Mutual Fund Dealers Association of Canada
Association canadienne des courtiers de fonds mutuels

IN THE MATTER OF A DISCIPLINARY HEARING
PURSUANT TO SECTIONS 20 AND 24 OF BY-LAW NO. 1 OF
THE MUTUAL FUND DEALERS ASSOCIATION OF CANADA

Re: Zhengwen (Katherine) Qi and Xiaodan (Bonnie) Huang

Heard: May 29, 2013 in Toronto, Ontario
Decision and Reasons: July 8, 2013

DECISION AND REASONS
(Misconduct)

Hearing Panel of the Central Regional Council:

Frederick H. Webber	Chair
Guenther Kleberg	Industry Representative
Robert C. White	Industry Representative

Appearances:

H. C. Clement Wai	)))	Counsel, Mutual Fund Dealers Association of Canada ("MFDA")
Zhengwen (Katherine) Qi	)	In person
	)	
Xiaodan (Bonnie) Huang	)	In person

Allegations

1. A disciplinary hearing in this matter took place on May 29, 2013, pursuant to a Notice of Hearing issued by the MFDA and dated December 19, 2012 ("NOH"). In the NOH, the MFDA alleged the following violations of the By-laws, Rules or Policies of the MFDA:

> **Allegation #1**: In January 2009, the Respondents engaged in securities related business that was not carried on for the account of the Member and through the facilities of the Member by recommending, referring, selling or facilitating the sale of securities to client CPL outside the Member, contrary to MFDA Rules 1.1.1(a) and 2.1.1.
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> **Allegation #2**: In August 2010, the Respondents failed to inform the Member of a complaint by client CPL and a civil proceeding commenced against them by client CPL and thereafter entered into a settlement agreement with and paid monies to client CPL without advising or obtaining the prior written consent of the Member, contrary to sections 4.1(b) (iii) and (v) and 4.1(e) of MFDA Policy No. 6 and section 10 of MFDA Policy No. 3.

At the outset of the hearing MFDA counsel advised the Panel that he was not relying on a breach of section 4.1(b) (v).

Appearances

2. At the commencement of the hearing, the Panel urged the Respondents to obtain legal counsel and an interpreter if they felt uncomfortable with a hearing in the English language. The same recommendation had been made by the Panel at the first appearance in this matter on February 13, 2013. Notwithstanding such recommendations, the Respondents chose to participate in the hearing unrepresented by legal counsel and without any interpreter.

Background

3. Qi was registered in Ontario as a mutual fund sales person with Investia Financial Services Inc. (Investia) from June 28, 2008 to October 22, 2010, but is not currently registered in the industry.

4. Huang was registered in Ontario as a mutual fund sales person with Investia from February 25, 2008 to October 20, 2010, but is not currently registered in the industry.

5. Weizhen Tang ("Tang") purported to operate an investment fund called the Oversea Chinese Fund Limited Partnership (the "Oversea Chinese Fund") which promised investors weekly returns of 1%. Tang specifically targeted members of the Chinese-American and Chinese-Canadian communities as prospective investors in the fund. It is the securities of the Oversea Chinese Fund that are the subject matter of the first allegation; and it is claims made by CPL, a client of the Respondents, arising out of losses she suffered in such securities that are the subject matter of the second allegation.

6. In February 2009, Tang admitted to investors at a meeting he had convened that he had been using the monies obtained from new investors to return principal and make fictitious payments of profits or returns to existing investors since at least 2006. Tang stated that he posted the fictitious profits on investors' account statements for the purpose of concealing the substantial trading losses he had incurred and to continue to attract new investors to the Oversea Chinese Fund.

7. On March 17, 2009, the Ontario Securities Commission ("OSC") issued a Temporary Cease Trade Order against Tang, the Oversea Chinese Fund, Weizhen Tang and Associates Inc., and Weizhen Tang Corp. (two companies owned or controlled by Tang). The OSC alleged, among other things, that Tang had collected as much as $30 million from more than 100 investors in Canada and the U.S. and had used money from new investors to pay out early investors. The OSC also charged Tang under the *Securities Act* (Ontario) with 12 offences relating to securities fraud and related offences.

8. The OSC has extended the Temporary Cease Trade Order multiple times since it was first made.

9. On April 3, 2009, the Securities and Exchange Commission filed an emergency action in the United States District of Texas to halt an on-going multi-million dollar Ponzi scheme and affinity fraud involving investments in the Oversea Chinese Fund.

<u>Allegation #1 – Securities Related Business Outside the Member</u>

10. CPL was a client of Investia. Qi was the mutual fund salesperson responsible for servicing her account.

11. Huang, in addition to being a mutual fund salesperson, was also licensed to sell insurance and did so through her managing general agency, Trinity Financial Services Inc. ("Trinity").

