

# 2007 BCSECCOM 445

**Global Securities Corporation, Robert Semple, Robert Tassone  
and Bruce McConachie**

**and**

**TSX Venture Exchange (formerly the Canadian Venture Exchange)**

**Section 28 of the *Securities Act*, RSBC 1996, c. 418**

## **Hearing and Review**

<b>Panel</b>	Brent W. Aitken Neil Alexander John K. Graf	Vice Chair Commissioner Commissioner
<b>Submission filed</b>	June 22, 2007	
<b>Oral hearing adjourned</b>	July 3, 2007	
<b>Date of Decision</b>	July 26, 2007	
<b>Joint submission filed by</b>		
Robert W. Taylor	For Global Securities Corporation	
Larry R. Jackie	For TSX Venture Exchange	

## **Decision**

### **I Background**

#### **A. Synopsis**

- ¶ 1 This is a hearing and review under section 28 of the *Securities Act*, RSBC 1996, c. 418 of a March 13, 2003 decision of a disciplinary panel of the Canadian Venture Exchange (now the TSX Venture Exchange).
- ¶ 2 The Exchange notice of hearing alleged contraventions of Exchange rules by two of Global's registered representatives, a branch manager, and Global. All of the allegations arose from the opening and administration of a client's options account.

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- ¶ 3 This hearing and review relates only to the Exchange panel's dismissal of the allegation that Global failed to diligently supervise trading in the account, contrary to the rule relevant at the time, Rule F.1.01(1)(b) of the Vancouver Stock Exchange (a predecessor of the Canadian Venture Exchange).
- ¶ 4 Global and the Exchange have reached a settlement in the matter. For the purposes of that settlement, Global admits that it failed to diligently supervise trading in the account. Global and the Exchange have filed a joint submission asking us, in effect, to approve the settlement by:
- finding that the Exchange panel erred in dismissing the allegation that Global contravened Rule F.1.01(1)(b),
  - varying the panel's decision by substituting a finding that Global contravened the Rule, and
  - varying the panel's decision by ordering Global to pay the Exchange an administrative penalty of \$10,000.

¶ 5 In light of Global's admission, the executive director did not file submissions.

¶ 6 The parties filed their joint submission on June 22. By consent, there was no oral hearing.

### **B. Facts**

- ¶ 7 This summarizes the facts as agreed by the parties, which are based on the Exchange panel's findings of fact.
- ¶ 8 A client opened several accounts at a branch of Global in 1994 and 1995, including an options account. The account was in the name of a corporation controlled by the client, but the distinction is not important for the purposes of this decision.
- ¶ 9 The client had married into a well-known and wealthy family. At the time she opened the account she was divorced. She had a net worth of about \$6 million.
- ¶ 10 The registered representatives on the account, Robert Semple and Robert Tassone, were not qualified to trade options. A Global representative who was so qualified, Wendel Nunes, opened a new client application form for an options account for the client. The client was unaware of the form. He and Global's compliance officer at the time signed it. Global's "Designated Registered Options Principal" (DROP), the individual responsible for the supervision of options accounts, did not.

