2009 BCSECCOM 339

Kegam Kevin Torudag and Lai Lai Chan

Section 161 of the *Securities Act,* RSBC 1996, c. 418

Hearing

Panel	Brent W. Aitken	Vice Chair
	Kenneth G. Hanna	Commissioner
	Shelley C. Williams	Commissioner
Date of hearing	May 22, 2009	
Date of Decision	June 18, 2009	

Appearing

Sean K. Boyle	For the Executive Director
H. Roderick Anderson	For Kegam Kevin Torudag

Decision

I. Introduction

¶ 1 This is the sanctions portion of a hearing under sections 161(1) and 162 of the *Securities Act*, RSBC 1996, c. 418. Our Findings on liability made on March 11, 2009 (2009 BCSECCOM 145) are part of this decision.

¶ 2 Kegam Kevin Torudag facilitated the assignment to Icon Industries Limited of mineral claims owned by Lai Lai Chan. At the time of the assignment, Icon was an inactive company listed on the TSX Venture Exchange. The assignment was a material fact relating to Icon. Icon announced the assignment on March 13, 2007. Torudag and Chan separately bought Icon shares beginning about two and a half hours before the announcement.

¶ 3 Torudag and Chan admitted purchasing the Icon shares while being persons in a special relationship with Icon and having undisclosed material facts about the company, in contravention of section 86(1) of the Act as it read at the relevant time. They each admitted the essential facts of the contravention, subject to the defence in section 86(4) – that they reasonably believed that the material facts had been generally disclosed when they purchased the Icon shares.

¶ 4 Based on Torudag's and Chan's admissions, we found that they contravened section 86(1) and that they did not establish a defence under section 86(4). We found that Torudag, before purchasing the Icon shares on March 13, 2007, did not hold a reasonable belief, and failed to take all reasonable steps necessary to establish, that the material facts about Icon had been generally disclosed.

II. Discussion and Analysis

A. Positions of the parties

¶ 5 The executive director seeks orders against Torudag prohibiting him for five years from trading and from acting as a registrant, investment fund manager or promoter, and imposing an administrative penalty of $105,225.

¶ 6 Torudag says the appropriate sanction is a six-month to one-year cease trade order, with permission to acquire securities of exchange-listed issuers for services rendered or for assets vended to the issuer and to sell securities owned by him at the date of the order, and an administrative penalty of no more than $30,000.

¶ 7 The executive director seeks orders against Chan prohibiting her for one year from trading and from acting as a registrant, investment fund manager or promoter, with permission to trade through a personal account, and imposing an administrative penalty of $9,375.

¶ 8 Chan says the appropriate sanction for her, if any, would be an order requiring her to "undergo securities training." She says any administrative penalty should be no more than $1,000.

B. Factors to consider

¶ 9 In *Re Eron Mortgage Corporation* [2000] 7 BCSC Weekly Summary 22, the Commission discussed the factors relevant to sanction as follows (at page 24):

> In making orders under sections 161 and 162 of the Act, the Commission must consider what is in the public interest in the context of its mandate to regulate trading in securities. The circumstances of each case are different, so it is not possible to produce an exhaustive list of all of the factors that the Commission considers in making orders under sections 161 and 162, but the following are usually relevant:
>
> - the seriousness of respondent's conduct,
> - the harm suffered by investors as a result of the respondent's conduct,

- the damage done to the integrity of the capital markets in British Columbia by the respondent's conduct,

- the extent to which the respondent was enriched,
- factors that mitigate the respondent's conduct,
- the respondent's past conduct,
- the risk to investors and the capital markets posed by the respondent's continued participation in the capital markets of British Columbia,
- the respondent's fitness to be a registrant or to bear the responsibilities associated with being a director, officer or adviser to issuers,
- the need to demonstrate the consequences of inappropriate conduct to those who enjoy the benefits of access to the capital markets,
- the need to deter those who participate in the capital markets from engaging in inappropriate conduct, and
- orders made by the Commission in similar circumstances in the past.

C. Application of the factors

Seriousness of the conduct and damage to markets

¶ 10 The objective of the Act is to protect investors and the integrity of capital markets. Market participants expect that all those trading in a market with integrity have available to them the same material information about the securities traded in that market.

¶ 11 The Act has several provisions intended to ensure that expectation is met. Section 86 is one of the most important. It prohibits persons from trading in securities of an issuer while in possession of material information about the issuer that has not been generally disclosed. Trading in contravention of the section is serious misconduct – it damages the public's perception of the fairness of our markets.

¶ 12 Torudag, an experienced trader, would be aware of this. In our Findings, we said:

> 65 Torudag is an experienced trader, and is familiar with the junior resource issuer market. He has significant investor relations experience and understands how information is disseminated to the market. . . . He would also know that it can take some time after issuance of the news release for general disclosure to occur.