12. CPL dealt with Qi and Huang regarding her investing and insurance needs.

13. In or around January 2009, CPL met with Qi and Huang regarding an investment by her in the Oversea Chinese Fund. Client CPL already knew or, if not, learned at this meeting, that Qi and Huang were each investors in the Oversea Chinese Fund. According to Qi and Huang, CPL was already aware of the Oversea Chinese Fund and had asked Qi and Huang for their advice and assistance regarding an investment by CPL in the Oversea Chinese Fund. In a Statement of Claim referred to below, CPL alleged that Qi and Huang approached CPL about investing in the Oversea Chinese Fund. However, the Respondents testified that they did not introduce the Oversea Chinese Fund to CPL, but stated that they discussed it with her and advised her that it was a highly risky investment. Regardless, the Oversea Chinese Fund was not an investment product approved by Investia for sale by its Approved Persons.

14. On January 19, 2009, Qi and Huang escorted CPL to a bank where she obtained a bank draft in the amount of $40,000 payable to the Oversea Chinese Fund for the purpose of making an investment in the Oversea Chinese Fund. CPL told the Respondents she was working and therefore was too busy to deliver the bank draft to the head office of the Chinese Oversea Fund and asked the Respondents to deliver it for her. They agreed and CPL gave the bank draft to the Respondents who dropped it off at the head office of the Oversea Chinese Fund and arranged CPL's investment. There was evidence that a separate account was not opened for CPL, but rather that the Respondents invested $20,000 in each of their accounts in Chinese Oversea Fund on CPL's behalf. However the Respondents' unequivocal testimony at the hearing was that a separate account in the Chinese Oversea Fund was opened in CPL's name and that they were given a user identification and password for CPL so she could access her account on-line. Regardless, CPL's investment in the Oversea Chinese Fund was not processed for the account or through the facilities of Investia.

15. It was very shortly thereafter in February 2009 that Tang revealed that the Oversea Chinese Fund had, in effect, been operating as a Ponzi scheme and, on March 17, 2009, the OSC issued a Temporary Cease Trade Order against the Oversea Chinese Fund, Tang and others.

16. In order to succeed on this allegation, the MFDA must establish:

(a) that the Respondents engaged in a securities related business;
(b) that was not carried on for the account of the Member (Investia) and through the facilities of the Member;
(c) by recommending, referring, selling or facilitating;
(d) the sale of securities to CPL, outside the Member;
(e) contrary to MFDA Rules 1.1.1(a) and 2.1.1.

17. Rule 1.1.1(a) provides in part that "no Approved Person…shall, directly or indirectly, engage in any securities related business…except for the account of the Member, through the facilities of the Member and in accordance with the By-laws and Rules…"

Securities Related Business

18. "Securities Related Business" is defined in MFDA By-law No. 1 as "any business or activity (whether or not carried on for gain) engaged in, directly or indirectly, which constitutes trading or advising in securities for the purposes of applicable securities legislation in any jurisdiction in Canada, including for greater certainty, securities sold pursuant to exemptions under applicable securities legislation."

19. It is clear to the Panel that the actions of the Respondents in relation to their client CPL investing in the Oversea Chinese Fund, was a "securities related business" as defined. While their actions may not have been a "business", they certainly were an "activity". The fact that they earned no money as a result of their actions is irrelevant under the definition. The Respondents' actions may not have been "trading", but they admitted to "advising" CPL in relation to the Oversea Chinese Fund. Lastly, it is uncontroverted, and in the view of the Panel accurate, that the investment in the Oversea Chinese Fund was a "security".

Account of and Facilities of the Member

20. It is clear from the evidence that the actions of the Respondents regarding CPL's investment in the Oversea Chinese Fund were not carried on for the account of the Member (Investia) or through the facilities of the Member. In addition, the Investia Policies and Procedures Manual ("PPM") makes it very clear that representatives can sell only products which are on the Investia Approved Products List. If a representative wishes to offer a product for sale which has not been approved by Investia, they must submit product details on a prescribed form and receive product approval from Investia's Compliance Department. Selling a product that has not been approved for sale can result in disciplinary action and may affect the representative's ongoing registration. The Oversea Chinese Fund was never a product approved for sale by Investia and the Respondents never attempted to have it approved by Investia for sale.

