

Re Darrigo

IN THE MATTER OF:

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

and

Paul Christopher Darrigo

2015 IIROC 03

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

Heard: November 7 and December 19, 2014

Decision: December 19, 2014

Reasons: January 19, 2015

Hearing Panel:

Frederick H. Webber, Chair, Hugh McNabney and Ron Smith, Industry Members

Appearances:

Robert Del Frate, Enforcement Counsel, Bert Noguera, Investigator for IIROC

Paul Christopher Darrigo, Respondent, in person (December 19, 2014 only)

PANEL DECISION ON PENALTY

1. PROCEDURAL MATTERS

¶ 1 The panel made its decision on liability on September 26, 2014 finding that the Investment Industry Regulatory Organization of Canada (“IIROC”) had proven both allegations against Paul Christopher Darrigo (“Respondent”). The Panel’s written decision and reasons therefor were issued on October 16, 2014 (See Re Darrigo, 2014 IIROC 48). The penalty hearing was held commencing on November 7, 2014. IIROC counsel advised the Panel that, following issuance of the written decision on liability, IIROC attempted to forward the written decision to the Respondent and to arrange a mutually acceptable date for the penalty hearing, but were unable to get a response from the Respondent until November 6th. In the absence of a response from the Respondent, the date for the penalty hearing was set by IIROC for November 7, 2014. When IIROC was finally able to get in touch with the Respondent on November 6, he advised IIROC that he could not attend the scheduled penalty hearing, either in person or by phone. The Respondent told IIROC that he would like to attend the penalty hearing, but did not know when he would be able to do so. Therefore the Panel had to decide whether to proceed with the penalty hearing on November 7th in the absence of the Respondent.

¶ 2 Since the Panel had already received the IIROC written submissions on penalty, it decided to hear the oral submissions of IIROC counsel, but not to make any decision on penalty in order to give the Respondent an opportunity to participate in the penalty hearing. The Panel decided, and IIROC counsel agreed, as follows:

- IIROC would immediately forward by courier, the Panel’s written decision on liability and the materials provided to the Panel for the penalty hearing, viz. IIROC’s written submissions on penalty, the affidavit of Katie Trotman on costs and the IIROC penalty book, and would track the delivery to ensure that the materials had been received by the Respondent;

- the Respondent must decide, no later than November 21, 2014, whether he would participate in the penalty hearing, which must occur on a mutually acceptable date but no later than December 19, 2014, and IIROC would immediately advise the Respondent accordingly and would stay in contact with the Respondent in order to ensure that IIROC was aware that the Respondent understood the foregoing and what his decision was.

¶ 3 The hearing on penalty reconvened on December 19, 2014. Both IIROC counsel and the Respondent attended. At the outset, IIROC counsel advised the Panel that the matters referred to in paragraph 1.2 had been completed. The Respondent agreed that he had received all the required documents and he was prepared to proceed with the penalty hearing. IIROC counsel advised the Panel that he had completed his oral submissions on November 7, 2014, but reserved the right to make submissions in reply to any matters raised by the Respondent. The Respondent provided a copy of written submissions to the Panel and to IIROC counsel, and then commenced his oral submissions.

¶ 4 The Panel advised the Respondent that he was only to make submissions regarding penalty and not to revisit liability matters, which had already been decided by the Panel. Notwithstanding the foregoing, a number of the Respondent's submissions were directed to liability, but were received by the Panel to the extent that they also affected the determination of the appropriate penalty.

2. PROPOSED SANCTIONS

¶ 5 The following penalties were sought by IIROC:

1. a 12 month suspension on the Respondent's approval with IIROC;
2. a global fine of \$134,170, broken down as follows:
 - i. a fine of \$79,170 in relation to count 1, representing a disgorgement of commissions of \$69,170, plus an additional fine of \$10,000; and
 - ii. a fine of \$55,000 in relation to count 2, representing disgorgement of the loan proceeds of \$45,000, plus an additional fine of \$10,000; and
3. a 12 month period of strict supervision.

¶ 6 In addition to the penalties, IIROC also sought full payment of its costs in the amount of \$97,777.50 as outlined in the affidavit of Katie Trotman filed as Exhibit 1 to the penalty hearing.

3. GOALS OF SECURITIES REGULATION

¶ 7 The IIROC penalty submissions stated that the sanctions imposed in a securities regulatory context should be preventative, protective and prospective. They are intended to prevent likely future harm to the capital markets, and where circumstances warrant, the hearing panel's role is to "remove from the capital markets those whose past conduct is so abusive as to warrant apprehension of future conduct detrimental to the integrity of the capital markets", citing *Committee for the Equal Treatment of Asbestos Minority Shareholders v. Ontario (Securities Commission)*, [2001] 2 S.C.R. 132, and *In the Matter of Mithras Management LTD et al* 1990 LNONOSC 119.

