

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 80373 / April 4, 2017

INVESTMENT ADVISERS ACT OF 1940
Release No. 4678 / April 4, 2017

ADMINISTRATIVE PROCEEDING
File No. 3-17899

In the Matter of

**Credit Suisse Securities
(USA) LLC**

Respondent.

**ORDER INSTITUTING
ADMINISTRATIVE AND CEASE-AND-
DESIST PROCEEDINGS PURSUANT TO
SECTION 15(b) OF THE SECURITIES
EXCHANGE ACT OF 1934 AND
SECTIONS 203(e) AND 203(k) OF THE
INVESTMENT ADVISERS ACT OF 1940,
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 15(b) of the Securities Exchange Act of 1934 (“Exchange Act”) and Sections 203(e) and 203(k) of the Investment Advisers Act of 1940 (“Advisers 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 (the “Offer”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over it and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Section 15(b) of the Securities Exchange Act of 1934 and Sections 203(e) and 203(k) of the Investment Advisers Act of 1940, 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 finds¹ that:

Summary

1. These proceedings arise out of breaches of fiduciary duty, inadequate disclosures, and deficiencies in compliance policies and procedures by Credit Suisse. Between January 1, 2009 and January 21, 2014 (the "Relevant Period"), Credit Suisse investment adviser representatives purchased or held Class A mutual fund shares for advisory clients who were eligible to purchase or hold less expensive institutional share classes of the same mutual funds. A significant difference between Class A shares and institutional share classes is the existence of marketing and distribution fees imposed on Class A shareholders pursuant to Section 12(b) of the Investment Company Act and Rule 12b-1 thereunder ("12b-1 fees"), typically 25 basis points per year for Class A shares. The 12b-1 fees are paid out of the assets of the fund as a portion of its expense ratio. In this case, the 12b-1 fees were passed through to Credit Suisse, which in turn paid a portion of that amount to its investment adviser representatives, also referred to as Relationship Managers ("RMs"). Thus, 12b-1 fees decreased the value of advisory clients' investments in mutual funds and increased the compensation paid to Credit Suisse and its RMs.

2. Credit Suisse's disclosures did not adequately inform its advisory clients of the conflict of interest presented by its RMs' share class selection practices. Credit Suisse disclosed in its Forms ADV and client agreements that it "may" receive 12b-1 fees as the result of investments in certain mutual funds and that such fees created a conflict of interest due to a financial incentive for RMs to select or recommend investments that maximized this compensation. Credit Suisse did not disclose, however, that many mutual funds offered a variety of share classes, including some that did not pay 12b-1 fees and were accordingly less expensive for eligible investors. Thus, Credit Suisse's general disclosures regarding its potential receipt of 12b-1 fees were inadequate to advise advisory clients that an RM could select or recommend – and in many instances did select or recommend – mutual fund investments in share classes that paid 12b-1 fees to Credit Suisse when those clients were eligible to purchase share classes of the same mutual funds that did not pay such fees and were less expensive. In addition, Credit Suisse did not disclose in its brochure supplements on Form ADV, Part 2B related to certain RMs, that those RMs received 12b-1 fees from the sale of mutual funds, which created an incentive for those individual RMs to recommend Class A shares rather than less costly share classes.

3. Over time, as institutional share classes became more available to non-institutional purchasers, Credit Suisse did not update its policies and procedures to require personnel specifically to identify or evaluate available institutional share classes. Moreover, Credit Suisse did not update or enhance its policies or procedures to address instances in which RMs were purchasing and holding Class A shares when less costly institutional share classes were available.

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

Respondent

4. **Credit Suisse Securities (USA) LLC**, a Delaware limited liability company with headquarters in New York, New York, is dually registered with the Commission as a broker-dealer and an investment adviser. Credit Suisse is a wholly-owned subsidiary of Credit Suisse (USA), Inc., which is an indirect wholly-owned subsidiary of Credit Suisse Group AG.

