Re Pope

IN THE MATTER OF:

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

and

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

and

Julian Pope

2011 IIROC 68

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

Hearing: October 27, 2011
Oral Decision: November 2, 2011
Decision: December 19, 2011
Supplement to Decision: February 13, 2012
(28 paras.)

Hearing Panel:
Julia Dublin (Chair), Terry Bourne, David Kerr
Appearances:
Andrew P. Werbowski, Counsel for IIROC
Jeffrey Larry, Counsel for the Respondent

PENALTY DECISION

INTRODUCTION

Agreed Contraventions

¶ 1 By Notice of Hearing, dated, the following Allegations were made against Julian Pope ("the Respondent"):

(a) Between April 4 and 7, 2008, inclusive, the Respondent participated in a bond offering through a client, thereby failing to give priority to other client orders from the same bond offering, contrary to IDA [now IIROC] By-law 29.3A.

(b) Between April 4 and 7, 2008, inclusive, the Respondent failed to act fairly, honestly, and in good faith when executing and administering trades in the Domestic Debt Market by taking unfair advantage of non-public information whereby the client agreed to purchase bonds of the upcoming offering in the Respondent's behalf, contrary to IDA [now IIROC] Policy 5, Sections [sic] 4.1.

¶ 2 On May 2011 the Respondent and IIROC Staff executed an Agreed Statement of Facts that included an agreement as to a reformulated version of the IIROC rules contraventions as follows:

(a) On April 4, 2008 the Respondent participated in a bond offering by purchasing bonds into his firm's inventory account through a client, thereby failing to give priority to other client orders for the same bond offering, contrary to IDA By-law 29.3A.

(b) On April 4, 2008 and in connection with the bond offering, the Respondent failed to act fairly, honestly and in good faith when executing and administering the trades in the Domestic Debt Market by entering into an arrangement with a client whereby the client agreed to purchase bonds of the upcoming offering on behalf of the respondent's inventory account, contrary to IDA Policy 4.1.

¶ 3 The parties were unable to agree on appropriate sanctions and therefore a hearing was convened on October 27, 2011 to hear evidence and submissions of the parties relevant to the penalty to be imposed on Respondent pursuant to the Agreed Statement of Facts.

¶ 4 The Hearing Panel heard the representations of counsel and testimony of witnesses called by both parties and the testimony of the Respondent.

Press Release

¶ 5 As a preliminary matter, the Respondent's counsel pointed to statements in the initial IIROC press release regarding the penalty hearing and subsequent corrected versions as remaining inconsistent with the Agreed Statement of Facts and asked us to order IIROC to issue a new version. As a Hearing Panel we do not have the authority to do this. However we can confirm for the record that, IIROC press release statements to the contrary, the Respondent did not agree (1) that "he took advantage of non-public information about an upcoming issue" and (2) that the bond purchase was "on his behalf".

THE LAW

Applicable Principles

¶ 6 Counsel for both parties acknowledged that there is no precedent IIROC hearing panel decision addressing an appropriate penalty for the infractions at issue here. IIROC counsel directed us to IIROC staff's own guidelines for determining the gravity of IIROC rules infractions and to the Supreme Court's guidance on sanctions in *Re Cartaway Resources Corp*. [2004] 1 SCR 97 2. We were directed by both counsel to MFDA and IIROC penalty decisions involving variously: failure to provide best execution for equity trades, equity trading on undisclosed material information and personal deals with retail clients. No precedents cited involved institutional clients in the primary bond markets.

¶ 7 In our view the Panel's role was to decide the penalty for specific breaches of IIROC rules described in the Agreed Statement of Facts (ASF), provide for general deterrence, and articulate or clarify an industry standard of conduct in new bond offerings. We focused primarily on the particular facts before us and provided a balanced penalty as set out in *Re Mills*, [2001] I. D.A.C.D. No.7, April 17, 2001 at p 3:

> "Industry expectations and understandings are particularly relevant to general deterrence. If a penalty is less than industry understandings would lead its Members to expect for the conduct under consideration, it may undermine the goals of the Association's disciplinary process; similarly, excessive penalties may reduce respect for the process and concomitantly diminish its deterrent effect. Thus the responsibility of the District Council in a penalty hearing is to determine a penalty appropriate to the conduct and respondent before it, reflecting that its primary purpose is prevention rather than punishment."