¶ 13 Torudag purchased 119,000 Icon shares in 11 trades on March 13, 2007 before Icon issued its news release. We found that a reasonable person, with only the facts available to Torudag while he was purchasing those shares, could not, without confirming that Icon had issued its news release, form a reasonable belief that the information had been released, never mind judge whether it had become

generally disclosed. We also said that Torudag, as one who knew the material information about Icon because of his direct involvement in the relevant events, ought to have taken at least the reasonable initial step of confirming that Icon had announced the assignment.

¶ 14 We found that Chan appears unfamiliar with public markets and the requirements of securities regulation. She purchased 10,000 shares in two trades on March 13, 2007.

¶ 15 We did not find intentional misconduct on the part of either respondent.

Harm suffered by investors; enrichment

¶ 16 Torudag and Chan harmed investors in direct proportion to the degree to which they were enriched.

¶ 17 The executive director says that Torudag's and Chan's enrichment is equal to the profits they made trading the Icon shares they bought on March 13, 2007. The executive director proposed two methods to determine that profit. The first method would subtract their respective acquisition cost of the shares from the 20-day average Icon share price after March 13, 2007. The second method would subtract the acquisition cost of their shares from their subsequent share sale proceeds, on a "first-in-first-out" basis. This method could be applied only to Torudag because, unlike Chan, he sold all of the Icon shares he purchased and the sale prices are in the evidence. Using the first method, the executive director says Chan's profit is $6,250. Using an average of both methods, the executive director says Torudag's profit is $70,150.

¶ 18 In our opinion, there is no apparent rationale for either method or, in Torudag's case, for using an average of the two. Both methods produce arbitrary numbers that are likely to bear no relationship to the actual benefit derived by traders as a result of their illegal insider trading. Furthermore, the 20-day period in the first method, to the extent intended to correspond to the time necessary to achieve general disclosure, is far too long – it does not reflect the speed with which information is disseminated in today's markets, and accordingly may also reflect factors affecting the stock price that are unrelated to the release of the material information.

¶ 19 As for the first-in-first-out method, it is capable of being applied only where the trader has subsequently sold shares purchased in the course of illegal insider trading. Using this method, the level of enrichment would differ, not only between traders who sell and those who don't, but also between traders who sell, because the formula's result is affected by the prices of the subsequent trades.

¶ 20 To be useful, the measure of enrichment ought to be applicable to all instances of illegal insider trading, not dependent on whether or how the trader subsequently deals with the securities acquired.

¶ 21 In our opinion, the benefit a trader has derived from illegal insider trading is measured by the difference between the price at which the illegal trade takes place and the price of the securities after the material information has been generally disclosed. This compares the price at which the trader bought or sold to the price at which the trader could have bought or sold after general disclosure of the material information. The result is the trader's profit earned or loss avoided through the illegal trading.

¶ 22 Applying that method in this case, we have subtracted Torudag's and Chan's respective average acquisition cost per share on March 13, 2007 from the Icon share price after the material facts had been generally disclosed.

¶ 23 That leads to the question of when the material facts about Icon were generally disclosed. The point at which general disclosure occurs depends on the circumstances. For example, information about an actively traded senior issuer, whose announcements are closely followed by the market, can become generally disclosed very soon following a news release. Information about a lesser-known and less-actively traded issuer can take longer to become generally disclosed because it takes longer for the market to receive and absorb the information.

¶ 24 Factors relevant to determining whether general disclosure has occurred include trade volume, share volume, volatility, sustained changes in share price, the number of dealers trading, and the distribution of trading among those dealers. Other factors could apply in the circumstances of other cases.

¶ 25 At the time of its announcement, Icon was an inactive company. In the five weeks prior, there were only 35 trades of Icon shares, representing a total volume of about 240,000 shares.

¶ 26 Icon announced the material facts at about 3:30 in the afternoon of March 13, 2007. On March 14, between market open and 10:05, about 140,000 Icon shares traded, at prices between 21 and 25 cents. Another 124,000 shares traded until 11:02, when the price reached 30 cents. Volume and price increased steadily throughout the day. After reaching a high for the day of 49.5 cents, the shares closed at 41 cents on a volume for the day of nearly 1.2 million shares in 142 trades. The 15 dealers listed in the most active buying and selling lists for the day traded an average volume of about 150,000 shares each.

¶ 27 On March 15 Icon shares opened at 41 cents, rose to a high of 68 cents and closed at 66 cents on a volume of nearly 1.5 million shares in 207 trades. The 14 dealers listed in the most active buying and selling lists for the day traded an average volume of about 180,000 shares each. Total volume from March 16 to April 30 was about 7 million shares at prices ranging from 56 cents to $1.45.

