

Re Wong

IN THE MATTER OF:

**THE DEALER MEMBER RULES OF THE
INVESTMENT INDUSTRY REGULATORY ORGANIZATION OF CANADA**

AND

THE BY-LAWS OF THE INVESTMENT DEALERS ASSOCIATION OF CANADA

AND

HECTOR WONG

2010 IIROC 26

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

Hearing: April 21 and 22, 2010 in Toronto Ontario
Decision: June 16, 2010
(40 paras.)

Hearing Panel:

Paul M. Moore, Q.C, Chair
Hugh McNabney
Robert Guilday

Appearances:

Natalija Popovic, Counsel for IIROC Staff
Hector Wong, Respondent
Steven H. Goldman & Stephanie Mandin, Respondent's Counsel

DECISION AND REASONS ON THE MERITS

Purpose of Hearing

¶ 1 This was a hearing to determine whether the respondent, Hector Wong, a registrant and an employee of Hampton Securities Limited at the time, committed the following contravention alleged by IIROC:

In or about September to December, 2006, Wong, as an Officer (Trading, Resident) of a Member of IIROC, engaged in business conduct or practice which is unbecoming or detrimental to the public interest in that he misappropriated funds from his member firm employer by executing transactions in US treasury bills which had the net effect of generating profits in two of his personal accounts at the expense of the inventory account of his member firm employer, contrary to IIROC Rule 29.1.

Issues

¶ 2 The issues in this hearing were factual: namely, did the respondent

- (a) misappropriate funds from his member firm
- (b) by executing transactions in US treasury bills
- (c) which had the net effect of generating profits in two of his personal accounts
- (d) at the expense of the inventory account of his member firm?

Allegation

¶ 3 IIROC alleged that the respondent purchased, and entered the purchases in his accounts, several US treasury bills from his member firm's inventory account at prices that were below market. These prices were set out in trade tickets entered by him, were in Canadian dollars, and were approximately equivalent to what they would have been in Canadian dollars if the Canadian dollar had been trading at par with the US dollar at the time, and not at a discount from par, as was the case at the time. When the US treasury bills matured the respondent received the Canadian dollar equivalent of the US dollar proceeds from the maturity of the US treasury bills, converted into Canadian dollars at the current market value. As a consequence, the respondent's profit from his investments in US treasury bills was inflated by the mispricing of his purchases.

¶ 4 IIROC asserted that the respondent's conduct was deliberate, was deceptive of the firm, and resulted in the misappropriation of funds that would have accrued to the firm's inventory account but for the mispricing.

Respondent's position

¶ 5 The respondent asserted that each of his purchases of US treasury bills was part of a larger transaction which, according to firm practice, he put through the firm's inventory account, whereby he purchased a big amount of US treasuries of a particular maturity date from a customer of the firm and approximately simultaneously sold to another customer of the firm a slightly smaller amount of US treasuries with the same maturity. The purchase and sale prices were at a small spread from each other. The difference in amount between the amount of the US treasuries purchased from and sold to the customers, was documented as a purchase by the respondent from the firm's inventory account and the price of his purchase of the US treasury bills was set to transfer to him his profits from the price spread and currency exchange profit on his purchases from and sales to the customers.

¶ 6 The respondent asserted that the prices of his purchases were clearly set out in the trade tickets, for all who had access to the tickets to see, that he mislead no one, and that his pricing merely transferred to him what was his – namely, his profits from the larger transactions with customers.

¶ 7 Respondent's counsel argued that even if IIROC's allegation were true, the respondent did not have the necessary *mens rea* for his actions to constitute misappropriation.

Standards of evidence and proof

Standard of evidence

¶ 8 Because the respondent's ability to continue in the securities industry is potentially at stake in this matter, a finding against the respondent must be founded on clear and convincing proof based on cogent evidence.

¶ 9 We applied this standard in making our findings of fact in this matter.

Burden of proof

¶ 10 In deciding whether the allegation against the respondent has been proved, staff has the burden of proof.

¶ 11 The burden in this case is not the one applicable in criminal matters: it is not that the facts must give rise to a conclusion beyond a reasonable doubt.