¶ 8 We acknowledge there is little guidance on individual penalties for domestic debt market violations. For purposes of regulation of industry practices and deterrence of improper conduct we find there are five main considerations: position in the capital markets; duties as an officer of a member firm; industry experience; level of planning and organisation involved in the infraction; and degree of subterfuge demonstrated.

¶ 9 We accept the Agreed Statement of Facts as supplemented by the evidence given at the hearing. The

need for general deterrence applies to the domestic bond markets as much as the equity markets, especially because of the general lack of transparency in these largely OTC markets.

The Nature of the Infractions

¶ 10 The Respondent was the head corporate bond trader for HSBC Securities (Canada) Inc. ("HSBC"), part of major financial conglomerate of related and affiliated entities, and was a bond market-maker for bonds for those entities. By acquiring newly issued bonds through a firm pre-arranged deal with an institutional client of HSBC, Fiera YMG, the Respondent did indirectly what he knew he was not allowed to do directly. He covered a short position in bonds issued by HSBC Financial Corporation Limited ("HFC"), a company related to his employer, from a new offering of those bonds by HFC that he expected to be oversubscribed. The offer was in fact oversubscribed by HSBC clients. The Trade Blotter shows that a number of HSBC clients did not receive their full orders. Fiera YMG acquired a $21M fill, flipping $15M back to the Respondent at the prearranged price. This allowed him to cover his short position at below the market price.

¶ 11 Counsel for the Respondent and the Respondent himself in testimony urged on us that similar "riding" or "flipping" practices in new bond offerings had been common in the debt markets in 2008, that the HSBC clients who did not have their orders filled were all sophisticated institutions and that we should not break new regulatory ground in a gray area by making an example of the Respondent.

¶ 12 Mr. Sylvain Perreault, the Chief Operating and Compliance Officer at the Respondent's current employer, Desjardins Securities Inc, was called by the Respondent as a witness, and answered questions from the panel. He confirmed that it was common practice at the time of the infractions for some institutional traders ("riders") to acquire excess bonds in a popular offering with a view to flipping the excess to receptive purchasers at a profit, but that it was not then or now common for the purchasers to recruit riders and enter into firm repurchase arrangements with them in advance, as the Respondent did.

¶ 13 By acquiring bonds through a firm pre-arranged deal with Fiera YMG, the Respondent went beyond the industry practices described by his witness. This was not the fortuitous acquisition of bonds from a known "rider". The evidence shows the respondent approached a receptive client, solicited the trade and planned it over three days. The recorded conversations in our view indicate conscious subterfuge on his part.

¶ 14 In our view the Respondent cannot claim he did not benefit personally in any way from this transaction. His success in filling his short positions would be expected to ultimately affect his success in his proprietary trading portfolio and thus his total remuneration.

The Significance of the Infractions

¶ 15 We consider the Respondent's contravention to be serious because of its devious nature and his senior position in the industry. We note that the Supreme Court of Canada in *Re Cartaway* approved the principle that general deterrence and public confidence require that heavier penalties should attach to individuals with a leadership role in the capital markets who are the driving force behind deceitful conduct than would apply to the same conduct by less influential participants.

¶ 16 Mr. Perreault informed us that guidance as to applicable rules and industry standards was sketchy in the domestic bond markets at the time of the Respondent's infractions and some participants were pressing the limits or even knowingly flouting the rules. This is consistent with the IIROC Consolidated Compliance Report dated October 22, 2010 in the parties' Joint Book of Documents, which reminded firms at p. 8 of their basic obligations in the primary debt market and noted in effect that some firms did not have an adequate supervisory handle on the primary debt trading activities of their employees.

¶ 17 The Respondent testified that he was not aware of the IIROC rules governing the trade he made with Fiera YMG. This is not acceptable. The Respondent was an officer of a sophisticated registrant and had a concomitant duty as a fiduciary to the company and to its clients. As a registrant and market participant he had an obligation to understand and adhere to the rules and to set an example of self-governance to others. Faced with any ambiguity in what the rules required, it was his responsibility to take the high road rather than to push the envelope.

