UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60941 / November 4, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13677

In the Matter of **RHINO TRADING, LLC,** **FAT SQUIRREL** **TRADING GROUP, LLC,** **DAMON REIN, AND** **STEVEN PETER,** **Respondents.**	**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 Rhino Trading, LLC ("Rhino"), Fat Squirrel Trading Group, LLC ("FSTG"), Damon Rein, and Steven Peter (collectively, "Respondents").

II.

In anticipation of the institution of these proceedings, Respondents have submitted Offers of Settlement (the "Offers") 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 them and the subject matter of these proceedings, which are admitted, Respondents consent 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 Respondents' Offers, the Commission finds[1] that:

Summary

These proceedings arise out of Respondents Rhino's and FSTG's violations of Regulation SHO. At the time, Regulation SHO required "fail-to-deliver" positions[2] in certain securities that have lasted for thirteen consecutive settlement days to be immediately closed out.[3]

In this case, Respondents Rhino and FSTG engaged in certain transactions that resulted in violations of Regulation SHO's close-out requirement. The first type of transaction, known in the industry as a "reverse conversion," involves selling a put option and buying a call option – a transaction combination that creates what is known as a "synthetic" long position – while selling short the underlying stock. The short sale of the underlying stock serves as a hedge to the synthetic long position. By engaging in these transactions, Respondents Rhino and FSTG profited on the spread between the price of the put option and the price of the call option.

The second type of transaction, known as a "reset," is a transaction in which a market participant that has a "fail-to-deliver" position in a threshold security buys shares of that security while simultaneously selling short-term, deep in-the-money call options to – or buying short-term, deep in-the-money put options from – the counterparty to the share purchase. The purchase of shares creates the illusion that the market participant has satisfied Regulation SHO's close-out obligation. However, the shares that are apparently purchased during the reset transaction are never actually delivered to the purchaser because on the day after executing the reset, the option is

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1 The findings herein are made pursuant to Respondents' Offers of Settlement and are not binding on any other person or entity in this or any other proceeding.

2 "Fails-to-deliver" occur when a seller fails to deliver securities to the buyer when delivery is due. Generally, investors complete or settle their security transactions within three settlement days. This settlement cycle is known as T+3 (or "trade date plus three days"). T+3 means that when a trade occurs, the participants to the trade deliver and pay for the security at a clearing agency three settlement days after the trade is executed so the brokerage firm can exchange those funds for the securities on that third settlement day. The three-day settlement period applies to most security transactions, including stocks, bonds, municipal securities, mutual funds traded through a brokerage firm, and limited partnerships that trade on an exchange. Government securities and stock options settle on the next settlement day following the trade (or T+1).

3 At the time, a "close out" of a fail position involved the purchase of shares of like kind and quantity in the amount of the fail to deliver position.

either exercised (if a call) or assigned (if a put), transferring the shares back to the party that appeared to have sold them the previous day. This paired transaction allows the market participant with the "fail-to-deliver" position to effectively borrow the stock for a day in order to appear that it has satisfied Regulation SHO's close-out requirement.

Specifically, Rhino from June 2007 through August 2007, and FSTG from February 2007 through July 2007, willfully violated Rule 203(b)(3) of Regulation SHO by engaging in a series of transactions through Respondents Rein's and Peter's use of short-term FLEX options that did not satisfy their close-out obligations in Regulation SHO threshold securities[4] that had been allocated to Rhino and FSTG by their clearing firms.

Respondents

1. Fat Squirrel Trading Group, LLC ("FSTG"), a limited liability company located in New York, New York, is a market maker registered with the Chicago Board Options Exchange, Inc. ("CBOE") since January 2007. FSTG also is a broker-dealer registered with the Commission since October 2002. During February 2007 through July 2007, Steven Peter was the managing member of FSTG and both he and Damon Rein were associated with the firm as traders.

2. Rhino Trading, LLC ("Rhino"), a limited liability company located in New York, New York, is a market maker registered with the CBOE since May 2007. Rhino also is a broker-dealer registered with the Commission since May 2007. During June 2007 through August 2007, Damon Rein was associated with Rhino as a trader.