¶ 8 The IIROC submissions also stated that general deterrence is an appropriate consideration in making orders that are both protective and preventative, citing *Re Cartaway Resources Corp.*, [2004] 1 S.C.R. 672; and that for a penalty to have an appropriate general deterrent effect, it must be in line with industry expectations, citing the Dealer Member Disciplinary Sanction Guidelines ("the Guidelines") and *Re Mills*, [2001] I.D.A.C.D. No. 7.

¶ 9 As stated in the IIROC submissions, the Guidelines also provide that, when determining the appropriate penalty, a hearing panel should take into account protection of the investing public, IIROC's membership, the integrity of IIROC's process, the integrity of the securities markets and prevention of a repetition of the type of conduct under consideration.

¶ 10 This Panel agrees with the matters set forth in paragraphs 7, 8 and 9, and has followed them in arriving at its decision on penalty in this case.

4. THE GUIDELINES

¶ 11 The IIROC submissions included a copy of the Guidelines which were reviewed by the Panel, as applicable to this case. Although count 1 did not specifically refer to actions commonly known as “churning”, the facts are similar and the Guidelines regarding churning are instructive. They recommend a minimum fine of \$20,000, disgorgement of profits, a rewrite of the Conduct and Practices Handbook (“CPH”), a minimum of 12 months close and/or strict supervision and a period of suspension in egregious cases. For cases involving personal business with a client, including borrowing from the client without the knowledge or consent of the Member (as in count 2), the Guidelines recommend a minimum fine of \$10,000, disgorgement of commissions, successful completion of an appropriate industry program, a period of close supervision for 12 to 24 months, and a period of suspension in “cases involving multiple clients/client losses/conduct over a period of time” or a permanent prohibition in egregious cases. The following factors set out in the Guidelines are relevant in determining an appropriate penalty in this case.

Harm to Clients, employer and/or Securities Market

¶ 12 As set out in the Dealer Member Rules, registrants have an obligation to observe high standards of ethics and conduct, to not engage in conduct which is unbecoming or detrimental to the public interest and to ensure trading recommendations which are consistent with good business practices. As set out in the Panel liability decision, the Respondent recommended numerous transactions which resulted in substantial DSC fees being incurred by the clients who were unsophisticated, trusted the Respondent and relied on him to act in their best interests. They did not know or appreciate the amount of fees they were incurring or the extent to which the Respondent benefited from those transactions. In total, nine clients identified by Mr. Noguera paid DSC fees of \$116,000 and realized losses of \$72,000 as result of these transactions. The clients were clearly harmed by the transactions recommended to them by the Respondent.

¶ 13 In his submissions, the Respondent argued that all his recommendations were legitimate investment decisions and that the use of funds involving DSCs is a legitimate investment choice. The Panel’s liability decision recognized that using DSC based mutual funds may be a legitimate investment choice in certain circumstances, but concluded that the repetitive and excessive use of DSC funds and the inappropriate investment choices recommended by the Respondent amounted to a breach of the Respondent’s obligations to his clients. The Respondent also argued that the results realized by the clients were much better than stated by IIROC. IIROC acknowledged this, and the Panel’s liability decision reflected that it was not the overall result achieved in the client accounts, but the process involved that was inappropriate; excessive DSC fees and unnecessary losses were incurred as a result of the Respondent’s recommendations, as set out in the Panel’s liability decision. However, in coming to its decision on the appropriate penalty, the Panel took into account as a mitigating factor that some of the investment recommendations may have been appropriate as argued by the Respondent.

¶ 14 Further, the Dealer Member was clearly harmed by the Respondent’s borrowing from his clients. When the client loans were discovered, HSBC immediately repaid the loans in full and has not recovered these amounts from the Respondent.

Blameworthiness and Degree of Participation

¶ 15 As reflected in its decision on liability, the Panel agrees with the IIROC submissions on this point. The Respondent recommended all the transactions, the clients were not fully apprised of the costs and fees involved, certain of the transactions were not authorized by the clients, some of the trades were marked “unsolicited” despite client evidence that they did not initiate any of them and DSC fees were incurred by client RC despite his evidence that he advised the Respondent to avoid transactions involving DSC fees.

¶ 16 Furthermore, the Respondent admitted that he did not disclose to or seek approval from his Dealer Member prior to borrowing funds from his clients. He advised the Panel that he thought borrowing from clients

was allowed because it was not prohibited by a specific IIROC rule. However client borrowing is dealt with in the CPH, the Guidelines and prior cases published on the IIROC website; and the Respondent did not seek advice on the borrowings from the HSBC compliance department or from IIROC. Although borrowing from clients without obtaining his Member's approval may have been an oversight on his part, the Respondent is responsible for knowing his obligations as a registrant in the securities industry.

