Re Lee

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

and

Gabriel Ka Leung Lee

2013 IIROC 10

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

Heard: February 6, 2013 at Edmonton, Alberta
Decision: March 9, 2013

Hearing Panel:
Alan V.M. Beattie, Q.C. – Chair, James H. Ross, Donald Milligan
Appearances:
David McLellan - Senior Enforcement Counsel for the Investment Industry Regulatory Organization of Canada
Gabriel Ka Leung Lee, Respondent

REASONS FOR DECISION

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1. INTRODUCTION

¶ 1 A Settlement Agreement was entered into January 14, 2013 between the Investment Industry Regulatory Organization of Canada Enforcement Staff ("Staff" or "IIROC") and Gabriel Ka Leung Lee ("the Respondent") 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.

¶ 2 The Settlement Agreement contains a complete Statement of Facts, a description of the Contraventions and the Terms of Settlement (all below). In the Settlement Agreement the Respondent admits to the contraventions. Staff of IIROC and the Respondent jointly recommend that the Hearing Panel accept the Settlement Agreement. It is stated that the Settlement Agreement is subject to acceptance by the Hearing Panel and if the Panel accepts the Settlement Agreement, the Respondent waives his right under IIROC rules and any applicable legislation to a disciplinary hearing, review or appeal.

¶ 3 A Settlement Hearing Book was provided in advance of the Hearing by IIROC to the Respondent and his Counsel, and members of the Hearing Panel.

2. SETTLEMENT AGREEMENT

¶ 4 The Settlement Agreement includes the following:

CONTRAVENTIONS

7. The Respondent admits to the following contraventions of IIROC Rules, Guidelines, IDA By-Laws, Regulations or Policies:

   a) Between June 2008 and September 2011, the Respondent engaged in outside business activities by facilitating off-book investments and/or loans between eight clients and Asia Active Resources, without the knowledge of his firm and without proper exemptions under the *Securities Act (Alberta),* contrary to Dealer Member Rule 29.1;

   b) In 2009, the Respondent engaged in outside business activities by facilitating off-book investments by three clients in Castle Rock Research Corporation, without the knowledge of his firm, contrary to Dealer Member Rule 29.1;

   c) In or about February 2011, the Respondent engaged in personal financial dealings with a client without the knowledge or consent of his firm when he borrowed $100,000 from a client, FG, contrary to Dealer Member Rule 29.1.

TERMS OF SETTLEMENT

8. Staff and the Respondent agree to the following terms of settlement:

   a) The Respondent agrees to pay a fine to IIROC in the sum of seventy five thousand dollars ($75,000.00);

   b) The Respondent shall be prohibited from registration in any capacity for a period of six (6) months.

9. The Respondent agrees to pay costs to IIROC in the sum of five thousand dollars ($5,000.00).

STATEMENT OF FACTS

(i) Acknowledgment

10. 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

Overview

11. Without his firm's knowledge, Lee engaged in outside business activities by facilitating off-book equity and debt investments in private placements by six clients in two separate companies totaling $7,200,000. Lee also failed to question whether the investments in one of the companies was in accordance with the *Securities Act*.

12. In addition, Lee facilitated a short term loan of $100,000 from two elderly clients to one of the companies, without his firm's knowledge.

13. Lee also borrowed $100,000 from a client without his firm's knowledge.

Registration History

14. Lee became licensed in the securities industry as a registered representative "(RR)" in 1989. At all material times, he was employed as an RR in a branch of Richardson GMP Limited ("RGMP") in Edmonton.

Asia Active Resources Limited

15. In 2007, a friend introduced Lee to TC, the principal of Asia Active Resources Limited ("AAR"), a Hong Kong based company engaged in the supply chain logistics business in Asia. AAR was attempting to raise money from outside investors.

16. Beginning in May, 2008, Lee invited a number of his clients at RGMP to a meeting in Edmonton with TC, concerning a possible investment in AAR.

