

Re Everest

IN THE MATTER OF:

**The Rules of the Investment Industry Regulatory Organization of
Canada**

and

Christopher Everest

2019 IIROC 16

Investment Industry Regulatory Organization of Canada
Hearing Panel (Ontario District)

Heard: May 15, 2019, Toronto, Ontario

Decision: May 15, 2019

Written Decision: June 7, 2019

Hearing Panel:

Frederick H. Webber, Chair, Emily Jelic and Donald Lawson

Appearance:

Elissa Sinha, Enforcement Counsel

Gregory Temelini, for Christopher Everest

Christopher Everest (Respondent)

SETTLEMENT HEARING DECISION

SETTLEMENT AGREEMENT

¶ 1 This was a settlement hearing pursuant to a Settlement Agreement dated May 1, 2019, a copy of which is attached hereto (the "Settlement Agreement").

CONTRAVENTION

¶ 2 The respondent has admitted the following contravention:

Between February and November 2015, the Respondent, as CFO of Octagon Capital Corporation, failed to ensure that the Risk Adjusted Capital and financial circumstances of the Dealer Member were accurately reported, contrary to Dealer Member Rule 38.6(c).

AGREED PENALTIES

¶ 3 The Respondent agreed, as part of the Settlement Agreement, to:

- (a) pay a fine of \$10,000, payable within 30 days of acceptance of the Settlement Agreement by the hearing panel; and
- (b) a permanent ban from registration with IIROC.

PANEL'S OBLIGATION

¶ 4 Pursuant to IIROC Rule 8215 (5), a Hearing Panel has two options with respect to a settlement agreement. It may either accept the settlement agreement or reject it. As stated in *Milewski (Re)*, [1999] I.D.A.C.D. No. 17 and many other cases, in a settlement hearing, the panel "will tend not to alter a penalty that it considers to be within a reasonable range taking into account the settlement process and the fact that the parties have agreed. It will not reject a settlement unless it views the penalty as clearly falling outside a reasonable range of appropriateness"... and "will reflect the public interest benefits of the settlement process in its consideration of specific settlements."

¶ 5 IIROC counsel submitted, and the Respondent's counsel agreed, that the panel ought to accept the Settlement Agreement as the proposed resolution falls within the reasonable range of appropriateness having regard to the nature of the conduct admitted by the Respondent and IIROC's regulatory objective of protecting the public.

FACTS

¶ 6 The relevant facts are set out in Part III of the Settlement Agreement, and may be summarized as follows:

- (a) As Chief Financial Officer ("CFO") of Octagon Capital Corporation ("OCC"), the Respondent was responsible for monitoring and accurately reporting to IIROC the firm's Risk Adjusted Capital ("RAC") and financial circumstances;
- (b) Between February and November 2015, the Respondent did not accurately report OCC's RAC and financial circumstances. Instead he:
 - reported a management fee receivable charged monthly to OCC's parent company (the "Management Fee") as an allowable asset, even after being told by IIROC that such reporting was improper;
 - inflated the Management fee which increased OCC's income; and
 - on two occasions, reported the Management Fee on OCC's Monthly Financial Report ("MFR") to IIROC in a way that made it difficult for IIROC to identify that the fee in those months was larger than usual.
- (c) IIROC discovered the Respondent's actions in November 2015 and determined that OCC was capital deficient. IIROC then suspended OCC's membership and a bankruptcy order was made shortly thereafter.

CFO'S OBLIGATIONS

¶ 7 Under IIROC Rule 38.6(c):

"The Chief Financial Officer must monitor adherence to the Dealer Member's policies and procedures as necessary to provide assurance that the Dealer Member complies with the financial rules of [IIROC]."

The Respondent has admitted that he failed to carry out his obligations under this Rule.

