

Re Chung

IN THE MATTER OF:

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

and

Darin Lee Chung (Respondent)

2015 IIROC 40

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

Heard: October 6, 2015
Decision: November 9, 2015

Hearing Panel:

Joseph A. Bernardo (Chair), Bradley Doney and Barbara Fraser

Appearances:

Paul Smith, Enforcement counsel

Stephen Jackson, Respondent's counsel

REASONS FOR DECISION

¶ 1 On October 6, 2015, a proposed settlement agreement between the Investment Industry Regulatory Organization of Canada (IIROC) and the Respondent (Settlement Agreement) was presented for acceptance to the Hearing Panel in closed session.

Procedural issue

¶ 2 The usual practice is that a settlement agreement is brought forward for a Hearing Panel's consideration only after the parties have executed it. In this case, the Settlement Agreement was submitted unsigned and without the Respondent being present.

¶ 3 Respondent's counsel indicated that logistical reasons prevented his client from either attending the hearing or executing the Settlement Agreement beforehand and, indeed, that he had not yet had an opportunity read it. Counsel informed the Hearing Panel that his client nonetheless understood and accepted the Settlement Agreement, as he had explained its terms and their significance to the Respondent in a telephone conversation and that his client had indicated his assent.

¶ 4 Respondent's counsel and IIROC Enforcement counsel were agreed that, in the circumstances, this oral endorsement provided a sufficient basis for the Hearing Panel to receive the Settlement Agreement and hear their respective submissions.

¶ 5 The Settlement Agreement in this case concerns the Respondent's conduct when he was an Approved Person. A Hearing Panel's jurisdiction to accept or reject settlement agreements between an Approved Person and Enforcement staff is conferred by IIROC Dealer Member Rule 20.36. Under the Rule, a settlement agreement becomes effective upon acceptance by a Hearing Panel and the Approved Person is deemed to have been penalized under IIROC Dealer Member Rule 20.33.

¶ 6 Rule 20.33 is the provision that confers on Hearing Panels the authority to impose penalties on an

Approved Person at the conclusion of a disciplinary hearing. A Hearing Panel may exercise this power only after first concluding that the respondent has failed to comply with securities legislation, the Rules, or a term of an agreement or undertaking made with IIROC.

¶ 7 A Hearing Panel is likewise called upon to assess the legal and policy significance of the facts of a case when it is asked to review a settlement agreement. Before a Panel can accept a settlement, it must be satisfied that the agreement's legal conclusions are an accurate interpretation of the facts and, if so, that the proposed outcome is not an unreasonable regulatory response to the misconduct. In order to undertake this exercise, a Hearing Panel must receive from the parties a recitation of their points of agreement that is clear, specific, and certain. This is why, as a general matter, the full particulars of a settlement should be consigned to a written agreement that is executed before it is submitted to a Hearing Panel for approval.

¶ 8 This matter was originally scheduled to be heard in a disciplinary hearing. Shortly before it was due to commence, the Hearing Panel received notice that the matter would proceed as scheduled, but by way of a settlement hearing. It appears from Respondent counsel's remarks that obtaining and submitting an executed Settlement Agreement would likely have required scheduling a settlement hearing for a later time, pending the Respondent's availability. Following normal practice, therefore, would have introduced an element of delay and, possibly, greater uncertainty in disposing of the matter.

¶ 9 Regulatory proceedings are intended to, and should, proceed as expeditiously as possible. Accordingly, the Hearing Panel granted the joint request of counsel that it receive the unsigned Settlement Agreement and hear their submissions. The Panel informed counsel, however, that the rendering of a decision would be deferred pending receipt of the Settlement Agreement in executed form.

¶ 10 On October 23, 2015, IIROC's National Hearing Coordinator provided the Hearing Panel with a copy of the Settlement Agreement signed by the Respondent and by Enforcement counsel on behalf of IIROC.

FACTS

¶ 11 The Respondent was first registered in 2001, when he began employment with Raymond James Ltd. in Delta, British Columbia as a registered representative. His employment ceased in March 2012 and he has not been registered with any other Dealer Member Firm since that time.

Client background

¶ 12 In 2005, a client opened cash accounts for which the Respondent was the responsible registered representative.

