Re Chang

IN THE MATTER OF:

The Dealer Member Rules of the Investment Industry Regulatory Organization of Canada

and

The By-Laws of the Investment Dealers Association of Canada ("IDA")

and

Lawrence Chang

2014 IIROC 04

Investment Industry Regulatory Organization of Canada
Hearing Panel (Pacific District)

Sanction Hearing: November 22, 2013
Decision on Sanction: January 20, 2014

Hearing Panel:
Catharine Esson, Chair; Bob Sutherland and Brian Worth
Appearances:
Paul Smith, Enforcement Counsel for IIROC
Ron Pelletier, for Lawrence Chang

DECISION ON SANCTION

¶ 1 These are the reasons for judgment relating to sanction for a proceeding conducted pursuant to IIROC Dealer Member Rule 20. In a decision dated August 26, 2013, we concluded that:

- on six occasions from December 31, 2007 through March 28, 2008, the Respondent purchased a combined total of approximately $498,160 of one security (USSU) in a client account without authorization from the client, contrary to IDA Bylaw 29.1; and
- from January 2008 through May 2008, the Respondent, contrary to IDA Bylaw 29.1, made misrepresentations to the client regarding the number of shares of USSU held in the client's account in order to hide the fact that he had made unauthorized purchases of USSU.

¶ 2 We concluded that a third allegation had not been proven.

¶ 3 In our August 26, 2013 decision, we characterized the Respondent's conduct in the following manner:

> 186. Both the unauthorized purchases of USSU and the misrepresentations of what was in GP's account were substantial departures from the conduct expected of registrants and the level of financial probity which is essential for registrants. The transgressions occurred repeatedly and over a number of months. They involved a large amount of money. In engaging in each of the unauthorized trading and the misrepresentations, the Respondent failed to observe high standards of ethics and conduct in the transaction of his business and engaged in business conduct or practice unbecoming and detrimental to the public interest, contrary to IDA Bylaw 29.1.

¶ 4 Pursuant to IIROC Dealer Member Rule 20.33, we have the discretion to impose any one or more of a number of types of sanction on the Respondent, including a fine and a bar from approval with IIROC. We held a hearing on November 22, 2013 to consider sanction. The Respondent was represented by counsel who made submissions on his behalf. He did not attend the hearing personally. Neither party called evidence.

¶ 5 IIROC Staff sought the following sanction:

- A permanent bar from approval with IIROC;
- A fine of $100,000;
- Costs of $20,000, and
- Disgorgement of commissions earned on the impugned trades in the amount of $3,318.

¶ 6 The Respondent did not propose a specific sanction, although he argued that the facts did not justify a lengthy bar from approval. He posed the question whether any forward looking suspension was necessary, given that the Respondent has voluntarily been out of the industry since 2009.

¶ 7 IIROC Staff relied on IIROC's *Dealer Member Disciplinary Sanction Guidelines* as providing guidance for determining the appropriate sanction. We are not bound by the *Guidelines*, but we consider that they provide a useful analysis of the purposes of sanctions and of factors which a hearing panel may find relevant in assessing the sanction in a specific case. We have had regard to the *Guidelines* in reaching our decision. We have also considered the decision in *Re: Pan*, 2012 IIROC 22, although we recognize that there are substantial factual differences between it and this case.

¶ 8 In our view, the most significant considerations in determining sanction in this case are the following:

a. *The harm to the client* - The Respondent purchased about $500,000 worth of USSU in the client's account without authority and, during a period of time when the price of USSU was declining, repeatedly misrepresented the size of the share position to the client. In so doing, he exposed the client to large losses.

b. *The deliberate and dishonest nature of the misconduct* - We do not know the Respondent's motivation for purchasing USSU without instructions. However, he deliberately misrepresented to his client the size of the client's holdings of USSU in order to hide from the client the unauthorized transactions. He misrepresented the holdings on a number of occasions and in a number of ways. This was completely at odds with his fundamental obligation to treat his client honestly.

c. *The harm to the securities market generally from the type of misconduct in this case* – The securities market operates on the basis of trust between registrant and client. It is essential to this trust that registrants not expose their clients' assets to unauthorized risks. It is also essential that registrants are completely candid with clients about matters relating to the clients' assets.

   The Respondent's conduct fell substantially below what is expected of registrants. It was dishonest and exposed the Respondent's client to substantial financial harm. IIROC Staff characterized it as being exactly the type of conduct which gives IIROC a bad name and affects public trust. We agree. Conduct such as this undermines the public's trust in registrants, and therefore harms the securities market generally.

d. *Multiple incidents of misconduct over an extended period of time* – The Respondent made six unauthorized trades in one client's account and misrepresented the quantity of USSU in the account to the client on numerous occasions. The misconduct occurred over a number of months. It was not isolated.

