

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 10565 / September 28, 2018

SECURITIES EXCHANGE ACT OF 1934
Release No. 84314 / September 28, 2018

ADMINISTRATIVE PROCEEDING
File No. 3-18857

In the Matter of

CREDIT SUISSE
SECURITIES (USA) LLC

Respondent.

**ORDER INSTITUTING ADMINISTRATIVE
AND CEASE-AND-DESIST PROCEEDINGS,
PURSUANT TO SECTION 8A OF THE
SECURITIES ACT OF 1933 AND SECTION
15(b) 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 Section 8A of the Securities Act of 1933 (“Securities Act”) and Section 15(b) of the Securities Exchange Act of 1934 (“Exchange Act”) against Credit Suisse Securities (USA) LLC (“Respondent” or “Credit Suisse”).

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (“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 Section 8A of the Securities Act of 1933 and Section 15(b) 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:

INTRODUCTION

1. Broker-dealers that execute orders for retail customers often send such orders to other broker-dealers that specialize in handling such order flow. Between mid-2011 and March 2015 (the "Relevant Period"), Credit Suisse operated a wholesale market making desk called Retail Execution Services ("RES") in order to execute this type of order flow. During this period, RES executed both "held" and "not held" equity orders for its retail broker-dealer customers, including over 15 million held retail-originated equity orders (over 8.5 billion shares) having a total market value of approximately \$227 billion. Held orders that are marketable orders (either market orders, or buy (sell) limit orders whose limit price is at or above (below) the current market price) must be executed immediately (i.e., there is no price or time discretion), whereas not held orders do not require immediate execution and provide flexibility with respect to price and time of execution. Beginning in mid-2011 and continuing until March 2015, when RES closed, RES made material misrepresentations and omissions concerning its handling of held retail equity orders, in violation of Section 17(a)(2) of the Securities Act.

2. RES sought to differentiate itself by marketing its access to "vast" dark liquidity in Credit Suisse's own alternative trading system ("ATS") and dark pool, as well as RES's access to dark pools operated by other broker-dealers. Dark pools are markets in which bids and offers are not visible to market participants, unlike displayed exchanges and markets (i.e. "lit markets") where bids and offers are visible. During the Relevant Period, RES represented in its marketing materials that RES offered "enhanced liquidity" by accessing internal and external pools of liquidity, including access to Credit Suisse's own and other dark pools. However, between September 2011 and December 2012, RES executed only a *de minimis* number of held orders (unlike not held orders) in dark pools.

3. RES further represented in its Order Handling Guide that opportunities for "robust" and "enhanced" price improvement was one of the "core" elements of RES's approach to executing orders. Providing a better price than the currently quoted best bid or ask price is commonly referred to as "price improvement." Although RES described the factors relevant to the securities for which it would provide price improvement, it did not disclose that a subset of orders for which execution quality was not included in publicly reported execution quality reports pursuant to Commission Rule 605 ("non-605" orders) typically would not receive any price improvement. The RES computer code automated the decision-making about whether or not a particular order would receive price improvement from RES. To distinguish between Rule 605 eligible orders and non-605 orders, the RES computer code included a function called "CountsForStats." If the order had Rule 605-like characteristics, it was eligible for, and in most cases did in fact, receive price improvement from RES. If the order did not have those characteristics, it typically did not receive price improvement from RES (although RES would have generally passed through to the customer any price improvement that the executing venue provided). RES's marketing documents listed certain factors that the RES trading code used in

making price improvement decisions, but an order's Rule 605 status was not included in that list of factors.

4. RES stated in its Order Handling Guide that it would seek to execute customer orders at the "most favorable terms reasonably available." RES also represented in its Order Handling Guide that when RES commits capital, "[t]he benefit to our customer is a fill without market impact. The more liquidity we offer, the less impact a customer's order will have on the NBBO [i.e., the National Best Bid and Offer], potentially avoiding price dis-improvement."

