

Re Zhang

IN THE MATTER OF:

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

and

The Universal Market Integrity Rules (UMIR)

and

Yufeng Zhang

2013 IIROC 35

Investment Industry Regulatory Organization of Canada
Hearing Panel (British Columbia District)

Heard: May 30, 2013

Decision: May 30, 2013

Hearing Panel:

Jean P. Whittow Q.C. - Chair, Barbara Fraser and Robert Travers

Appearances:

Paul Smith, Enforcement Counsel for IIROC

Teresa M. Tomchak, Respondent Counsel for the Respondent

DECISION AND REASONS

¶ 1 As a result of a Settlement Agreement entered into between IIROC and the Respondent, a Settlement Hearing was conducted on May 30, 2013 in Vancouver, pursuant to the IROC Dealer Member Rules.

¶ 2 The Hearing Panel received oral submissions from IIROC counsel and the Respondent's counsel and received the IIROC Settlement Brief containing the Settlement Agreement, extracts from the UMIR Rules and Policies, and previous relevant decisions.

¶ 3 After the conclusion of counsels' submissions, the Panel retired to consider whether it would accept the Settlement Agreement. We subsequently advised the parties that we accepted the Settlement Agreement, with written reasons to follow.

The Admissions

¶ 4 The contravention alleged by IIROC and admitted by the Respondent is set out in the Settlement Agreement as follows:

On 25 days in the period July 2010 to December 2010, [the Respondent], a proprietary trader employed by Wolverton Securities Ltd., engaged in a manipulative or deceptive practice in the pre-opening on a marketplace contrary to UMIR 2.2(1) and UMIR Policy 2.2, for which he is liable under UMIR 10.4(1).

¶ 5 The Sanctions agreed to in the Settlement Agreement are:

- a. a fine of \$10,000;
- b. a suspension of access to IIROC-regulated marketplaces for 1 month beginning June 1, 2013;
and
- c. costs of \$1,500.

¶ 6 The relevant facts are set out in the Settlement Agreement attached hereto. In summary, the Respondent entered orders in the pre-opening session in several securities in order to identify the size of the “iceberg” orders entered on the opposite side of the market. “Iceberg” orders are large orders, where only a small portion of the order shows on the quote screen. At the time of the infraction, these partial (or “iceberg”) orders were identified as such. By placing a series of change orders and observing their impact on the price, the Respondent was able to determine the approximate size of the iceberg order. This practice is commonly referred to as “abusive liquidity detection”. The Respondent then cancelled his pre-opening orders. In some cases he entered orders just ahead of the bid/offer knowing there was a large order outstanding. This pattern occurred on 25 days over about 6 months.

¶ 7 The gravamen of the offence was that the Respondent placed fictitious orders that were not intended to be filled. The Panel was advised that, because the orders were placed and cancelled pre-opening, the market was not affected, but the orders gave a false or misleading appearance of interest in the purchase or sale of a security or an artificial ask price, bid price or sale price for a security. This is the conduct prohibited under UMIR 2.2(1) and UMIR Policy 2.2.

The Standard for Reviewing a Settlement Agreement

¶ 8 In considering a Settlement Agreement, a panel may only accept or reject the agreement (UMIR Policy 10.8, Part 3.4).

¶ 9 It is well established on the authorities that a Panel “should not interfere lightly in a negotiated settlement” and should accept the agreement provided that it falls within a “reasonable range” (*Re Geddes*, 2012 IIROC 12).

Submissions

¶ 10 IIROC counsel placed the case on the low end of the range of misconduct. He noted that the Respondent had earned minimal profit and that the Respondent had cooperated in the investigation and discipline process. The Respondent’s counsel noted that the Respondent has been in the industry for 20 years and has no prior discipline violations.

¶ 11 IIROC counsel reviewed three past cases involving similar conduct to the present case. These cases are summarized as follows.

¶ 12 In *Re Nguyen-Qui*, 2012 IIROC 53, the respondent entered and cancelled trades pre-market, over a 3 1/2-month period. IIROC counsel noted that there were 3 allegations, dealing with two different types of conduct, only one of which is similar to the present case. While the overall penalty was \$20,000 and a suspension of 2 months, the portion of fine attributed to the deceptive trading was \$10,000. He suggested that by application of the same logic, one-half of the 2 month suspension was attributable to the trading activity, therefore the same as the suspension agreed upon in the present case.

¶ 13 In *Re Geddes*, supra, the respondent entered orders late in the trading day in a particular stock which he admitted that he ought to have known would create an artificial price. The amount and duration of activity was longer than in the present case and did in fact impact the price. He was fined \$30,000 and suspended 60 days.