17. The clients were all high net worth individuals from Alberta, and nearly all were experienced business owners. For each of the clients, their stated investment knowledge in their account documentation was "good".

18. A number of the clients were interested in conducting due diligence concerning possibly investing in AAR. As a group, these clients hired a consultant (a friend of Lee's) to travel to Hong Kong to conduct due diligence.

19. The clients also retained legal counsel in Alberta, and in Hong Kong, to represent them.

20. Between approximately the middle of 2008 and September, 2011, six of Lee's clients invested a total of $6,000,000 in AAR private placements through a combination of debt and equity. For some of the clients, the funds invested were transferred from their RGMP account. However, the transactions were conducted off-book and AAR securities held by the clients were not held in their respective RGMP client accounts.

21. As compensation for facilitating the investments, AAR issued shares with a value of $50,000 to Lee in his wife's name, as well as options to purchase an additional 250,000 AAR shares. The options were never exercised and have since expired.

22. AAR did not make any filings with the Alberta Securities Commission ("ASC") in connection with the private placements. Although Lee was facilitating these investments to his clients who were all Alberta residents, Lee did not consider any requirements for filings with the ASC pursuant to the *Securities Act (Alberta)*.

23. In addition, also in September, 2011, Lee facilitated a short term loan in the amount of $100,000 from two of his clients, JH1 and JH2, to AAR. The clients, who were both in their eighties and had substantial liquid assets, were repaid in full within approximately one week.

24. Lee did not disclose to his firm that he was facilitating transactions for clients whereby they were investing in securities off-book and/or lending funds to AAR off-book.

Castle Rock Research Corporation ("Castle Rock")

25. In 2009, Lee facilitated an equity investment by three clients in Castle Rock Research Corporation ("Castle Rock"), an Alberta corporation engaged in the sale of textbooks and educational materials.

26. Two of Lee's clients, JH1 and JH2, invested $850,000 in Castle Rock, while another client, SM, invested $350,000. Both JH1/JH2, and SM, were high net worth clients with substantial liquid assets.

27. In addition, Lee personally invested approximately $1,000,000 in Castle Rock through his RRSP account held at RGMP.

28. Lee did not disclose his outside business activities with Castle Rock to his firm, and in particular that he was facilitating transactions for clients in Castle Rock securities off-book.

29. In February, 2012 Castle Rock filed a Notice of Intention to file a Proposal to its creditors under the *Bankruptcy and Insolvency Act,* and an Interim Receiver was appointed by Order of the Court of Queen's Bench of Alberta.

Borrowing from Client

30. During the last quarter of 2010, Lee borrowed $100,000 from a client, FG. The purpose of the loan was so that Lee could invest in a wine fund. FG was also an investor in AAR.

31. Lee has repaid $75,000 of the loan.

32. Lee did not disclose his personal financial dealings with FG to his firm.

Other Matters

33. In October, 2011, Lee's employment with RGMP ended. He is not currently employed with an IIROC Dealer Member firm, and has experienced significant financial difficulties since that time.

3. SUBMISSIONS OF IIROC

¶ 5 The foregoing Agreed Statement of Facts, Contraventions and Terms of Settlement were reviewed by Mr. McLellan, Senior Enforcement Counsel for IIROC.

¶ 6 Mr. McLellan ("Counsel") referred to pertinent parts of the Settlement Hearing Book including IIROC Dealer Member Rules 29.1 (Business Conduct"), 20.33(2) ("Penalties") and 20.36 ("Hearing Panel Powers"); and IIROC Rules of Practice and Procedure Rule 15 ("Settlement Hearings").

¶ 7 Counsel also referred to the IIROC Dealer Member Disciplinary Sanction Guidelines "General Principles" and emphasized the importance of the Guidelines entitled "1. Main Concerns When Determining an Appropriate Penalty"; "2. Disciplinary Sanctions as Deterrence", "3. Key Considerations When Determining Sanctions" (14 subheadings), "3.10 Outside Business Activities - Dealer Member Rule 29.1", and "2.5 Undisclosed Personal Business with a Client (includes borrowing from a client without firm knowledge or consent) - Dealer Member Rule 29.1".

