Re Credit Suisse Securities (Canada) Inc

IN THE MATTER OF:

The Market Integrity Rules of the
Investment Industry Regulatory Organization of Canada

and

The Universal Market Integrity Rules

and

Credit Suisse Securities (Canada) Inc

2011 IIROC 10

Investment Industry Regulatory Organization of Canada
Hearing Panel (Ontario District Council)

Heard: January 21, 2011
Decision: February 3, 2011
(5 paras.)

Hearing Panel:
Hon. Patrick T. Galligan, Q.C. (Chair), Guenther Kleberg, Peter Gribbin
Appearances:
Lorne Herlin, Enforcement Counsel
Joel Wiesenfeld & Doug Walker, Respondent's Counsel

REASONS FOR DECISION

¶ 1 This Panel was convened to consider, pursuant to Rule 20.36 of the Investment Industry Regulatory Organization of Canada ("IIROC"), whether to accept a settlement agreement which had been negotiated between IIROC's Enforcement Department and Credit Suisse Securities (Canada) Inc. ("Credit Suisse"). At the conclusion of the hearing, held for that purpose at Toronto on January 21, 2011, and after considering the Settlement Agreement and the submissions made by counsel, we accepted it. These are our reasons for doing so.

¶ 2 The terms of the settlement and the circumstances of the contravention are set out in the Offer of Settlement and in the Statement of Allegations. For completeness, we incorporate those two documents into these reasons.

OFFER OF SETTLEMENT

A. INTRODUCTION

1. On June 1, 2008, IIROC consolidated the regulatory and enforcement functions of the Investment Dealers Association of Canada and Market Regulation Services Inc. (RS). Pursuant to the *Administrative and Regulatory Services Agreement* between RS and the Investment Industry Regulatory Organization of Canada (IIROC), effective June 1, 2008, RS has retained IIROC to

provide services for RS to carry out its regulatory functions.

2. The Enforcement Department Staff (Staff) of IIROC has conducted an investigation (the Investigation) into the conduct of Credit Suisse Securities (Canada) Inc. (Credit Suisse).

3. The Investigation has disclosed matters for which IIROC seeks certain sanctions against Credit Suisse pursuant to Rule 10.5 of the Universal Market Integrity Rules (UMIR).

4. If this Offer of Settlement is accepted by Credit Suisse, the resulting settlement agreement (the Settlement Agreement), which has been negotiated in accordance with Part 3 of UMIR Policy 10.8, is conditional upon the approval by a hearing panel appointed pursuant to IIROC Transitional Rule No.1, Schedule C.1 (the Hearing Panel).

5. Credit Suisse agrees to waive all rights under UMIR to a hearing or to an appeal or review if the Settlement Agreement is approved by the Hearing Panel.

6. Credit Suisse consents to be subject to the jurisdiction of IIROC and its relevant disciplinary process and rules in relation to this matter.

7. Staff and Credit Suisse jointly recommend that the Hearing Panel approve the Settlement Agreement.

B. AGREEMENT AS TO REQUIREMENTS CONTRAVENED

8. Credit Suisse agrees that from June 2007 to December 2007 it failed to comply with its trading supervision obligations, contrary to UMIR 7.1(1) and UMIR Policy 7.1.

C. ADMITTED FACTS

9. For purposes of the Settlement Agreement, Staff and Credit Suisse agree with and rely upon the admitted facts and conclusions which are set out in the Statement of Allegations that is attached as Appendix "A" to the Settlement Agreement.

D. DISPOSITION

10. For the contravention in paragraph 8 above, Staff and Credit Suisse have agreed upon disposition as follows:

    i. a fine of $150,000.00 payable by Credit Suisse to IIROC; and

    ii. costs of $15,000.00 payable by Credit Suisse to IIROC.

11. If the Settlement Agreement is accepted by a Hearing Panel, Credit Suisse agrees to pay the amounts referred to in paragraph 10.

E. PROCEDURES FOR ACCEPTANCE OF OFFER OF SETTLEMENT AND APPROVAL OF SETTLEMENT AGREEMENT

12. Credit Suisse shall have until the close of business on Friday, January 14, 2011 to accept this Offer of Settlement and serve an executed copy thereof on Staff.

13. The Settlement Agreement shall be presented to a Hearing Panel at a hearing (the Approval Hearing) held for the purpose of approving the Settlement Agreement, in accordance with the procedures described in UMIR Policy 10.8 in addition to any other procedures as may be agreed upon between the parties. Credit Suisse acknowledges that IIROC shall notify the public and media of the Approval Hearing in such manner and by such media as IIROC sees fit.

14. Pursuant to Part 3.4 of UMIR Policy 10.8, the Hearing Panel may approve or reject the Settlement Agreement.

15. In the event the Settlement Agreement is approved by a Hearing Panel, the matter becomes final,

there can be no appeal or review of the matter, the disposition of the matter agreed upon in the Settlement Agreement will be included in the permanent record of IIROC in respect of Credit Suisse and IIROC will publish a summary of the requirements contravened, the facts, and the disposition agreed upon in the Settlement Agreement.

