IN THE MATTER OF THE SECURITIES ACT

R.S.O. 1990, C. S.5, as amended

- and –

IN THE MATTER OF MARK EDWARD VALENTINE

Hearing:	January 30, 2003		
Panel:	Howard I. Wetston, Q.C.	-	Vice-Chair (Chair of the Panel)
	Robert W. Davis,	-	Commissioner
	Robert L. Shirriff, Q.C.	-	Commissioner
Counsel:	Melissa Kennedy Alexandra Clark	-	For the Staff of the Ontario Securities Commission
	Jeffrey Kehoe	-	For the IDA
	Janice Wright Matthew Scott	-	For Mark E. Valentine

Reasons for Order

The Commission issued a temporary order dated June 17, 2002. On July 8, 2002 the Commission made a further temporary order. On January 31, 2003 the Commission extended the July Order until these reasons and our order.

Background

Staff, by amended Notice of Hearing, dated January 7, 2003 alleges that Valentine engaged in conduct that was contrary to the public interest. It is alleged that Valentine created a culture of conflict and non-compliance at Thomson Kernahan (TK) and breached Ontario securities laws in respect of a series of transactions. It is further alleged that Valentine breached the July Order.

The July Order removed his exemptions except for trades made for his own account or for his Registered Retirement Savings Plan of those securities contained in clause 1 of section 35(2) of the Act and those securities that are listed on the TSX or the NYSE (Carve Out).

Staff have applied to extend the July Order, pursuant to its clause 2 and to remove the Carve Out. Valentine consents to the extension until July 31, 2003 but not the removal of the Carve Out.

The panel must consider whether there is a risk of harm to the public to continue to allow Valentine to trade on a restricted basis.

The Breach

Mr. Scott Boyle, an Investigator in the Enforcement Branch of the Commission (OSC), testified that Valentine opened an account in the name of Q Corporation at Refco Futures Canada Limited in Toronto on July 22, 2002. He traded or acted in furtherance of trades involving futures contracts namely the E-mini Standard & Poors Stock Price Index Futures and the E-Mini Nasdaq 100 Index Futures (collectively the Contracts) on the Chicago Mercantile Exchange (CME).

Staff contend that these Contracts constitute securities within the meaning of s. 1(1) of the Ontario *Securities Act* (OSA) and the July Order. Valentine's exemptions contained in Ontario securities law do not apply and he breached the July Order. Valentine contends that he was not trading in non-exempt securities and therefore did not breach the July Order.

Analysis (S.1(1))

The threshold question is whether the Contracts are securities within the meaning of s.1(1) of the Act.

1.(1) "security" includes…

(p) any commodity futures contract or any commodity futures option that is not traded on a commodity futures exchange registered with or recognized by the Commission under the *Commodity Futures Act* or the form of which is not accepted by the Director under that Act.

We find that during the currency of the July Order Valentine traded or acted in furtherance of trades involving the Contracts.

Counsel for the Respondent argues that the Contracts are commodity futures governed by the *Commodity Futures Act* (CFA) and not securities contemplated by Section 1(1) of the OSA. Her argument has three bases: first, the differences between the commodity futures markets and the capital markets mentioned in the 1975 Report of the Interministerial Committee on Commodity Futures Trading (known as the Harry Bray Report); second, the separate regulatory regime for commodity futures under the CFA; and third, the interplay between OSC Rule 91-503 and the definitions of "security" and "recognized commodity futures exchange" contained in the OSA. Therefore, Counsel argues, trading in these Contracts could not constitute breach of the July Order.

We respectfully disagree. The Contracts are commodity futures contracts as defined in the CFA. The CFA defines a commodity as including "any goods, article, service, right or interest, or class thereof, designated as a commodity under the regulations". CFA R.S.O. 1990, c. C.20, s.1.