Relevant Party

5. Sanford Michael Katz, 54, resides in San Rafael, California. During the Relevant Period, Katz was a Managing Director and Relationship Manager in Credit Suisse's San Francisco branch office. Katz had Series 3, 7, and 63 securities licenses and was a registered representative and an investment adviser representative of Credit Suisse. The Commission has instituted a separate proceeding against Katz related to these matters.

Background

6. During the Relevant Period, Credit Suisse, through its private banking business ("PB North America"), offered products and services to clients in its capacities as a broker-dealer and an investment adviser.² PB North America offered investment advisory programs to clients through RMs pursuant to a fee-based, or "wrap fee," program. A wrap fee is an annual inclusive fee paid by the advisory client to PB North America based on a percentage of the client's assets under management. PB North America's wrap fee covered investment advice, execution, custody, administrative and account reporting services.

7. In 2008, Credit Suisse created the Discretionary Managed Portfolio ("DMP") program to oversee discretionary and non-discretionary wrap fee advisory accounts. The DMP program was administered centrally by a team of professionals who were responsible for establishing investment guidelines for the program and, along with Credit Suisse's Compliance Department, for monitoring DMP accounts.

Mutual Fund Share Class Selection

8. DMP accounts could be invested in an array of securities, including stocks, bonds, and mutual funds, based on the clients' investment objectives and needs. DMP accounts could be invested in a wide selection of mutual funds across numerous mutual fund complexes, including multiple share classes of the same funds. Mutual fund share classes represent an interest in the same portfolio of underlying securities with the same investment objective. The primary difference among the various share classes is their fee structure.

9. Class A shares generally can be purchased in retail brokerage accounts or advisory accounts. Class A shares are sold with sales charges or "loads" in retail brokerage

² On October 21, 2015, Credit Suisse Group AG announced that PB North America would oversee a gradual transition of its RMs and customer accounts to other financial institutions. By March 31, 2016, PB North America had terminated all investment advisory contracts and no longer purchases or recommends mutual funds for advisory clients.

accounts based on the dollar amount of the investment. The sales charges are generally waived for Class A shares purchased in wrap fee or fee-based advisory accounts. Class A shares, including “load-waived”³ Class A shares purchased in advisory accounts, also carry 12b-1 fees which are paid from a mutual fund’s assets on an ongoing basis for shareholder services, distribution, and marketing expenses.⁴ The 12b-1 fee for Class A shares is typically 25 basis points per year.

10. Many mutual funds also offer “institutional” share classes, which are available only to investors who meet certain criteria (*e.g.*, a minimum investment amount or eligible investment program) and do not carry 12b-1 fees.⁵ Many of these mutual funds offered institutional share classes with high minimum investment thresholds, and many such funds waived or substantially reduced that amount for purchases in wrap fee advisory accounts (such as DMP accounts).⁶ An investor who holds institutional share classes of a mutual fund will pay lower fees over time – and earn higher investment returns – than an investor who holds Class A shares of the same fund. Therefore, if a mutual fund offers an institutional share class, and an investor is eligible to own it, it is almost invariably in the investor’s best interests to select the institutional share class.

11. During the Relevant Period, Credit Suisse assigned responsibility for approving mutual fund transactions to its respective offices’ Branch Managers. In the San Francisco branch office, the Branch Manager delegated this responsibility to the Branch Administrative Manager (“Administrative Manager”).

12. During the Relevant Period, Credit Suisse RMs purchased or held, on behalf of DMP clients, share classes with 12b-1 fees when those clients were eligible to purchase or hold share classes without 12b-1 fees of those same funds. As a result, Credit Suisse received approximately \$3.2 million in 12b-1 fees that it would not have collected had its DMP clients been invested in lower-cost share classes for which they were eligible.