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- ¶ 11 Global admitted in the Exchange hearing that it did not ensure the client's options account was properly documented, contrary to Exchange rules.
- ¶ 12 Nunes traded all the options in the account until Semple became qualified to trade options in mid-1995, although the client received all her advice from Semple.
- ¶ 13 The evidence before the panel was that the options trading done for the client was not appropriate. The client, the panel found, was "an unsophisticated and inexperienced investor." The panel also found that the documentation Semple and Tassone provided her was "not transparent or easily understood, nor was it frequently, routinely and consistently provided." In the panel's view, "[i]t would have been extremely difficult for a relatively unsophisticated and inexperienced investor . . . to keep abreast of what was happening in her accounts."
- ¶ 14 Losses were incurred in the account, the most substantial ones occurring from May through September 1995.
- ¶ 15 The Exchange panel found that Semple and Tassone provided advice on options trading to the client without being qualified to do so, and failed to ensure their recommendations for her accounts were appropriate and in keeping with her investment objectives, contrary to Exchange rules.
- ¶ 16 The Exchange panel reviewed the following evidence relevant to supervision of the client's options account:
- Bruce McConachie, the branch manager, did not review trading in the options account as he understood Global's head office performed that function through the DROP.
  - Typically the DROP dealt directly with investment advisers, not the branch manager. In this client's case, neither the DROP nor Global's compliance department involved McConachie in matters relating to her accounts.
  - Busby, as Global's DROP, was responsible for reviewing options trading to determine suitability and credit risk. (Busby became Global's DROP in April 1995, after the options account was opened.)
  - Busby did not independently review the client's investment objectives. He never met the client, but was familiar with the client's ex-husband and knew that his family was wealthy. He knew the client had a high net worth but did not know that she was divorced.
  - Busby saw account statements for July and September 1995 and would normally have had concerns about credit risk but dismissed them in light of the wealth of the family with whom he assumed the client was still connected.

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¶ 17 The panel concluded that McConachie, as a supervisor, should have been aware of the trading in the account (and in fact did know that Semple was endeavouring to trade in options without being qualified to do so) and should have reviewed the suitability of that trading. The panel found that McConachie did not do so, and failed to diligently supervise the options trading for the client, contrary to Rule F.1.01(1)(b),

### **C. The Exchange panel's decision**

¶ 18 The Exchange notice of hearing alleged that Global failed to diligently supervise the client's options account, contrary to Rule F.1.01(1)(b). The Exchange panel dismissed this allegation, on these grounds:

1. A firm's supervisory obligation relating to head office suitability reviews is less onerous than the branch manager's.
2. A firm may not have failed to discharge its supervisory obligations if
  - it adopts a two-tier supervisory mechanism in accordance with the Exchange's Policy Statement CR06 reasonably expected to detect non-compliance,
  - it carries out its supervisory responsibilities appropriately under that mechanism, and
  - there is nothing to show it knew or ought to have known of a supervisory failure at the first level.
3. There was nothing in McConachie's activities that would have alerted Global that he was failing to diligently supervise the trading in the options account.
4. Busby's review of the account conformed to at least the minimum requirements under Policy Statement CR06 and did not disclose unusual trading activity.

¶ 19 About Global's supervisory responsibilities, the panel said:

Given the different obligations in the two-tier structure of supervision as between Branch Manager and the Head Office, the Panel accepts that there are different standards applicable to each. In particular, it agrees that the Branch Manager bears the more onerous responsibilities with respect to account supervision and that the responsibilities borne and Head Office are secondary to the front-line supervision which the Branch Manager is expected to provide.

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¶ 20 About Busby's conduct, the panel said:

. . . Although he was not familiar with the investment objectives for the [options account], he was familiar with [the client's] family and knew that she was a high net worth client. He believed that the suitability and appropriateness of the trading had been assessed by his predecessors. His review of the trading did not disclose anything unusual that was not justifiably explained to him when he queried the brokers handling the account.

### **D. Subsequent civil litigation**

¶ 21 In civil proceedings related to the same facts, the British Columbia Supreme Court found that Global breached its duty of care to the client by failing to properly supervise trading in the options account. Global paid damages (including interest) and costs totalling about \$324,000.

## **II Analysis**

### **A. Standard of review**

¶ 22 On a hearing and review under section 28, the Commission may confirm or vary the decision under review, or make another decision it considers proper: section 165(4).

¶ 23 The Commission's standard for reviewing decisions of the Exchange is set out in section 5.9(a) of BC Policy 15-601 as follows:

5.9(a) The Commission does not provide parties with a second opinion on a matter decided by an SRO. If the decision under review is reasonable and was made in accordance with the law, the evidence, and the public interest, the Commission is generally reluctant to interfere simply because it might have made a different decision in the circumstances. For this reason, generally, the person requesting the review presents a case for having the decision revoked or varied and the SRO responds to that case.