CONSIDERATIONS IN ACCEPTING A SETTLEMENT

¶ 8 In previous cases, such as *Re Donnelly* 2016 IIROC 23, IIROC hearing panels have taken into account the following considerations when determining whether a proposed settlement should be accepted:

- (a) whether acceptance of the settlement agreement would be in the public interest and whether

- the penalty imposed will protect investors;
- (b) whether the settlement agreement is reasonable and proportionate, having regard to the conduct of the Respondent as set out in the settlement agreement;
 - (c) whether the settlement agreement addresses the issues of both specific and general deterrence;
 - (d) whether the settlement agreement will foster confidence in the integrity of the Canadian capital markets, in IIROC and in the regulatory process.

SPECIFIC FACTORS RE APPROPRIATENESS OF PENALTY

¶ 9 Factors that hearing panels frequently consider when determining whether a penalty is appropriate include the following:

- (a) the seriousness of the allegations proved against the Respondent;
- (b) the Respondent's past conduct, including prior sanctions;
- (c) the Respondent's experience and level of activity in the capital markets;
- (d) whether the Respondent recognizes the seriousness of the improper activity;
- (e) the harm suffered by investors as a result of the Respondent's activities;
- (f) the benefits received by the Respondent as a result of the improper activity;
- (g) the risk to investors and the capital markets in the jurisdiction, were the Respondent to continue to operate in capital markets in the jurisdiction;
- (h) the damage caused to the integrity of the capital markets in the jurisdiction by the Respondent's improper activities;
- (i) the need to deter not only those involved in the case being considered, but also any others who participate in the capital markets, from engaging in similar improper activity;
- (j) the need to alert others to the consequences of inappropriate activities to those who are permitted to participate in the capital markets; and
- (k) previous decisions made in similar circumstances.

¶ 10 These factors are cited in IIROC's Sanction Guidelines. The Guidelines are not mandatory or binding on the hearing panel, but provide a summary of the key factors upon which discretion can be exercised consistently and fairly. Many of the same factors that are listed above have been considered in previous decisions of IIROC hearing panels.

CONSIDERATION IN THIS CASE

¶ 11 The following factors were particularly relevant in reaching IIROC's Settlement Agreement with the Respondent.

(a) The nature of the misconduct

Even though the Respondent may have genuinely believed that he did not act dishonestly, he failed to comply with his obligations under IIROC Rule 38.6(c) which is a serious breach of the IIROC Rules.

(b) Benefits Received by the Respondent

The Respondent did not benefit, financially or otherwise from engaging in the misconduct at issue in

this proceeding.

(c) Respondent's Past Conduct including Prior Sanctions

The Respondent has not previously been the subject of IIROC disciplinary proceedings.

(d) Respondent's Recognition of the Seriousness of the Misconduct

By entering into the Settlement Agreement, the Respondent has accepted responsibility for his misconduct. He has also saved the IIROC the time, resources and expenses associated with a full disciplinary proceeding.

(e) Deterrence

The proposed penalties will act as a general deterrent and reinforce the message that a CFO's obligations under Rule 38.6(c) must be taken seriously. The proposed penalties will also act as a specific deterrent regarding the Respondent engaging in misconduct in the future.

(f) The Respondent's Ability to Pay

The Respondent provided IIROC with sworn evidence that he is experiencing financial hardship and is unable to pay a fine penalty greater than set out in the Settlement Agreement. He has not worked in the industry or had any employment since November 2015. The Respondent has acknowledged that, if not for his inability to pay, the monetary fine would have been significantly higher and he would have been required to contribute to the costs incurred by IIROC in this case.

This panel confirms that, but for the Respondent's inability to pay, it would have accepted in a settlement case, and would have imposed in a contested case, a much larger fine and costs.

(g) Previous Decisions Made in Similar Cases

This panel reviewed several cases which were referred to by IIROC counsel, and set out in IIROC's Settlement Book. Those cases support this panel's conclusion that the proposed resolution is within the reasonable range of appropriateness.

ORDER

¶ 12 At the conclusion of the hearing, this panel accepted the Settlement Agreement and signed a Settlement Agreement to that effect. A copy of that Settlement Agreement is attached.

