

Re Golden Capital Securities Ltd

IN THE MATTER OF:

THE BY-LAWS OF THE INVESTMENT DEALERS ASSOCIATION OF CANADA

AND

GOLDEN CAPITAL SECURITIES LTD

2008 IIROC 1

Investment Dealers Association of Canada
Hearing Panel (Pacific District)

Heard: March 12, 2008 at Vancouver, BC.
Decision: April 19, 2008
(68 paras.)

Hearing Panel:

John Rogers, Chair, Brian Field and James Harkness

Appearances:

Lorne Herlin, Enforcement Counsel for the Investment Dealers Association of Canada; and
Roger D. McConchie and R. Alan McConchie, McConchie Law Corporation, Barristers & Solicitors, Counsel
for the Respondent, Golden Capital Securities Ltd.

REASONS FOR DECISION

1. Pursuant to Part 10 of By-law 20 of the by-laws of the Investment Dealers Association of Canada (“Association”) a Hearing Panel was convened to determine whether Golden Capital Securities Ltd. (the “Respondent”) contravened the by-laws of the Association as alleged by the enforcement division of the Association (“Association Staff”) in an Amended Notice of Hearing dated May 28, 2007 (“Amended Notice of Hearing”).

History

2. In accordance with the provisions of the Amended Notice of Hearing, a disciplinary hearing (“Disciplinary Hearing”) was held on October 24th, 25th, 26th, 29th and November 1st and 2nd, 2007. The Disciplinary Hearing was adjourned pending the Hearing Panel’s decision on the question of liability and the issuance of its reasons.
3. In its decision dated November 26, 2007 (“Decision”), the Hearing Panel found that the Respondent had breached the Association’s by-laws as alleged in the Amended Notice of Hearing by refusing Association Staff access to data copied from computer hard drives used by employees of the Respondent (the “Mirrored Records”), which Mirrored Records were in the possession of an independent third party retained by the Association.
4. The adjourned hearing reconvened on December 20, 2007. At this adjourned hearing the Respondent

advised that it was not prepared to proceed with submissions on the imposition of a penalty or the determination of costs.

5. Following consultation with the parties, the Hearing was further adjourned to March 12, 2008 for the Hearing Panel to receive such submissions from Association Staff and the Respondent.

Penalty and Costs

6. As a result of the finding in the Decision that the Respondent has breached the Association's by-laws, pursuant to the provisions of By-laws 20.34(1)(b) and 20.34(2) we hereby impose on the Respondent and order it to pay a fine of \$75,000 and assess and order the Respondent to pay Association Staff investigation and prosecution costs in the amount of 76,760.

Reasons

Penalty

7. By-law 20.34 authorizes a hearing panel to impose a penalty upon a Member where the hearing panel has determined that that Member has failed to comply with the provisions of an Association by-law.
8. The relevant portion of By-law 20.34 (1) provides that:

20.34 Members

(1) Upon conclusion of a disciplinary hearing, a Hearing Panel may impose the penalties set out at By-law 20.34(2) if, in the opinion of the Hearing Panel, the Member:

....

(b) failed to comply with the provisions of any By-law, Regulation, Ruling or Policy of the Association;

and the relevant portion of By-law 20.34 (2) provides that once a hearing panel has made such a finding, it may:

..... impose any one or more of the following penalties upon the Member:

(b) a fine not exceeding the greater of:

(i) \$5,000,000 per contravention; and

9. Association Staff submits that an appropriate penalty is a fine amounting to between \$75,000 and \$100,000. It is the Respondent's position that a monetary fine is inappropriate in the unique circumstances of this matter and that a reprimand is sufficient. However, the Respondent submits, if we find a fine to be an appropriate penalty, the fine sought by Association Staff is excessive and that only a modest fine should be imposed.

Fine or Reprimand

10. In *Re: Derivative Services Inc.* [1999] I.D.A.C.D. No. 29, the Ontario District Council confirmed that a refusal to comply with a request for information made by Association Staff during the course of an investigation is a serious matter. At p. 12, the District Council stated that:

The District Council views a refusal to comply with a request for information pursuant to an Association investigation as a serious matter. Membership in the Association and employment by a Member firm carry with them obligations to comply with the Association's By-laws, Regulations and other rules, including paragraph 19.5 of the By-laws which is a key element of the Association's investigation powers. Full co-operation with a request under it is necessary if the Association is to be able to fulfill its self regulatory supervisory functions with respect to its members and their approved persons. Failure to provide information requested in an investigation undermines the integrity of the self regulatory system and the effectiveness of its

operations.