3. Steven Peter, age 49, is a resident of Millbrook, New York and served as the managing member and a trader at FSTG during the relevant time period. Peter holds a series 63 securities license.

4. Damon Rein, age 39, is a resident of Westport, Connecticut. From February 2007 through April 2007, he worked as a trader at FSTG. He ended his association with FSTG in April 2007 and began work as a trader associated with Rhino.

Facts

5. Respondent Rhino during the period June 2007 through August 2007, and Respondent FSTG during the period February 2007 through July 2007, engaged in transactions known as "reverse conversions" with purchasers of Regulation SHO threshold securities.

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[4] A "threshold security" is a security for which there is an aggregate "fail-to-deliver" position exceeding the criteria set forth in Rule 203(c)(6) of Regulation SHO for a period of five consecutive settlement days.

6. As part of these reverse conversions, Respondent Rein on behalf of Rhino, and Respondents Rein and Peter on behalf of FSTG, sold short shares of Regulation SHO threshold securities while simultaneously creating a synthetic long position by purchasing call options and selling put options (with the same strike price and expiration date) on the same threshold securities.[5] Rhino and FSTG purchased enough call options and sold enough put options so that the number of shares underlying the options equaled the number of shares they sold short. Through this set of transactions, Respondents Rhino and FSTG reduced their market risk because the short position was used to hedge the synthetic long position that had been created by purchasing call options and selling put options.

7. Respondents Rhino and FSTG profited from this set of transactions because the premium they received for the put options they sold was greater than the premium they paid to purchase the call options. As a general matter, this disparity in premiums for the put and call options (despite their same strike price and expiration date) on Regulation SHO threshold securities exists because of the additional cost that is incurred to hedge the sale of the put option. Specifically, the seller of the put option hedges that transaction by selling short the underlying security. Because these threshold securities were generally hard to borrow, they were more expensive to sell short. Consequently, the cost of hedging the sale of put options in Regulation SHO threshold securities causes the corresponding put options to trade at a higher price than that of the corresponding call options.

8. Respondents Rhino's and FSTG's short sales resulted in a "fail-to-deliver" position in the threshold security on the books and records of their clearing firms – i.e., Rhino and FSTG had not delivered the shares they sold short to their clearing firms so that the clearing firms could settle the trades.

9. Rule 203(b)(3) of Regulation SHO requires clearing firms immediately to close out any "fail-to-deliver" position in a threshold security that lasts for thirteen consecutive settlement days by purchasing securities of a like kind and quantity. In addition, pursuant to Rule 203(b)(3)(vi) of Regulation SHO, a clearing firm is permitted reasonably to allocate a "fail-to-deliver" position to a broker or dealer whose sale resulted in the position. Once the clearing firm has allocated the "fail-to-deliver" position to another broker or dealer, the obligation for complying with the mandatory close-out shifts to that broker or dealer.

10. Respondents Rhino's and FSTG's clearing firms, through electronic mail or other means, notified Rhino and FSTG that they were shifting the obligation to Rhino and FSTG to close out the "fail-to-deliver" positions and that they would close out those positions if Rhino and FSTG themselves did not do so.

11. Respondents Rhino and FSTG did not want their "fail-to-deliver" position – which resulted from the short sale portion of the reverse conversion – to be closed out by the clearing

[5] In general, a call option purchaser pays a premium to buy the call option, and a put option seller (or writer) receives a premium for selling (or writing) the put option.

firms because this would result in the clearing firms making large purchases of Regulation SHO threshold securities at a price determined by the market and allocating that cost to Rhino and FSTG. Additionally, the close-out would have exposed Respondents Rhino and FSTG to market risk on their initial reverse conversion transactions because it would eliminate the short positions that had been used to hedge the synthetic long positions created by purchasing call options and selling put options.

12. In order to avoid a close-out, Respondent Rein on behalf of Rhino, and Respondents Rein and Peter on behalf of FSTG, entered into a series of transactions that failed to satisfy Rhino's and FSTG's obligations under Regulation SHO to close out their "fail-to-deliver" positions. These complex transactions gave the appearance that Rhino and FSTG were closing out their "fail-to-deliver" position by purchasing securities of like kind and quantity.