   That being said, we recognize that the misconduct did not involve multiple clients or multiple different factual situations. It does not establish that the Respondent generally treated his clients dishonestly.

e. *The Respondent's participation in the investigative and hearing process even after leaving the industry*. In our view, this is somewhat mitigating. It indicates respect for the regulatory process and, as a general matter, should be encouraged as it allows for a better disciplinary process.

¶ 9 We also note that the Respondent has a prior disciplinary record, having been sanctioned in late 2009 for failing to make inquiries of a client in violation of his gatekeeper obligation. We have not considered this to be an aggravating factor for two reasons. First, the previous misconduct was of a different type and relatively minor in comparison to the misconduct in this case. Second, the previous sanction was imposed after the events which form the basis of this hearing. It cannot be said that the Respondent failed to be deterred by the earlier sanction.

¶ 10 In the circumstances of this case, we have concluded that it is appropriate to permanently bar the Respondent from membership in IIROC. We recognize that this is a severe penalty and may impose substantial economic hardship on the Respondent. However, in our view the misconduct, viewed as a whole, was sufficiently dishonest and abusive of the Respondent's client that the Respondent should not be trusted as a registrant in the future.

¶ 11 We have also concluded that it is appropriate to impose a fine of $100,000. We have reduced the fine which we otherwise would have imposed on these facts to acknowledge both the potential economic impact of a permanent ban and that the Respondent participated responsibly in the disciplinary process and presumably incurred substantial costs to do so.

¶ 12 IIROC Staff sought disgorgement, in addition to a fine. IIROC's Rules do not provide for disgorgement, although Rule 20.33 frames the maximum allowable fine in terms of a multiple of the profit made by the Respondent. In this case, the fine we have imposed is very large in comparison to the amount of the commissions earned by the Respondent on the impugned trades. We do not consider it appropriate to increase the fine to add on the amount of the commissions.

¶ 13 Pursuant to Dealer Member Rule 20.49, we have discretion to assess and order any IIROC Staff investigation and prosecution costs we determine are appropriate and reasonable in the circumstances. IIROC Staff acknowledged the ongoing issues in applying Rule 20.49. These issues have been discussed in decisions such as *Re: Blackmont Capital Inc.* 2010 IIROC 57.

¶ 14 IIROC Staff sought costs of $20,000 and provided us with a Bill of Costs in the amount of $24,719. Enforcement counsel advised us it was based on a very conservative tally of the hours that he and IIROC's investigator incurred in connection with this matter, multiplied by the hourly rate IIROC's Finance Department ascribes to these individuals. IIROC Staff did not attempt in the Bill of Costs to include only time which related to the counts on which we found against the Respondent.

¶ 15 IIROC Staff did not call any evidence in support of its claim for costs. In our view, it should do so. However, we conclude based on the evidence we received at the hearing about the investigation and based on the hearing itself that IIROC Staff's investigator and Enforcement Counsel spent more hours on this matter than are claimed on the Bill of Costs.

¶ 16 We accept that the amount claimed of $20,000 is significantly less than IIROC would have paid a third party to investigate and prosecute this matter. It is less clear how the amount claimed relates to IIROC's actual costs in connection with this matter. That being said, if costs were to be ordered solely to compensate IIROC for the costs it incurred, without regard to the fact that there was divided success or other factors, we would accept the amount claimed as reasonable.

¶ 17 In our view, however, Rule 20.49 requires that we consider more than simply whether IIROC Staff succeeded on part of its claim and the costs it reasonably incurred. In *Blackmont*, supra, the hearing panel declined to make an order regarding costs, despite IIROC Staff having succeeded on some of its allegations. The panel in that case took into account that the Respondent had responsibly approached the disciplinary process and that the parties had had divided success.

¶ 18 We recognize that in this case IIROC Staff succeeded on the most serious allegations it made and that

IIROC has a legitimate interest in recovering its costs related to that. At the same time, however, there are equally legitimate interests in ensuring that costs awards (which can be made in IIROC's favor, but not in favor of a Respondent) do not cause a perception of unfairness or undermine the goal of allowing respondents to defend themselves in a reasonable manner.

¶ 19 The Respondent in this case attended an investigative interview and defended himself through counsel at the hearings into both liability and sanction. He was successful in defending himself on one of the three allegations made against him. While it was the least serious of the allegations, it consumed a significant amount of time at the hearing and, presumably, during the investigation.

¶ 20 We have concluded that IIROC Staff should recover a portion of the costs which it reasonably and appropriately incurred, but that the total amount of costs awarded to it should be relatively modest, on account of divided success and to ensure that costs awards do not become a deterrent to respondents defending themselves. In an effort to balance these objectives, we order costs in the amount of $7500.

Summary of Sanction

¶ 21 We make the following orders against the Respondent:

- A permanent bar from approval with IIROC;
- A fine of $100,000, and
- Costs of $7,500.

Dated at Vancouver, BC, this 20th day of January, 2014.

Catharine Esson, Chair

Bob Sutherland, Member

Brian Worth, Member