¶ 13 The client was born in 1937. His intention was to generate a 5 or 6% annual rate of return by investing approximately \$200,000 in a low risk portfolio.

¶ 14 The New Client Application Form (NCAF) for the cash accounts identified the investment objectives for the accounts as 90% growth and 10% speculative, and the client's risk tolerance as 90% medium and 10% high. It indicated that he worked part-time and had net liquid assets of \$200,000 and net fixed assets of \$800,000.

¶ 15 In 2008, the client opened a registered retirement account on the basis of the same financial information, investment objectives, and risk tolerance previously indicated in 2005 for the cash accounts.

Margin trading

¶ 16 In June 2009, the client, now aged 71 or 72, opened margin accounts denominated in both Canadian and United States currencies. He did this on the Respondent's recommendation. The Respondent did not explain to the client either how interest is charged on such accounts or how the risks associated with cash and margin accounts differ.

¶ 17 The NCAF for the margin accounts identified the investment objectives for the accounts as 25% growth and 75% speculative, and the client's risk tolerance as 80% medium and 20% high. A year later, the client's investment profile for these accounts was amended. The speculative component of the investment objectives was increased to 80%, while the client's tolerance for high risk investments was increased to 30%.

¶ 18 At the time the margin accounts were opened, it appears that the client's combined portfolio in his cash and registered retirement accounts had a net asset value of approximately \$240,000.

¶ 19 In the three year period from 2009 to 2012, the Respondent recommended and implemented trading in the margin accounts.

¶ 20 By September 2009, three months after the margin accounts were opened, the client's margin debt exceeded \$200,000. Continued margin trading resulted in more debt and a worsening of the client's net investment position. The client's accumulation of margin debt peaked in March 2011, with the client holding \$566,000 in debt against \$239,000 in total portfolio equity. In the 24 month period from January 2010 through to December 2011, the client's average monthly margin debt was \$356,000 and resulted in total interest charges of \$32,000.

Borrowing from the Client

¶ 21 In June 2009, at the same time as he was advising his client to open margin accounts, the Respondent borrowed money from him. The Respondent borrowed the funds without seeking or receiving the permission of his firm and was aware that the loan arrangement was contrary to IIROC Rules.

¶ 22 The Respondent borrowed \$10,000 from the client, providing him with a signed note confirming that he would repay the funds, together with an additional \$1000, within 30 days. The Respondent failed to do so.

¶ 23 In July 2012, more than three years after borrowing the funds, the Respondent provided the client with a cheque in the amount of \$1700 that he purported had been issued by his sister. The cheque was not honoured when the client attempted to deposit it.

¶ 24 In August 2012, the Respondent gave the client a bank draft in the amount of \$2,700 that he purported had been issued by his aunt.

¶ 25 As of the date of the Settlement Agreement, the unpaid \$7,300 balance of the principal loan amount and the interest payable remained outstanding.

MISCONDUCT

¶ 26 As a registered representative, the Respondent was required by IIROC Dealer Member Rule 1300.1 (q) to provide the client with recommendations that took into consideration the client's financial situation, investment knowledge, investment objectives and time horizon, risk tolerance and the composition and risk level of his investment portfolio.

¶ 27 As a registered representative, the Respondent was also subject to IIROC Dealer Member Rule 29.1, which placed him under a duty to observe high ethical standards and to refrain from business conduct that was unbecoming or detrimental to the public interest.

¶ 28 The Respondent acknowledges in the Settlement Agreement that his conduct was contrary to Rules 1300.1(q) and 29.1.

FACTORS CONSIDERED

¶ 29 In exercising its discretion under Rule 20.36, the Hearing Panel considered the following factors:

1. The purpose of the IIROC disciplinary process is to protect the investing public and the integrity of the securities industry and the capital market it serves.
2. The disciplinary process is more effective when enforcement outcomes are obtained without the expense and delay of litigation.
3. A settlement agreement represents a compromise negotiated by the parties who are most familiar with the strengths, weaknesses, and nuances of a case.
4. Enforcement outcomes are reasonable and appropriate when they are timely, efficient, fair, and proportionate to the harm caused by the misconduct.

