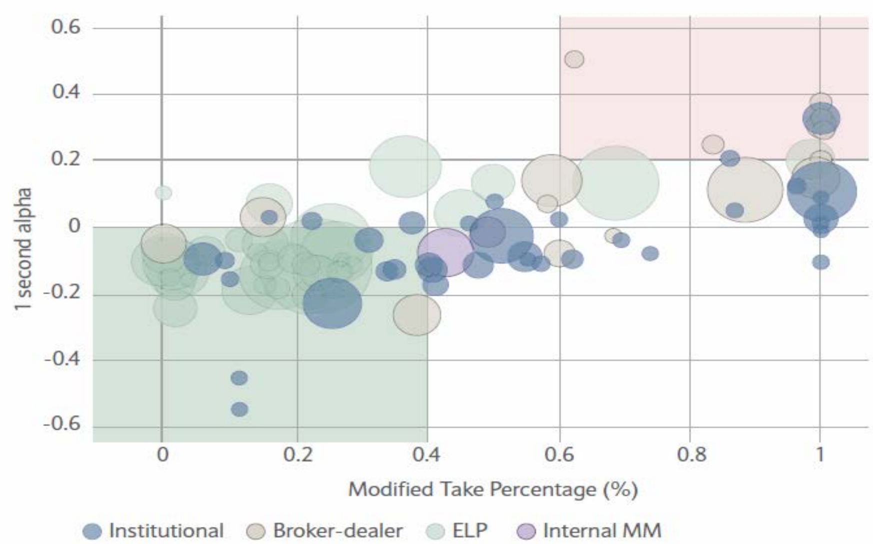
A. Barclays Falsified an Analysis Purporting to Show the Extent of High Frequency Trading in its Dark Pool

34. Barclays made false representations regarding the participants in its dark pool.

35. As one part of its marketing effort, Barclays created and disseminated analyses about the landscape of trading in its dark pool, purporting to show how clients were protected from aggressive high frequency trading activity and underscoring Barclays' commitment to transparency. One such analysis was contained in a widely-disseminated document intended for institutional clients titled *Liquidity Profiling – Protecting You in the Dark*. That document included an analysis purporting to represent the "liquidity landscape" of Barclays' dark pool. The results of the analysis were presented as follows:

Figure 1: Sample liquidity landscape by category

Participants in the same category do not trade in the same manner. With LX Profiling, the Barclays ATS team can quickly identify aggressive flow from an individual client.



36. Each circle in the chart represents one firm trading in Barclays' dark pool. The size of the circle corresponds to the level of trading activity conducted in the dark pool by that firm. Different types of traders are assigned different color circles; the pale green circles are

"electronic liquidity providers" ("ELP"), which is the term Barclays used for high frequency traders. Within the chart are two color-coded regions, a green rectangle representing "passive" (*i.e.*, safe, non-predatory) trading activity, and a red rectangle representing "aggressive" (*i.e.*, predatory) trading. The x-axis, ("modified take percentage," which is percentage of a trader's orders that take liquidity), and the y-axis, ("1-second alpha," which is the price movement in the one-second following each trader's trades), are presented here as relevant measures of trading behavior on the dark pool.

37. The chart represents that very little of the trading in Barclays' dark pool is "aggressive." As represented by the chart, most of the trading in the dark pool is "passive," and most of the ELP/high frequency activity is "passive." In its entirety, the chart represents that Barclays' dark pool is a safe venue with few aggressive traders.

38. Barclays' sales staff heavily promoted this analysis to investors as a representation of the trading within the dark pool, and marketed that analysis as "a snapshot of the participants" in order to show clients "an accurate view of our pool." In addition, certain Barclays marketing materials appended a notation to the chart explaining that it portrays the top 100 clients trading in the dark pool.

39. These representations were false. The chart and accompanying statements misrepresented the trading taking place in Barclays' dark pool. That is because senior Barclays personnel de-emphasized the presence of high frequency traders in the pool, and removed from the analysis one of the largest and most toxic participants in Barclays' dark pool.