DATED THIS 7 DAY OF June 2019.

Frederick H. Webber

Emily Jelich

Donald Lawson"

SETTLEMENT AGREEMENT

PART I - INTRODUCTION

1. The Investment Industry Regulatory Organization of Canada ("IIROC") will issue a Notice of Application to announce that it will hold a settlement hearing to consider whether, pursuant to Section 8215 of the Consolidated Enforcement, Examination and Approval Rules of IIROC, a hearing panel ("Hearing Panel") should accept the settlement agreement ("Settlement Agreement") entered into between the staff of IIROC ("Staff") and Christopher Everest ("Respondent").

PART II – JOINT SETTLEMENT RECOMMENDATION

2. Staff and the Respondent jointly recommend that the Hearing Panel accept this Settlement Agreement in accordance with the terms and conditions set out below.

PART III – AGREED FACTS

3. For the purposes of this Settlement Agreement, the Respondent agrees with the facts as set out in Part III of this Settlement Agreement.

Overview

4. As Chief Financial Officer (“CFO”) of Octagon Capital Corporation (“OCC”), the Respondent was responsible for monitoring and accurately reporting to IIROC the firm’s Risk Adjusted Capital (“RAC”) and financial circumstances.
5. Between February and November 2015, the Respondent did not accurately report his Dealer Member firm’s RAC and financial circumstances. Instead, the Respondent:
 - a) reported a management fee receivable charged monthly to OCC’s parent company (the “Management Fee”) as an allowable asset;
 - b) inflated the Management Fee, which increased OCC’s income; and
 - c) on two occasions, reported the Management Fee on OCC’s Monthly Financial Report (“MFR”) to IIROC in a way that made it difficult for IIROC to identify that the fee in those months was larger than usual;
6. IIROC discovered the Respondent’s actions in November 2015 and determined that OCC was capital deficient. IIROC took immediate steps to suspend the firm’s membership and a bankruptcy order was made shortly thereafter.

The Respondent

7. The Respondent, Christopher Everest, was the CFO of OCC, an IIROC Dealer Member, from 2009 to December 2015 when OCC’s membership was suspended. The Respondent has not been registered with IIROC since OCC was suspended.
8. The Respondent is not an accountant and has no formal accounting education.

OCC

9. OCC’s business focus was corporate finance and investment banking for institutional clients.
10. OCC was wholly owned by Octagon Capital Partners (“OCP”). When OCC required capital beyond the revenues it generated from its business, OCP provided additional funding. OCP and OCC had the same board of directors and management. Accordingly, the Respondent was CFO of OCP as well as OCC.
11. OCP maintained trading and non-trading accounts at OCC. Although fund transfers from OCP to OCC were supposed to be paid from OCP’s non-trading account, an improper practice had developed for OCC to debit OCP’s trading account.
12. In 2015, the OCP trading account held a large debit balance, which had been the case for years. OCC’s President and some of his family members guaranteed the outstanding debit balance.
13. In 2015, OCC was struggling financially. OCC reported operating losses throughout 2015.
14. On December 3, 2015, IIROC suspended OCC’s membership due to the capital deficiency. On December

4, 2015, OCC was adjudged bankrupt following a court application by the Canadian Investor Protection Fund.

Risk Adjusted Capital and Financial Monitoring by IIROC

15. RAC is a defined measure of a Dealer Member's capital that has been adjusted for regulatory purposes according to a specific formula. Dealer Member Rule 17.2 requires all Dealer Members to maintain a RAC greater than zero and a Dealer Member must immediately inform IIROC if it has a negative RAC. RAC is a factor in IIROC's prescribed tests for Early Warning, which may be triggered by a Dealer Member's capital, profitability and/or liquidity position.
16. Every month Dealer Members are required to file a MFR with IIROC. The MFR states the firm's RAC position and the results of the Early Warning tests for capital, profitability, and liquidity. The MFR allows IIROC's Financial & Operations Compliance Group ("FINOPS") to monitor the capital and solvency of its Dealer Members. The MFR is signed by the UDP and the CFO.
17. As CFO, the Respondent's primary responsibilities included monitoring OCC's RAC and accurately reporting the RAC and OCC's financial circumstances to IIROC in the MFR, and as otherwise required by FINOPS.
18. FINOPS conducts periodic examinations of each Dealer Member's financial records and operational controls and issues a report that identifies any deficiencies that require action.