¶ 28 Torudag says that general disclosure of the Icon material facts had occurred by the close of trading on March 14. We agree. Applying the relevant factors mentioned above, the trading that day shows that the material information about Icon was generally disclosed by that time:

- the volume of both trades and shares traded had increased significantly compared to previous trading activity in Icon shares
- the share price had increased significantly – to about double what it was at the time of the announcement, and was following a sustained upward trend
- more than 15 dealers traded, and the 15 most active dealers averaged about 150,000 shares each.

¶ 29 Torudag's average acquisition cost per share was 20.4 cents. Subtracting this number from the closing price on March 14 of 41 cents, and multiplying the result (20.6 cents) by the 119,000 shares he bought shows he was enriched by $24,514.

¶ 30 Chan's average acquisition cost per share was 20 cents. Subtracting this number from the March 14 closing price of 41 cents, and multiplying the result (21 cents) by the 10,000 shares she bought shows she was enriched by $2,100.

¶ 31 These amounts show that neither Torudag nor Chan was greatly enriched as a consequence of their illegal insider trading.

Mitigating factors

¶ 32 Torudag cooperated with the Commission's investigation. He travelled to Vancouver from Montreal to be interviewed by Commission staff. On the advice of his counsel at the time he asked to be summonsed (the summons was served on him at the outset of the interview), but his participation in the interview was voluntary.

¶ 33 Torudag bought the 119,000 Icon shares through one of his companies, Farlack Ventures Limited. Farlack is incorporated in the British Virgin Islands. In the course of their investigation, Commission staff sought documents from the BVI authorities that would establish the identity of Farlack's beneficial owners. The documents that staff sought were not located in the BVI but in Liechtenstein, the location of Farlack's administrative office. The Commission staff investigator testified at the hearing that "the likelihood of getting information from

Liechtenstein was . . . very slim to none." When Torudag learned from Farlack's representative in the BVI that the Commission was seeking those documents, he directed the administrative office in Liechtenstein to provide them. By ensuring that Commission staff received these documents, Torudag assisted the investigation.

¶ 34 Chan is a person of modest means who entered the field of prospecting through a natural interest in minerals and mining, and a hope that it would supplement her income. As noted above, she is unfamiliar with securities markets and the rules that govern them.

¶ 35 There are no aggravating factors relevant to the conduct of either respondent.

Past conduct

¶ 36 Torudag has worked with public companies and been an active trader for many years and has no prior disciplinary history. Chan has no prior disciplinary history.

Risk to investors and markets

¶ 37 In our opinion, the continued participation by Torudag and Chan in the capital markets poses no undue risk to investors or markets.

¶ 38 The executive director acknowledges that Torudag earns his living through investor relations activities and seeks no order that would prevent him from continuing to do so. The executive director also seeks no order prohibiting Torudag from acting as a director or officer. Torudag's misconduct was the result of a serious error in judgment, but it does not represent a calculated intention to profit through wrongdoing. In these circumstances, an order prohibiting Torudag from engaging in investor relations activities would be disproportionately harsh, given it is his primary means of livelihood; neither do we consider it necessary in the public interest to prohibit him from acting as a director or officer.

¶ 39 Chan's misconduct was a result of a complete lack of knowledge about the rules. She says she is committed to educating herself about the securities regulation requirements and intends never to repeat this sort of oversight in future. The executive director is not seeking an order against Chan prohibiting her from acting as a director or officer, but in light of her unfamiliarity with the rules, it is appropriate that she not act as a director or officer of an issuer until she receives relevant training.

Specific and general deterrence

¶ 40 The orders we are making are intended to deter Torudag and Chan from future misconduct and will demonstrate the consequences of inappropriate conduct to other market participants.

Previous orders

¶ 41 The executive director and Torudag referred us to seven decisions and settlements as authority for their respective positions as to the appropriate sanction for Torudag. The ones we consider most relevant are *Gorrie* 2006 ABASC 1087, *Conrad* 2009 ABASC 69, and *Ruttan* 2002 LNABASC 346.

¶ 42 Gorrie admitted all elements of the insider trading prohibition. In a sanctions hearing, the Alberta Securities Commission found that it was not reasonable for him to have assumed that the material information had been generally disclosed, and that he made insufficient efforts to determine whether it had been. There was no intentional misconduct. The Commission ordered Gorrie not to trade for a period of one year, ordered an administrative penalty equal to about 1.25 times his agreed profit and ordered him to pay costs of $3,000.

¶ 43 Conrad's settlement agreement with the Alberta Securities Commission reflected his honest and mistaken belief that the material information had been generally disclosed, and his admission that he failed to exercise all reasonable care to determine that was so. Conrad agreed to a one-year cease trade order, an administrative penalty equal to about 1.5 times his agreed unrealized profit, and to pay costs of $15,000.

¶ 44 Ruttan, an officer of the issuer whose shares he traded, settled with the Alberta Securities Commission by agreeing to one-year prohibitions against trading and acting as a director or officer, to an administrative penalty about equal to his agreed gross profit, and to pay costs of about $3,900.

