INVESTMENT DEALERS ASSOCIATION OF CANADA

bulletin

ASSOCIATION CANADIENNE DES COURTIERS EN VALEURS MOBILIÈRES

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Discipline

Discipline Penalties Imposed on Emerging Equities Inc. and James Baker Hartwell - Violations of By-laws 17, 29.1 and 38

Person Disciplined

A Hearing Panel appointed pursuant to IDA By-law 20 has imposed discipline penalties on Emerging Equities Inc. ("EEI"), a Member of the IDA and James Baker Hartwell ("Hartwell"), at all material times, Chief Executive Officer, President and Ultimate Designated Person of Emerging Equities Inc.

By-laws, Regulations, Policies Violated

On, October 26, 2004, in Calgary, Alberta, a Hearing Panel considered, reviewed and accepted a Settlement Agreement negotiated between EEI, Hartwell and Staff of the IDA.

Pursuant to the Settlement Agreement, EEI admitted that it failed to maintain adequate capital for the month ending January 31, 2001, contrary to IDA By-law 17.1. Further, Hartwell admitted the he failed in his capacity as the Ultimate Designated Person to ensure that EEI maintained adequate capital for the period ending January 31, 2001, contrary to IDA By-law 17.1.

Penalty Assessed

The discipline penalties assessed against EEI is a fine in the amount of $55,000.00.

The discipline penalties assessed against Hartwell are:

(i) fine in the amount of $15,000.00;
(ii) a twelve (12) month period of prohibition from acting in the registered capacities of Ultimate Designated Person, Alternate Designate Person, Chief Financial Officer, Chief Compliance Officer, Designated Registered Options Principal, Alternate Registered Options Principal, Designated Registered Futures Principal, Alternate Designated Registered Futures Principal, Branch Manager and Assistant Branch Manager, for any Member of the Association.

The prohibition period to commence from the date that a new UDP is registered for EEI.

(iii) Requirement to rewrite and pass the Partners, Directors, and Officers examination, of the Canadian Securities Institute within six (6) months of the date of the approval of this Settlement Agreement; and

The Respondents shall have up to six (6) months to appoint and register a new UDP for EEI.

Costs:

EEI and Hartwell are also required to pay the sum of $15,000.00 towards the Association's cost in this matter.

Summary of Facts

Facts:

Association Staff monitored the risk adjusted capital and other financial and administrative records of EEI for a period of approximately 24 months preceding January 2002. During this period, EEI was subject to Early Warning (Level 2) restrictions from May 11, 2000, to August 17, 2000, and again from September 2000 to December 6, 2001, primarily due to triggering profitability tests under the Early Warning rules of Association By-law 30.

Association Staff conducted two (2) financial compliance field examinations during the stated 24 month period.

On November 1, 2000, the Association issued it's Field Examination Report ("2000 FER"), relating to the period ended March 31, 2000. The 2000 FER identified 16 records and internal control deficiencies, of which 10 were considered to be significant.

The deficiencies of particular relevance were securities concentration charge calculation errors, insufficient margin for a number of client accounts, broker warrants incorrectly margined and the fact that the position of Chief Financial Officer ("CFO") had been vacant since EEI's inception. Some of the identified deficiencies impacted the accuracy of the firm's risk adjusted capital ("RAC") calculation.

On February 15, 2001, EEI filed its Monthly Financial Report ("MFR") for the period ending January 31, 2001. Upon review of the MFR, Association Staff identified a securities concentration calculation error, which resulted in a reduction to the firm's RAC.

Hartwell and EEI had previously (January 2001) identified the possibility of a securities concentration issue in the client accounts of a particular broker (the "broker") and were aware there could be a negative affect on the firm's RAC. Hartwell and EEI directed the broker to rectify the securities concentration issue but the broker failed to do so.

EEI was determined to be capital deficient for the period ending January 31, 2001. It has been acknowledged that EEI's internal control systems and the timeliness of its record keeping did not allow EEI to correct the broker concentration issue prior to month-end, which was the significant factor contributing to the capital deficiency as at January 31, 2001.

In the latter part of February 2001, EEI filed a revised January 31, 2001, MFR, reflecting an increase in the reported securities concentration charge and consequent revised RAC. EEI and Hartwell liquidated securities to rectify the capital deficiency prior to March 1, 2001.

The Association commenced the second financial compliance field examination on or about March 1, 2001, focussing on EEI's January 31, 2001, MFR. In the course of the examination, Association Staff identified further inaccuracies in the calculation of the securities concentration charge, as well as, other calculation errors demonstrating that the firm's RAC had been significantly overstated, resulting in an increased capital deficiency position.

In April 2001, the Alberta District Council imposed additional Early Warning Restrictions on EEI, due to specific identified concerns of the firm's viability, including the lack of a registered CFO.

EEI engaged a qualified CFO in approximately May of 2001. This individual's registration with the Association in the capacity of CFO became effective on October 31, 2001.

On August 7, 2001, the Association issued its 2001 Field Examination Report ("2001 FER"). The 2001 FER related to the period ending January 31, 2001, and identified 27 capital, records and internal control deficiencies, of which 10 were noted as significant. The relevant significant and repeated deficiencies included errors in the securities concentration charge calculation, errors in the weekly capital calculation and insufficient margin for a number of client accounts.

The issues of capital deficiency as of January 31, 2001, were rectified in February 2001 and no client accounts, monies or securities were at risk during the period of the capital deficiency.

Since November, 2002, EEI's systems and financial reporting have substantially improved and, as of the Association's 2003 financial compliance field examination, EEI demonstrated no material internal controls and/or books and records deficiencies.

Hartwell has acknowledged, as UDP, that he had an obligation to take all reasonable steps to ensure compliance with the Association's rules regarding capital and that he failed to do so in a timely manner. Further, EEI and Hartwell have agreed that the capital deficiencies and underlying financial compliance deficiencies, as well as the related failure of Hartwell in his role as UDP, constitute serious violations of the Association's Bylaws that are deserving of sanction.

Kenneth A. Nason
Association Secretary