5. Despite these statements, between February 2013 and March 2015, for certain orders, RES used a routing tactic that sent an order only to lit markets (referred to herein as "Routing Tactic A") without first attempting to fill the order in Credit Suisse's and other dark pools and electronic liquidity providers ("ELPs"). RES applied Routing Tactic A disproportionately often to non-605 orders (identified using the "CountsForStats" function) that were larger than (i.e., "outsized") the number of shares displayed at the then-prevailing market price, and thus had the potential to cause market impact. Outsized non-605 orders that RES executed using Routing Tactic A generally created a greater market impact and therefore received a less favorable overall execution price than orders executed with other routing tactics that RES used.¹ RES's use of Routing Tactic A provided RES an opportunity to profit from, or "capture," market impact if there was post-trade price reversion, in which stock prices that have been temporarily displaced as a result of market activity may revert toward the original price level. The frequency with which RES used Routing Tactic A for certain outsized orders was not disclosed in RES's marketing materials.

FACTS

A. Respondent

6. Credit Suisse, a registered broker-dealer, is a Delaware limited liability company with headquarters in New York, New York. Credit Suisse is a wholly-owned subsidiary of Credit Suisse Group AG.

7. Between mid-2011 and March 2015, Credit Suisse operated a New York-based wholesale market making business called Retail Execution Services, which executed retail-originated orders in equity securities sent by other broker-dealers. In March 2015, Credit Suisse closed RES, which was generally not profitable.

B. Background

8. RES received customer orders on either a "held" or a "not held" basis. Held orders that are marketable must be immediately executed at the then-prevailing market price (i.e., there is no price or time discretion), whereas not held orders allow for price and time discretion. For both held and not held orders, the executing broker-dealer generally has discretion to select the routing

¹ This document does not reflect or constitute any finding that RES executed any orders outside of the then-prevailing NBBO.

strategy, including the venues to which the orders are routed, but must do so in a manner consistent with its representations. Some RES customers sent to the RES desk both held and not held orders, while other customers sent only held or not held orders.

9. The RES desk executed order flow on either a “principal” basis or a “riskless principal” basis. In a principal execution, also referred to as “internalization,” RES took a proprietary position with risk by either buying from or selling to the customer. In a riskless principal execution, RES also bought from or sold to a customer, but RES did not take on any meaningful risk because RES, with a customer order in hand, first obtained the position in the marketplace (e.g., by trading principally on lit markets or in a dark pool), and then provided a corresponding execution to its customer at the same price (or better). RES executed held customer orders in one of three ways: (i) RES traded as principal to fill the entire order; (ii) RES executed the entire order on a riskless principal basis; or (iii) RES executed some of the order on a principal basis and some on a riskless principal basis (referred to herein as “split fills”).

10. For the held orders at issue, RES did not charge customers commissions or markups, and instead sought to profit from its principal trading. RES considered two elements of potential profit: (i) spread capture (i.e., capturing the difference between the bid and ask for a security at the time the order was received); and (ii) impact capture (as set forth below). RES also considered the potential risk associated with internalizing all or part of the order.

11. The RES desk executed over 15 million held orders (over 8.5 billion shares) with a total market value of approximately \$227 billion during the Relevant Period.²

C. RES Made Misleading Statements to Customers about Access to Dark Pool Liquidity

12. In marketing materials such as RES’s Order Handling Guide and responses to customer questionnaires in 2011 and 2012, RES promoted its access to dark pool liquidity. Access to liquidity is a relevant factor in a retail wholesaler’s ability to provide quality executions, and the liquidity to which RES had access was a material consideration for many of RES’s retail broker-dealer customers in determining where to route their order flow.

a. RES’s Order Handling Guide, distributed to all RES customers, represented that RES offered “enhancement opportunities from Credit Suisse’s vast liquidity,” including access to Credit Suisse’s dark pool, which was at the time was the largest U.S. equity dark pool, as well as external dark pools. For example, RES’s 2011 Order Handling Guide described “enhancement opportunities from Credit Suisse’s vast liquidity, including access to Crossfinder, the largest ATS in the U.S.”

b. In response to customer queries, RES highlighted its access to liquidity, including its access to Credit Suisse’s own and other dark pools. For example, in a 2011 response to a questionnaire that a retail broker-dealer was using to help determine how to route order flow, RES focused on its ability to provide “[l]iquidity as a differentiating factor.” RES

² During the same time period, RES executed approximately 45 million not held orders (over 8 billion shares) with a total market value of approximately \$270 billion.

further stated: “A vital component in a principal market maker’s ability to provide quality executions is the ability to efficiently source and interact with liquidity.” RES then provided expanded details concerning the “three key resources . . . that enhance RES’s ability to source and interact with liquidity.” One of these “key resources” was access to Credit Suisse’s dark pool, about which RES stated: “RES has access to Crossfinder, an anonymous matching engine that is solely owned by Credit Suisse Securities (USA) LLC. Crossfinder continues to hold its spot as the largest US equity dark pool by a considerable margin[.]” A second of these “key resources” was access to external venues, such as dark pools, through Credit Suisse’s smart order router. Specifically, in describing RES’s “Access to External Dark Pools,” RES stated that it had access to a “broad and expanding list” of dark pools through “Credit Suisse’s proprietary solution for dark book smart order routing.”