¶ 14 In *Re Mashregi*, [2005] R.S.D.D. No. 8, the respondent engaged in a pattern of order entry on both sides of the market in the pre-opening of a trading session. This occurred on 248 days over two years, and therefore was more prolonged than in the present case. The penalty imposed was a \$50,000 fine only.

Conclusion

¶ 15 The Panel agrees with counsels’ submission that the *Re Nguyen-Qui* case is most similar to the one

before the Panel.

¶ 16 Given the nature of the misconduct, and having considered the relevant cases, and noting the UMIR Guidelines for the imposition of sanction, the Panel agreed that the terms of the Settlement Agreement were within the appropriate range. The Panel therefore accepted the Settlement Agreement.

Dated as of the 30th day of May, 2013.

Jean P. Whittow, Q.C., Chair

Barbara Fraser, Member

Robert Travers, Member

OFFER OF SETTLEMENT

A. INTRODUCTION

1. The Enforcement Department Staff (Staff) of the Investment Industry Regulatory Organization of Canada (IIROC) has conducted an investigation (the Investigation) into the conduct of Yu Feng Zhang (the Respondent).
2. The Investigation has disclosed matters for which IIROC seeks certain sanctions against the Respondent pursuant to Rule 10.5 of the Universal Market Integrity Rules (UMIR).
3. If this Offer of Settlement is accepted by the Respondent, 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).
4. The Respondent 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.
5. The Respondent consents to be subject to the jurisdiction of IIROC and its relevant disciplinary process and rules in relation to this matter.
6. Staff and the Respondent jointly recommend that the Hearing Panel accept this Settlement Agreement.

B. AGREEMENT AS TO REQUIREMENTS CONTRAVENED

7. The Respondent agrees to the following contravention:
 - (i) On 25 days in the period July 2010 to December 2010, Yufeng Zhang, a proprietary trader employed by Wolverton Securities Ltd., engaged in a manipulative or deceptive practice in the pre-opening on a marketplace contrary to UMIR 2.2(1) and UMIR Policy 2.2, for which he is liable under UMIR 10.4(1).

C. ADMITTED FACTS

8. For the purposes of this Settlement Agreement only, Staff and the Respondent agree with and rely upon the admitted facts and conclusions which are set out in the Statement of Allegations attached as Appendix A to this Settlement Agreement.

D. DISPOSITION

9. For the contravention in paragraph 7 above, Staff and the Respondent have agreed upon disposition as follows:
 - (i) a fine of \$10,000.00 payable by the Respondent to IIROC;
 - (ii) a suspension of access to IIROC-regulated marketplaces for 1 month beginning June 1, 2013; and

(iii) costs of \$1,500.00 payable by the Respondent to IIROC.

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

10. The Respondent shall have until the close of business on May 29, 2013 to accept the Offer of Settlement and serve an executed copy thereof on Staff.
11. This Settlement Agreement shall be presented to a Hearing Panel at a public 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. The Respondent acknowledges that IIROC shall notify the public and media of the Approval Hearing in such manner and by such media as IIROC sees fit.
12. Pursuant to Part 3.4 of UMIR Policy 10.8, the Hearing Panel may accept or reject this Settlement Agreement.
13. In the event the Settlement Agreement is accepted 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 this Settlement Agreement will be included in the permanent record of IIROC in respect of the Respondent and IIROC will publish a summary of the Requirements contravened, the facts, and the disposition agreed upon in the Settlement Agreement.
14. 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 this Settlement Agreement may not be referred to without the consent of both parties.
15. The Respondent agrees that, in the event he fails to comply with any of the terms of the Settlement Agreement, IIROC may enforce this settlement in any manner it deems appropriate and may, without limiting the generality of the foregoing, suspend the Respondent's access to marketplaces regulated by IIROC until IIROC determines that the Respondent is in full compliance with all terms of the Settlement Agreement.
16. The Respondent agrees that neither he, nor anyone on his behalf, will make a public statement inconsistent with this Settlement Agreement.

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

DATED at Vancouver, British Columbia on the ___ day of May, 2013.

“Witness”

“Yufeng Zhang”

Witness Signature

Yufeng Zhang

DATED at Vancouver, British Columbia on the 30 day of May, 2013.