40. On October 5, 2012, a draft version of the analysis was circulated by email to senior executives in Barclays' Equities Electronic Trading division. The accompanying email noted that Barclays "de-emphasized the number of ELPs [electronic liquidity providers, or high frequency traders] by moving them to the back." The email also stated that the chart "remov[es]

Tradebot." Tradebot Systems had historically been, and was at that time, the largest participant in Barclays' dark pool, with an established history of trading activity that was known to Barclays as "toxic." Those alterations had the effect of obscuring the amount of high frequency trading activity in the dark pool by disguising the total number of high frequency trading firms, and deleting one significant firm altogether.

41. In a response email, one employee objected to the modified chart, stating that removing Tradebot from the analysis was a falsification of the data.

42. In response to this objection, a Director in the Equities division wrote that "the point of the chart is not to show what's in the pool. The point is to market our capability . . . to monitor individual participants in the pool."

43. A Vice President responsible for selling the dark pool to clients disputed that explanation, replying to the group that "[m]y point when selling that picture was always: 'here is a snapshot of the participants in [Barclays' dark pool] as an accurate view of our pool.' I was never using it like an 'illustration'" of Barclays capability to monitor the pool. "I had always liked the idea that we were being transparent, but ***happy to take liberties if we can all agree***" (emphasis added).

44. Barclays' Head of Product Development (who was also the second in command within Barclays' Equities Electronic Trading division) agreed. He responded, "I think the accuracy [of the chart] is secondary to [the] objective" of showing clients that Barclays monitors the trading in its dark pool, and "so if you want to move/kill certain bubbles, it doesn't really matter."

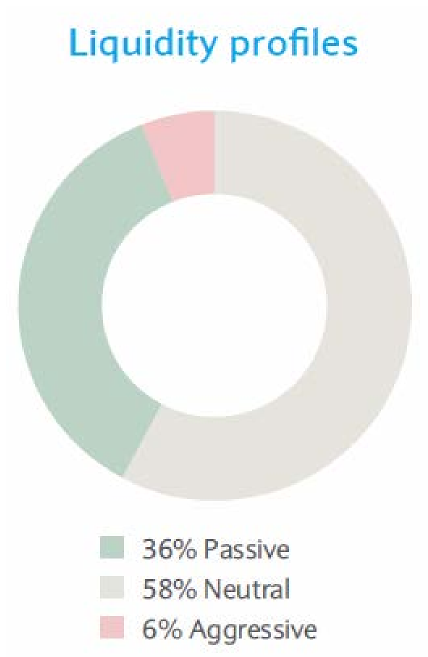
45. Barclays' Head of Equities Sales responded, "Yes! U smart."

46. In another email that same day, Barclays' Head of Equities Sales noted in reference to the analysis that some in the industry viewed Barclays' dark pool as a "toxic landfill," and so "[i]f we can help ourselves we should[;] its in our control."

47. As of the filing of this Complaint, that marketing material remains in circulation, containing the same illustration and the same misrepresentations.

B. Barclays Underrepresented the Amount of "Aggressive" Trading Activity in its Dark Pool

48. As part of its effort to convince clients that it protected them from aggressive high frequency trading, Barclays issued marketing material that included representations purporting to show the amount of aggressive trading activity in its dark pool. In marketing materials released in early 2013, Barclays claimed that the trading in its dark pool was "48% passive," "43% neutral," and "9% aggressive." In March 2014, Barclays issued revised marketing materials that were even more favorable for Barclays – asserting that its dark pool was comprised of 36% passive activity, 58% neutral activity, and 6% aggressive activity:



This marketing material was used by Barclays at least through April 2014.

49. Those figures were false. Barclays separately acknowledged there is significantly more "aggressive" activity in Barclays' dark pool than the "6% aggressive" represented to clients.

50. In March 2014, Barclays was engaged in discussions with a prominent high frequency trading firm wherein Barclays itself categorized approximately 25% percent of the orders taking liquidity in its dark pool as aggressive. In an internal document collecting the information received from Barclays, that firm summarized the data provided to it by Barclays, and concluded that the trading activity in Barclays' dark pool was "50% good, 50% aggressive."