¶ 8 With respect to AAR, and Castle Rock, Counsel discussed the main aspects of the Respondent's involvement in relation to each of the headings of the Dealer Member Disciplinary Sanction Guidelines, Section 3.10 "Outside Business Activities - Considerations in Addition to General Principles":

1. Magnitude (in size and value) of outside business activity.

2. Number of clients affected.

The Respondent facilitated, as contrasted with recommended, the investment by six clients in AAR, the total debt and equity investment being a very substantial total of $6 million. The clients were all high net worth individuals, most were experienced business owners and their stated investment knowledge was "good".

The Respondent also facilitated the investment by three clients in the Castle Rock equity investment.

All the investments were made without the knowledge of the member firm.

3. Magnitude of client losses.

AAR is apparently still operating, and the clients are still shareholders, but it is unclear as to whether the clients will suffer losses. Castle Rock is in Bankruptcy proceedings with an Interim Receiver appointed. It remains to be seen whether the investors will receive return of any portion of their investments.

4. Suitability of outside business activity if involving securities.

The situation is different than the usual in that the Respondent was facilitating, not recommending, the investments. The reasonably sophisticated investors undertook considerable due diligence on their own with respect to the AAR investment.

5. Compensation received by registrant.

Shares with a then value of $50,000 in AAR were issued in the Respondent's wife's name. Again, the value is unknown.

6. Any personal interest of registrant in outside business activity.

The Respondent indirectly received the benefit of the $50,000 worth of shares in AAR. He also received options for $250,000 worth of shares but the options have expired. He invested $1 million in Castle Rock shares.

7. Existence of client complaints.

It is notable, and somewhat surprising, that no client complaints were received.

8. Whether registrant had honest but mistaken belief that proper approval obtained.

The Respondent knew he was acting outside the rules.

9. Legality of outside activity.

The Respondent should have known that there were no filings with the Alberta Securities Commission regarding AAR.

¶ 9 Counsel referred to the "Recommended Sanctions" under the above Guideline 3.10 including "minimum fine of $10,000" and "period of suspension (in most egregious cases involving large value high risk off-book distributions)". He said that the penalties agreed upon are in keeping with the "recommended sanctions".

¶ 10 With respect to the loan of $100,000 from a client, of which $75,000 has been repaid, Counsel discussed the situation in terms of the "Considerations in Addition to General Principles" set out in Guideline 2.5 ("Undisclosed Personal Business with a Client" of the Disciplinary Sanction Guidelines. Counsel said that the considerations which apply in this case are that the Respondent was "aware of the prohibited nature of his activity", the client was reasonably sophisticated, and there is potential for a $25,000 loss which harms the client and represents a "profit" to the Respondent.

¶ 11 Counsel referred to the "Recommended Sanctions" with respect to "Undisclosed Personal Business" which include a minimum fine of $10,000.

¶ 12 Counsel discussed the following nine decisions as providing some guidance in determining the reasonable range of penalties (the decisions are discussed in the Reasons for Decision section, below):

Re Milewski, 1999 I.D.A.C.D. No. 17, July 28, 1999 (Ontario District Council)

Re Schiesser, 2001 IIROC 78, January 23, 2012 (Alberta District Council)

Re Taylor, 2005 I.D.A.C.D., No. 20, June 21, 2005 (Ontario District Council)

Re White, 2010 IIROC 25, June 2, 2010 (Ontario District Council)

Re Dass, 2009 IIROC 22, April 20, 2009 (Pacific District Council)

Re Kwok, 2010 IIROC 38, July 29, 2010 (Pacific District Council)

Re Gunderson, 2012 IIROC 66, November 13, 2012 (Alberta District Council)