In these circumstances, the Commission generally confirms the decision of the SRO, unless

- the SRO has made an error in law
- the SRO has overlooked material evidence
- new and compelling evidence is presented to the Commission or
- the Commission's view of the public interest is different from the SRO's

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### **B. The issue**

- ¶ 24 The issue is whether the Exchange panel’s decision to dismiss the allegation that Global failed to diligently supervise the account was reasonable and made in accordance with the law, the evidence and the public interest.
- ¶ 25 The parties say that the decision does not pass this test. They say we should vary the decision because
1. the panel erred in law;
  2. the panel overlooked material evidence; and
  3. the Commission’s view of the public interest ought to be different on the particular facts of this case than the panel’s.

### **C. Relevant Exchange Rules and Policy**

- ¶ 26 At the relevant time, Rule F.1.01(1)(b) said:
1. Every member is required through a designated partner or director or officer or in the case of a branch manager, a manager reporting directly to the partner, director, or officer to:  
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.  
(b) diligently supervise all accounts handled by his registered representatives.
- ¶ 27 At the relevant time, Part IV of the Exchange’s Policy Statement CR06, “Head Office Supervision” said:
- A two-tier structure is required to adequately supervise client account activity. While the head office or regional area level of supervision by its nature cannot be in the same depth as branch level supervision, it should cover all the same elements.
- ¶ 28 Part V of the Policy, “Option Account Supervision”, said:
- Each member dealing in options . . . must have an approved Designated Registered Options Principal . . . with overall responsibility for the opening of new option accounts and the supervision of account activity to ensure that all recommendations made for any account are and continue to be appropriate for the client and in keeping with [the client’s] investment objectives.

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### D. Analysis

#### 1. *Did the Exchange panel err in law?*

- ¶ 29 The parties say that the Exchange panel erred in law when it concluded that, because the branch manager and head office have different obligations and responsibilities, they should be held to different standards. They say the correct interpretation is that the appropriate standard of care, at all levels of supervision, is to “diligently” supervise. Therefore, they say, supervision at any level that is not carried out diligently fails to meet the requirements of Rule F.1.01(1)(b).
- ¶ 30 We agree. Rule F.1.01(1)(b) required both Global and McConachie to supervise diligently, and to the same standards. This is supported by the language of Policy CR06. It acknowledges that head office supervision may not go into as much depth as branch level supervision, but says “it should cover all the same elements”.
- ¶ 31 Diligent supervision has as its goal the detection of improper conduct. A VSE panel in *Vancouver Stock Exchange, Whalen Beliveau & Associates Inc., and John Frederick Brighten* (Decision of the VSE, January 23, 1998) said (at page 15) that diligent supervision means “more than following a set of rules, it means reviewing the trading with a view to detecting activity which would be detrimental to clients.”
- ¶ 32 Global therefore failed to ensure that McConachie was diligently exercising his supervisory responsibilities. In a two-tier system of supervision, part of the responsibility of head office is to ensure that the supervisory functions it is relying on at the front-line level are in fact being discharged properly and effectively. Global did not, and so failed to diligently supervise trading in the account.
- ¶ 33 Global also failed to exercise diligence at head office because Busby did not diligently supervise trading in the options account. We discuss this further in the next section.
- ¶ 34 We therefore find that the Exchange panel erred in law in its interpretation of Global’s obligations under Rule F.1.01(1)(b).

#### 2. *Did the Exchange panel overlook material evidence?*

- ¶ 35 The parties say that the panel failed to adequately consider the evidence that Busby had no knowledge of the client’s investment objectives. The parties say he did not, and so failed to diligently supervise trading in the options account.
- ¶ 36 We agree. The panel acknowledged that Busby was unaware of the investment objectives in the account, but appears to excuse this lapse by stating that “he was familiar with [the client’s] family and knew that she was a high net worth client.” Busby was unaware that the client was divorced, and therefore her relationship to

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the family was no longer relevant. Yet he dismissed concerns about risk on the basis that she was still connected to the family and its wealth. The Exchange panel failed to give appropriate weight to that evidence.

