

Re First Financial Securities

IN THE MATTER OF:

**The Rules of the Investment Industry Regulatory Organization of
Canada (IIROC)**

and

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

and

First Financial Securities Inc.

2013 IIROC 44

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

Heard: July 31, 2013
Decision: August 1, 2013

Hearing Panel:

Linda J. Murray (Chair), L. Karen Henderson, and Barbara Fraser

Appearances:

Ms. Wietzke Gerber, Senior Enforcement Counsel, for IIROC

Mr. Gary Hein, representative for First Financial Securities Inc.

Hearing Panel Reasons for Decision (Settlement Hearing)

Introduction

¶ 1 Pursuant to Investment Industry Regulatory Organization of Canada (IIROC) Dealer Member Rule 20.36, this Panel was constituted to consider whether to accept a settlement agreement (the “Settlement Agreement”) negotiated between IIROC's Enforcement Department and First Financial Securities Inc. (“First Financial”).

¶ 2 At the conclusion of a settlement hearing held in Vancouver, British Columbia on July 30, 2013, and after considering submissions by the parties and the terms of the Settlement Agreement, we determined unanimously to accept the Settlement Agreement. We advised the parties that our written reasons would follow. These are our reasons.

The Settlement Agreement

¶ 3 The Settlement Agreement, which is annexed to this decision, contains:

- (a) a summary of the underlying facts;
- (b) an admission by First Financial that, since December 12, 2012, it has failed to meet IIROC's minimum capitalization requirements, contrary to IIROC Dealer Member Rule 17.1; and

- (c) First Financial's agreement to termination of its membership in IIROC, pursuant to IIROC Dealer Member Rule 20.34(2)(e).

¶ 4 Ms. Gerber referred us to the following relevant decisions regarding the role of the Panel in considering the Settlement Agreement:

- a. *Re Milewski* [1999] IDACD No. 17;
- b. *Rault v. Law Society of Saskatchewan* [2009] SKCA 81;
- c. *Re Higgs* [2010] LNIIROC 3;
- d. *Re Graydon Elliott Capital Corporation*, [2007] IDACD No. 43;
- e. *Re Prodigy Wealth Management Corp.*, [2009] LNIIROC 51; and
- f. *Re Gateway Securities Inc.*, [2011] LNIIROC 8.

¶ 5 We adopt the comments of the Panel in *Re Gateway Securities Inc.* [2011] LNIIROC 8 (para 4), which quoted with approval comments by the Panel in *Re Higgs*, regarding the Panel's role when considering a settlement agreement pursuant to IIROC Dealer Member Rule 20-36:

[4] There are two broad related principles that apply in connection with a decision to accept or reject a settlement;

[5] The first is succinctly stated in the following passage from the decision in *Re Milewski* [1999] I.D.A.C. No. 17, August 5, 1999 at page 11:

A District Council considering a settlement agreement will tend not to alter a penalty that it considers to be within a reasonable range, taking into account the settlement process and the fact that the parties have agreed. It will not reject a settlement unless it views the penalty as clearly falling outside a reasonable range of appropriateness.

[6] Secondly, in the recent decision of the Saskatchewan Court of Appeal in *Rault v. Law Society of Saskatchewan* [2009 SKCA 81 (Can Lii)], the court cited with approval and applied to an administrative tribunal the principles applicable to joint submissions on sentencing in criminal cases described by the Alberta Court of Appeal in *R. v. G.W.C.* [2000 ABCA 333 (Can Lii)], namely, that there is an obligation on the tribunal to give serious consideration to a joint submission on sentencing agreed upon by counsel unless the sentence is unfit or unreasonable; or contrary to the public interest; and, it should not be departed from unless there are good or cogent reasons for doing so.

¶ 6 We are of the unanimous view that acceptance of this Settlement Agreement is consistent with the foregoing principles. Counsel for IIROC and First Financial's representative jointly recommended that the Panel accept the Settlement Agreement as negotiated by the parties.

DISCUSSION

¶ 7 We noted that the breach of IIROC Dealer Member Rule 17.1 did not occur at the time when First Financial was actively carrying on business as a Dealer Member. As of September 26, 2012 First Financial sold its book of business to another Dealer Member, as of November 23, 2012 all nominee positions had been successfully transferred, and by January 7, 2013 only a few client registered positions remained to be transferred. At the time that the capital deficiency arose on December 12, 2012, the bulk of the client name account transfers were completed, all of the nominee account transfers were completed, and there were no Approved Persons remaining at the firm with authority to trade. As a result, the breach did not cause imminent harm to the public or to the market.