Re Stefiuk, 2011 IIROC No. 24, April 26, 2011 (Alberta District Council)

Re Couture, 2009 IIROC 45, October 20, 2009 (Québec District Council)

¶ 13 Counsel closed by emphasizing the seriousness of the contraventions as evidenced by the magnitude of the transactions and the fact that the Respondent knew he was operating outside the rules. On the other hand there are many mitigating circumstances including that the Respondent has been in the industry since 1989, has no disciplinary record, is no longer in the industry, has suffered very significant financial difficulties, facilitated not recommended the investments, admitted everything that occurred and cooperated with the investigation, and the clients were very substantial net worth individuals who did not complain.

¶ 14 Counsel requested that the Panel accept the Settlement Agreement and the sanctions which fall within he asserted the reasonable range of sanctions.

4. SUBMISSIONS OF THE RESPONDENT

¶ 15 Mr. Lee spoke very briefly expressing regret for his conduct and for acting so unwisely.

5. REASONS FOR DECISION

¶ 16 In the Settlement Agreement the Respondent admits to the Contraventions of IIROC Rules, IDA By-

Laws, Regulations or Policies set out above. The Hearing Panel accepts that the Contraventions have been established.

¶ 17 Each of the Contraventions is stated as being contrary to Dealer Member Rule 29.1. That Rule is:

> **BUSINESS CONDUCT**
>
> 29.1 Dealer Members and each partner, Director, Officer, Supervisor, Registered Representative, Investment Representative and employee of a Dealer Member (i) shall observe high standards of ethics and conduct in the transaction of their business, (ii) shall not engage in any business conduct or practice which is unbecoming or detrimental to the public interest, and (iii) shall be of such character and business repute and have such experience and training as is consistent with the standards described in clauses (i) and (ii) or as may be prescribed by the Board.
>
> For the purposes of disciplinary proceedings pursuant to the Rules, each Dealer Member shall be responsible for all acts and omissions of each partner, Director, Officer, Supervisor, Registered Representative, Investment Representative and employee of a Dealer Member; and each of the foregoing individuals shall comply with all Rules required to be complied with by the Dealer Member.

¶ 18 The opening section of the **Disciplinary Sanction Guidelines** merits reference:

> **GENERAL PRINCIPLES**
>
> The following principles and rules are proposed to provide a framework for assessing the gravity of a particular breach of the Dealer Member Rules, and help to determine which sanction(s) is reasonable in the circumstances.
>
> **1. Main Concerns When Determining An Appropriate Penalty**
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> As set out in *Re Derivative Services Inc.,* [2000] I.D.A.C.D. No. 26, at page 3, a Hearing Panel's main concerns in determining an appropriate penalty are:
>
> 1. Protection of the investing public;
> 2. Protection of the Investment Industry Regulatory Organization's membership;
> 3. Protection of the integrity of the Investment Industry Regulatory Organization's process;
> 4. Protection of the integrity of the securities markets, and
> 5. Prevention of a repetition of conduct of the type under consideration.
>
> The penalty imposed in a specific proceeding should reflect the Hearing Panel's assessment of the measures necessary in the specific case to accomplish these goals, ranging from a reprimand to an absolute bar, and may take into account the seriousness of the respondent's conduct and specific and general deterrence.

¶ 19 As submitted by Counsel for IIROC, Guidelines 3.10 and 2.5 of the IIROC Dealer Member Disciplinary Sanction Guidelines specifically address the contraventions in this case. The opening portions of those Guidelines are:

> **3.10 Outside Business Activities - Dealer Member Rule 29.1**
>
> Standard C of the Standards of Conduct relates to professionalism and states among other things, that all methods of conducting business must be such as to merit public respect and confidence. Outside business activities that is not known or consented to by the Dealer Member firm, does not merit public confidence or respect. As explained in the related commentary to Standard C of the CPH handbook, "Dealings in securities outside of the normal business of the firm, sometimes referred to as selling away or outside deals may expose clients to unknown risks and expose

registrants and firms to civil liability. Such activity done without the knowledge of the firm also prevents effective supervision of the handling of client accounts, which is a requirement placed upon firms by the SROs. Firms may be exposed to liability for the actions of their employees in effecting such trades, even though the firm is unaware of the activities."

