# 2007 BCSECCOM 257

**Edward Bernard Johnson**

**Sections 161 and 162 of the *Securities Act,* RSBC 1996, c. 418**

**Hearing**

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| **Panel** | Brent W. Aitken | Vice Chair |
| | David J. Smith | Commissioner |
| | Suzanne K. Wiltshire | Commissioner |
| **Dates of Hearing** | March 12, 13, April 3 and 11, 2007 | |
| **Date of Findings** | May 11, 2007 | |
| **Appearing** | | |
| C. Paige Leggat<br>Lisa Ridgedale | For the Executive Director | |
| John S. Forstrom | For Edward Bernard Johnson | |

**Findings**

## I Background

***Introduction***

¶ 1 This is a hearing under sections 161(1) and 162 of the *Securities Act,* RSBC 1996, c. 418.

¶ 2 Edward Bernard Johnson was a registered representative for a brokerage account in the name of a Robert Taylor. Johnson knowingly accepted trading instructions on that account from a third party. The third party was Stanley Steven Ross, who at the time was prohibited from trading because of a 1999 order of the executive director.

¶ 3 In an amended notice of hearing dated March 9, 2007, the executive director alleges that Johnson contravened By-law No. 29.1 and Regulation 1300.1(b) of the Investment Dealers Association of Canada when he "allowed Ross to trade" in the Taylor account between 2000 and 2004.

¶ 4 Commission staff interviewed Johnson on November 2, 2004 and again on January 20, 2005.

¶ 5 When staff investigators asked Johnson about the trading instructions in his interviews, he said that he did not know that Taylor had allowed Ross to trade in the account, and that to his knowledge, Ross did not do so. In the notice of hearing, the executive director also alleges that those statements were false or misleading, contrary to section 168.1 of the Act.

¶ 6 The original notice of hearing contained allegations against Ross relating to his trading in the Taylor account. The executive director and Ross settled those allegations (see *Stanley Steven Ross* 2007 BCSECCOM 113).

***Johnson's admissions***

¶ 7 At the opening of the hearing, Johnson entered a letter into evidence in which he admitted that he was the registered representative for the Taylor account, and that he accepted instructions to trade in that account from Ross. He says he accepted instructions from both Taylor and Ross, but of the 450 or so trades in the account between April 2000 and September 2004, Ross gave the instructions on at least 400.

¶ 8 In Johnson's closing submissions, he acknowledges that:

- he permitted Ross to trade in the Taylor account without a duly signed authorization from Taylor, contrary to IDA Regulation 200.1(i)(3)
- he failed to exercise due diligence to ensure that the acceptance of instructions from Ross with respect to trading in the Taylor account was within the bounds of good business practice, contrary to IDA Regulation 1300.1(b)
- his failure to exercise due diligence constituted conduct unbecoming or detrimental to the public interest, contrary to IDA By-law 29.1
- the statements described above that he made in his interviews were misleading, contrary to section 168.1.

***Johnson's knowledge***

¶ 9 In her closing submissions, the executive director argues that Johnson knew that Ross was trading for his own account through the Taylor account in violation of the 1999 order. The executive director wants us to make this finding because it would be relevant when we determine sanctions.

¶ 10 Johnson says that we ought not to consider this issue because the executive director did not allege it in the notice of hearing, and so it was not part of the case that he had to meet.

***Conduct of other brokers***

¶ 11 The evidence includes information about the conduct of other brokers who dealt with Ross. Johnson says that we should make findings about the conduct of these other brokers because it would be relevant when we determine sanctions.

## II Analysis and Findings

***Applicable law***

¶ 12 IDA Regulation 1300.1(b) says:

> 1300.1 Each Member shall use due diligence:
> . . .
> (b) to ensure that the acceptance of any order for any account is within the bounds of good business practice . . .

¶ 13 IDA By-law 29.1 says:

> 29.1 Members and each . . . registered representative . . . (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 of Directors.
> . . .

¶ 14 IDA Regulation 200.1(i)(3) says:

> 200.1 . . . every Member shall make and keep current books and records necessary to record properly its business transactions and financial charts including, without limitation:
> . . .
> (i) A record in respect of each cash and margin account:
> . . .
> 3) Where trading instructions are accepted from a person or corporation other than the customer, written authorization or ratification from the customer naming the person or company . . .

¶ 15 Section 168.1 of the Act says:

> 168.1 (1) A person must not

> (a) make a statement in evidence or submit or give information under this Act or the regulations to the commission, the executive director, or any person appointed under this Act or the regulations that, in a material respect and in light of circumstances under which it is made, is false or misleading . . .

***Findings based on admissions***

¶ 16 Based on Johnson's admissions and acknowledgements, we find that he contravened:

1. IDA By-law 201.1(i)(3) by permitting Ross to trade in the Taylor account without a duly signed authorization from Taylor;

2. IDA Regulation 1300.1(b) by failing to exercise due diligence to ensure that the acceptance of instructions from Ross with respect to trading in the Taylor account was within the bounds of good business practice;

3. IDA By-law 29.1 by failing to exercise due diligence, which constituted conduct unbecoming or detrimental to the public interest; and

4. section 168.1 of the Act by making misleading statements to an investigator appointed under the Act.