C. "Liquidity Profiling," as Applied by Barclays, Does Not Protect Barclays' Clients from Predatory High Frequency Trading Tactics

51. As noted above, Barclays represented that its Liquidity Profiling helps "protect you from predatory trading . . . [by] ***quickly respond[ing]*** with ***corrective action*** when adverse behavior is detected" (emphasis added). According to Barclays, "Liquidity Profiling analyzes ***each interaction*** in the dark pool" to "***police*** trading behavior" so that Barclays is "able to ***restrict HFTs*** interacting with our clients" (emphasis added).

52. Those claims were false. Contrary to Barclays' representations, the Liquidity Profiling service offers little or no benefit to Barclays' clients – those who are supposed to be protected by Liquidity Profiling – because Barclays does not actually police or punish bad trading behavior. Also, Barclays has failed to regularly update the profiles of traders in its dark pool. Furthermore, Barclays altered the profiles of certain predatory traders when it benefitted Barclays to do so, and Barclays does not even apply the Liquidity Profiling service to the bulk of orders submitted to the dark pool.

53. In sum, Barclays' representations that it provided a robust, continuous service that protected Barclays' clients was not true.

54. *First*, despite Barclays' claim that it uses Liquidity Profiling to police its dark pool, and will "refuse a client access" if that trader's activity becomes toxic, Barclays has never prohibited a single firm from participating in its dark pool, no matter how toxic or predatory its activity was determined to be.

55. Indeed, Barclays has known about the high levels of toxic activity occurring in its dark pool – including latency arbitrage – and has been aware of which firms are responsible, yet Barclays has refused to stop it.

56. For example, on January 16, 2014, senior leaders in the Equities Electronic Trading division were provided an analysis identifying over a dozen major high frequency trading firms engaged in significant trading activity in Barclays' dark pool. That analysis discussed those firms' history of sending "toxic" order flow. One high frequency trading firm was described in the analysis as "historically . . . very toxic." Another firm was described as having "[trading activity that] is very toxic, and the client is up-front about this." Another firm was described as having "[k]nown latency arbitrage flow" in the dark pool.

57. Barclays has not denied any of those firms (or others) access to its dark pool, despite its representations that it will identify "aggressive behavior, [and] take corrective action" to "refuse a client access" to the dark pool if such aggressive or toxic high frequency trading strategies are discovered.

58. *Second*, Barclays has not regularly updated the ratings of traders monitored by the Liquidity Profiling service, meaning that traders have often been categorized in ways that did not reflect their aggressive trading activity in Barclays' dark pool. Failing to properly rate traders

gives Barclays' clients a false understanding of their exposure to predatory high frequency trading activity.

59. According to a former senior-level employee in the Equities Electronic Trading division, updates to Liquidity Profiles were infrequent and inconsistent, and participants "could be and would be in the wrong tiers for months before [re-]calibration happened." In an internal document dated December 13, 2013, Barclays recognized that Liquidity Profiling "reviews were sporadic and sometimes not performed" for months at a time. "As a result Liquidity Profiles may become stale and inaccurate," which would result in "clients . . . not getting the quality executions expected."

60. *Third*, Barclays has applied "overrides" to a number of traders in the dark pool, assigning safe Liquidity Profiling ratings to certain traders that should have been rated as toxic.

61. A number of those "overrides" have been applied to internal Barclays trading desks. For instance, an internal, proprietary trading desk named Barclays Capital Market Making, which engaged in high-speed, high-order volume trading akin to high frequency trading, was granted an "override." That trading desk should have been categorized as a "0" or "1" trader in the Liquidity Profiling system based on objective profiling criteria (and, as such, been blocked by those relying on the Liquidity Profiling service to help them avoid trading with high frequency traders), but instead was categorized as a "4." That "override" had the effect of making Barclays Capital Market Making appear to be a safe trading partner to Barclays' clients, when in fact it was not.