Mutual Fund Share Class Practices

13. In October 2008, Credit Suisse hired Katz as an RM in its San Francisco branch office. Credit Suisse permitted Katz to manage DMP accounts in accordance with his own strategy, which utilized investments in mutual funds to a greater degree than other Credit Suisse RMs servicing DMP clients. Soon after joining Credit Suisse, Katz’s team determined that they were not receiving 12b-1 fee income from his clients’ Class A mutual fund holdings in DMP

³ Certain mutual funds known as “no load” funds can be purchased in wrap fee accounts but may also have 12b-1 fees. These no load funds are equivalent to “load-waived” Class A shares in wrap fee accounts.

⁴ 12b-1 fees are paid to the fund’s distributor or principal underwriter, which, in turn, generally remits the fees to the broker-dealer (such as Credit Suisse) that distributes or “sells” the fund’s shares. Credit Suisse then shared a percentage of those 12b-1 fees with the DMP client’s RM.

⁵ “Institutional” shares go by a variety of names in the mutual fund industry. As used in this Order, the term refers to share classes that carry neither up-front sales charges nor 12b-1 fees.

⁶ The number of mutual funds that waived their minimum investment requirement, or otherwise permitted wrap fee participants to acquire institutional share classes increased over the course of the Relevant Period.

accounts. The reason was that Credit Suisse had previously instructed its clearing broker – whose systems did not segregate Credit Suisse’s retirement accounts from its other accounts at the time – to block any 12b-1 fees generated from advisory accounts and return them to the respective mutual fund companies. Katz questioned Credit Suisse management about the block, asserting that he had received credit for such revenue at his prior employer and that his DMP accounts generated \$300,000 to \$500,000 in annual 12b-1 revenue to Credit Suisse. Following Katz’s inquiry, Credit Suisse instructed its clearing broker to lift the block, thereby allowing Credit Suisse and its RMs to receive 12b-1 fees derived from its DMP accounts.⁷

14. In June 2009, an Administrative Manager in the San Francisco branch office questioned Katz’s proposed purchase of Class A shares for DMP clients when the mutual fund prospectuses suggested that less expensive institutional share classes may be available, and did not approve the transactions. Katz escalated the issue to the San Francisco Branch Manager and to DMP management. The Branch Manager approved Katz’s Class A mutual fund purchases in that instance. Thereafter, Administrative Managers approved Katz’s purchase of Class A mutual fund shares in DMP accounts without evaluating whether the account was eligible to purchase an institutional share class.

15. During the Relevant Period, Katz purchased or held Class A shares for DMP clients where: (a) the mutual fund prospectus indicated that institutional share classes were available for wrap fee accounts, (b) other Credit Suisse RMs had purchased the institutional share class for DMP accounts, and/or (c) Katz himself had previously purchased the institutional share class for other DMP clients. As a result, Katz received approximately \$1.1 million in 12b-1 fees that he would not have collected had his DMP clients been invested in lower-cost share classes for which they were eligible. In some instances, other Credit Suisse RMs also purchased Class A shares for DMP clients when those clients were eligible to purchase institutional share classes.

16. During the Relevant Period, Credit Suisse did not require that Class A shares held for DMP clients be exchanged for less expensive institutional share classes, when it knew or should have known that such holdings were eligible for conversion on a tax-free basis.

Inadequate Disclosure Concerning Mutual Fund Share Class Selection

17. As an investment adviser, Credit Suisse was obligated to fully disclose, *inter alia*, all material conflicts of interest between itself and its clients that could affect the advisory relationship. To accomplish this disclosure obligation, Credit Suisse was required to provide its clients with sufficient information so that its clients would be able to understand the conflicts of interest that Credit Suisse had, and could give informed consent to such conflicts or reject them.