The Management Fee

19. OCC regularly charged OCP the Management Fee as compensation for time that OCC employees spent on OCP. OCP was a holding company and its administrative, bookkeeping, and various other needs were filled by the Respondent and other OCC employees.
20. FINOPS required OCC to implement a formal agreement in respect of the Management Fee in its 2012/2013 examination. One of the reasons for requiring an agreement was to provide some certainty regarding the amounts that would be charged.
21. OCC and OCP executed a Management Agreement dated December 27, 2012 (the "Management Agreement") which recognized certain services OCC provided to OCP and provided for OCP to pay a base annual fee of \$240,000 "plus reimbursements as reasonably determined on an annual basis".
22. OCC charged the following Management Fee from 2011 to 2015:

| Year | Management Fee |
|-----------------------|----------------|
| 2011 | \$400,000 |
| 2012 | \$380,000 |
| 2013 | \$400,000 |
| 2014 | \$320,000 |
| 2015 (Jan to Sept) | \$690,000 |

(a) Reporting the Management Fee as an Allowable Asset

23. OCC reported its Management Fee as an allowable asset on the MFR filed monthly by the Respondent. This increased OCC's RAC by the amount of the Management Fee. However, this accounting was incorrect since OCP never actually paid the Management Fee.
24. The Respondent would direct OCC's bookkeeping Staff to "pay" the Management Fee by debiting OCP's

trading account and crediting OCC. However, increasing the debit in a client account was not payment since it did not increase OCC's capital.

25. Accordingly, the Management Fee was a receivable owed by an affiliated company that should have been recorded as a non-allowable asset on the MFR. A non-allowable asset is RAC neutral and would not increase OCC's capital.
26. In February 2015, FINOPS issued the report for its 2014/2015 examination of OCC (the "2014/2015 Report") which reviewed OCC's September 2014 MFR. FINOPS specifically directed OCC to report its Management Fee receivable from OCP as an advance to affiliates in the non-allowable assets category. FINOPS noted that due to the misreporting of the Management Fee as an asset, OCC's RAC was overstated by \$260,000 in September 30, 2014, although it remained positive. FINOPS identified OCC's treatment of the Management Fee as a "significant" deficiency.
27. The Respondent and the UDP received a copy of the 2014/2015 Report and OCC acknowledged that going forward it would report the Management Fee as a non-allowable asset until it was received and paid for by OCP.
28. However, the Respondent continued to record the Management Fee as an asset on behalf of OCC, even though it was never paid. Accordingly, OCC's reported RAC continued to be overstated until the next FINOPS examination in November 2015. The Respondent believed that the guarantees addressed the debit increases in the OCP trading account which were made to offset the Management Fee and, more generally, the capital adequacy of OCC.
29. The table at Schedule "A" identifies OCC's Management Fee in 2014/2015 and compares the RAC reported by the Respondent on OCC's MFRs to the adjusted RAC if the Management Fee was treated as directed by FINOPS. If OCC and the Respondent had followed FINOPS' direction from the 2014/2015 Report issued in February 2015, OCC would have been capital deficient for much of 2015.