¶ 18 As soon as the Respondent became aware he was short HFC bonds he should also have been mindful of HSBC's conflict on any new offering. It was reasonable under the economic conditions in 2008 to expect the offering to be oversubscribed by institutional investors. Further, beyond the common sense precautions appropriate for a fiduciary and the specific IIROC restrictions, the Respondent signed a standard form Confidential Information Agreement as a result of being "over the wall" on the offering that prohibited him from buying or procuring others to buy the offering until the information became public. This should have alerted him that there were problems with his arrangements, particularly as they were finalised before the bond information became public.

¶ 19 We expect exemplary conduct from an individual who occupies and benefits from a special position of trust and influence in the marketplace, particularly in a relatively small, specialized community.

PENALTIES

¶ 20 In respect of the admission by the Respondent that on April 4, 2008 he participated in a bond offering by purchasing bonds into his firm's inventory account, through a client, thereby failing to give priority to other client orders for the same bond offering, contrary to IDA By-law 29.3A [now IIROC Rule 29.3A], a fine of $25 000.

¶ 21 In respect of the admission by the Respondent that on April 4, 2008 and in connection with bond offering he failed to act fairly, honestly and in good faith when executing and administering trades in the Domestic Debt Market by entering into an arrangement with a client whereby the client agreed to purchase bonds of the upcoming offering on behalf of the Respondent's inventory account, contrary to IDA Policy 5, section 4.1 [now IIROC Rule 2800], a fine of $25,000.

¶ 22 We considered the Respondent's argument that there was only one rules violation, warranting a lesser penalty. We accept that to characterise the same set of facts as both a specific violation and, solely because it breaches a rule, as a public interest violation and in consequence to impose separate penalties could be duplicative. However here we find there is no such duplication here, as there are conceptually separate violations. We find that a total penalty of $50,000 should be allocated half to the Respondent's breach of his prescribed duty to specific HSBC clients, and half to the breach of his duty as senior market participant to support fair practices and to lead by example.

¶ 23 The Respondent's counsel suggested a minimal total fine on the basis that the Respondent had already suffered job loss and public embarrassment. We note however that he found new employment within three months of leaving HSBC and has resumed his career as valued trading officer of Desjardins Securities Inc. We consider the total amount of the fine to be appropriate.

¶ 24 Consistent with our view as to the seriousness of the Respondent's dereliction of duty, we accept IIROC staff's recommendation that Mr. Pope will repeat and successfully complete the Conduct & Practices Handbook Course (CPH) and the Trader Training Course (TTC) by January 31, 2011.

¶ 25 The Respondent has spent over 38 months under close supervision at his current employer without incident. We do not propose to impose this restriction as requested by IIROC staff. We do not think its continuance would serve any useful purpose for general deterrence, specific deterrence or as an additional individual penalty.

COSTS

¶ 26 IIROC staff did not make any submissions as to costs. Accordingly, each party will be responsible for their own costs.

DATED the 19th day of December, 2011.

Julia Dublin, Chair

Terry Bourne, Member

David Kerr, Member

SUPPLEMENT TO PENALTY DECISION

INTRODUCTION

¶ 27 By a joint submission letter dated January 30, 2012, IIROC staff and the Respondent submitted that

a. due to various administrative misunderstandings, the Respondent did not receive formal notice of the requirement to repeat and successfully complete the Conduct & Practices Handbook Course (CPH) and the Trader Training Course (TTC) by January 31, 2012 in time to reasonably meet the prescribed deadline; and

b. costs of $15,000 should be awarded to IIROC.

SUPPLEMENTARY DECISION

¶ 28 After considering the parties' joint submission we have decided that

a. Mr. Pope must repeat and successfully complete the Conduct & Practices Handbook Course (CPH) and the Trader Training Course (TTC) by April 20, 2012; and

b. Costs of $15,000 shall be awarded to IIROC.

DATED the 13th day of February, 2012.

Julia Dublin, Chair

Terry Bourne, Member

David Kerr, Member