Team Assignment: Case Study 2

**2024F FIN 4203 1 [B103] Investments Conduct and Compliance**

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Group 4

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**Final due date:**

Your group has been assigned a disciplinary case that either has been or is currently being dealt with by the IIROC. Carefully read all the relevant details of your case.

Refer to all the material that we have studied so far in the CPH course, as well as other relevant information that you learned in previous securities related courses at the college.

Discuss what caused the events described in this case to lead to this disciplinary process.

Identify the IIROC Dealers Members Rules that have been violated.

Be sure to discuss how the (alleged) offender should have acted/behaved in their particular situation to avoid the action being taken by the IIROC.

The IIROC disciplinary case that you have been assigned is as follows:

The Respondent was a registered representative with IIROC from February 10, 1998, until February 24, 2016. 5. During this period, the Respondent was, among others, employed with ABC Securities (ABC), until his dismissal on February 24, 2016.

Since February 24, 2016, the Respondent is no longer employed with any IIROC Dealer Member.

On January 28, 2016, the client LC contacted the Respondent by telephone to have the latter purchase shares in Rona Inc. (Rona) for his account, for a value of $30,000.

At around 13:10 that same day, the Respondent therefore proceeded to purchase 2,500 shares in Rona on behalf of his client LC, at an average cost of $11.81 per share.

At around 13:20, the Respondent proceeded to purchase 5,000 Rona shares for his own account, at an average cost of $11.81 per share.

At around 14:15, the Respondent had a discussion with his client LC, during which the latter allegedly informed him of the reasons why he had decided to purchase Rona shares at that time.

In addition to the explanations of the client LC’s checks and analyses of Rona, one of the reasons invoked by the latter is that he had learned that a due diligence audit of Rona had allegedly been conducted recently.

Until that moment, the Respondent had never, since 2015, purchased Rona shares for his own account, nor recommended the purchase of this security to his clients. The client DB

The Client DB

On January 29, 2016, at a prescheduled meeting with his client DB, the Respondent recommended to the latter that he purchase shares in Rona.

During this meeting, the Respondent and DB communicated with LC, as the latter was better able to answer some of DB’s questions on this investment opportunity.

During this discussion, LC mentioned that there were apparently a few rumours circulating about the issuer Rona.

DB ultimately accepted the Respondent’s recommendation, who proceeded that same day to purchase 4,000 shares at an average cost of $11.99 per share. The clients MB and GO

The Clients MB and GO

Still on January 29, 2016, the Respondent met with his client GO in his office.

GO is MB’s spouse and has an Authorization to Trade in her account.

At this prescheduled meeting, the Respondent recommended the purchase of Rona shares to GO.

The Respondent proceeded that same day to purchase 1,700 shares in GO’s TFSA account, at an average cost of $12.29 per share.

The Respondent also purchased 1,700 shares in MB’s TFSA account, at an average cost of $12.30 per share, in accordance with the instruction given in this regard by GO, pursuant to his Authorization to Trade in his spouse’s account.

For both GO and MB, the cost of purchasing these Rona shares represented, at the time, the maximum contribution permitted in their respective TFSA accounts. The client DG

The Client DG

On February 2, 2016, the Respondent met with his client DG at the latter’s home.

During this prescheduled meeting, the Respondent recommended the purchase of Rona shares to DG.

The Respondent proceeded that same day to purchase 2,000 shares, at an average cost of $11.67 per share. The February 3, 2016, announced.

The February 3, 2016 Announcement

On the morning of February 3, 2016, Lowe’s Inc.’s offer to purchase Rona was publicly announced.

The Rona share price, which had closed at $11.77 the day before, stood at $23.44 when the markets opened on February 3, 2016.

That same day, after checking with ABC Compliance, the Respondent proceeded to sell the Rona shares purchased previously by himself and his clients LC, DB, GO, MB and DG.

**Overview**

The above case study focuses on a disciplinary case filed by the Investment Industry Regulatory Organization of Canada against an ABC Securities registered representative. The research methodology is based on a review of the IIROC Dealer Membership Rules.

Events from January 28, 2016 through February 2, 2016 that involved the Respondent led to allegations of improper trading relating to insider information, conflict of interest, and suitability.

The sequence of events involved the Respondent purchasing shares of Rona Inc. for their own account and recommending similar investments to clients without proper due diligence. The announcement on February 3, 2016, of Lowe’s Inc.'s offer to purchase Rona at a significantly higher price raised red flags about the timing and propriety of the Respondent’s actions.

**I) Particulars of Facts Giving Rise to Disciplinary Action**

1. Trading on Possible Insider Information

- Respondent, on January 28, 2016, traded on the client LC's information with respect to a due diligence audit on Rona, which may have constituted non-public material information.

- Respondent purchased 5,000 Rona shares in his own account shortly after executing the purchase for LC.

2. Conflict of Interest

- The respondent had put himself in a conflict-of-interest position when he purchased shares of Rona before recommending the same to the other clients. This is a conflict of interest.

3. Inadequate Disclosure and Suitability Concerns

- Recommendations to DB, MB, GO, and DG to purchase Rona shares were made without adequately disclosing the speculative nature of the investment.

- No evidence that due diligence was performed to confirm the Rona shares were suitable for each client's individual risk tolerance.

4. Rapid Sale of Shares upon Announcement - Respondent, for his own account and for his clients', sold shares upon announcement on February 3, 2016, when the price of Rona shares jumped, giving rise to a concern of opportunistic selling.

**ii) What the Respondent Should Have Done to Avoid Disciplinary Proceedings**

1. Avoid Personal Transactions Where There is Potential Insider Information

- Upon learning that Rona was going to conduct a due diligence audit, the Respondent should not have purchased shares in any of his personal accounts.

2. Disclosure and Suitability Requirements

- The Respondent should have conducted proper due diligence and done suitability on a client-by-client basis prior to recommending the Rona shares in light of each client's investment objectives, risk tolerance, and financial situation.

3. Conflict of Interest Management

- The Respondent ought to have disclosed any conflict of interest, including personal ownership of the Rona shares, to all clients before recommending the investment.

4. Involve Compliance Team Early

- Once the Respondent became aware of the audit and the rumors regarding Rona, he ought to have contacted the compliance department and checked whether his act of trading those shares constituted a breach of the rules.

**iii) Violations of Principles of Conduct**

1. IIROC Dealer Member Rules Violated

- Rule 42, Conflicts of Interest: Non-disclosure of self-ownership of shares in Rona and giving preference to personal interests against official interest is a failure on conflict-of-interest.

- Rule 1300: Suitability determination is required when accepting an order: The recommendations to buy Rona shares were not demonstrably suitable in the light of the clients' investment profile.

2. Ethical Breach - Duty of Care: The respondent failed to exercise due care in acting on the possible insider information and failing to conduct reasonable due diligence.

- Integrity and Professionalism: The placing of personal monetary gain above client interest violated the most basic tenets governing professionalism.

**Conclusion**

The Respondent's conduct exhibited serious failures of judgment, professionalism, and adherence to the IIROC Rules. The contravention was an avoidable one had there been due adherence to the regulatory regimes, rather more timely consultations with the compliance departments, and a priority concern for the best interest of the clients. This case lends further credence to the stern obligations for integrity in conduct and compliance with regulations as integral components of a system designed to protect the integrity of the financial markets and preserve the confidence of clients.

**Reference:**

Investment Industry Regulatory Organization of Canada (IIROC). (n.d.). Dealer Member Rules (repealed December 31, 2021). <https://www.iiroc.ca/dealer-member-rules-repealed-december-31-2021>