5. For any given instance of misconduct, the protective purpose of the disciplinary process is capable of being achieved by a range of reasonable and appropriate enforcement outcomes.
6. The sanctions proposed by a settlement agreement should be accepted if they do not fall outside the range of enforcement outcomes that are reasonable and appropriate for the misconduct in question.
7. The Respondent has not been previously disciplined.

DECISION

¶ 30 The Respondent's client sought to earn annual returns of 5 to 6% on his investments.

¶ 31 The NCAFs for his cash and registered retirement accounts were consistent with that goal. They disclosed a preference for obtaining growth through medium risk investments, a minimal interest in speculative investments, and an overall low tolerance for risk. This investment profile was objectively appropriate for a senior citizen with a relatively limited amount of investment capital at his disposal.

¶ 32 Although the NCAF for the client's margin accounts reflected the level of risk inherent in such accounts, it was neither reasonable nor appropriate for the Respondent to recommend margin trading to his client without specifically advising him of the nature and higher level of the risks involved.

¶ 33 Extensive margin trading was, in any case, inconsistent with his client's age and financial situation. Nonetheless, the Respondent recommended and facilitated transactions that exposed the client to margin debt levels that, for all practical purposes, overwhelmed the solvency of his overall portfolio.

¶ 34 The Respondent's recommendation that his client engage in margin trading and the extent to which he facilitated it was a breach of his client suitability obligations under Rule 1300.1(q).

¶ 35 IIROC Dealer Member Rule 43 was introduced in 2013 to explicitly prohibit Approved Persons and other employees of Dealer Members from directly or indirectly engaging in personal financial dealings with clients, except in certain limited and controlled circumstances. A registered representative's obligation to his client, however, has always included an ethical duty to avoid financial conflicts of interest.

¶ 36 The Respondent entered into a conflict of interest with his client when he borrowed money from him in 2009 and then failed to meet the terms of the loan, all while serving as the client's registered representative. He neglected to seek the consent of his employer before entering into personal financial dealings with a firm client, which by itself was a failure to meet conduct standards. In these respects, the Respondent failed to meet the high ethical standards imposed by Rule 29.1.

¶ 37 The sanctions contemplated by the Settlement Agreement are:

1. \$40,000 fine and \$5000 costs.
2. A five year suspension from registration in any capacity.
3. Future registration being subject to
 - (a) The Respondent having repaid, or otherwise discharging, the debt owed to his former client.
 - (b) Strict supervision for the first six months of registration, followed by six months close supervision.

¶ 38 The Respondent's failure to meet his professional obligations to one client was his only misconduct during an eleven year career as a registered representative. A five year suspension from registration for, in effect, an anomalous episode might therefore give pause, except for the extent of the client's losses and the fact that the Respondent's continuing failure to repay the debt he owes his former client perpetuates the hardship imposed by the original misconduct. For the same reason, any future registration being made subject to the Respondent first discharging the debt is an entirely appropriate and well-calibrated regulatory response to the particular circumstances of this case.

¶ 39 Taking into account the agreed facts of the case, the Hearing Panel finds that the sanctions agreed upon by IIROC Enforcement staff and the Respondent are not unreasonable. The Settlement Agreement is therefore accepted.

Dated at Vancouver, British Columbia, this 9th day November, 2015.

Joseph A. Bernardo (Chair)

Bradley Doney

Barbara Fraser

SETTLEMENT AGREEMENT

I. INTRODUCTION

1. IIROC Enforcement Staff (“Staff”) and Darin Lee Chung (the “Respondent”) consent and agree to the settlement of this matter by way of this agreement (the “Settlement Agreement”).
2. The Enforcement Department of IIROC has conducted an investigation (the “Investigation”) into the conduct of the Respondent.
3. The Investigation discloses matters for which the Respondent may be disciplined by a hearing panel appointed pursuant to IIROC Transitional Rule No.1, Schedule C.1, Part C (the “Hearing Panel”).