The *Commodity Futures Act* regulations, in a section titled "Designation of Commodities"[1], designates as commodities:

> interests that are cash values deliverable under contracts traded on a commodity futures exchange, the amounts of which are determined with reference to…indices of prices or values pertaining to any commodities, goods, articles, services, rights or interests or any combination thereof.
> R.R.O. 1990, Reg. 90, s.2

However, the CME has neither been registered with nor recognized by this Commission under the CFA nor exempted from these requirements. Also the form of the contracts has not been accepted by the Director under the CFA. Accordingly they are securities under s. 1(1) of the OSA.

OSC Rule 91-503 provides relief from the registration and prospectus requirements under the OSA in respect of trades in commodity futures contracts and commodity futures options on exchanges, such as the CME, outside Ontario. The rule does not recognize, register or exempt the CME under the CFA. Indeed, if these contracts and options were not securities as defined in the OSA, there would be no need for the Rule as they would not be subject to the registration and prospectus requirements of Sections 25 and 53 of the OSA.

[1] But mistakenly referenced to "paragraph 5 of section 65 of the Act".

We also note that the removal by the July Order of the exemptions available to the Respondent under Ontario securities law includes the exemptions contained in Rule 91-503 thus the Contracts were not exempt exchange contracts.

Accordingly, we find that the Contracts were securities within the provisions of the OSA and the July Order and the trades in question were in breach of that Order.

The Carve Out

We have concluded that the Contracts were included within the meaning of s. 1(1) of the Act and accordingly were also securities within the meaning of the July Order. However, we also observe that this analysis is not straightforward.

Staff contends Valentine was in breach of the July Order. He opened the account in the name of Q Corporation about two weeks after the cease trade order. He traded in the Mini Nasdaq Index even though he was explicitly precluded from trading on the NASDAQ. He was one of two designated trading officers on that account. He personally guaranteed each trade. The account was opened at $50,000 U.S. and he closed it at $42,235.00 U.S. He received the proceeds of the account, which he closed on August 26, 2002.

Despite Ms. Wright's very able argument that while there is no direct evidence that Valentine traded, there is sufficient evidence that his acts were in furtherance of these trades, we do accept that there is no evidence that the trades, in and of themselves, were abusive, or that Valentine attempted to conceal his identity or objectives with respect to Refco.

Staff further contends that the Carve Out should be removed because in August, 2002 Valentine was charged with certain securities fraud violations in the U.S. Moreover, the Trustee in Bankruptcy for TK filed, but appears to have not yet served, a statement of claim dated January 6, 2003 naming 47 defendants including Valentine. Apparently Lemmon, a co-accused in the U.S., has pleaded guilty to a securities fraud charge and awaits sentencing. Valentine's trial date has not yet been set.

Staff counsel ably argued that, taken together, these facts suggest that confidence in the capital markets would be undermined if the Carve Out were continued. Ms. Wright submits that there would be little or no risk of harm to the capital markets if the Carve Out were continued.

We agree with staff counsel that if there is any doubt, it is preferable for a registrant, subject to a temporary order, to approach the Commission to determine its limits. Clearly, this is one measure of integrity. However, we accept the argument that Valentine may have thought he was under the CFA and there is no evidence that he knowingly breached the July Order. While we agree that knowledge may not be required, its presence would be decisive.

Conclusion

We have decided to continue the Carve Out contained in the July Order but to vary it as follows:

1. Valentine must submit standing instructions to each registrant with whom he has an account, or through or with whom he trades any securities, directing that copies of monthly account statements be forwarded to the Commission.

2. For all personal trading Valentine must carry out permitted trading through accounts opened in his name only and must close any accounts in which he has any beneficial ownership or interest that were not opened in his name only.

3. If the hearing does not commence, for whatever reason, on or before July 31, 2003, staff may apply to the Commission for an order to extend this order for such further periods, as the Commission considers appropriate.

DATED at Toronto this 14th day of February, 2003.

"Howard I. Wetston" "Robert L. Shirriff"

HOWARD I. WETSTON ROBERT L. SHIRRIFF

"Robert W. Davis"

ROBERT W. DAVIS