Recommending, Referring, Selling or Facilitating

21. The Statement of Claim of the client, CPL, alleged that the Respondents brought the investment opportunity in the Oversea Chinese Fund to CPL. This was denied by the Respondents who stated that CPL already knew about the Oversea Chinese Fund and made the investment decision on her own. In the end MFDA counsel did not rely on the words, "recommending", "referring" or "selling", but based this part of his case on the allegation that the Respondents "facilitated" CPL's investment in the Oversea Chinese Fund. He admitted that the mere physical transport of the bank draft to the head office of the Oversea Chinese Fund by the Respondents would not, in itself, constitute "facilitating" the investment by CPL. However, MFDA counsel pointed out to the Panel that the Respondents also discussed the nature of, and advised CPL regarding the risk of, investing in the Oversea Chinese Fund. According to their testimony, the Respondents also passed on to CPL her user name and password so that she could access her account in the Oversea Chinese Fund. The Panel agrees with MFDA counsel that these actions constitute "facilitating" CPL's investment in the Oversea Chinese Fund.

Sale of Securities Outside the Member

22. The Respondents acknowledged in their testimony that CPL received her own account in the Oversea Chinese Fund in exchange for her investment of $40,000. There was clearly a sale of

securities of the Oversea Chinese Fund to CPL. In addition, as stated in paragraph 16(b), this sale was outside the Member.

Contrary to Rules 1.1.1(a) and 2.1.1

23. As outlined in paragraph 16 above, the Panel has concluded that the MFDA has proven all of the elements of Rule 1.1.1(a).

24. Rule 2.1.1 provides that each Approved Person shall:

- Deal fairly, honestly and in good faith with its clients;
- Observe high standards of ethics and conduct in the transaction of its business;
- Not engage in any business conduct or practice which is unbecoming or detrimental to the public interest; and
- Be of such character and business repute and have such experience and training as is consistent with the standards described in this Rule 2.1.1 or as may be prescribed by the MFDA.

25. As stated in the MFDA submission, Rule 2.1.1 encompasses the most fundamental obligations of all registrants in the securities industry and is designed to protect the public interest. The Respondents knew or ought to have known that the Oversea Chinese Fund was not approved for sale by Investia. This was not merely a technical failure to comply with the Investia PPM. In order to provide protection to the investing public, Members must provide due diligence on all potential products before approving them for sale, and it is therefore only products which have been so approved which may be sold by Approved Persons. Even if the possibility of investing in the Oversea Chinese Fund was initiated by the client, CPL, and not by the Respondents, they should have immediately told CPL that the Oversea Chinese Fund was not approved for sale by Investia and that they could not discuss it or do anything to facilitate its sale. By failing to do so, it is the Panel's decision that the Respondents failed to live up to the standards expressed in Rule 2.1.1.

26. It is therefore the Panel's decision that the first allegation has been proven by the MFDA.

Allegation #2: Failing to Inform Member of a Claim and Settling a Claim without Consent

27. On August 12, 2010, client CPL, as plaintiff, commenced a claim in the Ontario Superior Court of Justice against Huang, Qi, the Oversea Chinese Fund and Trinity, as defendants, by way of a Statement of Claim bearing Court File No CV-10-408610 (the "Claim"). In the Claim, client CPL alleged, amongst other things, that:

(a) Huang and Qi, acting as agents for Trinity (the entity through which Huang processed her insurance sales), approached CPL with an investment opportunity in the Oversea Chinese Fund whereby if CPL made an investment of $20,000 she would be guaranteed a 15% annual return on the investment for a term of one year with a guaranteed return of her full principal payment at the end of one year or earlier if so desired. CPL was further advised by Huang and Qi that this opportunity was originally only for internal workers of Trinity but that the company had agreed to make a limited offer available to certain existing clients such as CPL, as a favor. The offer was limited to a $20,000 investment per agent;

(b) Huang and Qi provided CPL with two contracts with a face value of $20,000 each, specifying a return of 15% p.a. (or $250 per month) for each contract;

(c) One month following the commencement date of the contracts, client CPL began to receive direct deposits of interest payments into her chequing account;

(d) By November 2009, client CPL became extremely alarmed as she was able to determine from her chequing account that the monthly deposits of interest were being made in cash by Huang or Qi. At this time, CPL contacted Qi and Huang directly and demanded the return of her investment, Qi and Huang refused and made excuses; and

(e) Between November 2009 and March 2010, CPL continued to make demands of Huang and Qi for the return of her $40,000, all of which were rebuffed by Huang and Qi. In March 2010, without explanation, the interest payments ceased altogether.

28. The Respondents admitted that CPL made demands for return of her investment in Oversea Chinese Fund, as described in paragraph 27(d) and (e) above, and that they failed to

inform Investia of such demands by CPL, and also failed to inform Investia that they had each been named as defendants in the Claim. In emails dated February 10 and 11, 2013 addressed to the MFDA (which emails constituted the Respondents' official replies to the NOH), each of the Respondents stated that she informed her branch manager of the demands made by CPL in August 2010. In a letter to the MFDA dated November 17, 2010, Qi stated that she did not inform Investia of the Claim because it was settled soon after it was commenced. There is no evidence that Huang ever informed Investia about the Claim.