62. Other overrides were applied to firms for whom Barclays' acted as a broker. Barclays justified these "overrides" based not on the characteristics those firms' trading activity in the dark pool, but simply based on Barclays' own economic interest, noting that "it is our darkpool, after all."

63. Barclays' management has recognized that its "overrides" are problematic. In an internal document dated December 13, 2013, Barclays noted that management did not "formalise a control framework for monitoring customer trading patterns (Liquidity Profiling), including . . . documentation and escalation requirements for profile overrides." Barclays recognized that this could "give the appearance that certain clients are shown favoritism during the profiling process."

64. *Fourth,* Liquidity Profiling does not apply to a significant portion of the trading activity in Barclay's dark pool. Client orders that are routed to the dark pool via Barclays' proprietary algorithms are not included in the Liquidity Profiling service. Similarly, Liquidity Profiling only protects traders when they ***provide*** liquidity (*i.e.*, post an order to the dark pool). Liquidity Profiling does not protect traders when they ***take*** liquidity (*i.e*., accept an already-posted order). As such, a significant portion of Barclays' clients' traders are completely unprotected by Liquidity Profiling from interaction with aggressive or toxic traders. Those material facts are not disclosed in Barclays' marketing materials.

65. *Fifth*, Barclays falsely represented to clients how Liquidity Profiling evaluated traders. As discussed in Section III (A), above, Barclays disseminated a document entitled *Liquidity Profiling – Protecting You in the Dark*, which included a chart purporting to represent the "liquidity landscape" in Barclays' dark pool. That chart is misleading because traders represented to be in the "passive" field of the chart were not necessarily rated by the Liquidity Profiling service as having passive trading behavior on the 0-5 scale described above. The same is true of the "aggressive" field. Those traders that were represented to be in the "aggressive" field of the chart were not necessarily rated by the Liquidity Profiling service as having aggressive trading behavior. That is because "Modified Take %" (the x-axis of the chart) is not used to categorize traders by the Liquidity Profiling service, which uses an altogether different

metric. The chart therefore misrepresents both the metrics used by Barclays to classify traders in the dark pool, and the kind of trading taking place in the dark pool.

66. Barclays is aware of the failings of its Liquidity Profiling service. In an internal document dated December 2013, Barclays recognized that "Liquidity Profiling reviews may not be completed for all clients, may rely on inaccurate information and results and rationale for profiling changes may not be evidenced; leading to reputational damage as the service . . . may not function as advertised to clients."

67. As stated by one former Barclays Director in the Equities Electronic Trading division, Barclays "purport[s] to have a toxicity framework that will protect you when everybody knows internally that that thing is done manually with outliers removed and things are classified [only] if they feel like it." Another former Director in the division described Liquidity Profiling as "a scam."

D. Barclays Falsely Represented the Manner in Which it Routes Client Orders

68. One of the services offered by Barclays as a broker is to direct, or route, its clients' orders for securities to the various exchanges on which those securities trade. Barclays markets its order routing capability as an essential part of its electronic trading business. Barclays operates its electronic order routing within the Equities Electronic Trading division, the same division in which Barclays' dark pool is operated.

69. In marketing materials, Barclays represented that its routing system "uses unique market intelligence, predictive liquidity models, and high-performance technology to maximize fill rates while reducing information leakage." According to Barclays, it "synthesizes historical and real-time data and executions to predict liquidity," using "[p]robability of fill models for both aggressive and passive trading." Barclays represented to investors that, when routing client orders to the various trading venues in the United States, Barclays ranks trading venues

"dynamically," using "parallel routing to all venues based on probability of fill." Barclays claimed that it "[t]reat[s] all venues the same based on execution quality." In short, Barclays claimed that it routed client orders in a manner that was not biased in favor of any particular trading venue.

70. On March 28, 2014, Barclays distributed a document to employees that included "Selling points on our dark pool and order handling practices." Barclays instructed its employees to tell clients that, among other things:

- Barclays "[e]mploy[s] predictive models to optimize where and how we post and take liquidity," (emphasis omitted),
- The "primary factors" taken into account by Barclays when routing its clients' orders "include: real-time market data, real-time venue fill rates, and historical venue market share," and
- Barclays "dynamically learns where liquidity is trading" and routes trades to those venues.