2.5 Undisclosed Personal Business with a Client (includes borrowing from a client without firm knowledge or consent) - Dealer Member Rule 29.1

As a professional, a registrant must use his specialized knowledge to protect his client. He must strive to put the interest of his client ahead of his own.

The relationship between the client and the registrant is one of principal and agent. The registrant is bound not only to carry out his client's instructions, but also has a duty to act in the client's best interest and is not permitted to allow personal interest to conflict with the interests of the client.

Personal business dealings with clients should be avoided as they create a potential for the registrant to place his interests above those of his client. When such dealings are not objectionable, such as in cases of a pre-existing relationship or a family relationship between the client and the registrant the consent of both the client and the registrant's firm should be sought and obtained.

(*The "Considerations in Addition to General Principles" and "Recommended Sanctions" for both of the above guidelines were extensively reviewed by Counsel for IIROC, above.*)

¶ 20 We agree with the rationale in the ***Milewski*** decision (above) about panels not altering the terms of a settlement agreement unless the penalty "clearly fall(s) outside a reasonable range of appropriateness".

¶ 21 We have reviewed all the cases relied upon by Counsel for IIROC (above) seven of which involved off-book transactions and one (***Gunderson***) which involved the respondent borrowing money from clients. In all cases the member firms had no knowledge of the activities of the respondents. The situations in the cases, as is usual, vary widely, with correspondingly divergent penalties. None of the cases involve the magnitude of the investments in this case but very few of them involved the extent of mitigating circumstances which exist in this case. The only case with more severe penalties than those proposed in the present case is ***Dass*** which involved a respondent who did not participate in the disciplinary process, frustrated the investigation of both the dealer member and IIROC, was involved in undisclosed personal business with a client and misappropriated clients' funds. The panel imposed a permanent bar from approval with IIROC, a fine of $220,000, and ordered payment of costs of $83,184.

¶ 22 In ***Gunderson*** the respondent borrowed money from clients, and reimbursed a client for losses, all without his member firm's knowledge or consent. The panel approved the Settlement Agreement which involved a fine of $25,000, a one month suspension, successful completion of the Conduct and Practices Handbook examination, and payment of costs in the amount of $3,000.

¶ 23 Applying the general principles of protection of the investing public, protection of the integrity of the IIROC process, protection of the integrity of the securities market, prevention of a repetition of conduct of the type under consideration, and general deterrence, leads us to the conclusion that the penalties agreed upon between IIROC and the Respondent in the Settlement Agreement fall within the reasonable range established in the decisions, are appropriate and should be accepted. The seriousness of the misconduct warrants very significant penalties but we have also taken into consideration the extensive mitigating circumstances. The six month suspension, with the Respondent already being out of the industry for some time, probably means that he will not be able to re-enter the industry. The suspension becomes tantamount to a lifetime prohibition.

¶ 24 The Hearing Panel advised, at the conclusion of the Hearing, that we accepted and we signed, the Settlement Agreement. We confirm that decision.

¶ 25 The Respondent, in the Settlement Agreement, agreed to the following terms of settlement, which we

have accepted as appropriate:

(a) pay a fine to IIROC of $75,000;

(b) be prohibited from registration in any capacity for a period of six months;

(c) pay costs to IIROC of $5,000.

¶ 26 We consider the amount of the costs to be within the reasonable range and although they will not fully cover IIROC's costs, they reflect the reduced involvement and cost for IIROC resulting from the Respondent's cooperation.

March 9, 2013

A1an V.M. Beattie, Chair

James H. Ross - Industry Representative

Donald Milligan - Industry Representative