29. The MFDA allegation is that the Respondents failed to report CPL's demands for repayment and also her Claim, as required under sections 4.1(b)(iii) and 4.1(e) of MFDA Policy No. 6. The allegation refers to section 4.1(b) (iii), but it is clear from the Book of Authorities that the correct reference should have been to section 4.1(b)(ii) of Policy No. 6. Consequently the Panel considered section 4.1(b)(ii) and 4.1(e) of Policy No. 6 in regard to the second allegation.

30. Section 4.1(b)(ii) and 4.1(e) of Policy 6 (in effect at the relevant times) provided that:

> "An Approved Person shall report the following events to his or her current Member… within 2 business days:
>
> (b) the Approved Person is aware of a complaint from any person…with respect to him or herself…involving allegations of:
>
> > (ii) engaging in securities related business outside of the Member.
>
> (e) the Approved Person is named as a defendant in a civil claim…relating to the handling of client accounts or trading or advising in securities".

31. In addition, the Investia PPM provided that:

- All complaints must be brought to the attention of the Chief Compliance Officer the same day they are received;
- Under no circumstances may a Representative pay money to a client to settle a complaint directly with a client; and

- Records must be kept at the branch level and at Head Office of all documentation and notes relating to a client complaint.

32. The PPM also provides that Representatives must notify the Branch Manager, Regional Branch Manager and the Head Office Compliance Department immediately upon receiving a Statement of Claim, and must keep Investia abreast of the status of the claim.

33. The demands for repayment by CPL starting in November 2009 were “complaints”, whether in accordance with the common English meaning of the word or as defined in MFDA Policy No. 3 or the Investia PPM (“any written or verbal statement of grievance…alleging a grievance involving the Approved Person…”). The Respondents were required to report such “complaints” and the Claim in accordance with section 4.1(b)(ii) and section 4.1(e) of Policy No. 6 and the Investia PPM. The Respondents did not do so. Even their reporting to their Branch Manager in August 2010 was not timely reporting as required. Consequently it is the Panel’s decision that the MFDA has proven the allegation that the Respondents were in breach of sections 4.1(b)(ii) and 4.1(e) of MFDA Policy No. 6.

34. On August 13, 2010, Qi and Huang provided bank drafts in the amount of $11,500 and $11,400 respectively to their client, CPL, who signed a settlement in which she agreed to dismiss the Claim and not to commence another lawsuit or action on the basis of the same facts. On August 23, 2010, a Notice of Discontinuance was filed in respect of the Claim. In their testimony, the Respondents both took the position that the payments to CPL were loans and were not in settlement of the Claim. There is no documentation to support that these payments were loans (e.g. a promissory note or loan agreement). Furthermore in Qi’s letter to the MFDA dated November 17, 2010, she stated that she “entered into a settlement agreement with [CPL]. I gave [CPL] $11,500. [CPL] decided to drop the lawsuit and any other related claims after she received my money orders.” In the same letter, Qi also states, “[CPL] told us she really needs the money because of her financial difficulties. We returned her money right away. After doing so, she agreed to drop the lawsuit and other related claims. That is why I never disclosed the lawsuit, because I thought that I did not need to do so because the matter got settled right away.” This Panel does not accept the Respondents’ position that the payments were loans to CPL rather than payments to settle the Claim; no payments were made to CPL from November, 2009 till August 2010 despite her repeated demands for money, but these payments were made immediately after

the Claim was served on the Respondents, and contemporaneously with the settlement and release, and there is no documentary evidence that the payments were loans. Whatever the nature of these payments, there is no doubt that the Claim was settled and the Respondents were released. The Respondents did not properly inform Investia of the Claim, the settlement and release or the payments by the Respondents as required by section 10 of MFDA Policy No. 3 which provides that "No Approved Person shall, without the prior written consent of the Member, enter into any settlement agreement with, pay any compensation to or make any restitution to a client." Consequently it is the Panel's decision that the Respondents were in breach of section 10 of MFDA Policy No. 3.

Penalties

35. The parties and the Panel agreed that the issue of the appropriate penalties would be heard only if and after the Panel decided that one or both of the MFDA allegations had been proven. That has now occurred and the MFDA is to arrange for the hearing regarding the appropriate penalties in this case.

DATED this 8th day of July, 2013.

"Frederick H. Webber"
Frederick H. Webber,
Chair

"Guenther Kleberg"
Guenther Kleberg,
Industry Representative

"Robert C. White"
Robert C. White,
Industry Representative

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