71. In April 2014, in response to media coverage about the prevalence of high frequency trading in the U.S. markets, Barclays distributed a special communication to clients seeking to assuage worries about Barclays' order routing and dark pool practices. That communication stated, in relevant part, that Barclays "handle[s] orders in the best interests of our clients. Order routing decisions are primarily based on the probability of fill; venue ranking is data-driven and our router dynamically learns with experience."

72. These representations were consistent with how Barclays' sales staff has marketed Barclays' smart order routing services to investors. One former Director in Barclays' Equities Electronic Division recalled that in every sales presentation that they were present for, clients were told that "the router was routing based on best execution," and that it was "dynamic, making decisions based on market conditions and probability of achieving a trade."

73. Barclays' representations about its order routing practices were false and misleading.

74. In truth, and contrary to Barclays' representations that it "treat[s] all venues the same based on execution quality," essentially all client orders were routed to Barclays' dark pool first, regardless of the probability that a given trade would execute there, would execute at a favorable price, or would cause information leakage. According to an internal analysis conducted by Barclays, after having been routed to Barclays' dark pool, unfilled orders were then routed disproportionately to other trading venues based on where Barclays had been most profitable over the previous twenty days.

75. However, Barclays did reveal its true order routing preferences to a select group of high frequency trading firms. In March 2014, Barclays told one such firm that, apart from minor exceptions, "everything goes to [Barclays' own dark pool] first." Barclays told another high frequency trading firm that approximately 90% of all orders "are first directed into the dark pool."

76. As recalled by a former Barclays employee whose job required knowledge of order routing: "[Barclays was] supposed to route trades based on best probability of a fill. Based on what was the best benefit to clients. That is the way it was supposed to work . . . [it did not work that way] because that was not economically advantageous for Barclays." In the words of this Director, Barclays routes trades to its own dark pool "whether it is right or not."

77. Barclays was well-aware that its order routing practices were in conflict with its public representations. In 2013, senior Directors in the Equities Electronic Trading division began a broad analysis of Barclays' order routing practices, gathering detailed trade data from over 100 million unique trades. Upon analyzing the data, these Directors determined that Barclays had an extremely high "internalization rate" – that is, a high rate of routing client orders

into Barclays' own dark pool. The analysis also determined that certain trading venues were disadvantaged by Barclays' routing procedures, either because Barclays was submitting orders that had no chance of being accepted in that particular venue, or because those venues were not seen as financially beneficial for Barclays. The analysis also determined that the trading venues to which Barclays routed unfilled orders (after first having routed them to its own dark pool) tended to be venues hosted by high-speed trading firms, "[n]one of which," recalled one Director, "had a reputation for being favorable to clients from an execution perspective." Those venues included Knight Capital, Getco, and Citadel.

78. In October, 2013, Barclays prepared a trading analysis for a major institutional investor that services millions of individual accounts both inside the United States and abroad ("Institutional Investor"). The analysis determined that:

- Approximately 88% of this Institutional Investor's sampled trades in dark venues were executing in Barclays' dark pool;
- Approximately 60% of the trading counterparties for the Institutional Investor's sampled orders were high frequency trading firms; and
- Approximately 75% of *all* orders routed by Barclays to dark venues were executing in Barclays' own dark pool.

79. Those extraordinarily high internalization rates suggest that Barclays' representations to investors that it did not route orders in favor of any particular trading venue were false or misleading.

80. In preparation for a meeting with the Institutional Investor to explain these findings, two senior Directors prepared a PowerPoint presentation that included the results of the trading analysis. Two days before the scheduled meeting, one of those Directors was called into a meeting with senior leadership in the Equities Electronic Trading division, who instructed him not to disclose the findings to the client. According to this Director, "[t]here was no suggestion

at that meeting, or at any other point, that the analysis was wrong," merely that it should not be shared with the client because it reflected poorly on Barclays. Despite the pressure from senior leadership, this Director declined to withhold the findings from Institutional Investor. The next day, and prior to the scheduled meeting with the Institutional Investor, this Director was fired.