¶ 12 In our case, the burden is that the facts must give rise to a conclusion against the respondent on a balance of probabilities.

¶ 13 We applied this standard in making our decision on the allegation.

Witnesses and evidence

¶ 14 We heard from one witness, Mr. Ed Varela, an investigator with IIROC. In addition, we heard from the respondent.

¶ 15 We examined several documents, including transcripts of the respondent's examination on December 17, 2007 and May 21, 2008, transcripts of Mr. Peter Deeb's (an officer of Hampton) examination on November 2, 2007, trade tickets, trading blotters, account statements and new client application forms.

¶ 16 We also considered the respondent's Response to the Notice of Hearing, a document entitled "Supplementary Witness Statement of Hector Wong", and written submissions of counsel.

¶ 17 Respondent's counsel stressed that IIROC did not call any witness from Hampton, and did not put in evidence documents that he implied he would have liked to see. We were asked to make adverse inferences from the failure of IIROC in this regard.

¶ 18 We did not do so. We were advised that IIROC had disclosed all relevant documentation in its possession. IIROC was under no obligation to the respondent to call witnesses for him or to undertake investigations or to seek documentation for his case. In our adversarial system, each party to the proceeding is free to present its own case as it sees best, subject to the rules of fairness and the system.

Review of the evidence

The trades

¶ 19 As set out in trade tickets and blotters, and summarized in the Notice of Hearing, during the relevant period the respondent bought and had redeemed at maturity 14 US treasury bills trades with a gross face amount of US\$1,480,000 for a total profit of Cdn\$210,088.84. This represented an annualized return on his investments of more than 300%, at a time when, as admitted by the respondent, US treasury bills were yielding approximately 3% to 5%.

Trade tickets

¶ 20 Each trade reflecting the purchase of US treasury bills by the respondent from the firm's inventory account was set out in a trade ticket signed by the respondent, and entered into the firm's system by him. It set out the price of the purchase in Canadian dollars, indicated that the purchase was from the firm's inventory account, and indicated Deeb as the respondent's representative for the trade.

¶ 21 There were no trade tickets showing purchases or sales by the respondent of US treasury bills from or to customers or others.

¶ 22 The respondent stated that he did not receive and there were no confirmations for his alleged purchases from and sales to customers of the firm of the larger transaction in US treasury bills.

Trade blotters and account statements

¶ 23 The respondent's account statements showed the purchases and redemptions of the US treasury bills he purchased from the firm's inventory account. They did not reflect any sales by him to or purchases by him from customers of US treasury bills that he alleged were put through the firm's inventory account.

¶ 24 We did see blotter entries and trade tickets for one series of a purchase and a sale by and from the firm's inventory account with customers where the face amount of the treasuries purchased equaled the face amount sold plus the face amount of a smaller purchase of the treasuries by the respondent from the inventory account. All of these purchases and sales were shown as being with the inventory account. The registered representative on the transactions with the customers was not the respondent's representative, Deeb, but HC (a house account). There was no currency exchange on the series of trades on the blotter. The respondent was not able to show us similar series of trades for the other 13 transactions in question. The respondent agreed that his trades were an exception to how other client trades were booked.

¶ 25 Although the respondent claimed that he was the counterparty to the purchase from and the sale to the customers, he adduced no evidence to support this in the form of his banking records, account records, or other documents or to raise reasonable doubt to counter the evidential record establishing the contrary.

¶ 26 There was no evidence that Hampton and the respondent had agreed that the respondent could purchase and sell for his own account US treasury bills or other securities and put the transactions through the firm's inventory account, and not his own accounts.

¶ 27 Indeed, as a term of his employment, and pursuant to Hampton's compliance manual, the respondent testified, he was required to open personal accounts with Hampton. He admitted that one purpose of this was to enable Hampton to monitor his personal trading activity.

The respondent's role and capacities

¶ 28 The respondent was a registrant and was qualified, and his duties at Hampton included the role, to do order entry, trade reconciliation, trade control, deal with settlement and clearing issues, trading support for the private client group, new issues syndication and receiving and executing retail trade orders. He was not a registered representative with authority to trade for customers.