¶ 17 It is the Panel's decision that the Respondent is fully responsible for his misconduct under both counts.

Extent to which Respondent Benefited from his Misconduct

¶ 18 The Respondent earned commissions of over \$69,000 on the transactions identified by Mr. Noguera, and also borrowed, without repaying, \$45,000 from clients. It is the decision of the Panel that the Respondent should not benefit from his misconduct and therefore disgorgement of the commissions and the amount borrowed, in the amounts requested by IIROC, is appropriate.

Acceptance of Responsibility, Acknowledgment of Misconduct and Remorse

¶ 19 It is clear to the Panel that the Respondent has not accepted responsibility for his actions, continuing to assert that the transactions were legitimate investment decisions for the benefit of his clients notwithstanding the Panel's finding that the transactions resulted in unnecessary costs to the clients and unwarranted commissions earned by the Respondent. Furthermore, once he learned that borrowing from clients was wrong, the Respondent acknowledged his wrongdoing, but there is no evidence that the Respondent has attempted to repay the money borrowed from clients nor to compensate his Member after they repaid the clients.

Prior Disciplinary Record

¶ 20 As a mitigating factor, the Respondent has no prior disciplinary record.

Planning and Organization

¶ 21 The Panel agrees with the IIROC submissions that the Respondent's actions were calculated and deliberate, were designed to benefit him and not his clients and the majority of, if not all, the transactions were inappropriate investment decisions as outlined in the Panel's liability decision.

Multiple Incidents over an Extended Time Period

¶ 22 The Panel agrees with the IIROC submissions that the Respondent recommended numerous inappropriate transactions in at least nine client accounts; these took place over a period of 15 months and amounted to a pattern of behaviour, which is an aggravating factor in determining the appropriate penalty.

Vulnerability of Victims

¶ 23 The two clients who testified were both unsophisticated investors who relied on the Respondent for investment advice and to act in their best interests. They were unable to appreciate the costs to them of the DSC fees being incurred or the inappropriateness of the transactions recommended by the Respondent.

5. PREVIOUS REGULATORY DECISIONS

¶ 24 The IIROC written submissions on penalty referred the Panel to a number of prior case involving circumstances similar to those giving rise to counts 1 and 2 in this case. Regarding count 1, the Panel were referred to and reviewed *Re Fridgant*, [2000] I.D.A.C.D. No. 27, *Re Herd*, [2003] I.D.A.C.D. No. 20, *Re Newman*, 2012 LNIROOC 55, *Re Burner*, 2010 LNCMFDA 46 and MFDA File No. 201004, and *Re Budnik*, 2011 IIROC 55. Regarding count 2 the cases were *Re Evans*, [2007] I.D.A.C.D. No.53, *Re Dass* 2009 IIROC 22 and *Re Hackett*, 2010 IIROC 5.

¶ 25 Although the facts in these cases were all somewhat different than in our case, the Panel found these cases to be instructive in reaching its decision on the appropriate penalty in this case.

6. PENALTY DECISION

¶ 26 Regarding the suspension requested by IIROC, the Panel decided that, although a suspension is

appropriate, due to the long time that the Respondent has been out of the industry, no additional suspension is warranted. Regarding the fine of \$79,170 requested by IIROC for count 1, the Panel decided that the portion representing disgorgement of profits should be reduced from \$69,170 to \$50,000 on the basis that some of the transactions may have been legitimate investment decisions, resulting in a total fine of \$60,000 in regard to count 1. The Panel agreed that the fine of \$55,000 for count 2 and the period of supervision requested by IIROC were both appropriate.

¶ 27 In addition, IIROC requested costs of \$97,777.50. The Panel decided that a portion of the costs incurred in this case was due to the numerous adjournments to which the Panel had agreed. Consequently the Panel decided to reduce the costs awarded to IIROC to \$65,000.

¶ 28 Therefore the Panel decided that the following penalties were appropriate in this case:

- a global fine of \$115,000 broken down as follows:
- \$50,000 representing disgorgement of commissions plus an additional fine of \$10,000 in relation to count 1;
- \$55,000 in relation to count 2, representing disgorgement of loan proceeds of \$45,000 plus an additional fine of \$10,000; and
- a 12 month period of strict supervision upon any reregistration with IIROC.

Dated as of the 19th day of December, 2014.

Reasons released January 19, 2015.

Frederick H. Webber- Chair

Hugh McNabney- Industry Member

Ron Smith- Industry Member

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