III. Decision

¶ 45 We are making cease-trade orders against both Torudag and Chan. In our opinion, the seriousness of illegal insider trading requires some period of prohibition from trading. The orders are drafted to prevent Torudag and Chan from having any opportunity to trade while in possession of undisclosed material information.

¶ 46 In determining the nature and duration of the cease-trade order against Torudag, we considered that it is not contrary to the public interest that Torudag be able to continue making a living by providing services to listed companies. That said, a cease-trade order will affect him seriously. Although the order will allow him to

continue to receive securities as compensation for services or property (many junior issuers are unwilling or unable to pay cash), he will be prohibited from selling those securities for the duration of the order, increasing the risk that they will fall in value before he is able to realize on his compensation. Torudag is also an active trader and in recent years has made a significant portion of his living by trading securities. This income stream will not be available to him for the duration of the order.

¶ 47 In determining the nature and duration of the cease-trade order against Chan, we considered it not contrary to the public interest that she be able to receive securities in exchange for properties she finds through her prospecting activities. Like Torudag, she will be prohibited from selling those securities for the duration of the order.

¶ 48 We have not made orders prohibiting Torudag and Chan from acting as registrants, investment fund managers or promoters. We do not think those orders are necessary in public interest in light of our finding that Torudag's and Chan's continued participation in the capital markets would not pose undue risk to investors and markets.

¶ 49 We have ordered administrative penalties. The objective of an administrative penalty in an illegal insider trading case is to ensure that, generally, a person who engages in illegal insider trading cannot be seen to have profited from that wrongdoing, and that the penalty serves as a disincentive, both to the person and to others from engaging in similar illegal conduct.

¶ 50 The amount of an administrative penalty is not determined by a formula, but one way to arrive at an appropriate penalty for illegal insider trading is to consider the extent to which the trader is enriched. In our opinion, that approach is suitable in this case. We have found that by buying the Icon shares before general disclosure of the material facts, Torudag was enriched by $24,514. The amount by which the enrichment should be multiplied for the penalty to offset profit and provide both specific and general deterrence will vary with the circumstances of each case. Here, the executive director and Torudag agree that 1.5 is an appropriate multiplier for an administrative penalty based on enrichment in these circumstances. We agree and have imposed an administrative penalty on Torudag using that multiplier. We do not consider it necessary to impose any additional administrative penalty against Torudag.

¶ 51 Although we think an administrative penalty is appropriate in Chan's case to offset her enrichment, we do not think a multiplier is necessary.

¶ 52 Therefore, considering it to be in the public interest, we order:

1. under section 161(1)(b) of the Act, that Torudag cease trading, and is prohibited from purchasing, securities or exchange contracts except that:

   (a) Torudag may trade and purchase securities and exchange contracts for his own account through an RRSP account with a registrant, if he gives the registrant a copy of this decision
   (b) Torudag, or an issuer all the securities of which are owned by him or members of his immediate family, may acquire securities of issuers listed on the Toronto Stock Exchange or the TSX Venture Exchange in consideration for services rendered (including finder's fees) or for assets he transfers or assigns to the listed issuer
   (c) Torudag, or an issuer all the securities of which are owned by him or members of his immediate family, may sell any securities owned by them on the date of this order if Torudag gives the executive director a list of the securities stating the registered dealers in which each security is held and the details of the relevant accounts

   until the later of June 18, 2010 and the date he pays the amount in paragraph 2 of these orders;

2. under section 162, that Torudag pay an administrative penalty of $36,771;

3. under section 161(1)(b), that Chan cease trading, and is prohibited from purchasing, securities and or exchange contracts except that:

   (a) Chan may trade and purchase securities or exchange contracts for her own account through an RRSP account with a registrant, if she gives the registrant a copy of this decision
   (b) Chan, or an issuer all the securities of which are owned by her or members of her immediate family, may acquire securities of issuers listed on the Toronto Stock Exchange or the TSX Venture Exchange in consideration for assets she transfers or assigns to the listed issuer

   until the later of June 18, 2010 and the date she pays the amount in paragraph 5 of these orders;

4. under section 161(1)(d)(ii), that Chan is prohibited from acting as a director or officer of any issuer, other than an issuer all the securities of which are owned by her or members of her immediate family until the latest of

(a) the date she completes a course of study satisfactory to the executive director on the duties and responsibilities of directors and officers,
(b) June 18, 2010, and
(c) the date she pays the amount in paragraph 5 of these orders;

and

5. under section 162, that Chan pay an administrative penalty of $2,100.

¶ 53 June 18, 2009

¶ 54 **For the Commission**

Brent W. Aitken
Vice Chair

Kenneth G. Hanna
Commissioner

Shelley C. Williams
Commissioner