13. These representations were misleading under the circumstances. Unlike not held orders, which RES regularly executed in Credit Suisse’s own and other dark pools, RES rarely executed held orders in such venues between September 2011 and December 2012. In particular, RES trading data indicates that during this time, RES executed only a *de minimis* number of customer held orders in Credit Suisse’s own dark pool (i.e., 512 orders out of 4 million, or approximately 0.01%) or other dark pools during this period.

D. RES Did Not Disclose that Non-605 Orders Typically Did Not Receive Certain Represented Benefits

14. In determining how to allocate order flow among various retail wholesalers, a primary factor that retail broker-dealers consider is the execution quality that each retail wholesaler delivers. Generally, the better the execution quality, the more order flow broker-dealers send to a particular retail wholesaler.

15. In RES’s Order Handling Guides that were distributed to all customers, RES stated that it “seeks to execute its customers’ orders at the most favorable terms reasonably available under prevailing market conditions.” RES also stated in its Order Handling Guides that “RES execution algorithms focus on optimizing the execution experience of retail orders.” RES also highlighted in its Order Handling Guides that when RES commits capital, “[t]he benefit to our client is a fill without market impact. The more liquidity we offer, the less impact a client’s order will have on the NBBO, potentially avoiding price dis-improvement. Our price improvement and liquidity enhancement levels are all geared to commit capital to the potential benefit of our clients.”

16. Rule 605 requires that market centers such as RES publicly report certain aggregate order execution information, including measures of execution quality, on an aggregate basis. Certain orders are excluded from Rule 605 required reporting; for example, orders of 10,000 shares or more, orders of less than 100 shares, and not held orders are, by definition, non-605 orders. Statistics published pursuant to Rule 605 include, among other things, the spreads paid by investors (i.e., “effective spreads”), levels of price improvement provided, and speed of execution for various categories of orders. Although RES’s broker-dealer customers received the same information from RES regarding pricing and timing of executions of their Rule 605-eligible and

non-605 orders, and the execution prices of both Rule 605-eligible and non-605 orders are reported publicly, retail broker-dealers differ in the extent to which they monitor (and have the ability to monitor) execution quality for their non-605 orders.

17. RES received both Rule 605-eligible and non-605 order flow. The computer code RES used to execute orders included a function called “CountsForStats” that distinguished between held orders that had Rule 605 characteristics, and those that did not. The output of the CountsForStats function played a role in RES’s decisions about how certain orders were routed, and about whether to apply price improvement to orders.

18. Between mid-2011 and March 2015, RES treated many non-605 orders less favorably as compared to Rule 605-eligible orders that were similar in other respects. Indeed, in certain instances, RES internally referred to non-605 orders as “EQ-ineligible” orders (where “EQ” stood for execution quality). This differential treatment of certain non-605 orders was not disclosed to RES customers, which was misleading under the circumstances.

i. RES Generally Did Not Price Improve Non-605 Orders

19. In executing customer orders, RES frequently offered price improvement to improve the execution quality of certain orders. RES had discretion with respect to whether and how much price improvement to provide, but was required to do so in a manner consistent with its representations. In addition, the external venues to which RES routed orders, or portions of orders (i.e., “child orders”), sometimes offered price improvement (although the price improvement that RES offered was generally more than the amounts that the external venues offered).

20. Credit Suisse represented to its customers that opportunities for “robust” and “enhanced” price improvement was one of the “core” elements of RES’s approach to executing orders. Further, RES’s Order Handling Guides stated that RES’s systems “automatically evaluate a number of factors, including the quoted spread at the time of order receipt, the quoted size at the time of order receipt, and the type of security (NDX, S&P 100, S&P 500, etc.) in determining the appropriate level of price improvement.” While RES listed these non-exhaustive security-specific factors that were included in its evaluation of potential price improvement, RES did not disclose that an order’s Rule 605 status was also a determinative factor in assessing whether RES itself would price improve a customer order.