Hampton's surveillance

¶ 29 Deeb was aware that the respondent purchased US treasury bills from time to time, but believed the respondent was making only small profits, eg. \$150, here and there. The respondent did not inform Deeb of the true state of affairs and let his mispricing fly under the firm's radar.

¶ 30 Deeb was shocked and upset when he realized that the respondent had mispriced the respondent's purchases of US treasury bills from the firm's inventory account.

¶ 31 Deeb demanded and received from the respondent restitution for approximately \$1 million that in Deeb's view the respondent had misappropriated through the purchase of the US treasury bills that are the subject matter of this proceeding and other transactions that Deeb stated the respondent told him had occurred. This suggested to us that the respondent considered that he had been found out and that he made the payments to make his problems go away. The payment of such a sum of money in these circumstances is not the typical reaction of a person with a colour of right to disputed property.

Analysis and additional findings of fact

Misappropriation

¶ 32 Misappropriation is the taking or using without consent, or colour of right, funds or other property belonging to another, and often involves deception or other inappropriate behaviour. Wikipedia defines "misappropriation" as follows: "In law, misappropriation is the intentional, illegal use of the property or funds of another person for one's own use or other unauthorized purpose."

¶ 33 The respondent had no right to the price spread between US treasury bills purchased from customers in the firm's inventory account and sold to customers from the account. There was no documentation or evidence to suggest this other than the respondent's bold assertion that he was the purchaser and seller transacting with the customers. Indeed, no trade tickets, trading blotters or trade confirmations were produced to support this, and the respondent admitted that there were no such confirmations. The respondent was not a party to any such purchases or sales. The beneficial owner of the firm's inventory account, as admitted by the respondent, was Hampton.

¶ 34 The pricing of the US treasury bills purchased by the respondent was well below market at the time and without any reasonable justification. The prices were set by the respondent, without the actual knowledge or informed consent of Hampton. Even if Hampton were less diligent than appropriate in supervising the respondent's behaviour and reviewing his records to safeguard its own interests (which we do not determine one way or the other) that would not be a justification for the respondent's behaviour.

Restitution

¶ 35 The respondent stated that he made payments to reimburse Hampton because he does not like confrontation and felt physically threatened by Deeb when Deeb demanded reimbursement. And yet Deeb and the respondent subsequently attended at the respondent's bank to transfer some funds for reimbursement and the respondent subsequently borrowed funds from his sister to fund some additional reimbursement payments to Hampton. We did not believe the respondent's explanation of why he paid reimbursement funds to Hampton.

Mispricing

¶ 36 It is not clear how the respondent determined the price he set for his purchases of US treasury bills from the firm's inventory account. Staff believed he deliberately used prices in Canadian dollars approximately equal to prices that would have been appropriate (if the US and Canadian dollars had been at par) to reflect a market-based discount to maturity. The respondent stated that he used a price to capture the price spread on larger purchases and sales by him with customers through the inventory account.

¶ 37 It is not necessary for us to decide the basis on which the respondent set the prices. It is only necessary for us to determine that the prices were inappropriately low, were set deliberately by the respondent, and were set to effect a transfer of funds from the firm's inventory account to the respondent's account. This we did determine.

Mens rea

¶ 38 The allegation against the respondent is that he engaged in improper business conduct or practice and not that he committed a criminal offence. The doctrine of *mens rea* does not apply to contraventions of IIROC Rule 29.1. Nevertheless, the respondent's actions were intentional, deliberate, and intended to transfer to his account funds that did not belong to him. He knew what he was doing and the consequences of his actions.

Conclusion

¶ 39 We concluded that the respondent engaged in business conduct or practice which is unbecoming or detrimental to the public interest in that he misappropriated funds from his member firm employer by executing transactions in US treasury bills which had the net effect of generating profits in two of his personal accounts at the expense of the inventory account of his member firm employer, contrary to IIROC Rule 29.1.

Penalty Hearing

¶ 40 The National Hearing Co-ordinator will arrange for a penalty hearing for this matter.

Dated at Toronto this 16th day of June, 2010.

Paul M. Moore, Q.C.

Hugh McNabney

Robert Guilday

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