18. Credit Suisse disclosed in its Forms ADV and in its advisory agreements that it “may” receive 12b-1 fees from the sale of mutual funds and that the availability of such fees creates a conflict of interest. The disclosure did not address the selection or recommendation of share classes of mutual funds that paid 12b-1 fees when less expensive share classes were available for purchase. Credit Suisse also disclosed in a separate sub-item that it “may also

⁷ Credit Suisse continued to block 12b-1 payments for mutual fund investments in advisory accounts covered by the Employee Retirement Income Security Act of 1974.

receive revenue sharing payments from a mutual fund, its service providers, or [clearing broker].” It then disclosed that “[m]utual funds that do not pay revenue sharing payments are available. You must advise your Relationship Manager if you wish to restrict mutual funds selected or recommended for your account to those funds that do not make revenue sharing payments to [Credit Suisse].” The disclosure did not define the term “revenue sharing payments,” a term that generally is used in the mutual fund industry to refer to payments by the mutual fund adviser or its affiliates, and not payments by mutual funds pursuant to Rule 12b-1. Thus, the provision did not apply to Rule 12b-1 fees.

19. Credit Suisse’s disclosure failed to identify the actual conflict presented by its purchase of mutual fund share classes that charged 12b-1 fees when its DMP clients were eligible to purchase share classes of the same funds that did not charge 12b-1 fees. The Forms ADV did not disclose the fact that many mutual funds offered multiple share classes, including those expressly designed for, or made available to, clients in fee-based advisory programs. Because there was no mention of share class distinctions, Credit Suisse’s disclosures did not inform clients that Credit Suisse would recommend or discretionarily purchase or hold a share class that bears 12b-1 fees when a less costly share class of the same fund was available.

20. Beginning in 2011, Credit Suisse was obliged to prepare disclosures specific to each of its RMs on Form ADV, Part 2B and distribute these disclosures to clients. In response to Item 4 of that form, Credit Suisse was required to disclose that certain RMs received 12b-1 fees from the sale of mutual funds, and that the receipt of those fees created an incentive to recommend Class A shares rather than less costly share classes that were available to eligible clients. Rather than make that required disclosure for RMs who received 12b-1 fees, Credit Suisse disclosed that the RM “[did] not receive compensation from any other person or entity other than Credit Suisse in connection with the provision of investment advice to clients.”

Failure to Obtain Best Execution for DMP Clients’ Mutual Fund Transactions

21. Section 206 of the Advisers Act imposes on investment advisers a fiduciary duty to act for the benefit of their clients. That duty includes, among other things, an obligation to seek best execution for client transactions – *i.e.*, “to seek the most favorable terms reasonably available under the circumstances.” *In the Matter of Fidelity Management Research Company*, Investment Advisers Act Rel. No. 2713 (Mar. 5, 2008). The Commission has stated in settled enforcement actions that an investment adviser failed to seek best execution when it caused a client to purchase a more expensive share class when a less expensive class was available.⁸ By purchasing Class A shares when its DMP clients were eligible for institutional share classes, and by failing to disclose to its clients that best execution might not be sought for mutual funds with multiple available share classes, Credit Suisse breached its duty to seek best execution on behalf of its DMP clients.

⁸ See *In the Matter of Everhart Financial Group, Inc.*, Investment Advisers Act Rel. No. 4314 (Jan. 14, 2016) (settled matter); *In the Matter of Manarin Investment Counsel, Ltd.*, Investment Advisers Act Rel. No. 3686 (Oct. 2, 2013) (settled matter); and *In the Matter of Pekin Singer Strauss Asset Management Inc.*, Investment Advisers Act Rel. No. 4126 (June 23, 2015) (settled matter).

Failure to Adopt and Implement Reasonably Designed Policies and Procedures

22. Credit Suisse's policies and procedures provided inadequate and incomplete guidance to RMs regarding how to evaluate institutional share classes in comparison to other mutual fund share classes. Moreover, to the extent that Credit Suisse had policies and procedures governing the selection of mutual fund share classes, they were not consistently observed or enforced.