11. In the Decision, the Hearing Panel found that the Respondent had refused to comply with a request for information similar in form to that dealt with by the Ontario District Council in *Re: Derivative Services Inc.* We agree with the observation of the Ontario District Council that a Member's refusal to comply with a request for information made by Association Staff is a serious matter. We therefore do not agree with the Respondent that a reprimand is a sufficient penalty for the breach of the Association's by-laws as set out in the Decision.
12. Similarly, in *Re: Union Securities Ltd.*, [2005] I.D.A.C.D. No. 51 the Ontario District Council stressed the seriousness of a refusal to comply with a request for information. It stated at paragraph 55:

A failure to cooperate, even if based upon a matter of principle, strikes at the very integrity of the Association's duty and ability to police itself. For that reason, the seriousness of the offence mitigates against a mere reprimand. The penalty must be a significant one.
13. We believe that a fine is an appropriate penalty in the matter at hand

Disciplinary Sanction Guidelines.

14. Guideline 5.1 of the Disciplinary Sanction Guidelines of the Association (January 2006) ("Disciplinary Guidelines") sets out the following six considerations in assessing a penalty following a finding, similar to that in the Decision, that a respondent has breached the provisions of By-law 19.6:

1. The Disciplinary History of the Respondent

15. This is not the first time the Respondent has been disciplined by securities regulatory authorities.
16. In a 1999 settlement with the Vancouver Stock Exchange, the Respondent admitted a breach of the rules of the Vancouver Stock Exchange, paid a fine of \$10,000, and was assessed \$1,000 in costs.
17. In a 2004 settlement agreement with the Association, the Respondent admitted to a failure to supervise an employee contrary to the Association's rules, agreed to pay a fine of \$20,000, and agreed to pay \$5,000 in costs.
18. In a 2007 settlement with Market Regulatory Services Inc., the Respondent admitted that it was deficient in a number of its order designation and audit trail requirements. It agreed to pay a fine of \$180,000 and to pay \$20,000 in costs.
19. The Respondent takes the position that this reference in Guideline 5.1 to the Respondent's disciplinary history pertains only to the Respondent's disciplinary history with respect to contraventions of By-law 19.6. The Respondent has not before been disciplined with respect to By-law 19.6.
20. We agree with the Respondent that reference to the disciplinary history of the Respondent in Guideline 5.1 is directed to the disciplinary history of the Respondent relevant to the breach of By-law 19.6 and that the Respondent has no history of previous disciplinary history with respect to By-law 19.6.
21. However, elsewhere in the Guidelines under the heading "Key Considerations When Determining Sanctions" it is observed in paragraph 3.5 that it "is also important for the Hearing Panel to consider past misconduct that, while unrelated to the misconduct at issue, nevertheless offers evidence of prior disregard for regulatory requirements, investor protection and market integrity". We would suggest that the Respondent's disciplinary history reflects if not a "poor disregard", at least a disinterest in the rules and regulations governing the investment industry.

2. The Intention of the Respondent

22. While not denying that its refusal to grant Association Staff access to the Mirrored Records was intentional, the Respondent submits that its intention was not to impede the investigation being

conducted by Association Staff.

23. The relevant consideration for us in this matter is not whether or not the Respondent intended to adversely affect the efforts of Association Staff. The relevant consideration is whether or not the Respondent intended not to comply with the request of Association Staff. There is no question that the Respondent intended its lack of cooperation.
24. Nevertheless, in the Decision, we addressed the agreement between Association Staff and the Respondent made in January 2007 (the "January Agreement") whereby Association Staff and the Respondent together with two employees of the Respondent negotiated a method through which the Respondent and the two employees granted Association Staff access to the Mirrored Records. Association Staff in accordance with the terms of the January Agreement carried out their obligations during a period from March 7, 2007 until April 3, 2007. During this time period, the two employees of the Respondent to the most part carried out their obligations under the January Agreement. The Respondent, on the other hand, carried out none of its obligations and without prior notice to Association Staff on April 18, 2007 effectively repudiated the January Agreement.
25. The repudiation of the January Agreement by the Respondent clearly impeded the investigation by Association Staff. The Respondent clearly intended the repudiation of this agreement. We therefore do not accept the Respondent's submission that it did not intend to impede the investigation being conducted by Association Staff.