***Johnson's knowledge***

¶ 17 In her submissions, the executive director argues that Johnson "knew or ought to have known" that Ross was trading for his own account in the Taylor account in violation of the 1999 order. This is really two arguments in one. First, that Johnson had actual knowledge. Second, that in the alternative, Johnson ought to have had that knowledge.

¶ 18 The consequences attached to these two issues are much different.

¶ 19 If Ross was in fact trading for his own account, Johnson knew that, and also knew about the 1999 order, his knowledge of the 1999 order would be a significant aggravating factor.

¶ 20 For us to make that finding, we would have to find affirmative answers to three questions:

1. Was Ross trading for his own account when he gave instructions on the Taylor account?
2. Did Johnson know that Ross was trading for his own account?

3. Did Johnson know about the 1999 order?

¶ 21 Of these questions, the third one is the most significant. It would be Johnson's knowledge that Ross was wilfully trading for his own account in defiance of the 1999 order that would be the aggravating factor.

¶ 22 Johnson allowed Ross to trade in the Taylor account without due authorization from Taylor, contrary to IDA Regulation 200(i)(3), which led to his failure to exercise proper due diligence, contrary to IDA Regulation 1300.1(b). Had he exercised proper due diligence, he would have learned of the 1999 order, and therefore it follows that he ought to have known about it.

¶ 23 However, if the evidence does not establish that Johnson had actual knowledge of the 1999 order, then even if Ross were trading for his own account and Johnson knew it, that would not be a significant aggravating factor when we determine sanctions. It would be merely another fact that Johnson would have uncovered had he done proper due diligence as required by IDA Regulation 1300.1, and another aspect of his contravention of IDA By-law 29.1.

¶ 24 The executive director says this is the evidence that proves that Johnson knew about the 1999 order:

- the order was a public document
- there was at least one newspaper article about the order
- Ross and Johnson had known each other for many years
- Ross and Johnson spoke on the phone regularly
- the investment/financial community is small and the circumstances surrounding the 1999 order were "so egregious that it would have been common knowledge that Ross had been disciplined"
- an "obvious inference" to be drawn from Ross giving instructions on at least 400 trades is that he was trading in the Taylor account because he could not trade in his own account

¶ 25 In our opinion, this evidence is not sufficient to prove that Johnson had actual knowledge of the 1999 order. That the 1999 order was a public document, reported on by a newspaper, does not establish that Johnson learned of it.

¶ 26 That Ross and Johnson knew each other for many years and spoke on the phone regularly does not establish that Ross actually told Johnson about the 1999 order. It is equally plausible that Ross would avoid mentioning it.

¶ 27 We cannot conclude that Johnson must have been aware of the 1999 order due to the "egregious" circumstances, because there is no evidence as to the actual notoriety of those circumstances.

¶ 28 Finally, although one could infer that Ross' trading in the Taylor account was to circumvent a trading ban, there is no evidence that Johnson knew that, or even asked about it.

¶ 29 Accordingly, we do not find that Johnson knew about the 1999 order.

¶ 30 Even had Johnson known about the 1999 order, we agree with him that it would not be fair for us to consider that when we determine sanctions.

¶ 31 The notice of hearing makes no direct allegation about Johnson's knowledge. It alleges that Ross traded securities in the Taylor account, and describes Taylor as a "nominee". The allegation against Johnson related to trading is that Johnson "allowed Ross to trade in the [Taylor] account, contrary to IDA By-law 29.1 and Regulation 1300.1(b)." Suppose the account were a true nominee account – that is, that Taylor was the account holder in name only, and Ross the beneficial owner. Absent other factors, there would have been nothing improper about Johnson's accepting Ross' instructions to trade in that account if he had obtained the authorization required by IDA By-law 200.1(i)(3). It is therefore not relevant to this allegation whether Ross was trading for his own account or whether Johnson knew that. The notice of hearing therefore cannot be construed to give the reader any notice that Johnson's knowledge of what Ross was doing would be in issue.

¶ 32 Had the notice of hearing alleged that Johnson allowed Ross to trade, knowing that he was doing so for his own account *and* in violation of the 1999 order, the case Johnson would have had to meet would have been materially different. As noted above, those facts would have introduced a significant aggravating factor into our determination of sanctions. Considering this issue now would not be fair to Johnson.

***Conduct of other brokers***

¶ 33 We make no findings regarding the conduct of other brokers who dealt with Ross. Their conduct is not before us, and we do not consider it relevant to the question of what sanctions may be appropriate for Johnson.

## III Submissions on Sanctions

¶ 34 We direct the parties to make their submissions on sanctions as follows:

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| By June 1 | The Executive Director delivers submissions to Johnson and the Secretary to the Commission |
| By June 15 | Johnson delivers response submissions to the Executive Director and the Secretary to the Commission |
| | Either party wishing an oral hearing on the issue of sanctions so advises the other party and the Secretary to the Commission |
| By June 22 | The Executive Director delivers reply submissions (if any) to Johnson and the Secretary to the Commission |

¶ 35 May 11, 2007

¶ 36 **For the Commission**

Brent W. Aitken
Vice Chair

David J. Smith
Commissioner

Suzanne K. Wiltshire
Commissioner