21. Between mid-2011 and March 2015, RES itself generally did not improve the execution price of non-605 orders. This decision-making was automated by the RES computer code. Specifically, if the execution would not be included in the publicly reported execution quality statistics (i.e., CountsForStats was false), RES generally would not price improve the customer order. Alternatively, if the execution would be included in the publicly reported

execution quality statistics (i.e., CountsForStats was true), the order was eligible for and generally received RES price improvement.³

22. Credit Suisse's representations concerning the factors that RES considered in determining price improvement levels were misleading because Credit Suisse did not disclose that non-605 orders were generally ineligible for price improvement by RES. Such information would have been a material consideration for many retail broker-dealers in determining where to route non-605 order flow.

ii. RES Sought to Capture Impact on Select Non-605 Orders

23. From February 2013 through March 2015, RES utilized two primary tactics to route customer orders that it did not fully internalize. One tactic attempted to fill the order in Credit Suisse's and other dark pools and ELPs, where the available liquidity was unknown. The other was Routing Tactic A, which routed the non-internalized portions of certain customer orders to lit markets without first attempting to secure an execution in dark pools and ELPs. RES applied Routing Tactic A to outsized non-605 orders disproportionately often compared to Rule 605-eligible orders. Specifically, pursuant to the RES computer code, if a particular order had Rule 605 characteristics (i.e., CountsForStats was "true"), then Routing Tactic A was set to "false," and the order would generally not be routed pursuant to Routing Tactic A. Conversely, if the order did not have those characteristics (i.e., CountsForStats was "false"), then Routing Tactic A was set to "true," and the order would be more likely to be routed using Routing Tactic A.

24. RES's differential application of Routing Tactic A was particularly important with respect to orders that, due to their relatively large size, outsized the available liquidity at the then-prevailing market price, or market depth, because those orders had the potential to cause market impact. Market impact refers to a phenomenon in which buying or selling a security, or attempting to buy or sell a security, may result in the market price becoming less favorable to the buyer or seller. For example, buying a security may cause its price to increase if there are fewer shares available at the current price than the customer wishes to buy. Different trading tactics may result in different degrees of market impact, influencing the overall execution quality of the order. In particular, to the extent that significant market impact occurs before an order is completely filled, it may be more costly to fill the remainder of the order, which results in a less favorable overall execution price.

25. Outsized marketable held orders often can only be filled in their entirety by executing at more than one price level, including at least one price level outside of the NBBO at the time of arrival. By their nature, such orders have the potential to cause market impact. Outsized orders that RES routed pursuant to Routing Tactic A generally had the potential to cause, and in fact generally caused greater market impact over the course of the entire order (i.e., including any internalized portion) than orders executed with other strategies that RES used.

³ One RES customer reached a separate agreement with RES whereby RES agreed to provide price improvement for that customer's non-605 held orders, which was written into the RES code.

26. RES's code attempted to calculate RES's risk and potential to profit from each order, and used that calculation to determine whether and how much of the order to internalize, and how much if any to route out and fill on a riskless principal basis. This calculation attempted to predict, among other things, RES's potential opportunity to capture market impact. Specifically, this decision was made using a utility function in the RES computer code. In making this decision, RES considered three factors: (1) potential spread capture, (2) potential impact capture, and (3) potential risk to RES. Generally, the utility function selected the level of RES's capital commitment in order to maximize the potential spread and impact capture, while minimizing potential risk. For large outsized orders, with the potential to cause significant market impact, impact capture was frequently the most important factor in the code's determination of how much of an order to internalize.

27. When RES filled orders on a split (partially principal and partially riskless principal) basis, it typically began the execution by routing one or more child orders to the lit markets using Routing Tactic A. As those child orders were filled, the stock price often moved higher for purchases and lower for sales. RES would then internalize the final piece of the order (often larger than any of the individual child orders) at the new prevailing market price. Following the execution of an outsized order, there may be price reversion, in which stock prices that have been temporarily displaced as a result of market activity could potentially revert toward the original price level. If price reversion did occur, RES was left with a potentially profitable position in the internalized portion of the order. Further, RES used Routing Tactic A significantly more often to route the riskless principal portion of split fills compared to otherwise equivalent orders filled on an entirely riskless basis. Because RES took no principal position when orders were filled completely on a riskless principal basis, and there was no market impact of orders that RES fully internalized, split fills were those where RES had the potential to capture impact.