II. JOINT SETTLEMENT RECOMMENDATION

4. Staff and the Respondent jointly recommend that the Hearing Panel accept this Settlement Agreement.
5. The Respondent admits to the following contraventions of IIROC Dealer Member Rules, Guidelines, Regulations or Policies:
 - (a) From January, 2010 through December 2011, the Respondent acted contrary to IIROC Dealer Member Rule 1300.1 (q) by making unsuitable investment recommendations to a client.
 - (b) From June, 2009 through August, 2012 the Respondent acted contrary to IIROC Dealer Member Rule 29.1 by engaging in personal financial dealings with a client when he borrowed money from that client.
6. Staff and the Respondent agree that the following terms of settlement:
 - (a) A fine in the amount of forty thousand dollars (\$40,000);
 - (b) A five year suspension from registration in any capacity with IIROC;
 - (c) At the end of the five year period of suspension, it shall be a precondition of any future registration that the Respondent demonstrate to the satisfaction of IIROC Staff that he has fully repaid the debt to the client or received a discharge from the client or his estate;
 - (d) Any future registration of the Respondent shall also be subject to a period of six months strict supervision followed by a period of six months close supervision in addition to any supervision requirements imposed on new registered representatives.
7. The Respondent agrees to pay costs to IIROC in the sum of five thousand dollars (\$5,000).

III. STATEMENT OF FACTS

(i) Acknowledgment

7. Staff and the Respondent agree with the facts set out in this Section III and acknowledge that the terms of the settlement contained in this Settlement Agreement are based upon those specific facts.

(ii) Factual Background

Overview

8. These particulars relate to the period of time from June 2009 through March 2012 when the Respondent was a Registered Representative (“RR”) working at Raymond James Ltd. (“Raymond James”) in Delta, British Columbia. During that period, the Respondent recommended extensive use of margin for a 72 year old client for whom margin was not suitable. The Respondent also engaged in personal financial dealings with the same client by borrowing \$10,000 from him. Despite promising to repay the full amount plus interest within 30 days, no amount of money was paid back to the client until August 2012, after the Respondent was no longer registered at Raymond James. The bulk of that loaned amount remains unpaid by the Respondent.

The Respondent

9. The Respondent was first registered in 2001 and worked continuously at Raymond James in Delta, British Columbia until March 2012. He has not been registered with any other Dealer Member Firm since that time.

The Client and the Accounts

10. GK (the “Client”) is a British Columbia resident who was born in 1937. In 2005, the Client opened cash accounts at Raymond James with the Respondent as the RR responsible for the accounts. The Client planned to invest approximately \$200,000 and wanted a low risk portfolio that would generate a 5% or 6% annual rate of return.
11. The New Client Application Form (“NCAF”) for the accounts opened in 2005 indicated that the Client’s net liquid assets were \$200,000 and that he worked part time. The NCAF also indicated that the Client’s net fixed assets were \$800,000. It listed the Client’s account objectives as 90% Growth and 10% Speculative and the Client’s risk tolerance as 90% Medium and 10% High.
12. In 2008 a Registered Retirement account was added with the same financial information and the same listed account objectives and risk tolerance.
13. In June 2009, at the Respondent’s recommendation, the Client opened margin accounts denominated in both Canadian and United States currencies. Although he recommended that the Client open a margin account, the Respondent did not advise the Client how a margin account differed from a cash account from a risk perspective and did not explain to the Client how interest was charged in a margin account.
14. The NCAF for the margin accounts listed the Client’s account objectives as 25% Growth and 75% Speculative and the Client’s risk tolerance as 80% Medium and 20% High. A year later these objectives were changed to 80% Speculative and the risk tolerance was increased to 30% High.

Borrowing from the Client

15. At the same time that he recommended a margin account for the Client, in June 2009, the Respondent met with and arranged to borrow \$10,000 from the Client. The Respondent promised the Client that he would repay \$11,000 within 30 days and gave him a signed note to that effect.
16. At the time that he borrowed the money from the Client, the value of the Respondent’s own investment accounts at Raymond James totaled less than \$100.
17. The Respondent did not seek or receive permission from any supervisor at Raymond James to enter into personal financial dealings with any client and he knew that such a loan arrangement was contrary to IIROC rules.