¶ 8 Although First Financial submitted a letter of intent to resign its membership to IIROC on January 29, 2013, a subordinated loan had been withdrawn on December 12, 2012, effectively putting the firm in contravention of IIROC Dealer Member Rule 17.1 regarding Risk Adjusted Capital requirements and

preventing First Financial from completing a resignation under IIROC Rule 8 which provided:

8.2 Dealer Member which tenders its resignation shall in its letter of resignation state its reasons for resigning and shall file with the Secretary one of:

(a) A balance sheet of the Dealer Member reported upon by the Dealer Member's Auditor without qualification as of such date as the Corporation may require which balance sheet shall indicate that the Dealer Member has liquid assets sufficient to meet all its liabilities other than subordinated loans, if any; or

(b) A report from the Dealer Member's Auditor without qualification that in his or her opinion the Dealer Member has liquid assets sufficient to meet all its liabilities other than subordinated loans, if any;

And a report from the Dealer Member's Auditor that clients' free securities are properly segregated and earmarked. If the financial information required by (a) or (b) above is not filed with the letter of resignation the Dealer Member shall indicate in the letter of resignation the date by which such financial information shall be filed.

¶ 9 We were advised by Mr. Hein, the representative for First Financial, that the subordinated loan was cancelled due to unrelated proceedings involving a matrimonial matter. Mr. Hein and Ms. Gerber advised us that, had the timing been different and the subordinated loan remained in place, First Financial's resignation application would have proceeded and been referred to IIROC's Board of Directors in the normal course pursuant to IIROC Rule 8. Due to the Risk Adjusted Capital deficiency, First Financial's resignation application could not proceed under IIROC Rule 8. Accordingly, this matter proceeded instead by way of Settlement Agreement.

¶ 10 Ms. Gerber advised us that the parties agreed to termination of membership under IIROC Dealer Member Rule 20.34(2)(e) rather than expulsion from membership under Rule 20.34(2)(f) due to the unique facts of this case and, in particular, the fact that First Financial's resignation application had already been filed but could not be completed by IIROC's Board of Directors due to operation of IIROC Rule 8 and the outstanding capital deficiency.

¶ 11 By virtue of this Panel's decision, the Settlement Agreement effectively concludes First Financial's involvement as an IIROC Dealer Member.

¶ 12 The Panel, after careful consideration, concluded that the Settlement Agreement terms:

- a. are reasonable and within the appropriate range for sanctions, given the facts and circumstances set out in the Settlement Agreement, the submissions of counsel, and the authorities cited; and
- b. meet IIROC's *Dealer Member Disciplinary Sanction Guidelines* and the principles of specific and general deterrence.

¶ 13 For the reasons set out above, the Panel unanimously accepted the Settlement Agreement. In accordance with the terms of the Settlement Agreement, the Panel ordered, effective on the date of the Settlement Hearing, being July 30, 2013, that First Financial's membership in IIROC be terminated pursuant to IIROC Dealer Member Rule 20.34(2)(e).

Dated as of August 1, 2013

Linda J. Murray, Chair

Barbara Fraser, Member

L. Karen Henderson, Member

APPENDIX - SETTLEMENT AGREEMENT

INVESTMENT INDUSTRY REGULATORY ORGANIZATION OF CANADA

IN THE MATTER OF:

THE RULES OF THE INVESTMENT INDUSTRY REGULATORY ORGANIZATION OF CANADA (IIROC)

AND

THE BY-LAWS OF THE INVESTMENT DEALERS ASSOCIATION OF CANADA (IDA)

AND

FIRST FINANCIAL SECURITIES INC.

SETTLEMENT AGREEMENT

I. INTRODUCTION

1. IIROC Enforcement Department Staff (Staff) has received information from IIROC's Financial and Operations Compliance Department regarding First Financial Securities Inc. (the Respondent).
2. Staff's review of the referral disclosed matters for which the Respondent may be disciplined by a hearing panel appointed pursuant to IIROC Transitional Rule No.1 (the Hearing Panel).
3. Staff and the Respondent consent and agree to the settlement of this matter by way of this settlement agreement (the Settlement Agreement).

II. JOINT SETTLEMENT RECOMMENDATION

4. Staff and the Respondent jointly recommend that the Hearing Panel accept this Settlement Agreement.
5. The Respondent admits that since December 12, 2012, it has failed to meet IIROC's minimum capitalization requirement, contrary to IIROC Dealer Member Rule 17.1.
6. Staff and the Respondent agree to the following terms of settlement:
 - a) The Respondent agrees to the termination of its membership in IIROC, pursuant to IIROC Dealer Member Rule 20.34(2)(e).

III. STATEMENT OF FACTS

(i) Acknowledgment

7. Staff and the Respondent agree with the facts set out in this Section III and acknowledge that the terms of the settlement contained in this Settlement Agreement are based upon those specific facts.

(ii) Factual Background

8. Effective December 11, 2002, the Respondent was admitted to membership in the Investment Dealers Association of Canada.
9. Effective June 1, 2008, the Respondent was admitted to the membership of IIROC.
10. As of September 26, 2012, the Respondent sold its book of business to another Dealer Member (the Acquiring Dealer Member) and informed its clients that the transfer of their accounts would occur over the weekend of October 27/28, 2012.
11. As of November 23, 2012, no Approved Persons with authority to trade remained at the Respondent.
12. All nominee accounts were transferred to the Acquiring Dealer Member on November 23, 2012.
13. On January 7, 2013, the Respondent advised IIROC that only a few client registered positions remained to be transferred to the Acquiring Dealer Member.