23. Credit Suisse's policies and procedures provided that a mutual fund purchase ticket must be completed by an RM and approved by an Administrative Manager (or other branch supervisor) for every mutual fund purchase. As part of the approval process, Credit Suisse's policies and procedures also required a branch supervisor to analyze whether the share class proposed for purchase was appropriate for the client, including cost considerations. When load-waived Class A shares were purchased for DMP accounts, however, Credit Suisse's mutual fund purchase ticket did not require any information regarding the availability of institutional or less expensive share classes. Credit Suisse's policies also did not provide for any cost comparison of available share class alternatives. Thus, even if Administrative Managers had been inclined to analyze the purchase of a load-waived Class A share, the procedures provided them with insufficient information upon which to base such an analysis. As a result, Administrative Managers routinely approved purchases of load-waived Class A shares for DMP clients when those clients were eligible to purchase less expensive institutional share classes.

24. By at least August 2012, Credit Suisse's Investment Advisory Task Force, an internal group that periodically reviewed PB North America's policies and procedures with respect to its investment advisory business, was aware that Class A shares were being purchased and held in DMP accounts when those clients were eligible to purchase and hold institutional share classes. Credit Suisse's policies and procedures were not updated or enhanced to address this issue.

25. On January 21, 2014, after receiving a deficiency letter from the Commission's Office of Compliance Inspections and Examinations, Credit Suisse revised its policies to prohibit the purchase of 12b-1 fee-bearing share classes in DMP accounts.

Violations

26. Section 206(2) of the Advisers Act makes it unlawful for an adviser directly or indirectly to engage in any transaction, practice, or course of business that operates as a fraud or deceit upon any client or prospective client. Scienter is not required to establish a violation of Section 206(2), but rather may rest on a finding of negligence. *SEC v. Steadman*, 967 F.2d 636, 643 n.5 (D.C. Cir. 1992) (citing *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 194-95 (1963)). As a result of the negligent conduct described above, Credit Suisse willfully violated Section 206(2).⁹

⁹ 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)).

27. Section 207 of the Advisers Act makes it “unlawful for any person willfully to make any untrue statement of a material fact in any registration application or report filed with the Commission . . . or willfully to omit to state in any such application or report any material fact which is required to be stated therein.” As a result of the conduct described above, Credit Suisse willfully violated Section 207 of the Advisers Act.

28. Section 206(4) of the Advisers Act and Rule 206(4)-7 thereunder require a registered investment adviser to, among other things, “[a]dopt and implement written policies and procedures reasonably designed to prevent violation” of the Advisers Act and its rules. As a result of the conduct described above, Credit Suisse willfully violated Section 206(4) of the Advisers Act and Rule 206(4)-7 thereunder.

IV.

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

Accordingly, pursuant to Section 15(b) of the Exchange Act and Sections 203(e) and 203(k) of the Advisers Act, it is hereby ORDERED that:

A. Respondent cease and desist from committing or causing any violations and any future violations of Sections 206(2), 206(4), and 207 of the Advisers Act and Rule 206(4)-7 promulgated thereunder.

B. Respondent is censured.

C. Respondent shall, within 10 days of the entry of this Order, pay disgorgement of \$2,099,624.12, prejudgment interest of \$380,090.37, and a civil money penalty in the amount of \$3,275,000 to the Securities and Exchange Commission. If timely payment of disgorgement or prejudgment is not made, additional interest shall accrue pursuant to SEC Rule of Practice 600. If timely payment of the civil money penalty 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 Securities (USA) LLC as a Respondent in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to Melissa R. Hodgman, Associate Director, Division of Enforcement, Securities and Exchange Commission, 100 F St., NE, Washington, DC 20549-5553.

D. Pursuant to Section 308(a) of the Sarbanes-Oxley Act of 2002, as amended, a Fair Fund is created for the disgorgement, prejudgment interest, and penalty referenced in paragraphs IV.C above. This Fair Fund is expected to include all funds collected from the Commission's related proceeding, *Sanford Michael Katz*, [A.P. No. 3-17900](#) (filed April 4, 2017). The Fair Fund will be distributed to affected investors in accordance with a Commission-approved plan of distribution. 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