3. Complete or Partial Non-Compliance

26. The Respondent argues that its actions did not constitute complete non-compliance with the request of Association Staff. It points out that:
- i. It consented to the creation of the Mirrored Records;
 - ii. Before and after the creation of the Mirrored Records, it produced in a timely manner copies of all records and information kept in hard copy form specifically requested by the Association; and
 - iii. There has not been a request made by Association Staff to produce any specific electronic records.
27. We agree that the Respondent produced copies of other records in a timely manner as and when request by Association Staff. However, the relevant question before us is the production of the Mirrored Records. The Respondent failed completely to produce any portion of the Mirrored Records as and when requested by Association Staff.

4. The Impact of Non-Compliance on the Investigation

28. There was clear evidence during the hearing that the effect of the Respondent's non-compliance with Association Staff's request for access to the Mirrored Records effectively shut down the investigation. In an effort to achieve prompt access to the Mirrored Records, Association Staff attempted to negotiate an agreed upon form of access rather than facing the potential delay in seeking an order from a hearing panel. The information on the Mirrored Records was sought by Association Staff for the purpose of identifying the beneficial parties behind certain trading accounts. Without this information the investigation could not proceed.
29. And, as importantly, the information sought by Association Staff may prove to be time sensitive. This means that the more time that elapses before securing access to the Mirrored Records, the less useful any information thereon might be found to be.
30. Therefore, the Respondent's refusal to grant access to the Mirrored Records had a very serious negative effect on the investigation while at the same time greatly increasing its costs.

5. Reliance on Competent Legal Advice

31. The Respondent submits that its refusal to grant Association Staff access to the Mirrored Records was based in good faith on the competent legal advice of its legal counsel. Such legal advice was to the effect that until it was assured that a proper protocol was in place to address the issues of relevance, privilege and third party privacy issues, the Respondent should not grant Association Staff access to the Mirrored Records.
32. In *Betmar(Re)* [2003] I.D.A.C. No.32 at paragraph 48, the Hearing Panel found that reliance upon competent legal advice was a mitigating factor in the determination of an appropriate penalty, stating:
- In determining these penalties ... [w]e have also taken into account that the Respondent was acting on the advice of counsel in not co-operating with the Association. We believe that this lack of co-operation was in good faith and was not done in an attempt to unduly impede the investigation of the Association.
33. We disagree with the Respondent that in the matter at hand the Respondent's reliance upon competent legal advice should be taken as a mitigating factor.
34. From November 2006 until at least the end of May 2007 the Respondent claimed to rely upon legal advice which differed from that given to Association Staff. This reliance succeeded in delaying Association Staff's access to the Mirrored Records. Indeed, to paraphrase the words of the Hearing Panel in *Betmar*, we believe that the Respondent's lack of cooperation acting on the advice of legal counsel *was* done in an attempt to unduly impede the investigation of the Association.
35. The evidence before us is that Association Staff provided Respondent's counsel with a copy of the decision of the Ontario District Council in *Re: Union Securities Ltd.* [2005] I.D.A.D. No. 51. Association Staff took the position that *Union Securities* clearly determined that Association Staff had the right to access the Mirrored Records. Respondent's counsel disagreed that *Union Securities* dealt with virtually the same facts and the same legal issues as claimed by counsel for Association Staff.
36. It is the submission of the Respondent that it was this clear disagreement between its counsel and counsel for Association Staff as to the effect of the finding of the Ontario District Council in *Union Securities* that lead to its refusal to grant Association Staff access to the Mirrored Records. For this reason, the Respondent submits, it should not be penalized.
37. In addition, the Respondent points out, there is no provision in the Association's by-laws or rules to deal with a disputed interpretation of the application of a particular provision. Without such a dispute resolution forum, the Respondent submits, it had no option but to deny Association Staff access to the Mirrored Records. The Respondent's position is that it should not be penalized for such a deficiency in the Association's by-laws.
38. We agree with the Respondent that it would certainly be beneficial if the Association by-laws and rules contained a mechanism whereby a Member or an Approved Person could seek a binding interpretation of a particular provision of the Association's by-laws, rules and regulations without facing a sanction if the Member's or Approved Person's interpretation was found to be incorrect. However, such a mechanism does not exist.
39. As the Ontario District Council observed in *Derivative Securities* at p. 10:
- A conscious intention to test the rules carried with it acceptance of a risk that penalties will follow if the respondent's position is not sustained
40. In the matter at hand, the Respondent claimed reliance upon a legal opinion to take a course of action over a number of months. This course of action we determined in the Decision to be in contravention of the by-laws of the Association. The Respondent's course of action unduly impeded the investigation by Association Staff. In taking this course of action, the Respondent had ample time to reflect upon the consequence of its actions. The Respondent must be taken to have accepted the risk that consequences would follow if its position were not sustained by us.