16. In the event the Hearing Panel rejects the Settlement Agreement, IIROC may proceed with a hearing of the matter before a differently constituted Hearing Panel pursuant to Part 3.7 of UMIR Policy 10.8 and the Settlement Agreement may not be referred to without the consent of both parties.

17. Credit Suisse agrees that, in the event it fails to comply with any of the terms of the Settlement Agreement, IIROC may enforce the Settlement Agreement in any manner it deems appropriate and may, without limiting the generality of the foregoing, suspend Credit Suisse's access to marketplaces regulated by IIROC until IIROC determines that Credit Suisse is in full compliance with all terms of the Settlement Agreement.

18. Credit Suisse agrees that no one on its behalf will make a public statement inconsistent with the Settlement Agreement.

19. The Settlement Agreement may be signed in counterparts.

IN WITNESS WHEREOF the parties have signed the Settlement Agreement as of the dates noted below.

STATEMENT OF ALLEGATIONS

I. REQUIREMENTS CONTRAVENED

1. It is alleged that Credit Suisse Securities (Canada) Inc. (Credit Suisse) has committed the following contravention:

   From June 2007 to December 2007, Credit Suisse failed to comply with its trading supervision obligations, contrary to Universal Market Integrity Rule (UMIR) 7.1(1) and UMIR Policy 7.1 (collectively, the Requirements).

2. The text of the Requirements is set out in Schedule "A". [Schedule "A" omitted.]

II. RELEVANT FACTS AND CONCLUSIONS

Overview

3. From June 2007 to December 2007 Credit Suisse failed to comply with its trading supervision obligations. In particular, Credit Suisse failed to:

   i. conduct artificial pricing reviews within a reasonable period of time for the months of May 2007, June 2007, and July 2007;

   ii. conduct an artificial pricing review for October 2007; and

   iii. question a client until December 27, 2007 about buy orders that the client placed, despite the fact that Credit Suisse's artificial pricing reviews for August 2007, September 2007, and November 2007 generated a number of red flag warnings that the client's account was executing buy orders that appeared to create artificial prices.

Credit Suisse

4. Credit Suisse is a Participating Organization of the Toronto Stock Exchange (TSX) and Member of the TSX Venture Exchange (TSX-V). Therefore, Credit Suisse is a Participant under UMIR.

5. Credit Suisse offers direct market access (DMA), also known as dealer sponsored access (DSA) to eligible clients. DMA allows an eligible client to directly enter orders to market places by means of an electronic connection to Credit Suisse's trading system.

Credit Suisse's Trading Supervision Obligations

6. Pursuant to UMIR 7.1 and UMIR Policy 7.1, and as reaffirmed in, among other things, two Market Integrity Notices[1], a Participant is not relieved from any supervisory obligations under UMIR with respect to any order that is entered on a marketplace by means of DMA.

7. Market Integrity Notice 2007-010 (April 20, 2007), *Compliance Requirements for Dealer-Sponsored Access Trading* states:

> **Supervisory Obligations of Participants**
>
> Part 1 of Policy 7.1 provides that a Participant has an obligation to supervise orders which are entered on a marketplace:
>
> …
>
> - directly by a client and routed to a marketplace through the trading system of a Participant
>
> ...
>
> In the view of RS, the means by which an order is entered on a marketplace does not relieve a Participant of the responsibility for the supervision of such orders. RS is also of the view that orders entered directly on a marketplace without the involvement of staff of the Participant present heightened risks to both the integrity of the markets and the Participant through whom the order is routed.
>
> ...
>
> **Why does RS believe there is a greater "risk" to market integrity associated with an order entered by a DSA Client?**
>
> Orders entered by DSA Clients are conducted, for the most part, in the absence of any meaningful pre-order or pre-trade oversight by the Participant. It is RS's view that this lack of involvement by staff of the Participant eliminates a significant opportunity for a Participant to perform its "gatekeeper" function and to act on "red flags". If an investment adviser or trader "handles" an order, the experience and knowledge of the employee increases the possibility that unusual trading patterns or anomalies can be detected prior to the entry of an order to a marketplace. The performance of the "gatekeeper" function would require the employee to inquire about unusual trading patterns or anomalies or to involve a supervisor. These actions may prevent offending orders from being entered on a marketplace. This same safeguard is not available for orders entered by a DSA Client that are routed directly to a marketplace.

The DMA Client

8. The trades at issue were buy orders that were placed by a client which had a DMA account (the DMA Account) with Credit Suisse, using Time Weighted Average Price algorithms in the execution of the orders. The DMA Account placed buy orders for shares of the following four TSX-V listed issuers:

   i. Wealth Minerals Ltd. (WML);

   ii. Blue Rock Resources (BRD);

   iii. Midasco Capital Corporation (MGC); and

   iv. International Tower Hill Mines (ITH)

   (collectively, the Issuers).

Credit Suisse's Artificial Pricing Review Policy

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[1]Market Integrity Notice No. 2005-006 (March 4, 2005) – *Obligations of an Access Person and Supervision of Persons with Direct Access* and Market Integrity Notice No. 2007-010 (April 20, 2007) - *Compliance Requirements for Dealer-Sponsored Access Trading*.