(b) Increased Management Fee

30. As described above, the Management Agreement provided for a base Management Fee of \$240,000, or approximately \$20,000 per month.
31. From 2011 to 2014, the Management Fee ranged from \$300,000 to \$400,000 per year. However, in the first nine months' of 2015, OCC charged a Management Fee of \$690,000.
32. The Respondent prepared daily capital calculations to estimate OCC's RAC and the results of the Early Warning tests, which he shared with the UDP. Towards the end of the month, the Respondent would add additional amounts to the calculation to achieve a purported capital position that did not trigger Early Warning. At the end of the month, the Respondent instructed OCC's comptroller how much to charge OCP for the Management Fee and the comptroller debited the OCP trading account and credited OCC.
33. The Respondent admitted that he adjusted the Managements Fee to avoid triggering early warning. He used the term "reversed engineering" to describe his process of setting the Management Fee while doing the capital estimates.

(c) Unusual Reporting of the Management Fee

34. Typically, the Respondent reported the Management Fee on OCC's MFR at Statement E Line 19 "Fees". The "Fees" would only include other minor items so FINOPS could easily identify the Management Fee charged by reviewing that line item.

35. In March and April 2015, OCC charged a significantly larger Management Fee than it had in the past (\$130,000 and \$140,000 respectively). However, the Respondent did not report the Management Fee as he had previously done. Instead he split it into two separate entries on the MFRs for March and April 2015. This made it difficult for FINOPS to detect..
36. The Respondent shared the MFRs with the UDP before they were submitted to IIROC.

Capital Deficiency

37. In November 2015, FINOPS undertook a routine examination of OCC that focused on the September 2015 MFR. In the course of that examination, FINOPS uncovered the significant Management Fee charged since its last examination and determined that OCC continued to report the Management Fee as an allowable asset, contrary to the specific direction given in the 2014/2015 Report.
38. FINOPS determined that the Management Fee for 2015 of \$690,000 had been incorrectly recorded as an asset with the result that RAC was overstated by that amount as well as the amount of a doubtful GST receivable. FINOPS determined that OCC was capital deficient in the amount of (\$351,000).
39. In fact, further investigation revealed that OCC had negative RAC and had been capital deficient for much of 2015. The effect of the Respondent's treatment of the Management Fee was to obscure OCC's true capital position from IIROC and facilitate OCC's avoidance of Early Warning and the requirement to maintain a positive RAC.
40. On or about November 25, 2015, FINOPS advised the Respondent of the capital deficiency. He stopped returning phone and email communications and OCC advised FINOPS that the Respondent was not expected to return to work.
41. OCC did not remedy the capital deficiency and indicated it would not continue operations. Accordingly, on December 4, 2015, IIROC suspended OCC's membership.

Mitigating Factors

42. The Respondent genuinely believed that the guarantees addressed the debit increases in the OCP trading account which were made to offset the Management Fee and, more generally, the capital adequacy of OCC. The Respondent did not benefit financially or otherwise from his admitted misconduct.
43. The Respondent has not previously been subject to IIROC disciplinary proceedings.

Inability to Pay

44. The Respondent has not worked in the industry or had any employment since November 2015.
45. The Respondent has provided Staff with sworn evidence substantiating that he is experiencing financial hardship and unable to pay a fine greater than the amount recommended.
46. The Respondent acknowledges that, if not for his inability to pay, the monetary fine imposed against him would have been significantly higher and that he would have been required to contribute to the costs that IIROC has incurred in this matter.

PART IV – CONTRAVENTIONS

47. By engaging in the conduct described above, the Respondent committed the following contraventions of IIROC's Rules:

Between February and November 2015, the Respondent, as CFO of Octagon Capital Corporation, failed to ensure that the Risk Adjusted Capital and financial circumstances of the Dealer Member were accurately reported, contrary to Dealer Member Rule 38.6(c).

PART V – TERMS OF SETTLEMENT

48. The Respondent agrees to the following sanctions and costs:
 - a) Fine of \$10,000; and
 - b) Permanent ban from registration with IIROC.
49. If this Settlement Agreement is accepted by the Hearing Panel, the Respondent agrees to pay the amounts referred to above within 30 days of such acceptance unless otherwise agreed between Staff and the Respondent.