41. It is the Respondent's further position that a Member or Approved Person is entitled to resist Association Staff's request for information on the basis of a reliance upon legal advice with respect to issues of privilege and the privacy interests associated with third party documents. In making this submission, the Respondent relies upon *Tumer Salih Bahcheli (Re)* the September 12, 2007 decision of the Alberta District Council, where at p. 38 the Alberta District Council concluded that:
- ... in the circumstances of the unaddressed privacy and privilege issues, and the Respondent's efforts to satisfy the Association's demands, the Respondent should not be found guilty of failing to cooperate with the Association.
42. Based upon this finding of the Alberta District Council, the Respondent submits that its reliance upon legal advice dealing with the issues of privilege and the privacy interests associated with third party documents should be taken as a mitigating factor in the determination of an appropriate penalty.
43. We disagree with the Respondent that Tumer Salih Bacheli stands for the proposition espoused by the Respondent. Therefore, we don't find the Tumer Salih Bacheli decision of assistance to us in the matter at hand.
44. In summary, we do not find that reliance upon competent legal advice by the Respondent is a mitigating factor in determining an appropriate fine.

6. The Importance of the Information Sought

45. As was referred to above, without the information sought, the investigation by Association Staff was virtually shut down. The information sought was obviously very important to the investigation.

Actions of Association Staff

46. This matter commenced with a number of unsuccessful negotiations between the Respondent and Association Staff with a view to permitting Association Staff access to the Mirrored Records. These negotiations resulted in the investigation incurring delay and a great deal of extra costs. Although we have found that up until the end of May 2007 most of the responsibility for this delay and extra costs should be laid at the feet of the Respondent, during the period between May 2007 and the commencement of the Disciplinary Hearing in October 2007, Association Staff must share some of the blame for the delay and the extra costs incurred.

The June 14th Letter

47. In the first week of June, 2007, in a renewed attempt to allow Association Staff access to the Mirrored Records, Associated Staff entered into a new set of negotiations with the Respondent. As a result of this new initiative, Respondent's counsel forwarded to Association Staff a letter dated June 14, 2007 (the "June 14th Letter") setting out his understanding of what he believed to have been the agreement between the Respondent and Association Staff. The Respondent in its submissions at the Disciplinary Hearing claimed that it in good faith relied upon the terms of the June 14th Letter and believed that the terms of this letter constituted a fair method of permitting Association Staff access to the Mirrored Records.
48. In the Decision, we found that a binding agreement had not been made between the Respondent and Association Staff. However, there is no doubt from the evidence before us that the Respondent in good faith entered into these negotiations and believed that an agreement had been reached between it and Association Staff.

Claim of Conflict

49. During the course of this matter, the Vancouver office of the national law firm which serves as general counsel for the Association acted as counsel for the Respondent. Association Staff were aware of this fact and raised no objection. However, following the break down of negotiations following the June 14th Letter, Association Staff pressed the issue of the Respondent's then counsel continuing to act for the

Respondent claiming that there was a conflict of interest. This objection forced the Respondent to have to instruct new counsel causing the Respondent additional costs and further delaying the investigation and the entire hearing process.

50. It is acknowledged by Association Staff that the Respondent is blameless for this further delay.

Lack of Complete Disclosure

51. Rule 1.2 of the Rules of Practice and Procedure of the Association (the “Rules”) sets out that when it comes to the conduct of Association Staff in carrying out their role in disciplinary proceedings, the general principle to be followed in the interpretation and application of the Rules is as follows:

1.2 General Principle

These Rules shall be interpreted and applied to secure a fair hearing and a just determination in the interests of justice, with a view to securing such result in a timely and cost effective manner.

52. In the context of a disciplinary hearing, Association Staff assumes a role similar to that of the prosecutor in a criminal proceeding. With this role comes a number of responsibilities imposed upon Association Staff to satisfy the General Principle and to secure a fair hearing and a just determination. One of these responsibilities is a duty imposed upon Association Staff to disclose all information in its possession relevant to the disciplinary hearing.
53. In this matter, due to a claim of solicitor/client privilege by the national law firm which serves as general counsel for the Association, the Respondent was initially denied access to information it considered relevant to this hearing. To secure this information, the Respondent brought an application to stay the Disciplinary Hearing. The information sought was subsequently provided to the Respondent and it therefore elected not to proceed with its stay application.
54. As well, during the course of the Disciplinary Hearing, Association Staff brought forward a document which was relevant to the matter before us and which should have been disclosed to the Respondent prior to the commencement of the Disciplinary Hearing.