9. Pursuant to Part 3 of UMIR Policy 7.1, as part of its trading supervision obligations Credit Suisse was required to conduct a monthly review for artificial pricing. Accordingly, Credit Suisse's Compliance Manual indicated that it would review the trading activity for the last week of every month for possible artificial pricing using monthly reports generated by the TSX Compliance Alerts Reporting System (CARS). The CARS reports identified all tick setting trades by a Participant that occurred during the last thirty minutes of the trading session. CARS reports were available for review following each month end.

10. Credit Suisse's Compliance Manual stated:

> The {CARS} reports … are reviewed against the "Highly-Liquid Security List" on the Market Regulation Services web page to determine if further due diligence is required as a highly-liquid security is difficult to manipulate. If the security is highly liquid it is noted on the report and all other trades are reviewed further.
>
> The Compliance Analyst will review all others *(sic)* trades using Bloomberg and taking into account the following criteria:
>
> - Percentage change greater than 1% for the last trade
> - The number of tick setting trades
> - Price movement of the security
> - The bid/ask spread and liquidity of the security
> - News releases that may affect the security
> - Possible patterns for tick setting trades by accounts

11. At all material times, the Issuers were never listed on the Highly Liquid Security List. Therefore, pursuant to its Compliance Manual, Credit Suisse was required to review any trades in the Issuers that appeared on a monthly CARS report.

Failure to Comply With its Trading Supervision Obligations

12. Credit Suisse did not conduct artificial pricing reviews within a reasonable period of time for the months of May 2007, June 2007, and July 2007. These reviews were conducted in September 2007 and they noted activity in the DMA Account in one or more of the Issuers during each of these three months.

13. Credit Suisse did not conduct an artificial pricing review for October 2007.

14. The CARS reports for August 2007 to November 2007 showed trades for the DMA Account in the Issuers in each of the following reports: August (2 trades); September (7 trades); October (6 trades); and November (10 trades).

15. Further, the CARS reports for August 2007 to November 2007 contained red flag warnings that the buy orders for the DMA Account for the shares of the Issuers appeared to create artificial sale prices, these included:

    i. the fact that the buy orders were being filled near the close of the market;

    ii. the number of upticks that the last trades of the day established;

    iii. the changes in price of the Issuers effected by the last trades of the day; and

    iv. the number of months the Issuers appeared on the CARS reports.

16. The information in the CARS reports should have caused Credit Suisse to scrutinize all the buy orders that the DMA Account executed and to promptly question its client.

17. Scrutiny of all the buy orders that the DMA Account placed for shares of the Issuers, in addition

to those contained in the month end CARS reports, would have revealed a number of other trades in August 2007, September 2007,
October 2007, and November 2007 that appeared to create artificial prices. Further particulars of all the buy orders for shares of the Issuers that were placed by the DMA Account between August 2007 and December 2007 are set out in Schedule "B". [Schedule "B" omitted.]

18. On November 28, 2007, Market Regulation Services Inc. (RS) contacted Credit Suisse regarding the trading in one of the Issuers.

19. On December 4, 2007, Credit Suisse contacted its Information Technology Department to request detailed data regarding the trading that RS had brought to Credit Suisse's attention.

20. On December 27, 2007, after analyzing the data, Credit Suisse contacted its client to obtain additional information regarding the activity in the DMA Account.

21. On January 4, 2008, Credit Suisse was advised that the DMA Account would no longer place orders so near the close of the market.

Mitigating Factors and Remedial Steps Taken by Credit Suisse

22. Credit Suisse has undertaken numerous projects to improve its trading supervision and compliance monitoring procedures, including:

    i. the testing and implementation of Compliance Explorer (a real-time cross market surveillance system);

    ii. the creation of a Compliance Surveillance Manual, a DMA Client Training Manual, and a Client Account Opening Procedures Manual; and

    iii. the redrafting of its Compliance Manual.

23. Further, IIROC's 2009 Trade Conduct Compliance Review of Credit Suisse did not reveal any deficiencies with Credit Suisse's artificial pricing reviews.

24. Therefore, IIROC is satisfied that the above noted deficiencies in Credit Suisse's trade supervision for artificial pricing have been remedied.

¶ 3 In *Re BMO Nesbitt Burns Inc.*, [2010] IIROC No. 39, at paragraph 11, that Hearing Panel stated that it is important that a proposed penalty will serve as "a punishment for the party but also a warning to others ...". That Panel also confirmed that a hearing panel should not attempt to fine-tune a settlement agreement, but rather consider whether, in the circumstances of an individual case, the proposed settlement is a reasonable one.

¶ 4 In our opinion, the fine agreed to is a significant one. The respondent has taken proper steps to correct its failure to comply with its trading supervision obligations. Thus, the settlement serves the purpose of punishing the respondent and of warning others that they must comply with their supervisory obligations.

¶ 5 In those circumstances, we concluded that the settlement was a reasonable one and we approved it.

Reasons for Decision dated this 3rd day of February 2011.

Patrick T. Galligan, Q.C., Chair

Guenther Kleberg

Peter Gribbin