- ¶ 37 Busby said he did not review the account opening documentation because he became the DROP only after the account was opened. That is irrelevant. One of his primary obligations was do suitability reviews of trading activity in options accounts. This he could not do if he was not familiar with each client's circumstances and investment objectives. In this client's case, instead of familiarizing himself with that information, he assumed his predecessor had done so and made no independent inquiry. This is not sufficient. Under Policy CR06, the DROP is responsible for ensuring that all recommendations made for the account "are *and continue to be* appropriate for the client [our emphasis]". The words we emphasize make it clear that suitability is to be reviewed on an ongoing basis.
- ¶ 38 Busby was also influenced by his belief that the client was associated with a wealthy family. In doing so, he erred twice. The client was no longer associated with that family and a suitability review still requires an assessment of whether the investments held in the account correspond to the client's risk tolerance and investment objectives.
- ¶ 39 We therefore find that Busby's supervision of the client's options account was not diligent within the meaning of Rule F.1.01(1)(b), and that the Exchange panel overlooked material evidence that would have led to that finding.

### **3. *Was the Exchange panel's view of the public interest appropriate?***

- ¶ 40 We have found that the Exchange panel erred in law and overlooked material evidence. In our opinion, these are sufficient grounds to vary its decision. It is therefore not necessary for us to consider the panel's view of the public interest.

### **E. Is the parties' proposed administrative penalty appropriate in the circumstances?**

- ¶ 41 The Exchange panel fined Semple and Tassone \$15,000 and \$10,000 respectively, and each were assessed costs of \$10,000. The panel fined McConachie \$20,000 and assessed costs of \$5,000. For Global's admitted contraventions, the panel fined it \$10,000 and assessed costs of \$5,000.
- ¶ 42 The parties propose a penalty of \$10,000 for Global's admission that it failed to diligently supervise the options account.



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- ¶ 43 The Exchange says has taken into account these facts in mitigation of the sanctions it would otherwise recommend:
- Global has admitted its wrongdoing and thereby avoided the need to hold a full hearing
  - Global has paid a civil judgement of about \$324,000, including interest and costs
  - Global has already paid the Exchange fines and costs totalling \$15,000
  - in combination with the \$10,000 fine Global has already paid, the total penalty it will pay is commensurate with the \$20,000 penalty imposed on McConachie
- ¶ 44 The proposed penalty is below the range of penalty we would ordinarily impose in these circumstances. Global had the ultimate responsibility for ensuring adequate supervision, so we would likely have imposed a total penalty on Global greater than the Exchange imposed on McConachie.
- ¶ 45 However, we are considering a settlement between Global and the Exchange. The settlement includes both Global's admission that it failed to diligently supervise and the proposed penalty. Global has made that admission only for the purpose of the settlement with the Exchange. That settlement relies on our accepting the proposed penalty. It is not open to us to make that finding and reject the penalty proposal.
- ¶ 46 If we were to reject the settlement, the parties would have two alternatives: come to a different settlement, or put the matter before another panel in a full hearing. In our opinion, the difference between the proposed penalty and that which would likely result from a full hearing in the matter does not justify the time and cost that would be incurred in connection with holding that hearing. It therefore makes sense to accept the proposed penalty.
- ¶ 47 The settlement is also an expeditious means of putting Global's admission on the record, and clearing up the Exchange panel's misinterpretation of head office supervision responsibilities.
- ¶ 48 In our opinion, the consequences to Global of the civil proceedings are not a mitigating factor. Global has paid only what a court has determined it is obligated to pay to compensate the client for Global's misconduct.

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### **III Decision**

¶ 49 We therefore vary the Exchange panel's decision by finding that Global failed to diligently supervise the client's option account, contrary to Rule F.1.01(1)(b), and by ordering Global to pay the Exchange an administrative penalty of \$10,000.

¶ 50 July 26, 2007

¶ 51 **For the Commission**

Brent W. Aitken  
Vice Chair

Neil Alexander  
Commissioner

John K. Graf  
Commissioner