13. Specifically, Respondent Rein on behalf of Rhino, and Respondents Rein and Peter on behalf of FSTG, effected short-term in-the-money FLEX (and, in the case of Rhino, occasionally standard in-the-money call) option transactions in conjunction with stock-purchase transactions that did not satisfy the Regulation SHO close-out requirements.

14. A FLEX option allows the investor to customize the option's terms, such as strike price and expiration date. In this case, the FLEX options allowed Respondents Rhino and FSTG to reset the close-out date so that they would have an additional thirteen days to close out any "fail-to-deliver" position. Specifically, Respondents Rhino and FSTG "purchased" stock in the Regulation SHO threshold security from another market participant and simultaneously purchased a short-term, deep in-the-money FLEX put option for a corresponding number of shares from the same market participant. On the day that they "purchased" the stock, Rhino's and FSTG's clearing firms received notice of the "purchase" and closed out the "fail-to-deliver" position. Respondents Rhino and FSTG, however, knew that the following day, or shortly thereafter, the FLEX put option would expire in-the-money, causing Rhino and FSTG to exercise the option and sell the stock.

15. Respondents Rhino and FSTG, however, did not actually receive any shares from the other market participant because that market participant was selling short the stock without having any shares to sell. Accordingly, Respondents Rhino and FSTG did not receive any shares and did not in fact close out the short position – as required by Regulation SHO – that was initially established during the reverse conversion transaction. In these instances, Rhino and FSTG knew, or should have known, that the combination of the purchase of securities and the purchase of the FLEX option would result in maintenance of the "fail-to-deliver" position.

16. Rhino's and FSTG's clearing firms, however, reset Rhino's and FSTG's Regulation SHO close-out obligation to day one (thus giving Rhino and FSTG a fresh thirteen days in which to close out the short position) based on the "purchase" of shares and the exercise of the FLEX option.

17. After receiving close-out notices from their clearing firms, Rhino and FSTG continued to engage in these and similar types of transactions until the initial options positions (call options purchase/put options sale) expired, at which point they no longer had a synthetic long position that needed to be hedged, and so closed out the short position. By engaging in this course of conduct, Rhino and FSTG impermissibly maintained "fail-to-deliver" positions in numerous Regulation SHO threshold securities.

18. During the relevant period, FSTG engaged in a large volume of reverse conversions and reset transactions in numerous threshold securities, including, but not limited to, iMergent, Inc., American Home Mortgage Investment Corp., and NovaStar Financial, Inc. As a result of FSTG's repeated violation of Regulation SHO's close-out requirement, it received ill-gotten gains of $45,000.

19. During the relevant period, Rhino engaged in a large volume of reverse conversions and reset transactions in numerous threshold securities, including, but not limited to, Medis Technologies Ltd., NovaStar Financial, Inc., and USANA Health Sciences, Inc. As a result of Rhino's repeated violation of Regulation SHO's close-out requirement, it received ill-gotten gains of $350,000.

20. In addition, in a limited number of instances, Respondent Rhino engaged in FLEX option transactions in conjunction with stock sales as the counterparty to other market participants who failed to comply with their own Regulation SHO close-out obligations.

Legal Analysis

21. At the time, Rule 203(b)(3) imposed an obligation on clearing firms to immediately close out any "fail-to-deliver" positions in a threshold security that lasts for thirteen consecutive settlement days by purchasing securities of like kind and quantity.[6] Pursuant to Rule 203(b)(3)(vi), however, a clearing firm is permitted reasonably to allocate a "fail-to-deliver" position to a broker or dealer whose short sale resulted in the position. Once the clearing firm has allocated the "fail-to-deliver" position to another broker or dealer, the obligation for complying with the mandatory close-out shifts to that broker or dealer.