Per: “Warren Funt”

Warren Funt

Vice President, Western Canada

INVESTMENT INDUSTRY REGULATORY ORGANIZATION OF CANADA

Suite 2800, 1055 West Georgia Street

Vancouver, British Columbia V6E 3R5

This foregoing Settlement Agreement is hereby approved this 30th day of May, 2013 by the following hearing panel constituted to review the terms thereof:

Per: “Jean Whittow
Panel Chair
Per: “Barbara Fraser”
Panel Member
Per: “Robert Travers”
Panel Member

APPENDIX “A”

INVESTMENT INDUSTRY REGULATORY ORGANIZATION OF CANADA

IN THE MATTER OF:

**THE RULES OF THE INVESTMENT INDUSTRY REGULATORY ORGANIZATION OF
CANADA**
AND
THE UNIVERSAL MARKET INTEGRITY RULES
AND
YUFENG ZHANG

STATEMENT OF ALLEGATIONS

I. REQUIREMENTS CONTRAVENED

1. On 25 days in the period July 2010 to December 2010 (the “Relevant Period”), Yufeng Zhang (the “Respondent”), a proprietary trader employed by Wolverton Securities Ltd., engaged in a manipulative or deceptive practice in the pre-opening on a marketplace contrary to UMIR 2.2(1) and UMIR Policy 2.2, for which he is liable under UMIR 10.4(1).
2. Schedule “A” sets out the text of the relevant UMIR Requirements.

II. RELEVANT FACTS AND CONCLUSIONS

Overview

3. During the Relevant Period, the Respondent entered orders in the pre-opening session in several TSXV-listed securities in order to identify the depth of the market and more particularly to detect the size of iceberg orders entered on the opposite side of the market.
4. The practice of entering orders, either disclosed or iceberg, during the pre-opening session, to detect the existence of a large trading interest on the opposite side of the market with the intention of trading ahead of the large buyer or seller constitutes a manipulative or deceptive practice contrary to UMIR 2.2(1). This practice is commonly known as “abusive liquidity detection.”

Background

5. Wolverton Securities Ltd. (“Wolverton”) is registered as an investment dealer and is a Participant under UMIR.
6. The Respondent has been employed in the securities industry since 1994 and has been a proprietary inventory trader at Wolverton since 2003. The Respondent has no prior disciplinary history.
7. In the course of an IIROC Trading Conduct Compliance review of Wolverton in 2011, IIROC Staff identified a pattern of large volume orders entered and subsequently cancelled in the pre-opening session by the Respondent in three TSXV-listed securities over a period of three days in December 2010.

8. A further analysis of the Respondent's order entry for the period June 1, 2010 to December 31, 2010 identified 25 trading days on which the Respondent engaged in a manipulative or deceptive practice in the pre-opening session.

The Manipulative or Deceptive Practice – Abusive Liquidity Detection

9. On 25 days during the Relevant Period, the Respondent entered orders for the purpose of detecting the size of iceberg orders on the opposite side of the market.

10. The Respondent engaged in this practice in several TSX-listed securities as set out below:

July 15, 2010	Natcore Technology Inc. – NXT
July 26, 2010	Anglo Canadian Oil Corp. – ACG
July 27, 2010	Anglo Canadian Oil Corp. – ACG
August 4, 2010	Anglo Canadian Oil Corp. – ACG
August 10, 2010	Anglo Canadian Oil Corp. – ACG
August 10, 2010	EnWave Corp. – ENW
August 13, 2010	Anglo Canadian Oil Corp. – ACG
August 17, 2010	Anglo Canadian Oil Corp. – ACG
August 20, 2010	Probe Mines Ltd. – PRB
August 24, 2010	Probe Mines Ltd. – PRB
August 25, 2010	Probe Mines Ltd. – PRB
August 26, 2010	Probe Mines Ltd. – PRB
September 7, 2010	Titan Medical Inc. – TMD
October 1, 2010	Typhoon Exploration Inc. – TYP
October 6, 2010	Strategic Metals Ltd. – SMD
October 7, 2010	Strategic Metals Ltd. – SMD
October 8, 2010	Strategic Metals Ltd. – SMD
October 12, 2010	Strategic Metals Ltd. – SMD
October 13, 2010	Strategic Metals Ltd. – SMD
October 26, 2010	Strategic Metals Ltd. – SMD
October 27, 2010	Strategic Metals Ltd. – SMD
November 30, 2010	Western Potash Corp. – WPX
December 9, 2010	Reservoir Capital Corp. – REO
December 13, 2010	Reservoir Capital Corp. – REO
December 14, 2010	Reservoir Capital Corp. – REO

11. The Respondent's trading activity in TYP on October 1, 2010 is representative of the Respondent's practice of engaging in abusive liquidity detection.

12. On October 1, 2010, the Respondent entered an anonymous iceberg sell order in the pre-opening session and then proceeded to CFO the size of the order until the size of the buying interest on the opposite side of the market was discovered to be between 65,000 and 95,000 shares. Once the size of the buying interest was discovered the Respondent cancelled his sell order. Shortly before the market opened the

Respondent entered an order to buy 5,000 shares at \$1.51 which was filled when trading opened.