81. Another Director was then instructed to change crucial figures in the PowerPoint presentation, in order to make them more favorable to Barclays. Specifically, that Director was instructed to change Barclays' internalization rate for all orders routed to dark venues from 75%, as noted above, to 35% – a number far less damning to Barclays and which would have the effect of making the Institutional Investor's 88% internalization rate look like an outlier. As described by this former Director, this was an "intent [by Barclays] to shift blame to the client . . . This 35 percent is not true and not validated by anything." Despite this Directors' protestations, the analysis was altered, and the PowerPoint was presented to the Institutional Investor. Shortly after this incident, this Director resigned from Barclays.

82. As one former Barclays employee recalled, "what Barclays did was rather than route [client orders] in a manner that would fulfill [their] needs that would give best execution . . . they jammed it all into [Barclays own dark pool]." Another former employee recalls, "such a high [] internalization rate could suggest that there were other opportunities being missed and [clients] weren't receiving the true best executions."

E. Contrary to its Representations, Barclays Did Not Protect Clients from High Frequency Traders; In Fact, Barclays Catered to High Frequency Traders

83. As noted above, Barclays represented to clients that its dark pool offered protection from aggressive or predatory high frequency traders. As just one example, the Head of Barclays' Equities Electronic Trading division represented to clients that "we are able to

restrict HFTs interacting with our clients" in the dark pool. Barclays also claimed that trading in its dark pool minimizes information leakage.

84. At the same time that Barclays represented to clients that it is working to keep them safe from predatory high frequency trading tactics, Barclays supplied high frequency trading firms with advantages over more traditional investors trading in its dark pool. As described by one former senior-level Director within the Equities Electronics Trading division, "Barclays was doing deals left and right with high frequency firms to invite them into the pool to be trading partners for the buy side. So the pool is mainly made up of high frequency firms." "[T]he way the deal would work is [Barclays] would invite the high frequency firms in. They would trade with the buy side. The buy side would pay the commissions. The high frequency firms would pay basically nothing. They would make their money off of manipulating the price. Barclays would make their money off the buy side. And the buy side would totally be taken advantage of because they got stuck with the bad trade . . . this happened over and over again."

1. Barclays Disclosed Information Regarding the Workings of its Dark Pool to High Frequency Traders That Was Not Generally Available to Others

85. On numerous occasions since 2011, Barclays disclosed detailed, sensitive information to major high frequency trading firms in order to encourage those firms to increase their activity in Barclays' dark pool. That information, which was not generally supplied to other clients, included data that helped those firms maximize the effectiveness of their aggressive trading strategies in the dark pool. The information included:

- The routing logic of Barclays' order router, including the percentage of Barclays' internal order flow that was first directed into its own dark pool;
- A breakdown of trades executed in the dark pool by participant type (*e.g.*, percentage of orders from institutional investors, high frequency traders, etc.); and
- A breakdown of trades executed in the dark pool by "toxicity" level (*see* Section III (C), above, for discussion of Liquidity Profiling "toxicity" levels).

86. Barclays shared this information in order to attract high frequency trading activity to its dark pool. For instance, in 2013, Barclays was approached by a prominent high frequency trading firm seeking information similar to that set forth above. This firm informed Barclays that "we have our largest trading team . . . looking to get into the dark pool space," and "are try[ing] to get more teams connected to your dark pool." Barclays readily provided the requested information, despite the fact that this information was not generally provided to other clients. Similarly, in 2013, Barclays was approached by another prominent high frequency trading firm with questions regarding the dark pool's "functionality, mechanics, and general color." The firm stated that it wanted to make sure that it was "not missing any opportunities." Barclays provided the information requested.