28. For example, in the case of a customer sell order, if the stock price decreased as RES executed child orders (i.e., sold small amounts) in a riskless principal capacity in the lit market, RES's purchase of the remaining portion of the order from the RES customer on a principal basis at the prevailing market price would be at a lower price than the price when the parent order arrived. If the price of the stock subsequently reverted back towards its original (higher) level before RES unwound its position, RES would be left with a potentially profitable position. RES had the opportunity to exit that position at a profit, by liquidating its position on another trading venue or by matching it against a customer buy order.⁴

29. RES's disproportionate use of Routing Tactic A on non-605 orders allowed RES the potential opportunity to profit from impact capture on a category of orders without affecting RES's published execution quality statistics. RES used Routing Tactic A on a greater percentage of non-605 orders than Rule 605-eligible orders, and on a greater percentage of outsized non-605 orders than outsized Rule 605-eligible orders. RES's use of Routing Tactic A varied over time.

⁴ The RES code included a function that sent liquidating orders to trading venues no earlier than 10 minutes after RES established a position, if the position had not already been liquidated by matching it against customer orders.

a. From February 2013 through November 2013 (referred to herein as “Period 1”), for all RES customers, RES used Routing Tactic A almost exclusively on select categories of outsized non-605 held orders, and rarely on outsized Rule 605-eligible held orders. In particular, RES’s use of Routing Tactic A was concentrated among non-605 orders of 10,000 shares or more, and orders received while the markets were closed. In Period 1, RES used Routing Tactic A on approximately 8,600 non-605 outsized held orders that were filled on a split basis. These orders comprised a total of approximately 120 million shares, and had a total market value of approximately \$2.5 billion.

b. From December 2013 through January 2015 (referred to herein as “Period 2”), RES continued to use Routing Tactic A more frequently for outsized non-605 held orders than for outsized Rule 605-eligible orders. Further, RES used Routing Tactic A across all categories of non-605 orders, not limited to orders of 10,000 shares or more and orders received after the markets closed. During Period 2, RES’s use of Routing Tactic A varied by customer group. For one set of customers, RES used Routing Tactic A almost exclusively on outsized non-605 orders, and rarely on outsized Rule 605-eligible orders. In Period 2, for those customers, RES used Routing Tactic A on approximately 4,500 held outsized non-605 orders. These orders comprised a total of approximately 60 million shares, and had a total market value of approximately \$990 million.

IV.

VIOLATIONS

30. As a result of the conduct described above, Respondent willfully⁵ violated Section 17(a)(2) of the Securities Act, which prohibits, directly or indirectly, in the offer or sale of securities, obtaining money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading.

V.

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

Accordingly, pursuant to Section 8A of the Securities Act and Section 15(b) of the Exchange Act, it is hereby ORDERED that:

A. Respondent cease and desist from committing or causing any violations and any future violations of Section 17(a)(2) of the Securities Act.

⁵ 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)).

B. Respondent is censured.

C. Respondent shall, within 14 (fourteen) days of the entry of this Order, pay a civil money penalty in the amount of \$5,000,000 to the Securities and Exchange Commission for transfer to the general fund of the United States Treasury, subject to Exchange Act Section 21F(g)(3). 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 identifying Credit Suisse 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 Lara S. Mehraban, Associate Regional Director, Division of Enforcement, Securities and Exchange Commission, 200 Vesey Street, New York, NY 10281.

Amounts ordered to be paid as civil money penalties pursuant to this Order shall be treated as penalties paid to the government for all purposes, including all tax purposes. To preserve the deterrent effect of the civil penalty, Respondent agrees that in any Related Investor Action, it shall not argue that it is entitled to, nor shall it benefit by, offset or reduction of any award of compensatory damages by the amount of any part of Respondent's payment of a civil penalty in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, Respondent agrees that it shall, within 30 days after entry of a final order granting the Penalty Offset, notify the Commission's counsel in this action and pay the amount of the Penalty Offset to the Securities and Exchange Commission. Such a payment shall not be deemed an additional civil penalty and shall not be deemed to change the amount of the civil penalty imposed in this proceeding. For purposes of this paragraph, a "Related Investor Action" means a private damages action brought against Respondent by or on behalf of one or more investors based on substantially the same facts as alleged in the Order instituted by the Commission in this proceeding.

By the Commission.

Brent J. Fields
Secretary