PART VI – STAFF COMMITMENT

50. If the Hearing Panel accepts this Settlement Agreement, Staff will not initiate any further action against the Respondent in relation to the facts set out in Part III and the contraventions in Part IV of this Settlement Agreement, subject to the provisions of the paragraph below.
51. If the Hearing Panel accepts this Settlement Agreement and the Respondent fails to comply with any of the terms of the Settlement Agreement, Staff may bring proceedings under Rule 8200 against the Respondent. These proceedings may be based on, but are not limited to, the facts set out Part III of this Settlement Agreement.

PART VII – PROCEDURE FOR ACCEPTANCE OF SETTLEMENT

52. This Settlement Agreement is conditional on acceptance by the Hearing Panel.
53. This Settlement Agreement shall be presented to a Hearing Panel at a settlement hearing in accordance with the procedures described in Sections 8215 and 8428, in addition to any other procedures that may be agreed upon between the parties.
54. Staff and the Respondent agree that this Settlement Agreement will form all of the agreed facts that will be submitted at the settlement hearing, unless the parties agree that additional facts should be submitted at the settlement hearing. If the Respondent does not appear at the settlement hearing, Staff may disclose additional relevant facts, if requested by the Hearing Panel.
55. If the Hearing Panel accepts the Settlement Agreement, the Respondent agrees to waive all rights under the IIROC Rules and any applicable legislation to any further hearing, appeal and review.
56. If the Hearing Panel rejects the Settlement Agreement, Staff and the Respondent may enter into another settlement agreement or Staff may proceed to a disciplinary hearing based on the same or related allegations.
57. The terms of this Settlement Agreement are confidential unless and until this Settlement Agreement has been accepted by the Hearing Panel.
58. The Settlement Agreement will become available to the public upon its acceptance by the Hearing Panel and IIROC will post a full of copy of this Settlement Agreement on the IIROC website. IIROC will also publish a summary of the facts, contraventions, and the sanctions agreed upon in this Settlement Agreement.
59. If this Settlement Agreement is accepted, the Respondent agrees that neither he nor anyone on his behalf, will make a public statement inconsistent with this Settlement Agreement.
60. The Settlement Agreement is effective and binding upon the Respondent and Staff as of the date of its acceptance by the Hearing Panel.

PART VIII – EXECUTION OF SETTLEMENT AGREEMENT

- 61. This Settlement Agreement may be signed in one or more counterparts which together will constitute a binding agreement.
- 62. A fax or electronic copy of any signature will be treated as an original signature.

DATED this “1st” day of “May”, 2019.

“Greg Temelini”
Witness

“Christopher Everest”
CHRISTOPHER EVEREST

“Ricki Ann Newmarch”
Witness

“Elissa Sinha”
Elissa Sinha
Enforcement Counsel on behalf of Enforcement
Staff of the Investment Industry Regulatory
Organization of Canada

The Settlement Agreement is hereby accepted this “15” day of “May”, 2019 by the following Hearing Panel:

Per: “Fred Webber”
Panel Chair

Per: “Emily Jelich”
Panel Member

Per: “Donald Lawson”
Panel Member

Schedule “A” – OCC Management Fees and Adjusted RAC

| Month | Management Fees (\$) | Accumulated Management Fees (\$) | Reported RAC (\$) | Adjusted RAC (\$) |
|--------------|-----------------------------|---|--------------------------|--------------------------|
| January-15 | 40,000 | 40,000 | 362,000 | 322,000 |
| February-15 | 40,000 | 80,000 | 313,000 | 233,000 |
| March-15 | 130,000 | 210,000 | 318,000 | 108,000 |
| April-15 | 140,000 | 350,000 | 335,000 | -15,000 |
| May-15 | 20,000 | 370,000 | 187,000 | -183,000 |
| June-15 | 60,000 | 430,000 | 517,000 | 87,000 |
| July-15 | 120,000 | 550,000 | 501,000 | -49,000 |
| August-15 | 20,000 | 570,000 | 443,000 | -127,000 |
| September-15 | 120,000 | 690,000 | 381,000 | -309,000 |
| Total | 690,000 | | | |