SEC Charges ITG With Operating Secret Trading Desk and Misusing Dark Pool Subscriber Trading Information

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Washington D.C., Aug. 12, 2015 — The Securities and Exchange Commission today announced that ITG Inc. and its affiliate AlterNet Securities have agreed to pay $20.3 million to settle charges that they operated a secret trading desk and misused the confidential trading information of dark pool subscribers.

An SEC investigation found that despite telling the public that it was an "agency-only" broker whose interests don't conflict with its customers, ITG operated an undisclosed proprietary trading desk known as "Project Omega" for more than a year. While ITG claimed to protect the confidentiality of its dark pool subscribers' trading information, during an eight-month period Project Omega accessed live feeds of order and execution information of its subscribers and used it to implement high-frequency algorithmic trading strategies, including one in which it traded against subscribers in ITG's dark pool called POSIT.

ITG agreed to admit wrongdoing and pay disgorgement of $2,081,034 (the total proprietary revenues generated by Project Omega) plus prejudgment interest of $256,532 and a penalty of $18 million that is the SEC's largest to date against an alternative trading system.

"ITG created a secret trading desk and misused highly confidential customer order and trading information for its own benefit," said Andrew J. Ceresney, Director of the SEC's Division of Enforcement. "In doing so, ITG abused the trust of its customers and engaged in conduct justifying the significant sanctions imposed in this case."

According to the SEC's order instituting a settled administrative proceeding:

- Project Omega traded a total of approximately 1.3 billion shares, including approximately 262 million shares with unsuspecting subscribers in ITG's own dark pool.
- Project Omega employed an algorithmic trading strategy called the "Facilitation Strategy" in which it executed trades based on a live feed of information concerning orders that its sell-side subscribers sent to ITG's algorithms for handling.
- Project Omega accessed the feed by connecting to a software utility that was used by ITG's sales and support teams. As a result, Project Omega had a real-time view of subscriber orders being placed through ITG's algorithms.
- From April to December 2010, the Facilitation Strategy was designed to detect open orders of sell-side subscribers being handled by ITG. Based on that information, Project Omega opened positions in displayed markets on the same side of the market as the detected orders, and then closed these positions in POSIT by trading against the detected orders. By employing this strategy, Project Omega sought to capture the full "bid-ask spread" between the National Best Bid and Offer (NBBO).

- Project Omega had access to the identities of POSIT subscribers and used this information to identify sell-side subscribers and trade with them in the dark pool in connection with the Facilitation Strategy.
- To earn the full "bid-ask spread" in connection with the Facilitation Strategy, Project Omega needed the subscribers with which it traded in POSIT to be configured to trade "aggressively" so that the subscribers would "cross the spread" to trade with Project Omega. Project Omega took steps to ensure that the sell-side subscribers were configured to trade aggressively in POSIT.
- Project Omega's other primary strategy called the "Heatmap Strategy" involved trading on markets other than POSIT based on a live feed of confidential information relating to customer executions in other dark pools. Based on customer executions, Project Omega's Heatmap algorithm was designed to open positions in specific securities in displayed markets at the bid or the offer and then close them at midpoint or better in the external dark pools where customers had received midpoint executions. The goal of this strategy was to earn a "half spread" or better based on knowledge of ITG customers' executions.

The SEC's order finds that ITG violated Sections 17(a)(2) and (3) of the Securities Act of 1933 in connection with Project Omega by engaging in a course of business that operated as a fraud and by failing to make disclosures about Project Omega and its proprietary trading activities. ITG also violated Rules 301(b)(2) and 301(b)(10) of Regulation ATS by failing to amend its Form ATS filings in light of Project Omega's trading activities in POSIT, failing to establish adequate safeguards, and failing to implement adequate oversight procedures to protect the confidential trading information of POSIT subscribers.

The SEC's continuing investigation is being conducted by Paul T. Chryssikos, Scott A. Thompson, Matthew Koop, and Mandy B. Sturmfelz of the SEC Enforcement Division's Market Abuse Unit with assistance from G. Jeffrey Boujoukos of the Philadelphia Regional Office. The case is being supervised by Joseph G. Sansone, acting co-chief of the unit. Substantial assistance was provided by Michael J. Gaw and Tyler Raimo of the Division of Trading and Markets.

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Related Materials

- SEC order