2. Barclays Took Other Steps to Make its Dark Pool Attractive to High Frequency Traders

87. Despite Barclays' representations that it operates its dark pool "transparently" in order to protect clients from aggressive high frequency trading activity, Barclays has taken a number of actions (beyond those already discussed above) to invite high frequency traders to trade, and trade aggressively, in its dark pool:

- Barclays charges high frequency trading firms little or nothing to trade in its dark pool. For instance, Barclays' charges the two largest participants in its dark pool – both of which are high frequency trading firms – virtually nothing to execute trades. Since at least 2011, these firms were charged nothing per share when posting orders, and between $0.0002 and $0.0005 per share when taking available orders.

- Barclays allows high frequency traders to "cross-connect" to its servers. As of the filing of this Complaint, several dozen of the most well-known and sophisticated high frequency trading firms in the world are cross-connected with Barclays, allowing them to take advantage of Barclays' non-high frequency trading clients, by getting a speed advantage over those slower-moving counterparties.

- While Barclays represented that it used ultra-fast “direct data feeds” to process market price and trade data in order to deter latency arbitrage by high frequency traders in its dark pool, Barclays in fact processed that market data so slowly as to allow latency arbitrage. Internal analyses confirmed that Barclays’ slow processing of market data allowed high frequency traders to engage in such predatory activity.

88. In sum, Barclays’ courting of high frequency traders, and its willingness to falsify the extent of high frequency trading activity in its dark pool, was contrary to Barclays’ representations to clients that Barclays operated with “transparency” and provided a safe venue in which to trade. As described by one former senior Barclays Director: “there was a lot going on in the dark pool that was not in the best interests of clients. The practice of almost ensuring that every counterparty would be a high frequency firm, it seems to me that that wouldn’t be in the best interest of their clients . . . It’s almost like they are building a car and saying it has an airbag and there is no airbag or brakes.”

<u>CAUSES OF ACTION</u>

FIRST CAUSE OF ACTION

(Martin Act Securities Fraud – General Business Law §§ 352 *et seq.*)

89. The Attorney General repeats and re-alleges the paragraphs above as if fully stated herein.

90. The acts and practices of Defendants alleged above violated General Business Law §§ 352 *et seq.*, insofar as such acts, practices, and omissions employed deception, misrepresentations, concealment, suppression, fraud, and false promises regarding the issuance, distribution, exchange, sale, negotiation, or purchase within or from this state of securities.

SECOND CAUSE OF ACTION

(Persistent Fraud and Illegality – Executive Law § 63(12))

91. The Attorney General repeats and re-alleges the paragraphs above as if fully stated herein.

92. The acts and practices of Defendants alleged herein constitute conduct proscribed by § 63(12) of the Executive Law, in that Defendant Barclays (a) engaged in repeated fraudulent or illegal acts or otherwise demonstrated persistent fraud and (b) repeatedly violated the Martin Act in the carrying on, conducting or transaction of business within the meaning and intent of Executive Law § 63(12).

WHEREFORE, Plaintiff demands judgment against Defendants as follows:

A. Providing an accounting of all fees, revenues, or other compensation received, directly or indirectly, from Defendants' operation of its Equities Electronic Trading division, and the various business units thereof;

B. Directing Defendants to pay damages caused, directly or indirectly, by the fraudulent and deceptive acts and repeated fraudulent acts and persistent illegality complained of herein plus applicable pre-judgment interest;

C. Directing Defendants to disgorge all amounts obtained in connection with or as a result of the violations of law alleged herein, all moneys obtained in connection with or as a result of the fraud alleged herein, and all amounts by which Defendants have been unjustly enriched in connection with or as a result of the acts, practices, and omissions alleged herein;

D. Directing that Defendants make restitution of all funds obtained from investors in connection with the fraudulent and deceptive acts complained of herein;

E. Enjoining Defendants from engaging in any ongoing and future violations of New York law;

F. Directing such other equitable relief as may be necessary to redress Defendant's violations of New York law;

G. Directing that Defendants pay Plaintiff's costs, including attorneys' fees; and

H. Granting such other and further relief as may be just and proper.

Dated: New York, New York
June 25, 2014

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