Failure to repay loan

18. More than three years passed before the Respondent took any action to repay the loan.
19. In July 2012, the Respondent gave the Client a cheque for \$1,700. The cheque was payable to the Client but was not from the Respondent. It was from another individual whom the Respondent claimed was his

sister. The Client attempted to deposit this cheque to his account but the cheque was not honoured by the bank. The Client was, therefore, left without any repayment.

20. In August 2012, the Respondent gave the Client a bank draft for \$2,700. The bank draft was drawn from the account of another individual, not the Respondent. The Respondent claimed that this individual was his aunt.
21. As of the date of this Settlement Agreement, the Respondent has not paid the Client \$7,300 of the principal amount of the loan or any interest since he obtained the loan in June 2009.

Use of Margin

22. After opening the margin accounts in June 2009, the Client immediately began accumulating significant margin debt. By September 2009, the margin debt was more than \$200,000 at a time when the equity value of the combined assets contained in all of the Client's non registered accounts was approximately the same amount. Except for approximately \$40,000 contained in his Registered Retirement account, this amount was essentially the Client's entire portfolio.
23. For more than three years the Respondent continued to recommend and use margin in the Client's accounts beyond a level that could be considered reasonable for the Client.
24. In the 24 month period from January 2010 through December 2011 the average monthly margin debt was \$356,000. During this period the client was charged a total of \$32,000 in interest.
25. In the 6 month period from February 2011 through July 2011 the average monthly margin debt was \$497,000 when the average account equity during the same period was \$231,000.
26. At its peak, at the end of March, 2011 the Client's account had \$566,000 of margin debt and assets worth only \$239,000.
27. The extensive use of margin was not suitable for the Client. It exposed the Client's accounts to risk that the Client did not want or need and exacerbated losses in the accounts.
28. After July, 2011 the value of the Client's accounts declined significantly. By the end of December, 2012 the Client's account equity had been reduced to \$62,000 which was less than half of its original value.

Mitigating Factors

29. The Respondent has not previously been subject to disciplinary sanction.

IV. TERMS OF SETTLEMENT

30. This settlement is agreed upon in accordance with IIROC Dealer Member Rules 20.35 to 20.40, inclusive and Rule 15 of the Dealer Member Rules of Practice and Procedure.
31. The Settlement Agreement is subject to acceptance by the Hearing Panel.
32. The Settlement Agreement shall become effective and binding upon the Respondent and Staff as of the date of its acceptance by the Hearing Panel.
33. The Settlement Agreement will be presented to the Hearing Panel at a hearing ("the Settlement Hearing") for approval. Following the conclusion of the Settlement Hearing, the Hearing Panel may either accept or reject the Settlement Agreement.
34. If the Hearing Panel accepts the Settlement Agreement, the Respondent waives his right under IIROC rules and any applicable legislation to a disciplinary hearing, review or appeal.
35. 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 in relation to the matters disclosed in the Investigation.

36. The Settlement Agreement will become available to the public upon its acceptance by the Hearing Panel.
37. Staff and the Respondent agree that if the Hearing Panel accepts the Settlement Agreement, they, or anyone on their behalf, will not make any public statements inconsistent with the Settlement Agreement.
38. Unless otherwise stated, any monetary penalties and costs imposed upon the Respondent are payable immediately upon the effective date of the Settlement Agreement.
39. Unless otherwise stated, any suspensions, bars, expulsions, restrictions or other terms of the Settlement Agreement shall commence on the effective date of the Settlement Agreement.

AGREED TO by the Respondent at Vancouver, British Columbia, this 9 day of October, 2015.

“Witness”

WITNESS

“David Lee Chung”

RESPONDENT

AGREED TO by Staff at Vancouver, British Columbia, this 6th day of October, 2015.

“Witness”

WITNESS

“Paul Smith”

PAUL SMITH

Senior Enforcement Counsel on behalf of Staff of
the Investment Industry Regulatory Organization of
Canada

ACCEPTED at Vancouver, British Columbia, this _____ day of October, 2015, by the following Hearing Panel:

Per: “Joseph Bernardo”
Joseph Bernardo, Chair

Per: “Brad Doney”
Bradley Doney

Per: “Barbara Fraser”
Barbara Fraser

Copyright © 2015 Investment Industry Regulatory Organization of Canada. All Rights Reserved.