Amount of Fine

55. The Disciplinary Sanctions for a breach of By-law 19.6 recommends a minimum fine of \$50,000. The Respondent argues in favour of a modest fine and Association Staff recommends a fine of between \$50,000 and \$100,000.
56. The Respondent has submitted that the actions of Association Staff as enumerated above should be taken as mitigating factors and lead to a reduction of the penalty assessed. We disagree with the Respondent. The actions of Association Staff should certainly be taken into account in the assessment of costs against the Respondent, but in this instance we do not find the actions of Association Staff are a mitigating factor in the determination of a penalty.
57. In *Union Securities*, the Ontario District Council when dealing with issues similar to those dealt with in the Decision assessed a fine of \$50,000. To a certain extent, the Ontario District Council was breaking new ground with its decision. A copy of this decision was provided to the Respondent very early on in this matter. In the Decision, we found that the reasoning of the Ontario District Council in *Union Securities* applied to the matter at hand. To paraphrase the words of the Ontario District Council in *Derivative Securities* referred to above, it is clear that there was a conscious intention on the part of the Respondent to test the rules. With this test comes the concomitant acceptance of a risk by the Respondent that penalties will follow if its position is not sustained. Therefore, we believe that a fine in excess of the \$50,000 assessed in *Union Securities* is appropriate.
58. However, although the position taken by the Respondent markedly delayed the investigation for which the Mirrored Records was sought, through the cooperation of the Respondent, the data in the Mirrored Records has been preserved. This cooperation by the Respondent with Association Staff should be

recognized as a mitigating factor.

59. We have therefore determined that a fine of \$75,000 is an appropriate amount. This amount reflects the seriousness of the Respondent's actions in refusing to grant Association Staff access to the Mirrored Records. It also recognizes as a mitigating factor the Respondent's partial cooperation in creating the Mirrored Records and preserving the data.

Assessment of Costs

60. By-law 20.49 provides a hearing panel with the ability to assess Association Staff investigation and prosecution costs against a respondent found liable for failure to comply with any by-law, regulation, ruling or policy of the Association.
61. The relevant provisions of By-law 20.49 provide:
- 1) In addition to imposing any of the penalties set out in By-law 20.33, By-law 20.34 or By-law 20.45, the Hearing Panel may assess and order any Association Staff investigation and prosecution costs determined to be appropriate and reasonable in the circumstances.
62. It is to be noted that there is no provision in the Association by-laws permitting the awarding of costs against the Association. The authority of a hearing panel to award costs is restricted to awarding such costs only against a Member or Approved Person upon whom a fine has been imposed.
63. Association Staff has presented us with a Bill of Costs in support of their submission that we should award costs against the Respondent in the amount of \$95,950. The Bill of Costs provides details of some, but not all of the costs incurred by the Association in this matter. The details that were provided in the Bill of Costs suggest that the amount of the costs incurred by the Association greatly exceeds the amount of \$95,950 claimed by the Association.
64. This claim for a reduced amount by Association Staff is a noble gesture and, no doubt, very much appreciated by the Respondent. However, By-law 20.49 empowers a hearing panel, not Association Staff to assess and order the payment by a respondent of Association costs. For a hearing panel to properly make that determination, it should have before it as nearly as possible the actual costs incurred by the Association in a matter.
65. This, obviously, does not preclude Association Staff from making their recommendation as to what they believe is a proper assessment of costs. However, as the authority to determine the actual amount of costs assessed against a respondent rests with the hearing panel the recommendation of Association Staff although being an important element in the hearing panel's determination is not the sole element. Indeed, if in the opinion of the hearing panel it is the proper course of action, the hearing panel is free to choose to award costs in excess of those recommended by Association Staff. (see for example *McLellan (Re)* [2007] I.D.A.C.D. No. 14).
66. In the matter at hand, Association Staff has sought an order for costs against the Respondent in the amount of \$95,950. We see no reason to increase that amount. However, we do see a reason to reduce that amount. We listed above some of the actions of Association Staff which we believe prolonged this process and which lead to an increase in expenses incurred by both the Association and the Respondent.
67. We believe that the award of costs against the Respondent should be reduced to reflect this increase in expenses. We have no method of determining the actual amount of this increase, so we are left with the application of an arbitrary calculation. We believe that an appropriate reduction is 20%, reducing the amount of costs assessed against the Respondent by \$19,190 from the amount sought by Association Staff.
68. Therefore, pursuant to By-law 20.49, we have determined that the Respondent should contribute the amount of \$76,760 to Association Staff investigation and prosecution costs in this matter.

Dated at Vancouver, B.C. this 19th day of April 2008.

John Rogers, Chair
Brian Field
James Harkness

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