13. The table below sets out the particulars of this order entry:

Time	Action	Bid Size	Bid Price	Ask Price	Ask Size	Price	Volume	Undisclosed Volume
7:44:10	QUOTE	5000	\$1.42	\$1.53	5000			
8:32:19	PARTICIPANT BUY ORDER					\$1.50	71,000	66,000
8:32:19	QUOTE	5000	\$1.50	\$1.53	5000			
8:56:55	RESPONDENT'S SELL ORDER					\$1.49	15,000	13,000
8:56:55	QUOTE	5000	\$1.50	\$1.50	2000			
8:57:02	CFO					\$1.49	25,000	23,000
8:57:07	CFO					\$1.49	35,000	33,000
8:57:14	CFO					\$1.49	55,000	53,000
8:57:19	CFO					\$1.49	95,000	93,000
8:57:19	QUOTE	5000	\$1.49	\$1.49	2000			
8:57:25	CFO					\$1.49	75,000	73,000
8:57:31	CFO					\$1.49	65,000	63,000
8:57:31	QUOTE	5000	\$1.50	\$1.50	2000			
8:57:34	ORDER CANCELLED					\$1.49	65,000	63,000
8:57:34	QUOTE	5000	\$1.50	\$1.53	5000			

14. The Respondent entered an anonymous iceberg sell order at 8:32:19 for 15,000 shares of TYP at \$1.49, with only 2,000 shares displayed. The prevailing quote at the time of the order was \$1.50 bid/\$1.53 ask. The respondent's order changed the quote to \$1.50 bid/\$1.50 ask. Over the next 17 seconds, the Respondent "CFO'd" his order four times to increase its size. When the size of the order reached 95,000 shares, the quote changed to \$1.49 bid/\$1.49 ask. The Respondent then "CFO'd" the order twice down to 65,000 shares at which time the quote returned to \$1.50 bid/\$1.50 ask. Three seconds later, the Respondent cancelled his sell order.

Mitigating Factors

15. The Respondent realized minimal profits from engaging in the manipulative or deceptive practice.
16. At an early juncture of the IIROC investigation, the Respondent approached IIROC Staff and acknowledged that his order entry was a violation of UMIR Requirements, thereby reducing the cost of resolving this matter.

Supervision by Wolverton

17. After the December 2010 trading activity was brought to Wolverton's attention during the IIROC Trade Conduct Compliance Review, the Respondent was told to immediately cease engaging in the practice.
18. Although Wolverton's supervisory system did not detect the Respondent's manipulative or deceptive practice, the firm did have a supervision system in place at the time that was reasonably well designed to prevent and detect contraventions of UMIR. Wolverton has since implemented more comprehensive pre-opening supervisory policies and procedures.

III. CONCLUSION

19. The purpose of UMIR 2.2(1) and Policy 2.2 is to prohibit the use of manipulative or deceptive methods, acts or practices which harm market integrity.
20. The Respondent's practice of entering orders in the pre-opening session in several TSXV-listed securities in order to detect the size of iceberg orders entered on the opposite side of the market constituted a manipulative or deceptive method, act or practice. This practice harmed the integrity of the TSXV marketplace.

May 13, 2013

INVESTMENT INDUSTRY REGULATORY ORGANIZATION OF CANADA

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SCHEDULE "A"

EXCERPTS FROM THE UNIVERSAL MARKET INTEGRITY RULES

2.2 Manipulative and Deceptive Activities

- (1) A Participant or Access Person shall not, directly or indirectly, engage in or participate in the use of any manipulative or deceptive method, act or practice in connection with any order or trade on a marketplace if the Participant or Access Person knows or ought reasonably to know the nature of the method, act or practice.

POLICY 2.2 – MANIPULATIVE AND DECEPTIVE ACTIVITIES

Part 1 – Manipulative or Deceptive Method, Act or Practice

There are a number of activities which, by their very nature, will be considered to be a manipulative or deceptive method, act or practice. For the purpose of subsection (1) of Rule 2.2 and without limiting the generality that subsection, the following activities when undertaken on a marketplace constitute a manipulative or deceptive method, act or practice:

- (a) making a fictitious trade;*
- (b) effecting a trade in a security which involves no change in the beneficial or economic ownership;*
- (c) effecting trades by a single interest or group with the intent of limiting the supply of a security for settlement of trades made by other persons except at prices and on terms arbitrarily dictated by such interest or group; and*
- (d) purchasing a security with the intention of making a sale of the same or a different number of units of the security or a related security on a marketplace at a price which is below the price of the last sale of a standard trading unit of such security displayed in a consolidated market display.*

If persons know or ought reasonably to know that they are engaging or participating in these or similar types of activities those persons will be in breach of subsection (1) of Rule 2.2 irrespective of whether such method, act or practice results in a false or misleading appearance of trading activity or interest in the purchase or sale of a security or an artificial ask price, bid price or sale price for a security or a related security.

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