22. Once the "fail-to-deliver" position is allocated to the broker or dealer, that broker or dealer, in order to satisfy the close-out requirement of Rule 203(b)(3) of Regulation SHO, must

[6] On July 27, 2009, the Commission made permanent the requirements of interim final temporary rule, Rule 204T, that seeks to reduce potentially abusive "naked" short selling in the securities market. Rule 204T amends Regulation SHO by, among other things, requiring that participants of a registered clearing agency close out fails resulting from short sales no later than the beginning of regular trading hours on the settlement day immediately after the fail occurs. The rule also requires participants of a registered clearing agency to close out fails resulting from long sales or market making activity by no later than the beginning of regular trading hours on the third settlement day after the fail occurs.

purchase securities of like kind and quantity. Borrowing securities, or otherwise entering into an arrangement that merely creates the appearance of a purchase, does not satisfy Regulation SHO's close-out requirement. Specifically, Rule 203(b)(3)(vii) provides that a clearing firm – or a broker or dealer to which the clearing firm allocated a "fail-to-deliver" position – will be deemed not to have satisfied the close-out obligation if it knows, or has reasonable grounds to believe, that the close-out purchase will result in a "fail-to-deliver."

23. By purchasing deep in-the-money FLEX (and, in the case of Rhino, occasionally standard in-the-money call) options while simultaneously purporting to "purchase" stock, Respondents Rhino and FSTG engaged in transactions that gave the appearance that they were closing out their "fail-to-deliver" positions. As a result, Rhino and FSTG willfully violated Rule 203(b)(3) of Regulation SHO.

24. As a result of their conduct, Rein willfully aided and abetted and caused Rhino's violations of Rule 203(b)(3) of Regulation SHO, and Rein and Peter willfully aided and abetted and caused FSTG's violations of Rule 203(b)(3) of Regulation SHO.

Undertakings

25. Pursuant to the CBOE Decision Accepting Offer of Settlement (File No. 09-0010), Respondents Rhino and Rein shall pay, jointly and severally, a fine in the amount of $150,000 to the CBOE's Business Conduct Committee pursuant to the entry of the CBOE's issuance of its Decision Accepting Offer of Settlement (File No. 09-0010).

26. Pursuant to the CBOE Decision Accepting Offer of Settlement (File No. 09-0009), Respondents FSTG, Rein, and Peter shall pay, jointly and severally, a fine in the amount of $30,000 to the CBOE's Business Conduct Committee pursuant to the entry of the CBOE's issuance of its Decision Accepting Offer of Settlement (File No. 09-0009).

27. Respondent Rein shall provide to the Commission, within thirty days after the end of the three-month suspension period described below, an affidavit confirming that he has complied fully with the sanctions described in Section IV(C) below.

28. Respondent Peter shall provide to the Commission, within thirty days after the end of the three-month suspension period described below, an affidavit confirming that he has complied fully with the sanctions described in Section IV(D) below.

In determining whether to accept the Offers, the Commission has considered these undertakings.

IV.

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

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

A. Respondents Rhino, Rein, FSTG, and Peter cease and desist from committing or causing any violations and any future violations of Exchange Act Rule 203(b)(3);

B. Respondents Rhino and FSTG are censured;

C. Respondent Rein be, and hereby is, suspended from association with any broker or dealer for a period of three (3) months, effective on the second Monday following the entry of this Order;

D. Respondent Peter be, and hereby is, suspended from association with any broker or dealer for a period of three (3) months, effective on the second Monday following the entry of this Order;

E. Respondent Rhino shall pay disgorgement in the amount of $350,000, which shall be deemed satisfied by entry of the CBOE's issuance of its Decision Accepting Offer of Settlement (File No. 09-0010);

F. Respondent FSTG shall pay disgorgement in the amount of $45,000, which shall be deemed satisfied by entry of the CBOE's issuance of its Decision Accepting Offer of Settlement (File No. 09-0009);

G. Respondent Rein shall comply with the undertakings enumerated in Section III, paragraph 27 above; and

H. Respondent Peter shall comply with the undertakings enumerated in Section III, paragraph 28 above.

By the Commission.

Elizabeth M. Murphy
Secretary