14. Presently, all of the Respondent's client assets have been transferred to the Acquiring Dealer Member.
15. By way of a January 29, 2013 letter, the Respondent informed IIROC that it intended to resign its IIROC membership.
16. On February 1, 2013, IIROC published IIROC Notice 13-0031, announcing that IIROC had been informed of the Respondent's intention to resign.
17. The resignation of the Respondent's IIROC membership is currently pending.

Risk Adjusted Capital

18. Risk adjusted capital is a defined measure of a Dealer Member's capital (calculated pursuant to Generally Accepted Accounting Principles) that has been adjusted for regulatory purposes. The calculation of risk adjusted capital is the primary means by which the financial status of a Dealer Member is prescribed and monitored.
19. IIROC Dealer Member Rule 17.1 requires all Dealer Members to always maintain risk adjusted capital greater than zero as calculated in accordance with Form 1. If at any time the risk adjusted capital of a Dealer Member is less than zero, that Dealer Member is required to immediately notify IIROC.
20. The requirement that a Dealer Member must maintain positive risk adjusted capital is essential for the determination of the financial solvency of a Dealer Member and ultimately for the protection of the public, other Dealer Members, and IIROC.
21. Through the filing of an annual audited Form 1 and a monthly financial report (MFR), Dealer Members are required to regularly calculate and then submit their risk adjusted capital status to IIROC.

Risk Adjusted Capital Deficiency (Capital Deficiency)

22. On February 2, 2013, the Respondent electronically filed its MFR for December 2012. The December 2012 MFR indicated that as of December 31, 2012, the Respondent had a Capital Deficiency of \$241,000.
23. The Capital Deficiency occurred due to the cancellation of a subordinated loan and the subsequent removal of \$290,000 on December 12, 2012.
24. The Respondent was designated in Early Warning Level 2 on February 5, 2013. IIROC requested a written action plan by February 12, 2013 to address the Capital Deficiency.
25. On February 13, 2013, IIROC was informed that the Respondent was unable to remedy the Capital Deficiency.
26. Pursuant to IIROC Dealer Member Rule 8, the IIROC Board of Directors may only consider an application for resignation if a Dealer Member has liquid assets sufficient to meet all its liabilities other than subordinated loans. Given that the Respondent presently has an unresolved Capital Deficiency and does not have liquid assets sufficient to meet all its liabilities, the IIROC Board of Directors cannot consider the Respondent's application for resignation.

IV. TERMS OF SETTLEMENT

27. This settlement is agreed upon in accordance with IIROC Dealer Member Rules 20.35 to 20.40, inclusive and Rule 15 of the Dealer Member Rules of Practice and Procedure.
28. The Settlement Agreement is subject to acceptance by the Hearing Panel.
29. The Settlement Agreement shall become effective and binding upon the Respondent and Staff as of the date of its acceptance by the Hearing Panel.
30. The Settlement Agreement will be presented to the Hearing Panel at a hearing (the Settlement Hearing) for approval. Following the conclusion of the Settlement Hearing, the Hearing Panel may either accept or reject the Settlement Agreement.

31. If the Hearing Panel accepts the Settlement Agreement, the Respondent waives his/her/its rights under IIROC rules and any applicable legislation to a disciplinary hearing, review or appeal.
32. If the Hearing Panel rejects the Settlement Agreement, Staff and the Respondent may enter into another settlement agreement; or Staff may proceed to a disciplinary hearing in relation to the matters disclosed in the Investigation.
33. The Settlement Agreement will become available to the public upon its acceptance by the Hearing Panel.
34. Staff and the Respondent agree that if the Hearing Panel accepts the Settlement Agreement, they, or anyone on their behalf, will not make any public statements inconsistent with the Settlement Agreement.
35. Unless otherwise stated, any monetary penalties and costs imposed upon the Respondent are payable immediately upon the effective date of the Settlement Agreement.
36. Unless otherwise stated, any suspensions, bars, expulsions, restrictions or other terms of the Settlement Agreement shall commence on the effective date of the Settlement Agreement.

AGREED TO by the Respondent at the City of Courtenay in the Province of British Columbia, this 6th day of June, 2013.

“Witness”

Witness

“Respondent”

Respondent

AGREED TO by Staff at the City of Vancouver in the Province of British Columbia, this 25th day of July, 2013.

“Shannon Mathieson”

Witness

“Wietzke Gerber”

Wietzke Gerber

Enforcement Counsel on behalf of Staff of
the Investment Industry Regulatory
Organization of Canada

ACCEPTED at the City of Vancouver in the Province of British Columbia, this 30th day of July, 2013, by the following Hearing Panel:

Per: “Linda Murray”

Panel Chair

Per: “Barbara Fraser”

Panel Member

Per: “Karen Henderson”

Panel Member

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